

No securities regulatory authority has expressed an opinion about these securities and it is an offence to claim otherwise.

This short form prospectus constitutes a public offering of these securities only in those jurisdictions where they may be lawfully offered for sale and therein only by persons permitted to sell such securities. **Information has been incorporated by reference in this short form prospectus from documents filed with securities commissions or similar authorities in Canada.** Copies of the documents incorporated herein by reference may be obtained on request without charge from the Secretary of the Corporation at Suite 1201, 139 Water Street, St. John's, Newfoundland and Labrador A1B 3T2 (telephone (709) 737-2800) or by accessing the Corporation's disclosure documents available through the Internet on the Canadian System for Electronic Document Analysis and Retrieval which can be accessed at [www.sedar.com](http://www.sedar.com). For the purpose of the province of Québec, this simplified prospectus contains information to be completed by consulting the permanent information record. A copy of the permanent information record may be obtained from the Secretary of the Corporation at Suite 1201, 139 Water Street, St. John's, Newfoundland and Labrador A1B 3T2 (telephone (709) 737-2800). The securities being offered under this short form prospectus have not been and will not be registered under the United States Securities Act of 1933, as amended, or any state securities laws, and, except in limited circumstances, will not be offered or sold within the United States to or for the account or benefit of United States persons. See "Plan of Distribution".

New Issue

SHORT FORM PROSPECTUS

January 20, 2004

FORTIS INC.  
**FORTIS**

**\$50,000,000**

**8,000,000 First Preference Units**

**Each First Preference Unit consisting of**

**one Cumulative Redeemable Convertible First Preference Share, Series D and  
one Cumulative Redeemable Convertible First Preference Share, Series E Purchase Warrant**

Fortis Inc. ("Fortis" or the "Corporation") is hereby qualifying for distribution (the "Offering") 8,000,000 first preference units (the "Units"), each of which consists of one cumulative redeemable convertible first preference share, series D of the Corporation (a "Series D First Preference Share") and one cumulative redeemable convertible first preference share, series E purchase warrant of the Corporation (a "Warrant").

The holders of Series D First Preference Shares will be entitled to receive fixed cumulative preferential cash dividends, if, as and when declared by the board of directors of the Corporation (the "Board of Directors") in the amount of \$0.3063 per Series D First Preference Share per annum, to accrue from the original date of issue, payable on March 31, 2004, July 15, 2004 and thereafter on the first business day of September, December, March and June of each year. Assuming an issue date of January 29, 2004, the first dividend, if declared, will be payable on March 31, 2004 in the amount of \$0.0519 per Series D First Preference Share, the second dividend, if declared, will be payable on July 15, 2004 in the amount of \$0.0887 per Series D First Preference Share, the third dividend, if declared, will be payable on September 1, 2004 in the amount of \$0.0402 per Series D First Preference Share and each dividend thereafter will be payable in equal quarterly instalments in the amount of \$0.0766 per Series D First Preference Share, except as described herein. **If the Acquisition (as defined below) has closed on or prior to June 30, 2004, quarterly cash dividends payable in respect of the Series D First Preference Shares after July 15, 2004, if declared, will be reduced to \$0.01 per Series D First Preference Share, being equivalent to 0.64% per annum per Series D First Preference Share.** See "Details of the Offering — Description of the Series D First Preference Shares — Dividends".

If the acquisition by the Corporation, directly or indirectly, of all of the issued and outstanding shares of Aquila Networks Canada (Alberta) Ltd. (the "Alberta Utility") and Aquila Networks Canada (British Columbia) Ltd. (the "B.C. Utility") (the "Acquisition") closes on or prior to June 30, 2004, the holder of a Series D First Preference Share will have the right, subject to applicable law and any necessary regulatory approvals, to convert on July 15, 2004, September 1, 2004 or December 1, 2004 such Series D First Preference Share into 0.25 of a fully-paid and freely-tradeable cumulative redeemable convertible first preference share, series E of the Corporation (a "Series E First Preference Share"), provided such holder concurrently exercises one Warrant. The concurrent exercise of a Warrant together with a cash payment of \$18.75 per Warrant will entitle the holder to acquire 0.75 of a fully-paid and freely-tradeable Series E First Preference Share. **A Series D First Preference Share cannot be converted into 0.25 of a fully-paid and freely-tradeable Series E First Preference Share without the concurrent exercise of a Warrant and a Warrant cannot be exercised without the concurrent conversion of a Series D First Preference Share into 0.25 of a fully-paid and freely-tradeable Series E First Preference Share. A Warrant may not be separated from the related Series D First Preference Share forming a Unit.** Consequently, the conversion of one Series D First Preference Share, the concurrent exercise of one Warrant and the additional cash payment of \$18.75 will entitle the holder of a Unit to receive one fully-paid and freely-tradeable Series E First Preference Share. If the Acquisition has closed on or prior to June 30, 2004, all conversion rights of the holder of a Series D First Preference Share that have not been exercised for any reason by 5:00 p.m. (Toronto time) on December 1, 2004 (the "Expiry Time") will terminate and all Warrants that have not been exercised for any reason by the Expiry Time will be void and of no effect. If the Acquisition does not close on or prior to June 30, 2004, all Warrants will be void and of no effect as of 5:00 p.m. (Toronto time) on July 15, 2004 (the "Early Expiry Time"). See "Details of the Offering — Description of the Series D First Preference Shares — Conversion by the Holder into Series E First Preference Shares" and "Details of the Offering — Description of the Warrants".

If the Acquisition does not close on or prior to June 30, 2004, subject to applicable law and any necessary regulatory approvals, on and after September 1, 2016, each Series D First Preference Share will be convertible at the option of the holder, upon not less than 30 days and not more than 60 days prior written notice (which notice shall be irrevocable), on the first business day of September, December, March and June of each year, into that number of fully-paid and freely-tradeable common shares of the Corporation (the "Common Shares") determined by dividing \$6.25 plus all accrued and unpaid dividends up to but excluding the date fixed for conversion, by the greater of \$1.00 and 95% of the weighted average trading price of the Common Shares on the Toronto Stock Exchange (the "TSX") for the 20 consecutive trading days ending on the fourth day prior to the date fixed for conversion or, if that fourth day is not a trading day, on the immediately preceding trading day (the "Current Market Price"). Fractional Common Shares will not be issued on any conversion of Series D First Preference Shares, but in lieu thereof, the Corporation will make cash payments. If a holder of Series D First Preference Shares elects to convert any of such shares into Common Shares, the Corporation may, upon not less than 20 days written notice prior to the conversion date, elect to redeem such Series D First Preference Shares for cash and/or arrange for the sale of those shares to other purchasers. See "Details of the Offering — Description of the Series D First Preference Shares — Conversion by the Holder into Common Shares" and "Details of the Offering — Description of the Warrants".

On and after June 1, 2013, the Corporation may, at its option, upon not less than 30 days and not more than 60 days prior written notice, subject to applicable law and any necessary regulatory approvals, convert all, or from time to time any part of, the outstanding Series D First Preference Shares into that number of fully-paid and freely-tradeable Common Shares determined by dividing the then applicable redemption price per Series D First Preference Share (as set out below) plus all accrued and unpaid dividends up to but excluding the date fixed for conversion, by the greater of \$1.00 and 95% of the Current Market Price. Fractional Common Shares will not be issued on any conversion of Series D First Preference Shares, but in lieu thereof, the Corporation will make cash payments. If less than all of the outstanding Series D First Preference Shares are at any time to be converted, such Series D First Preference Shares will be converted on a *pro rata* basis. See “Details of the Offering — Description of the Series D First Preference Shares — Conversion by the Corporation into Common Shares”.

On and after June 1, 2013, subject to the terms of any shares of the Corporation ranking prior to the Series D First Preference Shares, to applicable law, to any necessary regulatory approvals, and to the provisions described under “Details of the Offering — Description of the Series D First Preference Shares — Restrictions on Dividends and Retirement and Issue of Shares”, the Corporation may, at its option, upon not less than 30 days and not more than 60 days prior written notice, redeem all, or from time to time any part of, the outstanding Series D First Preference Shares by the payment in cash of a sum per redeemed share equal to \$6.4375 if redeemed during the 12 months commencing June 1, 2013; \$6.375 if redeemed during the 12 months commencing June 1, 2014; \$6.3125 if redeemed during the 12 months commencing June 1, 2015; and \$6.25 if redeemed on or after June 1, 2016 plus, in each case, all accrued and unpaid dividends up to but excluding the date fixed for redemption (less any tax required to be deducted and withheld by the Corporation). If less than all of the outstanding Series D First Preference Shares are at any time to be redeemed, such Series D First Preference Shares will be redeemed on a *pro rata* basis. See “Details of the Offering — Description of the Series D First Preference Shares — Redemption”.

The holders of Series E First Preference Shares will be entitled to receive fixed cumulative preferential cash dividends, if, as and when declared by the Board of Directors in the amount of \$1.2250 per Series E First Preference Share per annum, to accrue from the original date of issue, payable in equal quarterly installments in the amount of \$0.3063 per Series E First Preference Share on the first business day of March, June, September and December of each year. Assuming an issue date of July 15, 2004, the first dividend, if declared, will be payable on September 1, 2004 in the amount of \$0.1607 per Series E First Preference Share to account for the initial partial period during which the Series E First Preference Shares will be outstanding. Assuming an issue date of September 1, 2004 or December 1, 2004, the first dividend, if declared, will be payable on December 1, 2004 or March 1, 2005, respectively, in the amount of \$0.3063 per Series E First Preference Share. See “Details of the Offering — Description of the Series E First Preference Shares — Dividends”.

On and after September 1, 2016, subject to applicable law and any necessary regulatory approvals, each Series E First Preference Share will be convertible at the option of the holder, upon not less than 30 days and not more than 60 days prior written notice (which notice shall be irrevocable), on the first business day of September, December, March and June of each year, into that number of fully-paid and freely-tradeable Common Shares determined by dividing \$25.00 plus all accrued and unpaid dividends up to but excluding the date fixed for conversion, by the greater of \$1.00 and 95% of the Current Market Price. Fractional Common Shares will not be issued on any conversion of Series E First Preference Shares, but in lieu thereof, the Corporation will make cash payments. If a holder of Series E First Preference Shares elects to convert any of such shares into Common Shares, the Corporation may, upon not less than 20 days written notice prior to the conversion date, elect to redeem such Series E First Preference Shares for cash and/or arrange for the sale of those shares to other purchasers. See “Details of the Offering — Description of the Series E First Preference Shares — Conversion by the Holder into Common Shares”.

On and after June 1, 2013, the Corporation may, at its option, upon not less than 30 days and not more than 60 days prior written notice, subject to applicable law and any necessary regulatory approvals, convert all, or from time to time any part of, the outstanding Series E First Preference Shares into that number of fully-paid and freely-tradeable Common Shares determined by dividing the then applicable redemption price per Series E First Preference Share (as set out below) plus all accrued and unpaid dividends up to but excluding the date fixed for conversion, by the greater of \$1.00 and 95% of the Current Market Price. Fractional Common Shares will not be issued on any conversion of Series E First Preference Shares, but in lieu thereof, the Corporation will make cash payments. If less than all of the outstanding Series E First Preference Shares are at any time to be converted, such Series E First Preference Shares will be converted on a *pro rata* basis. See “Details of the Offering — Description of the Series E First Preference Shares — Conversion by the Corporation into Common Shares”.

On and after June 1, 2013, subject to the terms of any shares of the Corporation ranking prior to the Series E First Preference Shares, to applicable law, to any necessary regulatory approvals and to the provisions described under “Details of the Offering — Description of the Series E First Preference Shares — Restrictions on Dividends and Retirement and Issue of Shares”, the Corporation may, at its option, upon not less than 30 days and not more than 60 days prior written notice, redeem all, or from time to time any part of, the outstanding Series E First Preference Shares by the payment in cash of a sum per redeemed share equal to \$25.75 if redeemed during the 12 months commencing June 1, 2013; \$25.50 if redeemed during the 12 months commencing June 1, 2014; \$25.25 if redeemed during the 12 months commencing June 1, 2015; and \$25.00 if redeemed on or after June 1, 2016 plus, in each case, all accrued and unpaid dividends up to but excluding the date fixed for redemption (less any tax required to be deducted and withheld by the Corporation). If less than all of the outstanding Series E First Preference Shares are at any time to be redeemed, such Series E First Preference Shares will be redeemed on a *pro rata* basis. See “Details of the Offering — Description of the Series E First Preference Shares — Redemption”.

**There is currently no market through which the Units may be sold and purchasers may not be able to resell securities purchased under this short form prospectus (the “Prospectus”).**

The TSX has conditionally approved the listing of the Units, including the Series D First Preference Shares and the Warrants comprised therein, and the Series E First Preference Shares issuable in respect of the Units, as well as the Common Shares issuable upon the conversion of either the Series D First Preference Shares or the Series E First Preference Shares. The listing of the Units, including the Series D First Preference Shares and the Warrants comprised therein, and the Common Shares issuable upon the conversion of either the Series D First Preference Shares or the Series E First Preference Shares will be subject to the Corporation fulfilling all of the listing requirements of the TSX on or before April 12, 2004. The listing of the Series E First Preference Shares will be subject to the Corporation fulfilling all of the listing requirements of the TSX on or before July 12, 2004. The Corporation’s outstanding Common Shares are listed on the TSX under the symbol “FTS”. On January 19, 2004, the closing price of the Common Shares on the TSX was \$61.06. See “Details of the Offering — Description of the Units — Listing”, “Details of the Offering — Description of the Series D First Preference Shares — Listing”, “Details of the Offering — Description of the Series E First Preference Shares — Listing” and “Plan of Distribution”.

**An investment in the Units involves certain risks that should be considered by a prospective purchaser. See “Risk Factors”.**

## Price: \$6.25 per Unit

	Price to the Public	Underwriters’ Fee (1)	Net Proceeds to the Corporation (2)
Per Unit .....	\$6.25	\$0.75	\$5.50
Total .....	\$50,000,000	\$6,000,000	\$44,000,000

(1) The Underwriters’ fee for the Units is \$0.25 for each Unit purchased by the Underwriters and sold to certain institutions and \$0.75 per Unit for all other Units purchased by the Underwriters. The Underwriters’ fee indicated in the table assumes that no Units are sold to these institutions. No additional fee is payable by the Corporation to the Underwriters in connection with the exercise of Warrants or the conversion of Series D First Preference Shares or otherwise in respect of the Offering.

(2) Before deducting expenses of the Offering estimated at \$650,000 which, together with the Underwriters’ fees, will be paid out of the general funds of Fortis. See “Plan of Distribution”.

Scotia Capital Inc. (“Scotia Capital”), BMO Nesbitt Burns Inc., CIBC World Markets Inc., National Bank Financial Inc., RBC Dominion Securities Inc., TD Securities Inc. and Beacon Securities Limited are acting as underwriters (the “Underwriters”) of the Offering. The Underwriters, as principals, conditionally offer the Units, subject to prior sale, if, as and when issued, sold and delivered by the Corporation to, and accepted by, the Underwriters in accordance with the terms and conditions contained in the underwriting agreement referred to under “Plan of Distribution” and subject to the approval of certain legal matters on behalf of the Corporation by Davies Ward Phillips & Vineberg LLP and Curtis, Dawe and on behalf of the Underwriters by Stikeman Elliott LLP.

**Each of Scotia Capital, BMO Nesbitt Burns Inc., CIBC World Markets Inc., National Bank Financial Inc., RBC Dominion Securities Inc. and TD Securities Inc. is an affiliate of a Canadian chartered bank that is part of a syndicate of banks that have agreed to extend credit facilities to the Corporation in connection with the financing of the Acquisition. Scotia Capital has agreed to act as the sole lead arranger and book runner in connection with this financing and is receiving a fee for its role as financial advisor to Fortis in connection with the Acquisition. Consequently, the Corporation may be considered a “connected issuer” of these Underwriters within the meaning of applicable securities legislation. See “Plan of Distribution”.**

Subscriptions for the Units will be received, subject to rejection or allotment in whole or in part, and the right is reserved to close the subscription books at any time without notice. It is expected that the closing of the Offering will take place on or about January 29, 2004 (the “Closing Date”), or such other date as may be agreed upon by the Corporation and the Underwriters, but not later than February 27, 2004. The Units, Series E First Preference Shares and, following the Early Expiry Time if the Acquisition does not close on or prior to June 30, 2004, Series D First Preference Shares will be issued in book-entry only form and must be purchased or transferred through a registered dealer who is a participant in The Canadian Depository for Securities Limited (“CDS”) book-entry only system (a “CDS Participant”). The Corporation will cause global certificates representing the Units, Series E First Preference Shares and, following the Early Expiry Time if the Acquisition does not close on or prior to June 30, 2004, Series D First Preference Shares to be delivered to and registered in the name of CDS or its nominee. All rights of holders of the Units, Series E First Preference Shares and, following the Early Expiry Time if the Acquisition does not close on or prior to June 30, 2004, Series D First Preference Shares must be exercised through, and all payments or other money to which such holders are entitled will be made or delivered by CDS, its nominee or the CDS Participant through which the holders hold such securities. Each holder of Units, Series E First Preference Shares and, following the Early Expiry Time if the Acquisition does not close on or prior to June 30, 2004, Series D First Preference Shares will receive only a customer confirmation of purchase from the registered dealer from or through which such securities are acquired in accordance with the practices and procedures of that registered dealer. The practices of registered dealers may vary, but generally customer confirmations are issued promptly after execution of a customer order. CDS is responsible for establishing and maintaining book-entry accounts for CDS Participants having interests in the Units, Series E First Preference Shares and, following the Early Expiry Time if the Acquisition does not close on or prior to June 30, 2004, Series D First Preference Shares.

**The Prospectus includes financial statements of the Alberta Utility for the year ended December 31, 2001 and of the B.C. Utility for the years ended December 31, 2001 and 2000 that were audited and reported on by Arthur Andersen LLP (“Arthur Andersen”). The Corporation has not obtained the consent of Arthur Andersen to the use of its audit report in respect of these financial statements. Arthur Andersen’s consent was not obtained because on June 3, 2002, Arthur Andersen ceased to practise public accounting. Because Arthur Andersen has not provided this consent, purchasers of Units pursuant to the Prospectus will not have the statutory right of action for damages against Arthur Andersen as prescribed by applicable securities legislation with respect to these financial statements. In addition, Arthur Andersen may not have sufficient assets available to satisfy any judgments against it. See “Risk Factors — Arthur Andersen” and “Purchasers’ Statutory Rights”.**

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## DOCUMENTS INCORPORATED BY REFERENCE

The disclosure documents of the Corporation listed below and filed with the appropriate securities commissions or similar regulatory authorities in each of the provinces of Canada are specifically incorporated by reference into and form an integral part of the Prospectus:

- (a) Annual Information Form dated April 15, 2003;
- (b) Audited comparative consolidated financial statements for the years ended December 31, 2002 and 2001 together with the notes thereto and the auditors' report thereon as contained in the Corporation's 2002 Annual Report;
- (c) Management Discussion and Analysis of financial condition and results of operations contained in the Corporation's 2002 Annual Report;
- (d) Management Information Circular dated March 31, 2003, prepared in connection with the Corporation's annual meeting of shareholders held on May 14, 2003, excluding the portions thereof that appear under the headings "Performance Chart", "Report on Corporate Governance" and "Report on Executive Compensation";
- (e) Material Change Report dated May 20, 2003, describing the entering into of an agreement between the Corporation and a syndicate of underwriters led by Scotia Capital in respect of the offering of first preference shares, series C of the Corporation (the "Series C First Preference Shares");
- (f) Unaudited comparative financial statements for the three and nine month periods ended September 30, 2003 and 2002;
- (g) Interim Management Discussion and Analysis of financial condition and results of operations of the Corporation for the three and nine month periods ended September 30, 2003 and 2002;
- (h) Material Change Report dated September 16, 2003, describing the entering into by the Corporation of agreements to acquire all of the shares of the Alberta Utility and the B.C. Utility from two indirect subsidiaries of Aquila, Inc. for aggregate consideration of \$1.36 billion; and
- (i) Material Change Report dated January 13, 2004 describing the entering into of an agreement between the Corporation and a syndicate of underwriters led by Scotia Capital in respect of the Offering.

Any document of the type referred to in the preceding paragraph and any material change report (excluding confidential reports) subsequently filed by the Corporation with such securities commissions or regulatory authorities after the date of the Prospectus, and prior to the termination of the Offering, shall be deemed to be incorporated by reference into the Prospectus.

**Any statement contained in a document incorporated or deemed to be incorporated by reference herein shall be deemed to be modified or superseded for purposes of the Prospectus to the extent that a statement contained herein, or in any other subsequently filed document that is also incorporated or is deemed to be incorporated by reference herein, modifies or supersedes such statement. The modifying or superseding statement need not state that it has modified or superseded a prior statement or include any other information set forth in the document that it modifies or supersedes. The making of a modifying or superseding statement will not be deemed an admission for any purpose that the modified or superseded statement, when made, constituted a misrepresentation, an untrue statement of a material fact or an omission to state a material fact that is required to be stated or that is necessary to make a statement not misleading in light of the circumstances in which it was made. Any statement so modified or superseded shall not be deemed, except as so modified or superseded, to constitute a part of the Prospectus.**

Copies of the documents incorporated herein by reference may be obtained on request without charge from the Secretary of the Corporation at Suite 1201, 139 Water Street, St. John's, Newfoundland and Labrador A1B 3T2 (telephone (709) 737-2800). These documents are also available through the Internet on the Canadian System for Electronic Document Analysis and Retrieval ("SEDAR") which can be accessed at [www.sedar.com](http://www.sedar.com). The Corporation's filings available through SEDAR are not incorporated by reference in the Prospectus except as specifically set out herein.

#### **ELIGIBILITY FOR INVESTMENT**

In the opinion of Davies Ward Phillips & Vineberg LLP, counsel to the Corporation, and Stikeman Elliott LLP, counsel to the Underwriters, the Series D First Preference Shares and the Warrants that together comprise the Units, the Series E First Preference Shares issuable upon the conversion of Series D First Preference Shares and the exercise of the Warrants and the Common Shares issuable upon the conversion of either the Series D First Preference Shares or the Series E First Preference Shares would, if issued on the date hereof, be qualified investments under the *Income Tax Act* (Canada) (the "Tax Act") for trusts governed by a registered retirement savings plan, a registered retirement income fund, a registered education savings plan and a deferred profit sharing plan. None of the Warrants or the Series D First Preference Shares that together comprise the Units, the Series E First Preference Shares issuable upon the conversion of the Series D First Preference Shares and the exercise of the Warrants or the Common Shares issuable upon the conversion of either the Series D First Preference Shares or the Series E First Preference Shares would, if issued on the date hereof, be foreign property for purposes of Part XI of the Tax Act.

#### **DEFINED TERMS**

For an explanation of certain terms and abbreviations used in the Prospectus, reference is made to the "Glossary of Terms".

## SUMMARY

*The following information is a summary only and is to be read in conjunction with, and is qualified in its entirety by, the more detailed information appearing elsewhere in this short form prospectus (the "Prospectus") and in the documents incorporated by reference herein.*

### The Offering

<b>Issuer:</b>	Fortis Inc. ("Fortis" or the "Corporation").
<b>Offering:</b>	8,000,000 first preference units (the "Units"), each consisting of one cumulative redeemable convertible first preference share, series D of the Corporation (a "Series D First Preference Share") and one cumulative redeemable convertible first preference share, series E purchase warrant of the Corporation (a "Warrant"). See "Details of the Offering — Description of the Units".
<b>Amount:</b>	\$50,000,000.
<b>Price:</b>	\$6.25 per Unit.
<b>Date of Closing:</b>	On or about January 29, 2004 (the "Closing Date").
<b>Use of Proceeds:</b>	The proceeds of this offering (the "Offering"), after deducting the fee payable to Scotia Capital Inc. ("Scotia Capital"), BMO Nesbitt Burns Inc., CIBC World Markets Inc., National Bank Financial Inc., RBC Dominion Securities Inc., TD Securities Inc. and Beacon Securities Limited (the "Underwriters") and expenses of the Offering, which are estimated to be \$650,000, will be used for general corporate purposes, including the repayment of certain short-term indebtedness and the financing of a portion of the Corporation's acquisition, directly or indirectly, of all of the issued and outstanding shares of Aquila Networks Canada (Alberta) Ltd. (the "Alberta Utility") and Aquila Networks Canada (British Columbia) Ltd. (the "B.C. Utility") (the "Acquisition"). If the Acquisition does not close on or prior to June 30, 2004, the net proceeds intended to be used to finance the Acquisition will be used for other general corporate purposes. The proceeds received from the exercise of the Warrants will be used to repay certain short-term indebtedness incurred by the Corporation to fund the Acquisition. If the Acquisition does not close on or prior to June 30, 2004, no Warrants can be exercised and no further proceeds will therefore be received by the Corporation. See "Use of Proceeds" and "Financing of the Acquisition — Credit Agreements".
<b>Risk Factors:</b>	An investment in the Series D First Preference Shares and Warrants that together comprise the Units, the cumulative redeemable convertible first preference shares, series E of the Corporation (the "Series E First Preference Shares") issuable upon the conversion of Series D First Preference Shares and the exercise of the Warrants and the common shares of the Corporation (the "Common Shares") issuable upon the conversion of either the Series D First Preference Shares or the Series E First Preference Shares involve certain risks which should be carefully considered by prospective investors, including: regulation, lack of an existing market for the Units, the closing of the Acquisition, results of operations and financing risks, management of expanding operations, the ability to realize benefits from the Acquisition, asset maintenance, damage from weather and other natural disasters, loss of service areas, obtaining

and maintaining government permits, the financial position of Aquila, Inc. (“Aquila”), potential undisclosed liabilities associated with the Acquisition, litigation affecting the Corporation, ability to maintain satisfactory labour relations, exposure to interest rate changes, matters relating to insurance, availability of capital resources, environmental matters and the lack of consent by Arthur Andersen LLP (“Arthur Andersen”). See “Risk Factors”.

**Listing:**

The Toronto Stock Exchange (the “TSX”) has conditionally approved the listing of the Units, including the Series D First Preference Shares and the Warrants comprised therein. Listing will be subject to the Corporation fulfilling all of the listing requirements of the TSX on or before April 12, 2004. As the Units will be listed upon the fulfillment of these listing requirements, the Series D First Preference Shares and the Warrants will not trade separately while the Units exist. See “Details of the Offering — Description of the Units — Listing”, “Details of the Offering — Description of the Series D First Preference Shares — Listing” and “Plan of Distribution”.

**Purchase for Cancellation:**

Subject to applicable law and any necessary regulatory approvals, the Corporation may, at any time, purchase for cancellation all or any of the Units in the open market or by private agreement or otherwise at the lowest price or prices at which, in the opinion of the board of directors of the Corporation (the “Board of Directors”), such Units are obtainable. See “Details of the Offering — Description of the Units — Purchase for Cancellation”.

**Warrants:**

If the Acquisition closes on or prior to June 30, 2004, each Warrant, when exercised in accordance with its terms, which include the payment of additional cash consideration of \$18.75, will entitle the holder thereof to acquire on July 15, 2004, September 1, 2004 or December 1, 2004, 0.75 of a fully-paid and freely-tradeable Series E First Preference Share. **A Series D First Preference Share cannot be converted into 0.25 of a fully-paid and freely-tradeable Series E First Preference Share without the concurrent exercise of a Warrant, and a Warrant cannot be exercised without the concurrent conversion of a Series D First Preference Share into 0.25 of a fully-paid and freely-tradeable Series E First Preference Share. A Warrant may not be separated from the related Series D First Preference Share forming a Unit.** If the Acquisition does not close on or prior to June 30, 2004, all Warrants will be void and of no effect as of 5:00 p.m. (Toronto time) on July 15, 2004 (the “Early Expiry Time”). If the Acquisition closes on or prior to June 30, 2004, all Warrants that have not been exercised for any reason by 5:00 p.m. (Toronto time) on December 1, 2004 (the “Expiry Time”) will be void and of no effect. See “Details of the Offering — Description of the Series D First Preference Shares” and “Details of the Offering — Description of the Warrants”.

**The Series D First Preference Shares**

**Dividends:**

The holders of Series D First Preference Shares will be entitled to receive fixed cumulative preferential cash dividends, if, as and when declared by the Board of Directors in the amount of \$0.3063 per Series D First Preference Share per annum, to accrue from the original date of issue, payable on March 31, 2004, July 15, 2004 and thereafter on the first business day of September, December, March and June of each year.

Assuming an issue date of January 29, 2004, the first dividend, if declared, will be payable on March 31, 2004 in the amount of \$0.0519 per Series D First Preference Share, the second dividend, if declared, will be payable on July 15, 2004 in the amount of \$0.0887 per Series D First Preference Share, the third dividend, if declared, will be payable on September 1, 2004 in the amount of \$0.0402 per Series D First Preference Share and each dividend thereafter will be payable in equal quarterly instalments in the amount of \$0.0766 per Series D First Preference Share, except as described herein. **If the Acquisition has closed on or prior to June 30, 2004, quarterly cash dividends payable in respect of the Series D First Preference Shares after July 15, 2004, if declared, will be reduced to \$0.01 per Series D First Preference Share, being equivalent to 0.64% per annum per Series D First Preference Share.** See “Details of the Offering — Description of the Series D First Preference Shares — Dividends”.

**Conversion by the Holder into Series E First Preference Shares:**

If the Acquisition closes on or prior to June 30, 2004, the holder of a Series D First Preference Share will have the right, subject to applicable law and any necessary regulatory approvals, to convert on July 15, 2004, September 1, 2004 or December 1, 2004 such Series D First Preference Share into 0.25 of a fully-paid and freely-tradeable Series E First Preference Share, provided such holder concurrently exercises one Warrant. The concurrent exercise of a Warrant together with a cash payment of \$18.75 per Warrant will entitle the holder to acquire 0.75 of a fully-paid and freely-tradeable Series E First Preference Share. **A Series D First Preference Share cannot be converted into 0.25 of a fully-paid and freely-tradeable Series E First Preference Share without the concurrent exercise of a Warrant and a Warrant cannot be exercised without the concurrent conversion of a Series D First Preference Share into 0.25 of a fully-paid and freely-tradeable Series E First Preference Share. A Warrant may not be separated from the related Series D First Preference Share forming a Unit.** Consequently, the conversion of one Series D First Preference Share, the concurrent exercise of one Warrant and the additional cash payment of \$18.75 will entitle the holder of a Unit to receive one fully-paid and freely-tradeable Series E First Preference Share. If the Acquisition has closed on or prior to June 30, 2004, all conversion rights of the holder of a Series D First Preference Share that have not been exercised for any reason by the Expiry Time will terminate. See “Details of the Offering — Description of the Series D First Preference Shares — Conversion by the Holder into Series E First Preference Shares” and “Details of the Offering — Description of the Warrants”.

**Conversion by the Holder into Common Shares:**

If the Acquisition does not close on or prior to June 30, 2004, subject to applicable law and any necessary regulatory approvals, on and after September 1, 2016, each Series D First Preference Share will be convertible at the option of the holder, upon not less than 30 days and not more than 60 days prior written notice (which notice shall be irrevocable), on the first business day of September, December, March and June of each year, into that number of fully-paid and freely-tradeable Common Shares determined by dividing \$6.25 plus all accrued and unpaid dividends up to but excluding the date fixed for conversion, by the greater of \$1.00 and 95% of the weighted average trading price of the Common Shares on the TSX for the 20 consecutive trading days ending on the fourth day prior to the date fixed for conversion or, if that fourth day is not a trading day, on



the immediately preceding trading day (the “Current Market Price”). Fractional Common Shares will not be issued on any conversion of Series D First Preference Shares, but in lieu thereof, the Corporation will make cash payments. If a holder of Series D First Preference Shares elects to convert any of such shares into Common Shares, the Corporation may, upon not less than 20 days written notice prior to the conversion date, elect to redeem such Series D First Preference Shares for cash and/or arrange for the sale of those shares to other purchasers. See “Details of the Offering — Description of the Series D First Preference Shares — Conversion by the Holder into Common Shares”.

**Conversion by the Corporation into Common Shares:**

On and after June 1, 2013, the Corporation may, subject to applicable law and any necessary regulatory approvals, at its option, upon not less than 30 days and not more than 60 days prior written notice, convert all, or from time to time any part of, the outstanding Series D First Preference Shares into that number of fully-paid and freely-tradeable Common Shares determined by dividing the then applicable redemption price per Series D First Preference Share (as set out below) plus all accrued and unpaid dividends up to but excluding the date fixed for conversion, by the greater of \$1.00 and 95% of the Current Market Price. Fractional Common Shares will not be issued on any conversion of Series D First Preference Shares, but in lieu thereof, the Corporation will make cash payments. If less than all of the outstanding Series D First Preference Shares are at any time to be converted, such Series D First Preference Shares will be converted on a *pro rata* basis. See “Details of the Offering — Description of the Series D First Preference Shares — Conversion by the Corporation into Common Shares”.

**Redemption:**

On and after June 1, 2013, subject to the terms of any shares of the Corporation ranking prior to the Series D First Preference Shares, to applicable law, to any necessary regulatory approvals and to the provisions described under “Details of the Offering — Description of the Series D First Preference Shares — Restrictions on Dividends and Retirement and Issue of Shares”, the Corporation may, at its option, upon not less than 30 days and not more than 60 days prior written notice, redeem all, or from time to time any part of, the outstanding Series D First Preference Shares by the payment in cash of a sum per redeemed share equal to \$6.4375 if redeemed during the 12 months commencing June 1, 2013; \$6.375 if redeemed during the 12 months commencing June 1, 2014; \$6.3125 if redeemed during the 12 months commencing June 1, 2015; and \$6.25 if redeemed on or after June 1, 2016 plus, in each case, all accrued and unpaid dividends up to but excluding the date fixed for redemption (less any tax required to be deducted and withheld by the Corporation). If less than all of the outstanding Series D First Preference Shares are at any time to be redeemed, such Series D First Preference Shares will be redeemed on a *pro rata* basis. See “Details of the Offering — Description of the Series D First Preference Shares — Redemption”.

**Purchase for Cancellation:**

Subject to applicable law and any necessary regulatory approvals, the Corporation may, at any time, purchase for cancellation all or any of the Series D First Preference Shares in the open market or by private agreement or otherwise at the lowest price or prices at which, in the opinion of the Board of Directors, such Series D First Preference Shares are obtainable. See “Details of the Offering — Description of the Series D First Preference Shares — Purchase for Cancellation”.

<b>Priority:</b>	The Series D First Preference Shares rank <i>pari passu</i> with all other series of first preference shares of the Corporation (the “First Preference Shares”) and senior to all other shares of the Corporation with respect to priority to the payment of dividends and the distribution of assets on the dissolution, liquidation or winding up of the Corporation. See “Details of the Offering — Description of the Series D First Preference Shares — Priority”.
<b>Voting Rights:</b>	The Series D First Preference Shares are non-voting except if the Corporation fails to pay eight quarterly dividends on the Series D First Preference Shares, whether or not consecutive and whether or not such dividends have been declared and whether or not there are any monies of the Corporation properly applicable to the payment of dividends (and except as otherwise provided by law and except for meetings of the holders of First Preference Shares as a class and meetings of the holders of Series D First Preference Shares as a series). In that event and for only so long as any such dividends remain in arrears, the holders of the Series D First Preference Shares will be entitled to receive notice of and to attend all shareholders’ meetings, other than meetings at which only holders of another specified class or series are entitled to vote, and to one vote for each Series D First Preference Share held. See “Details of the Offering — Description of the Series D First Preference Shares — Voting Rights”.
<b>Ratings:</b>	Dominion Bond Rating Service Limited (“DBRS”): Pfd-3 (high). Standard & Poor’s (“S&P”): P-2 (low). See “Ratings”.
<b>Tax on Preference Share Dividends:</b>	The Corporation will elect, in the manner and within the time provided under subsection 191.2(1) of the <i>Income Tax Act</i> (Canada) (the “Tax Act”), to pay or cause payment of the tax under Part VI.1 of the Tax Act at a rate such that the corporate holders of Series D First Preference Shares will not be required to pay tax under Part IV.1 of the Tax Act on dividends received on such shares. See “Details of the Offering — Description of the Series D First Preference Shares — Tax on Preference Share Dividends” and “Canadian Federal Income Tax Considerations”.
<b>Listing:</b>	The TSX has conditionally approved the listing of the Common Shares issuable upon the conversion of either the Series D First Preference Shares or the Series E First Preference Shares. Listing will be subject to the Corporation fulfilling all of the listing requirements of the TSX on or before April 12, 2004. If the Acquisition does not close on or prior to June 30, 2004, the Corporation will apply to have the Series D First Preference Shares separately listed and posted for trading on the TSX on the trading day immediately following the Early Expiry Time. As the Units will be listed upon the fulfillment by the Corporation of the listing requirements of the TSX relating thereto, the Series D First Preference Shares and the Warrants will not trade separately while the Units exist. If the Acquisition closes on or prior to June 30, 2004, any Series D First Preference Shares not converted prior to the Expiry Time will not be listed on the TSX after the Expiry Time. See “Details of the Offering — Description of the Series D First Preference Shares — Listing” and “Plan of Distribution”.
<b>Earnings Coverage:</b>	Earnings coverage information for the Series D First Preference Shares is provided in the Prospectus under the heading “Earnings Coverage Ratios”.

### **The Series E First Preference Shares**

#### **Dividends:**

The holders of Series E First Preference Shares will be entitled to receive fixed cumulative preferential cash dividends, if, as and when declared by the Board of Directors in the amount of \$1.2250 per Series E First Preference Share per annum, to accrue from the original date of issue, payable in equal quarterly instalments in the amount of \$0.3063 per Series E First Preference Share on the first business day of March, June, September and December of each year. Assuming an issue date of July 15, 2004, the first dividend, if declared, will be payable on September 1, 2004 in the amount of \$0.1607 per Series E First Preference Share to account for the initial partial period during which the Series E First Preference Shares will be outstanding. Assuming an issue date of September 1, 2004 or December 1, 2004, the first dividend, if declared, will be payable on December 1, 2004 or March 1, 2005, respectively, in the amount of \$0.3063 per Series E First Preference Share. See “Details of the Offering — Description of the Series E First Preference Shares — Dividends”.

#### **Conversion by the Holder into Common Shares:**

On and after September 1, 2016, subject to applicable law and any necessary regulatory approvals, each Series E First Preference Share will be convertible at the option of the holder, upon not less than 30 days and not more than 60 days prior written notice (which notice shall be irrevocable), on the first business day of September, December, March and June of each year, into that number of fully-paid and freely-tradeable Common Shares determined by dividing \$25.00 plus all accrued and unpaid dividends up to but excluding the date fixed for conversion, by the greater of \$1.00 and 95% of the Current Market Price. Fractional Common Shares will not be issued on any conversion of Series E First Preference Shares, but in lieu thereof, the Corporation will make cash payments. If a holder of Series E First Preference Shares elects to convert any of such shares into Common Shares, the Corporation may, upon not less than 20 days written notice prior to the conversion date, elect to redeem such Series E First Preference Shares for cash and/or arrange for the sale of those shares to other purchasers. See “Details of the Offering — Description of the Series E First Preference Shares — Conversion by the Holder into Common Shares”.

#### **Conversion by the Corporation into Common Shares:**

On and after June 1, 2013, the Corporation may, at its option, upon not less than 30 days and not more than 60 days prior written notice, subject to applicable law and any necessary regulatory approvals, convert all, or from time to time any part of, the outstanding Series E First Preference Shares into that number of fully-paid and freely-tradeable Common Shares determined by dividing the then applicable redemption price per Series E First Preference Share (as set out below) plus all accrued and unpaid dividends up to but excluding the date fixed for conversion, by the greater of \$1.00 and 95% of the Current Market Price. Fractional Common Shares will not be issued on any conversion of Series E First Preference Shares, but in lieu thereof, the Corporation will make cash payments. If less than all of the outstanding Series E First Preference Shares are at any time to be converted, such Series E First Preference Shares will be converted on a *pro rata* basis. See “Details of the Offering — Description of the Series E First Preference Shares — Conversion by the Corporation into Common Shares”.

**Redemption:**

On and after June 1, 2013, subject to the terms of any shares of the Corporation ranking prior to the Series E First Preference Shares, to applicable law, to any necessary regulatory approvals and to the provisions described under “Details of the Offering — Description of the Series E First Preference Shares — Restrictions on Dividends and Retirement and Issue of Shares”, the Corporation may, at its option, upon not less than 30 days and not more than 60 days prior written notice, redeem all, or from time to time any part of, the outstanding Series E First Preference Shares by the payment in cash of a sum per redeemed share equal to \$25.75 if redeemed during the 12 months commencing June 1, 2013; \$25.50 if redeemed during the 12 months commencing June 1, 2014; \$25.25 if redeemed during the 12 months commencing June 1, 2015; and \$25.00 if redeemed on or after June 1, 2016 plus, in each case, all accrued and unpaid dividends up to but excluding the date fixed for redemption (less any tax required to be deducted and withheld by the Corporation). If less than all of the outstanding Series E First Preference Shares are at any time to be redeemed, such Series E First Preference Shares will be redeemed on a *pro rata* basis. See “Details of the Offering — Description of the Series E First Preference Shares — Redemption”.

**Purchase for Cancellation:**

Subject to applicable law and any necessary regulatory approvals, the Corporation may, at any time, purchase for cancellation all or any of the Series E First Preference Shares in the open market or by private agreement or otherwise at the lowest price or prices at which, in the opinion of the Board of Directors, such Series E First Preference Shares are obtainable. See “Details of the Offering — Description of the Series E First Preference Shares — Purchase for Cancellation”.

**Priority:**

The Series E First Preference Shares rank *pari passu* with all other series of First Preference Shares and senior to all other shares of the Corporation with respect to priority to the payment of dividends and the distribution of assets on the dissolution, liquidation or winding up of the Corporation. See “Details of the Offering — Description of the Series E First Preference Shares — Priority”.

**Voting Rights:**

The Series E First Preference Shares are non-voting except if the Corporation fails to pay eight quarterly dividends on the Series E First Preference Shares, whether or not consecutive and whether or not such dividends have been declared and whether or not there are any monies of the Corporation properly applicable to the payment of dividends (and except as otherwise provided by law and except for meetings of the holders of First Preference Shares as a class and meetings of the holders of Series E First Preference Shares as a series). In that event and for only so long as any such dividends remain in arrears, the holders of the Series E First Preference Shares will be entitled to receive notice of and to attend all shareholders’ meetings, other than meetings at which only holders of another specified class or series are entitled to vote, and to one vote for each Series E First Preference Share held. See “Details of the Offering — Description of the Series E First Preference Shares — Voting Rights”.

**Ratings:**

DBRS: Pfd-3 (high). S&P: P-2 (low). See “Ratings”.

**Tax on Preference Share Dividends:**

The Corporation will elect, in the manner and within the time provided under subsection 191.2(1) of the Tax Act, to pay or cause payment of the tax under Part VI.1 of the Tax Act at a rate such that the corporate holders of Series E First Preference Shares will not be required to pay tax under Part IV.1 of the Tax Act on dividends received on such shares. See

“Details of the Offering — Description of the Series E First Preference Shares — Tax on Preference Share Dividends” and “Canadian Federal Income Tax Considerations”.

**Listing:**

The TSX has conditionally approved the listing of the Series E First Preference Shares, as well as the Common Shares issuable upon the conversion of either the Series D First Preference Shares or the Series E First Preference Shares. Listing will be subject to the Corporation fulfilling all of the listing requirements of the TSX on or before July 12, 2004. See “Details of the Offering — Description of the Series E First Preference Shares — Listing” and “Plan of Distribution”.

**Earnings Coverage:**

Earnings coverage information for the Series E First Preference Shares is provided in the Prospectus under the heading “Earnings Coverage Ratios”.

**Book-Entry Only System**

Registration of interests in and transfers of the Units, Series E First Preference Shares and, following the Early Expiry Time if the Acquisition does not close on or prior to June 30, 2004, Series D First Preference Shares will be made through the book-entry only system of The Canadian Depository for Securities Limited (“CDS”). The Units, Series E First Preference Shares and, following the Early Expiry Time if the Acquisition does not close on or prior to June 30, 2004, Series D First Preference Shares must be purchased, transferred and surrendered for conversion or redemption through a participant in the CDS book-entry only system (a “CDS Participant”). Beneficial owners of Units, Series E First Preference Shares and, following the Early Expiry Time if the Acquisition does not close on or prior to June 30, 2004, Series D First Preference Shares will not have the right to receive physical certificates evidencing their ownership of such securities. If the Acquisition closes on or prior to June 30, 2004, following the Expiry Time, certificates for the Series D First Preference Shares will be issued in fully registered form to beneficial owners of such shares or their nominees.

**The Acquisition**

**Overview**

On September 15, 2003, Fortis entered into (i) a share purchase agreement with Aquila Networks Canada Ltd. (“ANCL”) for the purchase of all of the issued and outstanding shares, and the repayment of certain indebtedness, of the Alberta Utility (the “Alberta Purchase Agreement”), and (ii) a share purchase agreement with Aquila Networks British Columbia Ltd. (“ANBC” and together with ANCL, the “Vendors”) for the purchase of all of the issued and outstanding shares, and the repayment of certain indebtedness, of the B.C. Utility (the “B.C. Purchase Agreement”), for aggregate consideration of \$1,360 million. The Alberta Purchase Agreement and the B.C. Purchase Agreement are hereinafter collectively referred to as the “Acquisition Agreements”. The purchase price is subject to certain adjustments, including with respect to working capital and changes to property, plant and equipment. The closing of the Acquisition is subject to receipt of required regulatory and other approvals, including those of the Alberta Energy Utilities Board (“AEUB”) and the British Columbia Utilities Commission (“BCUC”), and the satisfaction of closing conditions customary to acquisitions of this type. Applications to the AEUB and BCUC for approval of the sale of the Alberta Utility and the B.C. Utility were filed on October 17, 2003 and December 1, 2003, respectively. The application to the AEUB with respect to the Alberta Utility’s sale will be heard in February 2004. The BCUC has not yet made a decision as to whether it will proceed without a hearing with respect to the application for the B.C. Utility’s sale. The closing of the Acquisition is expected to occur in the second quarter of 2004. See “Acquisition Agreements”.

