

Financial Statements

**BROOKFIELD POWER CORPORATION**

December 31, 2006

## Auditors' Report

To the Shareholder of  
Brookfield Power Corporation

We have audited the balance sheets of Brookfield Power Corporation (the "Company") as at December 31, 2006 and 2005 and the statements of deficit, loss, and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2006 and 2005 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

*"Deloitte & Touche LLP"*

Chartered Accountants

Toronto, Canada  
February 6, 2007

**BROOKFIELD POWER CORPORATION**  
**BALANCE SHEETS**  
**As at December 31**

<i>thousands of CDN dollars</i>	Notes	2006	2005
<b>Assets</b>			
<b>Current assets</b>			
Cash		\$ 72	\$ 72
Accounts receivable and other		12	-
Interest receivable	4	4,095	1,072
Derivative asset	8	4,873	-
Promissory note from Brookfield Power Inc.	4	-	99,750
		<b>9,052</b>	100,894
<b>Promissory notes from Brookfield Power Inc</b>	4	<b>795,595</b>	447,360
<b>Deferred financing fees</b>	6	<b>5,346</b>	4,137
<b>Future income tax asset</b>	10	<b>1,216</b>	511
		<b>\$ 811,209</b>	\$ 552,902
<b>Liabilities and Shareholder's Deficit</b>			
<b>Current liabilities</b>			
Accounts payable and other		\$ 269	\$ 15
Interest payable		4,141	1,045
Due to related parties	5	4,325	2,483
Derivative liability	8	4,873	-
Current portion of long-term debt	7	-	100,000
		<b>13,608</b>	103,543
<b>Long-term debt</b>	7	<b>800,059</b>	450,232
		<b>813,667</b>	553,775
<b>Shareholder's deficit</b>	9	<b>(2,458)</b>	(873)
		<b>\$ 811,209</b>	\$ 552,902

*See accompanying notes to the financial statements*

APPROVED ON BEHALF OF BROOKFIELD POWER CORPORATION

/s/ Richard Legault  
Richard Legault  
Director

/s/ Harry A. Goldgut  
Harry A. Goldgut  
Director

**BROOKFIELD POWER CORPORATION**  
**STATEMENTS OF DEFICIT**  
**Year ended December 31**

<i>thousands of CDN dollars</i>	<b>2006</b>		2005	
Deficit, beginning of year	\$	<b>(873)</b>	\$	(33)
Net loss for the year		<b>(1,585)</b>		(840)
<b>Deficit, end of year</b>	<b>\$</b>	<b>(2,458)</b>	<b>\$</b>	<b>(873)</b>

*See accompanying notes to the financial statements*

**BROOKFIELD POWER CORPORATION**  
**STATEMENTS OF LOSS**  
Year ended December 31

<i>thousands of CDN dollars</i>	Notes	2006	2005
<b>Revenues</b>			
Interest	4	\$ 28,811	\$ 24,291
<b>Expenses</b>			
Interest	7	29,303	24,103
Amortization of deferred financing fees	6	1,506	1,429
Other		292	89
		<b>31,101</b>	<b>25,621</b>
		<b>(2,290)</b>	<b>(1,330)</b>
<b>Income tax (recovery) expense</b>			
Current		-	7
Future	10	(705)	(497)
		<b>(705)</b>	<b>(490)</b>
<b>Net loss</b>		<b>\$ (1,585)</b>	<b>\$ (840)</b>

