**September 16, 2009**

# CAPITAL POWER CORPORATION
# FORM 51-102F4
# BUSINESS ACQUISITION REPORT

## Item 1: Identity of Company

### 1.1 Name and Address of Company

Capital Power Corporation
5th Floor, TD Tower
10088-102 Avenue
Edmonton, Alberta
T5J 2Z1

Within the context of this Report, except where otherwise noted, any reference to “Capital Power” or “the Company” refers to Capital Power Corporation, together with it subsidiary entities.

### 1.2 Executive Officer

The name of the executive officer of Capital Power, who is knowledgeable about this report and the acquisition referred to herein is Stuart A. Lee, Senior Vice President and Chief Financial Officer, and his business telephone number is (780) 392-5100.

## Item 2: Details of Acquisition

Forward-Looking Information

Certain information in this Business Acquisition Report is forward-looking within the meaning of Canadian securities laws as it relates to anticipated financial performance, events or strategies. When used in this context, words such as will, anticipate, believe, plan, intend, target, and expect or similar words suggest future outcomes.

Forward-looking information in this Business Acquisition Report includes: (i) the sale of the Company’s remaining interest in the Battle River Power Purchase Arrangement (PPA) will reduce cash flow from operations and adjusted earnings before foreign exchange, interest, income taxes, depreciation and amortization and impairments (adjusted EBITDA); (ii) Keephills 3 construction will be completed in 2011 and will contribute to earnings starting in 2011; (iii) installation of the remaining two units at the Clover Bar Energy Centre in 2009 and 2010; (iv) 2010 earnings will benefit from a full year of operations of the second unit at the Clover Bar Energy Centre and from unit 3 after being commissioned in 2010; (v) current estimate for annual maintenance capital spending, excluding EPCOR Power LP (EPLP), of $30 million to $40 million with an additional $10 million to $20 million in other capital expenditures; (vi) committed capital spending, excluding EPLP, of $207 million and $189 million in 2009 and 2010 respectively; (vii) electricity revenue will be lower for the remainder of 2009 based on the expectation that the Alberta forward power prices will remain low; and (viii) planned outages at the Genesee facilities in 2010 at an expected cost of $18 million to $22 million.

These statements are based on certain assumptions and analyses made by the Company in light of its experience and perception of historical trends, current conditions and expected future developments and other factors it believes are appropriate. The material factors and assumptions used to develop these forward-looking statements include, but are not limited to: (i) the operation of the Company’s facilities; (ii) power plant availability, including those subject to acquired PPAs (iii) the Company’s financial position and credit facilities (iv) the Company’s assessment of commodity and power markets; (v) the Company's assessment of the markets and regulatory environments in which it operates; (vi) weather; (vii) availability and cost of labour and management resources; (viii) performance of contractors and suppliers; (ix) availability and cost of financing; (x) foreign exchange rates; (xi) management's analysis of applicable tax legislation; (xii) the currently applicable and proposed tax laws will not change and will be implemented; (xiii) currently applicable and proposed environmental regulations will be implemented; (xiv) counterparties will perform their obligations; (xv) renewal and terms of PPAs (xvi) ability to successfully integrate and realize benefits of its acquisitions (xvii) ability to implement strategic initiatives which will yield the expected benefits; and (xviii) the Company's assessment of capital markets and ability to complete future share offerings.

Whether actual results, performance or achievements will conform to the Company's expectations and predictions is subject to a number of known and unknown risks and uncertainties which could cause actual results and experience to differ materially from the Company's expectations. Such risks and uncertainties include, but are not limited to risks relating to: (i) operation of the Company's facilities (ii) power plant availability and performance; (iii) unanticipated maintenance and other expenditures; (iv) availability and price of energy commodities; (v) electricity load settlement; (vi) regulatory and government decisions including changes to environmental, financial reporting and tax legislation; (vii) weather and economic conditions; (viii) competitive pressures; (ix) construction; (x) availability and cost of financing; (xi) foreign exchange; (xii) availability and cost of labour, equipment and management resources; (xiii) performance of counterparties, partners, contractors and suppliers in fulfilling their obligations to the Company; (xiv) developments in the North American capital markets; (xv) compliance with financial covenants; (xvi) ability to successfully realize the benefits of acquisitions and investments; (xvii) the tax attributes of and implications of any acquisitions; and (xviii) other factors and assumptions discussed in the section entitled Risk Factors in the Prospectus and in other documents filed with provincial securities commissions in Canada. If any such risks actually occur, they could materially adversely affect the Company's business, financial condition or results of operations. In that case the trading price of the Company's common shares could decline, perhaps materially. Readers are cautioned not to place undue reliance on any such forward-looking statements, which speak only as of the date made. Forward-looking statements are provided for the purpose of providing information about management's current expectations, and plans relating to the future. Readers are cautioned that such information may not be appropriate for other purposes. The Company does not undertake or accept any obligation or undertaking to release publicly any updates or revisions to any forward-looking statements to reflect any change in the Company's expectations or any change in events, conditions or circumstances on which any such statement is based, except as required by law.

## 2.1 Nature of Business Acquired

On May 8, 2009, EPCOR Utilities Inc. (EPCOR) announced its plans to create Capital Power Corporation (Capital Power), a power generation company permanently headquartered in Edmonton, Alberta. Capital Power issued 21,750,000 common shares in the capital of Capital Power at $23 per share pursuant to its initial public offering (IPO) on July 9, 2009. Proceeds from the IPO net of underwriting commissions were approximately $475 million, of which approximately $468 million were used to purchase a 27.8% equity interest in Capital Power L.P. (CPLP).

EPCOR Power Group, which was substantially all of the power generation assets of EPCOR, was purchased by CPLP on July 9, 2009, with effect from July 1, 2009, through the following series of transactions (the Reorganization):

- Formation of CPLP: Capital Power and a wholly-owned subsidiary of Capital Power (Capital Power LP Holdings Inc.) formed CPLP. Capital Power acquired one general partner unit (a GP Unit) and was the initial general partner of CPLP. Capital Power LP Holdings Inc. acquired one common limited partnership unit and as a result, became the initial limited partner in CPLP.

- Sale of EMCC Limited to Capital Power: EPCOR transferred all of the outstanding common shares of EMCC Limited to Capital Power in return for payment of approximately $468 million in cash.

- Contribution of assets by EMCC Limited to CPLP: EMCC Limited contributed substantially all of its assets (consisting primarily of certain securities of subsidiary entities, its class B shares in the capital of EPLP Investments Inc. and a promissory note of EPLP Investments Inc.) to CPLP in return for GP Units. Capital Power transferred its GP Unit in CPLP to EMCC Limited and as a result EMCC Limited became the general partner of CPLP.

- Sale of Assets by EPCOR Power Development Corporation (EPDC) to CPLP: EPDC transferred substantially all of its assets (consisting primarily of assets related to Genesee Units 1 and 2, the Genesee Coal Mine joint venture and certain interests in partnerships) to CPLP in return for 56.625 million exchangeable limited partnership units of CPLP and approximately $896 million in cash. CPLP financed the cash payment with the proceeds from a long-term debt obligation to EPCOR. Concurrently, EPDC subscribed for 56.625 million special voting shares of Capital Power for a nominal amount.

Immediately following completion of the Reorganization, Capital Power held approximately 27.8% of CPLP while EPCOR held 56.625 million exchangeable limited partnership units of CPLP (exchangeable for common shares of Capital Power on a one-for-one basis) representing approximately 72.2% of CPLP. Each exchangeable limited partnership unit is accompanied by a special voting share in the capital of Capital Power which entitles the holder to a vote at Capital Power shareholder meetings, subject to the restriction that such special voting shares must at all times represent not more than 49% of the votes attached to all Capital Power common shares and special voting shares, taken together. Capital Power and EPCOR have agreed that for so long as EPCOR holds not less than a 20% interest in the common shares of Capital Power, the number of directors will not be less than nine. The special voting shares also entitle EPCOR, voting separately as a class, to nominate and elect a maximum of four directors of Capital Power. There are currently twelve directors on Capital Power's board of directors. Accordingly, Capital Power controls CPLP and, on that basis, the operations of CPLP will be consolidated by Capital Power for financial statement purposes.

Immediately following completion of the Reorganization, CPLP held 49% and EPCOR held 51% of the voting rights in EPLP Investments Inc. EPLP Investments Inc. owns the approximate 30.6% interest in EPCOR Power L.P. (EPLP) previously owned by EPCOR. However, CPLP is entitled to all of the economic interest in EPLP Investments Inc. Accordingly, effective early July 2009, Capital Power will consolidate the financial results of EPCOR Power L.P.

For a description of the EPCOR Power Group's power generation assets acquired pursuant to the acquisition, refer to the section entitled "Business - Overview" on pages 15 and 16 of Capital Power's Supplemented PREP Prospectus dated June 25, 2009 as filed by Capital Power on SEDAR on June 26, 2009, which section is incorporated by reference in this report.

## 2.2 Date of Acquisition

The date of the acquisition was July 9, 2009 which was agreed between the Company and EPCOR to be effective July 1, 2009.

## 2.3 Consideration

Consideration for the acquisition was composed of $1,364 million in cash and 56.625 million exchangeable limited partnership units of CPLP.

The cash portion was funded by approximately $468 million of the $475 million net proceeds of the IPO and $896 million in loans from EPCOR. Some of the indebtedness of CPLP to EPCOR mirrors existing indebtedness of EPCOR under debt issued by EPCOR to the public, which is to be repaid on the originally-scheduled maturity dates of such mirrored debt, and bears interest at rates corresponding to the interest rates of each component of the mirrored debt. The indebtedness of CPLP to EPCOR also includes an amount sufficient to meet existing obligations of EPCOR related to indebtedness of The City of Edmonton assumed by EPCOR, which will be repaid in accordance with an amortization schedule. The long-term debt payable to EPCOR is composed of $200 million due June, 2010; $200 million due November, 2011; $130 million due March, 2016; $163 million due January, 2018; and $203 million with annual principal repayments ending June, 2018.

The common shares issuable upon exchange of such exchangeable limited partnership units would represent approximately 72.2% of the common shares outstanding. Under the terms of the exchange agreement, an exchangeable limited partnership unit may not be exchanged if, immediately following such exchange, EPCOR would own, directly or indirectly, more than 49% of the common shares.

Exchangeable limited partnership units are exchangeable for common shares at the option of the holder on a one-for-one basis (subject to customary anti-dilution protections) at any time, subject to the limitation on the maximum number of common shares as described above. Each exchangeable limited partnership unit is accompanied by a special voting share, conferring on the holder certain voting rights at meetings of shareholders of Capital Power. EPCOR holds, indirectly through EPDC, 100% of the outstanding special voting shares. The votes attached to the special voting shares will at all times represent not more than 49% of the votes attached to all outstanding common shares and special voting shares, taken together. The holders of special voting shares are entitled, voting separately as a class, to nominate and elect a maximum of four directors of Capital Power so long as they beneficially own not less than 20% of the aggregate outstanding common shares of Capital Power and common shares issuable upon exchange of exchangeable limited partnership units. Capital Power and EPCOR have agreed that for so long as EPCOR holds directly or indirectly not less than 20% of such shares, the number of directors will not be less than nine. There are currently twelve directors on Capital Power's board of directors, of which four have been nominated and elected by EPDC and are directors or officers of EPCOR. Until such time as the holders of special voting shares beneficially own less than 10% of the aggregate outstanding common shares and common shares issuable upon exchange of exchangeable limited partnership units, they will not be entitled to vote together with holders of common shares in the election for the remaining directors of the Company. EPDC has significant voting power pursuant to its special voting shares other than in connection with the election of directors of Capital Power.

EPCOR holds one issued and outstanding special limited voting share of Capital Power. The special limited voting share entitles EPCOR to the right to vote as a class on any matter that would (i) change the location of Capital Power's head office to a place other than The City of Edmonton in the Province of Alberta;(ii) amend the articles of Capital Power to, or result in a transaction that would, in each case, impact the location of the head office or its meaning as defined in Capital Power's articles; or (iii) amend the rights attaching to the special limited voting share.