The Alberta Utility and the B.C. Utility together provide electricity to more than 525,000 customers in 160 communities in southern British Columbia and southern and central Alberta. The Alberta Utility and the B.C. Utility own and operate an aggregate of approximately 110,000 kilometres of electric transmission and distribution lines and the B.C. Utility owns 205 megawatts (“MW”) of hydroelectric generation capacity. On December 31, 2002, the Alberta Utility and the B.C. Utility had an aggregate of \$1,308 million in assets, an aggregate rate base of approximately \$943 million and an aggregate of approximately 1,200 employees.

The Corporation intends to finance the purchase price for the Acquisition, including the repayment of certain indebtedness of the Alberta Utility and the B.C. Utility, from a portion of the net proceeds of the Offering, the net proceeds from the exercise of the Warrants and from the subscription receipt offering completed by the Corporation in October 2003 and funds to be made available to the Corporation, the Alberta Utility and the B.C. Utility under acquisition financing arranged by the Corporation for this purpose. See “Financing of the Acquisition” and “Use of Proceeds”.

Under the Acquisition Agreements, either party thereto may elect to terminate the agreements if the Acquisition is not completed prior to 12:00 (noon) (Toronto time) on June 30, 2004 (subject to extension, if any, for completion of dispute resolution relating to defect payments, which may be payable to Fortis). It is a condition of closing that the acquisition of the Alberta Utility and the B.C. Utility occur contemporaneously.

### **The Alberta Utility**

The Alberta Utility owns and operates a largely rural distribution system in a substantial portion of southern and central Alberta. It distributes electricity to more than 385,000 customers in Alberta, of which 311,000 are classified as residential. The Alberta Utility’s distribution system includes approximately 100,000 kilometres of power lines that distribute electricity from transmission systems or generators owned by third parties to consumers. The Alberta Utility does not own any substation, transmission or generation assets. The retail business, including accounts receivable, that formerly comprised part of the Alberta Utility’s assets was disposed of in transactions completed on November 28, 2000 and January 1, 2001, for aggregate consideration of approximately \$210 million. The Alberta Utility is not engaged in any material unregulated activities.

On December 31, 2002, the Alberta Utility had \$847 million in assets and a rate base of approximately \$527 million. Fortis expects the Alberta Utility’s rate base to grow to approximately \$800 million by 2008 as a result of customer growth and capital expenditures. For the year ended December 31, 2002, the Alberta Utility had electrical rate revenues of \$248 million and net income of \$28 million.

The Alberta Utility is regulated by the AEUB using a cost of service methodology. The regulated capital structure for the Alberta Utility is currently 60% debt and 40% equity. The Alberta Utility’s rates currently provide for a regulated rate of return of 9.50% on the 40% equity component of its rate base.

Fortis believes that the business operated by the Alberta Utility is attractive for the following reasons: (i) the Alberta Utility’s operations are entirely regulated and complement Fortis’ experience in regulated distribution; (ii) the cost of service regulatory framework in Alberta allows recovery of all approved costs as well as an appropriate return on equity; (iii) it is not subject to any electricity commodity risk; (iv) the Alberta Utility’s distribution system is efficient and well maintained; (v) the Alberta Utility has an attractive service territory providing for well diversified distribution revenues; and (vi) strong economic trends in Alberta are anticipated to result in low-risk rate base growth provided by new customer connections and required capital expenditures.

### **The B.C. Utility**

The B.C. Utility operates as a regulated, integrated utility which generates, transmits and distributes electricity in the southern interior of British Columbia to approximately 140,000 customers, of which 50,000 customers are served through the wholesale sale of power by the B.C. Utility to municipal distributors. The B.C. Utility’s integrated utility assets include four hydroelectric generating plants on the Kootenay River with an aggregate installed capacity of 205 MW, which supply approximately 50% of the B.C. Utility’s customer electricity requirements, and approximately 10,000 kilometres of transmission and distribution lines. The balance of the B.C. Utility’s electricity requirements are met through a portfolio of long and short-term power purchase contracts approved by the BCUC, the cost of which is flowed through to customers. The B.C. Utility’s unregulated activities are not material relative to its regulated operations, but provide an opportunity to enhance utilization of the B.C. Utility’s utility operation and management resources under service contracts to third parties.

On December 31, 2002, the B.C. Utility had \$461 million in assets and a rate base of approximately \$416 million. Fortis expects the B.C. Utility’s rate base to grow to approximately \$780 million by 2008 as a result of a comprehensive capital expenditure program aimed at meeting customer growth, improving reliability and lowering operating costs. For the year ended December 31, 2002, the B.C. Utility had revenues of \$154 million and net income of \$12 million, excluding a \$6 million after-tax, non-recurring charge.

The B.C. Utility is regulated by the BCUC. The regulated capital structure for the B.C. Utility is approximately 60% debt and 40% equity. The regulated return on equity for 2003 was 9.82% and is expected to be 9.55% in 2004 based on the application of the BCUC formula for setting regulated return on equity. The B.C. Utility also has the benefit of a performance-based regulation mechanism that allows it to share up to 50% of various cost savings with the balance returned to customers.

Fortis believes that the business operated by the B.C. Utility is attractive for the following reasons: (i) the business of the B.C. Utility is virtually entirely regulated and complements Fortis' experience with integrated utilities; (ii) the B.C. Utility has an attractive service territory with revenue diversity from a mature customer base; (iii) the B.C. Utility offers significant opportunity for low-risk, regulated rate base growth due to its capital expenditure program focused on reliability; (iv) the B.C. Utility has 205 MW of regulated hydroelectric generation capacity; and (v) the B.C. Utility has virtually no commodity exposure.

### Utility Management Approach of Fortis

Fortis' approach to utility management is based on creating value for customers that ultimately translates into long-term value for shareholders. Fortis maintains proximity to its customers in each jurisdiction where it carries on a utility business by structuring its operating utilities as separate operating companies with dedicated, focused, local management teams that have the benefit of access to Fortis' utility management experience and expertise. This allows local managers to build relationships with customers and regulators. Fortis recognizes that regulation is a key aspect of its core business and has developed a disciplined, cost-conscious asset investment and operating philosophy to achieve these objectives.

Fortis believes the businesses of the Alberta Utility and the B.C. Utility are complementary to its proven core competencies in managing regulated distribution and hydroelectric investments. In addition, Fortis believes the Acquisition provides a broader platform on which to deploy its regulatory operating and management expertise.

The Acquisition is expected to be slightly dilutive to the earnings of Fortis in the early years following the closing of the Acquisition.

### Selected Pro Forma Consolidated Financial Information of the Corporation

The following table presents selected *pro forma* consolidated financial information of the Corporation for the year ended December 31, 2002 and the nine months ended September 30, 2003, after giving effect to the Acquisition and the Offering, based upon the assumptions and adjustments, as set out in the notes to the unaudited *pro forma* consolidated financial statements contained herein. The *pro forma* consolidated financial information set out below has been derived from these unaudited *pro forma* consolidated financial statements and should be read in conjunction with such statements and the notes thereto. The unaudited *pro forma* consolidated financial statements included in the Prospectus are not necessarily indicative of results of operations that would have occurred in the year ended December 31, 2002 or the nine months ended September 30, 2003 had the Acquisition been effective January 1, 2002.

	Nine months ended September 30, 2003	Year ended December 31, 2002
	(in millions of dollars, except per share amounts)	
Operating revenues .....	873	1,138
Operating expenses .....	652	849
Net operating income .....	222	289
Earnings (loss) applicable to common shares .....	(4) (1)	79
Total assets .....	3,809	— (2)
Earnings (loss) per common share (basic) .....	(0.17)	3.49

(1) Includes goodwill impairment charge of \$80 million.

(2) A *pro forma* balance sheet is required to be prepared as at September 30, 2003 but not as at December 31, 2002. Accordingly, a *pro forma* total assets amount has not been calculated as at December 31, 2002.

## FORTIS

Fortis was incorporated as 81800 Canada Ltd. under the *Canada Business Corporations Act* on June 28, 1977. The Corporation was continued under the *Corporations Act* (Newfoundland) on August 28, 1987 and on October 12, 1987 the Corporation amended its articles to change its name to “Fortis Inc.” The address of the head office and principal place of business of the Corporation is The Fortis Building, Suite 1201, 139 Water Street, St. John’s, Newfoundland and Labrador A1B 3T2.

Fortis is principally a diversified, electric utility holding company with six electric distribution and generation utility subsidiaries. It holds all of the common shares of Newfoundland Power Inc. (“Newfoundland Power”) and, through Fortis Properties Corporation (“Fortis Properties”), holds all of the common shares of Maritime Electric Company, Limited (“Maritime Electric”), which are the principal distributors of electricity in the provinces of Newfoundland and Labrador and Prince Edward Island, respectively. Through Maritime Electric, the Corporation owns FortisUS Energy Corporation (“FortisUS Energy”), which operates four hydroelectric generating stations in the State of New York. As well, through its wholly owned subsidiary FortisOntario Inc. (“FortisOntario”) and its subsidiaries Canadian Niagara Power Inc. (“CNPI”), Cornwall Street Railway, Light and Power Company Limited (“Cornwall Electric”) and Eastern Ontario Power Inc. (“Eastern Ontario Power”), Fortis distributes electricity to customers in Fort Erie, Port Colborne, Cornwall and Gananoque, Ontario.

Fortis also owns 100% of Central Newfoundland Energy Inc., (“Central Newfoundland Energy”), a non-regulated subsidiary, whose principal activity is its 51% involvement in the Exploits River Hydro Partnership project (the “Partnership Project”). The Partnership Project is a partnership with Abitibi-Consolidated Inc. (“Abitibi-Consolidated”) to develop additional capacity at Abitibi-Consolidated’s hydroelectric plant at Grand Falls-Windsor and to redevelop Abitibi-Consolidated’s hydroelectric plant at Bishop’s Falls, both in Newfoundland and Labrador.

Through a wholly owned subsidiary, Fortis also holds a 95% interest in Belize Electric Company Limited (“BECOL”). BECOL owns and operates the Mollejon hydroelectric facility, located on the Macal River in Belize, Central America. Also in Belize, Fortis, through wholly owned subsidiaries, holds 67% of the outstanding shares of Belize Electricity Limited (“Belize Electricity”), the prime transmitter and distributor of electricity in Belize. Fortis also owns, through a wholly owned subsidiary, a 38.2% interest in Caribbean Utilities Company, Ltd. (“Caribbean Utilities”), the sole provider of electricity to the island of Grand Cayman, Cayman Islands.

Through its non-utility, wholly owned subsidiary, Fortis Properties, Fortis has investments in commercial real estate and hotel operations primarily in Atlantic Canada.

Fortis believes that its primary focus of growth will be the acquisition of electric utility assets. Fortis will continue to pursue acquisition opportunities both in Canada and outside of Canada. Fortis will also carry out strategic assessments of its non-utility operations to identify and, in appropriate circumstances, capitalize on opportunities where prospects of enhancing existing non-utility operations exist.

### **Newfoundland Power**

Newfoundland Power operates an integrated generation, transmission and distribution system throughout the island portion of Newfoundland and Labrador. Newfoundland Power serves approximately 220,000 customers, constituting 85% of all electricity customers in the province. Approximately 90% of the energy required by Newfoundland Power is purchased from Newfoundland and Labrador Hydro Corporation, a provincial Crown corporation. Newfoundland Power generates the balance of its energy requirements. It has an installed generating capacity of approximately 147 MW comprised of hydroelectric, diesel and gas turbine generation with the bulk, 95 MW, coming from hydroelectric facilities.

### **FortisOntario**

FortisOntario is an integrated electric utility. Through FortisOntario’s wholly owned subsidiaries, CNPI, Cornwall Electric and Eastern Ontario Power, electricity is distributed to approximately 52,000 Ontario customers in Fort Erie, Port Colborne, Gananoque, Cornwall, South Glengarry, South Stormont and the Ontario portion of the Mohawk Territory of Akwesasne. FortisOntario owns and operates the 75 MW Rankine Electric Generating Station on the Niagara River in Niagara Falls, Ontario. FortisOntario’s licence to divert water from the Niagara River will expire on April 30, 2009. The Lieutenant Governor in Council of Ontario may, in its sole discretion, extend this licence for a further 20-year term. FortisOntario also owns and operates a 5 MW gas-fired cogeneration plant that provides district heating to commercial customers in Cornwall, Ontario. FortisOntario’s wholly owned subsidiary, FortisOntario



Generation Corporation, generates electricity from five hydroelectric generating stations with a combined capacity of 8 MW.

On August 14, 2003, CNPI and Cornwall Electric, both regulated subsidiaries of FortisOntario, issued by way of private placement \$52 million aggregate principal amount of 7.092% senior unsecured notes maturing in 2018. The proceeds of the private placement were used primarily to refinance existing short-term indebtedness.

### **Maritime Electric**

Maritime Electric operates an integrated electric utility, which directly supplies approximately 67,500 customers constituting over 90% of the electricity consumers on Prince Edward Island. Maritime Electric owns and operates generating plants on Prince Edward Island with a total capacity of 100 MW but purchases most of the energy it distributes to its customers from New Brunswick Power, a provincial Crown corporation, and Emera Inc. Maritime Electric's system is connected to the mainland power grid via two submarine cables between Prince Edward Island and New Brunswick.

In December 2003, the Legislative Assembly of Prince Edward Island passed legislation to return Maritime Electric to traditional cost of service regulation effective January 1, 2004. Previously, Maritime Electric operated under price cap regulation. Maritime Electric's rates are currently frozen at December 31, 2003 levels pending approval of new rates by the Island Regulatory and Appeals Commission. Maritime Electric is in the process of preparing a submission to the Island Regulatory and Appeals Commission pursuant to which it will request a favourable return on equity and revenue requirements for 2004. The submission must be filed by May 1, 2004.

On September 29, 2003, Hurricane Juan hit Prince Edward Island and caused approximately \$800,000 in damages to Maritime Electric's electrical system. The majority of the cost will be recovered through insurance and no long-term impact to the electrical system is expected.

Maritime Electric's wholly owned subsidiary, FortisUS Energy, operates four hydroelectric generating stations in upper New York State having a combined generating capacity of 23 MW.

### **Belize Electricity**

Belize Electricity is the primary transmitter and distributor of electric power in Belize. Serving approximately 62,900 customers, Belize Electricity satisfies Belize's aggregate peak demand of 57 MW from multiple sources, which include power purchases from BECOL, the Comisión Federal de Electricidad, which is the Mexican state-owned power company, and from its own oil-fired generating stations. Belize Electricity currently operates 49.3 MW of oil generation.

Belize Electricity has signed a new power purchase agreement with Hydro Maya Limited. The agreement is to purchase output from a 2.6 MW run of the river hydroelectric plant in the Punta Gorda District (Southern Belize) which is expected to become operational in January 2006. It is expected that annual energy output will average 11.5 gigawatt hours ("GWh").

### **BECOL**

BECOL owns and operates the Mollejon hydroelectric facility located on the Macal River in Belize, Central America. The facility is a 25 MW generating plant capable of delivering average annual energy of 80 GWh and is the only commercial hydroelectric facility in Belize. BECOL sells its entire output to Belize Electricity. BECOL operates under various agreements with the Government of Belize and Belize Electricity, including a 50-year power purchase agreement with Belize Electricity and a franchise agreement with the Government of Belize. The franchise agreement grants BECOL the right to use the water in the Macal River upstream of the Mollejon plant for hydroelectric generation and the Government of Belize has agreed not to grant any rights or take any action that would impede the amount or quality of water flow on the upper Macal River.

In November 2001, BECOL received environmental clearance for the Chalillo project (the "Chalillo Project"), an upstream storage and generation facility that is expected to increase BECOL's annual energy production from an average of 80 GWh to 160 GWh. In December 2002, BECOL received additional support for the Chalillo Project when, in response to a challenge initiated by the Belize Alliance for Conservation Non-Government Organizations ("BACONGO") who oppose the construction of a hydroelectric dam, the Supreme Court of Belize ruled that the environmental approvals for the Chalillo Project were in order. In March 2003, the Court of Appeal upheld this ruling of the Supreme Court of Belize and the Public Utilities Commission of Belize approved construction of the Chalillo

Project. In its decision, the Court of Appeal also granted leave to appeal its decision to the Judicial Committee of the Privy Council (the “Privy Council”). In April 2003, an application for injunctive relief was filed with the Privy Council to prevent construction of the Chalillo Project. On August 13, 2003, the Privy Council ruled that it would not grant BACONGO its request for an injunction against the Chalillo Project. On December 4, 2003, the Privy Council concluded the hearing of the full appeal application. A decision is expected to be rendered in the first quarter of 2004.

### **Caribbean Utilities**

Caribbean Utilities is the sole provider of electricity to the Island of Grand Cayman, Cayman Islands pursuant to an exclusive 25-year licence renewable in 2011 with the Government of the Cayman Islands (the “Cayman Government”). Caribbean Utilities generates, transmits and distributes electricity to more than 20,000 customers and currently has an installed capacity of 123 MW.

Caribbean Utilities submitted a proposal to the Cayman Government in July 2002 to extend its current licence and replace the 15% return on rate base mechanism for adjusting consumer rates with a price cap mechanism. Under the proposal, electricity rates would be tied to and move with published inflation indices. Additionally, Caribbean Utilities would continue to recover fuel cost, regulatory cost, and government levies. Caribbean Utilities anticipates that, under the proposed regulatory framework, it would continue to have the potential to achieve returns that are consistent with investor expectations.

Caribbean Utilities filed its 2003 annual return with the Cayman Government as required under the terms of its licence. The annual return indicated that, pursuant to the terms of its licence, Caribbean Utilities was entitled to a 3% rate increase, which it implemented effective August 1, 2003. The Cayman Government responded in August 2003 by requesting a voluntary rollback of the rate increase effective immediately and indicating that it would consider seeking injunctive relief against Caribbean Utilities if it did not comply. Caribbean Utilities and the Cayman Government have agreed to resume negotiations in an attempt to resolve this matter. Concurrent with the re-commencement of negotiations, Caribbean Utilities agreed to reduce basic electricity rates by 3% with effect from November 1, 2003.

### **Central Newfoundland Energy**

In June 2001, the Corporation, through a non-regulated subsidiary, Central Newfoundland Energy, entered into an agreement with Abitibi-Consolidated to develop additional capacity at Abitibi-Consolidated’s hydroelectric plant at Grand Falls-Windsor and to redevelop Abitibi-Consolidated’s hydroelectric plant at Bishop’s Falls, Newfoundland and Labrador. The project is expected to cost \$68 million, of which \$65 million has been incurred as of September 30, 2003. The project has been financed principally with non-recourse debt and will increase annual energy production from the two hydroelectric plants by approximately 140 GWh. The installation of six new generating units and the refurbishment of the remaining three units at the Bishop’s Falls generating station was completed in April 2003 and the Bishop’s Falls hydroelectric plant was officially inaugurated on July 28, 2003. On November 3, 2003, Central Newfoundland announced the installation of the new 30 MW Beeton turbine unit at the Grand Falls-Windsor hydroelectric generating station, which was completed two months ahead of schedule.

### **Fortis Properties**

Fortis Properties is a leading owner and operator of commercial real estate and hotels in Atlantic Canada and has recently expanded its hotel operations to Ontario. Fortis Properties is the only non-utility subsidiary of Fortis and the primary vehicle for diversification and growth outside the electric utility business, with interests in office buildings, shopping centres, hotels and the provision of property management services. At December 31, 2003, Fortis Properties held a commercial real estate portfolio of 2.7 million square feet and 12 hotels with more than 2,100 rooms. Its assets and income are distributed between Newfoundland and Labrador, Nova Scotia, New Brunswick and Ontario and are diversified between commercial real estate and hotel operations, providing stability and opportunity for growth.

On September 17, 2003, Fortis Properties completed a \$35 million, ten-year refinancing of the Brunswick Square complex in Saint John, New Brunswick.

On October 1, 2003, Fortis Properties acquired four full-service hotels in Ontario from FelCor Lodging Trust for \$43.2 million. The hotels are located in Sarnia, Kitchener-Waterloo, Cambridge and Peterborough. The four hotels, with a total of 630 rooms, range in size from 143 to 184 rooms. On October 20, 2003, Fortis Properties secured a \$30 million 10-year 7.3% secured term credit facility in relation to these hotels.

## **Recent Developments**

Effective January 1, 2004, Karl W. Smith, the former Vice President, Finance and Chief Financial Officer of Fortis, was appointed President and Chief Executive Officer of Newfoundland Power replacing Philip G. Hughes who has been appointed the President of FortisWest Inc., which will be the holding company for the Alberta Utility and the B.C. Utility. Effective January 1, 2004, Barry V. Perry, the former Vice President, Finance and Chief Financial Officer of Newfoundland Power, was appointed Vice President, Finance and Chief Financial Officer of Fortis. Newfoundland Power expects to appoint a new Vice President, Finance and Chief Financial Officer in February 2004.

## **THE ACQUISITION**

### **Overview**

On September 15, 2003, Fortis entered into the Acquisition Agreements for aggregate consideration of \$1,360 million. The purchase price is subject to certain adjustments, including with respect to working capital and changes to property, plant and equipment. The closing of the Acquisition is subject to receipt of required regulatory and other approvals, including those of the AEUB and the BCUC, and the satisfaction of closing conditions customary to acquisitions of this type. Applications to the AEUB and BCUC for approval of the sale of the Alberta Utility and the B.C. Utility were filed on October 17, 2003 and December 1, 2003, respectively. The application to the AEUB with respect to the Alberta Utility's sale will be heard in February 2004. The BCUC has not yet made a decision as to whether they will proceed without a hearing with respect to the application for the B.C. Utility's sale. See "Acquisition Agreements". Under the Acquisition Agreements, either party thereto may elect to terminate the agreements if the Acquisition is not completed prior to 12:00 (noon) (Toronto time) on June 30, 2004 (subject to extension, if any, for completion of dispute resolution relating to defect payments, which may be payable to Fortis). It is a condition of closing that the acquisition of the Alberta Utility and the B.C. Utility occur contemporaneously.

Aquila, a U.S.-based utility company with approximately US\$9 billion in assets at December 31, 2002 and 2002 revenues of over US\$2 billion, experienced a loss from operations of US\$2.1 billion in 2002. Fortis understands that Aquila has been working to restore its financial stability and refocus its business on owning and operating natural gas and electric utilities in the United States. Fortis understands that in the second quarter of 2003, Aquila, through its financial advisor Credit Suisse First Boston LLC, began a process to solicit interested buyers for its Canadian electric utility businesses in Alberta and British Columbia. Aquila received indicative bids in July from interested parties. Certain of these interested parties were selected to submit further bids in August. Following a period of negotiation, Fortis and the Vendors entered into the Acquisition Agreements on September 15, 2003.

The Corporation intends to finance the purchase price for the Acquisition, including the repayment of certain indebtedness of the Alberta Utility and the B.C. Utility, from a portion of the net proceeds of the Offering, the net proceeds from the exercise of the Warrants and from the subscription receipt offering completed by the Corporation in October 2003 and funds to be made available to the Corporation, the Alberta Utility and the B.C. Utility under acquisition financing arranged by the Corporation for this purpose. See "Financing the Acquisition" and "Use of Proceeds".

The Alberta Utility and the B.C. Utility together provide electricity to more than 525,000 customers in 160 communities in southern British Columbia and southern and central Alberta. The Alberta Utility and the B.C. Utility own and operate an aggregate of approximately 110,000 kilometres of electric transmission and distribution lines and the B.C. Utility owns 205 MW of hydroelectric generation capacity. On December 31, 2002, the Alberta Utility and the B.C. Utility had an aggregate of \$1,308 million in assets, an aggregate rate base of approximately \$943 million and approximately 1,200 employees.

### **Utility Management Approach of Fortis**

Fortis' approach to utility management is based on creating value for customers that ultimately translates into long-term value for shareholders. Fortis maintains proximity to its customers in each jurisdiction where it carries on a utility business by structuring its operating utilities as separate operating companies with dedicated, focused local management teams that have the benefit of access to Fortis' utility management experience and expertise. This allows local managers to build relationships with customers and regulators. Fortis recognizes that regulation is an important aspect of its core business and has developed a disciplined, cost-conscious asset investment and operating philosophy to achieve these objectives.

Fortis believes the businesses of the Alberta Utility and the B.C. Utility are complementary to its proven core competencies in managing regulated distribution and hydroelectric investments. In addition, Fortis believes the Acquisition provides a broader platform on which to deploy its regulatory and management expertise.

The Acquisition is expected to be slightly dilutive to the earnings of Fortis in the early years following the closing of the Acquisition.

## **ELECTRIC UTILITIES MARKET OVERVIEW**

### **Alberta**

#### ***History of Regulation of Distribution and Retail Services***

As a result of the 1998 amendments to the *Electric Utilities Act* (Alberta) (the ‘‘EUA’’) and the enactment and amendment of various related regulations, customers of regulated electric distribution access systems were given a choice, commencing January 1, 2001, to select their electric energy retailer. The electric distribution access systems continued to be regulated to provide distribution service for the commodity sale of electricity to end-users. Independent retailers became eligible to sell electricity to end-users within an electric distribution system service area, with the utility providing the distribution service.

The EUA provides the framework for the new structure in Alberta’s electric utility industry and introduces competition into the electric utility business. As of January 1, 2001, new generation was completely deregulated and retail competition was introduced. In August 2002, the Government of Alberta announced further changes to utility legislation in order to improve the environment for retail competition in the province of Alberta. The Government of Alberta introduced a new EUA during 2003, which is designed to bring customer choice for both natural gas and electricity into closer alignment as well as to move towards consistent regulatory treatment of investor-owned and municipally-owned utilities.

#### ***Generation***

Under the EUA, generation assets constructed after December 31, 1995 are not considered part of utility operations and rates are not regulated by the AEUB. All owners of new and existing generating units must exchange their electric energy through the Alberta Power Pool. Since 1998, 3,286 MW of new capacity has been added in Alberta and an additional 5,458 MW of new capacity is expected to be completed by 2006.

#### ***Transmission***

The electricity delivery system in Alberta consists of a large network of interconnected transmission and distribution lines and related facilities. Alberta has transmission interconnection with British Columbia and Saskatchewan. Alberta has virtually no direct interconnection with the United States. Power is typically imported or exported through British Columbia via the transmission lines of British Columbia Hydro and Power Authority (‘‘B.C. Hydro’’).

Under the EUA, separate wholesale tariffs for transmission must be approved by the AEUB. The transmission tariffs allow any owner of a generating unit to have access to the transmission system in Alberta and thus facilitate the sale of its power. The same transmission tariff is charged to each distribution utility or customer directly connected to the transmission system regardless of location. The equalization of transmission costs is achieved by having each owner of transmission facilities charge its costs to the independent system operator which aggregates these costs and charges a common transmission rate to all who use the transmission system.

#### ***Distribution***

Distribution of electricity throughout Alberta continues to be regulated by the AEUB. Under the EUA, separate rates for distribution access must be approved by the AEUB. Costs of distribution access are not equalized. The distribution utility provides the distribution access services for all customers under AEUB approved tariffs, which provide for the recovery of the cost-of-service, including a fair return on rate base.

The distribution system in Alberta is comprised of networks of the Alberta Utility, ATCO Ltd., multiple local distributors, including companies owned by the cities of Calgary and Edmonton, smaller municipalities and rural electrification associations.

## ***Retail***

As of January 1, 2001, all customers were granted a choice as to the supplier of their electric energy. Industrial and large commercial customers were required to select a retailer effective January 1, 2001. Residential, farm and small commercial and industrial customers may continue to purchase electricity from their current distribution utility until July 1, 2006 under a regulated rate option (a “Regulated Rate Option”).

The Regulated Rate Option tariff is also set by the AEUB and permits the distribution system utility to recover the cost of service of buying electric energy for and reselling it to customers within the distribution utility’s service area.

On December 11, 2002, the AEUB approved an application requesting the implementation on January 1, 2003 of a monthly method of calculating electricity prices for regulated rate option customers. The new methodology is intended to provide greater price transparency for customers and to prevent large collection shortfalls or surpluses that would require subsequent adjustment by the AEUB.

Current regulations in Alberta effectively permit the recovery of shortfalls in retail collection for electrical service for a period of one year.

## **British Columbia**

Historically, the electric market in British Columbia has been generally characterized by the traditional, integrated utility model, where electric utilities generate, transmit and distribute electricity throughout their respective service territories. The BCUC regulates electric utilities in British Columbia and is responsible for setting and enforcing reliability and quality of service standards and for setting rates.

The B.C. Utility and B.C. Hydro, a Crown corporation, are the two largest, vertically integrated utilities in British Columbia. B.C. Hydro serves the majority of electricity customers in British Columbia except in the B.C. Utility’s service area in the West Kootenay region and parts of the Okanagan region in the interior of British Columbia. B.C. Hydro owns over 80% of the provincial generating capacity (11,115 MW). The remaining capacity is owned by the B.C. Utility, Columbia Power Corporation (“CPC”), the City of Nelson, industrial plants, and various independent power producers. CPC is a Crown corporation whose primary mandate is to undertake power project investments as the agent of the province on a joint venture basis with the Columbia Basin Trust.

The British Columbia grid is connected to Alberta and to Washington State allowing power to be sold and purchased outside the province. Current transfer capacity is 3,150 MW from British Columbia to the United States, 2,000 MW from the United States to British Columbia, 1,000 MW from Alberta to British Columbia and 1,200 MW from British Columbia to Alberta.

On September 24, 1997, B.C. Hydro opened its transmission system to third parties as part of the requirement to obtain a Federal Energy Regulatory Commission licence. The wholesale market in British Columbia was opened to competition in 1999, when a portion of the wholesale electric customers was allowed to choose an alternative electricity supplier. In November 2002, the government issued its new energy policy, “Energy For Our Future: A Plan for B.C.”. The four cornerstones of the policy (the “Proposals”) are low electricity rates and public ownership of B.C. Hydro, secure reliable supply, more private sector opportunities, and environmental responsibility and no nuclear power sources. The Proposals recommended that B.C. Hydro be divided into three entities responsible for generation, transmission and distribution.

Under the Proposals, B.C. Hydro would manage its existing heritage assets and private producers would be expected to provide new power generation. Under the Proposals, B.C. Hydro would be expected to restructure such that its transmission activities are independent of its generation and distribution facilities. To date, an independent transmission company, the B.C. Transmission Company, has been established to plan, operate and manage the B.C. Hydro system with continuing public ownership of transmission assets and to provide non-discriminatory access to B.C. Hydro transmission system at rates determined by the BCUC.

In its Proposal, the government directed the BCUC to conduct an inquiry to develop and refine certain policy areas and to make recommendations on key policy initiatives. Pursuant to the government’s direction, the BCUC conducted a public inquiry process and on October 17, 2003, the BCUC released a report with 27 recommendations. On October 28, 2003, the government accepted 22 of the BCUC’s recommendations, including the two key recommendations that B.C. Hydro’s generation line of business enter into heritage contracts with B.C. Hydro’s distribution business in order to secure low-cost generation for all British Columbians and that a stepped-rate structure be adopted for large commercial and industrial consumers in order to encourage conservation and encourage investment in independent power generation.

## THE ACQUIRED BUSINESSES

The descriptions of the Alberta Utility and the B.C. Utility contained in the Prospectus are based on information provided by the Vendors in connection with the Acquisition Agreements. Fortis, after making its purchase investigations, believes it to be accurate in all material respects.

### **Aquila Networks Canada (Alberta) Ltd.**

#### ***Overview and History***

On August 31, 2000, the Alberta Utility acquired the electricity retail and distribution businesses in Alberta of TransAlta Utilities Corporation (“TransAlta”). On November 28, 2000, the Alberta Utility sold to EPCOR Energy Services (Alberta) Inc. (“EPCOR”) its intangible retail assets and certain related property, plant and equipment for consideration of \$110 million. On January 1, 2001, EPCOR also acquired the entire right, title and interest in the Alberta Utility’s customer accounts receivable for additional cash consideration of approximately \$100 million, before purchase price adjustments. No gain or loss was recorded on either the sale of the retail assets or the customer accounts receivable.

The Alberta Utility distributes electricity to more than 385,000 customers in Alberta. The Alberta Utility’s service territory is mainly rural and covers approximately 169,000 square kilometres. At December 31, 2002, the Alberta Utility had \$847 million in assets and a rate base of \$527 million. Fortis expects the Alberta Utility’s rate base to grow to approximately \$800 million by 2008 as a result of customer growth and capital expenditures. For the year ended December 31, 2002, the Alberta Utility had electrical rate revenues of \$248 million and net income of \$28 million.

#### ***Principal Benefits of Acquisition of the Alberta Utility***

Fortis believes that the business operated by the Alberta Utility is attractive for the following reasons: (i) the Alberta Utility’s operations are entirely regulated and complement Fortis’ experience in regulated distribution; (ii) the cost of service regulatory framework in Alberta allows recovery of all approved costs as well as an appropriate return on equity; (iii) it is not subject to any electricity commodity risk; (iv) the Alberta Utility’s distribution system is efficient and well maintained; (v) the Alberta Utility has an attractive service territory providing for well diversified distribution revenues; and (vi) strong economic trends in Alberta are expected to result in low-risk rate base growth provided by new customer connections and required capital expenditures.

### *The Alberta Utility Service Territory*



### *Asset and Business Summary*

The Alberta Utility is an electricity distribution utility whose physical asset base is entirely regulated. As an electricity distribution utility, the Alberta Utility's distribution system receives power from either the transmission system (which it does not own) or from small, third party power producers connected to the Alberta Utility's distribution system and then distributes the power at 25 kilovolt ("KV") and lower voltages to end-use customers in its territory. It, therefore, has no exposure to fuel or power purchase prices. In 2002, the Alberta Utility distributed approximately 23,000 GWh to its customers, which represented approximately 47% of total electricity consumption in Alberta in that year.

The Alberta Utility's distribution system comprises approximately 100,000 kilometres of overhead and underground conductors, approximately 150,000 service transformers and approximately 850,000 support structures. The Alberta Utility does not own any substation, transmission or generation assets. The overall quality of the Alberta Utility assets is consistent with a modern, utility standard. The Alberta Utility has entered into joint use agreements with telephone companies, municipal electricity companies and cable television companies under which the parties share the use and maintenance costs of the support structures they own and jointly use. The Alberta Utility is not engaged in any material unregulated activities.

### *System Growth*

The Alberta Utility's forecasted capital expenditures, which are primarily comprised of routine maintenance of the distribution system and expansion related to the connection of new customers, will increase the Alberta Utility's rate base. Fortis expects the Alberta Utility will have approximately \$117 million of capital expenditures, net of customer contributions, in 2004, which will be funded from internally generated funds. Over the next five years through 2008, Fortis expects capital expenditures will contribute to rate base growth averaging approximately 6% annually.

### ***Regulation and Current Distribution Rates***

The Alberta Utility is regulated by the AEUB under cost of service methodology, which allows the Alberta Utility to recover all prudently incurred operating expenses, depreciation, income tax and interest on debt in addition to a return on equity. Current rates were approved in July 2003 and became effective August 1, 2003. The Alberta Utility was provided a regulated rate of return on its equity of 9.50% on a capital structure that has a 40% deemed equity component. The actual capital structure of the Alberta Utility is consistent with the deemed structure.

An annual revenue requirement of \$205 million was approved by the AEUB for 2003. Approved operating costs of \$107 million were \$14 million less than requested in the Alberta Utility's application. Capital expenditures of approximately \$107 million were also approved. The most significant change in the revenue requirement was a reduction in the depreciation rate of its distribution system assets from about 5.2% to 3.8% which is more in line with industry averages. This change resulted in a reduction in annual depreciation expense of approximately \$25 million requiring a \$37 million (13.5%) reduction in rates, and a \$40 million rebate of 2002 rates. This change was applied retroactively and will remain in effect until a detailed depreciation study is completed by the Alberta Utility. During 2003, actual revenues were reduced by approximately \$68 million to reflect over collections during the January 2002 through September 2003 period. Since the rebate in respect of 2002 revenue was made in 2003, financial results in 2003 compare unfavourably to 2002 and are expected to compare unfavourably to 2004. A lower depreciation rate means capital expenditures will exceed approved depreciation by a greater amount (all things being equal), resulting in growth in rate base.

Under current legislation, the Alberta Utility may maintain existing rates and generally does not need to reapply each year unless it wishes to establish new rates.

On September 30, 2002, the AEUB issued a notice that it will be conducting a generic cost of capital proceeding for the purpose of considering the advisability of adopting standard methodologies for setting utility rates of return and capital structures. This proceeding commenced in late 2003 and is ongoing. The implementation of a standardized approach to determination of capital structure and rate of return for utilities in Alberta will be examined in the generic cost of capital proceeding. Fortis believes that the AEUB may begin setting rates of return by automatic formula beginning in 2005.

### ***Service Territory Demographics — Customer and Load Mix***

Alberta is an attractive service territory with strong economic growth measured by Gross Domestic Product ("GDP") growth at 9.2% annually for the five-year period ended 2002, ranking it second only to Newfoundland and Labrador among all provinces during that period.

The Alberta Utility serves approximately 385,000 residential, commercial, farm and industrial customers. Distribution revenues are well diversified by customer type. Residential customers constitute the largest customer class numbering over 311,000 and accounted for approximately 33% of total revenues and 9% of total electricity load ("load") in 2002. Industrial customers accounted for 29% of total revenues and 73% of total load in 2002. The oil and gas industry represents a significant majority of the Alberta Utility's industrial revenues. Commercial customers, including office buildings, department stores, malls, schools, hospitals, warehouses and other businesses, accounted for 23% of total revenues and 12% of total load in 2002. Farm customers accounted for 12% of the total revenues and 5% of total load in 2002.

Since 1996, the residential segment has experienced the strongest customer growth at over 3% annually. Over the past decade the Alberta Utility's distribution system has experienced average annual customer growth of 2% to 3%. Fortis expects annual customer growth to remain consistent with historical levels.

Fortis believes that there are opportunities for significant improvement in customer service to a level equivalent to other Fortis utilities.

### ***Franchises***

The Alberta Utility serves 115 communities through standardized, individual franchise agreements that allow it to provide service in those communities. The typical franchise agreement in Alberta is for ten years, and it can be extended for five years upon mutual consent. Approximately 80% of the Alberta Utility's municipal franchises are based on a standard agreement that has an initial term that runs to 2011 or 2016 with the renewal option. The remaining municipal franchises are governed by legislation that requires the municipality to give notice of termination in which



case the Alberta Utility, as franchise holder, is required to be compensated. The City of Airdrie has given the Alberta Utility notice of its intention to terminate its franchise agreement. The Alberta Utility and the City of Airdrie are currently before the AEUB to establish the appropriate compensation of the Alberta Utility's assets in the City of Airdrie. The assets in the City of Airdrie have a rate base in excess of \$9 million. The AEUB will hear this matter in April 2004.

### ***Supply of Power to Customers***

As an owner of an electric distribution system under the EUA, the Alberta Utility is required to make arrangements with or act as a default retailer to carry out the retailer functions for those large commercial and industrial customers that did not select a retailer by November 1, 2000 and may designate a supplier of last resort to provide electricity services to customers otherwise unable to obtain electricity services. In order to remain solely a distribution utility, in November 2000, the Alberta Utility appointed EPCOR to be a default retailer and supplier of last resort in its territory until the end of 2005. The Alberta Utility also has, either directly or indirectly, entered into approximately 80 service contracts with retailers.

### ***Selected Historical Financial Information of the Alberta Utility***

The following table presents selected financial and operating information for the Alberta Utility for the years ended December 31, 2002 and 2001 and the nine months ended September 30, 2003 and 2002. The following information should be read in conjunction with the historical financial information of the Alberta Utility included in the Prospectus.

	<b>Nine months ended September 30,</b>		<b>Year ended December 31,</b>	
	<b>2003</b>	<b>2002</b>	<b>2002</b>	<b>2001</b>
	(in millions of dollars)			
Total revenues . . . . .	123	187	269	253
Operating expenses . . . . .	86 (1)	123	183	178
Net operating income . . . . .	37 (1)	64	86	75
Net earnings (loss) . . . . .	(61)	20	28	12
Total assets . . . . .	802	— (2)	847	1,011

(1) Excludes goodwill impairment charge of \$80 million.

(2) A balance sheet as at September 30, 2002 was not required for the purpose of the Prospectus.

### ***Operational Environment***

The operational environment in the Alberta Utility's service territory does not materially adversely impact utility operations with relatively limited snow, ice and extreme wind conditions.

### ***Safety and Reliability***

The Alberta Utility provides safe and reliable service throughout its service territory. The Alberta Utility's reliability statistics are in the top quartile when compared with other Canadian Electricity Association utilities.

### ***Employees***

The Alberta Utility has approximately 820 employees. The Alberta Utility has two collective agreements with the United Utility Workers Association, which expire on December 31, 2005.

### ***EPCOR Litigation***

In November 2000, EPCOR purchased from the Alberta Utility various assets necessary to operate the call centre and billing centre operations of the Alberta Utility. Additionally, EPCOR entered into agreements (the "EPCOR Agreements") pursuant to which it was appointed as the exclusive default retailer and supplier of last resort to customers within the Alberta Utility's service area and was granted the exclusive right to act as a retailer within the Alberta Utility's service area for customers purchasing electricity under the Alberta Utility's regulated rate tariff pursuant to a Regulated Rate Option Appointment Agreement.

Under the EPCOR Agreements, the Alberta Utility agreed to supply EPCOR, in a timely manner, with all information, including load settlement meter data in relation to customers in the Alberta Utility's service area, to permit EPCOR to exercise its rights and perform its duties under the EPCOR Agreements. On August 18, 2003, EPCOR filed a Statement of Claim in the Court of Queen's Bench of Alberta in the Judicial District of Edmonton against the Alberta Utility, ANCL and Aquila. EPCOR's claim is that the Alberta Utility, as owner of the distribution system, and ANCL, as the wire services provider, failed to provide EPCOR with timely and accurate information and data required by EPCOR to operate the retail business acquired from the Alberta Utility. EPCOR's claim alleges breaches of the EPCOR Agreements, breach of fiduciary duty and statutory duty by the Alberta Utility and ANCL, as well as negligence. EPCOR is seeking approximately \$83 million in damages, interest, costs, an order compelling the Alberta Utility and ANCL to comply with the EPCOR Agreements and an order requiring the Alberta Utility to comply with its obligations. Aquila has been named as a defendant in the litigation as it guaranteed the performance by the Alberta Utility and ANCL of the EPCOR Agreements.

No statement of defence has yet been filed. The Alberta Utility and ANCL have asked for further and better particulars regarding certain aspects of the statement of claim and are waiting for a further response from EPCOR before preparing and submitting a statement of defense. Given the preliminary stage of the pleadings, the Alberta Utility and ANCL have not to date made any definitive assessment of potential liability with respect to the litigation. In negotiating the purchase price and the terms of the Acquisition, Fortis took into consideration the potential liability of the defendants to EPCOR as a result of this claim. See "Acquisition Agreements — Indemnities" and "Risk Factors — EPCOR Litigation".

#### **Aquila Networks Canada (British Columbia) Ltd.**

##### ***Overview***

The B.C. Utility operates as a regulated integrated utility and generates, transmits, distributes and sells electricity in the southern interior of British Columbia to approximately 140,000 customers, of which 50,000 customers are served through the wholesale sale of power to municipal distributors in Summerland, Penticton, Kelowna, Grand Forks, Nelson and Princeton. The B.C. Utility's operations cover a 50,000 square kilometre service territory.

To supply customers with electricity, the B.C. Utility owns 205 MW of regulated hydroelectric generation capacity and meets the balance of its requirements through a portfolio of long-term and short-term power purchase contracts approved by the BCUC, the costs of which are flowed through to customers.

At December 31, 2002, the B.C. Utility had assets of \$461 million and a rate base of approximately \$416 million. Fortis expects the B.C. Utility's rate base to grow to approximately \$780 million by 2008. Rate base growth is expected as a result of a comprehensive capital expenditure program aimed at meeting customer growth, improving reliability and lowering operating costs. Major components of the planned capital program, which have regulatory approval, include replacement of significant portions of the transmission system, upgrades to the hydroelectric generating plants and development of new substations. For the year ended December 31, 2002, the B.C. Utility had revenues of \$154 million and net income of \$12 million, excluding a \$6 million after-tax non-recurring charge.

##### ***Principal Benefits of Acquisition of the B.C. Utility's Business***

Fortis believes that the business operated by the B.C. Utility is attractive for the following reasons: (i) the business of the B.C. Utility is virtually entirely regulated and complements Fortis' experience with integrated utilities; (ii) the B.C. Utility has an attractive service territory with revenue diversity from a mature customer base; (iii) the B.C. Utility offers significant opportunity for low-risk, regulated rate base growth due to its capital expenditure program focused on reliability; (iv) the B.C. Utility has 205 MW of regulated hydroelectric generation capacity; and (v) the B.C. Utility has virtually no commodity exposure.

## *The B.C. Utility Service Territory*



### *Asset and Business Summary*

The B.C. Utility's integrated utility assets comprise an integrated network of generation, transmission and distribution assets. The B.C. Utility system interconnects with the B.C. Hydro system and generation facilities owned by others providing additional supply and reliability benefits. The generation assets consist of four hydroelectric generating plants on the Kootenay River with an aggregate installed capacity of 205 MW. Its operations include approximately 10,000 kilometres of transmission and distribution power lines. The transmission assets include approximately 18 terminal transformers. The distribution system is comprised of 70 distribution substations, approximately 28,000 distribution service transformers and approximately 75,000 support structures. The B.C. Utility has entered into joint use agreements with telephone, municipal electricity and cable television companies under which the parties share the use and maintenance costs of the support structures they own and jointly use. Total electricity distributed to end use customers was approximately 2,800 GWh, with a peak system load of approximately 675 MW in 2002.