*See accompanying notes to the financial statements*

**BROOKFIELD POWER CORPORATION**  
**STATEMENTS OF CASH FLOWS**  
Year ended December 31

<i>thousands of CDN dollars</i>	Notes	<b>2006</b>	2005
<b>Operating activities</b>			
Net loss		\$ (1,585)	\$ (840)
Items not affecting cash			
Amortization of deferred financing fees	6	1,506	1,429
Amortization of debenture premium	7	(59)	(61)
Amortization of note discounts	7	1	-
Derivative asset		(4,873)	-
Derivative liability		4,873	-
Future income taxes		(705)	(497)
		<b>(842)</b>	31
Net change in non-cash working capital			
Accounts receivable and other		(12)	-
Interest receivable	4	(3,023)	(90)
Accounts payable and other		254	(8)
Interest payable		3,096	86
		<b>315</b>	(12)
		<b>(527)</b>	19
<b>Investing activities</b>			
Repayment of promissory note	4	99,750	-
Purchase of promissory notes	4	(348,235)	(50,000)
		<b>(248,485)</b>	(50,000)
<b>Financing activities</b>			
Repayment of term debentures	7	(100,000)	-
Issuance of medium term notes	7	349,885	50,293
Due to related parties		1,842	1,231
Financing fees paid	6	(2,715)	(1,471)
		<b>249,012</b>	50,053
Increase in cash		-	72
Cash, beginning of year		72	-
<b>Cash, end of year</b>		<b>\$ 72</b>	<b>\$ 72</b>
<b>Supplementary information</b>			
Interest paid during year		\$ 26,266	\$ 24,078
Cash taxes paid		41	9

*See accompanying notes to the financial statements*

# **BROOKFIELD POWER CORPORATION**

## **NOTES TO FINANCIAL STATEMENTS**

**December 31, 2006**

(in thousands of CDN dollars, except otherwise specified)

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### **1. NATURE AND DESCRIPTION OF THE COMPANY**

Brookfield Power Corporation (the "Company") was incorporated under the laws of Ontario on June 20, 2002. The activities of the Company commenced on December 16, 2004, upon the issuance of the term debentures (see Note 7).

The Company is a wholly owned subsidiary of Brookfield Power Inc. ("BPI").

### **2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

#### **Basis of presentation**

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

The significant accounting policies are summarized below:

#### **Deferred financing fees**

Financing costs associated with the Company's credit facility and the long-term debt are capitalized as deferred financing fees and are amortized over the term of the financing.

#### **Premium on term debenture**

Premiums received on the issue of term debentures are deferred and amortized into income over the term of the debentures.

#### **Discounts on medium-term notes**

Discounts given on the issue of medium-term notes are deferred and amortized into income over the term of the notes.

#### **Income taxes**

Income taxes are calculated using the asset and liability method. Temporary differences between the carrying amount of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes give rise to future income tax assets and liabilities. These temporary differences are measured using the tax rates substantively enacted at the balance sheet date.

# BROOKFIELD POWER CORPORATION

## NOTES TO FINANCIAL STATEMENTS

December 31, 2006

(in thousands of CDN dollars, except otherwise specified)

### Use of estimates

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities, and the reported amounts of revenues and expenses during the period. During the years presented, management has made estimates and valuation assumptions in the determination of accruals, amortization and future income tax assets. Estimates are based on historical experience, current trends and various other assumptions that are believed to be reasonable under the circumstances. Actual results could differ from estimates.

### 3. FUTURE ACCOUNTING POLICY CHANGES

On January 27, 2005, the CICA issued three new accounting standards: Handbook Section 1530, Comprehensive Income; Handbook Section 3855, Financial Instruments – Recognition and Measurement; and Handbook Section 3865, Hedges. These standards will be effective on January 1, 2007. The impact of the implementation of these new standards on the Company's financial statements will result in long-term debt being presented at amortized cost rather than carrying value. The difference will be adjusted to the deficit as at January 1, 2007. The impact on the financial statements as of January 1, 2007 is expected to be as follows:

	December 31, 2006	January 1, 2007	Net Financial Impact
Long-term debt	\$ 800,000	\$ 795,131	\$ (4,869)
Deferred financing fees	5,346	535	(4,811)
Premium on term debentures	173	-	(173)
Discounts on medium-term notes	114	-	(114)
Shareholder's deficit	2,458	2,341	(117)