## 2.4 Effect on Financial Position

The following table sets forth the pro forma consolidated capitalization of the Company as at June 30, 2009 and the pro forma consolidated capitalization of the Company as at June 30, 2009 after giving effect to the acquisition of the EPCOR Power Group assets. This table should be read in conjunction with the unaudited interim comparative combined and consolidated financial statements of EPCOR Power Group as at and for the six months ended June 30, 2009, contained in the appendices. A discussion of the results of operations of EPCOR Power Group for the six months ended June 30, 2009 is provided in Appendix A of this report.

| (unaudited, $millions) | **As at June 30, 2009** | **As at June 30, 2009 after giving effect to the Acquisition** |
|---|---|---|
| Long-term debt (including current portion) | $ 2,684 | $ 1,762 |
| Non-controlling interests | 492 | 1,941 |
| Shareholders' equity | 862 | 468 |
| Total capitalization | $ 4,038 | $ 4,168 |

Further details on the effect of the Reorganization on the Company's financial position are outlined in the Company's unaudited pro forma consolidated financial statements which are contained in Appendix B of this report.

Other than the above, the Company does not have any plans or proposals for material changes in its business affairs or the affairs of EPCOR Power Group that could have a significant effect on the results of operations and financial position of the Company.

## 2.5 Prior Valuations

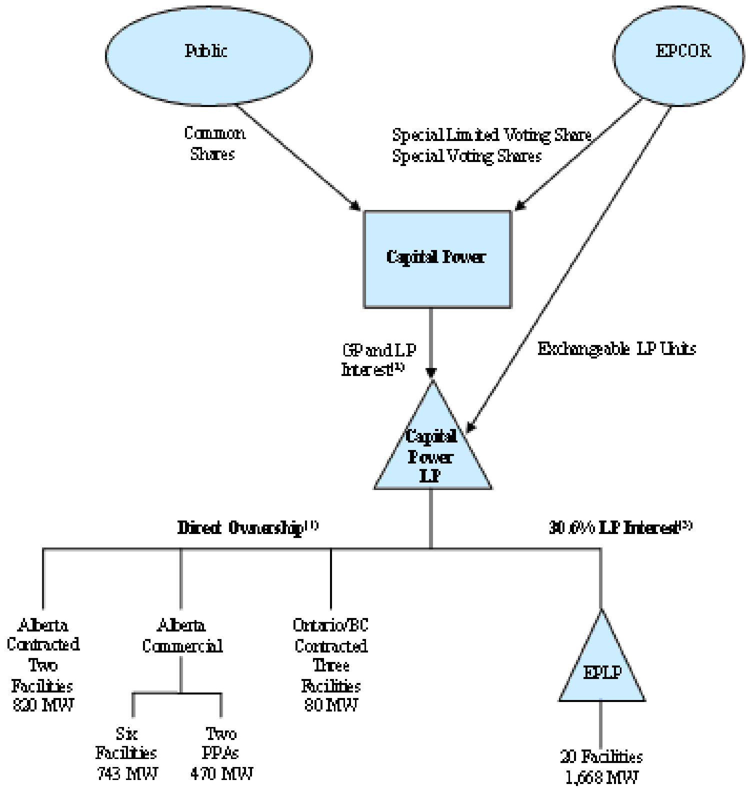
Not applicable.

## 2.6 Parties to Transaction

Following the closing of the Initial Public Offering and the acquisition of the EPCOR Power Group assets by Capital Power, EPCOR owns indirectly, 100% of the outstanding exchangeable limited partnership units of CPLP, representing an approximate 72.2% partnership interest in CPLP.

Capital Power has entered into various agreements with EPCOR to provide for certain aspects of the separation of the business of Capital Power from EPCOR, to provide for the continuity of operations and services and to govern the ongoing relationships between the two groups of entities.

The following organization chart sets out the inter-corporate relationships of EPCOR, the Company and its material subsidiaries after giving effect to the completion of the IPO and the Reorganization:




(1) Stated capacity represents owned and/or operated capacity.
(2) Held through EMCC Limited, a subsidiary of Capital Power.
(3) Capital Power LP has a 49% voting interest and a 100% economic interest in a holding company that owns a 30.6% interest in the limited partnership units of EPLP and 100% of the shares of EPLP General Partner. EPCOR owns the other 51% voting interest in this holding company. EPLP facilities are managed by indirect wholly-owned subsidiaries of Capital Power.

## 2.7 Date of Report

September 16, 2009.

## Item 3: Financial Statements and Other Financial Information

The unaudited pro forma consolidated financial statements of EPCOR Power Group as at and for the six months ended June 30, 2009 are appended as Appendix B to this report.

The audited combined and consolidated financial statements of EPCOR Power Group as at and for the year ended December 31, 2008 and 2007 at pages F-1 to F-56 of Capital Power's Supplemented PREP Prospectus dated June 25, 2009 as filed on SEDAR on June 26, 2009 are incorporated by reference to this report.

The unaudited interim combined and consolidated financial statements of EPCOR Power Group as at June 30, 2009 and for the six month periods ended June 30, 2009 and June 30, 2008 is appended as Appendix C to this report.

# APPENDIX A

## ANALYSIS OF EPCOR POWER GROUP'S SECOND QUARTER 2009 FINANCIAL RESULTS OF OPERATIONS

This analysis of financial results of operations has been prepared as at the date of this Business Acquisition Report and should be read in conjunction with the combined and consolidated financial statements of EPCOR Power Group that appear elsewhere in this document. Included herein are certain forward-looking statements that involve various risks, uncertainties and other factors. See Forward-Looking Information. This analysis has been prepared for the three and six months ended June 30, 2009 and is based on financial statements prepared in accordance with Canadian Generally Accepted Accounting Principles (GAAP).

### Non-GAAP financial measures

The Company uses (i) gross margin, (ii) adjusted Earnings before foreign exchange, interest, income tax, depreciation and amortization and impairments (adjusted EBITDA), (iii) funds from operations and (iv) funds from operations excluding non-controlling interests in EPLP as financial performance measures. These terms are not defined financial measures according to Canadian GAAP and do not have standardized meanings prescribed by GAAP, and therefore may not be comparable to similar measures used by other enterprises. These measures should not be considered an alternative to net earnings, cash provided by operating activities or other measures of financial performance calculated in accordance with Canadian GAAP. Rather, these measures are provided as additional information to complement those Canadian GAAP measures by providing further understanding of the Company's results of operations from management's perspective. See Results of operations – non-GAAP financial measures.

The Company uses gross margin and adjusted EBITDA to measure the operating performance of plants and groups of plants from period to period.

The Company uses funds from operations as its primary cash flow measure because changes in non-cash operating working capital are primarily made up of intercompany payables and receivables between it and EPCOR and are not representative of how working capital would be managed by Capital Power on a stand-alone basis. The Company uses funds from operations excluding non-controlling interests in EPLP to measure its interest in cash flow by excluding non-controlling interest in EPLP's cash flow.

Capital Power segregates the unrealized fair value changes and foreign exchange gains and losses within the gross margin and adjusted EBITDA measures since the changes do not consider the items that these items economically hedge and they are not considered predictors of future economic performance.

### Summary of combined and consolidated financial information

Capital Power reports operational results summarized into the following categories: (i) Alberta commercial plants and portfolio optimization, (ii) Alberta contracted plants, (iii) Ontario/British Columbia contracted plants, (iv) EPLP plants, and (v) other portfolio activities.

For a description of the power generation assets, refer to the section entitled "Business - Overview" on pages 15 and 16 of Capital Power's Supplemented PREP Prospectus dated June 25, 2009 as filed by Capital Power on SEDAR on June 26, 2009, which section is incorporated by reference in this report.

### *Summarized volume and financial information*

| (unaudited) | Three months ended June 30, | | Six months ended June 30, | |
|---|---|---|---|---|
| | 2009 | 2008 | 2009 | 2008 |
| **Electricity generation** (GWh) | | | | |
| Alberta commercial plants[1] | 772 | 463 | 1,462 | 1,088 |
| Alberta contracted plants | 1,623 | 1,275 | 3,251 | 2,698 |
| Ontario/British Columbia contracted plants | 67 | 72 | 116 | 125 |
| | 2,462 | 1,810 | 4,829 | 3,911 |
| EPLP plants[2] | 1,030 | 1,065 | 2,331 | 2,319 |
| **Total** | 3,492 | 2,875 | 7,160 | 6,230 |

(1) Alberta commercial plants excludes acquired PPAs.
(2) Excludes Castleton, the sale of which closed on May 26, 2009.

| (unaudited) | Three months ended June 30, | | Six months ended June 30, | |
|---|---|---|---|---|
| | 2009 | 2008 | 2009 | 2008 |
| **Generation plant availability** (%)[1] | | | | |
| Alberta commercial plants | 94% | 77% | 96% | 88% |
| Alberta contracted plants | 99% | 83% | 99% | 85% |
| Ontario/British Columbia contracted plants | 98% | 95% | 93% | 97% |
| EPLP plants | 90% | 87% | 92% | 92% |
| **Overall Average[2]** | 93% | 84% | 95% | 89% |

(1) Plant availability represents the percentage of time in the period that the plant is available to generate power, whether actually running or not, and is reduced by planned and unplanned outages.
(2) Overall average generation plant availability is an average of individual plant availability weighted by owned and/or operated capacity.

The overall average availability of the Company's facilities, as indicated in the above table, was 93% for the three months ended June 30, 2009 and 95% for the six months ended June 30, 2009 compared to 84% and 89% respectively for the same periods in 2008. The increased availability is primarily due to planned outages on all three Genesee units in 2008.

### *Combined and consolidated net income*

| (unaudited, $ millions) | Three months | Six months |
|---|---|---|
| **Net income (loss) for the periods ended June 30, 2008** | $ (18) | $ 17 |
| Unrealized fair value changes on derivative instruments excluding EPLP fair value changes | 44 | 82 |
| Higher Genesee PPA availability incentive income | 18 | 29 |
| Lower Genesee 1, 2 and 3 maintenance expenses | 11 | 18 |
| Gains on sale of portfolio investments in 2008 | (3) | (3) |
| Lower gain on sale of Battle River PPA | - | (4) |
| Higher financing expenses, excluding EPLP financing | (8) | (17) |
| Lower income from EPLP | (8) | (27) |
| Lower Alberta commercial plants gross margin | (17) | (19) |
| Higher administration expenses, excluding EPLP administration | (13) | (16) |
| Other | (4) | (4) |
| Increase in net income | 20 | 39 |
| **Net income for the periods ended June 30, 2009** | $ 2 | $ 56 |

Net income increased by $20 million and $39 million for the three and six months ended June 30, 2009, respectively, compared with the corresponding period in 2008, due to the net impact of the following items:

- In the three and six months ended June 30, 2009, the unrealized fair value changes were favourable compared with the corresponding periods in the prior year primarily due to the fair value changes relating to electricity and natural gas contracts that were not designated as hedges for accounting purposes, as discussed under Comparison of results by plant category.

- Availability incentive income was earned under the terms of the Genesee 1 and 2 PPA in the three and six months ended June 30, 2009 compared with net availability penalties incurred in the corresponding periods in 2008. The net penalty in 2008 was due to major scheduled turnaround work on Genesee 1 in the first and second quarters and on Genesee 2 in the second quarter. There were no significant outages in the first half of 2009.

- Maintenance expenses for Genesee were lower due to the scheduled maintenance turnarounds in the first quarter of 2008 for Genesee unit 1 and for all 3 units in the second quarter of 2008 whereas there were no major maintenance outages in 2009. The back-to back timing of the maintenance turnarounds in 2008 was required to accommodate the Alberta Electric System Operator's upgrade of the new high-voltage transmission lines in the Genesee and Keephills area.