### *System Growth*

In the late 1990s, in response to growing customer load and the desire to upgrade significant portions of the system to modern standards in order to ensure continued high reliability and reduced operating cost, the B.C. Utility established a comprehensive system renewal and redevelopment plan (the "Master Plan"). The Master Plan has been filed with the BCUC and, subject to making individual CPCN (as defined below) applications, the B.C. Utility expects it will be allowed to recover capital expenditures incurred to implement those expenditures of the Master Plan approved by the BCUC through its rates. While sustaining capital expenditures related to routine maintenance are approximately \$15 million annually, investment in the B.C. Utility's electrical system is expected to add over \$300 million to its rate base by the end of 2008, an average annual increase in the B.C. Utility's rate base of approximately 11%. Capital expenditures are undertaken when approved by the BCUC pursuant to applications by the B.C. Utility for Certificates of Public Convenience and Necessity ("CPCN") which ensures proposed expenditures have regulatory support and

can be added to the rate base to earn a regulated return. When the projects identified in the Master Plan are complete, significant portions of the B.C. Utility system will consist of components consistent with a modern, utility standard.

Major projects identified in the Master Plan include:

- (a) a new, 230kV line and related station facilities in the Lower Columbia area to replace the current 63kV system;
- (b) upgrades to the B.C. Utility's four Kootenay River hydroelectric plants;
- (c) a new substation at Vaseux Lake (South Okanagan); and
- (d) distribution system upgrades.

#### 230kV System Development Project

A CPCN was granted in June 2000 for this project which involves the construction of a single new 230kV transmission line from South Slocan to Warfield, following a high-elevation backcountry corridor from South Slocan to Castlegar and the removal of multiple 63kV transmission lines. Switchyard improvements are also planned at the Brilliant Power Plant, Kootenay Canal Plant, and the B.C. Utility's four power plants on the Kootenay River and at the Warfield Station near Trail. This project represents a complete rebuild and reconfiguration of the transmission system in the Lower Columbia area. The new 230kV system will be interconnected with the facilities of other power producers and transmission operators in the region, thereby providing the B.C. Utility customers increased supply reliability and significantly reducing the likelihood of major outages. Additional expected benefits of the new system include reduced long-term operating and maintenance costs, improved safety, increased regional transmission capacity and reduced system losses.

When completed, the project is anticipated to be able to meet customer requirements in this region for the foreseeable future. The total cost of improvements is estimated to be approximately \$115 million of which approximately \$82 million is the B.C. Utility's estimated share. The first elements of this project were placed into service during 2003 and the project is expected to be complete during 2004. As part of this project, the B.C. Utility has recently entered into facility operations, management and interconnection agreements which will govern the operating and cost-sharing responsibilities between the B.C. Utility and the other utility system owners in the region.

#### Upgrades to the Kootenay River Hydroelectric Plants

A comprehensive hydroelectric generation upgrade program which will result in standardized electrical and mechanical components across all of the B.C. Utility's hydroelectric power plants has been initiated by the B.C. Utility. Total expected project costs from 2003 until completion in 2008 are approximately \$136 million. Newly installed equipment is expected to enhance reliability and efficiency, while the use of standardized components is expected to reduce future maintenance and capital expenditures.

#### Vaseux Lake (South Okanagan) Substation

In the late 1980s the B.C. Utility identified the need for additional electricity supply to the south Okanagan region to ensure customer demand post 2005 could be met at a reliability standard consistent with regulatory requirements. In order to increase supply to this region, the B.C. Utility is constructing a new 500kV substation. System improvements include terminal upgrades at Warfield, Grand Forks, Oliver and Penticton.

A CPCN for this project was granted by the BCUC in April 2003. Total project costs of approximately \$75.9 million are expected and the facilities are scheduled to be in service by September 2005.

#### Distribution System Upgrades

Distribution system upgrades consist of improvements in the Trail area distribution system to renew obsolete components at or near the end of their useful life, to establish a standard voltage and to accommodate load growth that has caused load on the existing system to approach design capacity. Additional projects over the next five years include reliability upgrades in the Creston, Osoyoos and Slocan Valley regions.

Serious forest fires in British Columbia in 2003 caused an estimated \$1.4 million in damage to the transmission and distribution system of the B.C. Utility. Fortis expects that these costs for the repair and upgrading of the system will be recovered in future rates.

### ***Regulation and Current Rates***

The B.C. Utility is regulated by the BCUC under a performance-based framework. The performance-based framework rewards cost-efficiency by allowing the utility shareholder to participate in achieved cost reductions, while providing for cost of service regulation during certain test years with subsequent rates determined by inflation less a defined productivity improvement factor. The reset of rates at defined intervals pursuant to a cost of service methodology allows the utility the benefit of recovery of prudently incurred operating costs and appropriate return on capital. The B.C. Utility operates as a regulated integrated utility — all of its assets constitute part of its rate base and prudently incurred power purchase costs are passed through to customers.

The B.C. Utility's 2003 rates were set through a combination of the performance-based rate setting mechanism and a negotiated settlement of forecasts and extraordinary costs and deferrals. The existing performance-based rate mechanism has established a revenue requirement for 2003 based on tested forecast cost of service for 2000. The base revenue requirement is escalated each year based on customer and sales growth and inflation, less defined productivity improvement factors which for 2003 had been set at 1.0%. The revenue requirement is also adjusted for extraordinary capital and operating costs approved by the BCUC, forecast power purchases and changes in the cost of capital. The B.C. Utility regulated rate of return on its equity was set at 9.82% on a capital structure that has a 40% deemed equity component for 2003. The actual capital structure of the B.C. Utility is consistent with the deemed structure.

The year 2004 was to be a rate rebasing year for the performance-based rate mechanism. However, because of the proposed change in ownership, the B.C. Utility has filed an application with the BCUC to extend the existing settlement agreement and performance-based rate setting mechanism for 2004, with a rebasing in 2005. The application requests rates be established with a revenue requirement of \$169.2 million representing a 3.6% rate increase over 2003. The requested revenue requirement for 2004 is based on a combination of certain base costs, forecasts of sales and cost of purchased power, extraordinary costs and the amortization of approved deferrals, some of which may be adjusted through a negotiated settlement expected to take place in February 2004. A regulated rate of return of 9.55% on a 40% deemed equity is expected to be applied to the final settlement. Under the performance-based framework, risk and reward is shared with customers. The B.C. Utility shares in up to 50% of achieved savings. In light of the substantial capital expenditures, to mitigate the impact of rate increases for customers, the B.C. Utility, with the approval of the BCUC, has established a rate stabilization reserve that has been used to limit rate increases to a maximum of 5% annually.

Assuming that the B.C. Utility's application to extend the current settlement agreement and performance-based rate setting mechanism is granted, the performance-based rate mechanism is expected to be rebased for 2005 in a regulatory proceeding to be commenced in 2004. The rebasing will establish rates for 2005 on a cost of service basis using expected 2005 costs after a detailed review of each individual cost category. The performance-based rate mechanism and sharing mechanism used for establishing the B.C. Utility's revenue and rates for most years since 1992 has provided a return slightly higher than the regulated return set by the formula.

### ***Service Territory Demographics — Customer Mix***

The B.C. Utility serves a 50,000 square km service territory in the lower inland of British Columbia including the communities of Trail, Kelowna, Summerland, Penticton, Grand Forks, Castlegar, Rossland, Nelson and Princeton, serving approximately 140,000 customers, of which 50,000 customers are served through the wholesale sale of power to municipal distributors in Kelowna, Summerland, Penticton, Nelson and Grand Forks. The service territory is characterized as primarily rural residential. Key industries served by the B.C. Utility include the forestry and minerals industries.

The B.C. Utility has a diverse customer base comprised of residential, general service, wholesale (including municipal) and industrial customers. Low-risk residential customers constitute the largest customer class and accounted for approximately 42% of total revenues and 36% of the total load in 2002. Additional residential customers are served under wholesale service, whereby the B.C. Utility sells power to municipally owned distribution systems. This accounted for approximately 22% of total revenues and 31% of the total load in 2002. General service customers, including office buildings, department stores, malls, schools, hospitals, warehouses and other businesses accounted for 22% of total revenues and 19% of total load in 2002. Industrial customers accounted for 11% of total revenues and 12% of the total load in 2002.

Fortis believes that there are opportunities for significant improvement in customer service to a level equivalent to other Fortis utilities.

### *Supply of Power to Customers*

The B.C. Utility owns four hydroelectric generation facilities with an aggregate generation capacity of 205 MW located on the Kootenay River. The B.C. Utility meets approximately 50% of its power needs through generation or power entitlements related to these hydroelectric facilities and acquires most of its remaining supply requirements through power purchase contracts. The balance is met through spot market purchase contracts. Power purchase contracts are approved by the BCUC and prudently incurred costs are flowed through to customers through rates. This diverse power supply mix provides the B.C. Utility with the flexibility to respond to changes in demand load with virtually no commodity exposure.

#### **Owned Generation Facilities**

<u>UNIT</u>	<u>LOCATION</u>	<u>YEAR INSTALLED</u>	<u>UNIT CAPACITY (MW)</u>	<u>2002 NET GENERATION (MWH)</u>
No. 1 .....	Lower Bonnington	1924	41	289,851
No. 2 .....	Upper Bonnington	1907	59	214,662
No. 3 .....	South Slocan	1928	55	252,522
No. 4 .....	Corra Linn	1932	50	201,848
Total .....			205	958,883

### *Power Purchase Agreements*

#### Canal Plant Agreement

B.C. Hydro owns the 650 MW Kootenay Canal Generating Station (the “Canal Plant”), which diverts water from the Kootenay River into a man-made canal that feeds the Canal Plant and runs parallel to the B.C. Utility’s existing four plants on the Kootenay River, which are located between Castlegar and Nelson. In order to make efficient use of water flowing out of the Kootenay Lake and to avoid competing water demands between the existing generation facilities of the B.C. Utility and the Canal Plant, a coordination agreement (the “Canal Plant Agreement”) was entered into in August 1972.

The Canal Plant Agreement provides for certain electrical generation arrangements among the owners of hydroelectric generation in the Kootenay Region of southeastern British Columbia. Under the Canal Plant Agreement, B.C. Hydro utilizes water otherwise licensed for use by the B.C. Utility in its power generation plants at Corra Linn, Upper Bonnington, Lower Bonnington and South Slocan. In return, B.C. Hydro provides the B.C. Utility with a fixed annual entitlement to energy and capacity. The annual entitlement is determined, in accordance with the agreement, as a percentage of the simulated average capability of the generation facilities. The B.C. Utility’s power entitlements are approximately 205 MW of capacity and 1,540 GWh of energy. The B.C. Utility plants have to be maintained in a state of operational readiness in order to receive the full entitlements. In the event of a forced or maintenance outage, the entitlements are reduced by a proportionate amount. Allocation of the original generation entitlements considered the relative water use efficiencies of each of the generating units sharing the total water resources.

The Canal Plant Agreement is currently under negotiation for renewal prior to expiry in 2005.

#### Brilliant Power Purchase Agreement

Electricity generated by the Columbia Power Corporation and the Columbia Basin Trust (“CPC/CBT”) owned Brilliant Power Plant is transmitted to B.C. Hydro and, in exchange, B.C. Hydro allocates a specified amount of power and capacity to the Brilliant Power Plant under the Canal Plant Agreement. Under a power purchase agreement (the “BPPA”), the B.C. Utility has agreed to purchase from CPC/CBT on a long-term basis (a) the power and capacity allocated to the Brilliant Power Plant by B.C. Hydro and (b) after the expiration of the Canal Plant Agreement, the actual electrical output generated by the Brilliant Power Plant (collectively, the “Brilliant Entitlement”). During the 60-year term of the BPPA, CPC/CBT has agreed to sell and make available to the B.C. Utility the entirety of the Brilliant Entitlement. During the second 30 years of the BPPA, a market-based adjustment will be made to the price. The BPPA provides the B.C. Utility with approximately 25% of its power requirements in its service territory.

### Power Purchases from B.C. Hydro

The B.C. Utility is also party to a power purchase agreement with B.C. Hydro (the “B.C. Hydro PPA”) that provides the B.C. Utility with additional electricity for purposes of supplying its load requirements, up to a maximum demand of 200 MW, which constitutes about 23% of the B.C. Utility’s energy requirements. The current term of the B.C. Hydro PPA extends until 2013 and provides the B.C. Utility with electricity under fixed prices for that term.

### ***Selected Historical Financial Information of the B.C. Utility***

The following table presents selected financial and operating information for the B.C. Utility for the years ended December 31, 2002, 2001 and 2000 and the nine months ended September 30, 2003 and 2002. The following information should be read in conjunction with the historical financial information of the B.C. Utility included in the Prospectus.

	Nine months ended		Year ended		
	September 30, 2003	September 30, 2002	December 31, 2002	December 31, 2001	December 31, 2000
	(in millions of dollars)				
Total revenues	118	115	154	148	139
Operating expenses	90	86	134	109	105
Net operating income	28	29	20	39	34
Net earnings	12	12	6	17	12
Total assets	523	—(1)	462	408	367

(1) A balance sheet as at September 30, 2002 was not required for the purpose of the Prospectus.

### ***Operational Environment***

The operational environment in the B.C. Utility’s service territory is more challenging than that of the Alberta Utility and includes heavy snowfall, high wind conditions and rural mountain terrain. See “Risk Factors — Weather and Other Natural Disasters”.

### ***Safety and Reliability***

The B.C. Utility provides safe service throughout its service territory. While in recent years reliability has shown deterioration, the B.C. Utility has performed at or near the Canadian Electricity Association average for reliability.

### ***Employees***

The B.C. Utility has approximately 400 employees. The B.C. Utility has a collective agreement with the International Brotherhood of Electrical Workers, which expires on January 31, 2005, and a collective agreement with the Office and Professional Workers International Union in British Columbia, which expires on January 31, 2006.

### ***Unregulated Activities***

The B.C. Utility’s unregulated activities are not material relative to its regulated operations, but provide an opportunity to enhance utilization of the B.C. Utility’s utility operation and management resources under service contracts to third parties.

The B.C. Utility provides operations, maintenance and management services relating to (i) the 400 MW Waneta hydroelectric generation facility owned by Teck-Cominco, (ii) the 150 MW Brilliant Hydroelectric Plant owned by CPC/CBT, (iii) the 150 MW Arrow Lakes Hydroelectric Plant owned by CPC/CBT, and (iv) the distribution system owned by the City of Kelowna.

In addition, the B.C. Utility owns the Walden Power Partnership, an independent power producer, which owns and operates a 16 MW run of the river, hydroelectric power plant near Lillooet, British Columbia. The Walden plant commenced operating in 1992 and sells 100% of its output to B.C. Hydro under a long-term contract.

Certain revenues generated by the B.C. Utility’s unregulated activities are taken into account in establishing rates approved by the BCUC.

## **Environmental Matters**

Although primarily regulated at the provincial level, jurisdiction over the environment is shared by Canadian federal, provincial and local governments. As a result, the Alberta Utility and the B.C. Utility are subject to extensive federal, provincial and local regulation relating to the protection of the environment, including air emissions, water discharges and the generation, storage, transportation, disposal and release of various substances. In addition, both the provincial and federal governments have environmental assessment legislation, which is designed to foster better planning and the identification and mitigation of potential environmental impacts of projects or undertakings prior to their commencement.

The primary federal legislation is the *Canadian Environmental Protection Act, 1999* (Canada), which regulates the use, import, export and storage of toxic substances, including PCBs and ozone-depleting substances, specifically to enable pollution prevention and the protection of the environment and human health in order to contribute to sustainable development. Another important piece of federal legislation is the *Fisheries Act* (Canada), which prohibits the deposit of deleterious substances into water which may be inhabited by fish and the destruction of fish habitat.

In December 2002, the Government of Canada ratified the Kyoto Protocol. This protocol calls for Canada to reduce its greenhouse gas emissions to 6% below the 1990 level by 2012. The protocol will only become legally binding when it is ratified by at least 55 countries, covering at least 55% of the emissions addressed by the protocol. If the protocol becomes legally binding, it is expected to affect the operation of all industries in Canada. Although the impact of the Kyoto agreement on the Alberta Utility and the B.C. Utility cannot be fully determined at this point, as a wire service provider and a hydroelectric generator (in the case of the B.C. Utility), Fortis expects that the overall impact should be minimal.

In Alberta, the principal provincial environmental legislation includes the *Environmental Protection and Enhancement Act* (Alberta), which establishes a comprehensive regime regulating releases and spills of contaminants, including PCBs and ozone-depleting substances, waste management and release reporting and cleanup criteria. Additionally, the *Water Act* (Alberta) supports and promotes the conservation and management of water, including the wise allocation and use of water.

In British Columbia, the primary provincial legislation includes the *Waste Management Act* (British Columbia), the *Environmental Assessment Act* (British Columbia), the *Water Act* (British Columbia) and the *Forest Practices Code of British Columbia Act* (British Columbia). The *Waste Management Act* (British Columbia) is an omnibus piece of legislation that regulates most aspects of the environment, including substance releases, waste storage and remediation standards. The *Forest Practices Code of British Columbia Act* (British Columbia), the *Forest Act* (British Columbia) and the *Forest and Range Practices Act* (British Columbia) are intended to ensure sustainable use of the forests through planning, stewardship and protection initiatives. The *Water Act* (British Columbia) is intended to coordinate the overall management of water through coordination of licences and permits to divert, use and store water.

Municipal regulation is primarily relevant in the context of discharges of industrial sewage and storm water run off to the municipal sewer system.

As part of its purchase investigations, Fortis reviewed environmental records provided by the Vendors with respect to the policies, practices and assets of the Alberta Utility and the B.C. Utility. Fortis believes that the environmental compliance policies and practices of the Alberta Utility and the B.C. Utility are in accordance with industry standards.

## **ACQUISITION AGREEMENTS**

On September 15, 2003, Fortis entered into the Acquisition Agreements providing for the acquisition, directly or indirectly, by Fortis of all of the issued and outstanding shares of the Alberta Utility and the B.C. Utility for aggregate consideration of \$1,360 million.

### **Purchase Price**

The purchase price under the Alberta Purchase Agreement is \$686 million (the “Alberta Unadjusted Purchase Price”) and the purchase price under the B.C. Purchase Agreement is \$674 million (the “B.C. Unadjusted Purchase Price”). Under each Acquisition Agreement, the purchase price will be adjusted by (i) deducting indebtedness of the company being purchased to related companies and to certain third parties, (ii) adding (or deducting in the case of a deficit) the working capital of the applicable company as at the date of the closing of the Acquisition (which in the case



of the Alberta Purchase Agreement will be reduced by an agreed amount of \$19.2 million), (iii) adding or deducting, as applicable, an amount equal to the change in property, plant and equipment amounts reflected on balance sheets of the applicable company between December 31, 2003 and the date of the closing of the Acquisition, and (iv) in the case of the Alberta Purchase Agreement, adding the balance of a \$21.7 million “defect allowance” to the extent it is not applied in respect of claims for breaches of representations and warranties. In certain circumstances where the value of the shares sold under an Acquisition Agreement is reduced as a result of an uncured or unwaived breach of a representation or warranty in such agreement by an amount that exceeds \$6.74 million in the case of the B.C. Purchase Agreement, and \$6.86 million, plus a “defect allowance” in an amount of \$21.7 million, in the case of the Alberta Purchase Agreement, the purchase price will be adjusted downward by the amount the diminution in value exceeds the appropriate threshold. In the case where the diminution in value exceeds \$68.6 million in respect of the Alberta Purchase Agreement or \$67.4 million in respect of the B.C. Purchase Agreement, Fortis may terminate the applicable Acquisition Agreement.

### **Representations and Warranties**

Under the Acquisition Agreements, the parties have made various representations and warranties that are customary for this type of transaction. The Vendors’ representations and warranties relate to, among other things, absence of undisclosed litigation, absence of unpaid taxes, certain financial matters, compliance with laws and licences, title to the shares being purchased and the assets of the Alberta Utility and the B.C. Utility, as the case may be, the lack of sales or offices in the United States, the completeness of information disclosed to Fortis, the solvency of the Vendors and Aquila and certain environmental matters. The Vendors have also represented and warranted to Fortis that (generally, in the case of the B.C. Utility, and since the acquisition of the Alberta Utility by Aquila, in the case of the Alberta Utility) the business of such companies has been conducted in the ordinary course and in compliance with good industry practice, applicable law and all necessary authorizations. The Vendors have certain rights to cure breaches of representations and warranties prior to the closing of the Acquisition. The representations and warranties generally survive for 12 months following the closing of the Acquisition, except for (i) claims in respect of certain corporate organization and authorization matters (in respect of the Vendors, the Alberta Utility or the B.C. Utility, as applicable) and share capital and share title matters which survive indefinitely, and (ii) claims in respect of taxes which survive for six months following the date on which notice of reassessment may be issued in respect of the year in which the closing of the Acquisition takes place. After the closing of the Acquisition, no action or proceeding may be brought or enforced by Fortis relating to the representation and warranty concerning completeness of information disclosed to Fortis in connection with the Acquisition.

### **Covenants**

The parties to each of the Acquisition Agreements have made customary covenants relating to the closing of the Acquisition and related matters. In particular, each Vendor has agreed to conduct the business of the Alberta Utility and the B.C. Utility, as the case may be, in the ordinary course in accordance with good industry practice. The B.C. Utility has also agreed to enter into agreements, undertake projects and implement plans approved by the BCUC. In addition, the Acquisition Agreements impose limitations on the scope of business that may be conducted prior to closing of the Acquisition, including, among other things: (i) the length or value of contractual commitments and capital expenditures that the Alberta Utility and the B.C. Utility may undertake without the consent of Fortis (which may not be unreasonably withheld); (ii) the obligation of the Vendors to notify Fortis of the occurrence of certain events; and (iii) the right of Fortis to reasonable access to the Alberta Utility and the B.C. Utility and their management, employees and consultants. Each Vendor has further agreed that, prior to the termination of the Acquisition Agreements, neither it nor any person on its behalf will discuss or negotiate any alternative transactions with third parties. Immediately following the closing of the Acquisition, Fortis has agreed to cause each of the Alberta Utility and the B.C. Utility to repay certain of their respective outstanding indebtedness.

### **Indemnities**

Pursuant to the Acquisition Agreements, the Vendors, subject to certain limits, have agreed to indemnify and save harmless Fortis and its affiliates, and Fortis, subject to certain limits, has agreed to indemnify and save harmless the Vendors and their affiliates in respect of all claims sustained or incurred by the other resulting from (i) any misrepresentation or breach of warranty (other than the representation of the Vendors concerning completeness of information disclosed to Fortis), or (ii) failure to comply with, or the breach of, any covenants or agreements contained in the Acquisition Agreements. The indemnities provided by the Vendors or Fortis, as the case may be, are limited in

certain respects in that claims may only be made under the indemnities in respect of a breach of a representation or warranty when the amount attributable thereto exceeds \$100,000. The Vendors or Fortis, as the case may be, will only be obligated to indemnify the other party when the aggregate of all such losses exceeds \$17.15 million in the case of the Alberta Purchase Agreement and \$16.85 million in the case of the B.C. Purchase Agreement; however when such limitations are exceeded, the indemnity will apply in respect of all such claimed amounts. Under each Acquisition Agreement the maximum claim under the indemnity provisions by a party is \$100 million. The above limitations do not apply to (i) any misrepresentation by a Vendor concerning certain corporate organization and authorization matters (in respect of both the Vendors and the Alberta Utility or the B.C. Utility, as applicable), share capital or share title matters or enforceability of the Acquisition Agreement, (ii) the obligation of Fortis to ensure the Alberta Utility or the B.C. Utility, as the case may be, repays certain outstanding indebtedness, or (iii) any misrepresentation by Fortis concerning certain corporate organization and authorization matters or enforceability of the Acquisition Agreement. The Vendors will also indemnify Fortis in respect of liabilities of the Alberta Utility and the B.C. Utility for taxes beyond amounts set out in tax filings or accounted for in closing adjustments. Acquisition Holdco (as defined below) will indemnify the Vendors and their affiliates in respect of certain claims made by EPCOR against the Alberta Utility, ANCL and Aquila. See “The Acquired Businesses — Aquila Networks Canada (Alberta) Ltd. — EPCOR Litigation”.

### **Closing Conditions**

Under each Acquisition Agreement, the obligations of a party to close are subject to certain conditions. These include: (i) the truth of the other party’s representations and warranties, except where inaccuracies would not have a material adverse effect or as are permitted, subject to reduction of the purchase price; (ii) compliance by the other party with, and performance by the other party of, its agreements and covenants under the Acquisition Agreements, except where such failure would not have a material adverse effect; (iii) satisfaction by each party that all regulatory approvals have been obtained on terms that would not reasonably be expected to have a material adverse effect; (iv) satisfaction by each party that the terms and conditions of certain third party consents, releases and approvals that have been obtained or that the failure to obtain any of the said consents, releases and approvals would not reasonably be expected to have a material adverse effect; (v) no material adverse change in the business, results of operations, regulatory environment, assets and financial condition of the Alberta Utility or the B.C. Utility having occurred; (vi) Aquila shall have provided the Alberta Utility and the B.C. Utility with releases of any claims it has or may have against them; (vii) Aquila shall have delivered a guarantee to Fortis in respect of the performance of the Vendors under the Acquisition Agreements; (viii) the acquisition by Fortis, or by subsidiaries of Fortis, of a reviewable interest pursuant to section 54 of the *Utilities Commission Act* (British Columbia) shall have been approved by the BCUC; (ix) there must not be any judgment, decree, injunction, writ or order in effect that has had or would reasonably be expected to have a material adverse effect; and (x) the receipt of customary legal opinions.

The regulatory approvals that must be obtained prior to closing include:

- (a) AEUB approval under section 102 and, if applicable, sections 101 and 109 of the *Public Utilities Board Act* (Alberta) of the transfer of the shares of the Alberta Utility to Fortis or a subsidiary of Fortis;
- (b) approval by the BCUC of the transfer of the shares of the B.C. Utility to Fortis or a subsidiary of Fortis; and
- (c) if the parties have jointly determined that a filing or notification is required under the *Competition Act* (Canada) (the “Competition Act”), one of the following has occurred: (i) an advance ruling certificate has been issued in respect of the Acquisition pursuant to section 102 of the Competition Act; (ii) the applicable waiting period under section 123 of the Competition Act has expired without the parties being advised that the Commissioner of Competition under the Competition Act (the “Commissioner”) intends to issue an order under section 92 or 100 of the Competition Act in respect of the Acquisition; or (iii) the Commissioner has advised Fortis that he does not intend at the current time to apply for an order under section 92 of the Competition Act in respect of the Acquisition.

On January 5, 2004, the Commissioner issued an advance ruling certificate in respect of the Acquisition pursuant to section 102 of the Competition Act.

In addition, the Vendors’ obligation to close the Acquisition is conditional on the Vendors obtaining (i) approval of the Kansas Corporation Commission of the transfer of the shares of the Alberta Utility and the B.C. Utility, and (ii) inclusion in the approvals listed above of AEUB and BCUC of a direction, order or decision that the proceeds of the transactions contemplated by the Acquisition Agreements are to be allocated to or otherwise accrue to the benefit of the shareholders of the Alberta Utility and the B.C. Utility.

Applications for approval to the AEUB and the BCUC were filed on October 17, 2003 and December 1, 2003, respectively. The application to the AEUB with respect to the Alberta Utility's sale will be heard in February 2004. The BCUC has not yet made a decision as to whether it will proceed without a hearing with respect to the application for the B.C. Utility's sale.

Aquila filed for Kansas Corporation Commission approval in June 2003. This approval has not been received as of yet.

Under the Acquisition Agreements, a Vendor is not required to close unless it is released from its obligations under certain collective agreements. Under the Acquisition Agreements, Fortis will not be required to close unless consents have been obtained with respect to the assignment of numerous service, software, support and maintenance agreements and interconnection agreements from Aquila or its affiliates to the Alberta Utility or the B.C. Utility, as the case may be, and such assignment to Fortis or an affiliate of Fortis has occurred, except where the failure to obtain such consents or make such assignment would not have a material adverse effect on the Alberta Utility or the B.C. Utility, as applicable, or where the Vendor has made other arrangements satisfactory to Fortis for the supply of the service or software following closing.

The closing of the Acquisition must occur prior to 12:00 (noon) (Toronto time) on June 30, 2004 (subject to extension, if any, for completion of dispute resolution relating to defect payments, which may be payable to Fortis). The closing must not violate any applicable order, decree or judgment of any government authority, and the closings of both the purchase of the Alberta Utility and the B.C. Utility must occur concurrently. The parties expect the closing to occur in the first half of 2004.

On October 17, 2003, Fortis assigned the Alberta Purchase Agreement to Fortis Alberta Holdings Inc. ("Fortis Alberta") and the B.C. Purchase Agreement to Fortis Pacific Holdings Inc. ("Fortis Pacific"), each of which is owned directly by FortisWest Inc., a direct wholly owned subsidiary of Fortis ("Acquisition Holdco").

Effective December 31, 2003, the Vendors were amalgamated and continued under the name "Aquila Networks Canada Ltd."

### **Termination**

An Acquisition Agreement may be terminated by a party thereto at any time prior to closing in certain circumstances including: (i) the mutual agreement of all of the parties to the agreement; (ii) if a government authority advises in writing that it will not be providing a necessary authorization; (iii) if an insolvency event occurs in respect of the other party; and (iv) if the closing of the transaction would violate an order, decree or judgment of a government authority that has not been stayed and the appeal periods in respect thereof have expired. An Acquisition Agreement may also be terminated by either party if the total of all defect amounts relating to breaches of representations and warranties exceeds \$68.6 million under the Alberta Purchase Agreement and \$67.4 million under the B.C. Purchase Agreement.

### **Related Agreements**

Pursuant to a letter agreement dated September 15, 2003, between Fortis and Aquila, Fortis has agreed that Acquisition Holdco will offer replacement guarantees to the beneficiaries of certain existing guarantees (the "Existing Guarantees") that Aquila has provided in respect of obligations of the B.C. Utility under approximately \$150 million of secured debentures and in respect of certain other obligations of the B.C. Utility. Fortis has also agreed to cause, among other things: (i) each of the Alberta Utility and the B.C. Utility to have certain minimum capitalization ratios at closing of the Acquisition; and (ii) Acquisition Holdco and the holders of the shares of the Alberta Utility and the B.C. Utility to agree to certain other financial obligations and restrictions, including in respect of the Alberta Utility, the B.C. Utility and the companies that hold their shares directly. In the event the beneficiaries of any Existing Guarantee do not release Aquila from its obligations thereunder prior to the closing of the Acquisition, Fortis will cause Acquisition Holdco to indemnify Aquila for any and all amounts paid by Aquila in accordance with the terms of Existing Guarantees.

## FINANCING OF THE ACQUISITION

### Subscription Receipts

On October 8, 2003, Fortis closed a public offering of 6,310,000 subscription receipts (the “Subscription Receipts”) each representing the right to receive one Common Share. The gross proceeds of \$350,205,000 are being held in escrow by Computershare Trust Company of Canada (“Computershare”), as escrow agent, and are invested in short-term interest bearing or discount debt obligations pending receipt by Fortis of all regulatory and government approvals required to finalize the Acquisition and fulfillment or waiver of all the other outstanding conditions precedent to closing the Acquisition as itemized in the Acquisition Agreements (collectively, the “Release Conditions”).

If the Release Conditions are satisfied prior to 5:00 p.m. (Toronto time) on June 30, 2004, the escrowed funds will be released by Computershare to Fortis and the holders of Subscription Receipts will receive, without payment of any additional consideration, one Common Share for each Subscription Receipt held plus an amount equal to the dividends declared on the Common Shares by Fortis to holders of record on a date during the period from the closing date of the Subscription Receipt offering to the date of issue of the Common Shares in respect of the Subscription Receipts. In the event that the Release Conditions are not satisfied prior to 5:00 p.m. (Toronto time) on June 30, 2004 or, if either of the Acquisition Agreements is terminated prior to such time, holders of Subscription Receipts will receive from Computershare an amount equal to the full subscription price thereof, plus their *pro rata* entitlement to interest earned or income generated on such amount.

### Credit Agreements

For purposes of financing the Acquisition, Fortis has entered into a credit agreement dated October 28, 2003 with a syndicate of Canadian chartered banks pursuant to which the lenders have agreed to make available non-revolving credit facilities in the aggregate principal amount of \$860 million in favour of Fortis (the “Fortis Credit Facility”). Fortis Alberta Holdings Inc. has entered into a credit agreement dated October 28, 2003 with the same syndicate of Canadian chartered banks pursuant to which the lenders have agreed to make available a \$393 million, non-revolving credit facility in favour of the Alberta Utility (the “Alberta Utility Credit Facility”). The funding of each of the Fortis Credit Facility and the Alberta Utility Credit Facility (collectively, the “Credit Facilities”) is subject to the fulfilment of customary conditions. The amount available under the Credit Facilities would be sufficient, if necessary, to fund the aggregate \$1,360 million consideration payable to the Vendors for the Acquisition and to repay certain indebtedness of the Alberta Utility and the B.C. Utility, other than \$148.3 million principal amount of secured debentures of various series of the B.C. Utility which will remain outstanding.

The Fortis Credit Facility is an unsecured single borrowing credit facility to be used by Fortis, to the extent required, to finance the payment of the cash portion of the purchase price for the Acquisition and to refinance certain of the existing indebtedness of the B.C. Utility. The obligations of Fortis under the Fortis Credit Facility will be guaranteed by Fortis Pacific and, provided that necessary regulatory approvals are obtained, by Fortis Alberta. The Alberta Utility Credit Facility is an unsecured single borrowing credit facility to be made available to Fortis Alberta to use to refinance certain existing indebtedness of the Alberta Utility. Any amount not drawn down under the Credit Facilities will be cancelled after the initial borrowing. The Credit Facilities will mature, in the case of the Fortis Credit Facility, on the second anniversary and, in the case of the Alberta Utility Credit Facility, 364 days following the earlier of: (i) the drawdown under the relevant facility; and (ii) the date that is six months after the credit agreement giving effect to the relevant credit facility is entered into, subject to the option of the Alberta Utility to extend the term for two additional terms of 364 days.

The Credit Facilities contain certain prepayment options in favour of the borrowers and certain prepayment obligations upon the occurrence of certain events. In particular, the net proceeds of any equity or debt offering by Fortis or the B.C. Utility and of any debt offering by the Alberta Utility or the B.C. Utility, and any post-closing purchase price adjustments paid to Fortis or its subsidiary purchasers in connection with the Acquisition, will be required to be used to prepay the relevant Credit Facilities. Any prepayment under the Credit Facilities may not be re-borrowed.

The Credit Facilities contain customary representations and warranties and affirmative and negative covenants of the borrowers, including, in the case of Fortis, a consolidated debt to consolidated capitalization ratio which may not exceed 0.75:1 at any time during the first year of the Fortis Credit Facility and 0.70:1 at any time thereafter and, in the case of the Alberta Utility and the B.C. Utility, a consolidated debt to consolidated capitalization ratio which may not exceed 0.70:1. The Credit Facilities contain customary events of default. In addition, any failure by Fortis, the Alberta

Utility or the B.C. Utility to maintain an investment grade credit rating (being a rating of at least BBB- or its equivalent) will constitute an event of default under the relevant Credit Facility.

Customary fees are payable by the borrowers in respect of the Credit Facilities and amounts outstanding under the Credit Facilities will bear interest at market rates.

Fortis expects that the amount borrowed under the Alberta Utility Credit Facility will be repaid from the proceeds of long-term debt to be borrowed by the Alberta Utility following the closing of the Acquisition. The cost of this debt, subject to regulatory approval, will form part of the cost of service of the Alberta Utility and will be recovered in rates.

A portion of the net proceeds from the Offering and the net proceeds from the exercise of the Warrants and from the offering of Subscription Receipts, will reduce the amount outstanding under the Fortis Credit Facility. Fortis expects that the balance of the amount outstanding under the Fortis Credit Facility will be repaid from the proceeds of one or more offerings of long-term debt. Fortis does not anticipate that it will issue additional Common Shares or preference shares to repay the Fortis Credit Facility.

### CAPITALIZATION

The following table sets out the consolidated capitalization of the Corporation (i) as at September 30, 2003, (ii) after giving effect to the Offering and prior to the closing of the Acquisition, and (iii) after giving effect to the Offering and completion of the Acquisition. The financial information set out below should be read in conjunction with the unaudited consolidated financial statements incorporated by reference into the Prospectus and the unaudited *pro forma* consolidated financial statements included in the Prospectus and, in each case, the notes thereto.

	<u>Outstanding at September 30, 2003</u>	<u>Pro forma outstanding at September 30, 2003<sup>(1)</sup></u> (in millions of dollars)	<u>Pro forma outstanding at September 30, 2003<sup>(2)</sup></u>
Total debt .....	\$1,141	\$1,141	\$2,082
Shareholders' equity			
Preference shares .....	123	123	123
Preference shares offered hereby .....	—	46	196
Common Shares .....	328	328	328
Common Shares represented by Subscription Receipts .....	—	—	341
Equity portion of convertible debentures .....	2	2	2
Retained earnings and contributed surplus .....	<u>281</u>	<u>281</u>	<u>281</u>
Total capitalization .....	<u>\$1,875</u>	<u>\$1,921</u>	<u>\$3,353</u>

(1) Prior to the closing of the Acquisition.

(2) Following conversion of all Series D First Preference Shares and exercise of all Warrants.

### SHARE CAPITAL OF FORTIS

The authorized share capital of the Corporation consists of an unlimited number of Common Shares, an unlimited number of First Preference Shares, issuable in series and an unlimited number of second preference shares (the "Second Preference Shares"), issuable in series, in each case without nominal or par value. As at January 20, 2004, 17,420,072 Common Shares and 5,000,000 Series C First Preference Shares were issued and outstanding.

Holders of Common Shares are entitled to dividends on a *pro rata* basis if, as and when declared by the Board of Directors. Subject to the rights of the holders of the First Preference Shares and Second Preference Shares and any other class of shares of the Corporation entitled to receive dividends in priority to or rateably with the holders of the Common Shares, the Board of Directors may declare dividends on the Common Shares to the exclusion of any other class of shares of the Corporation. On the liquidation, dissolution or winding up of Fortis, holders of Common Shares are entitled to participate rateably in any distribution of assets of Fortis, subject to the rights of holders of First Preference Shares and Second Preference Shares and any other class of shares of the Corporation entitled to receive the assets of the Corporation on such a distribution in priority to or rateably with the holders of the Common Shares. Holders of the Common Shares are entitled to receive notice of and to attend all annual and special meetings of the

shareholders of Fortis, other than separate meetings of holders of any other class or series of shares, and to one vote in respect of each Common Share held at such meetings.

## DETAILS OF THE OFFERING

The following is a summary of the material rights, privileges, conditions and restrictions attached to the Units, the First Preference Shares as a class, the Series D First Preference Shares, the Series E First Preference Shares and the Warrants.

### Description of the Units

Each Unit consists of one Series D First Preference Share and one Warrant. **The Series D First Preference Share and the Warrant are not separable. A Series D First Preference Share cannot be converted into 0.25 of a fully-paid and freely-tradeable Series E First Preference Share without the concurrent exercise of a Warrant and a Warrant cannot be exercised without the concurrent conversion of a Series D First Preference Share into 0.25 of a fully-paid and freely-tradeable Series E First Preference Share.** See “Description of the Series D First Preference Shares” and “Description of the Warrants”.

### *Book-Entry Only*

The Units will be issued in book-entry only form. The Corporation will cause a global certificate or certificates representing newly issued Units to be delivered to and registered in the name of CDS or its nominee. Each holder of Units will receive only a customer confirmation of purchase from the registered dealer from or through which the Units are acquired in accordance with the practices and procedures of that registered dealer. The practices of registered dealers may vary, but generally customer confirmations are issued promptly after execution of a customer order. CDS is responsible for establishing and maintaining book-entry accounts for the CDS Participants having interests in the Units.

**Any holder of Units who desires to convert the Series D First Preference Shares and exercise the Warrants comprised therein, must do so by causing a CDS Participant to deliver to CDS (at its office in the City of Toronto), on behalf of the holder, a written notice (the “Conversion and Exercise Notice and Declaration”) of the holder’s intention to convert such Series D First Preference Shares and exercise such Warrants, together with the payment required in relation to the exercise of such Warrants, sufficiently in advance of the relevant notice date so as to permit the CDS Participant to deliver notice to CDS by the required time.** The Conversion and Exercise Notice and Declaration may take the form of the notice and declaration attached as Exhibit A hereto or such other form as each CDS Participant may prescribe. Any expenses associated with the preparation and delivery of the Conversion and Exercise Notice and Declaration shall be for the account of the holder exercising the conversion and exercise rights.

By causing a CDS Participant to deliver the Conversion and Exercise Notice and Declaration, together with the payment required in relation to the exercise of the Warrants, to CDS, a holder shall be deemed to have irrevocably surrendered his or her Series D First Preference Shares for conversion and Warrants for exercise and appointed such CDS Participant to act as his or her exclusive settlement agent with respect to the conversion and exercise rights and the receipt of payment in connection with the settlement of obligations arising from such conversion and exercise.

Any Conversion and Exercise Notice and Declaration that CDS determines to be incomplete, not in proper form, lacking sufficient payment in connection with the exercise of the Warrants or not duly executed shall for all purposes be void and of no effect and the conversion and exercise rights to which it relates shall be considered for all purposes not to have been exercised thereby. In the event of a determination that the Conversion and Exercise Notice and Declaration is incomplete, not in proper form, lacking sufficient payment in connection with the exercise of the Warrants or not duly executed, CDS shall promptly notify the CDS Participant that delivered the notice. A failure by a CDS Participant to execute the conversion and exercise rights or to give effect to the settlement thereof in accordance with the holder’s instructions will not give rise to any obligations or liability on the part of the Corporation to the CDS Participant or the holder.

**The Corporation has the option to terminate registration of the Units through the book-entry only system, in which case certificates for the Units will be issued in fully registered form to beneficial owners of the Units or their nominees.**

### ***Transfers***

Transfers of ownership in the Units will be effected only through records maintained by CDS for such Units with respect to interests of CDS Participants and on the records of CDS Participants with respect to interests of holders other than CDS Participants. Holders of Units, other than CDS Participants, wishing to purchase, sell or otherwise transfer ownership of or other interests in the Units may do so only through CDS Participants. The ability of a holder to pledge Units or otherwise take action with respect to such holder's interest in Units (other than through a CDS Participant) may be limited due to the lack of a physical certificate.

### ***Payments and Deliveries***

Payments of dividends, if any, or other amounts in respect of Series D First Preference Shares forming part of the Units will be made by or on behalf of the Corporation to CDS or its nominee as the registered holder of the Units and the Corporation understands that such payments or deliveries will be forwarded by CDS or its nominee, net of any applicable withholding taxes, to CDS Participants in accordance with the customary practices and procedures of CDS ("CDS Procedures"). As long as CDS or its nominee is the registered holder of the Units, CDS or its nominee will be considered the sole owner of the Units for purposes of receiving any payments thereon and for all other purposes.

### ***Purchase for Cancellation***

Subject to applicable law and any necessary regulatory approvals, the Corporation may, at any time, purchase for cancellation, all or any of the Units in the open market or by private agreement or otherwise at the lowest price or prices at which, in the opinion of the Board of Directors, such Units are obtainable.

### ***Listing***

The TSX has conditionally approved the listing of the Units, including the Series D First Preference Shares and the Warrants comprised therein. Listing will be subject to the Corporation fulfilling all of the listing requirements of the TSX on or before April 12, 2004. As the Units will be listed upon the fulfillment of these listing requirements, the Series D First Preference Shares and the Warrants will not trade separately while the Units exist.

## **Description of the First Preference Shares**

### ***Issuance in Series***

The Board of Directors may from time to time issue First Preference Shares in one or more series. Prior to issuing shares in a series, the Board of Directors is required to fix the number of shares in the series and determine the designation, rights, privileges, conditions and restrictions attaching to that series of First Preference Shares.

### ***Priority***

The First Preference Shares rank as a class in priority to all other shares of the Corporation. Each series of First Preference Shares ranks on a parity with the First Preference Shares of every other series as to the payment of dividends, return of capital and the distribution of assets in the event of the liquidation, dissolution or winding up of the Corporation, whether voluntary or involuntary, or any other distribution of the assets of the Corporation among its shareholders for the purpose of winding up its affairs. Each series of First Preference Shares participates rateably with every other series of First Preference Shares in respect of accumulated cumulative dividends and return of capital if any amount of cumulative dividends, whether or not declared, or amount payable on the return of capital in respect of a series of First Preference Shares, is not paid in full.

### ***Voting Rights***

The holders of the First Preference Shares are not entitled to any voting rights as a class, except to the extent that voting rights may from time to time be attached to any series of First Preference Shares, and except as provided by law or as described below under "Modification". At any meeting of the holders of the First Preference Shares, each holder shall have one vote in respect of each First Preference Share held.

### ***Modification***

The class provisions attached to the First Preference Shares may only be amended with the prior approval of the holders of the First Preference Shares in addition to any other approvals required by the *Corporations Act* (Newfoundland and Labrador) or any other statutory provisions of like or similar effect applicable from time to time.

The approval of the holders of the First Preference Shares with respect to any and all matters affecting the class may be given by at least two-thirds of the votes cast at a meeting of the holders of the First Preference Shares duly called for that purpose.