### 4. PROMISSORY NOTES

Issuer	Maturity	Interest rates	2006	2005
Brookfield Power Inc.	December 16, 2009	4.70%	<b>\$ 397,360</b>	\$ 397,360
Brookfield Power Inc.	December 18, 2006	BA Rate + 0.73%	-	99,750
Brookfield Power Inc.	December 16, 2009	4.70%	<b>50,000</b>	50,000
Brookfield Power Inc.	November 5, 2018	5.30%	<b>199,028</b>	-
Brookfield Power Inc.	November 5, 2036	5.89%	<b>149,207</b>	-
			<b>795,595</b>	547,110
Less current portion of promissory notes			-	(99,750)
			<b>\$ 795,595</b>	\$ 447,360



# BROOKFIELD POWER CORPORATION

## NOTES TO FINANCIAL STATEMENTS

### December 31, 2006

(in thousands of CDN dollars, except otherwise specified)

Interest on outstanding promissory notes is receivable on a semi-annual basis.

On November 1, 2006, BPI issued two promissory notes to the Company totalling \$348,235. On December 18, 2006, BPI repaid the \$99,750 promissory note which had matured.

The fair value of the promissory notes as at December 31, 2006 is \$799,452 (2005 - \$559,866) based on current market prices for investments with similar terms and risks.

Interest charged to BPI during the year was \$28,811 (2005 - \$24,291), of which \$4,095 (2005 - \$1,072) is classified as interest receivable as at December 31, 2006.

#### 5. RELATED PARTY TRANSACTIONS

A net payable of \$4,325 (2005 - \$2,483) due to BPI and its wholly owned subsidiaries is included in current liabilities. These amounts are non-interest bearing, unsecured and are due on demand.

#### 6. DEFERRED FINANCING FEES

The Company has incurred \$8,328 (2005 - \$5,613) of financing fees which have been deferred and are being amortized over the term of the underlying financing. Accumulated amortization at December 31, 2006 is \$2,982 (2005 - \$1,476).

#### 7. LONG-TERM DEBT

	Maturity	Interest Rates	2006	2005
Term Debentures				
Series 1	December 16, 2009	4.65%	\$ 450,000	\$ 450,000
Series 2	December 18, 2006	CDOR +68 bps	-	100,000
Unamortized premium on Series 1			173	232
			<b>450,173</b>	550,232
Medium-Term Notes				
Series 3	November 5, 2018	5.25%	200,000	-
Series 4	November 5, 2036	5.84%	150,000	-
Unamortized discount on Series 3			(71)	-
Unamortized discount on Series 4			(43)	-
			<b>800,059</b>	550,232
Less current portion of term debentures			-	(100,000)
			<b>\$ 800,059</b>	\$ 450,232

# **BROOKFIELD POWER CORPORATION**

## **NOTES TO FINANCIAL STATEMENTS**

### **December 31, 2006**

(in thousands of CDN dollars, except otherwise specified)

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The \$100,000 Series 2 term debentures matured and were repaid on December 18, 2006.

The total premium amortized to interest expense during the year ended December 31, 2006 was \$59 (2005 - \$61). The total discount amortized to interest expense during the year ended December 31, 2006 was \$1 (2005 - \$nil).

The medium-term notes were issued by the Company on November 1, 2006. Both notes are unsecured, rank pari passu with all other existing debt, and have semi-annual interest payments.

The fair value of the Company's long-term debt is \$802,184 as at December 31, 2006 (2005 - \$554,203) based on current market prices.

The debentures and notes are unconditionally guaranteed by BPI as to the payment of principal, premium, if any, and interest.

#### **8. DERIVATIVE FINANCIAL INSTRUMENTS**

The Company has entered into forward-starting interest rate swap agreements with major financial institutions on behalf of other subsidiaries of BPI that do not currently maintain the necessary credit facilities to execute agreements of this nature. The agreements, which have a notional amount totalling \$300 million, are intended to lock in a fixed interest rate on the anticipated issuance of long-term debt to finance the wind power facility operating in Northern Ontario.