- In the second quarter of 2008, the Company sold shares in venture capital investments and recognized after-tax gains of $3 million whereas there were no changes to the investment portfolio in 2009.

- On January 15, 2009, the Company sold a 10% interest in the Battle River PPA for cash proceeds of $47 million resulting in an after-tax gain of $26 million compared with proceeds of $53 million and an after-tax gain of $30 million in January 2008. The sale was pursuant to the purchase and sale agreement entered into in June 2006 whereby the Company is selling its Battle River PPA and related interest in the Battle River Power Syndicate Agreement (PSA) over a four year period ending January 2010. An initial interest of 55% was sold in June 2006, followed by subsequent sales of 10% in each of January 2007, 2008 and 2009 and the final 15% interest will be sold in 2010. The year over year decrease was due to lower proceeds reflecting the one year shorter term to maturity for the PPA.

- Financing expenses were higher in the three and six months ended June 30, 2009 primarily due to an increase in guarantee fees and other costs for credit services provided by EPCOR. Credit fees increased due to higher amounts of issued guarantees, higher interest rate spreads, and the impact of foreign exchange translation on guarantees related to the Company's U.S. dollar denominated activities compared with the corresponding periods in 2008. The increase in credit costs reflects the general tightening of the credit market in the latter part of 2008 and the first quarter of 2009. Financing expenses were also higher due to lower cash balances in the three and six months ended June 30, 2009 resulting from the payment of dividends to EPCOR in 2008.

- Net income from EPLP was lower in the three and six months ended June 30, 2009 compared with the corresponding periods in 2008 primarily due to the net impact of unrealized changes in the fair value of natural gas supply and forward foreign exchange contracts. Gross margin for the EPLP plants was higher in both periods ended June 30, 2009 due to the acquisition of Morris Cogeneration LLC (Morris) in the fourth quarter of 2008 and a step-up in pricing under the Curtis Palmer PPA in December 2008, partly offset by lower gross margins at the North Carolina plants due to reduced dispatch.

- Alberta commercial plants gross margin was lower in the three and six months ended June 30, 2009 compared with the corresponding periods in 2008 primarily due to lower generation sales resulting from lower Alberta spot electricity prices, partly offset by favourable settlements on financial power sales and higher margins from commercial power supply contracts due to lower Alberta spot electricity prices.

- Administration expenses, excluding EPLP administration expenses, were higher in the three and six months ended June 30, 2009 compared with the corresponding periods in 2008 mainly due to increased spending on business development activities and the Company's integrated gasification combined cycle and carbon capture and storage technology projects, as well as transaction costs related to the Company's IPO.

## Comparison of results by plant category

| (unaudited, $ millions) | Three months ended June 30, | | Six months ended June 30, | |
|---|---|---|---|---|
| | **2009** | **2008** | **2009** | **2008** |
| **Revenues** | | | | |
| Alberta commercial plants and portfolio optimization | $ 233 | $ 295 | $ 569 | $ 632 |
| Alberta contracted plants | 68 | 38 | 139 | 97 |
| Ontario/British Columbia contracted plants | 4 | 4 | 8 | 9 |
| EPLP plants | 134 | 140 | 280 | 277 |
| Other portfolio activities | 61 | 249 | 176 | 397 |
| Inter-plant category transaction eliminations | - | - | (3) | (4) |
| | 500 | 726 | 1,169 | 1,408 |
| Unrealized fair value changes in derivative instruments | 37 | (40) | 77 | (89) |
| | 537 | 686 | 1,246 | 1,319 |
| **Gross margin**[1] | | | | |
| Alberta commercial plants and portfolio optimization | 55 | 76 | 122 | 147 |
| Alberta contracted plants | 57 | 26 | 117 | 77 |
| Ontario/British Columbia contracted plants | 4 | 4 | 8 | 8 |
| EPLP plants | 83 | 73 | 160 | 151 |
| Other portfolio activities | 8 | 13 | 17 | 16 |
| Inter-plant category transaction eliminations | (2) | (2) | (2) | (2) |
| | 205 | 190 | 422 | 397 |
| Unrealized fair value changes in derivative instruments | 45 | 57 | 27 | 86 |
| | 250 | 247 | 449 | 483 |
| **Adjusted EBITDA**[1] | | | | |
| Alberta commercial plants and portfolio optimization | 29 | 52 | 75 | 103 |
| Alberta contracted plants | 24 | (3) | 64 | 15 |
| Ontario/British Columbia contracted plants | 2 | 2 | 4 | 6 |
| EPLP plants | 47 | 33 | 86 | 81 |
| Other portfolio activities | 1 | 9 | 9 | 11 |
| Inter-plant category transaction eliminations | - | (1) | - | - |
| | 103 | 92 | 238 | 216 |
| Unrealized fair value changes in derivative instruments | 45 | 57 | 27 | 86 |
| | $ 148 | $ 149 | $ 265 | $ 302 |

(1) The comparison of results by plant category has been prepared in accordance with Canadian GAAP except for gross margin and adjusted EBITDA. See "— Results of operations - non-GAAP financial measures".

***Comparison of results - Three and six months ended June 30, 2009***

*Alberta commercial plants and portfolio optimization*

Revenues and expenses from Alberta commercial plants and portfolio optimization decreased by $62 million and $41 million, respectively, for the three months ended June 30, 2009, and $63 million and $38 million, respectively, for the six months ended June 30, 2009 compared with the corresponding periods in 2008. Revenues decreased primarily due to the impact of lower Alberta spot prices on generation sales, partly offset by favourable settlements on financial power sales contracts. Expenses decreased primarily due to the impact of lower Alberta spot prices on energy purchases with respect to the Company's commercial power customers, partly offset by unfavourable settlements on financial power purchases.

Alberta power prices averaged $32/MWh compared with $108/MWh for the three months ended June 30, 2009 and 2008, respectively, and $48/MWh compared with $92/MWh for the six months ended June 30, 2009 and 2008, respectively. The decrease in Alberta spot prices was primarily due to the large number of scheduled outages from the AESO's upgrade of the high-voltage transmission lines in the Genesee and Keephills area in the first half of 2008, lower natural gas prices in 2009 and general slowdown of the Alberta economy in the second quarter of 2009 compared with the second quarter of 2008.

The average realized price for commercial contracted sales and portfolio hedging activities for the three and six months ended June 30, 2009 was $58/MWh and $60/MWh respectively, compared to the spot prices of $32/MWh and $48/MWh respectively.

Gross margin and adjusted EBITDA from Alberta commercial plants and portfolio optimization decreased by $21 million and $23 million, respectively, for the three months ended June 30, 2009, and $25 million and $28 million, respectively, for the six months ended June 30, 2009 compared with the corresponding periods in 2008. These decreases were primarily due to lower generation sales resulting from lower Alberta spot electricity prices, partly offset by favourable settlements on financial power sales and higher margins from commercial power supply contracts due to lower Alberta spot electricity prices.

*Alberta contracted plants*

Revenues and gross margin from Alberta contracted plants increased by $30 million and $31 million, respectively, for the three months ended June 30, 2009, and $42 million and $40 million, respectively, for the six months ended June 30, 2009 compared with the corresponding periods in 2008. These increases were primarily due to increased availability incentive income payments in 2009 compared with net availability penalty incurred in 2008. The net penalty in both periods of 2008 was due to major planned maintenance turnarounds on the Genesee 1 and 2 facilities. Expenses increased by $2 million for the six months ended June 30, 2009 due to higher mining and fuel costs for the Genesee facilities

Adjusted EBITDA increased $27 million and $49 million for the three and six months ended June 30, 2009, respectively, compared with the corresponding periods in 2008, primarily due to higher availability incentive income in 2009 and higher maintenance expenses in 2008 on the Genesee 1 and 2 facilities resulting from the major maintenance turnaround in those periods.

*EPLP plants*

EPLP's revenues and expenses decreased by $6 million and $16 million, respectively, and gross margin increased by $10 million in the second quarter of 2009 as compared with the corresponding period in 2008. Revenues and expenses decreased primarily due to lower electricity prices at the California plants driven by lower natural gas prices. Revenues also decreased due to lower dispatch of the North Carolina plants partly offset by the acquisition of Morris on October 31, 2008 and a step-up in pricing of 18% under the Curtis Palmer PPA in December 2008.

EPLP's revenues and expenses increased by $3 million and decreased by $6 million, respectively, and gross margin increased by $9 million in the six months ended in June 30, 2009 as compared with the corresponding period in 2008. The increase in revenues was primarily due to the acquisition of Morris on

October 31, 2008 and the step-up in pricing under the Curtis Palmer PPA, partly offset by lower pricing at the California facilities and lower dispatch of the North Carolina facilities. Expenses decreased primarily due to lower natural gas prices at the California plants.

EPLP's adjusted EBITDA increased by $14 million and $5 million for the three and six months ended June 30, 2009, respectively, compared with the corresponding periods in 2008. These increases were primarily due to lower maintenance costs primarily due to the turbine overhaul at North Bay and the scheduled major overhauls performed at Williams Lake, North Island, Castleton and Manchief plants in the first half of 2008.

*Other portfolio activities*

Revenues and expenses from other portfolio activities decreased by $188 million and $183 million, respectively, for the three months ended June 30, 2009 and $221 million and $222 million, respectively, for the six months ended June 30, 2009, compared with the corresponding periods in 2008. These decreases were primarily due to lower natural gas trading activity and decreased electricity trading activity in the U.S. Pacific Northwest, Ontario and the U.S. Northeast regions resulting from fewer trading opportunities due to depressed electricity demand, lower electricity prices, and reduced market volatility in the second quarter of 2009 compared with the second quarter of 2008. The impact of these activities on gross margin and adjusted EBITDA was not significant.

Gross margin and adjusted EBITDA also decreased for the three and six months ended June 30, 2009, primarily due to a $4 million pre-tax gain on sale of venture capital investments in 2008 and lower operating margin earned from fees for managing EPLP. The decrease in fees reflect the impact of the EPLP distribution reduction on the incentive fees for the six months ended June 30, 2009 and the change in the method of determining the incentive fees thereafter. Enhancement fees also declined as lower natural gas prices in 2009 reduced the opportunities to curtail operations and re-sell contracted natural gas at market prices.

*Unrealized fair value changes in derivative instruments*

Unrealized fair value changes in financial derivative electricity contracts increased revenues and expenses by $77 million and $89 million respectively, for the three months ended June 30, 2009 and increased revenues and expenses by $166 million and $225 million respectively, for the six months ended June 30, 2009 compared with the corresponding periods of 2008. Unrealized fair value adjustments increased revenues in 2009 primarily due to a net short position arising from financial electricity contracts that were not designated as hedges for accounting purposes combined with a decrease in forward Alberta power prices, compared with increasing forward power prices in 2008. Revenues also increased due to an increase in the fair value of EPLP's foreign exchange contracts due to a decrease in the forward prices for US dollars relative to Canadian dollars compared with an increase in forward prices during the same periods in 2008.

Unrealized fair value adjustments increased expenses for the three and six months ended June 30, 2009 primarily due to a decrease in the fair value of EPLP's natural gas supply contracts due to a decrease in forward natural gas prices compared with an increase in fair value and forward prices in the corresponding periods of 2008.

## Consolidated other expenses

| (unaudited, $ millions) | **Three months ended June 30,** | | **Six months ended June 30,** | |
|---|---|---|---|---|
| | **2009** | **2008** | **2009** | **2008** |
| Depreciation, amortization and asset retirement accretion | $ 43 | $ 46 | $ 89 | $ 91 |
| Foreign exchange losses (gains) | 2 | (3) | 2 | 10 |
| Net financing expenses | 63 | 50 | 127 | 101 |

*Depreciation, amortization and asset retirement accretion*

Depreciation, amortization and asset retirement accretion decreased by $3 million and $2 million in the three and six months ended June 30, 2009 compared with the corresponding periods in 2008 primarily due to the lower amortization on the Battle River PPA. This resulted from the additional sale of interest in the Battle River PPA in the first quarter of 2009 and the reclassification of the remaining interest held in the Battle River PPA on the combined and consolidated balance sheet from power purchase arrangements to assets held for sale, since the disposal of the remaining interest will occur within one year of the balance sheet date, whereby amortization ceases on assets held for sale.