## **Description of the Series D First Preference Shares**

### ***Dividends***

The holders of Series D First Preference Shares will be entitled to receive fixed cumulative preferential cash dividends, if, as and when declared by the Board of Directors in the amount of \$0.3063 per Series D First Preference Share per annum, to accrue from the original date of issue, payable on March 31, 2004, July 15, 2004 and thereafter on the first business day of September, December, March and June of each year. Assuming an issue date of January 29, 2004, the first dividend, if declared, will be payable on March 31, 2004 in the amount of \$0.0519 per Series D First Preference Share, the second dividend, if declared, will be payable on July 15, 2004 in the amount of \$0.0887 per Series D First Preference Share, the third dividend, if declared, will be payable on September 1, 2004 in the amount of \$0.0402 per Series D First Preference Share and each dividend thereafter will be payable in equal quarterly instalments in the amount of \$0.0766 per Series D First Preference Shares, except as described herein. **If the Acquisition has closed on or prior to June 30, 2004, quarterly cash dividends payable in respect of the Series D First Preference Shares after July 15, 2004, if declared, will be reduced to \$0.01 per Series D First Preference Share, being equivalent to 0.64% per annum per Series D First Preference Share.**

### ***Conversion by the Holder into Series E First Preference Shares***

If the Acquisition closes on or prior to June 30, 2004, the holder of a Series D First Preference Share will have the right, subject to applicable law and any necessary regulatory approvals, to convert on July 15, 2004, September 1, 2004 or December 1, 2004 such Series D First Preference Share into 0.25 of a fully-paid and freely-tradeable Series E First Preference Share, provided such holder concurrently exercises one Warrant. The concurrent exercise of a Warrant together with a cash payment of \$18.75 per Warrant will entitle the holder to acquire 0.75 of a fully-paid and freely-tradeable Series E First Preference Share. **A Series D First Preference Share cannot be converted into 0.25 of a fully-paid and freely-tradeable Series E First Preference Share without the concurrent exercise of a Warrant and a Warrant cannot be exercised without the concurrent conversion of a Series D First Preference Share into 0.25 of a fully-paid and freely-tradeable Series E First Preference Share. A Warrant may not be separated from the related Series D First Preference Share forming a Unit.** Consequently, the conversion of one Series D First Preference Share, the concurrent exercise of one Warrant and the additional cash payment of \$18.75 will entitle the holder of a Unit to receive one fully-paid and freely-tradeable Series E First Preference Share. If the Acquisition has closed on or prior to June 30, 2004, all conversion rights of the holder of a Series D First Preference Share that have not been exercised for any reason by the Expiry Time will terminate.

The conversion of a Series D First Preference Share will be effected by the registered holder thereof depositing with Computershare no later than 5:00 p.m. (Toronto time) on the date set for conversion, being July 15, 2004, September 1, 2004 or December 1, 2004 at one of its offices in Toronto or Montréal, a Unit certificate with a duly completed exercise and conversion panel and a cash payment in the amount of \$18.75 per Warrant to be exercised. As long as the Units are held in the CDS book-entry only system, beneficial owners of Units may convert Series D First Preference Shares and exercise Warrants by providing instructions to the CDS Participants through which they hold Units, and such CDS Participants will communicate such exercise instructions to CDS in accordance with CDS Procedures.

Upon exercise of this conversion right by the holder of Series D First Preference Shares, the Corporation is not required to issue Series E First Preference Shares to a purchaser having an address in, or in such circumstances where the Corporation or its transfer agent has reason to believe such purchaser is a resident of, any jurisdiction outside Canada, to the extent that such issue would require compliance by the Corporation with the securities or other laws of such jurisdiction. Subscriptions for Series E First Preference Shares pursuant to the exercise of the Warrants and conversion of Series D First Preference Shares by any person who is not a U.S. Person (as defined in Regulation S under the United States *Securities Act of 1933*, as amended (the "1933 Act")) or a person in the United States (as defined in Regulation S under the 1933 Act) or by any person on behalf of or for the account of a U.S. Person or a person in the United States will be conditioned upon delivery to the Corporation of a certification to that effect in order to establish the availability of an exemption from registration under the 1933 Act.



### ***Conversion by the Holder into Common Shares***

If the Acquisition does not close on or prior to June 30, 2004, subject to applicable law and any necessary regulatory approvals, on and after September 1, 2016, each Series D First Preference Share will be convertible at the option of the holder, upon not less than 30 days and not more than 60 days prior written notice (which notice shall be irrevocable), on the first business day of September, December, March and June of each year, into that number of fully-paid and freely-tradeable Common Shares determined by dividing \$6.25 plus all accrued and unpaid dividends up to but excluding the date fixed for conversion, by the greater of \$1.00 and 95% of the Current Market Price. Fractional Common Shares will not be issued on any conversion of Series D First Preference Shares, but in lieu thereof, the Corporation will make cash payments.

Upon exercise of this conversion right by the holder of Series D First Preference Shares, the Corporation is not required to issue Common Shares to a purchaser having an address in, or in such circumstances where the Corporation or its transfer agent has reason to believe such purchaser is a resident of, any jurisdiction outside Canada, to the extent that such issue would require compliance by the Corporation with the securities or other laws of such jurisdiction.

Subject to the provisions described below under “Restrictions on Dividends and Retirement and Issue of Shares”, as applicable, the Corporation may, by notice given not later than 20 days before the date fixed for conversion to all holders who have given a conversion notice, (i) redeem on the date fixed for conversion all or any part of the Series D First Preference Shares forming the subject matter of the applicable conversion notice, and/or (ii) cause the holder of such Series D First Preference Shares to sell on the date fixed for conversion all or any part of such Series D First Preference Shares to another purchaser or purchasers in the event that a purchaser or purchasers willing to purchase all or any part of such Series D First Preference Shares is or are found. Any such redemption or purchase shall be made by the payment to the holder of the Series D First Preference Shares in cash of a sum per redeemed or purchased share equal to \$6.25 plus, in each case, all accrued and unpaid dividends up to but excluding the date fixed for conversion (less any tax required to be deducted and withheld by the Corporation under applicable law). The Series D First Preference Shares to be so redeemed or purchased shall not be converted on the date set forth in the conversion notice.

If the Corporation elects to redeem or arrange for the purchase of any Series D First Preference Shares that are the subject of a conversion notice (the “Series D Subject Shares”), the Corporation shall, at least 20 days prior to the conversion date, give notice to all holders who have given a conversion notice to the Corporation, stating:

- (a) the number of Series D Subject Shares to be redeemed by the Corporation;
- (b) the number of Series D Subject Shares to be sold to another purchaser; and/or
- (c) the number of Series D Subject Shares to be converted into Common Shares,

such that all of the Series D Subject Shares will be redeemed, purchased or converted on that conversion date and that the proportion of the Series D Subject Shares which are either redeemed, purchased or converted on that conversion date shall, to the extent practicable, be the same for each holder delivering a conversion notice.

### ***Conversion by the Corporation into Common Shares***

The Series D First Preference Shares will not be convertible at the option of the Corporation prior to June 1, 2013. On and after this date, the Corporation may, at its option, upon not less than 30 days and not more than 60 days prior written notice, subject to applicable law and any necessary regulatory approvals, convert all, or from time to time any part of, the outstanding Series D First Preference Shares into that number of fully-paid and freely-tradeable Common Shares determined by dividing the then applicable redemption price per Series D First Preference Share (as set out below) plus all accrued and unpaid dividends up to but excluding the date fixed for conversion, by the greater of \$1.00 and 95% of the Current Market Price. Fractional Common Shares will not be issued on any conversion of Series D First Preference Shares, but in lieu thereof, the Corporation will make cash payments.

If less than all of the outstanding Series D First Preference Shares are at any time to be converted, such Series D First Preference Shares will be converted on a *pro rata* basis.

Upon exercise of this conversion right by the Corporation, the Corporation is not required to issue Series E First Preference Shares to a purchaser having an address in, or in such circumstances where the Corporation or its transfer agent has reason to believe such purchaser is a resident of, any jurisdiction outside Canada, to the extent that such issue would require compliance by the Corporation with the securities or other laws of such jurisdiction.

### ***Redemption***

The Series D First Preference Shares are not redeemable before June 1, 2013. On and after this date, subject to the terms of any shares of the Corporation ranking prior to the Series D First Preference Shares, to applicable laws, to any necessary regulatory approvals and to the provisions described below under “Restrictions on Dividends and Retirement and Issue of Shares”, the Corporation may, at its option, upon not less than 30 days and not more than 60 days prior written notice, redeem all, or from time to time any part of, the outstanding Series D First Preference Shares by the payment in cash of a sum per redeemed share equal to \$6.4375 if redeemed during the 12 months commencing June 1, 2013; \$6.375 if redeemed during the 12 months commencing June 1, 2014; \$6.3125 if redeemed during the 12 months commencing June 1, 2015; and \$6.25 if redeemed on or after June 1, 2016 plus, in each case, all accrued and unpaid dividends up to but excluding the date fixed for redemption (less any tax required to be deducted and withheld by the Corporation).

If less than all of the outstanding Series D First Preference Shares are at any time to be redeemed, such Series D First Preference Shares will be redeemed on a *pro rata* basis.

### ***Purchase for Cancellation***

Subject to applicable law and any necessary regulatory approvals, the Corporation may, at any time, purchase for cancellation, all or any of the Series D First Preference Shares in the open market or by private agreement or otherwise at the lowest price or prices at which, in the opinion of the Board of Directors, such Series D First Preference Shares are obtainable.

### ***Consolidation in Certain Circumstances***

In the event that the Acquisition does not close on or prior to June 30, 2004, on and after the Early Expiry Time, the Board of Directors shall be entitled to consolidate the Series D First Preference Shares on a four-for-one basis and in such circumstances the rights of a holder of Series D First Preference Shares will be adjusted accordingly. No action on the part of the holders of Series D First Preference Shares will be required to approve such consolidation.

### ***Listing***

The TSX has conditionally approved the listing of the Common Shares issuable upon the conversion of the Series D First Preference Shares, which Common Shares are also listed in connection with the listing of the Series E First Preference Shares. Listing will be subject to the Corporation fulfilling all of the listing requirements of the TSX on or before April 12, 2004. As the Units will be listed upon the fulfillment by the Corporation of the listing requirements of the TSX relating thereto, the Series D First Preference Shares and the Warrants will not trade separately while the Units exist. If the Acquisition does not close on or prior to June 30, 2004, the Corporation will apply to have the Series D First Preference Shares separately listed and posted for trading on the TSX on the trading day immediately following the Early Expiry Time. If the Acquisition closes on or prior to June 30, 2004, the Series D First Preference Shares are convertible into Series E First Preference Shares, which are, in turn, convertible into Common Shares. If, however, the Acquisition does not close on or prior to June 30, 2004, the Series D First Preference Shares will be directly convertible into Common Shares on and after September 1, 2016 at the option of the holder and on and after June 1, 2013 at the option of the Corporation. If the Acquisition closes on or prior to June 30, 2004, any Series D First Preference Shares not converted prior to the Expiry Time will not be listed on the TSX after the Expiry Time.

### ***Liquidation, Dissolution and Winding Up***

In the event of the liquidation, dissolution or winding up of the Corporation or any other distribution of assets of the Corporation among its shareholders for the purpose of winding up its affairs, the holders of the Series D First Preference Shares will be entitled to payment of an amount equal to \$6.25 per Series D First Preference Share plus all accrued and unpaid dividends up to but excluding the date fixed for payment or distribution (less any tax required to be deducted and withheld by the Corporation), before any amount is paid or any assets of the Corporation are distributed to the holders of the Common Shares or any other shares ranking junior as to return of capital to the Series D First Preference Shares. The holders of the Series D First Preference Shares will not be entitled to share in any further distribution of the assets of the Corporation.

### ***Restrictions on Dividends and Retirement and Issue of Shares***

So long as any of the Series D First Preference Shares are outstanding, the Corporation will not, without the approval of the holders of the Series D First Preference Shares:

- (a) declare, pay or set apart for payment any dividends (other than stock dividends payable in shares of the Corporation ranking as to return of capital and dividends junior to the Series D First Preference Shares) on any shares of the Corporation ranking as to dividends junior to the Series D First Preference Shares;
- (b) except out of the net cash proceeds of a substantially concurrent issue of shares of the Corporation ranking as to return of capital and dividends junior to the Series D First Preference Shares, redeem or call for redemption, purchase or otherwise pay off, retire or make any return of capital in respect of any shares of the Corporation ranking as to capital junior to the Series D First Preference Shares;
- (c) redeem or call for redemption, purchase or otherwise retire for value or make any return of capital in respect of less than all of the Series D First Preference Shares then outstanding;
- (d) except pursuant to any purchase obligation, sinking fund, retraction privilege or mandatory redemption provisions attaching thereto, redeem or call for redemption, purchase or otherwise pay off, retire or make any return of capital in respect of any First Preference Shares, ranking as to dividends or capital on a parity with the Series D First Preference Shares; or
- (e) issue any additional Series D First Preference Shares or any shares ranking as to dividends or capital prior to or on a parity with the Series D First Preference Shares (other than Series E First Preference Shares),

unless, in each such case, all accrued and unpaid dividends up to and including the dividend payable for the last completed period for which dividends were payable on the Series D First Preference Shares and on all other shares of the Corporation ranking as to dividends prior to or on a parity with the Series D First Preference Shares with respect to the payment of dividends have been declared and paid or set apart for payment.

### ***Voting Rights***

The holders of the Series D First Preference Shares will not be entitled (except as otherwise provided by law and except for meetings of the holders of First Preference Shares as a class and meetings of the holders of Series D First Preference Shares as a series) to receive notice of, attend or vote at, any meetings of shareholders of the Corporation except if the Corporation fails to pay eight quarterly dividends on the Series D First Preference Shares, whether or not consecutive and whether or not such dividends have been declared and whether or not there are any monies of the Corporation properly applicable to the payment of dividends. In that event and for only so long as any such dividends remain in arrears, the holders of the Series D First Preference Shares will be entitled to receive notice of and to attend all shareholders' meetings of the Corporation which take place more than 60 days after the date on which the failure first occurs (other than a separate meeting of the holders of another series or class of shares) and such holders shall have the right, at any such meeting, to one vote for each Series D First Preference Share held. No other voting rights shall attach to the Series D First Preference Shares in any circumstances. The voting rights of the holders of the Series D First Preference Shares shall forthwith cease upon payment by the Corporation of all such dividends in arrears on the Series D First Preference Shares to which the holders are entitled, until such time as the Corporation may again fail to pay eight quarterly dividends on the Series D First Preference Shares, whether or not consecutive and whether or not such dividends have been declared and whether or not there are any monies of the Corporation properly applicable to the payment of dividends, in which event such voting rights shall become effective again and so on from time to time.

### ***Shareholder Approvals***

The approval of all amendments to the rights, privileges, restrictions and conditions attaching to the Series D First Preference Shares as a series and any other approval to be given by the holders of the Series D First Preference Shares may be given by a resolution carried by an affirmative vote of at least  $66\frac{2}{3}\%$  of the votes cast at a meeting at which the holders of not less than a majority of the outstanding Series D First Preference Shares are present or represented by proxy or, if no quorum is present at such meeting, at an adjourned meeting at which the holders of Series D First Preference Shares then present would form the necessary quorum. At any meeting of holders of Series D First Preference Shares as a series, each such holder shall be entitled to one vote in respect of each Series D First Preference Share held.

### ***Priority***

The Series D First Preference Shares rank *pari passu* with all other series of First Preference Shares and senior to all other shares of the Corporation with respect to priority to the payment of dividends and the distribution of assets on the dissolution, liquidation or winding up of the Corporation.

### ***Tax on Preference Share Dividends***

The Corporation will elect, in the manner and within the time provided under subsection 191.2(1) of the Tax Act, to pay or cause payment of tax under Part VI.1 of the Tax Act at a rate such that the corporate holders of Series D First Preference Shares will not be required to pay tax under Part IV.1 of the Tax Act on dividends received on such shares.

### ***Book-Entry Only***

If the Acquisition closes on or prior to June 30, 2004, following the Expiry Time, certificates for the Series D First Preference Shares will be issued in fully registered form to beneficial owners of such shares or their nominees. If, however, the Acquisition does not close on or prior to June 30, 2004, following the Early Expiry Time, the Series D First Preference Shares will be issued in book-entry only form. At such time, the Corporation will cause a global certificate or certificates representing the Series D First Preference Shares to be delivered to and registered in the name of CDS or its nominee. Each holder of Series D First Preference Shares will receive only a customer confirmation of purchase from the registered dealer from or through which the Series D First Preference Shares are acquired in accordance with the practices and procedures of that registered dealer. The practices of registered dealers may vary, but generally customer confirmations are issued promptly after execution of a customer order. CDS is responsible for establishing and maintaining book-entry accounts for the CDS Participants having interests in the Series D First Preference Shares.

**If the Acquisition does not close on or prior to June 30, 2004, following the Early Expiry Time, any holder of Series D First Preference Shares who desires to exercise conversion rights thereunder must do so by causing a CDS Participant to deliver to CDS (at its office in the City of Toronto), on behalf of the holder, a written notice (the “Series D Conversion Notice”) of the holder’s intention to convert shares sufficiently in advance of the relevant notice date so as to permit the CDS Participant to deliver notice to CDS by the required time.** The Series D Conversion Notice may take the form of the notice attached as Exhibit B hereto or such other form as each CDS Participant may prescribe. Any expenses associated with the preparation and delivery of the Series D Conversion Notice shall be for the account of the holder exercising the conversion right.

By causing a CDS Participant to deliver the Series D Conversion Notice to CDS, a holder shall be deemed to have irrevocably surrendered his or her shares for conversion and appointed such CDS Participant to act as his or her exclusive settlement agent with respect to the exercise of the conversion right and the receipt of payment in connection with the settlement of obligations arising from such exercise.

Any Series D Conversion Notice that CDS determines to be incomplete, not in proper form or not duly executed shall for all purposes be void and of no effect and the conversion right to which it relates shall be considered for all purposes not to have been exercised thereby. In the event of a determination that the Series D Conversion Notice is incomplete, not in proper form or not duly executed, CDS shall promptly notify the CDS Participant that delivered the conversion notice. A failure by a CDS Participant to exercise conversion rights or to give effect to the settlement thereof in accordance with the holder’s instructions will not give rise to any obligations or liability on the part of the Corporation to the CDS Participant or the holder.

**The Corporation has the option to terminate registration of the Series D First Preference Shares through the book-entry only system, in which case certificates for the Series D First Preference Shares will be issued in fully registered form to beneficial owners of such shares or their nominees.**

### ***Transfers***

If the Acquisition does not close on or prior to June 30, 2004, following the Early Expiry Time, transfers of ownership in the Series D First Preference Shares will be effected only through records maintained by CDS for such Series D First Preference Shares with respect to interests of CDS Participants, and on the records of CDS Participants with respect to interests of holders other than CDS Participants. Holders of Series D First Preference Shares, other than CDS Participants, wishing to purchase, sell or otherwise transfer ownership of or other interests in the Series D First Preference Shares may do so only through CDS Participants. The ability of a holder to pledge Series D First Preference Shares or otherwise take action with respect to such holder’s interest in Series D First Preference Shares (other than through a CDS Participant) may be limited due to the lack of a physical certificate.

### ***Payments and Deliveries***

If the Acquisition does not close on or prior to June 30, 2004, following the Early Expiry Time, payments of dividends, if any, or other amounts in respect of Series D First Preference Shares will be made by or on behalf of the Corporation to CDS or its nominee as the registered holder of the Series D First Preference Shares and the Corporation understands that such payments or deliveries will be forwarded by CDS or its nominee, net of any applicable withholding taxes, to CDS Participants in accordance with CDS Procedures. As long as CDS or its nominee is the registered holder of the Series D First Preference Shares, CDS or its nominee will be considered the sole owner of the Series D First Preference Shares for purposes of receiving any payments thereon and for all other purposes.

### **Description of the Series E First Preference Shares**

#### ***Dividends***

The holders of Series E First Preference Shares will be entitled to receive fixed cumulative preferential cash dividends, if, as and when declared by the Board of Directors in the amount of \$1.2250 per Series E First Preference Share per annum, to accrue from the original date of issue, payable in equal quarterly instalments in the amount of \$0.3063 per Series E First Preference Share on the first business day of March, June, September and December of each year. Assuming an issue date of July 15, 2004, the first dividend, if declared, will be payable on September 1, 2004 in the amount of \$0.1607 per Series E First Preference Share to account for the initial partial period during which the Series E First Preference Shares will be outstanding. Assuming an issue date of September 1, 2004 or December 1, 2004, the first dividend, if declared, will be payable on December 1, 2004 or March 1, 2005, respectively, in the amount of \$0.3063 per Series E First Preference Share.

#### ***Conversion by the Holder into Common Shares***

On and after September 1, 2016, subject to applicable law and any necessary regulatory approvals, each Series E First Preference Share will be convertible at the option of the holder, upon not less than 30 days and not more than 60 days prior written notice (which notice shall be irrevocable), on the first business day of September, December, March and June of each year, into that number of fully-paid and freely-tradeable Common Shares determined by dividing \$25.00 plus all accrued and unpaid dividends up to but excluding the date fixed for conversion, by the greater of \$1.00 and 95% of the Current Market Price. Fractional Common Shares will not be issued on any conversion of Series E First Preference Shares, but in lieu thereof, the Corporation will make cash payments.

Upon exercise of this conversion right by the holder of Series E First Preference Shares, the Corporation is not required to issue Common Shares to a purchaser having an address in, or in such circumstances where the Corporation or its transfer agent has reason to believe such purchaser is a resident of, any jurisdiction outside Canada, to the extent that such issue would require compliance by the Corporation with the securities or other laws of such jurisdiction.

Subject to the provisions described below under “Restrictions on Dividends and Retirement and Issue of Shares” as applicable, the Corporation may, by notice given not later than 20 days before the date fixed for conversion to all holders who have given a conversion notice, (i) redeem on the date fixed for conversion all or any part of the Series E First Preference Shares forming the subject matter of the applicable conversion notice, and/or (ii) cause the holder of such Series E First Preference Shares to sell on the date fixed for conversion all or any part of such Series E First Preference Shares to another purchaser or purchasers in the event that a purchaser or purchasers willing to purchase all or any part of such Series E First Preference Shares is or are found. Any such redemption or purchase shall be made by the payment to the holder of the Series E First Preference Shares in cash of a sum per redeemed or purchased share equal to \$25.00 plus, in each case, all accrued and unpaid dividends up to but excluding the date fixed for conversion (less any tax required to be deducted and withheld by the Corporation under applicable law). The Series E First Preference Shares to be so redeemed or purchased shall not be converted on the date set forth in the conversion notice.

If the Corporation elects to redeem or arrange for the purchase of any Series E First Preference Shares that are the subject of a conversion notice (the “Series E Subject Shares”), the Corporation shall, at least 20 days prior to the conversion date, give notice to all holders who have given a conversion notice to the Corporation, stating:

- (a) the number of Series E Subject Shares to be redeemed by the Corporation;
- (b) the number of Series E Subject Shares to be sold to another purchaser; and/or
- (c) the number of Series E Subject Shares to be converted into Common Shares,

such that all of the Series E Subject Shares will be redeemed, purchased or converted on that conversion date and that the proportion of the Series E Subject Shares which are either redeemed, purchased or converted on that conversion date shall, to the extent practicable, be the same for each holder delivering a conversion notice.

#### ***Conversion by the Corporation into Common Shares***

The Series E First Preference Shares will not be convertible at the option of the Corporation prior to June 1, 2013. On and after this date, the Corporation may, at its option, upon not less than 30 days and not more than 60 days prior written notice, subject to applicable law and any necessary regulatory approvals, convert all, or from time to time any part of, the outstanding Series E First Preference Shares into that number of fully-paid and freely-tradeable Common Shares determined by dividing the then applicable redemption price per Series E First Preference Share (as set out below) plus all accrued and unpaid dividends up to but excluding the date fixed for conversion, by the greater of \$1.00 and 95% of the Current Market Price. Fractional Common Shares will not be issued on any conversion of Series E First Preference Shares, but in lieu thereof, the Corporation will make cash payments.

If less than all of the outstanding Series E First Preference Shares are at any time to be converted, such Series E First Preference Shares will be converted on a *pro rata* basis.

Upon exercise of this conversion right by the Corporation, the Corporation is not required to issue Common Shares to a purchaser having an address in, or in such circumstances where the Corporation or its transfer agent has reason to believe such purchaser is a resident of, any jurisdiction outside Canada, to the extent that such issue would require compliance by the Corporation with the securities or other laws of such jurisdiction.

#### ***Redemption***

The Series E First Preference Shares are not redeemable before June 1, 2013. On and after this date, subject to the terms of any shares of the Corporation ranking prior to the Series E First Preference Shares, to applicable law, to any necessary regulatory approvals and to the provisions described below under “Restrictions on Dividends and Retirement and Issue of Shares”, the Corporation may, at its option, upon not less than 30 days and not more than 60 days prior written notice, redeem all, or from time to time any part of, the outstanding Series E First Preference Shares by the payment in cash of a sum per redeemed share equal to \$25.75 if redeemed during the 12 months commencing June 1, 2013; \$25.50 if redeemed during the 12 months commencing June 1, 2014; \$25.25 if redeemed during the 12 months commencing June 1, 2015; and \$25.00 if redeemed on or after June 1, 2016 plus, in each case, all accrued and unpaid dividends up to but excluding the date fixed for redemption (less any tax required to be deducted and withheld by the Corporation).

If less than all of the outstanding Series E First Preference Shares are at any time to be redeemed, such Series E First Preference Shares will be redeemed on a *pro rata* basis.

#### ***Purchase for Cancellation***

Subject to applicable law and any necessary regulatory approvals, the Corporation may, at any time, purchase for cancellation, all or any part of the Series E First Preference Shares in the open market or by private agreement or otherwise at the lowest price or prices at which, in the opinion of the Board of Directors, such Series E First Preference Shares are obtainable.

#### ***Listing***

The TSX has conditionally approved the listing of the Series E First Preference Shares, as well as the Common Shares issuable upon the conversion of either the Series D First Preference Shares or the Series E First Preference Shares. Listing will be subject to the Corporation fulfilling all of the listing requirements of the TSX on or before July 12, 2004.

#### ***Liquidation, Dissolution and Winding Up***

In the event of the liquidation, dissolution or winding up of the Corporation or any other distribution of assets of the Corporation among its shareholders for the purpose of winding up its affairs, the holders of the Series E First Preference Shares will be entitled to payment of an amount equal to \$25.00 per Series E First Preference Share plus all accrued and unpaid dividends up to but excluding the date fixed for payment or distribution (less any tax required to be deducted and withheld by the Corporation), before any amount is paid or any assets of the Corporation are distributed to the holders of the Common Shares or any other shares ranking junior as to return of capital to the Series E First

Preference Shares. The holders of the Series E First Preference Shares will not be entitled to share in any further distribution of the assets of the Corporation.

#### ***Restriction on Dividends and Retirement and Issue of Shares***

So long as any of the Series E First Preference Shares are outstanding, the Corporation will not, without the approval of the holders of the Series E First Preference Shares:

- (a) declare, pay or set apart for payment any dividends (other than stock dividends payable in shares of the Corporation ranking as to return of capital and dividends junior to the Series E First Preference Shares) on any shares of the Corporation ranking as to dividends junior to the Series E First Preference Shares;
- (b) except out of the net cash proceeds of a substantially concurrent issue of shares of the Corporation ranking as to return of capital and dividends junior to the Series E First Preference Shares, redeem or call for redemption, purchase or otherwise pay off, retire or make any return of capital in respect of any shares of the Corporation ranking as to capital junior to the Series E First Preference Shares;
- (c) redeem or call for redemption, purchase or otherwise retire for value or make any return of capital in respect of less than all of the Series E First Preference Shares then outstanding;
- (d) except pursuant to any purchase obligation, sinking fund, retraction privilege or mandatory redemption provisions attaching thereto, redeem or call for redemption, purchase or otherwise pay off, retire or make any return of capital in respect of any First Preference Shares, ranking as to dividends or capital on a parity with the Series E First Preference Shares; or
- (e) issue any shares (other than additional Series E First Preference Shares) ranking as to dividends or capital prior to or on a parity with the Series E First Preference Shares,

unless, in each such case, all accrued and unpaid dividends up to and including the dividend payable for the last completed period for which dividends were payable on the Series E First Preference Shares and on all other shares of the Corporation ranking as to dividends prior to or on a parity with the Series E First Preference Shares with respect to the payment of dividends have been declared and paid or set apart for payment.

#### ***Voting Rights***

The holders of the Series E First Preference Shares will not be entitled (except as otherwise provided by law and except for meetings of the holders of First Preference Shares as a class and meetings of the holders of Series E First Preference Shares as a series) to receive notice of, attend or vote at, any meetings of the shareholders of the Corporation except if the Corporation fails to pay eight quarterly dividends on the Series E First Preference Shares, whether or not consecutive and whether or not such dividends have been declared and whether or not there are any monies of the Corporation properly applicable to the payment of dividends. In that event and for only so long as any such dividends remain in arrears, the holders of the Series E First Preference Shares will be entitled to receive notice of and to attend all shareholders' meetings of the Corporation which take place more than 60 days after the date on which the failure first occurs (other than a separate meeting of the holders of another series or class of shares) and such holders shall have the right, at any such meeting, to one vote for each Series E First Preference Share held. No other voting rights shall attach to the Series E First Preference Shares in any circumstances. The voting rights of the holders of the Series E First Preference Shares shall forthwith cease upon payment by the Corporation of all such dividends in arrears on the Series E First Preference Shares to which the holders are entitled, until such time as the Corporation may again fail to pay eight quarterly dividends on the Series E First Preference Shares, whether or not consecutive and whether or not such dividends have been declared and whether or not there are any monies of the Corporation properly applicable to the payment of dividends, in which event such voting rights shall become effective again and so on from time to time.

#### ***Shareholder Approvals***

The approval of all amendments to the rights, privileges, restrictions and conditions attaching to the Series E First Preference Shares as a series and any other approval to be given by the holders of the Series E First Preference Shares may be given by a resolution carried by an affirmative vote of at least  $66\frac{2}{3}\%$  of the votes cast at a meeting at which the holders of not less than a majority of the outstanding Series E First Preference Shares are present or represented by proxy or, if no quorum is present at such meeting, at an adjourned meeting at which the holders of Series E First Preference Shares then present would form the necessary quorum. At any meeting of holders of Series E First

Preference Shares as a series, each such holder shall be entitled to one vote in respect of each Series E First Preference Share held.

### ***Priority***

The Series E First Preference Shares rank *pari passu* with all other series of First Preference Shares and senior to all other shares of the Corporation with respect to priority to the payment of dividends and the distribution of assets on the dissolution, liquidation or winding up of the Corporation.

### ***Tax on Preference Share Dividends***

The Corporation will elect, in the manner and within the time provided under subsection 191.2(1) of the Tax Act, to pay or cause payment of tax under Part VI.1 of the Tax Act at a rate such that the corporate holders of Series E First Preference Shares will not be required to pay tax under Part IV.1 of the Tax Act on dividends received on such shares.

### ***Book-Entry Only Form***

Upon the conversion of a Series D First Preference Share with the concurrent exercise of a Warrant and additional payment, the Series E First Preference Shares will be issued in book-entry only form. The Corporation will cause a global certificate or certificates representing newly issued Series E First Preference Shares to be delivered to and registered in the name of CDS or its nominee. Each holder of Series E First Preference Shares will receive only a customer confirmation of purchase from the registered dealer from or through which the Series E First Preference Shares are acquired in accordance with the practices and procedures of that registered dealer. The practices of registered dealers may vary, but generally customer confirmations are issued promptly after execution of a customer order. CDS is responsible for establishing and maintaining book-entry accounts for the CDS Participants having interests in the Series E First Preference Shares.

**Any holder of Series E First Preference Shares who desires to exercise conversion rights thereunder must do so by causing a CDS Participant to deliver to CDS (at its office in the City of Toronto), on behalf of the holder, a written notice (the “Series E Conversion Notice”) of the holder’s intention to convert shares sufficiently in advance of the relevant notice date so as to permit the CDS Participant to deliver notice to CDS by the required time.** The Series E Conversion Notice may take the form of the notice attached as Exhibit C hereto or such other form as each CDS Participant may prescribe. Any expenses associated with the preparation and delivery of the Series E Conversion Notice shall be for the account of the holder exercising the conversion right.

By causing a CDS Participant to deliver the Series E Conversion Notice to CDS, a holder shall be deemed to have irrevocably surrendered his or her shares for conversion and appointed such CDS Participant to act as his or her exclusive settlement agent with respect to the exercise of the conversion right and the receipt of payment in connection with the settlement of obligations arising from such exercise.

Any Series E Conversion Notice that CDS determines to be incomplete, not in proper form or not duly executed shall for all purposes be void and of no effect and the conversion right to which it relates shall be considered for all purposes not to have been exercised thereby. In the event of a determination that the Series E Conversion Notice is incomplete, not in proper form or not duly executed, CDS shall promptly notify the CDS Participant that delivered the conversion notice. A failure by a CDS Participant to exercise conversion rights or to give effect to the settlement thereof in accordance with the holder’s instructions will not give rise to any obligations or liability on the part of the Corporation to the CDS Participant or the holder.

**The Corporation has the option to terminate registration of the Series E First Preference Shares through the book-entry only system, in which case certificates for the Series E First Preference Shares will be issued in fully registered form to beneficial owners of such shares or their nominees.**

### ***Transfers***

Transfers of ownership in the Series E First Preference Shares will be effected only through records maintained by CDS for such Series E First Preference Shares with respect to interests of CDS Participants, and on the records of CDS Participants with respect to interests of holders other than CDS Participants. Holders of Series E First Preference Shares, other than CDS Participants, wishing to purchase, sell or otherwise transfer ownership of or other interests in the Series E First Preference Shares may do so only through CDS Participants. The ability of a holder to pledge



Series E First Preference Shares or otherwise take action with respect to such holder's interest in Series E First Preference Shares (other than through a CDS Participant) may be limited due to the lack of a physical certificate.

### ***Payments and Deliveries***

Payments of dividends, if any, or other amounts in respect of Series E First Preference Shares will be made by or on behalf of the Corporation to CDS or its nominee as the registered holder of the Series E First Preference Shares and the Corporation understands that such payments or deliveries will be forwarded by CDS or its nominee, net of any applicable withholding taxes, to CDS Participants in accordance with CDS Procedures. As long as CDS or its nominee is the registered holder of the Series E First Preference Shares, CDS or its nominee will be considered the sole owner of the Series E First Preference Shares for purposes of receiving any payments thereon and for all other purposes.

### **Description of the Warrants**

The Warrants will be issued pursuant to and governed by an indenture (the "Warrant Indenture") to be entered into between the Corporation and Computershare, as warrant trustee for the holders of Warrants, on the Closing Date. Each Warrant, together with a cash payment of \$18.75 per Warrant, will entitle the holder thereof to acquire 0.75 of a fully-paid and freely-tradeable Series E First Preference Share upon the exercise thereof. **A Series D First Preference Share cannot be converted into 0.25 of a fully-paid and freely-tradeable Series E First Preference Share without the concurrent exercise of a Warrant, and a Warrant cannot be exercised without the concurrent conversion of a Series D First Preference Share into 0.25 of a fully-paid and freely-tradeable Series E First Preference Share. A Warrant may not be separated from the related Series D First Preference Share forming a Unit.** Consequently, the conversion of one Series D First Preference Share, the exercise of one Warrant and a cash payment of \$18.75 will entitle the holder of a Unit to receive one fully-paid and freely-tradeable Series E First Preference Share. If the Acquisition closes on or prior to June 30, 2004, each Warrant will be exercisable on July 15, 2004, September 1, 2004 or December 1, 2004 in accordance with the provisions of the Warrant Indenture. If the Acquisition does not close on or prior to June 30, 2004, all Warrants will be void and of no effect as of the Early Expiry Time. If the Acquisition closes on or prior to June 30, 2004, all Warrants that for any reason have not been exercised by the Expiry Time will be void and of no effect.

The exercise of a Warrant will be effected by the registered holder thereof depositing with Computershare no later than 5:00 p.m. (Toronto time) on the date set for conversion, being July 15, 2004, September 1, 2004 or December 1, 2004 at its offices in Toronto or Montréal, a Unit certificate with a duly completed exercise and conversion panel as prescribed by the Warrant Indenture and a cash payment in the amount of \$18.75 per Warrant to be exercised. As long as the Units are held in the CDS book-entry only system, beneficial owners of Units may only exercise Warrants by providing instructions to the CDS Participants through which they hold Units, and such CDS Participants will communicate such exercise instructions to CDS in accordance with CDS Procedures.

Under the terms of the Warrant Indenture, subscriptions for Series E First Preference Shares pursuant to the exercise of the Warrants and conversion of Series D First Preference Shares by any person who is not a U.S. Person (as defined in Regulation S under the 1933 Act) or a person in the United States (as defined in Regulation S under the 1933 Act) or by any person on behalf of or for the account of a U.S. Person or a person in the United States will be conditioned upon delivery to the Corporation of a certification to that effect in order to establish the availability of an exemption from registration under the 1933 Act. The issuance of Series E First Preference Shares to any holder that does not make such certification will be conditioned upon the receipt by the Corporation and Computershare, as trustee for the holders of the Warrants, of such legal opinions, agreements and documentation as the Corporation or Computershare may reasonably request.

Under the Warrant Indenture, each person or company who exercises a Warrant (an "Exerciser") will have a contractual right of action against the Corporation for rescission following the issuance of Series E First Preference Shares to such Exerciser entitling the Exerciser to rescind its purchase and receive the \$18.75 exercise price per Warrant if the Prospectus or any amendment thereto contains a misrepresentation (as defined in the *Securities Act* (Ontario)) or if the Corporation's Disclosure Record (as defined below) contains a misrepresentation (as defined in the *Securities Act* (Ontario)).

Alternatively, the Warrant Indenture will provide that an Exerciser who is also an original purchaser of Units will have a contractual right of action against the Corporation for rescission following the issuance of Series E First Preference Shares to such Exerciser entitling the Exerciser to rescind its purchase and receive the amount paid for the

Units and the \$18.75 exercise price per Warrant if the Prospectus or any amendment thereto contains a misrepresentation (as defined in the *Securities Act* (Ontario)) or if the Corporation's Disclosure Record (as defined below) contains a misrepresentation (as defined in the *Securities Act* (Ontario)).

Under the Warrant Indenture, each Exerciser will have a contractual right of action against the Corporation for damages following the issuance of a Series E First Preference Share to the Exerciser entitling the Exerciser to claim up to the \$18.75 exercise price per Warrant if the Prospectus or any amendment thereto contains a misrepresentation (as defined in the *Securities Act* (Ontario)) or if the Corporation's Disclosure Record (as defined below) contains a misrepresentation (as defined in the *Securities Act* (Ontario)).

Alternatively, the Warrant Indenture will provide that an Exerciser who is also an original purchaser of Units will have a contractual right of action against the Corporation for damages following the issuance of a Series E First Preference Share to the Exerciser entitling the Exerciser to claim up to the amount paid for the Units and the \$18.75 exercise price per Warrant if the Prospectus or any amendment thereto contains a misrepresentation (as defined in the *Securities Act* (Ontario)) or if the Corporation's Disclosure Record (as defined below) contains a misrepresentation (as defined in the *Securities Act* (Ontario)).

Any statement contained in the Prospectus or any amendment thereto or in the Corporation's Disclosure Record (as defined below) shall be deemed to be modified or superseded for purposes of the contractual rights of action described herein to the extent that a statement contained in any subsequently filed Disclosure Document (as defined below) modifies or supersedes such statement. The modifying or superseding statement need not state that it has modified or superseded a prior statement or include any other information set forth in the document that it modifies or supersedes. The making of a modifying or superseding statement will not be deemed an admission for any purpose that the modified or superseded statement, when made, constituted a misrepresentation (as defined in the *Securities Act* (Ontario)), an untrue statement of a material fact or an omission to state a material fact that is required to be stated or that is necessary to make a statement not misleading in light of the circumstances in which it was made.

The contractual rights of action outlined above are subject to the following conditions: (i) if the Exerciser elects to exercise the right of action for rescission, the Exerciser will have no right of action for damages against the Corporation; (ii) the Corporation will not be liable if it proves that the Exerciser purchased the Units or, with respect to the \$18.75 exercise price per Warrant, exercised the Warrants, with knowledge of the misrepresentation (as defined in the *Securities Act* (Ontario)); (iii) in the case of an action for damages, the Corporation will not be liable for all or any portion of the damages that it proves do not represent the depreciation in value of the Series E First Preference Shares as a result of the misrepresentation (as defined in the *Securities Act* (Ontario)) relied upon; (iv) the recoverable amount will not exceed: (A) in the case of an action for rescission or damages by an Exerciser, the \$18.75 exercise price per Warrant; and (B) in the case of an action for rescission or damages by an Exerciser who is also an original purchaser, \$25.00 per Series E First Preference Share, less, in each case, any amount recovered pursuant to a statutory right of action in respect of such amount; (v) no action may be commenced to enforce a right of action for rescission more than 180 days after the date on which the Series E First Preference Shares were issued to the Exerciser; and (vi) no action may be commenced to enforce a right of action for damages more than the earlier of: (A) 180 days after the purchaser first had knowledge of the facts giving rise to the cause of action; and (B) three years after the date on which the Series E First Preference Shares were issued to the Exerciser.

The contractual rights of action described in the preceding paragraphs are in addition to and without derogation from any other right or remedy that purchasers of Units may have at law.

For the purposes of the Warrant Indenture, the "Corporation's Disclosure Record" means: (i) any material change reports (excluding confidential material change reports); (ii) any interim financial statements (including management discussion and analysis thereon); (iii) the audited annual comparative financial statements for the years ended December 31, 2003 and 2002 together with the notes thereto and the auditor's report thereon to be contained in the Corporation's 2003 Annual Report; (iv) the annual information form to be filed in 2004; and (v) any information circulars (excluding sections entitled "Report on Executive Compensation", "Performance Graph" and "Report on Corporate Governance"), which, in each case, are required to be filed pursuant to applicable securities legislation after the date hereof and prior to the Expiry Time. A "Disclosure Document" means any of the documents contained in the Corporation's Disclosure Record.

The Warrant Indenture provides for modifications and alterations to the rights of the holders of Warrants by way of an extraordinary resolution. The term "extraordinary resolution" is defined in the Warrant Indenture as a resolution

proposed at a meeting of holders of Warrants duly convened for that purpose and held in accordance with the Warrant Indenture at which there are present in person or by proxy holders of Warrants holding in the aggregate at least 25% of the total number of Warrants outstanding and passed by the affirmative votes of holders of Warrants holding in the aggregate not less than 66<sup>2</sup>/<sub>3</sub>% of the total number of Warrants then outstanding represented at the meeting and voted on the poll upon such resolution.

### **CHANGES IN SHARE AND LOAN CAPITAL STRUCTURE**

The following changes in the share and loan capital structure of Fortis have occurred since December 31, 2002:

- In January 2003, Fortis borrowed US\$45 million from a Canadian chartered bank, which was used to finance the purchase of additional shares of Fortis Energy (Bermuda) Ltd., to enable such subsidiary to increase its ownership interest in Caribbean Utilities to 38.2% from 22%. This loan was repaid in June 2003.
- During 2003, Fortis issued an aggregate of 188,355 Common Shares pursuant to the Corporation's Dividend Reinvestment and Share Purchase Plan, Consumer Share Purchase Plan and Employee Share Purchase Plan and upon the exercise of options granted pursuant to the Executive Stock Option Plan and Directors' Stock Option Plan for an aggregate consideration of \$9,431,330.
- On May 20, 2003, Fortis issued, by way of private placement, US\$10 million aggregate principal amount of Subordinated Convertible Debentures bearing interest at an annual rate of 5.5% and maturing on May 20, 2013. The debentures are convertible into Common Shares at US\$47.86 per share.
- In June 2003, Fortis completed a public offering of 5,000,000 5.45% Series C First Preference Shares at a price of \$25.00 per share for gross proceeds of \$125 million.
- In October 2003, Fortis completed a public offering of 6,310,000 Subscription Receipts at a price of \$55.50 per Subscription Receipt, for gross proceeds of \$350,205,000. Each such Subscription Receipt entitles the holder thereof to receive one Common Share upon the fulfillment of certain conditions related to the closing of the Acquisition.

### **USE OF PROCEEDS**

The proceeds to the Corporation from the Offering, after deducting the fee payable to the Underwriters and estimated expenses of the Offering, are expected to be \$43,350,000. The net proceeds of the Offering will be used for general corporate purposes, including the repayment of certain short-term indebtedness and the financing of a portion of the Acquisition. If the Acquisition does not close on or prior to June 30, 2004, the net proceeds intended to be used to finance the Acquisition will be used for other general corporate purposes. Proceeds of the exercise of the Warrants (assuming full exercise of the Warrants and conversion of the Series D First Preference Shares) will be \$150 million and will be used to repay certain short-term indebtedness incurred to fund the Acquisition. If the Acquisition does not close on or prior to June 30, 2004, no Warrants can be exercised and no further proceeds will therefore be received by the Corporation. See "The Acquisition" and "Financing of the Acquisition — Credit Agreements" and "Plan of Distribution".

### **EARNINGS COVERAGE RATIOS**

Based upon the annual dividend on the Series D First Preference Shares of \$0.3063, the annual dividend requirements of the Series D First Preference Shares and the 5,000,000 Series C First Preference Shares (adjusted to a before-tax equivalent using an effective income tax rate of 32.5%), would amount to \$13,709,000 for each of the 12 months ended December 31, 2002 and September 30, 2003. The Corporation's interest requirements for the 12 months ended December 31, 2002 and 12 months ended September 30, 2003 amounted to \$73,681,000 and \$81,180,000, respectively. The Corporation's earnings before interest and income tax for the 12 months ended December 31, 2002 and 12 months ended September 30, 2003 were \$169,421,000 and \$191,844,000, respectively, which is 1.94 times and 2.02 times the Corporation's aggregate dividend and interest requirements for the periods, respectively.

Based upon the annual dividend on the Series E First Preference Shares (assuming exercise of all of the Warrants and conversion of all the Series D First Preference Shares) of \$1.225, the annual dividend requirements for the Series E First Preference Shares and the 5,000,000 Series C First Preference Shares (adjusted to a before-tax equivalent using an effective income tax rate of 32.5%) would amount to \$24,587,000 for each of the 12 months ended December 31, 2002

and September 30, 2003. The Corporation's *pro forma* interest requirements for the 12 months ended December 31, 2002 and the 12 months ended September 30, 2003, assuming the closing of the Acquisition, amounted to \$126,295,000 and \$136,813,000, respectively. The Corporation's *pro forma* earnings before interest and income tax for the 12 months ended December 31, 2002 and 12 months ended September 30, 2003, assuming the closing of the Acquisition, were \$274,882,000 and \$189,072,000, respectively, which is 1.82 times and 1.17 times the Corporation's aggregate dividend and interest requirements for such periods, respectively.

## RATINGS

The Series D First Preference Shares and Series E First Preference Shares are rated Pfd-3 (high) by DBRS. The Series D First Preference Shares and Series E First Preference Shares are rated P-2 (low) by S&P.