On the same date, the Company entered into offsetting forward-starting interest rate swap agreements with the subsidiaries of BPI that anticipate issuing the fixed rate debt. As a result of these offsetting positions, the Company will pay to or receive from its related parties amounts that exactly offset its rights and obligations under the forward-starting interest rate swaps with the third party financial institutions.

As of December 31, 2006, the fair value of the swaps with third parties of (\$4.9) million was recognized as a derivative liability with the corresponding loss reflected in net loss. At the same time, the fair value of the swaps with related parties of \$4.9 million was recognized as a derivative asset with the corresponding gain reflected in net loss. The net impact of the mark-to-market of all swaps on the Company's net loss for the year was \$nil.

#### **9. SHAREHOLDER'S EQUITY**

The Company is authorized to issue an unlimited number of common shares. As at December 31, 2006 and 2005 there is 1 common share issued and outstanding.

# BROOKFIELD POWER CORPORATION

## NOTES TO FINANCIAL STATEMENTS

December 31, 2006

(in thousands of CDN dollars, except otherwise specified)

### 10. INCOME TAXES

The Company's future income tax asset of \$1,216 (2005 - \$511) is comprised of temporary differences relating to deferred finance fees net of unused non-capital losses. The difference between taxes calculated at the statutory rate and those recorded is reconciled as follows:

	<b>2006</b>	2005
Net loss before income tax	\$ (2,290)	\$ (1,330)
Statutory income tax rate	<b>36%</b>	36%
Statutory income tax rates applied to accounting income	<b>(824)</b>	(479)
Impact of rate change	<b>72</b>	-
Other	<b>47</b>	(11)
Income tax recovery	\$ <b>(705)</b>	\$ (490)

The Company has \$4,305 (2005 - \$1,892) in non-capital losses which expire as follows:

2014	\$ <b>820</b>
2015	<b>1,072</b>
2026	<b>2,413</b>
	<b>\$ 4,305</b>

These losses will be available to offset taxable income in future years and have been recorded as a future income tax asset.

### 11. CREDIT FACILITY

The Company has a US \$350,000 revolving unsecured credit facility for general corporate purposes which can be drawn upon in Canadian or US dollars. The credit facility is due in April 2009 and ranks pari passu with all senior unsecured indebtedness of the Company and BPI. The facility bears a floating interest rate and is unconditionally guaranteed by BPI. The guarantee will remain in place until such time as certain conditions with respect to its release are met. As at December 31, 2006, there were no direct borrowings under this credit facility but the Company has issued letters of credit totalling USD \$117,082 (2005 – USD \$130,084) under this credit facility.

# **BROOKFIELD POWER CORPORATION**

## **NOTES TO FINANCIAL STATEMENTS**

### **December 31, 2006**

(in thousands of CDN dollars, except otherwise specified)

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#### **12. COMMITMENTS, CONTINGENCIES AND GUARANTEES**

In the normal course of operations, the Company executes agreements that provide for indemnification and guarantees to third parties in transactions such as debt issuances. The nature of substantially all of the indemnification undertakings prevents management from making a reasonable estimate of the maximum potential amount the Company could be required to pay third parties as the agreements do not specify a maximum amount and the amounts are dependent upon the outcome of future contingent events, the nature and likelihood of which cannot be determined at this time.

#### **13. FINANCIAL INSTRUMENTS**

##### **Financial instruments**

The carrying amount of financial instruments included in current assets and current liabilities approximate fair value due to their short-term nature.

##### **Credit risk**

The Company is exposed to credit-related losses in the event of non-performance by a counterparty, BPI. BPI has investment grade issuer ratings, which significantly reduces the Company's credit risk.

##### **Interest rate risk**

The Company is not exposed to interest rate risk due to the fact that all long-term debt bears interest at fixed rates.