*Foreign exchange losses*

In the three and six months ended June 30, 2009, foreign exchange losses were $2 million which reflects a weakening of the US dollar relative to the Canadian dollar resulting in unfavourable translation losses on the Company's US subsidiaries net monetary assets and liabilities.

In the fourth quarter of 2008, EPLP re-evaluated the functional currency of its US subsidiaries and determined it to be US dollars. Accordingly, foreign exchange gains and losses on translating EPLP's US operations into Canadian dollars were reported as a component of partners' equity in other comprehensive income. EPLP recognized foreign exchange gains in the three months ended June 30, 2008 due to a strengthening of the Canadian dollar relative to the US dollar on the translation of its US dollar denominated debt, and foreign exchange losses in the six months ended June 30, 2008 due to a weakening of the Canadian dollar relative to the US dollar.

*Net financing expenses*

Financing expenses increased by $13 million and $26 million in the three and six months ended June 30, 2009 compared with the corresponding periods in 2008 primarily due to an increase in the cost of guarantee fees and other credit enhancement services provided by EPCOR. Credit fees increased due to higher amounts of issued guarantees, higher interest rate spreads, and the impact of foreign exchange translation on guarantees related to the Company's U.S. dollar denominated activities. Financing expenses were also higher due to lower cash balances in the three and six months ended June 30, 2009 resulting from the payment of dividends to EPCOR in 2008.

**Results of operations – non-GAAP financial measures**

The Company uses (i) gross margin, (ii) adjusted EBITDA, (iii) funds from operations, and (iv) funds from operations excluding non-controlling interests in EPLP as financial performance measures. These terms are not defined financial measures according to Canadian GAAP and do not have standardized meanings prescribed by GAAP, and therefore may not be comparable to similar measures used by other enterprises. These measures should not be considered an alternative to net earnings, cash flow from operating activities or other measures of financial performance calculated in accordance with Canadian GAAP. Rather, these measures are provided as additional information to complement those Canadian GAAP measures by providing further understanding of the Company's results of operations from management's perspective.

*Gross margin and adjusted EBITDA*

Capital Power uses gross margin and adjusted EBITDA to measure the operating performance of plants and groups of plants from period to period. A reconciliation of gross margin and adjusted EBITDA to net income is as follows:

| (unaudited, $ millions) | Three months ended June 30, | | Six months ended June 30, | |
|---|---|---|---|---|
| | 2009 | 2008 | 2009 | 2008 |
| **Revenues** | $ 537 | $ 686 | $ 1,246 | $ 1,319 |
| Energy purchases and fuel | 287 | 439 | 797 | 836 |
| **Gross margin** | 250 | 247 | 449 | 483 |
| Deduct (add): | | | | |
| Operations, maintenance, and administration | 102 | 98 | 184 | 181 |
| **Adjusted EBITDA** | 148 | 149 | 265 | 302 |
| Deduct (add): | | | | |
| Depreciation, amortization, and asset retirement accretion | 43 | 46 | 89 | 91 |
| Foreign exchange losses (gains) | 2 | (3) | 2 | 10 |
| Gain on sale of power purchase arrangement and related transactions | - | - | (30) | (34) |
| Net financing expenses | 63 | 50 | 127 | 101 |
| Income taxes | 7 | 6 | 12 | 11 |
| Non-controlling interests | 31 | 68 | 9 | 106 |
| **Net income (loss)** | $ 2 | $ (18) | $ 56 | $ 17 |

*Funds from operations and funds from operations excluding non-controlling interests in EPLP*

Capital Power uses funds from operations to measure the Company's ability to generate funds from current operations and measures its interest in cash flows by excluding the non-controlling interest in EPLP's cash flows. A reconciliation of funds from operations and funds from operations excluding non-controlling interests in EPLP to cash provided by operating activities is as follows:

| (unaudited, $ millions) | Three months ended June 30, | | Six months ended June 30, | |
|---|---|---|---|---|
| | 2009 | 2008 | 2009 | 2008 |
| **Funds from operations excluding non-controlling interests in EPLP** | $ 2 | $ 33 | $ 64 | $ 77 |
| Funds from operations due to non-controlling interests in EPLP | 26 | 16 | 45 | 42 |
| **Funds from operations** | 28 | 49 | 109 | 119 |
| Change in non-cash operating working capital | 34 | (7) | (20) | (10) |
| **Cash provided by operating activities** | $ 62 | $ 42 | $ 89 | $ 109 |

Changes in working capital are primarily made up of intercompany payables and receivables between the Company and EPCOR and are not representative of how working capital would be managed by the Company on a stand-alone basis. Therefore, the Company uses funds from operations as its primary operating cash flow measure.

| (unaudited, $ millions) | Three months | Six months |
|---|---|---|
| **Funds from operations for the periods ended June 30, 2008** | $ 49 | $ 119 |
| Higher Genesee PPA availability incentive income | 27 | 42 |
| Higher adjusted EBITDA from EPLP | 11 | 2 |
| Lower Genesee 1, 2 and 3 maintenance expenses | 16 | 26 |
| Lower (higher) current income taxes | (2) | 8 |
| Higher financing expenses | (13) | (26) |
| Lower adjusted EBITDA from other portfolio activities | (8) | (2) |
| Higher administration expense, excluding EPLP | (19) | (22) |
| Lower Alberta commercial plants electricity margin | (21) | (25) |
| Other | (12) | (13) |
| (Decrease) | (21) | (10) |
| **Funds from operations for the periods ended June 30, 2009** | $ 28 | $ 109 |

The $21 million and $10 million decrease in funds from operations in the three and six months ended June 30, 2009 respectively, compared with the corresponding periods in 2008 were primarily due to the following items:

- The electricity margin for the Alberta commercial plants was lower in the three and six months ended June 30, 2009 compared with the corresponding periods in 2008 for the reasons discussed in the Comparison of results by plant category.
- Administration expense, excluding EPLP, was higher in the three and six months ended June 30, 2009 compared with the corresponding periods in 2008 for the reasons explained under Combined and consolidated net income.
- Adjusted EBITDA from other portfolio activities was lower in the three and six months ended June 30, 2009 compared with the corresponding periods in 2008 primarily due to a sale of venture capital investments in 2008.
- Financing expenses were higher in the three and six months ended June 30, 2009 compared with in the corresponding periods in 2008 for the reasons explained under Combined and consolidated net income.

Decreases in funds from operations were partly offset by the following items:

- Genesee 1 and 2 PPA availability incentive income was higher and Genesee 1, 2 and 3 maintenance expenses were lower in the three and six months ended June 30, 2009 compared with the corresponding periods in 2008 for the same reasons as explained under Combined and consolidated net income.
- The decrease in current income taxes in the six months ended June 30, 2009 reflects higher financing expenses and a decrease in deferred partnership income compared with the six month period ended June 30, 2008.
- Adjusted EBITDA from EPLP was higher in the three and six months ended June 30, 2009 compared with the corresponding periods in 2008 for the same reasons as explained under the Comparison of results by plant category.

## Outlook

As discussed in the management's discussion and analysis of financial condition and results of operations included in the Prospectus, commencing in 2006 management's strategy for the EPCOR Power Group has been to sell its Battle River PPA and a portion of its interest in the Sundance PPA and replace this power output with power produced from its own new physical facilities. Interests in the PPAs were sold over the period from 2006 to 2009 with the remaining 15% interest in the Battle River PPA expected to be sold in January 2010. Clover Bar unit 1 commenced operations in 2008, followed by unit 2 which was commissioned in late August, 2009.  Clover Bar unit 3 is expected to be commissioned in 2010,while Keephills 3 is expected to commence operations in 2011. Accordingly, the Company's adjusted EBITDA and cash flow from operations are expected to be negatively impacted by the Company's reduced interests in PPAs in 2009 and 2010 and are expected to increase as the new facilities come on line in 2010 and 2011.

Alberta forward power prices declined in the first half of 2009 and are expected to remain low in the near term mainly due to low natural gas prices. Consistent with the second quarter results, lower power prices are expected to reduce adjusted EBITDA, excluding fair value adjustments, and cash flow from operations for the remainder of 2009 as approximately 53% of the Company's Alberta commercial portfolio  is exposed to the spot market. The remaining 47% has been sold forward at an average price in the mid $60/MWh range. The Alberta commercial plants represent approximately 40% to 50% of adjusted EBITDA, before unrealized fair value changes, excluding the non-controlling interest in EPLP.

For 2010, approximately 80% of the Alberta commercial portfolio position has been sold forward at an average price in the mid $60/MWh range which should reduce the exposure to decreases in power prices. For 2011, the Alberta commercial portfolio's open position is expected to increase to approximately 60% to 65% of the total portfolio which could introduce more variability in adjusted EBITDA and cash flow depending on changes in power prices. The average contracted price is in the low $70/MWh range for the generation sold forward in 2011. The Company will continue to monitor commodity price forecast movements and undertake transactions to optimize the portfolio and limit exposure to price movements.

The sensitivity to an increase/decrease of $1/MWh in the Alberta power price, assuming all other factors are held constant, is estimated to be an adjusted EBITDA increase/decrease of approximately $1 million for the remainder of 2009; $1 million for 2010 and $4 million for 2011. The increased sensitivity in 2011 is due to the open position on the Keephills 3 facility and the expiration of certain Alberta wholesale and commercial and industrial customer contracts.

The Company also expects the following factors to impact its results for the remainder of 2009:

- An outage is planned at the Genesee site in the fall for scheduled equipment repairs and maintenance to unit 1 which is expected to reduce availability incentive income and cash flow from operations and increase maintenance expenses.

- One time general and administration costs of approximately $5 million are expected to be incurred in the second half of 2009 as a result of the Reorganization which will reduce adjusted EBITDA and cash flow from operations.

- Engineering and design costs will be incurred for the Genesee integrated gasification combined-cycle (IGCC) project and are expected to reduce adjusted EBITDA and operating cash flow in the second half of 2009.

The Company is also faced with on-going cost pressures on the construction of its Keephills 3 facility. Despite slower regional economic conditions, construction costs remain under pressure as project work packages are finalized in the normal course of construction. For the remainder of 2009, the committed capital expenditures primarily for Keephills 3 and the Clover Bar Energy Centre and excluding EPLP's capital expenditures are approximately $207 million, with a further $189 committed for 2010. In addition to capital project costs, maintenance capital spending for any given year, excluding EPLP, is expected to be in the range of $30 million to $40 million with an additional $10 million to $20 million in other capital expenditures.

The major items that are expected to reduce adjusted EBITDA and cash flow from operations for 2010 compared with 2009 are:

- the impact of lower Alberta electricity prices on the Alberta commercial portfolio discussed above

- the impact of the Company's reduced interest in the Battle River PPA after the sale of the remaining portion in January 2010

- maintenance outages scheduled in 2010 at the Genesee site for units 2 and 3 compared with only one scheduled outage in 2009. In general, major maintenance expenses for the Genesee maintenance programs can vary significantly depending on the number of scheduled turnarounds in any given year. The total operating expenses for the two outages in 2010 for both units is expected to be between $18 million and $22 million.

These decreases are expected to be partly offset by higher adjusted EBITDA from a full year of operations from the second unit of Clover Bar which was commissioned in 2009 and a contribution to adjusted EBITDA after the commissioning of unit 3 in 2010. Keephills 3 is expected to contribute to adjusted EBITDA when it becomes operational in 2011.