The DBRS rating of Pfd-3 (high) is the first of three sub categories within the third highest rating of the five standard categories of ratings utilized by DBRS for preferred shares. A P-2 (low) rating by S&P is the third of the three sub-categories within the second highest rating of the eight standard categories of ratings utilized by S&P for preferred shares.

Credit ratings are intended to provide investors with an independent measure of the credit quality of an issue of securities. The credit ratings accorded to the Series D First Preference Shares and Series E First Preference Shares by these rating agencies are not recommendations to purchase, hold or sell the Units, the Series D First Preference Shares or the Series E First Preference Shares inasmuch as such ratings do not comment as to market price or suitability for a particular investor. There is no assurance that any rating will remain in effect for any given period of time or that any rating will not be revised or withdrawn entirely by a rating agency in the future if, in its judgment, circumstances so warrant.

On January 7, 2004, S&P announced that it had lowered its corporate credit rating of Fortis to BBB+ (negative outlook) from A-. At the same time, S&P removed Fortis from credit watch where it was placed in March 2003. The corporate credit rating of Fortis by DBRS is BBB+ (stable outlook).

## PLAN OF DISTRIBUTION

Pursuant to an underwriting agreement dated January 13, 2004 (the "Underwriting Agreement") between Fortis and the Underwriters, Fortis has agreed to issue and sell, and the Underwriters have agreed to purchase, as principals, on the Closing Date, 8,000,000 Units offered hereby at a price of \$6.25 per Unit, subject to compliance with all the necessary legal requirements and to the conditions contained in the Underwriting Agreement.

The Corporation has agreed to pay to the Underwriters a fee of \$0.25 for each Unit purchased by the Underwriters and sold to certain institutions and \$0.75 per Unit for all other Units purchased by the Underwriters in consideration for its services in connection with the Offering. The aggregate Underwriters' fee for the Units, assuming that no Units are sold to these institutions, will be \$6,000,000. No additional fee is payable by the Corporation to the Underwriters in connection with the exercise of the Warrants or the conversion of Series D First Preference Shares or otherwise in respect of the Offering.

Subscriptions for the Units will be received, subject to rejection or allotment in whole or in part, and the right is reserved to close the subscription books at any time without notice. It is expected that the closing of the Offering will take place on the Closing Date, or such other date as may be agreed upon by the Corporation and the Underwriters, but not later than February 27, 2004.

Pursuant to policy statements of the relevant securities commissions, the Underwriters may not, throughout the period of distribution under the Prospectus, bid for or purchase Units. The foregoing restriction is subject to certain exceptions, as long as the bid or purchase is not engaged in for the purpose of creating actual or apparent active trading in or raising the price of such securities. These exceptions include a bid or purchase permitted under the by laws and rules of the TSX relating to market stabilization and passive market-making activities and a bid or purchase made to and on behalf of a customer where the order was not solicited during the period of distribution. Pursuant to the first-mentioned exception, in connection with the Offering, the Underwriters may over allot or effect transactions which stabilize or maintain the market price of the Units at levels other than those which may otherwise prevail on the open market. Such transactions, if commenced, may be discontinued at any time.

The Units (and the Series D First Preference Shares and the Warrants comprised therein) and the Series E First Preference Shares relating to such Units have not been, and will not be, registered under the 1933 Act or any state securities laws and, subject to certain exceptions, may not be offered, or delivered, directly or indirectly, or sold in the

United States except in certain transactions exempt from the registration requirements of the 1933 Act and in compliance with any applicable state securities laws. The Underwriters have agreed that they will not offer or sell the Units within the United States, its territories, its possessions and other areas subject to its jurisdiction or to, or for the account or benefit of, a “U.S. Person” (as defined in Regulation S under the 1933 Act), except in accordance with the Underwriting Agreement pursuant to an exemption from the registration requirements of the 1933 Act provided by Rule 144A thereunder and in compliance with applicable state securities laws. In addition, until 40 days after the commencement of the Offering, an offer or sale of Units within the United States by any dealer (whether or not participating in the Offering) may violate the registration requirements of the 1933 Act if such offer is made otherwise than in reliance on Rule 144A.

The obligations of the Underwriters under the Underwriting Agreement are several and may be terminated at their discretion upon the occurrence of certain stated events. The Underwriters are, however, obligated to take up and pay for all of the Units if any are purchased under the Underwriting Agreement. Under the terms of the Underwriting Agreement, the Underwriters may be entitled to indemnification by the Corporation against certain liabilities, including liabilities for misrepresentation in the Prospectus.

Each of Scotia Capital, BMO Nesbitt Burns Inc., CIBC World Markets Inc., National Bank Financial Inc., RBC Dominion Securities Inc. and TD Securities Inc. is an affiliate of a Canadian chartered bank that is part of a syndicate of banks that have agreed to extend credit facilities to the Corporation in connection with financing the Acquisition. Scotia Capital has agreed to act as the sole lead arranger and book runner in connection with this financing and is receiving a fee for its role as financial advisor to Fortis in connection with the Acquisition. Consequently, the Corporation may be considered a “connected issuer” of these Underwriters within the meaning of applicable securities legislation. None of these Underwriters will receive any direct benefit from the Offering other than the underwriting commission relating to the Offering. The decision to distribute the Units hereunder and the determination of the terms of the Offering were made through negotiation between the Corporation and the Underwriters. The chartered banks did not have any involvement in such decision or determination. See “Use of Proceeds”.

The TSX has conditionally approved the listing of the Units, including the Series D First Preference Shares and the Warrants comprised therein, distributed under the Prospectus and the Series E First Preference Shares issuable in respect thereof, as well as the Common Shares issuable upon the conversion of either the Series D First Preference Shares or the Series E First Preference Shares. The listing of the Units, including the Series D First Preference Shares and the Warrants comprised therein, and the Common Shares issuable upon the conversion of either the Series D First Preference Shares or the Series E First Preference Shares will be subject to the Corporation fulfilling all of the listing requirements of the TSX on or before April 12, 2004. The listing of the Series E First Preference Shares will be subject to the Corporation fulfilling all of the listing requirements of the TSX on or before July 12, 2004. As the Units will be listed upon the fulfillment by the Corporation of the listing requirements of the TSX relating thereto, the Series D First Preference Shares and the Warrants will not trade separately while the Units exist. If the Acquisition closes on or prior to June 30, 2004, the Series D First Preference Shares are convertible into Series E First Preference Shares, which are, in turn, convertible into Common Shares. If, however, the Acquisition does not close on or prior to June 30, 2004, the Series D First Preference Shares will be directly convertible into Common Shares on and after September 1, 2016 at the option of the holder and on and after June 1, 2013 at the option of the Corporation. If the Acquisition does not close on or prior to June 30, 2004, the Corporation will apply to have the Series D First Preference Shares separately listed and posted for trading on the TSX on the trading day immediately following the Early Expiry Time.

## **CANADIAN FEDERAL INCOME TAX CONSIDERATIONS**

In the opinion of Davies Ward Phillips & Vineberg LLP, counsel to Fortis, and Stikeman Elliott LLP, counsel to the Underwriters, the following is a summary of the principal Canadian federal income tax considerations under the Tax Act generally applicable to a purchaser of Units comprised of Series D First Preference Shares and Warrants acquired pursuant to the Prospectus who, at all relevant times for purposes of the Tax Act, is or is deemed to be a resident of Canada, deals at arm’s length with Fortis, holds Series D First Preference Shares, Warrants, Series E First Preference Shares acquired upon the exercise of Warrants and the conversion of Series D First Preference Shares and Common Shares acquired upon the conversion of either Series D First Preference Shares or Series E First Preference Shares (collectively, the “Securities”) as capital property and is not exempt from tax under Part I of the Tax Act. Generally, the Securities will be considered to be capital property to a holder provided the holder does not hold the Securities in the course of carrying on a business and has not acquired them in a transaction or transactions considered

to be an adventure in the nature of trade. Purchasers whose Series D First Preference Shares, Series E First Preference Shares or Common Shares do not otherwise qualify as capital property may make, in certain circumstances, the irrevocable election under subsection 39(4) of the Tax Act to have such shares and every “Canadian security” (as defined in the Tax Act) owned by such holder in the taxation year of the election, and in all subsequent years, deemed to be capital property.

This summary is based on the current provisions of the Tax Act and the regulations thereunder, all specific proposals to amend the Tax Act and the regulations publicly announced by, or on behalf of, the Minister of Finance (Canada) prior to the date hereof and counsel’s understanding of the current published administrative practices of the Canada Customs and Revenue Agency (“CCRA”). This summary does not otherwise take into account or anticipate any change in law, whether by legislative, governmental or judicial decision or action, nor does it take into account or consider any provincial, territorial or foreign income tax legislation or considerations which might differ significantly from those discussed herein.

This summary does not take into account the “mark-to-market rules” applicable to securities held by certain financial institutions, registered securities dealers and corporations controlled by one or more of the foregoing and, accordingly, holders that are “financial institutions” (as defined in the Tax Act for purposes of these rules) should consult their own tax advisors.

**This summary is of a general nature only and is not intended to be, nor should it be construed to be, legal or tax advice to any particular purchaser. Accordingly, prospective purchasers should consult their own tax advisors with respect to their particular circumstances.**

Each purchaser of Units and Fortis must allocate the purchase price of each Unit comprised of one Series D First Preference Share and one Warrant on a reasonable basis between the Series D First Preference Share and the Warrant to determine the cost of each for the purposes of the Tax Act. For its purposes, Fortis intends to allocate all of the purchase price of a Unit to the Series D First Preference Share and nothing to the Warrant. Although Fortis believes this allocation to be reasonable, it will not be binding on the CCRA.

### ***Warrants***

No gain or loss will be realized by a holder on the exercise of a Warrant. The cost to the holder of the 0.75 of a Series E First Preference Share acquired on the exercise of a Warrant will be the aggregate of the holder’s adjusted cost base of the Warrant immediately before the exercise thereof and the \$18.75 paid on the exercise of the Warrant. The cost to the holder of Series E First Preference Shares acquired on the exercise of Warrants must then be averaged with the adjusted cost base of all other Series E First Preference Shares then held by the holder as capital property for purposes of subsequently computing the adjusted cost base of each Series E First Preference Share of the holder.

A holder who disposes of, or is deemed to dispose of, a Warrant, including on expiry of a Warrant (but otherwise than on exercise of the Warrant), generally will realize a capital gain (or a capital loss) equal to the amount by which the proceeds of disposition, net of any reasonable costs of disposition, exceed (or are less than) the adjusted cost base of the Warrant to the holder. If a Warrant expires without exercise by the holder, the holder will be treated as having disposed of the Warrant for nil proceeds. A holder whose unexercised Warrant expires generally will realize a capital loss equal to the adjusted cost base to the holder of the Warrant at the time of expiry. See “Capital Gains and Capital Losses”.

### ***Conversions***

The exercise by a holder of the right to convert such holder’s Series D First Preference Share into 0.25 of a Series E First Preference Share will be deemed not to constitute a disposition of such Series D First Preference Share and will not give rise to a capital gain or capital loss. The cost to the holder of the 0.25 of a Series E First Preference Share issued on such conversion will be the adjusted cost base to such holder of such Series D First Preference Share immediately before such conversion. The adjusted cost base of all Series E First Preference Shares of the holder will be determined in accordance with the cost averaging rules in the Tax Act.

The conversion of Series D First Preference Shares or Series E First Preference Shares into Common Shares by either Fortis or the holder will be deemed not to constitute a disposition of such Series D First Preference Shares or Series E First Preference Shares, as the case may be, and will not give rise to a capital gain or capital loss. Except as described below, the cost to the holder of the Common Shares issued on the conversion of Series D First Preference Shares will be the adjusted cost base to such holder of such Series D First Preference Shares immediately before such

conversion. Similarly, except as described below, the cost to the holder of the Common Shares issued on the conversion of Series E First Preference Shares will be the adjusted cost base to such holder of such Series E First Preference Shares immediately before such conversion. The adjusted cost base of all Common Shares of the holder will be determined in accordance with the cost averaging rules contained in the Tax Act.

Under the CCRA's current administrative practice, a holder of Series D First Preference Shares or Series E First Preference Shares who receives cash on a conversion thereof not exceeding \$200 in lieu of a fractional share will have the option of recognizing the capital gain or capital loss arising on the disposition of the fractional share in computing the holder's income for the taxation year in which the conversion occurs or, alternatively, of reducing the adjusted cost base of the Common Shares received at the time of the conversion by the amount of cash received by the holder.

Upon the conversion of either Series D First Preference Shares or Series E First Preference Shares into Common Shares, an amount equal to the fair market value of the Common Shares received on conversion in respect of declared and unpaid dividends will be included in a holder's income as a dividend, and will be the cost to the holder of such shares. See "Dividends".

### ***Dividends***

Dividends, including deemed dividends, received on the Series D First Preference Shares, the Series E First Preference Shares and the Common Shares by a holder who is an individual must be included in the individual's income and generally will be subject to the gross up and dividend tax credit rules normally applicable to taxable dividends received by an individual from taxable Canadian corporations. Taxable dividends received by an individual may give rise to alternative minimum tax under the Tax Act, depending upon the individual's circumstances.

Dividends, including deemed dividends, received on the Series D First Preference Shares, the Series E First Preference Shares and the Common Shares by a holder that is a corporation must be included in computing the corporation's income and will normally be deductible in computing the taxable income of the corporation.

The Series D First Preference Shares and the Series E First Preference Shares are "taxable preferred shares" (as defined in the Tax Act). The terms of the Series D First Preference Shares and the terms of the Series E First Preference Shares require Fortis to make the necessary election under Part VI.1 of the Tax Act so that corporate holders will not be subject to tax under Part IV.1 of the Tax Act on dividends received, or deemed to be received, on the Series D First Preference Shares and the Series E First Preference Shares, as the case may be.

A "private corporation" (as defined in the Tax Act) or any other corporation controlled (whether by reason of a beneficial interest in one or more trusts or otherwise) by or for the benefit of an individual (other than a trust) or a related group of individuals (other than trusts) will generally be liable to pay refundable tax under Part IV of the Tax Act of 33 $\frac{1}{3}$ % on dividends received, or deemed to be received, on the Series D First Preference Shares, the Series E First Preference Shares or the Common Shares, to the extent such dividends are deductible in computing its taxable income.

### ***Dispositions***

A holder who disposes of, or is deemed to dispose of, Series D First Preference Shares, Series E First Preference Shares or Common Shares (either on redemption or otherwise than upon a conversion) will generally realize a capital gain (or a capital loss) to the extent that the proceeds of disposition, net of any reasonable costs of disposition, exceed (or are less than) the adjusted cost base of such shares to such holder. The amount of any deemed dividend arising on the redemption or acquisition by Fortis of any such shares (see "Redemptions") will not generally be included in computing the proceeds of disposition for such shares. Any loss realized on a disposition of a Series D First Preference Share, Series E First Preference Share or Common Share may be suspended or denied as a superficial loss if the holder or a person affiliated with the holder acquires a Series D First Preference Share, Series E First Preference Share or Common Share, as the case may be, or certain other property considered identical to such share within the period commencing 30 days before, and ending 30 days after, the disposition of the relevant shares giving rise to the loss. For the purpose of the rules which suspend a loss, a Series E First Preference Share acquired on conversion of a Series D First Preference Share and a Common Share acquired on conversion of a Series D First Preference Share or a Series E First Preference Share, in each case, is deemed to be a property identical to the share so converted.

If the holder is a corporation, any capital loss arising on the disposition of a Series D First Preference Share, Series E First Preference Share or Common Share, as the case may be, may be reduced, in certain circumstances, by the

amount of any dividends, including deemed dividends, which have been received on the relevant share. Analogous rules apply to a partnership or trust of which a corporation, trust or partnership is a member or beneficiary.

### ***Capital Gains and Capital Losses***

One-half of any capital gain (a “taxable capital gain”) realized by a holder in a taxation year must be included in the holder’s income in that year and one-half of any capital loss (an “allowable capital loss”) realized by a holder in a taxation year will be deducted from the holder’s taxable capital gains in that year. Allowable capital losses in excess of taxable capital gains generally may be carried back and deducted in any of the three preceding taxation years or carried forward and deducted in any subsequent year against net taxable capital gains realized in such years to the extent and under the circumstances described in the Tax Act.

Capital gains realized by an individual may give rise to a liability for minimum tax under the Tax Act. A Canadian-controlled private corporation, as defined in the Tax Act, may be subject to an additional refundable tax of 6<sup>2</sup>/<sub>3</sub>% on investment income (including taxable capital gains).

### ***Redemptions***

If Fortis redeems or otherwise acquires a Series D First Preference Share or a Series E First Preference Share (otherwise than by a purchase in the open market in the manner in which shares are normally purchased by a member of the public in the open market), the holder will be deemed to have received a dividend equal to the amount, if any, paid by Fortis in excess of the paid-up capital (as determined for purposes of the Tax Act) of such share at such time. Generally, the difference between the amount paid by Fortis and the amount of the deemed dividend will be treated as proceeds of disposition for the purposes of computing the capital gain or capital loss arising on the disposition of such share. In the case of a corporate shareholder, it is possible that in certain circumstances all or part of the deemed dividend may be treated as proceeds of disposition and not as a dividend.

## **RISK FACTORS**

An investment in the Units offered hereby and the Series E First Preference Shares issuable upon the conversion of a Series D First Preference Share and the concurrent exercise of the related Warrant involves certain risks in addition to those described in the Management Discussion and Analysis of financial condition and results of operations contained in the Corporation’s 2002 Annual Report incorporated by reference herein. Before investing, prospective purchasers of Units should carefully consider, in light of their own financial circumstances, the factors set out below, as well as the other information contained or incorporated by reference in the Prospectus.

### **Regulation**

The regulated operations of the Alberta Utility and the B.C. Utility are subject to the normal uncertainties faced by regulated companies. These uncertainties include the approval by the AEUB and the BCUC, as applicable, of customer rates that permit a reasonable opportunity to recover on a timely basis the estimated costs of providing services, including a fair return on rate base. The ability of the Alberta Utility and the B.C. Utility to recover the actual costs of providing services and to earn the approved rates of return depends on achieving the forecasts established in the rate-setting process. Upgrades of existing facilities and the addition of new facilities requires the approval of the regulators. There is no assurance that capital projects perceived as required by the management of the Alberta Utility or the B.C. Utility will be approved or that conditions to such approval will not be imposed. Capital cost overruns relative to approvals granted might not be recoverable.

Rate applications that establish revenue requirements may be subject to negotiated settlement procedures in both Alberta and British Columbia. Failing a negotiated settlement, rate applications may be pursued through public hearing processes. The Corporation expects both the Alberta Utility and the B.C. Utility will file rate applications for 2005. As a result of the proposed change in ownership, the B.C. Utility has filed an application with the BCUC to extend the existing settlement agreement and performance-based rate setting mechanism for 2004. There can be no assurance that the rate orders issued will permit the Alberta Utility or the B.C. Utility to recover all costs actually incurred and to earn the expected rate of return. A failure to obtain acceptable rate orders may adversely affect the business carried on by each of the Alberta Utility and the B.C. Utility, the undertaking or timing of proposed expansion projects, the issue and sale of securities, ratings assigned by rating agencies, and other matters which may, in turn, negatively impact the Alberta Utility’s or the B.C. Utility’s results of operations or financial position, as well as those of the Corporation.



Although Fortis considers the regulatory frameworks in each of Alberta and British Columbia to be fair and balanced, uncertainties do exist at the present time. Alberta's regulatory framework has undergone significant changes since the deregulation of new generation and the introduction of retail competition on January 1, 2001. See "Electric Utilities Market Overview". The regulations and market rules which govern the competitive wholesale and retail electricity markets in Alberta are relatively new and there may be significant changes in these regulations and market rules that could adversely affect the ability of the Alberta Utility to recover its costs or to earn a reasonable return on its capital. Currently, British Columbia's regulatory framework is generally based on traditional cost of service methodologies for designing and setting rates.

### **Market for Securities**

There is currently no market through which the Units or the Series E First Preference Shares may be sold. There can be no assurance that an active trading market will develop for the Units or the Series E First Preference Shares after the Offering, or if developed, that such a market will be sustained at the price level of the Offering. A Warrant may not be separated from the related Series D First Preference Share comprised in a Unit.

If the Acquisition closes on or prior to June 30, 2004, any Series D First Preference Shares not converted prior to the Expiry Time will not be listed on the TSX after the Expiry Time.

### **Closing of the Acquisition**

If the Acquisition does not close on or prior to June 30, 2004, the gross proceeds of \$350,205,000 from the October 8, 2003 issue of Subscription Receipts by Fortis, which are currently being held in escrow by Computershare, will be returned to holders of Subscription Receipts.

If the Acquisition does not close, certain costs incurred by Fortis in connection with the Acquisition, which have been capitalized, as well as the cost of unwinding an interest rate hedging arrangement entered into in connection with the Acquisition, will be expensed by Fortis in 2004.

### **Results of Operations and Financing Risks**

Management of the Corporation believes, based on its expectations as to the Corporation's future performance (which reflects, among other things, the completion of the Acquisition), that the cash flow from its operations and funds available to it under its credit facilities will be adequate to enable the Corporation to finance its operations, execute its business strategy and maintain an adequate level of liquidity. However, expected revenue and the costs of planned capital expenditures are only estimates. Moreover, actual cash flows from operations are dependent on regulatory, market and other conditions that are beyond the control of the Corporation. As such, no assurance can be given that management's expectations as to future performance will be realized. In addition, management's expectations as to the Corporation's future performance reflect the current state of its information about the Alberta Utility and the B.C. Utility and their operations and there can be no assurance that such information is correct and complete in all material respects.

### **Management of Expanding Operations**

As a result of the Acquisition, significant demands will be placed on the Corporation's managerial, operational and financial personnel and systems. No assurance can be given that the Corporation's systems, procedures and controls will be adequate to support the expansion of the Corporation's operations resulting from the Acquisition. The Corporation's future operating results will be affected by the ability of its officers and key employees to manage changing business conditions and to implement and improve its operational and financial controls and reporting systems.

### **Realization of Acquisition Benefits**

The Corporation believes that the Acquisition will provide certain benefits to Fortis. However, there is a risk that some or all of the expected benefits of the Acquisition may fail to materialize, or may not occur within the time periods anticipated by the Corporation. The realization of such benefits may be affected by a number of factors including those disclosed in the Prospectus, many of which are beyond the control of the Corporation.

## **Asset Maintenance**

The asset base for the Alberta Utility and the B.C. Utility each requires significant maintenance, improvement and expansion. Both utilities could experience service disruptions and increased costs if they are unable to maintain and replace their assets. Planned capital expenditures to maintain, improve or expand the asset base of each of the Alberta Utility and the B.C. Utility are substantial. The failure to carry out these capital expenditure programs could have a material adverse effect on each of the Alberta Utility and the B.C. Utility. These large capital projects will proceed only under authorizations issued by the AEUB or the BCUC, as applicable. If actual costs exceed the forecast capital expenditure costs, it is uncertain as to whether any cost overruns will be approved by the AEUB or BCUC and recovered through rates.

## **Weather and Other Natural Disasters**

The facilities of the Alberta Utility and the B.C. Utility are exposed to the effects of severe weather conditions and other acts of nature. Although their facilities have been constructed, operated and maintained to withstand severe weather, there is no assurance that they will successfully do so in all circumstances. In addition, many of these facilities are located in remote areas, which makes access for repair of damage due to weather conditions and other acts of nature difficult. The B.C. Utility operates facilities in remote and mountainous terrain with a risk of loss or damage from forest fires, floods, washouts, landslides, avalanches and similar acts of nature. The Alberta Utility and the B.C. Utility have limited insurance against storm damage and other natural disasters. In the event of a large uninsured loss caused by severe weather conditions or other natural disasters, application will be made to the AEUB or the BCUC, as applicable, for the recovery of these costs through higher rates to offset any loss. However, there can be no assurance that the AEUB or the BCUC would approve any such application. Losses resulting from repair costs and lost revenues could substantially exceed insurance coverage and any increased rates. Furthermore, the Alberta Utility and the B.C. Utility could be subject to claims from their customers for damages caused by the failure to transmit or distribute electricity to them in accordance with their contractual obligations. Thus, any major damage to the Alberta Utility's or B.C. Utility's facilities could result in lost revenues, repair costs and customer claims that are substantial in amount, which amount could have a material adverse effect on the Alberta Utility or the B.C. Utility, as applicable.

## **Loss of Service Areas**

The Alberta Utility serves a number of direct customers that reside within various municipalities throughout its service areas. From time to time municipal governments in Alberta give consideration to creating their own electric distribution utility by purchasing the Alberta Utility's assets that are located within their municipal boundaries. Pursuant to the *Municipal Government Act* (Alberta), municipalities have the right to purchase the Alberta Utility's assets within municipal boundaries.

The consequence to the Alberta Utility of a municipality purchasing the Alberta Utility's assets would be an erosion of its rate base. This would reduce the capital upon which the Alberta Utility could earn a regulated return. Except for a current transaction involving the City of Airdrie, there have been no such transactions to date. The City of Airdrie recently gave the Alberta Utility notice of its intention to purchase the Alberta Utility's assets within its jurisdiction. The matter is currently before the AEUB, which is considering the appropriate methodology for valuing the distribution assets. The City of Airdrie is proposing a fair market value methodology whereas the Alberta Utility is proposing the traditional replacement cost less depreciation approach. A hearing on this matter is scheduled for April 5, 2004 and the City of Airdrie has indicated it may not purchase the assets if the AEUB does not decide in its favour. The assets within the City of Airdrie have a rate base in excess of \$9 million. The Corporation believes that the risk of a significant number of such transactions occurring is relatively low given that the cost of purchasing distribution assets will prove too high for most municipalities.

The B.C. Utility provides service to customers on First Nations reserves in British Columbia and maintains generation, transmission and distribution facilities on lands that are subject to land claims by various First Nations bands. A treaty negotiation process involving various First Nations bands and the British Columbia government is underway in British Columbia, but the basis upon which settlements might be reached in the B.C. Utility's service area is not clear. Furthermore, not all First Nations bands are participating in the process. To date, the policy of the British Columbia government has been to endeavour to structure settlements without prejudicing existing rights held by third parties such as the B.C. Utility, however, there can be no certainty that the settlement process will ultimately not adversely affect the B.C. Utility's business.

## **Government Permits**

The acquisition, ownership and operation of electricity businesses and assets require numerous permits, approvals and certificates from federal, provincial and local government agencies. Either or both of the Alberta Utility and the B.C. Utility may not be able to obtain or maintain all required regulatory approvals. If there is a delay in obtaining any required regulatory approval or if the Alberta Utility or the B.C. Utility fails to maintain or obtain any required approval or fails to comply with any applicable law or regulation, or condition of an approval, the operation of its assets and the sale of electricity could be prevented or become subject to additional costs, any of which could have a material adverse effect on the Alberta Utility or the B.C. Utility.

The B.C. Utility's ability to generate electricity from its facilities on the Kootenay River, and to receive its energy entitlement under the Canal Plant Agreement, depends upon the maintenance of its water licences issued under the *Water Act* (British Columbia). In addition, water flows in the Kootenay River are governed under the terms of the Columbia River Treaty between Canada and the United States. Government authorities in Canada and the United States have the power under the treaty to regulate water flows to protect environmental values in a manner that might adversely affect the amount of water available for the generation of power.

## **Financial Position of Aquila**

Aquila experienced a loss from operations of US\$2.1 billion in 2002. A deterioration in Aquila's financial position could adversely affect the ability of Aquila and the Vendors to satisfy their guarantee and indemnity obligations pursuant to the Acquisition and could affect the ability of the Vendors to complete the Acquisition. See "The Acquisition" and "Acquisition Agreements".

## **Potential Undisclosed Liabilities Associated with the Acquisition**

In connection with the Acquisition, there may be liabilities that the Corporation failed to discover or was unable to quantify in its due diligence which it conducted prior to the execution of the Acquisition Agreements and the Corporation may not be indemnified under the Acquisition Agreements for some or all of these liabilities. The discovery of any material liabilities could have a material adverse effect on the Corporation's business, financial condition or future prospects.

## **EPCOR Litigation**

The EPCOR litigation arises from issues related to the EPCOR Agreements. It is premature to make any definitive assessment of potential liability with respect to EPCOR's claim described under "The Acquired Businesses — Aquila Networks Canada (Alberta) Ltd. — EPCOR Litigation". However, if the EPCOR claim were to be successful, it could materially and adversely affect the business and operations of the Alberta Utility.

## **Labour Relations**

Approximately 72% and 75% of the employees of the Alberta Utility and the B.C. Utility, respectively, are members of labour unions which have entered into collective bargaining agreements with the Alberta Utility and the B.C. Utility, respectively. The provisions of such collective bargaining agreements affect the flexibility and efficiency of the business carried on by each of the Alberta Utility and the B.C. Utility. Each of the Alberta Utility and the B.C. Utility considers its relationships with its labour unions to be satisfactory, but there can be no assurance that current relations will continue in future negotiations or that the terms under the present collective bargaining agreements will be renewed. The inability to maintain, or to renew, the collective bargaining agreements on acceptable terms could result in increased labour costs, or service interruptions arising from labour disputes, for the Alberta Utility or the B.C. Utility that are not provided for in approved rate orders, that could have an adverse effect on the results of operations, cash flow and net income of the Alberta Utility or the B.C. Utility, as applicable.

## **Interest Rates**

The Alberta Utility and the B.C. Utility are exposed to the interest rate risks associated with floating rate debt. However, following the Acquisition, Fortis expects that the Alberta Utility and the B.C. Utility will replace these facilities with long-term fixed rate debt financing, the expenses of which will, subject to regulatory approval, be recovered in rates.

Allowed returns on equity for regulated utilities such as the Alberta Utility and the B.C. Utility are also exposed to changes in the general level of interest rates. As interest rates decrease, so does the allowed rate of return on equity.

## **Underinsured and Uninsured Losses**

The Corporation, the Alberta Utility and the B.C. Utility maintain at all times insurance coverage in respect of potential liabilities and the accidental loss of value of certain of their assets from risks, in amounts and with such insurers, as is considered appropriate, taking into account all relevant factors including the practices of owners of similar assets and operations. It is anticipated that such insurance coverage will be maintained. However, not all risks are covered by insurance, and no assurance can be given that insurance will be consistently available or will be consistently available on economically feasible terms or that the amounts of insurance will be sufficient to cover losses or claims that may occur involving the assets or operations of the Corporation, the Alberta Utility or the B.C. Utility.

## **Capital Resources**

Each of the Alberta Utility's and the B.C. Utility's financial position could be adversely affected if it fails to arrange sufficient and cost-effective financing to fund, among other things, capital expenditures and the repayment of maturing debt. Funds generated from operations after payment of expected expenses (including interest payments on any outstanding debt) will not be sufficient to fund the repayment of all outstanding liabilities when due and anticipated capital expenditures. The ability to arrange sufficient and cost-effective financing is subject to numerous factors, including the regulatory environment in each of Alberta and British Columbia, the results of operations and financial position of each of the Alberta Utility and the B.C. Utility, conditions in the capital and bank credit markets, the ratings assigned by rating agencies and general economic conditions. There can be no assurance that sufficient capital will be available on acceptable terms to fund such capital expenditures and to repay existing debt.

## **Environmental Matters**

The Alberta Utility and the B.C. Utility are subject to numerous laws, regulations and guidelines governing the management, transportation and disposal of hazardous substances and other waste materials and otherwise relating to the protection of the environment and health and safety. Potential environmental damage and costs could arise due to a severe weather event, human error or equipment failure. However, there can be no assurance that such costs will be recoverable and, if substantial, unrecovered costs may have a material effect on the business, results of operations and prospects of the Alberta Utility or the B.C. Utility.

The Alberta Utility and the B.C. Utility are exposed to environmental risks that property owners in Alberta and British Columbia generally face. These risks include the responsibility of any property owner for the site remediation of any properties determined to be contaminated, whether or not such contamination was actually caused by the owner. In addition, environmental and safety laws make owners, operators and persons in charge of management and control of facilities subject to prosecution or administrative action for breaches of environmental and safety laws, including the failure to obtain certificates of approval for the discharge of contaminants causing an adverse effect. Neither the Alberta Utility nor the B.C. Utility has been notified of any such regulatory action in regard to its operation or occupation of its facilities. However, it is not possible to predict with absolute certainty the position that a regulatory authority will take regarding matters of non-compliance with environmental and safety laws. Changes in environmental, health and safety regulations could also lead to significant increases in costs to the Alberta Utility or the B.C. Utility.

Most of the B.C. Utility's generating and transmission facilities have been in place for many years with no apparent adverse environmental impact. However, as facilities are upgraded and as new facilities are added, environmental assessments and regulatory approvals will be required in the ordinary course.

Extreme climatic factors could potentially cause government authorities to adjust water flows on the Kootenay River in order to protect environmental values and could affect the amount of water available for generation either at the B.C. Utility's plants or at plants operated by parties contracted to supply energy to the B.C. Utility.

Electricity transmission and distribution facilities have the potential to cause fires as a result of equipment failure, trees falling on a transmission or distribution line or lightning strikes to wooden poles. Risks associated with fire damage are related to weather, the degree of forestation, habitation and third party facilities located near the land on which the transmission facilities are situated. Each of the Alberta Utility and the B.C. Utility may be liable for fire-fighting costs and third party claims in connection with fires on these or other lands on which its transmission facilities are located, and such claims, if successful, could have a material effect on the business, results of operations and prospects of the Alberta Utility or the B.C. Utility.

## Arthur Andersen

The Prospectus includes financial statements of the Alberta Utility for the year ended December 31, 2001 and of the B.C. Utility for the years ended December 31, 2000 and 2001 that were audited and reported on by Arthur Andersen. The Corporation has not obtained the consent of Arthur Andersen to the use of its audit report in respect of these financial statements. Arthur Andersen's consent was not obtained because, on June 3, 2002, Arthur Andersen ceased to practise public accounting. Because Arthur Andersen has not provided this consent, purchasers of Units pursuant to the Prospectus will not have the statutory right of action for damages against Arthur Andersen as prescribed by applicable securities legislation with respect to these financial statements. In addition, Arthur Andersen may not have sufficient assets available to satisfy any judgments against it.

## LEGAL MATTERS

Certain legal matters relating to the Offering will be passed upon on behalf of Fortis by Davies Ward Phillips & Vineberg LLP and Curtis, Dawe and on behalf of the Underwriters by Stikeman Elliott LLP. At the date hereof, partners and associates of each of Davies Ward Phillips & Vineberg LLP, Curtis, Dawe and Stikeman Elliott LLP own beneficially, directly or indirectly, less than 1% of any securities of Fortis or any associate or affiliate of Fortis.

## AUDITORS, TRANSFER AGENT, REGISTRAR AND WARRANT TRUSTEE

Ernst & Young LLP, The Fortis Building, 7th Floor, 139 Water Street, St. John's, Newfoundland and Labrador, are the auditors of the Corporation.

The transfer agent and registrar for the Units, including the Series D First Preference Shares and the Warrants comprised therein, and the Series E First Preference Shares is Computershare Trust Company of Canada in Toronto and Montréal. Computershare Trust Company of Canada has been appointed by Fortis as trustee under the Warrant Indenture.

## PURCHASERS' STATUTORY RIGHTS

Securities legislation in certain provinces of Canada provides purchasers with the right to withdraw from an agreement to purchase securities within two business days after receipt or deemed receipt of the Prospectus and any amendments thereto. In several of the provinces, securities legislation further provides a purchaser with remedies for rescission or, in some provinces, damages where the short form prospectus and any amendments thereto contain a misrepresentation or are not delivered to the purchaser but such remedies must be exercised by the purchaser within the time limit prescribed by the securities legislation of such purchaser's province. Purchasers of Units may no longer have remedies for rescission following the issuance of the Series E First Preference Shares upon the conversion of the Series D First Preference Shares and exercise of the Warrants. Purchasers of Units will continue to have civil liability remedies, including remedies for damages that are provided to purchasers under securities legislation, in the event that the purchaser receives the Series E First Preference Shares upon the conversion of Series D First Preference Shares and concurrent exercise of Warrants. The purchaser should refer to any applicable provisions of the securities legislation of such purchaser's province for the particulars of these rights or consult with a legal advisor.

In addition, purchasers of the Units will have a contractual right of action for rescission and damages against the Corporation following the issuance of the Series E First Preference Shares to such purchaser. See "Details of the Offering — Description of the Warrants".

**In connection with the Offering, Fortis would normally be required to obtain a written consent from Arthur Andersen in order to include its audit report covering the audited financial statements of the Alberta Utility for the year ended December 31, 2001 and of the B.C. Utility for the years ended December 31, 2000 and 2001 included in the Prospectus. However, on June 3, 2002, Arthur Andersen ceased to practise public accounting in Canada. As a consequence, representatives of Arthur Andersen are no longer available to provide a consent in connection with the filing of the Prospectus. As a result of Arthur Andersen not having provided its consent, purchasers of Units pursuant to the Prospectus will not be able to recover damages from Arthur Andersen under applicable securities legislation with respect to its audit report. Furthermore, Arthur Andersen may not possess sufficient assets to satisfy any claims that may arise out of its audit of the financial statements.**

### AUDITORS' CONSENT

We have read the short form prospectus of Fortis Inc. (the "Corporation") dated January 20, 2004 relating to the issue and sale of 8,000,000 first preference units of the Corporation. We have complied with Canadian generally accepted standards for an auditor's involvement with offering documents.

We consent to the incorporation by reference in the above-mentioned prospectus of our report to the shareholders of the Corporation on the consolidated balance sheets of the Corporation as at December 31, 2002 and 2001 and the consolidated statements of earnings, retained earnings and cash flows for the years in the two-year period ended December 31, 2002. Our report is dated February 11, 2003.

St. John's, Canada  
January 20, 2004

(Signed) *Deloitte & Touche LLP*  
Chartered Accountants

### AUDITORS' CONSENT

We have read the short form prospectus of Fortis Inc. (the "Corporation") dated January 20, 2004 relating to the issue and sale of 8,000,000 first preference units of the Corporation. We have complied with Canadian generally accepted standards for an auditor's involvement with offering documents.

We consent to the use, in the above-mentioned prospectus, of our report dated January 20, 2004, to the Board of Directors of the Corporation on the unaudited *pro forma* consolidated balance sheet as at September 30, 2003, unaudited *pro forma* consolidated statement of earnings for the nine month period ended September 30, 2003 and unaudited *pro forma* consolidated statement of earnings for the year ended December 31, 2002.

St. John's, Canada  
January 20, 2004

(Signed) *ERNST & YOUNG LLP*  
Chartered Accountants

### AUDITORS' CONSENT

We have read the short form prospectus of Fortis Inc. (the "Corporation") dated January 20, 2004 relating to the issue and sale of 8,000,000 first preference units of the Corporation. We have complied with Canadian generally accepted standards for an auditor's involvement with offering documents.

We consent to the use, in the above-mentioned prospectus, of our report dated January 31, 2003, to the directors of Aquila Networks Canada (Alberta) Ltd. ("Aquila Alberta") on the balance sheet as at December 31, 2002 of Aquila Alberta and statements of operations, deficit and cash flows for the year ended December 31, 2002.

We also consent to the use, in the above-mentioned prospectus, of our report dated February 19, 2003, to the directors of Aquila Networks Canada (British Columbia) Ltd. ("Aquila B.C.") on the consolidated balance sheet as at December 31, 2002 of Aquila B.C. and consolidated statements of earnings, retained earnings and cash flows for the year ended December 31, 2002.

Calgary, Canada  
January 20, 2004

(Signed) *KPMG LLP*  
Chartered Accountants

## **SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS**

The Prospectus, and the documents incorporated herein by reference, contain forward-looking statements which reflect management's expectations regarding the Corporation's future growth, results of operations, performance and business prospects and opportunities. Wherever possible, words such as "anticipate", "believe", "expects", "intend" and similar expressions have been used to identify these forward-looking statements. These statements reflect management's current beliefs and are based on information currently available to the Corporation's management. Forward-looking statements involve significant risk, uncertainties and assumptions. A number of factors could cause actual results, performance or achievements to differ materially from the results discussed or implied in the forward-looking statements. These factors should be considered carefully and prospective investors should not place undue reliance on the forward-looking statements. Although the forward-looking statements contained in the Prospectus, and the documents incorporated herein by reference, are based upon what management believes to be reasonable assumptions, the Corporation cannot assure prospective purchasers that actual results will be consistent with these forward-looking statements. These forward-looking statements are made as of the date of the Prospectus, and the Corporation assumes no obligation to update or revise them to reflect new events or circumstances.

## GLOSSARY OF TERMS

*In the Prospectus, unless the context otherwise requires, the following terms have the meanings set forth below.*

“**1933 Act**” means the United States *Securities Act of 1933*, as amended;

“**Acquisition**” means the acquisition by the Corporation, directly or indirectly, of all of the issued and outstanding shares of the Alberta Utility and the B.C. Utility;

“**Acquisition Agreements**” means the Alberta Purchase Agreement and the B.C. Purchase Agreement;

“**AEUB**” means the Alberta Energy and Utilities Board;

“**Alberta Purchase Agreement**” means the share purchase agreement dated on September 15, 2003, between Fortis and ANCL for the purchase of all of the issued and outstanding shares, and the repayment of certain indebtedness, of the Alberta Utility, as amended;

“**Alberta Utility**” means Aquila Networks Canada (Alberta) Ltd.;

“**Alberta Utility Credit Facility**” means the \$393 million non-revolving credit facility made available to the Alberta Utility by a syndicate of Canadian chartered banks for purposes of the Acquisition;

“**ANBC**” means Aquila Networks British Columbia Ltd.;

“**ANCL**” means Aquila Networks Canada Ltd.;

“**Aquila**” means Aquila, Inc.;

“**Arthur Andersen**” means Arthur Andersen LLP;

“**B.C. Purchase Agreement**” means the share purchase agreement dated on September 15, 2003, between Fortis and ANBC for the purchase of all of the issued and outstanding shares, and the repayment of certain indebtedness, of the B.C. Utility, as amended;

“**B.C. Utility**” means Aquila Networks Canada (British Columbia) Ltd.;

“**BCUC**” means the British Columbia Utilities Commission;

“**CDS**” means The Canadian Depository for Securities Limited;

“**CDS Participant**” means a registered dealer who is a CDS participant from or through whom Units may be purchased or transferred;

“**CDS Procedures**” means the procedures of CDS;

“**Closing Date**” means January 29, 2004 or such other date as agreed to by the Corporation and the Underwriters, but not later than February 27, 2004;

“**Common Shares**” means common shares of the Corporation;

“**Conversion and Exercise Notice and Declaration**” means the notice and declaration relating to the conversion of the Series D First Preference Shares and the exercise of the Warrants, which is in the form of the notice and declaration attached hereto as Exhibit A;

“**Corporation**” means Fortis Inc.;

“**Corporation’s Disclosure Record**” means: (i) any material change reports (excluding confidential material change reports); (ii) any interim financial statements (including management discussion and analysis thereon); (iii) the audited annual comparative financial statements for the years ended December 31, 2003 and 2002 together with the notes thereto and the auditor’s report thereon to be contained in the Corporation’s 2003 Annual Report; (iv) the annual information form to be filed in 2004; and (v) any information circulars (excluding sections entitled “Report on Executive Compensation”, “Performance Graph” and “Report on Corporate Governance”), which, in each case, are required to be filed pursuant to applicable securities legislation after the date hereof and prior to the Expiry Time;

“**Credit Facilities**” means, collectively, the Fortis Credit Facility and the Alberta Utility Credit Facility;

“**Current Market Price**” means the weighted average trading price of the Common Shares on the TSX for the 20 consecutive trading days ending on the fourth trading day prior to the date fixed for conversion or, if that fourth day is not a trading day, on the immediately preceding trading day;

“**Disclosure Document**” means any of the documents contained in the Corporation’s Disclosure Record;



“**Early Expiry Time**” means 5:00 p.m. (Toronto time) on July 15, 2004;

“**EUA**” means the *Electric Utilities Act* (Alberta);

“**Exerciser**” means a person or company that exercises a Warrant;

“**Expiry Time**” means 5:00 p.m. (Toronto time) on December 1, 2004;

“**First Preference Shares**” means all series of first preference shares of the Corporation;

“**Fortis**” means Fortis Inc.;

“**Fortis Alberta**” means Fortis Alberta Holdings Inc.;

“**Fortis Credit Facility**” means the \$860 million non-revolving credit facility made available to the Corporation by a syndicate of Canadian chartered banks, for purposes of the Acquisition;

“**Fortis Pacific**” means Fortis Pacific Holdings Inc.;

“**Offering**” means the distribution of Units pursuant to the Prospectus;

“**Prospectus**” means this short form prospectus;

“**Release Conditions**” means the receipt by the Corporation of all regulatory and government approvals required to finalize the Acquisition, including those of AEUB and BCUC, and fulfillment or waiver of all other outstanding conditions precedent to closing the Acquisition as itemized in the Acquisition Agreements;

“**Second Preference Shares**” means all series of second preference shares of the Corporation;

“**SEDAR**” means the Canadian System for Electronic Document Analysis and Retrieval;

“**Series C First Preference Shares**” means cumulative redeemable convertible first preference shares, series C of the Corporation;

“**Series D Conversion Notice**” means the notice relating to the conversion of the Series D First Preference Shares, which is in the form of the notice attached hereto as Exhibit B;

“**Series D First Preference Shares**” means cumulative redeemable convertible first preference shares, series D of the Corporation;

“**Series D Subject Shares**” means Series D First Preference Shares that are the subject of a conversion notice;

“**Series E Conversion Notice**” means the notice relating to the conversion of the Series E First Preference Shares, which is in the form of the notice attached hereto as Exhibit C;

“**Series E First Preference Shares**” means cumulative redeemable convertible first preference shares, series E of the Corporation;

“**Series E Subject Shares**” means Series E First Preference Shares that are the subject of a conversion notice;

“**Subscription Receipts**” means the 6,310,000 subscription receipts issued by Fortis on October 8, 2003;

“**Tax Act**” means the *Income Tax Act* (Canada);

“**TSX**” means the Toronto Stock Exchange;

“**Underwriters**” means Scotia Capital Inc., BMO Nesbitt Burns Inc., CIBC World Markets Inc., National Bank Financial Inc., RBC Dominion Securities Inc., TD Securities Inc. and Beacon Securities Limited;

“**Underwriting Agreement**” means the underwriting agreement dated January 13, 2004, between the Corporation and the Underwriters relating to the sale of the Units offered under the Prospectus;

“**Units**” means first preference units of the Corporation, each of which is comprised of one Series D First Preference Share and one Warrant;

“**Vendors**” means ANCL and ANBC;

“**Warrant**” means a Series E First Preference Share purchase warrant of the Corporation; and

“**Warrant Indenture**” means the warrant indenture dated as of the Closing Date among Fortis and Computershare as trustee for the holders of the Warrants.