# APPENDIX B

## CAPITAL POWER UNAUDITED PRO FORMA CONSOLIDATED FINANCIAL INFORMATION

The unaudited pro forma consolidated financial information of Capital Power has been prepared by management based on the unaudited interim combined and consolidated financial statements of EPCOR Power Group as at and for the three and six months ended June 30, 2009 and the audited combined and consolidated financial statements of EPCOR Power Group for the year ended December 31, 2008. The pro forma consolidated financial information of Capital Power includes CPLP on a consolidated basis. See note 1(b). The pro forma consolidated financial information presents the effects of the completion of the initial public offering (IPO) and the Reorganization and the use of the net proceeds of the IPO as described on pages 2 and 3 of the Business Acquisition Report (BAR) filed by the Company, as if the IPO and Reorganization were completed on June 30, 2009 for the purpose of the pro forma consolidated balance sheet, and on January 1, 2008 for the purpose of the pro forma consolidated statements of income for the year ended December 31, 2008 and for the three and six months ended June 30, 2009.

The notes to the unaudited pro forma consolidated financial information have been prepared by management based on EPCOR Power Group's unaudited combined and consolidated balance sheet as at June 30, 2009 and the unaudited combined and consolidated statements of income for the year ended December 31, 2008 and for the three and six months ended June 30, 2009. These notes should be read in conjunction with EPCOR Power Group's audited combined and consolidated financial statements for the year ended December 31, 2008 at pages F-1 to F-56 of Capital Power's Supplemented PREP Prospectus dated June 25, 2009 as filed on SEDAR and EPCOR Power Group's unaudited interim combined and consolidated financial statements as at and for the three and six months ended June 30, 2009 on pages C1 to C15 of the BAR.

The unaudited pro forma consolidated financial information has been prepared in accordance with Canadian GAAP consistent with the significant accounting policies described in note 2 to EPCOR Power Group's audited combined and consolidated financial statements for the year ended December 31, 2008.

The unaudited pro forma combined financial information reflects pro forma adjustments that are described in the accompanying notes and are based on currently available information and assumptions that management believes provide a reasonable basis for presenting the significant effects of the completion of the Offering and the Reorganization. In management's opinion, all material adjustments necessary to present fairly the pro forma consolidated financial information have been made. The unaudited pro forma consolidated financial information is presented for informational purposes only and is not necessarily indicative of what the financial position and results of operations would have been had the completion of the Offering and the Reorganization occurred at the dates indicated, nor does it purport to be indicative of the financial position as of any future date or results of operations for any future period. Actual adjustments will differ from the pro forma adjustments.

**Unaudited Pro Forma Consolidated Statement of Income**
($ millions)
Year ended December 31, 2008

| | | Pro forma adjustments | | | | | |
|---|---|---|---|---|---|---|---|
| | Historical | Capital structure | Fair values | Public entity costs | Total | Notes | Pro forma |
| Revenues | $ 2,649 | | | | $ - | | $ 2,649 |
| Energy purchases and fuel | 1,914 | | | | - | | 1,914 |
| | 735 | | | | - | | 735 |
| Operations, maintenance and administration | 370 | | | 4 | 4 | 3d | 374 |
| Depreciation, amortization and asset retirement accretion | 181 | | 3 | | 3 | 3a | 184 |
| Foreign exchange losses | 18 | | | | - | | 18 |
| Gain on sale of power purchase arrangement and related transactions | (34) | | | | - | | (34) |
| Impairments | 52 | | (10) | | (10) | 3b | 42 |
| Net financing expenses | 219 | (116) | | | (116) | 3c | 103 |
| | 806 | (116) | (7) | 4 | (119) | | 687 |
| Income (loss) before income taxes and non-controlling interests | (71) | 116 | 7 | (4) | 119 | | 48 |
| Income taxes (reductions) | (24) | (6) | - | - | (6) | 3e | (30) |
| Income (loss) before non-controlling interests | (47) | 122 | 7 | (4) | 125 | | 78 |
| Non-controlling interests | (51) | 102 | (2) | (3) | 97 | 3f | 46 |
| Net income | $ 4 | $ 20 | $ 9 | $ (1) | $ 28 | | $ 32 |

See accompanying notes to unaudited pro forma consolidated financial information.

**Unaudited Pro Forma Consolidated Statement of Income**
($ millions)
Three months ended June 30, 2009

| | | Pro forma adjustments | | | | | |
|---|---|---|---|---|---|---|---|
| | Historical | Capital structure | Fair values | Public entity costs | Total | Notes | Pro forma |
| Revenues | $ 537 | | | | $ - | | $ 537 |
| Energy purchases and fuel | 287 | | | | - | | 287 |
| | 250 | | | | - | | 250 |
| Operations, maintenance and administration | 102 | | | 1 | 1 | 3d | 103 |
| Depreciation, amortization and asset retirement accretion | 43 | | 1 | | 1 | 3a | 44 |
| Foreign exchange losses | 2 | | | | - | | 2 |
| Gain on sale of power purchase arrangement and related transactions | - | | | | - | | - |
| Impairments | - | | | | - | | - |
| Net financing expenses | 63 | (55) | | | (55) | 3c | 8 |
| | 210 | (55) | 1 | 1 | (53) | | 157 |
| Income before income taxes and non-controlling interests | 40 | 55 | (1) | (1) | 53 | | 93 |
| Income taxes (reductions) | 7 | 4 | - | - | 4 | 3e | 11 |
| Income before non-controlling interests | 33 | 51 | (1) | (1) | 49 | | 82 |
| Non-controlling interests | 31 | 40 | - | - | 40 | 3f | 71 |
| Net income | $ 2 | $ 11 | $ (1) | $ (1) | $ 9 | | $ 11 |

See accompanying notes to unaudited pro forma consolidated financial information.

**Unaudited Pro Forma Consolidated Statement of Income**
($ millions)
Six months ended June 30, 2009

| | | Pro forma adjustments | | | | | |
|---|---|---|---|---|---|---|---|
| | Historical | Capital structure | Fair values | Public entity costs | Total | Notes | Pro forma |
| Revenues | $ 1,246 | | | | $ - | | $ 1,246 |
| Energy purchases and fuel | 797 | | | | - | | 797 |
| | 449 | | | | - | | 449 |
| Operations, maintenance and administration | 184 | | | 2 | 2 | 3d | 186 |
| Depreciation, amortization and asset retirement accretion | 89 | | 2 | | 2 | 3a | 91 |
| Foreign exchange losses | 2 | | | | - | | 2 |
| Gain on sale of power purchase arrangement and related transactions | (30) | | | | - | | (30) |
| Impairments | - | | | | - | | - |
| Net financing expenses | 127 | (84) | | | (84) | 3c | 43 |
| | 372 | (84) | 2 | 2 | (80) | | 292 |
| Income before income taxes and non-controlling interests | 77 | 84 | (2) | (2) | 80 | | 157 |
| Income taxes (reductions) | 12 | (9) | - | - | (9) | 3e | 3 |
| Income before non-controlling interests | 65 | 93 | (2) | (2) | 89 | | 154 |
| Non-controlling interests | 9 | 117 | (1) | (1) | 115 | 3f | 124 |
| Net income | $ 56 | $ (24) | $ (1) | $ (1) | $ (26) | | $ 30 |

See accompanying notes to unaudited pro forma consolidated financial information.

**Unaudited Pro Forma Consolidated Balance Sheet**
($ millions)
June 30, 2009

| | | Pro forma adjustments | | | |
|---|---|---|---|---|---|
| | **Historical** | **Offering** | **Reorganization** | **Notes** | **Pro forma** |
| **Assets** | | | | | |
| Current assets: | | | | | |
| Cash and cash equivalents | $ 115 | $ 468 | $ (468) | 1a | $ 115 |
| Accounts receivable | 209 | | | | 209 |
| Income taxes recoverable | 9 | | 30 | | 39 |
| Inventories | 53 | | | | 53 |
| Prepaid expenses | 10 | | | | 10 |
| Future income taxes | 1 | | 9 | 2d | 10 |
| Derivative instruments assets | 140 | | - | | 140 |
| | 537 | 468 | (429) | | 576 |
| Property, plant and equipment | 3,299 | | (137) | 2a, 2b | 3,162 |
| Power purchase agreements | 507 | | 71 | 2a, 2b | 578 |
| Contract and customer rights and other intangible assets | 194 | | (38) | 2a, 2b | 156 |
| Derivative instruments assets | 74 | | - | 2a, 2b | 74 |
| Future income tax assets | 93 | | (69) | 2a, 2b, 2d | 24 |
| Goodwill | 156 | | (33) | 2a, 2b | 123 |
| Other assets | 123 | | - | 2a, 2b | 123 |
| Assets held for sale | 26 | | 11 | 2a, 2b | 37 |
| | $ 5,009 | $ 468 | $ (624) | | $ 4,853 |
| **Liabilities and Shareholders' Equity** | | | | | |
| **Current liabilities:** | | | | | |
| Notes payable | $ 228 | $ - | $ (228) | 2c | $ - |
| Accounts payable and accrued liabilities | 307 | | - | | 307 |
| Income taxes payable | - | | - | | - |
| Derivative instruments liabilities | 143 | | - | | 143 |
| Future income tax liabilities | 34 | | (25) | 2d | 9 |
| Current portion of long-term debt | 20 | | 266 | 2a, 2b, 2c | 286 |
| | 732 | - | 13 | | 745 |
| Long-term debt | 2,664 | | (1,188) | 2a, 2b, 2c | 1,476 |
| Derivative instruments liabilities | 64 | | - | 2a, 2b | 64 |
| Other non-current liabilities | 88 | | 4 | 2a, 2b | 92 |
| Future income tax liabilities | 107 | | (40) | 2a, 2b, 2d | 67 |
| | 3,655 | - | (1,211) | | 2,444 |
| Non-controlling interests | 492 | | 1,449 | 1b | 1,941 |
| Shareholders' equity | 862 | 468 | (862) | 1a, 1b | 468 |
| | $ 5,009 | $ 468 | $ (624) | | $ 4,853 |

See accompanying notes to unaudited pro forma consolidated financial information.

## 1. Transactions:

(a) Offering: As described on pages 2 and 3 of the BAR, Capital Power issued 21,750,000 common shares for gross cash proceeds of $500 million less underwriting commissions of approximately $25 million. Of the net proceeds, $7 million was used toward offering expenses while approximately $468 million was used to acquire the shares of EMCC Limited.

(b) Reorganization: Through a series of reorganization steps, the assets and liabilities used to carry on the business of EPCOR Power Group were transferred to CPLP. This involved a number of reorganization and acquisition transactions that took place immediately prior to and following the completion of the Offering. For full description of the Reorganization, see the Combined and Consolidated Interim Financial Statements of EPCOR Power Group for the six months ended June 30, 2009 and 2008 (note 16) on pages C14 and C15 of the BAR.

The effect of the Reorganization is CPLP acquired from EPCOR and its subsidiaries, directly or indirectly, the assets and liabilities used to carry on EPCOR Power Group's business in exchange for an equity interest in CPLP, voting interests in Capital Power and debt in the amount of $896 million. The assets and liabilities, directly or indirectly owned by CPLP, are recorded at fair value (except EPLP, see note 2(b) resulting in an adjustment to the carrying amounts see note 2(a) in Capital Power's consolidated financial statements. Capital Power is expecting to consolidate the assets, liabilities and operations of CPLP on the basis of control. As EPCOR will hold an economic interest in CPLP, a non-controlling interest of approximately 72.2% of the assets and liabilities is reflected in the unaudited pro forma consolidated financial information of Capital Power after giving effect to completion of the Reorganization.

**2. Notes to unaudited pro forma consolidated balance sheet:**

The adjustments included in the unaudited pro forma consolidated balance sheet assumed the following events occurred on June 30, 2009.

(a) Fair value adjustments to assets and liabilities: Fair value adjustments, as determined by an independent third party valuation, are preliminary and subject to change. The amount of the fair value adjustments may differ materially from the amounts disclosed in the future purchase price allocation. Any such changes in the determination and allocation of the fair value adjustments could also result in material changes to operating results in subsequent periods.

(b) Fair value adjustments on the assets and liabilities of EPLP: Capital Power expects to consolidate EPLP. The non-controlling interest in EPLP continues to be recorded at carrying amounts. Adjustments from carrying amounts at the date of acquisition to fair values of the assets and liabilities have been recorded to the extent of Capital Power Corporation's effective 8.5% ownership interest. These fair value adjustments will be determined in accordance with, and are subject to, note 2(a)

(c) Adjustments to notes payable and long-term debt: As part of the Reorganization, existing third party debt with unrelated parties was assumed by CPLP and has been recorded at fair value. Notes payable and long-term debt with related parties was not transferred to Capital Power. CPLP incurred indebtedness in the aggregate principal amount of $896 million as part of the consideration payable to EPCOR under the Reorganization.

(d) Future income tax assets and liabilities have been adjusted to exclude those assets and liabilities recorded historically with respect to EPCOR's 72.2% interest which will not be included in Capital Power's financial statements.

**3. Notes to unaudited pro forma consolidated statements of income:**

The assumptions and adjustments made to the unaudited pro forma consolidated statements of income are as follows:

(a) Increase in depreciation, amortization and asset retirement accretion expense: Incremental depreciation and amortization expense arises from fair value changes on property, plant and equipment, power purchase agreements and contract and customer rights and other intangible assets.

(b) Reversal of impairment expense: The impairment expense consists of two components: (i) an impairment of the goodwill originally recognized on the purchase of EPLP and (ii) an impairment of EPLP's investment in PERH. The income statements have been adjusted to reflect the Reorganization as if it had occurred on January 1, 2008 which results in the assets and liabilities being recorded at fair value as at that date for the 27.8% acquired by Capital Power, thereby eliminating an impairment expense in 2008 related to that portion. Due to the non-controlling interest, 91.5% of the EPLP assets and liabilities continue to be the carrying amount and only 8.5% of the impairment of PERH was reversed.

(c) Reduction of interest expense: The decrease in long-term debt, as described in note 2d), results in lower interest expense.

(d) Incremental costs associated with the creation of a new public entity: Represents estimated incremental costs for financial reporting and compliance, corporate governance, legal, treasury, investor relations activities and professional fees to external service providers.

(e) Changes to income tax provision: Represents the change to income tax expense as a result of the other pro forma adjustments.

(f) EPCOR’s non-controlling interest: Represents the proportion of income and pro forma adjustments that relate to EPCOR’s non-controlling interest.

## APPENDIX C

**Unaudited interim combined and consolidated financial statements of EPCOR Power Group as at June 30, 2009 and December 31, 2008 and for the six month periods ended June 30, 2009 and June 30, 2008.**

### EPCOR POWER GROUP

Combined and Consolidated Statements of Income
(Unaudited, in millions of dollars)

| | Three months ended June 30, 2009 | Three months ended June 30, 2008 | Six months ended June 30, 2009 | Six months ended June 30, 2008 |
|---|---|---|---|---|
| Revenues | $ 537 | $ 686 | $ 1,246 | $ 1,319 |
| Energy purchases and fuel | 287 | 439 | 797 | 836 |
| | 250 | 247 | 449 | 483 |
| Operations, maintenance and administration | 102 | 98 | 184 | 181 |
| Depreciation, amortization and asset retirement accretion | 43 | 46 | 89 | 91 |
| Foreign exchange losses (gains) | 2 | (3) | 2 | 10 |
| Gain on sale of power purchase arrangement and related transactions (note 11) | - | - | (30) | (34) |
| Net financing expenses | 63 | 50 | 127 | 101 |
| | 210 | 191 | 372 | 349 |
| Income before income taxes and non-controlling interests | 40 | 56 | 77 | 134 |
| Income taxes | 7 | 6 | 12 | 11 |
| Income before non-controlling interests | 33 | 50 | 65 | 123 |
| Non-controlling interests (note 6) | 31 | 68 | 9 | 106 |
| Net income (loss) | $ 2 | $ (18) | $ 56 | $ 17 |

See accompanying notes to combined and consolidated financial statements.

## EPCOR POWER GROUP

Combined and Consolidated Balance Sheets
(Unaudited, in millions of dollars)

| | June 30, 2009 | December 31, 2008 |
|---|---|---|
| **Assets** | | |
| Current assets: | | |
| Cash and cash equivalents | $ 115 | $ 69 |
| Accounts receivable | 209 | 320 |
| Income taxes recoverable | 9 | 5 |
| Inventories | 53 | 62 |
| Prepaid expenses | 10 | 8 |
| Derivative instruments assets (note 9) | 140 | 126 |
| Future income tax asset | 1 | - |
| | 537 | 590 |
| Property, plant and equipment | 3,299 | 3,185 |
| Power purchase arrangements | 507 | 550 |
| Contract and customer rights and other intangible assets | 194 | 183 |
| Derivative instruments assets (note 9) | 74 | 75 |
| Future income tax assets | 93 | 97 |
| Goodwill | 156 | 159 |
| Other assets | 123 | 120 |
| Assets held for sale (note 11) | 26 | 43 |
| | $ 5,009 | $ 5,002 |
| **Liabilities and Shareholders' Equity** | | |
| Current liabilities: | | |
| Notes payable | $ 228 | $ 155 |
| Accounts payable and accrued liabilities | 307 | 430 |
| Income taxes payable | - | 4 |
| Derivative instruments liabilities (note 9) | 143 | 130 |
| Future income tax liabilities | 34 | 34 |
| Current portion of long-term debt | 20 | 20 |
| | 732 | 773 |
| Long-term debt | 2,664 | 3,007 |
| Derivative instruments liabilities (note 9) | 64 | 110 |
| Other non-current liabilities | 88 | 91 |
| Future income tax liabilities | 107 | 100 |
| | 3,655 | 4,081 |
| Non-controlling interests (note 6) | 492 | 540 |
| Shareholders' equity | 862 | 381 |
| Subsequent event (note 16) | | |
| | $ 5,009 | $ 5,002 |

See accompanying notes to combined and consolidated financial statements.

## EPCOR POWER GROUP

Combined and Consolidated Statements of Changes in Shareholders' Equity
(Unaudited, in millions of dollars)

| | Three months ended June 30, 2009 | Three months ended June 30, 2008 | Six months ended June 30, 2009 | Six months ended June 30, 2008 |
|---|---|---|---|---|
| **Share capital:** | | | | |
| Balance, beginning of period | $ 673 | $ 673 | $ 673 | $ 673 |
| Share capital issued (note 13) | 462 | - | 462 | - |
| Balance, end of period | 1,135 | 673 | 1,135 | 673 |
| **Retained earnings (deficit):** | | | | |
| Balance, beginning of period | (195) | 159 | (228) | 136 |
| Adjustment for change in accounting policy (note 4) | - | - | 1 | - |
| Net income (loss) | 2 | (18) | 56 | 17 |
| Common share dividends | (20) | (5) | (37) | (10) |
| Refundable taxes (note 11) | - | 2 | (5) | (5) |
| Balance, end of period | (213) | 138 | (213) | 138 |
| **Accumulated other comprehensive loss:** | | | | |
| Balance, beginning of period | (42) | (56) | (64) | (80) |
| Other comprehensive income (loss) | (18) | - | 4 | 24 |
| Balance, end of period | (60) | (56) | (60) | (56) |
| Total shareholders' equity, end of period | $ 862 | $ 755 | $ 862 | $ 755 |

See accompanying notes to combined and consolidated financial statements.

**EPCOR POWER GROUP**

Combined and Consolidated Statements of Comprehensive Income
(Unaudited, in millions of dollars)

| | Three months ended June 30, | | Six months ended June 30, | |
|---|---|---|---|---|
| | **2009** | **2008** | **2009** | **2008** |
| Net income (loss) | $ 2 | $ (18) | $ 56 | $ 17 |
| Other comprehensive income (loss), net of income taxes: | | | | |
| Unrealized (losses) gains on derivative instruments designated as cash flow hedges[1] | (10) | 22 | (1) | 29 |
| Reclassification of losses (gains) on derivative instruments designated as cash flow hedges to net income[2] | 4 | (24) | 12 | (9) |
| Unrealized gains on financial instruments designated as available for sale[3] | - | 6 | - | 6 |
| Reclassification of gains on financial instruments designated as available for sale to net income[4] | - | (2) | - | (2) |
| Unrealized loss in self-sustaining foreign operations[5] | (41) | (1) | (24) | - |
| Non-controlling interests[5] (note 6) | 29 | (1) | 17 | - |
| Increase/(decrease) | (18) | - | 4 | 24 |
| Comprehensive (loss) income | $ (16) | $ (18) | $ 60 | $ 41 |

1 For the three and six months ended June 30, 2009, net of income tax recovery of $4 million and nil respectively. For the three and six months ended June 30, 2008, net of income tax expenses of $10 million and $13 million respectively.

2 For the three and six months ended June 30, 2009, net of reclassification of income tax recoveries of $2 million and $5 million respectively. For the three and six months ended June 30, 2008, net of reclassification of income tax expenses of $11 million and $4 million respectively.

3 For the three and six months ended June 30, 2008, net of income tax expense of $2.

4 For the three and six months ended June 30, 2008, net of reclassification of income tax expense of $1.

5 For the three and six months ended June 30, 2009 and June 30, 2008, net of income tax expense of nil.

See accompanying notes to combined and consolidated financial statements.

**EPCOR POWER GROUP**

Combined and Consolidated Statement of Cash Flows
(Unaudited, in millions of dollars)

| | Three months ended June 30, 2009 | Three months ended June 30, 2008 | Six months ended June 30, 2009 | Six months ended June 30, 2008 |
|---|---|---|---|---|
| **Operating activities:** | | | | |
| Net income (loss) | $ 2 | $ (18) | $ 56 | $ 17 |
| Adjustments to reconcile net income to cash flows from operating activities: | | | | |
| Depreciation, amortization and asset retirement accretion | 43 | 46 | 89 | 91 |
| Gain on sale of power purchase arrangement and related transactions (note 11) | - | - | (30) | (34) |
| Non-controlling interests in Power LP (note 6) | 30 | 67 | 6 | 103 |
| Fair value changes on derivative instruments | (45) | (57) | (27) | (86) |
| Unrealized foreign exchange losses | 1 | (3) | (1) | 9 |
| Future income taxes | 9 | 10 | 26 | 17 |
| Other | (12) | 4 | (10) | 2 |
| | 28 | 49 | 109 | 119 |
| Change in non-cash operating working capital (note 7) | 34 | (7) | (20) | (10) |
| | 62 | 42 | 89 | 109 |
| **Investing activities:** | | | | |
| Property, plant and equipment and other assets | (125) | (132) | (233) | (208) |
| Net proceeds on PSA interests (note 11) | - | - | 47 | 53 |
| Proceeds on sale of Castleton (note 12) | 12 | - | 12 | - |
| Other | 1 | 4 | 3 | 7 |
| Change in non-cash investing working capital (note 7) | 93 | 117 | 129 | 126 |
| | (19) | (11) | (42) | (22) |
| **Financing activities:** | | | | |
| Repayment of long-term debt | (338) | (9) | (350) | (25) |
| Proceeds from issue of long-term debt | 9 | 200 | 38 | 200 |
| Distributions to non-controlling interests | (16) | (23) | (40) | (47) |
| Common share dividends | (20) | (5) | (37) | (10) |
| Issuance of share capital | 462 | - | 462 | - |
| Other | - | (3) | - | (2) |
| Change in non-cash financing working capital (note 7) | (104) | (184) | (75) | (164) |
| | (7) | (24) | (2) | (48) |
| Foreign exchange gain on cash held in a foreign currency | (1) | 1 | 1 | 2 |
| Increase in cash and cash equivalents | 35 | 8 | 46 | 41 |
| Cash and cash equivalents, beginning of year | 80 | 84 | 69 | 51 |
| Cash and cash equivalents, end of year | $ 115 | $ 92 | $ 115 | $ 92 |
| **Supplementary cash flow information:** | | | | |
| Interest paid net of interest received | $ 90 | $ 66 | $ 143 | $ 117 |
| Income taxes paid net of income taxes recovered | 12 | 7 | 18 | 58 |

See accompanying notes to combined and consolidated financial statements.