*All dollar amounts in the Prospectus are expressed in Canadian dollars.*

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***PRO FORMA CONSOLIDATED  
FINANCIAL STATEMENTS***

**FORTIS INC.**

Unaudited — See Compilation Report

**As at September 30, 2003 and for the nine month period ended  
September 30, 2003 and the year ended December 31, 2002**

## COMPILATION REPORT

To the Directors of  
FORTIS INC.

We have read the accompanying unaudited *pro forma* consolidated balance sheet of Fortis Inc. (the "Corporation") as at September 30, 2003 and unaudited *pro forma* consolidated statements of earnings for the nine months then ended and for the year ended December 31, 2002, and have performed the following procedures.

1. Compared the figures in the columns captioned "Fortis Inc." to the unaudited consolidated financial statements of the Corporation as at September 30, 2003 and for the nine months then ended, and the audited consolidated financial statements of the Corporation for the year ended December 31, 2002, respectively, and found them to be in agreement.
2. Compared the figures in the columns captioned "ANCA" and "ANCBC" to the unaudited financial statements of ANCA and ANCBC as at September 30, 2003 and for the nine months then ended and the audited financial statements of ANCA and ANCBC for the year ended December 31, 2002, respectively, and found them to be in agreement.
3. Made enquiries of certain officials of the Corporation who have responsibility for financial and accounting matters about:
  - (a) the basis for determination of the *pro forma* adjustments; and
  - (b) whether the *pro forma* financial statements comply as to form in all material respects with the securities legislation in Canada.

The officials:

- (a) described to us the basis for determination of the *pro forma* adjustments; and
  - (b) stated that the *pro forma* statements comply as to form in all material respects with the securities legislation in Canada.
4. Read the notes to the *pro forma* statements and found them to be consistent with the basis described to us for determination of the *pro forma* adjustments.
  5. Recalculated the application of the *pro forma* adjustments to the aggregate of the amounts in the columns captioned "Fortis Inc.", "ANCA" and "ANCBC" as at September 30, 2003 and for the nine months then ended, and for the year ended December 31, 2002, and found the amounts in the column captioned "Total" to be arithmetically correct.

A *pro forma* financial statement is based on management assumptions and adjustments, which are inherently subjective. The foregoing procedures are substantially less than either an audit or a review, the objective of which is the expression of assurance with respect to management's assumptions, the *pro forma* adjustments, and the application of the adjustments to the historical financial information. Accordingly, we express no such assurance. The foregoing procedures would not necessarily reveal matters of significance to the *pro forma* financial statements, and we therefore make no representation about the sufficiency of the procedures for the purposes of a reader of such statements.

St. John's, Canada,  
January 20, 2004

(Signed) ERNST & YOUNG LLP  
Chartered Accountants

**Fortis Inc.**

**PRO FORMA CONSOLIDATED BALANCE SHEET**

**As at September 30, 2003**

(Unaudited)

(in thousands of dollars)

	<b>Fortis Inc.</b>	<b>ANCA</b>	<b>ANCBC</b>		<i>Pro forma</i> <b>adjustments</b>	<b>Total</b>
	\$	\$	\$	Note	\$	\$
<b>ASSETS</b>						
<b>Current</b>						
Cash and cash equivalents .....	79,150	26,341	31,522		—	<b>137,013</b>
Receivables .....	131,011	71,242	30,939		—	<b>233,192</b>
Materials and supplies .....	16,979	10,844	4,812		—	<b>32,635</b>
Other receivables .....	—	11,290	3,444		—	<b>14,734</b>
Current portion of regulatory cost deferral .....	—	30,459	—		—	<b>30,459</b>
	<u>227,140</u>	<u>150,176</u>	<u>70,717</u>		<u>—</u>	<u><b>448,033</b></u>
Corporate income tax deposit .....	6,949	—	—		—	<b>6,949</b>
Cash held in escrow .....	7,792	—	—		—	<b>7,792</b>
Deferred charges .....	116,157	—	12,299	2(h)	4,000	<b>132,456</b>
Future income taxes .....	—	1,914	—	2(e)	9,149	<b>18,446</b>
				2(f)	5,096	
				2(g)	2,287	
Utility capital assets, net .....	1,250,180	460,760	440,730		—	<b>2,151,670</b>
Income producing properties .....	289,154	—	—		—	<b>289,154</b>
Investments .....	166,719	—	—		—	<b>166,719</b>
Intangibles, net of amortization .....	23,340	—	—		—	<b>23,340</b>
Goodwill .....	65,435	189,309	—	2(b)	309,926	<b>564,670</b>
	<u>2,152,866</u>	<u>802,159</u>	<u>523,746</u>		<u>330,458</u>	<u><b>3,809,229</b></u>
<b>LIABILITIES</b>						
<b>Current</b>						
Short-term borrowings & current portion of long-term debt	117,627	144,990	60,219		—	<b>322,836</b>
Accounts payable and accrued charges .....	142,652	115,189	56,080		—	<b>313,921</b>
Current installments securitization financing .....	—	63,957	—		—	<b>63,957</b>
Future income taxes .....	5,782	—	—		—	<b>5,782</b>
	<u>266,061</u>	<u>324,136</u>	<u>116,299</u>		<u>—</u>	<u><b>706,496</b></u>
Long-term debt .....	1,023,177	230,000	224,477	2(a)	193,795	<b>1,671,449</b>
				2(e)	24,000	<b>24,000</b>
Deferred credits .....	62,458	4,324	—		—	<b>66,782</b>
Future income taxes .....	30,327	—	1,744		—	<b>32,071</b>
Non-controlling interest .....	36,863	—	—		—	<b>36,863</b>
	<u>1,418,886</u>	<u>558,460</u>	<u>342,520</u>		<u>217,795</u>	<u><b>2,537,661</b></u>
<b>SHAREHOLDERS' EQUITY</b>						
Common shares .....	327,900	347,579	76,500		(424,079)	<b>669,201</b>
				2(f)	341,301	
Preference shares .....	122,992	—	—	2(g)	196,287	<b>319,279</b>
Contributed surplus .....	665	—	—		—	<b>665</b>
Equity portion of convertible debentures .....	1,741	—	—		—	<b>1,741</b>
Foreign currency translation adjustment .....	(8,945)	—	—		—	<b>(8,945)</b>
Retained earnings .....	289,627	(103,880)	104,726		(846)	<b>289,627</b>
	<u>733,980</u>	<u>243,699</u>	<u>181,226</u>		<u>112,663</u>	<u><b>1,271,568</b></u>
	<u>2,152,866</u>	<u>802,159</u>	<u>523,746</u>		<u>330,458</u>	<u><b>3,809,229</b></u>

See accompanying notes

**Fortis Inc.**

**PRO FORMA CONSOLIDATED STATEMENT OF EARNINGS**

**For the year ended December 31, 2002**

(in thousands of dollars, except for per share amounts)

	<b>Fortis Inc.</b>	<b>ANCA</b>	<b>ANCBC</b>		<i>Pro forma</i> <b>adjustments</b>	<b>Total</b>
	\$	\$	\$	Note	\$	\$
<b>Operating Revenues</b> .....	715,465	268,536	153,994		—	<b>1,137,995</b>
<b>Expenses</b>						
Operating .....	476,969	100,117	109,072		—	<b>686,158</b>
Amortization .....	65,063	82,578	14,685	2[h]	400	<b>162,726</b>
	<u>542,032</u>	<u>182,695</u>	<u>123,757</u>		<u>400</u>	<b>848,884</b>
<b>Net Operating Income</b> .....	173,433	85,841	30,237		(400)	<b>289,111</b>
<b>Finance Charges</b>						
Interest .....	70,728	24,924	14,341	2[d]	13,566	<b>123,559</b>
Dividends on preference shares .....	2,736	—	—		—	<b>2,736</b>
	<u>73,464</u>	<u>24,924</u>	<u>14,341</u>		<u>13,566</u>	<b>126,295</b>
<b>Earnings Before Undernoted Items, Income Taxes and</b>						
<b>Non-Controlling Interest</b> .....	99,969	60,917	15,896		(13,966)	<b>162,816</b>
Impairment in the carrying value of the Walden Power Plant ..	—	—	10,000		—	<b>10,000</b>
<b>Earnings Before Income Taxes and</b>						
<b>Non-Controlling Interest</b> .....	99,969	60,917	5,896		(13,966)	<b>152,816</b>
Income Taxes .....	32,488	33,376	(242)	2[i]	(5,603)	<b>60,019</b>
<b>Earnings Before Non-Controlling Interest</b> .....	67,481	27,541	6,138		(8,363)	<b>92,797</b>
Non-controlling interest .....	4,229	—	—		—	<b>4,229</b>
<b>Earnings</b> .....	<u>63,252</u>	<u>27,541</u>	<u>6,138</u>		<u>(8,363)</u>	<b>88,568</b>
Dividends on preference shares .....	—	—	—	2[g]	9,800	<b>9,800</b>
<b>Earnings Applicable to Common Shares</b> .....	<u>63,252</u>	<u>27,541</u>	<u>6,138</u>		<u>(18,163)</u>	<b>78,768</b>
<b>Average Common Shares Outstanding</b> .....	<u>16,277</u>	<u>—</u>	<u>—</u>	2[f]	<u>6,310</u>	<b>22,587</b>
<b>Earnings per Common Share</b>						
Basic .....	\$ 3.89	—	—	2[j]	—	<b>3.49</b>
Diluted .....	<u>\$ 3.85</u>	<u>—</u>	<u>—</u>		<u>—</u>	<b>3.45</b>

See accompanying notes

**Fortis Inc.**

**PRO FORMA CONSOLIDATED STATEMENT OF EARNINGS**  
**For The Nine Month Period Ended September 30, 2003**

(in thousands of dollars, except for per share amounts)

	<b>Fortis Inc.</b>	<b>ANCA<sup>(1)</sup></b>	<b>ANCBC</b>	Note	<b>Pro forma adjustments</b>	<b>Total</b>
	\$	\$	\$		\$	\$
<b>Operating Revenues</b> .....	632,456	122,598	118,340		—	<b>873,394</b>
<b>Expenses</b>						
Operating .....	425,652	69,529	79,698		—	<b>574,879</b>
Amortization .....	49,341	16,098	11,045	2[h]	300	<b>76,784</b>
	474,993	85,627	90,743		300	<b>651,663</b>
<b>Net Operating Income</b> .....	157,463	36,971	27,597		(300)	<b>221,731</b>
<b>Finance Charges</b>						
Interest .....	61,630	20,531	12,386	2[d]	10,174	<b>104,721</b>
Dividends on preference shares .....	—	—	—		—	—
	61,630	20,531	12,386		10,174	<b>104,721</b>
<b>Earnings Before Undernoted Items, Income Taxes and Non-Controlling Interest</b> .....	95,833	16,440	15,211		(10,474)	<b>117,010</b>
Goodwill impairment .....	—	80,000	—		—	<b>80,000</b>
<b>Earnings Before Income Taxes and Non-Controlling Interest</b> .....	95,833	(63,560)	15,211		(10,474)	<b>37,010</b>
Income taxes .....	31,993	(2,959)	3,690	2[i]	(3,993)	<b>28,731</b>
<b>Earnings Before Non-Controlling Interest</b> .....	63,840	(60,601)	11,521		(6,481)	<b>8,279</b>
Non-controlling interest .....	2,722	—	—		—	<b>2,722</b>
<b>Earnings</b> .....	61,118	(60,601)	11,521		(6,481)	<b>5,557</b>
Dividends on preference shares .....	2,248	—	—	2[g]	7,350	<b>9,598</b>
<b>Earnings Applicable to Common Shares</b> .....	58,870	(60,601)	11,521		(13,831)	<b>(4,041)</b>
<b>Average Common Shares Outstanding</b> .....	17,291	—	—	2[g]	6,310	<b>23,601</b>
<b>Earnings per common share</b>						
Basic .....	\$ 3.40	—	—	2[j]		<b>\$ (0.17)</b>
Diluted .....	\$ 3.35	—	—			<b>\$ (0.17)</b>

(1) Refer to the ANCA interim financial statements for the period ended September 30, 2003 for explanation of the results.

*See accompanying notes*

**Fortis Inc.**

**NOTES TO PRO FORMA CONSOLIDATED  
FINANCIAL STATEMENTS**

(amounts are expressed in thousands of dollars)  
(Unaudited)

**1. BASIS OF PRESENTATION**

The accompanying *pro forma* consolidated financial statements give effect to the acquisition of all of the issued and outstanding shares in Aquila Networks Canada (Alberta) Ltd. (“ANCA”) and Aquila Networks Canada (British Columbia) Ltd. (“ANCBC”) as described in the short form prospectus dated January 20, 2004, (the “Prospectus”). The accompanying *pro forma* consolidated financial statements have been prepared by management of Fortis Inc. (“Fortis” or the “Corporation”) and are derived from the unaudited and audited consolidated financial statements of Fortis as at and for the nine month period ended September 30, 2003 and for the year ended December 31, 2002, respectively; the unaudited and audited financial statements of ANCA as at and for the nine month period ended September 30, 2003, and for the year ended December 31, 2002, respectively; and the unaudited and audited financial statements of ANCBC as at and for the nine month period ended September 30, 2003 and for the year ended December 31, 2002, respectively.

The accounting policies used in the preparation of these *pro forma* consolidated financial statements are those disclosed in the Corporation’s audited financial statements. Management has determined that no adjustments to ANCA’s and ANCBC’s financial statements are required to comply with the accounting policies used by Fortis in the preparation of its consolidated financial statements.

As is standard with similar transactions in regulated utilities, the purchase price is primarily based upon the regulated assets at the time of closing. Based on the purchase price calculation as detailed in the purchase and sale agreements dated September 15, 2003, the estimated net purchase price of ANCA and ANCBC is \$720,000 (refer to note 2[a]) and is based on management’s estimate of working capital, capital assets and debt levels at April 30, 2004. Under the terms of the purchase and sale agreements, the final purchase price is to be adjusted for changes in working capital, capital assets and debt levels from these estimates.

The *pro forma* consolidated balance sheet and *pro forma* consolidated statements of earnings reflect the acquisition effected September 30, 2003 and January 1, 2002, respectively. The *pro forma* consolidated financial statements are not necessarily indicative of the results that actually would have been achieved if the transactions reflected therein had been completed on the dates indicated or the results which may be obtained in the future. The primary variance relates to:

- The estimated net purchase price of \$720,000, which is based on the expected levels of capital assets, working capital and debt at April 30, 2004, has been applied to the *pro forma* consolidated statements of earnings effective January 1, 2002. Had the purchase price been adjusted to reflect the actual level of working capital, capital assets and debt existing at that time, the net purchase price would have been \$449,000 and the after-tax interest expense and preference share dividends would have decreased by approximately \$11,906 and \$9,133 for the year-ended December 31 2002 and for the nine-month period ended September 30, 2003, respectively.
- The actual purchase price allocation will reflect the fair value, at the purchase date, of the assets acquired and liabilities assumed based upon the acquirer’s evaluation of such assets and liabilities following the closing of the transaction and, accordingly, the final purchase price allocation, as it relates principally to intangible assets, may differ significantly from the preliminary allocation reflected herein.

These *pro forma* consolidated financial statements should be read in conjunction with the description of the transactions described in the Prospectus; the audited and unaudited financial statements of ANCA, including the notes thereto, included in the Prospectus; the unaudited and audited financial statements of ANCBC, including the notes thereto, included in the Prospectus; and the unaudited and audited consolidated financial statements of Fortis including the notes thereto, incorporated by reference in the Prospectus.

**2. PRO FORMA ASSUMPTIONS AND ADJUSTMENTS**

These *pro forma* consolidated financial statements give effect to the completion of the acquisition of ANCA and ANCBC, as if it had occurred on September 30, 2003 in respect of the *pro forma* consolidated balance sheet, and on January 1, 2002 with respect to the *pro forma* consolidated statement of earnings for the year ended December 31, 2002 and for the nine month period ended September 30, 2003. The proposed acquisition has been reflected in the *pro forma* consolidated financial statements using the purchase method. For purposes of the preparation of the *pro forma* consolidated statements of earnings, this transaction is deemed effective on January 1, 2002 using the estimated net purchase price as of April 30, 2004.

**[a] Estimated Net Purchase Price as of April 30, 2004<sup>(1)</sup>**

	\$
Unadjusted purchase price .....	1,360,000
Working capital and other adjustments .....	14,000 <sup>(1)</sup>
Property, plant and equipment adjustment .....	51,000 <sup>(1)</sup>
Estimated acquisition costs (note 2[h]) .....	10,000
Estimated net purchase price, before assumed debt, as of April 30, 2004 .....	1,435,000
Assumed debt of ANCA and ANCBC .....	(715,000) <sup>(1)</sup>
Estimated net purchase price as of April 30, 2004 .....	720,000



**Estimated Net Funding Requirements as of April 30, 2004**

	\$
Estimated Net Purchase Price .....	720,000
Assumed debt of ANCA and ANCBC .....	715,000
Other Costs	
Preferred share issuance costs .....	6,000
Acquisition financing costs .....	4,000
Common share issuance costs .....	14,000
Estimated Net Funding Requirements as of April 30, 2004 .....	<u>1,459,000</u>

**Assumed Financing Structure as of April 30, 2004**

	\$
Assumed debt of ANCA and ANCBC .....	715,000
Common share issuance .....	350,205
Preferred share issuance .....	200,000
Incremental long-term debt issuance .....	193,795
	<u>1,459,000</u>

(1) Adjustments based on estimated financial position of ANCA and ANCBC as of April 30, 2004.

**[b] Allocation of estimated net purchase price**

The estimated net purchase price, which is based on the expected level of capital assets, working capital and debt at April 30, 2004 has been allocated to the fair values of ANCA and ANCBC net assets and liabilities at September 30, 2003, in accordance with the purchase method, as follows:

	<u>ANCA</u>	<u>ANCBC</u>	<u>Total</u>
	\$	\$	\$
Assets acquired:			
Cash and cash equivalents .....	26,341	31,522	57,863
Receivables .....	71,242	30,939	102,181
Material and supplies .....	10,844	4,812	15,656
Other Receivables .....	11,290	3,444	14,734
Regulatory cost deferral .....	<u>30,459</u>	—	<u>30,459</u>
Current assets .....	150,176	70,717	220,893
Other assets .....	—	12,299	12,299
Future income taxes .....	1,914	9,149(i)	11,063
Utility capital assets .....	<u>460,760</u>	<u>440,730</u>	<u>901,490</u>
	<u>612,850</u>	<u>532,895</u>	<u>1,145,745</u>
Liabilities assumed:			
Short-term debt and current portion of long-term debt .....	144,990	60,219	205,209
Accounts payable and accrued charges .....	115,189	56,080	171,269
Other liabilities .....	4,324	—	4,324
Future income taxes .....	—	1,744	1,744
Securitization financing .....	63,957	—	63,957
Long-term debt .....	<u>230,000</u>	<u>248,477(i)</u>	<u>478,477</u>
	<u>558,460</u>	<u>366,520</u>	<u>924,980</u>
<b>Net assets at fair value, September 30, 2003</b> .....	54,390	166,375	220,765
<b>Net purchase price</b> .....			<u>720,000</u>
Goodwill .....			499,235
Goodwill previously recorded by ANCA .....			(189,309)(ii)
<b>Additional goodwill</b> .....			<u>309,926 (iii)</u>

- (i) Fair value of the assumed ANCBC debentures exceed book value by approximately \$24,000. The future tax asset associated with the fair value increment is \$9,149.
- (ii) The goodwill recorded by ANCA was created when Aquila, Inc. purchased the distribution and retail assets of TransAlta Utilities Corporation.
- (iii) The \$720,000 estimated net purchase price, which is based on estimated financial information as of April 30, 2004, has been applied to the net assets as at September 30, 2003. Had the purchase price been calculated based on the working capital, capital asset and debt levels at September 30, 2003, the goodwill would have decreased by approximately \$64,000.

[c] **Goodwill**

The excess of the purchase price over the fair value of net assets acquired from ANCA and ANCBC is not amortized. In accordance with the standards of the Canadian Institute of Chartered Accountants, goodwill is no longer amortized to earnings, instead, will be assessed for impairment at least annually.

[d] **Financing**

The Corporation has entered into a bridge financing agreement with its bankers for up to \$1,400,000. This bridge will be refinanced with the issuance of common shares, preference shares and long-term debt facilities. It is assumed the total anticipated funding requirement of \$1,459,000 will be initially financed by the bridge acquisition facility and the assumed debt will be subsequently refinanced at an average rate of 7.0%.

Additional interest expense of the following has been assumed:

	<u>Nine month period ended September 30, 2003</u>	<u>Year ended December 31, 2002</u>
	\$	\$
Interest on \$193,795 incremental debt at 7.0% .....	10,174	13,566

[e] **Assumed ANCBC Debentures**

ANCBC has debentures outstanding of \$148,250, in various series with due dates ranging from 2009 to 2023. The rates range from 6.75% to 11%, resulting in the fair market value of the debentures exceeding book value by \$24,000, calculated as at December 31, 2002. The future tax asset associated with the fair value increment is \$9,149. This fair value increment is assumed constant and is applied to the September 2003 *pro forma* consolidated balance sheet. The debentures are expected to remain outstanding after the closing of the Acquisition.

[f] **Common share issuance**

To fund a portion of the acquisition purchase price, the Corporation issued 6,310,000 subscription receipts (the "Subscription Receipts") in October 2003 at \$55.50 per Subscription Receipt. The Subscription Receipts are convertible into common shares of the Corporation (the "Common Shares") on closing resulting in estimated gross proceeds of \$350,205 and net proceeds after Common Share issuance costs of \$341,301 (\$14,000 Common Share issuance costs less \$5,096 income taxes).

[g] **Preference share unit issuance**

To fund a portion of the acquisition purchase price, the Corporation plans to issue approximately 8,000,000 first preference units (the "Units") each of which consists of one series D first preference share of the Corporation (a "Series D First Preference Shares") and one series E first preference share purchase warrant of the Corporation (a "Warrant"). Assuming conversion of all Series D First Preference Shares and exercise of all Warrants comprising the Units the gross proceeds will be \$200,000 and the net proceeds after preference share issuance costs will be \$196,287 (\$6,000 issuance costs less \$2,287 income taxes). Dividends are calculated at the issue rate of 4.9%, resulting in total dividends of \$9,800 and \$7,350 for the 12 month period ended December 31, 2002 and the nine month period ended September 30, 2003, respectively.

[h] **Acquisition and financing costs**

It is assumed acquisition costs will approximate \$10,000, and will form part of the investment cost base. Financing costs are assumed to approximate \$4,000 and will be deferred and amortized over 10 years.

[i] **Income taxes**

Income taxes applicable to the *pro forma* adjustments are tax effected at Fortis' average tax rates of 40.12% and 38.12% for the year ended December 31, 2002 and the nine month period ended September 30, 2003, respectively.

[j] **Earnings per share**

The calculation of the *pro forma* earnings per share for the year ended December 31, 2002, and for the nine month period ended September 30, 2003, considers the issuance of 6,310,000 Common Shares as contemplated in the prospectus of Fortis relating to the issuance of Subscription Receipts dated September 29, 2003, as if the issuance had taken place as at January 1, 2002.

**Aquila Networks Canada (Alberta) Ltd.**  
Formerly UtiliCorp Networks Canada (Alberta) Ltd.

Financial Statements  
December 31, 2002 and 2001  
Together with Auditors' Report

## AUDITORS' REPORT

To the Directors of  
**Aquila Networks Canada (Alberta) Ltd.,**

We have audited the balance sheet of **AQUILA NETWORKS CANADA (ALBERTA) LTD.** as at December 31, 2002 and the statements of operations, deficit and cash flows for the year then ended. These 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, 2002 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

The financial statements as at December 31, 2001 and for the year then ended, prior to the restatement of transmission revenues and expenses as described in Note 2, were audited by other auditors who have ceased operations. Those auditors expressed an opinion without reservation on those financial statements in their report dated February 5, 2002. We have audited the restatement of transmission revenues and expenses in the 2001 statement of operations and in our opinion, such restatement, in all material respects, is appropriate and properly applied.

Calgary, Canada  
January 31, 2003

(Signed) *KPMG LLP*  
Chartered Accountants

**Aquila Networks Canada (Alberta) Ltd.**

**BALANCE SHEETS**

**As at December 31**

(All dollar amounts are in thousands)

	<b>2002</b>	<b>2001</b>
	\$	\$
<b>ASSETS</b>		
PROPERTY, PLANT AND EQUIPMENT, net of accumulated amortization (Notes 3 and 12) .....	505,927	496,885
Regulatory tax basis adjustment, net of accumulated amortization (Note 4) .....	(116,766)	(122,583)
	<u>389,161</u>	<u>374,302</u>
REGULATORY COST DEFERRAL (Note 5) .....	12,882	162,260
GOODWILL, net of accumulated amortization (Note 2) .....	269,309	278,032
FUTURE INCOME TAX (Note 13) .....	2,962	—
<b>CURRENT ASSETS</b>		
Accounts receivable (Notes 10, 12 and 15) .....	43,506	64,576
Current portion of regulatory cost deferral (Note 5) .....	116,664	120,368
Supplies .....	10,709	9,821
Regulatory deferred charges .....	1,996	1,268
	<u>172,875</u>	<u>196,033</u>
	<u>847,189</u>	<u>1,010,627</u>
<b>CAPITALIZATION AND LIABILITIES</b>		
<b>CAPITALIZATION (Note 6)</b>		
<b>SHAREHOLDER'S EQUITY</b>		
Share capital .....	347,579	383,579
Deficit .....	(43,279)	(70,550)
Total shareholder's equity .....	<u>304,300</u>	<u>313,029</u>
<b>DEBT</b> .....	<u>230,000</u>	<u>236,940</u>
	<u>534,300</u>	<u>549,969</u>
<b>LIABILITIES</b>		
SECURITIZATION FINANCING (Note 8) .....	25,346	—
OTHER OBLIGATIONS (Note 9) .....	—	90,174
FUTURE INCOME TAX (Note 13) .....	—	45,979
<b>CONTINGENCIES AND COMMITMENTS (Notes 10 and 14)</b>		
<b>CURRENT LIABILITIES</b>		
Accounts payable (Note 12) .....	61,245	64,203
Current portion of debt .....	6,940	58,675
Current portion of securitization financing .....	144,477	—
Short-term debt (Note 7) .....	—	106,970
Current portion of other obligations .....	—	90,174
Income taxes payable .....	74,881	4,483
	<u>287,543</u>	<u>324,505</u>
	<u>847,189</u>	<u>1,010,627</u>

Approved on behalf of the Board:

(Signed) *Fauzia Lalani*

(Signed) *Steve Raniseth*

\_\_\_\_\_  
Director

\_\_\_\_\_  
Director

*The accompanying notes are an integral part of these financial statements.*

**Aquila Networks Canada (Alberta) Ltd.**

**STATEMENTS OF OPERATIONS**

**For the year ended December 31**

(All dollar amounts are in thousands)

	<b>2002</b>	<b>2001</b>
	\$	\$
<b>REVENUES</b>		
Electric rate revenue (Note 10) .....	248,092	243,146
Other (Note 5) .....	<u>20,444</u>	<u>9,966</u>
	<u>268,536</u>	<u>253,112</u>
<b>EXPENSES</b>		
Depreciation and amortization .....	82,578	81,304
Operating labour .....	46,528	48,000
Contracted services (Note 12) .....	24,235	23,274
General operating expenses .....	20,465	18,561
Taxes other than income taxes .....	6,889	6,687
Regulatory deferred charges .....	<u>2,000</u>	<u>—</u>
	<u>182,695</u>	<u>177,826</u>
<b>EARNINGS FROM OPERATIONS</b> .....	85,841	75,286
<b>INTEREST EXPENSE</b> .....	<u>24,924</u>	<u>37,896</u>
<b>INCOME BEFORE INCOME TAXES</b> .....	60,917	37,390
<b>INCOME TAXES</b> (Note 13) .....	<u>33,376</u>	<u>25,242</u>
<b>NET EARNINGS</b> .....	<u><u>27,541</u></u>	<u><u>12,148</u></u>

**CONSOLIDATED STATEMENTS OF DEFICIT**

**For the year ended December 31**

(All dollar amounts are in thousands)

	<b>2002</b>	<b>2001</b>
	\$	\$
<b>DEFICIT, BEGINNING OF YEAR</b> .....	(70,550)	(82,698)
Net earnings .....	27,541	12,148
Dividends .....	<u>270</u>	<u>—</u>
<b>DEFICIT, END OF YEAR</b> .....	<u><u>(43,279)</u></u>	<u><u>(70,550)</u></u>

*The accompanying notes are an integral part of these financial statements.*

**Aquila Networks Canada (Alberta) Ltd.**

**STATEMENTS OF CASH FLOWS**

**For the year ended December 31**

(All dollar amounts are in thousands)

	<b>2002</b>	<b>2001</b>
	\$	\$
<b>OPERATING ACTIVITIES</b>		
Net earnings .....	27,541	12,148
Add items not involving cash		
Depreciation and amortization .....	82,578	81,304
Amortization of deferred charges .....	1,078	2,666
Future income taxes .....	(48,941)	18,189
Collection of regulatory cost deferral .....	<u>153,080</u>	<u>102,906</u>
	215,336	217,213
Change in non-cash working capital related to operating activities .....	<u>100,520</u>	<u>(265,566)</u>
	<u>315,856</u>	<u>(48,353)</u>
<b>INVESTING ACTIVITIES</b>		
Additions to property, plant and equipment .....	(103,538)	(96,399)
Additions to deferred charges .....	(3,935)	—
Change in non-cash working capital related to investing activities .....	—	(20,884)
Purchase price adjustments (Note 1) .....	<u>4,057</u>	<u>—</u>
	<u>(103,416)</u>	<u>(117,283)</u>
<b>FINANCING ACTIVITIES</b>		
Proceeds of note payable to Aquila Networks Canada Finance Limited Partnership .....	—	230,000
Repayment of debt .....	(58,675)	(313,715)
Proceeds from securitization financing .....	255,000	—
Repayments of securitization financing .....	(85,177)	—
Repayment of note payable to Aquila Networks Canada Corp. ....	—	(202,482)
Proceeds (repayment) of other obligations .....	(180,348)	41,256
Proceeds (repayment) of commercial paper .....	(106,000)	106,000
Proceeds (repayment) of line of credit .....	(970)	970
Financing charges .....	—	(3,489)
Issue of common shares, net of redemptions .....	(36,000)	66,000
Dividends .....	(270)	—
Change in non-cash working capital related to financing activities .....	<u>—</u>	<u>(6,016)</u>
	<u>(212,440)</u>	<u>(81,476)</u>
<b>DECREASE IN CASH AND CASH EQUIVALENTS</b> .....	—	(247,112)
<b>CASH AND CASH EQUIVALENTS, beginning of year</b> .....	<u>—</u>	<u>247,112</u>
<b>CASH AND CASH EQUIVALENTS, end of year</b> .....	<u>—</u>	<u>—</u>
Cash flows include the following elements:		
Interest paid .....	24,924	43,912
Income taxes paid .....	11,670	2,815

*The accompanying notes are an integral part of these financial statements.*

## AQUILA NETWORKS CANADA (ALBERTA) LTD.

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

For the year ended December 31, 2002 and 2001

(All tabular dollar amounts are in thousands, unless otherwise noted)

#### 1. ENTITY DEFINITION AND NATURE OF OPERATIONS

Aquila Networks Canada (Alberta) Ltd. ("ANCA" or the "Company") (formerly UtiliCorp Networks Canada (Alberta) Ltd.) was incorporated under the laws of Alberta for the initial purpose of acquiring the distribution and retail operations of TransAlta Utilities Corporation ("TAU"), pursuant to an asset transfer agreement, which had an effective closing date of August 31, 2000. The Company was acquired by an indirect wholly owned subsidiary of Aquila, Inc. ("Aquila"), a U.S. public company, on August 31, 2000. The consideration paid for this acquisition has been recorded in these financial statements using push-down accounting (see Note 6).

Effective January 1, 2001, the Company disposed of its retail operations and related assets and began operating solely as an owner and operator of distribution assets. As a distribution company, ANCA invoices retail energy companies for the distribution and transmission portions of electricity rates. In turn, the Company is invoiced by the transmission administrator for the transmission services.

#### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

##### Regulation

The Company is regulated by the Alberta Energy and Utilities Board ("AEUB"). The AEUB administers acts and regulations covering such matters as tariffs, rates, construction, operations, financing and accounting. The timing of ANCA's recognition of certain assets, liabilities, revenues and expenses as a result of regulation may differ from that otherwise expected using Canadian generally accepted accounting principles for entities not subject to rate regulation.

##### Use of estimates

The preparation of financial statements in accordance with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosures with respect to contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the period. Certain estimates are necessary since the regulatory environment in which the Company operates often requires amounts to be recorded at estimated values until finalization, and adjustments, if any, are determined pursuant to subsequent regulatory decisions or other regulatory proceedings. Due to the inherent uncertainty in making such estimates, actual results reported in future periods could differ materially from those estimated. See also Note 10 for specific commentary regarding revenue estimates.

##### Revenue recognition

As required by the AEUB, revenues are recognized on a billing cycle basis, at AEUB approved rates.

On January 1, 2002, the Company adopted Canadian Institute of Chartered Accountants Emerging Issues Committee Abstract 123. This abstract requires the Company to report revenues and expenses related to transmission services on a net basis. The Company has retroactively adopted the provisions of this abstract, resulting in the netting of prior year transmission service expense and electric rate revenue of \$155.2 million.

##### Property, plant and equipment

Property, plant and equipment are carried at cost including an allowance for funds used during construction. The cost of amortizable assets retired together with removal costs less salvage value is charged to accumulated amortization.

Amortization is provided on a straight-line basis calculated on the investment in amortizable assets in service. Rates are designed to amortize the cost of the assets over their estimated service life. The application of these rates, as approved by the AEUB, for the period ended December 31, 2002 results in an annualized composite amortization rate of 5.66% (2001 — 5.64%).

##### Customers' portion of costs

Certain additions to property, plant and equipment are made with the assistance of non-refundable contributions from customers when the estimated revenue is less than the cost of providing service or where special equipment is needed to supply the customers' specific requirements. Such amounts are recorded as a reduction of property, plant and equipment and are being amortized over the estimated service lives of the related assets by an offset against the provision for amortization.

##### Income taxes

The Company follows the taxes payable method of accounting for income taxes, consistent with the method and timing for determining the income tax component of its rates as regulated by the AEUB, except as described in Note 13. Future income taxes are generally recognized only to the extent they will not be recoverable in future rates charged to customers.

##### Cash and cash equivalents

Cash and cash equivalents are comprised of cash and highly liquid investments with original maturities of 90 days or less.



## Goodwill

Effective January 1, 2002, the Company adopted Canadian Institute of Chartered Accountants Handbook Section 3062 "Goodwill and Other Intangible Assets" and will no longer amortize goodwill. However, goodwill is subject to an impairment test at least annually or upon a significant potential impairment event. Prior to January 1, 2002, goodwill was amortized on a straight-line basis over 40 years. Amortization expense for the year ended December 31, 2001 was \$8.3 million.

As at January 1 and November 30, 2002, a goodwill impairment test was performed and it was determined that there is no impairment of goodwill.

## Employee future benefits

The Company records the costs of employee future benefits as employer contributions are paid. This is consistent with the method required by AEUB regulation for including employee future benefits in rates charged to customers. A measurement date of September 30 is used for the Company's pension plan assets and obligations.

### 3. PROPERTY, PLANT AND EQUIPMENT

The cost and accumulated amortization of property, plant, and equipment has been presented using TAU's historic amounts as they form the basis used to determine amortization for regulatory purposes.

	2002		2001	
	Cost	Accumulated Amortization	Net Book Value	Net Book Value
	\$	\$	\$	\$
Distribution network .....	1,826,907	(1,079,527)	747,380	743,882
Construction in progress .....	10,351	—	10,351	4,320
Customer contributions .....	(426,311)	174,507	(251,804)	(251,317)
	<u>1,410,947</u>	<u>(905,020)</u>	<u>505,927</u>	<u>496,885</u>

During the year ended December 31, 2002, interest of \$nil (2001 — \$0.3 million) was capitalized to construction in progress.

### 4. REGULATORY TAX BASIS ADJUSTMENT

The regulatory tax basis adjustment represents the excess of the deemed tax basis of the Company's property, plant and equipment for regulatory rate making purposes as compared to the Company's tax basis for income tax purposes.

The regulatory tax basis adjustment is being amortized over the estimated service lives of the Company's property, plant and equipment by an offset against the provision for depreciation and amortization. During 2002, depreciation and amortization expense was reduced by \$5.8 million (2001 — \$5.5 million) for the amortization of the regulatory tax basis adjustment.

### 5. REGULATORY COST DEFERRAL

The Electric Utilities Act of Alberta ("EUA") governs the exchange of all electric energy through the interconnected electric system in the Province of Alberta. Pursuant to the EUA, the dispatch and exchange of electric energy and the financial settlement for the exchange of electric energy in Alberta is conducted through the Power Pool of Alberta (the "Power Pool"). The EUA also mandates the use of an independent transmission administrator to administer the transmission of all electric energy through the province. The cost of transmission service is partially tied to the cost of electric energy as determined by the Power Pool.

During 2000, the pool price charged to ANCA and TAU for electric energy exceeded the AEUB approved forecast commodity pool price that was used to set regulated retail electricity rates for the 2000 calendar year. As a result, the Company incurred expenditures related to the purchases of both commodity and transmission services that exceeded the level of revenue received from customers for these costs (the "excess costs"). Excess costs deferred in this manner have been reflected as regulatory cost deferral in these financial statements.

During 2001, the Company was directed by the AEUB to collect its regulatory cost deferral during 2001 to 2003. In addition, as a result of an AEUB decision, the Company is entitled to recover its financing costs related to the regulatory cost deferral, based on a carrying cost recovery rate of 7.90% in 2001 and 6.45% for the period of January 1 to August 15, 2002. Included in 2002 electric rate revenue for the year ended December 31, 2002 is \$3.6 million (December 31, 2001 — \$19.1 million) related to the recovery of regulatory cost deferral financing costs.

In June 2002, the AEUB authorized the Company to enter into a securitization agreement whereby the deferral accounts could be sold to an unrelated financial institution (the "Purchaser"). On August 15, 2002, the Company completed the securitization of its deferral accounts for proceeds of \$255 million. This represented the balance of certain components of the regulatory cost deferral as at July 1, 2002. Under the terms of the agreement, the deferral accounts were sold to a third party for cash proceeds of \$255 million. The Company will continue to service the deferral accounts and accordingly will bill, collect, and between settlement dates, hold rate riders in trust for the purchaser.

Notwithstanding that the Purchaser has acquired all benefits associated with the deferral accounts, the deferral accounts do not meet the accounting definition of a financial asset eligible for sale accounting and accordingly, the transaction has been recorded as a financing in these financial statements.

The net proceeds of the securitization were used to pay amounts due to TAU (Note 9) and redeem common shares in the amount of \$51 million, with the remainder being used to retire commercial paper outstanding and for general corporate purposes.

The regulatory cost deferral is comprised as follows:

	<u>Commodity</u>	<u>Generation Entitlements</u>	<u>Transmission Service</u>	<u>Other</u>	<u>Total</u>
	\$	\$	\$	\$	\$
Balance at December 31, 2001 .....	285,361	44,805	(49,375)	1,837	282,628
Recovered through 2002 riders .....	(168,986)	(26,815)	18,183	—	(177,618)
Net 2002 revision to 2001 balances as a result of 2002					
AEUB decisions .....	2,887	2,166	—	(3,503)	1,550
2002 excess transmission costs .....	—	—	22,986	—	22,986
Balance at December 31, 2002 .....	119,262	20,156	(8,206)	(1,666)	129,546
Less: current portion .....	(106,380)	(20,156)	8,206	1,666	(116,664)
	<u>12,882</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>12,882</u>

Effective January 1, 2001, as a result of disposing of its retail operations, the Company became solely a distribution system owner and is no longer responsible for the purchase of electric energy. Accordingly, no excess commodity costs were incurred in 2001 or 2002. However, the Company continues to defer excess or deficient transmission service costs and expects that the 2001 and 2002 amounts will be refunded in subsequent periods.

Included in other revenue in 2002 is \$10.3 million (2001 — \$nil) related to transmission services expense originally recognized in 2000 but reversed in 2002 due to favorable regulatory decisions.

## 6. CAPITALIZATION

### (a) Share Capital

Authorized — unlimited number of:

Common shares

Class A Common shares

First Preferred non-voting shares, redeemable, cumulative dividend at 10% of the redemption price

Issued — 63 Class A Common shares (710 Class A Common shares in 2001)

	<u>2002</u>	<u>2001</u>
	\$	\$
Common shares .....	138,848	174,848
Contributed surplus .....	208,731	208,731
	<u>347,579</u>	<u>383,579</u>

During 2002 the Company's parent subscribed for an additional 13 Class A Common shares for cash consideration of \$30 million. The Company also redeemed 660 shares for cash consideration of \$66 million. During 2001 the Company issued 1,050 Class A Common shares for cash consideration of \$105 million and subsequently redeemed 390 Class A Common shares for \$39 million.

Contributed surplus relates to the push-down of the purchase price premium paid by the Company's parent on acquisition of TAU's retail and distribution assets.

### (b) Debt

	<u>2002</u>	<u>2001</u>
	\$	\$
Note Payable — Aquila Networks Canada Finance Limited Partnership .....	230,000	230,000
Notes payable to various Rural Electrification Associations .....	6,940	17,415
Term bank facility .....	—	48,200
	236,940	295,615
Current portion .....	(6,940)	(58,675)
	<u>230,000</u>	<u>236,940</u>

The note payable to Aquila Networks Canada Finance Limited Partnership, an affiliated company, bears interest at 8.66%, is unsecured and is due on June 15, 2011.

Notes payable to various Rural Electrification Associations are unsecured and bear interest, determined at January 1 and July 1 of each year, at the greater of the prevailing bank prime interest rate or the five-year bank term deposit rate, and are due on demand. The effective interest rate for the year ended December 31, 2002 was 4.13% (6.88% in 2001).

Included within interest expense is \$22.8 million related to long-term debt.

During the year ended December 31, 2002, the Company recorded interest expense on its note payable to Aquila Networks Canada Finance Limited Partnership of \$19.9 million (2001 — \$10.6 million).

## 7. SHORT-TERM DEBT

	<u>2002</u>	<u>2001</u>
	\$	\$
Commercial paper and credit facility .....	—	106,000
Revolving demand lines of credit .....	<u>—</u>	<u>970</u>
	<u>—</u>	<u>106,970</u>

The Company's commercial paper program provides for maximum borrowing of \$112.5 million. ANCA has arranged a \$112.5 million committed revolving facility which matures June 17, 2003 to support the commercial paper program. To the extent commercial paper has been issued, the amount of the committed revolving facility available is reduced.

The Company has also arranged a \$30 million unsecured revolving demand facility, which is made available by prime loans or Bankers' Acceptances. As at December 31, 2002, \$17.7 million of this facility has been utilized for outstanding letters of credit.

## 8. SECURITIZATION FINANCING

	<u>2002</u>	<u>2001</u>
	\$	\$
Securitization financing .....	169,823	—
Current portion .....	<u>(144,477)</u>	<u>—</u>
	<u>25,346</u>	<u>—</u>

The Company sold certain components of its regulatory cost deferral on August 15, 2002 (Note 5). The transaction has been treated as a financing for accounting purposes, and accordingly, securitization financing represents the cash received from the financial institution less repayments to date. The notional interest rate on the securitization financing is 3.45%.

## 9. OTHER OBLIGATIONS

Amounts due to TAU were unsecured and were payable upon receipt of the proceeds on securitization of the Company's regulatory cost deferral (see Note 5).

## 10. REVENUE MEASUREMENT

### (a) Regulated rates

The regulatory process with respect to final 2002 distribution rates is not complete. The Company has applied for a 8.7% increase in 2002 rates compared to 2001. Effective July 1, 2002 the Company received approval to collect an interim rate rider for the last six months of the year which is equivalent to an annual 6.9% increase over 2001 rates. Revenue has been recognized based on these interim rates. An AEUB ruling on 2002 and 2003 rates is expected in the first half of 2003. The impact of the ruling will be recorded prospectively.

### (b) Hourly electrical load

The Company records regulated transmission and distribution revenues based on regulated tariffs approved by the AEUB and the hourly electrical load delivered to end-use customers connected to the Company's distribution system. Commencing on January 1, 2001, hourly electrical load data is determined by the Company through a metering and load settlement function performed by the Company in its role as a distribution system owner.

The methodology used to determine the hourly electrical load by end-use customers is governed by regulation and includes an initial load determination on a monthly basis, used to issue preliminary invoices to the retailers and certain end-use customers. This preliminary load information is then subject to further adjustment by the Company, and a final negotiated settlement of delivered electrical load with applicable retailers and certain end-use customers, which then forms the basis for a final financial settlement of a specific month's delivered electrical load. At this time, the Company is to prepare final invoices to retailers for distribution and transmission services.

At December 31, 2002, due to industry-wide concerns regarding the accuracy and integrity of the load settlement process in general as adopted throughout the Province of Alberta, the Company was unable to reach a final monthly negotiated financial settlement with any of the retailers or end-use customers for any months in 2001 and 2002. Accordingly, the Company has recognized regulated revenue for 2001 and 2002 based on management's best estimate of the hourly electrical load, which will be finalized in the ongoing monthly negotiated final settlement processes. Subsequent adjustments, if any, may be material to these financial statements.