1. **Basis of presentation:**

   These unaudited interim combined and consolidated financial statements of EPCOR Power Group (the Group) have been prepared in accordance with Canadian generally accepted accounting principles (GAAP) for interim financial statements and do not include all of the disclosures normally found in the Group's annual combined and consolidated financial statements.

   These combined and consolidated interim financial statements of the Group have been derived from the consolidated financial statements and accounting records of EPCOR Utilities Inc. (EPCOR), on a basis which maintains the historical operations and the historical measurement of assets and liabilities, and principally include the accounts of EPCOR Power Development Corporation, EPCOR Power Generation Services Inc., EMCC Limited and EPCOR PPA Management Inc, their subsidiaries, and their proportionate share of assets, liabilities, revenues and expenses of joint ventures. The assets, liabilities and operations of the Rossdale generation plant are excluded from the accounts of EPCOR Power Development Corporation as included in these combined and consolidated financial statements. The accounts of the Group's approximate 30.6% interest in EPCOR Power L.P. (Power LP), a publicly traded entity, are also included in these combined and consolidated interim financial statements. Under GAAP, the Group controls Power LP which therefore is a subsidiary of the Group. The comparative figures include, on a continuity of interests basis, the financial position, results of operations and cash flows of certain other entities within the EPCOR corporate group that, as a result of various transactions within the EPCOR corporate group, form all or part of the historical results of the companies combined to form the group as at June 30, 2009. These unaudited interim combined and consolidated financial statements may not necessarily reflect the Group's financial position, results of operations and cash flows in the future, nor what its financial position, results of operations and cash flows would have been had the Group been a stand-alone entity during the periods presented.

   Management believes the assumptions underlying these unaudited interim combined and consolidated financial statements are reasonable. These unaudited interim combined and consolidated financial statements should be read in conjunction with the Group's audited combined and consolidated financial statements for the year ended December 31, 2008 included in the Supplemented PREP Prospectus of Capital Power Corporation.

   All significant intercompany balances and transactions have been eliminated on combination and consolidation.

   These financial statements have been prepared following the same accounting policies and methods as those used in preparing the most recent annual combined and consolidated financial statements except for the changes in accounting policies as described in note 4.

2. **Nature of operations:**

   Interim results will fluctuate due to plant maintenance schedules, the seasonal demands for electricity, and changes in energy prices. Consequently, interim results are not necessarily indicative of annual results.

3. **Measurement uncertainty:**

   In accordance with Canadian GAAP, the Group uses estimates in preparing its combined and consolidated financial statements. Interim combined and consolidated financial statements necessarily employ a greater use of estimates than the annual combined and consolidated financial statements.

## 4. Changes in significant accounting policies:

### Goodwill and intangible assets

In February 2008, the CICA issued Handbook Section 3064 – Goodwill and Intangible Assets and consequential amendments to Section 1000 – Financial Statement Concepts. The new section establishes standards for the recognition, measurement and disclosure of goodwill and intangible assets. The provisions relating to the definition and initial recognition of intangible assets, including internally generated intangible assets, are equivalent to the corresponding provisions in International Financial Reporting Standards (IFRS). These amendments have been adopted by the Group commencing January 1, 2009 and have been applied retrospectively resulting in $11 million of net assets being reclassified from property, plant and equipment to contract and customer rights and other intangible assets in the comparative December 31, 2008 balance sheet. The Group's adoption of these amendments had no other material impacts on these interim combined and consolidated financial statements.

### Credit risk in determining fair value of financial assets and liabilities

On January 20, 2009 the Emerging Issues Committee of the CICA issued EIC-173, Credit Risk and the Fair Value of Financial Assets and Financial Liabilities, which clarifies that an entity's own credit risk and the credit risks of the counterparties should be taken into account in determining the fair value of financial assets and liabilities, including derivative instruments. Effective January 1, 2009, the Group adopted the recommendations of EIC-173 and applied the recommendations retrospectively without restatement of prior periods. On January 1, 2009, the Group made the following adjustments to the balance sheet in adopting the recommendations of EIC-173:

| Balance sheet item | | Increase (decrease) |
|---|---|---|
| Derivative instruments assets – non-current | $ | (1) |
| Derivative instruments liabilities – non-current | | (6) |
| Future income tax liabilities – non-current | | 1 |
| Non-controlling interests – balance sheet | | 3 |
| Opening retained earnings | | 1 |

### Future accounting changes

The CICA has announced that Canadian reporting issuers will need to begin reporting under IFRS, including comparative figures, by the first quarter of 2011. The Group is currently assessing the impact of the differences in accounting standards on the Group's future financial reporting requirements.

In June 2009, the CICA amended Handbook Section 3862 Financial Instruments – Disclosures, to adopt the amendments recently made by the International Accounting Standards Board to IFRS 7 Financial Instruments: Disclosures. The amendments require enhanced disclosures about fair value measurements, including the relative reliability of the inputs used in those measurements, and about the liquidity risk of financial instruments. Although the amendments apply to financial statements relating to fiscal years ending after September 30, 2009, comparative information is not required in the first year of application. The impacts of these amendments on the financial statements will be assessed and the necessary additional disclosures implemented commencing with the annual financial statements for 2009.

In January 2009, the CICA issued Handbook Section 1601 – Consolidated Financial Statements and Section 1602 - Non-controlling Interests, which replace Section 1600 – Consolidated Financial Statements. Section 1601 establishes the standards for the preparation of consolidated financial statements while Section 1602 establishes the standards for accounting for a non-controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination. Section 1602 is equivalent to the corresponding provisions of IFRS IAS 27 – Consolidated and Separate Financial Statements.

**4. Changes in significant accounting policies, continued:**

**Future accounting changes, continued**

Sections 1601 and 1602 will apply to interim and annual combined and consolidated financial statements relating to periods commencing on or after January 1, 2011. Earlier adoption is permitted as of the beginning of a fiscal year, provided Section 1582 – Business Combinations is also adopted at the same time. The impact of the new standards and the option to adopt them early will be assessed as part of the Group's IFRS conversion project.

In January 2009, the CICA issued Handbook Section 1582 – Business Combinations, which replaces Section 1581 – Business Combinations and provides the Canadian equivalent to IFRS 3 – Business Combinations. The section will apply on a prospective basis to future business combinations for which the acquisition date is on or after January 1, 2011. Earlier adoption is permitted as of the beginning of a fiscal year provided Sections 1601 – Consolidated Financial Statements and 1602 – Non-controlling Interests are also adopted at the same time. The impact of the new standard and the option to adopt it early will be assessed as part of the Group's IFRS conversion project.

**5. Long-term debt:**

Unsecured three-year credit facilities of $100 million each for a total of $300 million, committed to June 2010, September 2010, and October 2011, respectively, are available to the Group's subsidiary, Power LP. At June 30, 2009, the Group had $56 million in bankers' acceptances and $64 million (US$55 million) in U.S. LIBOR loans outstanding under this facility (December 31, 2008 - $23 million in bankers' acceptances and $64 million (US$52 million) in U.S. LIBOR loans) at an effective interest rate of 0.58% (December 31, 2008 – 1.09%).

**6. Non-controlling interests:**

Results of operations which relate to non-controlling interests are as follows:

| | **Three months ended June 30,** | | **Six months ended June 30,** | |
|---|---|---|---|---|
| | **2009** | **2008** | **2009** | **2008** |
| Non-controlling interests in Power LP .................................. | $ 30 | $ 67 | $ 6 | $ 103 |
| Preferred share dividends paid by subsidiary companies ...... | 1 | 1 | 3 | 3 |
| | $ 31 | $ 68 | $ 9 | $ 106 |

## 6. Non-controlling interests, continued:

Non-controlling interests reflected in the combined and consolidated balance sheets for the six months ended June 30, 2009 and the year ended December 31, 2008 consisted of:

| | June 30, 2009 | December 31, 2008 |
|---|---|---|
| Non-controlling interests in Power LP, beginning of year | $ 418 | $ 618 |
| Net income (loss) attributable to non-controlling interests | 6 | (58) |
| Other comprehensive loss attributable to non-controlling interests | (17) | (48) |
| Opening retained earnings adjustments attributable to non-controlling interests (note 4) | 3 | - |
| Distributions to non-controlling interests | (40) | (94) |
| Non-controlling interests in Power LP, end of period | 370 | 418 |
| Preferred shares issued by subsidiary companies, beginning and end of period | 122 | 122 |
| | $ 492 | $ 540 |

## 7. Change in non-cash working capital:

| | Three months ended June 30, | | Six months ended June 30, | |
|---|---|---|---|---|
| | 2009 | 2008 | 2009 | 2008 |
| Notes receivable | $ - | $ (71) | $ - | $ (2) |
| Accounts receivable | 47 | (9) | 109 | 116 |
| Income taxes recoverable | 1 | - | (4) | (1) |
| Inventories | 1 | (11) | 8 | (9) |
| Prepaid expenses | (4) | (5) | (2) | (4) |
| Notes payable | 49 | - | 73 | - |
| Accounts payable and accrued liabilities | (58) | 33 | (122) | (87) |
| Income taxes payable | (13) | (11) | (28) | (61) |
| | $ 23 | $ (74) | $ 34 | $ (48) |
| **Relating to:** | | | | |
| Operating activities | $ 34 | $ (7) | $ (20) | $ (10) |
| Investing activities | 93 | 117 | 129 | 126 |
| Financing activities | (104) | (184) | (75) | (164) |
| | $ 23 | $ (74) | $ 34 | $ (48) |

## 8. Fair value and classification of non-derivative financial assets and liabilities:

| Financial asset or liability | Classification | June 30, 2009 Carrying amount | June 30, 2009 Fair value | December 31, 2008 Carrying amount | December 31, 2008 Fair value |
|---|---|---|---|---|---|
| **Other assets** | | | | | |
| Investment in preferred shares of Primary Energy Recycling Holdings LLC (PERH) | Available for sale | $ 15 | $ 15 | $ 16 | $ 16 |
| Loans and other long-term receivables | Loans and receivables | 50 | 49 | 52 | 46 |
| Net investment in lease | Loans and receivables | 31 | 30 | 33 | 33 |
| Portfolio investments | Available for sale | 7 | 7 | 6 | 6 |
| **Long-term debt** (including current portion) | Other financial liabilities | 2,684 | 2,731 | 3,027 | 2,841 |

## 9. Derivative instruments and hedge accounting:

Derivative financial and non-financial instruments are held for the purpose of energy purchases, merchant trading or financial risk management.