## 11. EMPLOYEE FUTURE BENEFITS

The Company sponsors a defined contribution plan for the majority of its employees. Certain other long-service employees accrue benefits under a defined benefit pension plan. The Company also provides certain other post-retirement benefits to its retired employees. For regulatory purposes, employee future benefits are recoverable in rates from customers at the time that the Company is required to fund its obligations. Accordingly, expenses for employee future benefits are recognized in these financial statements in accordance with regulatory requirements.

Information with respect to the Company's benefit plans is as follows:

	<u>2002</u>	<u>2001</u>
	\$	\$
Plan assets .....	20,777	25,319
Accrued benefit obligation .....	<u>(10,835)</u>	<u>(11,218)</u>
Plan surplus .....	<u>9,942</u>	<u>14,101</u>

As ordered by the AEUB, the Company is required to use the plan surplus to fund current and future pension and other post-retirement obligations.

## 12. RELATED PARTY TRANSACTIONS

In the normal course of business, the Company transacts with its parent and other related companies under common control. The following transactions were measured at the exchange amount:

	<u>2002</u>	<u>2001</u>
	\$	\$
Included in contracted services are the following amounts charged from related parties:		
Executive management services .....	2,800	5,022
Information technology costs .....	19,565	15,977
Aquila direct charges .....	1,870	2,275
Included in property, plant and equipment:		
Capital project costs .....	12,197	17,039
Included in accounts receivable .....	15,413	5,036
Included in accounts payable .....	19,439	10,195

Except as disclosed elsewhere in these financial statements, the amounts due to and from the Company's parent and other related companies under common control are non-interest bearing, unsecured and due on demand.

## 13. PROVISION FOR INCOME TAXES

The provision for income taxes varies from the amount that would be expected if computed by applying the enacted Canadian federal and provincial statutory income tax rates to the income before income taxes as shown in the following table:

	<u>2002</u>		<u>2001</u>	
	\$	%	\$	%
Income before income taxes .....	<u>60,917</u>	—	<u>37,390</u>	—
Expected provision for income taxes .....	23,940	39.3	15,741	42.1
Adjustments resulting from differences between income for accounting and income tax purposes related to:				
Capital assets .....	9,506	15.6	17,026	45.5
Other expenses .....	(2,439)	(4.0)	(1,893)	(5.0)
Large Corporations Tax .....	667	1.1	2,439	6.5
Future income taxes — tax rate changes and other .....	<u>1,702</u>	<u>2.8</u>	<u>(8,071)</u>	<u>(21.6)</u>
Provision for income taxes .....	<u>33,376</u>	<u>54.8</u>	<u>25,242</u>	<u>67.5</u>
	<u>2002</u>		<u>2001</u>	
Comprised of:				
Future income tax provision .....	(48,941)		17,772	
Current income tax provision .....	<u>82,317</u>		<u>7,470</u>	
	<u>33,376</u>		<u>25,242</u>	

The net future income tax liability is comprised as follows:

	<u>2002</u>	<u>2001</u>
	\$	\$
Future income tax asset:		
Regulatory cost deferral included for tax purposes against regulated taxable income .....	2,962	—
Future income tax liabilities:		
Regulatory cost deferral deducted for tax purposes against regulated taxable income .....	—	(31,979)
Regulatory cost deferral deducted for tax purposes against non-regulated taxable income .....	—	<u>(14,000)</u>
	<u>2,962</u>	<u>(45,979)</u>

In connection with ANCA's 2001 negotiated rate settlement with the AEUB, ANCA included a revenue requirement for current income taxes, notwithstanding that the Company's 2001 current income tax liability was reduced through the application of non-capital loss carryforwards, created as a result of the Company's deduction of its regulatory cost deferral in 2000. However, consistent with its negotiated rate settlement, the Company's revenues for the year ended December 31, 2001 included a component for income taxes, which has been reflected as a corresponding charge to future income tax expense.

As described in Note 2, the Company follows the taxes payable method of accounting for income taxes. Had the company accounted for its regulated operations using the liability method, the Company would have additional future income tax liabilities of approximately \$60 million at December 31, 2002 (\$38 million — 2001).

#### 14. CONTINGENCIES AND COMMITMENTS

##### (a) Operating lease obligations

The Company has contractual obligations in the normal course of business and operating leases for facilities, office premises and equipment. Future minimum annual lease payments, excluding estimated operating costs, are as follows:

	\$
2003 .....	2,999
2004 .....	2,787
2005 .....	2,651
2006 .....	2,620
2007 .....	2,537

##### (b) TAU operating agreements

The Company and TAU have entered into a number of service agreements to ensure operational efficiencies are maintained through coordinated operations. The agreements have minimum expiry terms of twenty years and are subject to extension based on mutually agreeable terms. Costs, net of related revenues, are estimated to be approximately \$3.4 million per year.

##### (c) Legal proceedings

The Company is subject to various legal proceedings and claims that arise in the ordinary course of business operations. The Company believes that the amount of liability, if any, would not have a material effect on the Company's financial position or results of operations.

##### (d) Capital expenditures

As an electric utility, the Company is obligated to provide service to customers within its service territory. The Company has forecast capital expenditures for 2003 of \$120.7 million, which are largely driven by customer requests or are specifically identified large capital projects. The Company will be required to raise additional capital during 2003 to fund its capital expenditures.

#### 15. CREDIT RISK MANAGEMENT

Substantially all of the customer accounts receivable relate to electricity retailers located in the Province of Alberta. One customer comprised 63% of accounts receivable as at December 31, 2002 (57% at December 31, 2001). The Company has obtained a parental guarantee from this customer. Credit risk is mitigated as the Company would apply to recover any bad debt realized on any retailer's account in future rates.

#### 16. FINANCIAL INSTRUMENTS

The Company's financial instruments consist primarily of accounts receivable, accounts payable, notes payable and short-term debt, debt and other obligations. These financial instruments, except for the note payable to Aquila Networks Canada Finance Limited Partnership, have a fair value that approximates their respective carrying values. As at December 31, 2002, the fair market value of this instrument exceeded the book value by \$26.2 million. Fair values for debt are determined using discounted cash flow analysis based on an estimate of the Company's current borrowing rate for each instrument.

**Aquila Networks Canada (Alberta) Ltd.**

Unaudited Interim Financial Statements  
for the nine month period ended September 30, 2003

**Aquila Networks Canada (Alberta) Ltd.**

**BALANCE SHEET**

(All dollar amounts are in thousands)

	<b>September 30, 2003</b>	<b>December 31, 2002</b>
	(Unaudited)	(Audited)
	\$	\$
<b>ASSETS</b>		
PROPERTY, PLANT AND EQUIPMENT, net of accumulated amortization . . . . .	573,367	505,927
Regulatory tax basis adjustment, net of accumulated amortization . . . . .	<b>(112,607)</b>	<b>(116,766)</b>
	<u>460,760</u>	<u>389,161</u>
REGULATORY COST DEFERRAL . . . . .	—	12,882
GOODWILL, net of accumulated amortization (Note 4) . . . . .	<u>189,309</u>	<u>269,309</u>
FUTURE INCOME TAX . . . . .	<u>1,914</u>	<u>2,962</u>
<b>CURRENT ASSETS</b>		
Cash and cash equivalents . . . . .	26,341	—
Funds on deposit (Note 6) . . . . .	36,335	—
Accounts receivable (Note 3) . . . . .	34,907	43,506
Current portion of regulatory cost deferral . . . . .	30,459	116,664
Supplies . . . . .	10,844	10,709
Income taxes receivable . . . . .	3,196	—
Regulatory deferred charges . . . . .	8,094	1,996
	<u>150,176</u>	<u>172,875</u>
	<u>802,159</u>	<u>847,189</u>
<b>CAPITALIZATION AND LIABILITIES</b>		
<b>CAPITALIZATION</b>		
<b>SHAREHOLDER'S EQUITY</b>		
Share capital . . . . .	347,579	347,579
Deficit . . . . .	<b>(103,880)</b>	<b>(43,279)</b>
Total shareholder's equity . . . . .	<u>243,699</u>	<u>304,300</u>
DEBT . . . . .	<u>230,000</u>	<u>230,000</u>
	<u>473,699</u>	<u>534,300</u>
<b>LIABILITIES</b>		
REGULATORY COST DEFERRAL . . . . .	<u>4,324</u>	—
SECURITIZATION FINANCING . . . . .	—	<u>25,346</u>
CONTINGENCIES (Note 7)		
<b>CURRENT LIABILITIES</b>		
Accounts payable and accrued liabilities . . . . .	75,212	61,245
Revenue subject to refund (Note 3) . . . . .	39,977	—
Note payable (Note 5) . . . . .	10,000	—
Current portion of debt . . . . .	—	6,940
Current portion of securitization financing . . . . .	63,957	144,477
Short-term debt (Note 5) . . . . .	134,990	—
Income taxes payable . . . . .	—	74,881
	<u>324,136</u>	<u>287,543</u>
	<u>802,159</u>	<u>847,189</u>

Approved on behalf of the Board:

(Signed) *Fauzia Lalani*

Director

(Signed) *Steve Raniseth*

Director

*The accompanying notes are an integral part of these financial statements.*

**Aquila Networks Canada (Alberta) Ltd.**

**STATEMENTS OF OPERATIONS**

(All dollar amounts are in thousands)

	3 months ended September 30		9 months ended September 30	
	2003	2002	2003	2002
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)
	\$	\$	\$	\$
<b>REVENUES</b>				
Electric rate revenue (Note 3) .....	52,123	49,696	120,450	175,036
Other .....	402	8,222	2,148	12,021
	<b>52,525</b>	<b>57,918</b>	<b>122,598</b>	<b>187,057</b>
<b>EXPENSES</b>				
Depreciation and amortization (Note 3) .....	11,876	16,682	16,098	57,358
Goodwill impairment (Note 4) .....	—	—	80,000	—
Operating labour .....	13,791	13,149	35,816	32,943
Contracted services .....	4,310	5,882	15,192	19,394
General operating expenses .....	4,258	4,619	12,853	16,165
Taxes other than income taxes .....	1,889	1,511	5,668	5,175
Regulatory deferred charges .....	—	1,287	—	(7,720)
	<b>36,124</b>	<b>43,130</b>	<b>165,627</b>	<b>123,315</b>
<b>EARNINGS (LOSS) FROM OPERATIONS</b> .....	<b>16,401</b>	<b>14,788</b>	<b>(43,029)</b>	<b>63,742</b>
<b>INTEREST EXPENSE</b> .....	<b>8,296</b>	<b>5,327</b>	<b>20,531</b>	<b>19,460</b>
<b>INCOME (LOSS) BEFORE INCOME TAXES</b> .....	<b>8,105</b>	<b>9,461</b>	<b>(63,560)</b>	<b>44,282</b>
<b>INCOME TAXES EXPENSE (RECOVERY)</b> .....	<b>2,503</b>	<b>6,314</b>	<b>(2,959)</b>	<b>24,574</b>
<b>NET EARNINGS (LOSS)</b> .....	<b>5,602</b>	<b>3,147</b>	<b>(60,601)</b>	<b>19,708</b>

**CONSOLIDATED STATEMENT OF DEFICIT**

(All dollar amounts are in thousands)

	9 months ended September 30	
	2003	2002
	(Unaudited)	(Unaudited)
	\$	\$
<b>DEFICIT, BEGINNING OF PERIOD</b> .....	<b>(43,279)</b>	<b>(70,550)</b>
Net earnings (loss) .....	<b>(60,601)</b>	<b>19,708</b>
<b>DEFICIT, END OF PERIOD</b> .....	<b>(103,880)</b>	<b>(50,842)</b>

*The accompanying notes are an integral part of these financial statements.*



**Aquila Networks Canada (Alberta) Ltd.**

**STATEMENTS OF CASH FLOWS**

(All dollar amounts are in thousands)

	3 months ended September 30		9 months ended September 30	
	2003	2002	2003	2002
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)
	\$	\$	\$	\$
<b>OPERATING ACTIVITIES</b>				
Net earnings (loss) .....	5,602	3,147	(60,601)	19,708
Add items not involving cash				
Depreciation and amortization .....	11,876	16,682	16,098	57,358
Goodwill impairment .....	—	—	80,000	—
Amortization of deferred charges .....	(2,315)	(170)	(2,078)	94
Future income taxes .....	1,048	(11,557)	1,048	(34,669)
Collection of regulatory cost deferral .....	42,407	56,469	103,411	125,881
	58,618	64,571	137,878	168,372
Change in non-cash working capital related to operating activities .....	(20,155)	56,391	(60,105)	89,178
	38,463	120,962	77,773	257,550
<b>INVESTING ACTIVITIES</b>				
Additions to property, plant and equipment .....	(32,477)	(23,529)	(81,596)	(64,796)
Additions to deferred charges .....	(1,571)	24	(2,020)	(3,370)
Purchase price adjustments .....	—	—	—	1,795
	(34,048)	(23,505)	(83,616)	(66,371)
<b>FINANCING ACTIVITIES</b>				
Proceeds of note payable to Aquila Networks Canada Finance Limited Partnership .....	—	—	10,000	—
Proceeds of short term debt .....	134,990	—	134,990	—
Proceeds from securitization financing .....	—	255,000	—	255,000
Repayments of securitization financing .....	(35,239)	(64,074)	(105,866)	(64,074)
Repayment of debt .....	—	—	(6,940)	(48,200)
Repayment of short term syndicated loan .....	(89,859)	—	—	—
Repayment of other obligations .....	—	(141,356)	—	(180,348)
Repayment of commercial paper .....	—	(112,000)	—	(106,000)
Repayment of line of credit .....	—	(3,994)	—	(970)
Redemption of common shares .....	—	(21,000)	—	(36,000)
	9,892	(87,424)	32,184	(180,592)
<b>INCREASE IN CASH AND CASH EQUIVALENTS ..</b>	<b>14,307</b>	<b>10,033</b>	<b>26,341</b>	<b>10,587</b>
<b>CASH AND CASH EQUIVALENTS, beginning</b> of period .....	<b>12,034</b>	<b>554</b>	<b>—</b>	<b>—</b>
<b>CASH AND CASH EQUIVALENTS, end of period . . .</b>	<b>26,341</b>	<b>10,587</b>	<b>26,341</b>	<b>10,587</b>

*The accompanying notes are an integral part of these financial statements.*

**Aquila Networks Canada (Alberta) Ltd.**

**NOTES TO FINANCIAL STATEMENTS  
For the nine months ended September 30, 2003**

(All tabular dollar amounts are in thousands, unless otherwise noted)

**1. BASIS OF PRESENTATION**

These unaudited interim financial statements have been prepared in accordance with Canadian generally accepted accounting principles for interim financial statements and do not include all of the disclosures normally found in the audited annual financial statements for Aquila Networks Canada (Alberta) Ltd. (“ANCA” or the “Company”). These interim financial statements should be read in conjunction with the Company’s audited financial statements for the year ended December 31, 2002.

These financial statements have been prepared following the same accounting policies and methods as those used in preparing the most recent audited financial statements. The Company is regulated by the Alberta Energy and Utilities Board (“AEUB”). The AEUB administers acts and regulations covering such matters as tariffs, rates, construction, operations, financing and accounting. The timing of ANCA’s recognition of certain assets, liabilities, revenues and expenses as a result of regulation may differ from that otherwise expected using Canadian generally accepted accounting principles for entities not subject to rate regulation.

**2. USE OF ESTIMATES**

The financial statements have been prepared based on nine months of operations ended September 30, 2003. The regulatory environment in which the Company operates often requires amounts to be recorded at estimated values until finalization and adjustment, if any, is determined pursuant to subsequent regulatory decisions or other regulatory proceedings. Due to the inherent uncertainty in making such estimates, actual results reported in future periods could differ materially from those estimated. See also Note 3 for specific commentary regarding revenue estimates.

Interim results will fluctuate due to seasonal demands for electricity and the timing and recognition of regulatory decisions. Consequently, interim results are not necessarily indicative of annual results.

**3. REVENUE MEASUREMENT**

**(a) Regulated rates**

As described in Note 10a of the December 31, 2002 audited financial statements, the Company had been operating on interim distribution rates for 2002 and 2003. On February 28, 2003, the AEUB issued a Decision, the effects of which were reflected in a refiled rate application dated March 28, 2003. On July 4, 2003, the AEUB issued a Decision which established distribution tariff rates for 2002 and 2003, subject to an appeal period ending in the fourth quarter of 2003.

The effects of the February 28, 2003 Decision have been recognized in the 2003 amounts as follows:

	<b>Relating to 2002</b>	<b>Relating to 2003</b>	<b>Total</b>
	\$	\$	\$
Reduction in revenue .....	(40,000)	(27,900)	(67,900)
Reduction in depreciation .....	20,400	18,720	39,120
Reduction in income taxes .....	15,500	9,180	24,680

As directed by the AEUB, the refund to customers is made via revised electricity rates applied to electric load consumed during the period August 1 to December 31, 2003.

Subsequent to September 30, 2003, the appeal period for the July 4, 2003 Decision terminated. Accordingly, in the 4th quarter of 2003, the company will reduce the previously recognized effects of the February 28, 2003 decision for differences totaling \$7.2 million (\$6.2 million after tax) between the original estimates and actual effects.

Included in electric rate revenue for the nine months ended September 30, 2003 is \$5.8 million related to Option “B” revenue collected in 2002, but not recognized until regulatory certainty was attained as a result of the AEUB decision on 2002 and 2003 tariff rates.

**(b) Hourly electrical load**

As described in Note 10b of the December 31, 2002 audited financial statements, the Company continues to recognize regulated revenue for 2001, 2002 and 2003 based on management’s best estimate of the hourly electrical load. The Company is continuing its efforts to reach a final negotiated settlement with its retailers or end-use customers for the electrical load delivered in each of the months from January 2001 to May 2002 inclusive. One retailer has filed a statement of claim which is related, in part, to the settlement of electrical load as described herein (see note 7). Any adjustments will be recorded once signed acceptance is obtained from participants involved in negotiation and these adjustments may be material to these financial statements.

Beginning June 30, 2003 and consistent with a process prescribed by the AEUB, the Company has begun to settle monthly electrical load amounts with its retailers and end-user customers for each month beginning June 2002 to present. As at the date of these financial statements, settlements have been reached for the electrical load delivered in the months of June to September 2002. These settlements resulted in a net increase in revenue of \$0.7 million compared to the revenue amount originally recorded for those months. These

settlement amounts are being recorded on a cash basis as settlement is reached each month. Future adjustments, if any, may be material to these financial statements.

#### **4. GOODWILL**

The Company's goodwill was written down by \$80 million in March 2003. The impairment charge was a result of the AEUB decision on 2002 and 2003 distribution tariff rates, which directed ANCA to decrease depreciation rates creating a reduction in ANCA's annual cash flow (see Note 3a).

#### **5. NOTE PAYABLE AND SHORT TERM DEBT**

On June 18, 2003, Aquila Networks Canada Finance Limited Partnership (ANCFLP) loaned \$10 million to ANCA as a short term demand loan at floating prime rate interest. These proceeds funded working capital requirements in the absence of a bank credit facility.

On July 31, 2003, ANCA received proceeds of a US\$100 million, 364 day unsecured debt facility from a U.S. lender, which is made available by alternate base rate loans (ABR's) or LIBOR loans. The proceeds were used to repay the Company's \$112.5 million short term syndicated loan facility that expired on July 31, and its unsecured revolving demand facility of \$25 million. The new facility bears interest at a variable rate based on prime, Federal funds rate or LIBOR rate, with a minimum rate of 6.75% plus the cost related to withholding tax (effective rate 10.71%). Placement fees of \$2.9 million were incurred and will be expensed over the term of the loan.

#### **6. FINANCIAL INSTRUMENTS**

##### **(a) Forward foreign exchange contracts**

The Company uses forward foreign exchange contracts to reduce its exposure to fluctuations in foreign currency exchange rates on U.S. dollar denominated debt. The contracts oblige the Company to buy U.S. dollars in the future at predetermined exchange rates. At September 30, 2003 the Company had entered into a contract to buy U.S. \$215 million on May 28, 2004 at an exchange rate of 1.4209. ANCA entered into the foreign exchange contract on its own behalf and at the request and on behalf of Aquila Networks Canada Corp. (ANCC). A proportionate amount of the benefit, obligations and liabilities under the foreign exchange contract have been assigned to ANCC based on the following fractions:

ANCA — 100/215  
ANCC — 115/215

Accounts payable included an unrealized loss of \$5.8 million on the Company's share of the contract, which is partially offsets a foreign exchange gain on the debt

##### **(b) Funds on deposit**

Funds on deposit include security as required by the Alberta Electric System Operator ("AESO") for transmission related projects. The scope of these projects is to provide service for new customers in the service territory and/or upgrade load capacity to existing customers. The Transmission Facility owner requires security equivalent to their costs of these upgrades until the project's completion. At September 30, 2003, there was \$30.8 million in funds on deposit either through security deposits made directly to AESO or to a financial institution to support letters of credit in favor of AESO.

Funds on deposit also include \$5.5 million in margin deposits on the forward foreign exchange contracts. Since this margin is posted by Aquila Inc. on behalf of the Canadian subsidiaries, these funds on deposit are offset by an equivalent intercompany liability included in accounts payable.

#### **7. LEGAL STATEMENT OF CLAIM**

In a statement of claim filed on August 18, 2003 in the Court of the Queen's Bench of Alberta, EPCOR Energy Services (Alberta) Inc. is pursuing damages of \$83 million for alleged breaches of (i) contract, (ii) common law duties and (iii) distribution tariff terms and conditions of service, relating to the provision of the Regulated Rate Option to customers. The Company has not to date made a definitive assessment of potential liability with respect to this claim, however management believes that these allegations are without merit. The outcome is not determinable and accordingly no amount has been accrued for this claim in these financial statements.

**UtiliCorp Networks Canada (British Columbia) Ltd.**  
(formerly West Kootenay Power Ltd.)

Consolidated Financial Statements  
December 31, 2001 and 2000  
Together with Auditors' Report

**The attached consolidated financial statements were audited and reported on by Arthur Andersen LLP (“Arthur Andersen”). Fortis Inc. (the “Corporation”) has not obtained the consent of Arthur Andersen to the use of its audit report in respect of these financial statements. Arthur Andersen’s consent was not obtained because on June 3, 2002, Arthur Andersen ceased to practice public accounting. Because Arthur Andersen has not provided this consent, purchasers of first preference units of the Corporation pursuant to the (final) short form prospectus to which these financial statements are annexed will not have the statutory right of action for damages against Arthur Andersen as prescribed by applicable securities legislation with respect to these financial statements. In addition, Arthur Andersen may not have sufficient assets available to satisfy any judgments against it.**

## AUDITORS' REPORT

To the Shareholder of

**UtiliCorp Networks Canada (British Columbia) Ltd.:**

We have audited the consolidated balance sheets of **UTILICORP NETWORKS CANADA (BRITISH COLUMBIA) LTD.** (formerly West Kootenay Power Ltd.) (a British Columbia company) as at December 31, 2001 and 2000 and the consolidated statements of earnings, retained earnings and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2001 and 2000 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles, as described in Note 2. As required by the British Columbia Company Act, we report that, in our opinion, these principles have been applied on a consistent basis.

Calgary, Canada

January 23, 2002, except for Note 5(i)  
which is as of February 1, 2002.

(Signed) *ARTHUR ANDERSEN LLP*  
Chartered Accountants

**UTILICORP NETWORKS CANADA (BRITISH COLUMBIA) LTD.**  
(formerly West Kootenay Power Ltd.)

**CONSOLIDATED BALANCE SHEETS**  
**Years ended December 31, 2001 and 2000**

(All dollar amounts are in thousands unless otherwise noted)

	<b>2001</b>	<b>2000</b>
<b>ASSETS</b>		
PROPERTY, PLANT AND EQUIPMENT (Note 3) .....	\$359,924	\$326,049
DEFERRED CHARGES AND OTHER ASSETS (Note 4) .....	15,689	14,870
<b>CURRENT ASSETS</b>		
Cash .....	—	473
Accounts receivable (Note 9) .....	24,490	17,388
Unbilled revenue .....	6,394	7,396
Inventory .....	682	564
Prepaid Expenses .....	1,267	529
	32,833	26,350
<b>TOTAL ASSETS</b> .....	<b>\$408,446</b>	<b>\$367,269</b>
<b>CAPITALIZATION AND LIABILITIES</b>		
<b>CAPITALIZATION</b> (Note 5)		
<b>SHAREHOLDER'S EQUITY</b>		
Shareholder's equity		
Common shares .....	\$ 61,500	\$ 41,500
Retained earnings .....	96,706	86,773
Total shareholder's equity .....	158,206	128,273
<b>DEBT</b> .....	176,090	177,238
<b>TOTAL CAPITALIZATION</b> .....	334,296	305,511
<b>LIABILITIES</b>		
<b>FUTURE INCOME TAXES</b> .....	6,287	7,801
<b>COMMITMENTS AND CONTINGENCIES</b> (Notes 2 and 8)		
<b>CURRENT LIABILITIES</b>		
Accounts payable and accrued liabilities (Note 9) .....	25,108	13,982
Current portion of debt (Note 5) .....	37,438	35,602
Accrued interest .....	3,239	2,789
Income taxes payable .....	2,078	1,584
	67,863	53,957
<b>TOTAL CAPITALIZATION AND LIABILITIES</b> .....	<b>\$408,446</b>	<b>\$367,269</b>

Approved on behalf of the Board:

(Signed) *Don Bacon*

(Signed) *V. Roy Phillips*

\_\_\_\_\_  
Director

\_\_\_\_\_  
Director

*The accompanying notes are an integral part of these consolidated statements.*

**UTILICORP NETWORKS CANADA (BRITISH COLUMBIA) LTD.**  
(formerly West Kootenay Power Ltd.)

**CONSOLIDATED STATEMENTS OF EARNINGS**

**Years ended December 31, 2001 and 2000**

(All dollar amounts are in thousands unless otherwise noted)

	<b>2001</b>	<b>2000</b>
<b>REVENUE</b>		
Sale of power .....	\$143,332	\$134,765
Other .....	4,585	4,117
	<u>147,917</u>	<u>138,882</u>
<b>EXPENSES</b>		
Power purchases .....	51,051	47,659
Operating and maintenance (Note 9) .....	26,390	26,235
Amortization .....	9,843	9,874
Property and B.C. capital taxes .....	10,342	9,918
Water fees .....	7,327	7,316
Wheeling .....	4,334	3,601
	<u>109,287</u>	<u>104,603</u>
<b>EARNINGS FROM OPERATIONS</b> .....	<u>38,630</u>	<u>34,279</u>
<b>INTEREST EXPENSE</b>		
Secured debentures (Note 5) .....	8,858	8,934
Other debt (Note 5) .....	6,333	6,135
	<u>15,191</u>	<u>15,069</u>
<b>EARNINGS BEFORE INCOME TAXES</b> .....	<u>23,439</u>	<u>19,210</u>
<b>INCOME TAXES</b> (Note 7) .....	6,692	6,715
<b>NET EARNINGS</b> .....	<u>\$ 16,747</u>	<u>\$ 12,495</u>

**CONSOLIDATED STATEMENTS OF RETAINED EARNINGS**

**Years ended December 31, 2001 and 2000**

	<b>2001</b>	<b>2000</b>
<b>RETAINED EARNINGS, BEGINNING OF YEAR</b> .....	\$ 86,773	\$ 81,084
Net earnings .....	16,747	12,495
Dividends .....	6,814	6,806
<b>RETAINED EARNINGS, END OF YEAR</b> .....	<u>\$ 96,706</u>	<u>\$ 86,773</u>

*The accompanying notes are an integral part of these consolidated statements.*

**UTILICORP NETWORKS CANADA (BRITISH COLUMBIA) LTD.**  
**(formerly West Kootenay Power Ltd.)**

**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**Years ended December 31, 2001 and 2000**

(All dollar amounts are in thousands unless otherwise noted)

	<b>2001</b>	<b>2000</b>
<b>OPERATING ACTIVITIES</b>		
Net earnings .....	\$ 16,747	\$ 12,495
Add items not involving cash		
Change in non-cash working capital .....	5,114	(14,246)
Amortization .....	9,843	9,874
Future income taxes .....	(1,514)	(278)
	<u>30,190</u>	<u>7,845</u>
<b>INVESTING ACTIVITIES</b>		
Property, plant and equipment .....	(41,464)	(36,453)
Deferred charges and other non-current assets .....	(3,073)	(650)
	<u>(44,537)</u>	<u>(37,103)</u>
<b>FINANCING ACTIVITIES</b>		
Common shares issued .....	20,000	—
Promissory notes payable .....	—	(15,000)
Term bank loans and demand loan issued .....	1,800	52,090
Debentures and mortgage repaid .....	(1,112)	(1,080)
Dividends .....	(6,814)	(6,806)
	<u>13,874</u>	<u>29,204</u>
<b>DECREASE IN CASH</b> .....	(473)	(54)
<b>CASH, OPENING BALANCE</b> .....	<u>473</u>	<u>527</u>
<b>CASH, CLOSING BALANCE</b> .....	<u>\$ —</u>	<u>\$ 473</u>
<b>SUPPLEMENTAL DISCLOSURE</b>		
<b>INTEREST PAID</b> .....	<u>\$ 15,587</u>	<u>\$ 14,184</u>
<b>INCOME TAXES PAID</b> .....	<u>\$ 7,712</u>	<u>\$ 4,943</u>

*The accompanying notes are an integral part of these consolidated statements.*



**UTILICORP NETWORKS CANADA (BRITISH COLUMBIA) LTD.**  
**(formerly West Kootenay Power Ltd.)**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**Years ended December 31, 2001 and 2002**

(All dollar amounts are in thousands unless otherwise noted)

**1. ENTITY DEFINITION AND NATURE OF OPERATIONS**

UtiliCorp Networks Canada (British Columbia) Ltd. ("UNCBC" or the "Company") (formerly West Kootenay Power Ltd.) was incorporated by an Act of the Legislature of British Columbia. On September 2, 1987 it became a wholly-owned subsidiary of UtiliCorp British Columbia Ltd. ("UCBC") which ultimately is a wholly-owned subsidiary of UtiliCorp United Inc. ("UCU"), a U.S. public company.

On October 22, 2001 the Company changed its name to UtiliCorp Networks Canada (British Columbia) Ltd.

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, Walden Power Partnership ("WPP"), ESI-Power Walden Corporation Ltd. and West Kootenay Power Ltd. (formerly 413569 British Columbia Ltd). All significant inter-company transactions and balances have been eliminated upon consolidation.

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Regulation**

The Company is regulated by the British Columbia Utilities Commission ("BCUC"). The BCUC administers acts and regulations, pursuant to the Utilities Commission Act, covering such matters as tariffs, rates, construction, operations, financing and accounting. The timing of UNCBC's recognition of certain assets, liabilities, revenues and expenses as a result of regulation may differ from that otherwise expected using Canadian generally accepted accounting principles for entities not subject to rate regulation.

**Use of estimates**

The preparation of financial statements in accordance with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the period. Certain estimates are necessary since the regulatory environment in which the Company operates often requires amounts to be recorded at estimated values until finalization and adjustment, if any, is determined pursuant to subsequent regulatory decisions or other regulatory proceedings. Due to the inherent uncertainty in making such estimates, actual results reported in future periods could differ materially from those estimated.

**Revenue recognition**

Revenues are recognized as customers are invoiced on a billing cycle basis. In addition, the Company accrues for unbilled revenue for power consumed by customers before year-end which is not yet billed in order to recognize revenue as determined by the BCUC.

**Property, plant and equipment**

Property, plant and equipment are recorded at cost including an allowance for funds used during construction. The cost of amortizable assets retired together with removal costs less salvage value is charged to accumulated amortization. Gains or losses on disposal are not taken into income unless the disposal is outside the normal course of business or involves a major item of plant.

The Company provides for amortization on a straight-line basis calculated on the investment in amortizable assets in service at the beginning of the year. Rates are designed to amortize the cost of the assets over their estimated service life that on average approximates 46 years. The application of these rates for the year ended December 31, 2001 results in a composite rate of 2.2% (2.1% — 2000).

Beginning in 2000, the BCUC has instructed the Company to utilize a rate stabilization mechanism to ensure annual customer rate increases do not exceed 5%. The BCUC has directed the Company to adjust the prior years' amortization rate of its transmission assets from an average of 35 years to a rate of 50 years on a prospective basis for rate making purposes. The rate stabilization is recorded as a charge to accumulated amortization of Plant and Equipment in the year only to the extent required. A total rate stabilization account of \$32.9 million is available to be used in years beginning in 2000 but is not recorded until utilized.

During 2001, the amortization expense has been reduced by \$3.1 million (\$nil — 2000) of rate stabilization, as approved by the BCUC.

**Customers' portion of costs**

Certain additions to property, plant and equipment are made with the assistance of non-refundable contributions from customers and others when the estimated revenue is less than the cost of providing service or when special equipment is needed to supply the customers' specific requirements. Such amounts are recorded as a reduction of property, plant and equipment and are being amortized over the estimated service lives of the related assets by an offset against the provision for amortization.

**Deferred charges and other assets**

Certain revenues and costs are carried on the consolidated balance sheets and are amortized against earnings as ordered or agreed to by the BCUC. Other deferred costs are carried on the consolidated balance sheets and are amortized against earnings over the expected period of benefit. During the year, amortization of \$2.0 million (\$1.3 million — 2000) was charged against operations.

## Income taxes

The Company follows the taxes payable method of accounting for income taxes on certain regulated earnings as ordered by the BCUC. For non-regulated business, income tax assets and income tax liabilities are recognized, at substantially enacted rates, for differences between the amounts reported for financial statement purposes and their respective tax basis. The effect of a change in income tax rates on future income tax assets and future income tax liabilities is recognized in income in the period that the rate change occurs.

## Employee benefits and post-retirement benefits

The Company and its subsidiaries have a number of defined benefit plans providing pensions to most of its employees. These plans are accounted for using the method recommended by Section 3461 of the CICA Handbook. The Company accrues its obligations under employee benefit plans and the related costs, net of plan assets. The Company has adopted the following policy:

### *Defined pension benefit*

For the purpose of calculating the expected return on plan assets, those assets are valued at fair value. The cost of these pensions is determined by independent actuaries using the projected benefit method prorated on service and management's best estimates of expected plan investment performance, salary escalation, and retirement ages of employees.

Adjustments arising from plan amendments, changes in assumptions and the excess of net actuarial gains or losses over 10% of the greater of the benefit obligation and the fair value of the plan assets are amortized on a straight line basis over the expected average remaining service life of the employees covered by the plans. The average remaining service life of the employees covered by these plans ranges from 13 to 15 years.

### *Post-retirement benefits*

As ordered by the BCUC, the Company accounts for post-retirement benefits as employer contributions are paid.

## Prior year amounts

Certain prior year amounts have been reclassified to conform with current year presentation.

## 3. PROPERTY, PLANT AND EQUIPMENT

	<u>Cost</u>	<u>Accumulated Amortization</u>	<u>Net Book Value</u>	
			<u>2001</u>	<u>2000</u>
Generation . . . . .	\$102,254	\$ 17,831	\$ 84,423	\$ 78,090
Substations . . . . .	90,606	31,577	59,029	55,503
Transmission . . . . .	85,852	17,481	68,371	56,759
Distribution . . . . .	152,783	52,151	100,632	90,441
General . . . . .	68,674	21,205	47,469	45,256
Total . . . . .	<u>\$500,169</u>	<u>\$140,245</u>	<u>\$359,924</u>	<u>\$326,049</u>

## 4. DEFERRED CHARGES AND OTHER ASSETS

	<u>Net Value</u>	
	<u>2001</u>	<u>2000</u>
Energy management costs . . . . .	\$ 5,296	\$ 5,854
Energy management loans . . . . .	1,810	187
Prepaid pension costs . . . . .	6,611	5,818
Other . . . . .	1,249	1,737
Debt issue costs . . . . .	993	1,085
Incentive sharing adjustment . . . . .	(270)	189
	<u>\$15,689</u>	<u>\$14,870</u>

## 5. CAPITALIZATION

### (i) SHARE CAPITAL

#### AUTHORIZED

500,000,000 (750,000 — 2000) Common shares, with a par value of \$100 each

500,000,000 (2,000,000 — 2000) Preferred shares, with a par value of \$25 each, issuable in series

	<u>2001</u>	<u>2000</u>
ISSUED		
615,000 (415,000 — 2000) Common shares . . . . .	\$61,500	\$41,500

Subsequent to year end, the Company issued 150,000 common shares for cash consideration of \$15 million.

(ii) DEBT

	<u>2001</u>	<u>2000</u>
Secured		
Series E 11% due December 1, 2009 .....	\$ 9,000	\$ 9,750
Series F 9.65% due October 16, 2012 .....	15,000	15,000
Series G 8.8% due August 28, 2023 .....	25,000	25,000
Series H 8.77% due February 1, 2016 .....	25,000	25,000
Series I 7.81% due December 1, 2021 .....	25,000	25,000
WPP mortgage 9.44% due October 31, 2013 .....	<u>8,238</u>	<u>8,600</u>
	107,238	108,350
Promissory note payable .....	50,000	50,000
Term bank loans and demand loan, interest at prime .....	<u>56,290</u>	<u>54,490</u>
	213,528	212,840
Current portion of debt .....	<u>(37,438)</u>	<u>(35,602)</u>
	<u>\$176,090</u>	<u>\$177,238</u>

The secured debentures are collateralized by a fixed and floating first charge on the assets of the Company and are guaranteed by UCU. The trust deed provides for sinking fund payments of \$750,000 per year for Series E debentures.

The promissory note payable to UtiliCorp Canada Finance Limited Partnership ("UCFLP"), an entity under common control, is unsecured, bears interest at 8.66% (6.95% — 2000) and is due June 15, 2011. During the year, the Company recorded interest expense of \$3.9 million on the UCFLP promissory note.

The term bank and demand loans are unsecured, guaranteed by UCU, and drawn under line of credit facilities which provide for maximum borrowings of \$60 million. A total of \$40 million of these facilities are repayable on demand of which \$36.3 million was outstanding at December 31, 2001. The remaining portion of \$20 million is due May 30, 2007.

As at December 31, 2001 the fair market value of the debt exceeded the book value by \$13.1 million (\$7.8 million — 2000).

Principal payments required within the next five years and thereafter are as follows:

	<u>Sinking Fund Requirement</u>	<u>Demand Loan and Maturing Issues of Debt</u>
2002 .....	750	36,688
2003 .....	750	436
2004 .....	750	480
2005 .....	750	527
2006 .....	750	579
Thereafter .....	2,250	168,818

6. PENSIONS AND OTHER POST RETIREMENT BENEFITS

The Company has several defined benefit pension plans, which cover most employees. Pension plan assets at December 31, 2001 had a market value of \$58.5 million (\$62.8 million — 2000). The value of accrued pension benefits, based on an independent valuation of the plans using management's best estimate of assumptions, was \$66.7 million (\$65.7 million — 2000) at December 31, 2001 including an allowance for the effect of future pay increases, where applicable. Experience gains and losses and amounts arising as a result of changes in assumptions and plan amendments are deferred and amortized to operations over the expected average remaining service life of the employee groups.

The expense for the Company's pension benefits is as follows:

	<u>2001</u>	<u>2000</u>
Employer current service cost .....	\$ 941	\$ 1,305
Interest cost .....	4,389	4,323
Expected return on plan assets .....	(4,776)	(4,161)
Amortization:		
Net transition obligations .....	976	1,020
Prior service cost .....	<u>123</u>	<u>56</u>
Total net benefit plan expense .....	<u>\$ 1,653</u>	<u>\$ 2,543</u>

Information about the Company's defined benefit plans is as follows:

<b>Accrued benefit obligation —</b>		
Balance, beginning of year .....	\$ 65,749	\$ 60,951
Current service cost .....	2,298	2,596
Interest cost .....	4,389	4,323
Benefits paid .....	(4,288)	(3,260)
Prior service cost .....	2,002	—
Actuarial losses (gains) .....	(1,303)	1,139
Transfers .....	<u>(2,187)</u>	<u>—</u>
Balance, end of year .....	<u>\$ 66,660</u>	<u>\$ 65,749</u>
<b>Plan assets —</b>		
Balance, beginning of year .....	\$ 62,847	\$ 51,412
Actual return on plan assets .....	(1,560)	10,230
Employer contributions .....	2,216	3,174
Member contributions .....	1,412	1,291
Benefits paid .....	(4,288)	(3,260)
Transfers .....	<u>(2,114)</u>	<u>—</u>
Fair value, end of year .....	<u>\$ 58,513</u>	<u>\$ 62,847</u>
Funded status .....	\$ (8,147)	\$ (2,902)
Contributions receivable .....	1,635	1,446
Unamortized net actuarial gain .....	(710)	(6,158)
Unamortized transitional obligation .....	10,869	12,349
Unamortized prior service cost .....	<u>2,964</u>	<u>1,083</u>
Accrued benefit asset .....	<u>\$ 6,611</u>	<u>\$ 5,818</u>

Included in the above accrued benefit obligation and fair value of plan assets at year-end are the following amounts in respect of plans that are not fully funded:

	<u>2001</u>	<u>2000</u>
Accrued benefit obligation .....	\$36,119	\$32,822
Fair value of plan assets .....	<u>27,869</u>	<u>26,823</u>
Funded status — plan deficit .....	<u>\$ 8,250</u>	<u>\$ 5,999</u>

The significant actuarial assumptions, adopted in measuring the Company's accrued benefit obligations, are as follows:

	<u>2001</u>	<u>2000</u>
Discount rate .....	7.0%	7.0%
Expected long-term rate of return on plan assets .....	8.0%	8.0%
Rate of compensation increase .....	3.5%	3.5%
Estimated remaining service life .....	13.5 years	13.6 years

## 7. INCOME TAXES

The provision for income taxes varies from the amount that would be expected if computed by applying the Canadian federal and provincial statutory income tax rates to the earnings before income taxes as shown in the following table:

	<u>2001</u>		<u>2000</u>	
		%		%
Earnings before income taxes .....	\$23,439		\$19,210	
Expected provision for income taxes .....	\$10,271	43.8	\$ 8,668	45.1
Adjustments in income taxes resulting from items capitalized for accounting but expensed for income tax purposes —				
Operating expenses .....	(1,074)	(4.6)	(1,120)	(5.8)
Allowance for funds used during construction .....	(371)	(1.6)	(266)	(1.4)
Other temporary differences .....	(1,644)	(7.0)	(811)	(4.2)
Large Corporation Tax .....	775	3.3	615	3.2
Changes in income tax rates .....	(1,500)	(6.4)	—	—
Other .....	235	1.0	(371)	(1.9)
Income tax expense .....	<u>\$ 6,692</u>	<u>28.5</u>	<u>\$ 6,715</u>	<u>35.0</u>

The future income tax liability is comprised as following:

	<u>2001</u>	<u>2000</u>
Net book value of non-regulated plant and equipment in excess of tax basis .....	<u>\$6,287</u>	<u>\$7,801</u>

## 8. COMMITMENTS

### (i) Capital Projects

Capital utility expenditures for 2002 are planned to total approximately \$89.6 million consisting of \$67.6 million for transmission system upgrading, \$5.1 million for generation system upgrading, \$1.9 million for customer extensions and upgrading, and \$15.0 million for other utility plant.

### (ii) Brilliant Power Purchase Contract

On May 3, 1996 an Order was granted by the BCUC approving a 60-year power purchase contract for the output of the Brilliant hydro-electric plant located near Castlegar, B.C. The Brilliant plant is owned by the Columbia Basin Power Corporation ("CBPC"), a joint venture between the Columbia Power Corporation and the Columbia Basin Trust. The Company operates and maintains the Brilliant plant for the CBPC in return for a management fee.

The contract requires fixed monthly payments based on specified take-or-pay amounts of energy. The contract includes a market related price adjustment after 30 years of the 60-year term. The Company has recorded the contract as an operating lease with minimum payments required over the next five years as follows:

	<u>Amount</u>
2002 .....	\$23,972
2003 .....	29,579
2004 .....	31,375
2005 .....	32,721
2006 .....	32,746

### (iii) Firm Power Purchase Contracts

The Company has a long-term, minimum-payment, firm power purchase contract with B.C. Hydro. The contract includes a take-or-pay provision based on a five-year rolling nomination of capacity requirements. The Company also has a short-term, firm power purchase contract with Aquila Canada Corporation, a company under common control, covering 50 to 100 MW at various intervals throughout 2002, with a take-or-pay clause based on specified amounts of energy.

Minimum payments required over the next five years are as follows:

	<u>Amount</u>
2002 .....	\$13,869
2003 .....	5,823
2004 .....	5,293
2005 .....	5,293
2006 .....	5,293

(iv) *Office Lease*

Under a sale-leaseback agreement, on September 29, 1993 the Company began leasing its Trail, B.C. office building for a term of 30 years. The terms of the agreement require future minimum aggregate lease payments of \$25 million and grant the Company repurchase options at year 20 and year 30 of the lease term. As directed by the BCUC, minimum payments required over the next five years are as follows:

	<u>Amount</u>
2002.....	\$310
2003.....	310
2004.....	600
2005.....	600
2006.....	600

(v) *Legal Proceedings*

The Company is subject to various legal proceedings and claims that arise in the ordinary course of business operations. The Company believes that the amount of liability, if any, from these actions would not have a material effect on the Company's financial position or results of operations.

## 9. RELATED PARTY TRANSACTIONS

In addition to transactions and balances disclosed elsewhere, in the normal course of business, the Company transacts with its parent and other related companies under common control. The following transactions were measured at the exchange amount.

At December 31, 2001, the amounts due to and from the Company's parent and other related companies under common control are non-interest bearing, unsecured and due on demand.

	<u>2001</u>	<u>2000</u>
Included in accounts receivable.....	\$7,401	\$1,518
Included in accounts payable.....	\$4,534	\$1,839

Other related transactions included in power purchase expense is the sale of excess power to Aquila Canada Corp. for \$6.1 million (\$nil — 2000). Included in operating and maintenance expenses are executive and management services from UtiliCorp Networks Canada Ltd. of \$1.7 million (\$nil — 2000). Costs of \$0.3 million (\$0.2 million — 2000) were charged to the Company by UCU for services obtained as requested and are included in operating and maintenance expenses.