The derivative instruments assets and liabilities used for risk management purposes consist of the following:

| | June 30, 2009 | | | |
|---|---|---|---|---|
| | Energy | | Foreign exchange | |
| | Cash flow hedges | Non-hedges | Non-hedges | Total |
| **Derivative instruments assets:** | | | | |
| Current | $ 12 | $ 126 | $ 2 | $ 140 |
| Non-current | 6 | 60 | 8 | 74 |
| **Derivative instruments liabilities:** | | | | |
| Current | (32) | (103) | (8) | (143) |
| Non-current | (11) | (35) | (18) | (64) |
| **Net fair value** | $ (25) | $ 48 | $ (16) | $ 7 |
| **Net notional buys (sells):** | | | | |
| Megawatt hours of electricity (millions) | - | (4) | | |
| Gigajoules of natural gas (millions) | - | 61 | | |
| Foreign currency (U.S. dollars) | | | $ (471) | |
| **Range of contract terms in years** | 0.1 to 7.5 | 0.1 to 7.4 | 0.1 to 6.5 | |

## 9. Derivative instruments and hedge accounting, continued:

| | December 31, 2008 | | | |
|---|---|---|---|---|
| | Energy | | Foreign exchange | |
| | Cash flow hedges | Non-hedges | Non-hedges | Total |
| **Derivative instruments assets:** | | | | |
| Current | $ 10 | $ 108 | $ 8 | $ 126 |
| Non-current | 9 | 62 | 4 | 75 |
| **Derivative instruments liabilities:** | | | | |
| Current | (31) | (88) | (11) | (130) |
| Non-current | (29) | (43) | (38) | (110) |
| Net fair value | $ (41) | $ 39 | $ (37) | $ (39) |
| **Net notional buys (sells):** | | | | |
| Megawatt hours of electricity (millions) | (2) | (2) | | |
| Gigajoules of natural gas (millions) | | 65 | | |
| Foreign currency (U.S. dollars) | | | $ (457) | |
| **Range of contract terms in years** | 0.1 to 8.0 | 0.1 to 8.0 | 0.1 to 6.0 | |

Unrealized and realized pre-tax gains and losses on derivative instruments recognized in other comprehensive income and net income were:

| | Three months ended June 30, | | | |
|---|---|---|---|---|
| | 2009 | | 2008 | |
| | Unrealized gains (losses) | Realized gains (losses) | Unrealized gains (losses) | Realized gains (losses) |
| Energy cash flow hedges | $ (7) | $ (6) | $ (4) | $ 37 |
| Energy non-hedges | 10 | (12) | 52 | (6) |
| Foreign exchange non-hedges | 34 | 4 | 5 | 3 |
| | **Six months ended June 30,** | | | |
| | **2009** | | **2008** | |
| | **Unrealized gains (losses)** | **Realized gains (losses)** | **Unrealized gains (losses)** | **Realized gains (losses)** |
| Energy cash flow hedges | $ 16 | $ (17) | $ 29 | $ 14 |
| Energy non-hedges | 9 | (32) | 96 | 7 |
| Foreign exchange non-hedges | 17 | - | (5) | 7 |

Realized gains and losses disclosed above relate only to financial derivative instruments. Realized gains and losses on non-financial derivative instruments are recorded in revenues or energy purchases and fuel, as appropriate.

**9. Derivative instruments and hedge accounting, continued**

The Group has elected to apply hedge accounting on certain derivatives it uses to manage commodity price risk relating to electricity prices. For the three and six months ended June 30, 2009, the ineffective portion of hedging derivatives required to be recognized in the income statement was nil (2008 - nil). Of the $18 million (December 31, 2008 - $29 million) of net losses related to derivative instruments designated as cash-flow hedges included in accumulated other comprehensive loss at June 30, 2009, net losses of $14 million (December 31, 2008 - $15 million), net of income tax recoveries of $6 million (December 31, 2008 - $7 million) are expected to settle and be reclassified to net income over the next twelve months. The Group's cash flow hedges extend up to 2016.

**10. Risk management:**

**Liquidity risk**

As at June 30, 2009, Power LP had undrawn and committed bank credit facilities, including operating lines of credit, of $222 million (December 31, 2008 - $213 million), with remaining terms ranging from two to three years.

Power LP has in place a Canadian universal shelf prospectus, which expires in August 2010, under which Power LP may raise up to $1 billion in partnership units or debt, of which a maximum of $600 million can be debt. At June 30, 2009, Power LP has not drawn on the shelf prospectus (December 31, 2008 – nil).

The following are the undiscounted cash flow requirements and contractual maturities of the Group's financial liabilities, including interest payments, as at June 30, 2009:

| | Due within 1 year | Due between 1 and 2 years | 2 and 3 years | 3 and 4 years | 4 and 5 years | Due after more than 5 years | Total contractual cash flows |
|---|---|---|---|---|---|---|---|
| **Non-derivative financial liabilities**: | | | | | | | |
| Long-term debt | $ 20 | $ 136 | $ 10 | $ 11 | $ 228 | $ 2,283 | $ 2,688 |
| Interest payments on long-term debt | 219 | 198 | 185 | 175 | 166 | 1,814 | 2,757 |
| Accounts payable and accrued liabilities [1] | 251 | | | | | | 251 |
| Loan commitments | 6 | | | | | | 6 |
| **Derivative financial liabilities:** | | | | | | | |
| Net forward foreign exchange contracts | 8 | 5 | 6 | 5 | 4 | 2 | 30 |
| Net commodity contracts-for-differences | 100 | 30 | 3 | 1 | - | - | 134 |
| Total | $ 604 | $ 369 | $ 204 | $ 192 | $ 398 | $ 4,099 | $ 5,866 |

[1] Excluding accrued interest on long-term debt of $56 million.

**11. Sale of power purchase arrangement and related transactions:**

In June 2006, the Group finalized an agreement to sell its Battle River Power Purchase Arrangement and its related interest in the Battle River Power Syndicate Agreement (Battle River PSA). The agreement resulted in the sale of 75% of the Battle River PSA through the year-ended December 31, 2008.

In January 2009, 10% of the Battle River PSA was sold. The transactions in the current and comparative periods are summarized as follows:

| | Six months ended June 30, | |
|---|---|---|
| | 2009 | 2008 |
| Cash proceeds from sale | $ 47 | $ 53 |
| Less net book value and costs of disposal | 17 | 19 |
| Gain on sale before income taxes | 30 | 34 |
| Less future income taxes | 4 | 4 |
| Gain on sale after income taxes | $ 26 | $ 30 |

Refundable taxes of $5 million (2008 - $6 million), which arose from the taxable capital gains on the sale of the Battle River PSA, have been charged to retained earnings.

The Group's remaining interest in the Battle River PSA will be disposed of on January 15, 2010. Since the final disposal will occur within one year of the balance sheet date, the remaining Battle River PSA assets on the combined and consolidated balance sheets have been retrospectively reclassified from power purchase arrangements to assets held for sale.

**12. Disposal of assets:**

On May 26, 2009, the Power LP completed the sale of its Castleton facility (Castleton). The disposition of Castleton resulted in proceeds of $12 million (US$11 million) and an accounting gain of $2 million recorded in revenues in the current quarter.

**13. Related party transactions and balances:**

In June 2009, as part of the reorganization steps for the creation of Capital Power (note 16), EMCC Limited issued two common voting shares to EPCOR for settlement of related party long-term debt of $330 million and notes payable of $132 million.

The remaining note payable to EPCOR at June 30, 2009 consists primarily of debt between EPCOR and EPCOR Power Development Corporation (EPDC).

**14. Guarantees:**

At June 30, 2009, on behalf of the Group's subsidiaries, EPCOR has issued letters of credit for $136 million (December 31, 2008 - $206 million) to meet the credit requirements of energy market participants, to meet conditions of certain service agreements, and to satisfy legislated reclamation requirements.

## 15. Geographic information:

| | Three months ended June 30, 2009 | | | |
|---|---|---|---|---|
| | Canada | U.S. | Inter-area eliminations | Total |
| Revenues – external | $ 439 | $ 98 | $ - | $ 537 |
| Inter-area revenues | 6 | - | (6) | - |
| Total revenues | $ 445 | $ 98 | $ (6) | $ 537 |

| | Three months June 30, 2008 | | | |
|---|---|---|---|---|
| | Canada | U.S. | Inter-area eliminations | Total |
| Revenues – external | $ 587 | $ 99 | $ - | $ 686 |
| Inter-area revenues | 17 | 1 | (18) | - |
| Total revenues | $ 604 | $ 100 | $ (18) | $ 686 |

| | Six months ended June 30, 2009 | | | |
|---|---|---|---|---|
| | Canada | U.S. | Inter-area eliminations | Total |
| Revenues – external | $ 1,032 | $ 214 | $ - | $ 1,246 |
| Inter-area revenues | 18 | 2 | (20) | - |
| Total revenues | $ 1,050 | $ 216 | $ (20) | $ 1,246 |

| | Six months ended June 30, 2008 | | | |
|---|---|---|---|---|
| | Canada | U.S. | Inter-area eliminations | Total |
| Revenues – external | $ 1,109 | $ 210 | $ - | $ 1,319 |
| Inter-area revenues | 27 | 5 | (32) | - |
| Total revenues | $ 1,136 | $ 215 | $ (32) | $ 1,319 |

## 16. Subsequent event:

### Creation of Capital Power

On May 8, 2009, EPCOR announced its plans to create Capital Power Corporation (Capital Power), a power generation company permanently headquartered in Edmonton, Alberta. Capital Power issued 21,750,000 common shares at $23 per share pursuant to its initial public offering (IPO) on July 9, 2009. Proceeds from the IPO net of underwriting commissions were approximately $475 million, of which approximately $468 million were used to purchase an approximate 27.8% equity interest in Capital Power L.P. (CPLP). EPCOR Power Group which is substantially all the power generation assets of EPCOR (see note 1) was purchased by CPLP on July 1, 2009 through the following series of transactions (the Reorganization):

- Formation of CPLP: Capital Power and a wholly-owned subsidiary of Capital Power (Capital Power LP Holdings Inc.) formed CPLP. Capital Power acquired one general partner unit (a GP Unit) and was the initial general partner of CPLP. Capital Power LP Holdings Inc. acquired one common limited partnership unit and as a result, became the initial limited partner in CPLP.

## 16. Subsequent event, continued:

- Sale of EMCC Limited to Capital Power: EPCOR transferred all of the outstanding common shares of EMCC Limited to Capital Power in return for payment of approximately $468 million in cash.
- Contribution of Assets by EMCC Limited to CPLP: EMCC Limited contributed substantially all of its assets (consisting primarily of certain securities of subsidiary entities, its class B shares in the capital of EPLP Investments Inc. and promissory note of EPLP Investments Inc.) to CPLP in return for GP Units. Capital Power transferred its GP Units in CPLP to EMCC Limited and as a result EMCC Limited became the general partner of CPLP.
- Sale of Assets by EPCOR Power Development Corporation (EPDC) to CPLP: EPDC transferred substantially all of its assets (consisting primarily of assets related to Genesee Units 1 and 2, the Genesee Coal Mine joint venture and certain interests in partnerships) to CPLP in return for 56.625 million exchangeable limited partnership units of CPLP and approximately $896 million in cash. CPLP financed the cash payment with the proceeds from a long-term debt obligation to EPCOR.

  Concurrently, EPDC subscribed for 56.625 million special voting shares of Capital Power for a nominal amount.

Immediately following completion of the Reorganization, Capital Power held approximately 27.8% of CPLP while EPCOR held 56.625 million exchangeable limited partnership units of CPLP (exchangeable for common shares of Capital Power on a one-for-one basis) representing approximately 72.2% of CPLP. Each exchangeable limited partnership unit is accompanied by a special voting share in the capital of Capital Power which entitles the holder to a vote at Capital Power shareholder meetings, subject to the restriction that such special voting shares must at all times represent not more than 49% of the votes attached to all Capital Power common shares and special voting shares, taken together. Capital Power and EPCOR have agreed that for so long as EPCOR holds not less than a 20% interest in the common shares of Capital Power, the number of directors will not be less than nine. The special voting shares also entitle EPCOR, voting separately as a class, to nominate and elect a maximum of four directors of Capital Power. There are currently twelve directors on Capital Power’s board of directors. Accordingly, Capital Power controls CPLP and, on that basis, the operations of CPLP will be consolidated by Capital Power for financial statement purposes.

Immediately following completion of the Reorganization, CPLP held 49% and EPCOR held 51% of the voting rights in EPLP Investments Inc. EPLP Investments Inc. owns the approximate 30.6% interest in EPCOR Power L.P. previously owned by EPCOR. However, CPLP is entitled to all of the economic interest in EPLP Investments Inc. Accordingly, effective early July 2009, Capital Power will consolidate the financial results of EPCOR Power L.P.

Capital Power has entered into various agreements with EPCOR to provide for certain aspects of the separation of the business of Capital Power from EPCOR, to provide for the continuity of operations and services and to govern the ongoing relationships between the two groups of entities.