## 10. FINANCIAL INSTRUMENTS

The Company uses forward foreign currency contracts to reduce its exposure to fluctuations in the U.S. dollar to Canadian dollar exchange rates. The contracts are normally for terms of up to twelve months and are used as hedges of the Company's net U.S. dollar denominated power purchase contracts. Gains and losses arising on these financial instruments are offset against the gains and losses arising on the maturity of the underlying transactions.

At December 31, 2001, the Company has forward foreign currency contracts to sell U.S.\$1.6 million between January 22, 2002 and March 20, 2002 at rates between \$0.6327 and \$0.6326. Had these contracts been settled on December 31, 2001, an additional profit of \$20 thousand would have been recognized.

The Company's other financial instruments consist primarily of accounts receivable, unbilled revenue, accounts payable and accrued liabilities, and debt. These financial instruments have a fair value, which approximates carrying value, unless otherwise disclosed.

**Aquila Networks Canada (British Columbia) Ltd.**  
Formerly UtiliCorp Networks Canada (British Columbia) Ltd.

Consolidated Financial Statements  
December 31, 2002 and 2001  
Together with Auditors' Report

## AUDITORS' REPORT

To the Directors of

**Aquila Networks Canada (British Columbia) Ltd.:**

We have audited the consolidated balance sheet of **AQUILA NETWORKS CANADA (BRITISH COLUMBIA) LTD.** as at December 31, 2002 and the consolidated statements of earnings, retained earnings and cash flows for the year then ended. These 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 consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2002 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles. As required by the British Columbia Company Act, we report that, in our opinion, these principles have been applied on a consistent basis.

The consolidated financial statements as at December 31, 2001 and for the year then ended were audited by other auditors who have ceased operations. Those auditors expressed an opinion without reservation on those financial statements in their report dated January 23, 2002 (except for Note 5(i) which was dated as of February 1, 2002).

Calgary, Canada  
February 19, 2003

(Signed) *KPMG LLP*  
Chartered Accountants



**Aquila Networks Canada (British Columbia) Ltd.**

**CONSOLIDATED BALANCE SHEETS**

**As at December 31**

(All dollar amounts are in thousands)

	<b>2002</b>	<b>2001</b>
	\$	\$
<b>ASSETS</b>		
PROPERTY, PLANT AND EQUIPMENT (Note 3) .....	416,015	359,924
DEFERRED CHARGES AND OTHER ASSETS (Note 4) .....	13,024	15,689
<b>CURRENT ASSETS</b>		
Cash .....	41	—
Accounts receivable (Note 9) .....	14,795	24,490
Unbilled revenue .....	12,882	6,394
Income taxes receivable .....	3,685	—
Inventory .....	428	682
Prepaid expenses .....	688	1,267
	<u>32,519</u>	<u>32,833</u>
	<u>461,558</u>	<u>408,446</u>
 <b>CAPITALIZATION AND LIABILITIES</b>		
<b>CAPITALIZATION (Note 5)</b>		
<b>SHAREHOLDER'S EQUITY</b>		
Common shares .....	76,500	61,500
Retained earnings .....	<u>93,205</u>	<u>96,706</u>
Total shareholder's equity .....	169,705	158,206
<b>DEBT</b> .....	<u>224,917</u>	<u>176,090</u>
	394,622	334,296
 <b>LIABILITIES</b>		
<b>FUTURE INCOME TAXES (Note 7)</b> .....	<u>1,807</u>	<u>6,287</u>
<b>COMMITMENTS (Note 8)</b>		
<b>CURRENT LIABILITIES</b>		
Accounts payable and accrued liabilities (Note 9) .....	39,237	25,108
Current portion of debt (Note 5) .....	21,962	37,438
Accrued interest .....	3,930	3,239
Income taxes payable .....	<u>—</u>	<u>2,078</u>
	<u>65,129</u>	<u>67,863</u>
	<u>461,558</u>	<u>408,446</u>

Approved on behalf of the Board:

(Signed) *V. Roy Phillips*

\_\_\_\_\_  
Director

(Signed) *Fauzia Lalani*

\_\_\_\_\_  
Director

*The accompanying notes are an integral part of these consolidated statements.*

**Aquila Networks Canada (British Columbia) Ltd.**

**CONSOLIDATED STATEMENTS OF EARNINGS**

**For the year ended December 31**

(All dollar amounts are in thousands)

	<b>2002</b>	<b>2001</b>
	\$	\$
<b>REVENUE</b>		
Sale of power .....	149,902	143,332
Other .....	<u>4,092</u>	<u>4,585</u>
	<u>153,994</u>	<u>147,917</u>
<b>EXPENSES</b>		
Power purchases .....	52,154	51,051
Operating and maintenance (Note 9) .....	35,670	26,390
Amortization (Note 10) .....	24,685	9,843
Property and B.C. capital taxes .....	9,877	10,342
Water fees .....	7,270	7,327
Wheeling .....	<u>4,101</u>	<u>4,334</u>
	<u>133,757</u>	<u>109,287</u>
<b>EARNINGS FROM OPERATIONS</b> .....	20,237	38,630
<b>INTEREST EXPENSE</b>		
Secured debentures (Note 5) .....	10,283	8,858
Other debt (Note 5) .....	6,509	7,179
Allowance for funds used during construction .....	<u>(2,451)</u>	<u>(846)</u>
	<u>14,341</u>	<u>15,191</u>
<b>EARNINGS BEFORE INCOME TAXES</b> .....	5,896	23,439
<b>INCOME TAX (RECOVERY) EXPENSE</b> (Notes 7 and 10) .....	<u>(242)</u>	<u>6,692</u>
<b>NET EARNINGS</b> .....	<u>6,138</u>	<u>16,747</u>

**CONSOLIDATED STATEMENTS OF RETAINED EARNINGS**

**For the year ended December 31**

(All dollar amounts are in thousands)

	<b>2002</b>	<b>2001</b>
	\$	\$
<b>RETAINED EARNINGS, BEGINNING OF YEAR</b> .....	96,706	86,773
Net earnings .....	6,138	16,747
Dividends .....	<u>9,639</u>	<u>6,814</u>
<b>RETAINED EARNINGS, END OF YEAR</b> .....	<u>93,205</u>	<u>96,706</u>

*The accompanying notes are an integral part of these consolidated statements.*

**Aquila Networks Canada (British Columbia) Ltd.**

**CONSOLIDATED STATEMENTS OF CASH FLOWS**

**For the year ended December 31**

(All dollar amounts are in thousands)

	<b>2002</b>	<b>2001</b>
	\$	\$
<b>OPERATING ACTIVITIES</b>		
Net earnings .....	6,138	16,747
Add items not involving cash		
Amortization .....	24,685	9,843
Future income taxes .....	(4,481)	(1,514)
Change in deferred charges related to operating activities .....	994	(793)
Change in non-cash working capital .....	13,098	5,114
	<u>40,434</u>	<u>29,397</u>
<b>INVESTING ACTIVITIES</b>		
Property, plant and equipment .....	(78,759)	(41,464)
Change in deferred charges related to investing activities .....	(22)	(2,280)
	<u>(78,781)</u>	<u>(43,744)</u>
<b>FINANCING ACTIVITIES</b>		
Common shares issued .....	15,000	20,000
Term bank loans and demand loan issued (repaid) .....	(15,476)	1,800
Debentures issued .....	50,000	—
Debentures and mortgage repaid .....	(1,173)	(1,112)
Dividends .....	(9,639)	(6,814)
Change in deferred charges related to financing activities .....	(324)	—
	<u>38,388</u>	<u>13,874</u>
<b>INCREASE (DECREASE) IN CASH</b> .....	41	(473)
<b>CASH, OPENING BALANCE</b> .....	<u>—</u>	<u>473</u>
<b>CASH, CLOSING BALANCE</b> .....	<u>41</u>	<u>—</u>
<b>CASH FLOWS INCLUDE THE FOLLOWING ELEMENTS:</b>		
Interest paid .....	16,249	15,587
Income taxes paid .....	9,407	7,712

*The accompanying notes are an integral part of these consolidated statements.*

## **Aquila Networks Canada (British Columbia) Ltd.**

### **NOTES TO CONSOLIDATED FINANCIAL STATEMENTS For the year ended December 31, 2002 and 2001**

(All tabular dollar amounts are in thousands, unless otherwise noted)

#### **1. ENTITY DEFINITION AND NATURE OF OPERATIONS**

Aquila Networks Canada (British Columbia) Ltd. ("ANCBC" or the "Company") (formerly UtiliCorp Networks Canada (British Columbia) Ltd.) was incorporated by an Act of the Legislature of British Columbia. On September 2, 1987 it became a wholly-owned subsidiary of Aquila Networks British Columbia Ltd. ("ANBC") which ultimately is a wholly-owned subsidiary of Aquila, Inc., a U.S. public company.

On May 31, 2002 the Company changed its name to Aquila Networks Canada (British Columbia) Ltd.

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, Walden Power Partnership ("WPP"), ESI-Power Walden Corporation Ltd. and West Kootenay Power Ltd. All significant inter-company transactions and balances have been eliminated upon consolidation.

#### **2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

##### **Regulation**

The Company is regulated by the British Columbia Utilities Commission ("BCUC"). The BCUC administers acts and regulations, pursuant to the Utilities Commission Act, covering such matters as tariffs, rates, construction, operations, financing and accounting. The timing of ANCBC's recognition of certain assets, liabilities, revenues and expenses as a result of regulation may differ from that otherwise expected using Canadian generally accepted accounting principles for entities not subject to rate regulation.

##### **Use of estimates**

The preparation of financial statements in accordance with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the period. Certain estimates are necessary since the regulatory environment in which the Company operates often requires amounts to be recorded at estimated values until finalization and adjustment, if any, is determined pursuant to subsequent regulatory decisions or other regulatory proceedings. Due to the inherent uncertainty in making such estimates, actual results reported in future periods could differ materially from those estimated.

##### **Revenue recognition**

Revenues are recognized as customers are invoiced on a billing cycle basis. In addition, the Company accrues for unbilled revenue for power consumed by customers before year-end in order to recognize revenue as determined by the BCUC.

##### **Cash and cash equivalents**

Cash and cash equivalents are comprised of highly liquid investments with original maturities of 90 days or less.

##### **Property, plant and equipment**

Property, plant and equipment are recorded at cost including an allowance for funds used during construction. The cost of amortizable assets retired together with removal costs less salvage value is charged to accumulated amortization. Gains or losses on disposal are not taken into income unless the disposal is outside the normal course of business or involves a major item of plant.

The Company provides for amortization on a straight-line basis calculated on the investment in amortizable assets in service at the beginning of the year. The application of these rates for the year ended December 31, 2002 results in a composite rate of 2.5% (2.2% — 2001).

Beginning in 2000, the BCUC has instructed the Company to utilize a rate stabilization mechanism to ensure annual customer rate increases do not exceed 5%. The BCUC has directed the Company to adjust the amortization rate of its transmission assets from an average of 35 years to a rate of 50 years on a prospective basis for rate making purposes. The rate stabilization is recorded as a charge to accumulated amortization of plant and equipment in the year only to the extent required. A total remaining notional rate stabilization account of \$29.8 million is available to be used in future years, but is not recorded until utilized.

During 2002, the amortization expense has been reduced by \$nil (\$3.1 million — 2001) of rate stabilization, as approved by the BCUC.

##### **Customers' portion of costs**

Certain additions to property, plant and equipment are made with the assistance of non-refundable contributions from customers and others when the estimated revenue is less than the cost of providing service or when special equipment is needed to supply the customers' specific requirements. Such amounts are recorded as a reduction of property, plant and equipment and are being amortized over the estimated service lives of the related assets by an offset against the provision for amortization.

##### **Deferred charges and other assets**

Certain revenues and costs are carried on the consolidated balance sheets and are amortized against earnings as ordered or agreed to by the BCUC. Other deferred costs are carried on the consolidated balance sheets and are amortized against earnings over the expected period of benefit. During the year, amortization of \$2.0 million (\$2.0 million — 2001) was charged against operations.

## Income taxes

The Company follows the taxes payable method of accounting for income taxes on certain regulated earnings as ordered by the BCUC. For non-regulated business, income tax assets and income tax liabilities are recognized, at substantially enacted rates, for differences between the amounts reported for financial statement purposes and their respective tax bases. The effect of a change in income tax rates on future income tax assets and future income tax liabilities is recognized in income in the period that the rate change occurs.

## Employee benefits and post-retirement benefits

The Company and its subsidiaries have a number of defined benefit plans providing pensions to most of their employees. These plans are accounted for using the method recommended by Section 3461 of the CICA Handbook. The Company accrues its obligations under employee benefit plans and the related costs, net of plan assets. The Company has adopted the following policies:

### *Defined pension benefit*

For the purpose of calculating the expected return on plan assets, those assets are valued at fair value. The cost of these pensions is determined by independent actuaries using the projected benefit method prorated on service and management's best estimates of expected plan investment performance, salary escalation, and retirement ages of employees.

Adjustments arising from plan amendments, changes in assumptions and the excess of net actuarial gains or losses over 10% of the greater of the benefit obligation and the fair value of the plan assets are amortized on a straight line basis over the expected average remaining service life of the employees covered by the plans. The average remaining service life of the employees covered by these plans ranges from 13 to 15 years. The Company uses a measurement date of September 30th for all of its plans.

The Company undertook a workforce reorganization during the year. In conjunction with this reorganization, approximately 40% of the active members of one of the Company's pension plans terminated employment. Management considers this workforce reduction to be a curtailment under pension accounting standards, and the curtailment would normally result in a charge to net income in 2002 of \$0.9 million. However, approval has been received from the BCUC to continue to record pension expense as if the curtailment did not occur. Accordingly, no expense relating to the curtailment is recorded in these financial statements.

### *Post-retirement benefits*

As ordered by the BCUC, the Company accounts for post-retirement benefits as employer contributions are paid.

## 3. PROPERTY, PLANT AND EQUIPMENT

	<u>Cost</u>	<u>Accumulated Amortization</u>	<u>Net Book Value</u>	
			<u>2002</u>	<u>2001</u>
Generation .....	\$103,646	\$ 30,666	\$ 72,980	\$ 84,423
Substations .....	91,589	32,897	58,692	59,029
Transmission .....	134,151	18,869	115,282	68,371
Distribution .....	178,145	55,697	122,448	100,632
General .....	69,189	22,576	46,613	47,469
Total .....	<u>\$576,720</u>	<u>\$160,705</u>	<u>\$416,015</u>	<u>\$359,924</u>

## 4. DEFERRED CHARGES AND OTHER ASSETS

	<u>2002</u>	<u>2001</u>
Energy management costs, net of tax of \$3.1 million (2001 — \$3.6 million) .....	\$ 4,909	\$ 5,296
Energy management loans .....	1,213	1,810
Prepaid pension costs .....	6,775	6,611
Other .....	539	1,249
Debt issue costs .....	1,264	993
Incentive sharing adjustment .....	(1,676)	(270)
	<u>\$13,024</u>	<u>\$15,689</u>

## 5. CAPITALIZATION

### (i) SHARE CAPITAL

#### AUTHORIZED

500,000,000 Common shares, with a par value of \$100 each

500,000,000 Preferred shares, with a par value of \$25 each, issuable in series

#### ISSUED

	<u>2002</u>	<u>2001</u>
765,000 Common shares (615,000 — 2001) .....	\$76,500	\$61,500

(ii) **DEBT**

	<u>2002</u>	<u>2001</u>
Secured		
Series E 11% due December 1, 2009 .....	\$ 8,250	\$ 9,000
Series F 9.65% due October 16, 2012 .....	15,000	15,000
Series G 8.8% due August 28, 2023 .....	25,000	25,000
Series H 8.77% due February 1, 2016 .....	25,000	25,000
Series I 7.81% due December 1, 2021 .....	25,000	25,000
Series J 6.75% due July 31, 2009 .....	50,000	—
WPP mortgage 9.44% due October 31, 2013 .....	7,840	8,238
	<u>156,090</u>	<u>107,238</u>
Promissory note payable .....	50,000	50,000
Term bank and demand loans .....	40,789	56,290
	<u>246,879</u>	<u>213,528</u>
Current portion of debt .....	<u>(21,962)</u>	<u>(37,438)</u>
	<u>\$224,917</u>	<u>\$176,090</u>

The secured debentures are collateralized by a fixed and floating first charge on the assets of the Company and are guaranteed by Aquila, Inc. The trust deed provides for sinking fund payments of \$750,000 per year for Series E debentures.

The promissory note payable to Aquila Networks Canada Finance Limited Partnership (“ANCFLP”), an entity under common control, is unsecured, bears interest at 8.66% and is due June 15, 2011. During the year, the Company recorded interest expense of \$4.3 million (\$3.9 million — 2001) on the ANCFLP promissory note.

The term bank and demand loans are unsecured and drawn under line of credit facilities which provide for maximum borrowings of \$50 million. A total of \$30 million of these facilities are repayable on demand of which \$20.8 million was outstanding at December 31, 2002. The demand facility bears interest at prime. The remaining outstanding balance of \$20 million is due May 29, 2005, is guaranteed by Aquila Inc., and is drawn by way of bankers acceptances.

As at December 31, 2002 the fair market value of the debt exceeded the book value by \$24.0 million (\$13.1 million — 2001).

Included within interest expense is \$13.6 million related to long-term debt.

Principal payments required within the next five years and thereafter are as follows:

	<u>Sinking Fund Requirement</u>	<u>Demand Loan and Maturing Issues of Debt</u>
2003 .....	750	21,212
2004 .....	750	474
2005 .....	750	20,521
2006 .....	750	572
2007 .....	750	629
Thereafter .....	1,500	198,221

**6. PENSIONS AND OTHER POST RETIREMENT BENEFITS**

The Company has several defined benefit pension plans, which cover most employees. The expense for the Company’s pension benefits is as follows:

	<u>2002</u>	<u>2001</u>
Employer current service cost .....	\$ 965	\$ 941
Interest cost .....	4,674	4,389
Expected return on plan assets .....	(4,460)	(4,776)
Amortization:		
Net transition obligations .....	980	976
Prior service cost .....	252	123
Total net benefit plan expense .....	<u>\$ 2,411</u>	<u>\$ 1,653</u>

Information about the Company's defined benefit plans is as follows:

	<u>2002</u>	<u>2001</u>
<b>Accrued benefit obligation-</b>		
Balance, beginning of year	\$ 66,660	\$65,749
Current service cost	2,273	2,298
Interest cost	4,674	4,389
Benefits paid	(3,506)	(4,288)
Prior service cost	—	2,002
Actuarial losses (gains)	5,086	(1,303)
Transfers	(583)	(2,187)
Balance, end of year	<u>\$ 74,604</u>	<u>\$66,660</u>
<b>Plan assets-</b>		
Balance, beginning of year	\$ 58,513	\$62,847
Actual return on plan assets	(371)	(1,560)
Employer contributions	3,498	2,216
Member contributions	1,671	1,412
Benefits paid	(3,506)	(4,288)
Transfers and non-investment expenses	(986)	(2,114)
Fair value, end of year	<u>\$ 58,819</u>	<u>\$58,513</u>
Funded status	\$(15,785)	\$(8,147)
Contributions receivable	239	1,635
Unamortized net actuarial gain	9,720	(710)
Unamortized transitional obligation	9,888	10,869
Unamortized prior service cost	2,713	2,964
Accrued benefit asset	<u>\$ 6,775</u>	<u>\$ 6,611</u>

Included in the above accrued benefit obligation and fair value of plan assets at year-end are the following amounts in respect of plans that are not fully funded:

	<u>2002</u>	<u>2001</u>
Accrued benefit obligation	\$74,604	\$36,119
Fair value of plan assets	<u>58,819</u>	<u>27,869</u>
Funded status — plan deficit	<u>\$15,785</u>	<u>\$ 8,250</u>

The significant actuarial assumptions, adopted in measuring the Company's accrued benefit obligations, are as follows:

	<u>2002</u>	<u>2001</u>
Discount rate	6.5%	7.0%
Expected long-term rate of return on plan assets	7.5%	8.0%
Rate of compensation increase	3.5%	3.5%
Estimated remaining service life	13.5 years	13.5 years

## 7. INCOME TAXES

The provision for income taxes varies from the amount that would be expected if computed by applying the Canadian federal and provincial statutory income tax rates to the earnings before income taxes as shown in the following table:

	<u>2002</u>		<u>2001</u>	
	\$	%	\$	%
Earnings before income taxes	5,896	—	23,439	—
Expected provision for income taxes	2,288	38.8	10,271	43.8
Adjustments in income taxes resulting from items capitalized for accounting but expensed for income tax purposes —				
Operating expenses	(844)	(14.3)	(1,074)	(4.6)
Allowance for funds used during construction	(951)	(16.0)	(371)	(1.6)
Other temporary differences	(1,224)	(20.8)	(1,644)	(7.0)
Large Corporation Tax	905	15.3	775	3.3
Changes in income tax rates	—	—	(1,500)	(6.4)
Other	(416)	(7.1)	235	1.0
Income tax (recovery) expense	<u>(242)</u>	<u>(4.1)</u>	<u>6,692</u>	<u>28.5</u>

Income tax (recovery) expense is comprised of:

	<u>2002</u>	<u>2001</u>
Future income tax recovery .....	\$ (4,481)	\$ (1,500)
Current income tax expense .....	4,239	8,192
	<u>\$ (242)</u>	<u>\$ 6,692</u>

The future income tax liability is comprised as follows:

	<u>2002</u>	<u>2001</u>
Net book value of non-regulated plant and equipment in excess of tax basis .....	\$1,807	\$6,287

As described in Note 2, the Company follows the taxes payable method of accounting for income taxes for regulated operations. Had the Company accounted for its regulated operations using the liability method, the Company would have additional future income tax liabilities of approximately \$36.5 million at December 31, 2002 (\$36.5 million — 2001).

## 8. COMMITMENTS

### (i) *Brilliant Power Purchase Contract*

On May 3, 1996 an Order was granted by the BCUC approving a 60-year power purchase contract for the output of the Brilliant hydro-electric plant located near Castlegar, B.C. The Brilliant plant is owned by the Columbia Basin Power Corporation (“CBPC”), a joint venture between the Columbia Power Corporation and the Columbia Basin Trust. ANCBC operates and maintains the Brilliant plant for the CBPC in return for a management fee.

The contract requires fixed monthly payments based on specified natural flow take-or-pay amounts of energy. The contract includes a market related price adjustment after 30 years of the 60-year term. The Company is accounting for the contract as an operating lease as directed by the BCUC, with minimum payments required over the next five years as follows:

	<u>Amount</u>
2003 .....	\$31,682
2004 .....	31,977
2005 .....	32,617
2006 .....	33,269
2007 .....	33,935

### (ii) *Firm Power Purchase Contracts*

The Company has a long-term, minimum-payment, firm power purchase contract with B.C. Hydro. The contract includes a take-or-pay provision based on a five-year rolling nomination of capacity requirements.

Minimum payments required over the next five years are as follows:

	<u>Amount</u>
2003 .....	\$7,103
2004 .....	5,388
2005 .....	5,496
2006 .....	5,606
2007 .....	5,718

### (iii) *Office Lease*

Under a sale-leaseback agreement, on September 29, 1993 the Company began leasing its Trail, B.C. office building for a term of 30 years. The terms of the agreement require future minimum aggregate lease payments of \$25 million and grant the Company repurchase options at year 20 and year 30 of the lease term. The Company is accounting for the lease as an operating lease, as directed by the BCUC. Minimum payments required over the next five years are as follows:

	<u>Amount</u>
2003 .....	\$310
2004 .....	600
2005 .....	600
2006 .....	600
2007 .....	600

### (iv) *Legal Proceedings*

The Company is subject to various legal proceedings and claims that arise in the ordinary course of business operations. The Company believes that the amount of liability, if any, from these actions would not have a material effect on the Company’s financial position or results of operations.



(v) *Capital Expenditures*

As an electric utility, the Company is obligated to provide service to customers within its service territory. The Company has forecast capital expenditures of \$62.8 million for 2003, which are largely driven by customer requests or are large capital projects specifically approved by the BCUC. The Company will be required to raise additional capital during 2003 to fund its capital expenditures.

**9. RELATED PARTY TRANSACTIONS**

In addition to transactions and balances disclosed elsewhere, in the normal course of business, the Company transacts with its parent and other related companies under common control. The following transactions were measured at the exchange amount.

At December 31, 2002, the amounts due to and from the Company's parent and other related companies under common control are non-interest bearing, unsecured and due on demand.

	<u>2002</u>	<u>2001</u>
Included in accounts receivable . . . . .	\$ 2,957	\$7,401
Included in accounts payable . . . . .	\$16,364	\$8,335
Capital project costs included in Property, Plant & Equipment . . . . .	\$ 8,098	\$5,007

Included in power purchase expense is the sale of excess power to Aquila Canada Corp. for \$0.1 million (\$6.1 million — 2001). Included in operating and maintenance expenses are executive and management services from Aquila Networks Canada Ltd. of \$1.1 million (\$1.7 million — 2001). Costs of \$0.3 million (\$0.3 million — 2001) were charged to the Company by Aquila, Inc. for services obtained as requested and are included in operating and maintenance expenses.

**10. ASSET IMPAIRMENT CHARGE**

Included in amortization expense for 2002 is a charge of \$10.0 million to reflect an impairment in the carrying value of the Walden power plant ('Walden'). Income tax expense includes a related future income tax recovery of \$4.4 million.

**11. FINANCIAL INSTRUMENTS**

The Company's financial instruments consist primarily of accounts receivable, accounts payable, and debt. These financial instruments, except for debt (Note 5), have a fair value that approximates their respective carrying values. Fair values for debt are determined using discounted cash flow analysis based on an estimate of the Company's current borrowing rate for each instrument.

**12. SUBSEQUENT EVENT**

In February 2003, the BCUC approved a 4.3% rate increase for 2003 and an extension of the terms of the performance-based regulation regime under which the Company currently operates.

**Aquila Networks Canada (British Columbia) Ltd.**

Unaudited Interim Consolidated Financial Statements  
for the nine month period ended September 30, 2003

**Aquila Networks Canada (British Columbia) Ltd.**

**CONSOLIDATED BALANCE SHEET**

(All dollar amounts are in thousands)

	<b>September 30, 2003</b>	<b>December 31, 2002</b>
	(Unaudited)	(Audited)
	\$	\$
<b>ASSETS</b>		
PROPERTY, PLANT AND EQUIPMENT (Note 4) .....	<b>440,730</b>	416,015
DEFERRED CHARGES AND OTHER ASSETS .....	<b>12,299</b>	13,024
<b>CURRENT ASSETS</b>		
Cash and cash equivalents .....	<b>31,522</b>	41
Accounts receivable .....	<b>22,819</b>	14,795
Unbilled revenue .....	<b>8,120</b>	12,882
Income taxes receivable .....	<b>3,444</b>	3,685
Inventory .....	<b>435</b>	428
Prepaid expenses .....	<b>4,377</b>	688
	<u><b>70,717</b></u>	<u>32,519</u>
	<u><b>523,746</b></u>	<u>461,558</u>
<b>CAPITALIZATION AND LIABILITIES</b>		
<b>CAPITALIZATION</b>		
<b>SHAREHOLDER'S EQUITY</b>		
Common shares .....	<b>76,500</b>	76,500
Retained earnings .....	<b>104,726</b>	93,205
Total shareholder's equity .....	<b>181,226</b>	169,705
DEBT (Note 5) .....	<b>224,477</b>	224,917
TOTAL CAPITALIZATION .....	<b>405,703</b>	394,622
<b>LIABILITIES</b>		
FUTURE INCOME TAXES .....	<b>1,744</b>	1,807
<b>CURRENT LIABILITIES</b>		
Accounts payable and accrued liabilities .....	<b>51,337</b>	39,237
Current debt (Note 5) .....	<b>60,219</b>	21,962
Accrued interest .....	<b>4,743</b>	3,930
	<u><b>116,299</b></u>	<u>65,129</u>
	<u><b>523,746</b></u>	<u>461,558</u>

Approved on behalf of the Board:

\_\_\_\_\_  
(Signed) *Fauzia Lalani*

Director

\_\_\_\_\_  
(Signed) *James M. Greene*

Director

*The accompanying notes are an integral part of these interim financial statements.*

**Aquila Networks Canada (British Columbia) Ltd.**

**CONSOLIDATED STATEMENTS OF EARNINGS**

(All dollar amounts are in thousands)

	3 Months Ended September 30		9 Months Ended September 30	
	2003	2002	2003	2002
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)
	\$	\$	\$	\$
<b>REVENUE</b>				
Sale of power .....	36,621	35,929	117,153	113,182
Other .....	<u>(295)</u>	<u>(301)</u>	<u>1,187</u>	<u>2,273</u>
	<b>36,326</b>	<b>35,628</b>	<b>118,340</b>	<b>115,455</b>
<b>EXPENSES</b>				
Power purchases .....	13,531	12,865	42,839	39,437
Operating and maintenance .....	5,400	6,866	20,766	20,074
Amortization .....	3,837	3,568	11,045	10,697
Property and B.C. capital taxes .....	2,393	2,105	7,179	7,397
Water fees .....	2,013	1,818	6,086	5,452
Wheeling .....	<u>1,019</u>	<u>1,019</u>	<u>2,828</u>	<u>3,125</u>
	<b>28,193</b>	<b>28,241</b>	<b>90,743</b>	<b>86,182</b>
<b>EARNINGS FROM OPERATIONS</b> .....	<b>8,133</b>	<b>7,387</b>	<b>27,597</b>	<b>29,273</b>
<b>INTEREST EXPENSE</b>				
Secured debentures .....	3,019	3,056	9,076	7,832
Other debt .....	2,437	1,506	6,223	4,395
Allowance for funds used during construction .....	<u>(446)</u>	<u>(641)</u>	<u>(2,913)</u>	<u>(1,575)</u>
	<b>5,010</b>	<b>3,921</b>	<b>12,386</b>	<b>10,652</b>
<b>EARNINGS BEFORE INCOME TAXES</b> .....	<b>3,123</b>	<b>3,466</b>	<b>15,211</b>	<b>18,621</b>
<b>INCOME TAXES</b> .....	<b>516</b>	<b>1,065</b>	<b>3,690</b>	<b>6,329</b>
<b>NET EARNINGS</b> .....	<b><u>2,607</u></b>	<b><u>2,401</u></b>	<b><u>11,521</u></b>	<b><u>12,292</u></b>

**CONSOLIDATED STATEMENT OF RETAINED EARNINGS**

(All dollar amounts are in thousands)

	9 months ended September 30	
	2003	2002
	(Unaudited)	(Unaudited)
	\$	\$
<b>RETAINED EARNINGS, BEGINNING OF PERIOD</b> .....	<b>93,205</b>	96,706
Net earnings .....	<b>11,521</b>	12,292
Dividends .....	<u>—</u>	<u>(7,229)</u>
<b>RETAINED EARNINGS, END OF PERIOD</b> .....	<b><u>104,726</u></b>	<b><u>101,769</u></b>

*The accompanying notes are an integral part of these interim financial statements.*

**Aquila Networks Canada (British Columbia) Ltd.**

**CONSOLIDATED STATEMENTS OF CASH FLOWS**

(All dollar amounts are in thousands)

	3 Months Ended September 30		9 Months Ended September 30	
	2003	2002	2003	2002
	(Unaudited) \$	(Unaudited) \$	(Unaudited) \$	(Unaudited) \$
<b>OPERATING ACTIVITIES</b>				
Net earnings .....	2,607	2,401	11,521	12,292
Add items not involving cash:				
Amortization .....	3,837	3,560	11,045	10,689
Future income taxes .....	(21)	(18)	(63)	(60)
Deferred charges and other non-current assets .....	3,690	1,007	2,815	2,219
Change in non-cash working capital .....	22,548	(4,314)	4,889	5,268
	<b>32,661</b>	2,636	<b>30,207</b>	30,408
<b>INVESTING ACTIVITIES</b>				
Property, plant and equipment .....	(16,258)	(22,976)	(33,975)	(44,693)
Deferred charges and other non-current assets .....	(1,198)	1,844	(2,259)	(345)
	<b>(17,456)</b>	(21,132)	<b>(36,234)</b>	(45,038)
<b>FINANCING ACTIVITIES</b>				
Common shares issued .....	—	—	—	15,000
Debentures issued .....	—	50,000	—	50,000
Term bank loans and demand loan repaid .....	(20,860)	(27,590)	(20,860)	(41,490)
Demand loans issued to affiliates .....	37,356	—	59,000	—
Mortgage repaid .....	(75)	(874)	(323)	(1,068)
Dividends .....	—	(2,410)	—	(7,229)
Deferred charges and other non-current assets .....	(299)	(287)	(309)	(240)
	<b>16,122</b>	18,839	<b>37,508</b>	14,973
<b>INCREASE IN CASH AND CASH EQUIVALENTS .....</b>	<b>31,327</b>	343	<b>31,481</b>	343
<b>CASH AND CASH EQUIVALENTS, OPENING BALANCE ..</b>	<b>195</b>	—	<b>41</b>	—
<b>CASH AND CASH EQUIVALENTS, CLOSING BALANCE ..</b>	<b>31,522</b>	343	<b>31,522</b>	343

*The accompanying notes are an integral part of these interim financial statements.*

## Aquila Networks Canada (British Columbia) Ltd.

### NOTES TO INTERIM FINANCIAL STATEMENTS

**For the nine months ended September 30, 2003**

(All tabular dollar amounts are in thousands, unless otherwise noted)

#### 1. BASIS OF PRESENTATION

These interim financial statements have been prepared in accordance with Canadian generally accepted accounting principles for interim financial statements and do not include all of the disclosures normally found in the annual financial statements for Aquila Networks Canada (British Columbia) Ltd. ("ANCBC" or the "Company"). These interim financial statements should be read in conjunction with the Company's audited financial statements for the year ended December 31, 2002.

These financial statements have been prepared following the same accounting policies and methods as those used in preparing the most recent annual financial statements. The Company is regulated by the British Columbia Utilities Commission ("BCUC"). The BCUC administers acts and regulations, pursuant to the Utilities Commission Act, covering such matters as tariffs, rates, construction, operations, financing and accounting. The timing of ANCBC's recognition of certain assets, liabilities, revenues and expenses as a result of regulation may differ from that otherwise expected using Canadian generally accepted accounting principles for entities not subject to rate regulation.

#### 2. USE OF ESTIMATES

The preparation of financial statements in accordance with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the period. Certain estimates are necessary since the regulatory environment in which the Company operates often requires amounts to be recorded at estimated values until finalization and adjustment, if any, is determined pursuant to subsequent regulatory decisions or other regulatory proceedings. Due to the inherent uncertainty in making such estimates, actual results reported in future periods could differ materially from those estimated. Interim financial statements necessarily employ a greater use of estimates than the annual financial statements.

#### 3. SEASONAL NATURE OF OPERATION

Interim results will fluctuate due to the seasonal demands for electricity, the movements of electricity prices and the timing and recognition of regulatory decisions. Consequently, interim results are not necessarily indicative of annual results.

#### 4. PROPERTY, PLANT AND EQUIPMENT

	<u>Cost</u>	<u>Accumulated Amortization</u>	<u>Net Book Value 2003</u>	<u>2002</u>
Generation .....	\$100,289	\$ 33,124	\$ 67,165	\$ 68,837
Substations .....	93,887	33,246	60,641	54,724
Transmission .....	76,704	21,377	55,327	56,518
Distribution .....	180,452	54,218	126,234	116,395
General .....	66,364	25,535	40,829	42,767
Construction work in progress .....	90,534	—	90,534	76,774
Total .....	<u>\$608,230</u>	<u>\$167,500</u>	<u>\$440,730</u>	<u>\$416,015</u>

#### 5. DEBT

	<u>2003</u>	<u>2002</u>
Secured		
Series E 11% due December 1, 2009 .....	\$ 8,250	\$ 8,250
Series F 9.65% due October 16, 2012 .....	15,000	15,000
Series G 8.8% due August 28, 2023 .....	25,000	25,000
Series H 8.77% due February 1, 2016 .....	25,000	25,000
Series I 7.81% due December 1, 2021 .....	25,000	25,000
Series J 6.75% due July 31, 2009 .....	50,000	50,000
WPP mortgage 9.44% due October 31, 2013 .....	7,517	7,840
	<u>155,767</u>	<u>156,090</u>
Promissory note payable .....	50,000	50,000
Bank term and demand loans .....	19,929	40,789
Other demand loans .....	59,000	—
	<u>284,696</u>	<u>246,879</u>
Current portion of debt .....	(60,219)	(21,962)
	<u>\$224,477</u>	<u>\$224,917</u>

The secured debentures are collateralized by a fixed and floating first charge on the assets of the Company and are guaranteed by Aquila, Inc. The trust deed provides for sinking fund payments of \$750,000 per year for Series E debentures.

The promissory note payable to Aquila Networks Canada Finance Limited Partnership ("ANCFLP"), an entity under common control, is unsecured, bears interest at 8.66% and is due June 15, 2011. During the period, the Company recorded interest expense of \$3.2 million (\$3.2 million — 2002) on the ANCFLP promissory note.

The bank term loans are unsecured and drawn under line of credit facilities with a Canadian chartered bank that provide for maximum borrowings of \$20 million. The outstanding balance of \$20 million is due May 29, 2005, is guaranteed by Aquila Inc., and is drawn by way of bankers acceptances, that bear an average interest rate of 4.75% at September 30, 2003.

Other demand loans consist of a \$29 million unsecured demand loan payable to ANCFLP bearing interest at prime, and a \$30 million 364 day unsecured debt facility from Aquila Networks Canada Corp. ("ANCC") which bears interest at 12.75%.

## **6. INCOME TAXES**

Interim period income tax expense is calculated by applying to the interim period's pre-tax income an effective income tax rate of 16.5%. This effective tax rate was used in the quarter to achieve an effective income tax rate for the nine month period ended September 30, 2003 equal to the estimated average annual effective income tax rate of 24.3%. The estimated average annual income tax rate reflects tax rate structure expected to be applicable to the full year's earnings.

## **7. SUBSEQUENT EVENT**

Subsequent to September 30, 2003, the Company received an assessment for provincial sales tax of \$1.7 million. The assessment relates to various transactions including the procurement of material and equipment for capital and operating expenditures and the billing of revenue to certain customers.

The Company has not determined its position on the assessment and accordingly no amount has been accrued for this assessment in these financial statements.

## **8. RECLASSIFICATIONS**

Certain items in the prior period have been reclassified to be consistent with the current period's presentation.

**CERTIFICATE OF FORTIS INC.**

Dated January 20, 2004

This short form prospectus, together with the documents and information incorporated herein by reference, constitutes full, true and plain disclosure of all material facts relating to the securities offered by this prospectus as required under securities legislation of all of the provinces of Canada. For the purpose of the Province of Québec, this simplified prospectus, as supplemented by the permanent information record, contains no misrepresentation likely to affect the value or the market price of the securities to be distributed.

(Signed) *H. Stanley Marshall*  
President and  
Chief Executive Officer

(Signed) *Barry V. Perry*  
Vice-President, Finance and  
Chief Financial Officer

On behalf of the Board of Directors

(Signed) *Angus A. Bruneau*  
Director

(Signed) *Bruce Chafe*  
Director



**CERTIFICATE OF THE UNDERWRITERS**

Dated January 20, 2004

To the best of our knowledge, information and belief, this short form prospectus, together with the documents and information incorporated herein by reference, constitutes full, true and plain disclosure of all material facts relating to the securities offered by this prospectus as required under securities legislation of all of the provinces of Canada. For the purpose of the Province of Québec, this simplified prospectus, to our knowledge, as supplemented by the permanent information record, contains no misrepresentation likely to affect the value or the market price of the securities to be distributed.

**SCOTIA CAPITAL INC.**

by: (Signed) *Donald A. Carmichael*

**BMO NESBITT  
BURNS INC.**

by: (Signed)  
*James A. Tower*

**CIBC WORLD  
MARKETS INC.**

by: (Signed)  
*David H. Williams*

**NATIONAL BANK  
FINANCIAL INC.**

by: (Signed)  
*William Wasson*

**RBC DOMINION  
SECURITIES INC.**

by: (Signed)  
*David Dal Bello*

**TD SECURITIES INC.**

by: (Signed) *James Gillis*

**BEACON SECURITIES LIMITED**

by: (Signed) *Lonsdale W. Holland*

**EXHIBIT A  
FIRST PREFERENCE UNIT  
CONVERSION AND EXERCISE NOTICE AND DECLARATION**

To: FORTIS INC.  
And to: COMPUTERSHARE TRUST COMPANY OF CANADA

The undersigned holder of the first preference units of Fortis Inc. (the "Corporation") (the "Units") represented by the attached Unit certificate hereby converts \_\_\_\_\_ cumulative redeemable convertible first preference shares, series D of the Corporation (the "Series D First Preference Shares") and exercises an equal number of cumulative redeemable convertible first preference shares, series E purchase warrants of the Corporation (the "Warrants") in accordance with the provisions attaching to the Series D First Preference Shares and in accordance with the indenture dated as of the closing date of the offering of the Units among the Corporation and Computershare Trust Company of Canada ("Computershare"), as trustee for the holders of the warrants (the "Warrant Indenture") and the attached Unit certificate, and tenders herewith, by certified cheque, bank draft or money order, payable to or to the order of the Corporation an amount equal to \$18.75 multiplied by the number of Warrants so exercised.

If less than all of the Warrants and Series D First Preference Shares represented by the attached Unit certificate are to be exercised and converted, as the case may be, a replacement Unit certificate shall be issued to the holder representing the Units in respect of which the Warrants and related Series D First Preference Shares have not been so exercised or converted, as the case may be.

The undersigned holder of the Units certifies that (i) it is not a U.S. Person or located in the United States, (ii) the conversion of the Series D First Preference Shares and exercise of the Warrants forming such Units is not being made by any person in the United States or for the account or benefit of any U.S. Person or any person in the United States, and (iii) at the time the decision to convert the Series D First Preference Shares and exercise the Warrants forming such Units was made, the person making such decision was outside of the United States. Terms used in this paragraph have the meanings given to them by Regulation S promulgated under the United States *Securities Act of 1933*, as amended.

The undersigned hereby irrevocably directs that the cumulative redeemable convertible first preference shares, series E of the Corporation (the "Series E First Preference Shares") that are issuable upon such conversion and exercise be registered and delivered as follows:

Name(s) in Full	Address(es) (See Note 1 below)	Number of Series E First Preference Shares

(Please print full name in which share certificates are to be registered. If any Series E First Preference Shares are to be registered in the name of a person other than the holder, the holder must pay to Computershare all exigible transfer taxes or other government charges.)

DATED this \_\_\_\_\_ day of \_\_\_\_\_, 2004.

<i>(Signature guarantee — See Note 2 below for when required)</i>	Signature of holder
_____	Name of holder

Please check if the share certificates representing the Series E First Preference Shares are to be delivered at the office where the attached Unit certificate is surrendered, failing which such certificates will be mailed. Certificates will be delivered or mailed as soon as practicable after the due surrender of the attached Unit certificate as aforesaid.

**Notes**

1. The Corporation reserves the right, pursuant to the Warrant Indenture, not to issue Series E First Preference Shares to any holder (acting on its own behalf or on behalf of any book-entry holder) where the Corporation or Computershare has reason to believe is a resident of, any jurisdiction outside Canada to the extent that such issue would require the Corporation to take any action to comply with the securities, banking or analogous laws of such jurisdiction.
2. No signature guarantee is required on this conversion and exercise notice and declaration if: (i) this conversion and exercise notice and declaration is signed by the holder of the Unit certificate(s) delivered therewith, unless such holder has indicated that share certificates representing Series E First Preference Shares are to be issued to a person other than the holder; or (ii) such share certificates representing Series E First Preference Shares are delivered for the account of a Canadian chartered bank, a trust company in Canada, a commercial bank or trust company having an office or correspondent in Canada or a member firm of a recognized stock exchange in Canada (each, an "Eligible Institution"). In all other cases, the signature of the holder must be guaranteed by an Eligible Institution.

**EXHIBIT B**

**SERIES D CONVERSION NOTICE  
FORTIS INC.**

To: CDS Participant

This notice (the "Series D Conversion Notice") is to be completed by a broker representing a holder of cumulative redeemable convertible first preference shares, series D of Fortis Inc. (the "Corporation") (the "Series D First Preference Shares") who desires to exercise conversion rights as set out in the (final) short form prospectus of the Corporation (the "Prospectus") dated January 20, 2004.

CDS Participants are urged to refer to the Prospectus to obtain details on the conversion dates and the notification periods.

Number of Series D First Preference Shares to  
be converted:

\_\_\_\_\_

Broker's Name:

\_\_\_\_\_

Fax No.:

\_\_\_\_\_

Telephone No.:

\_\_\_\_\_

Date of Series D Conversion Notice:

\_\_\_\_\_

Signature of Authorized Person:

\_\_\_\_\_

UPON AUTHENTICATING THIS SERIES D CONVERSION NOTICE, THE CDS PARTICIPANT IS DIRECTED TO FORWARD THE FOREGOING INSTRUCTIONS FORTHWITH TO CDS.

**EXHIBIT C**

**SERIES E CONVERSION NOTICE  
FORTIS INC.**

To: CDS Participant

This notice (the "Series E Conversion Notice") is to be completed by a broker representing a holder of cumulative redeemable convertible first preference shares, series E of Fortis Inc. (the "Corporation") (the "Series E First Preference Shares") who desires to exercise conversion rights as set out in the (final) short form prospectus of the Corporation (the "Prospectus") dated January 20, 2004.

CDS Participants are urged to refer to the Prospectus to obtain details on the conversion dates and the notification periods.

Number of Series E First Preference Shares to  
be converted:

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Broker's Name:

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Fax No.:

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Telephone No.:

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Date of Series E Conversion Notice:

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Signature of Authorized Person:

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UPON AUTHENTICATING THIS SERIES E CONVERSION NOTICE, THE CDS PARTICIPANT IS DIRECTED TO FORWARD THE FOREGOING INSTRUCTIONS FORTHWITH TO CDS.

**FORTIS**