



balancingpool

2009 ANNUAL REPORT



THE BALANCING POOL

GENERATING VALUE FOR ALBERTA'S CONSUMERS



The Balancing Pool was established in 1998 by the Government of Alberta to help manage the transition to competition in Alberta's electric industry. Our current obligations and responsibilities are governed by the *Electric Utilities Act* (effective June 1, 2003) and the *Balancing Pool Regulation*.

Our legislated duties include:

- To manage generation assets in a commercial manner, specifically any Power Purchase Arrangements (PPAs) held by the Balancing Pool that include the right to exchange electric energy and ancillary services, and any arrangements or agreements derived from these assets;
- To hold the Hydro PPA and manage associated payments;
- To forecast revenues and expenses (incorporating estimates of Pool price volatility and potential expenses related to risk backstop activities) and allocate the forecast surplus or deficiency as evenly as possible through a Consumer Allocation or charge;
- To participate in appropriate regulatory, dispute resolution and other proceedings and processes to protect the interests of the Balancing Pool and the value of its assets; and
- To manage risks prudently in all aspects of its operations.

PPAs are one of the mechanisms used by the Government of Alberta to introduce competition into the supply of thermal electric power from regulated generating units. The PPAs were auctioned in 2000 and provide buyers with the rights to formerly regulated generating capacity. The Balancing Pool assumed the unsold Sheerness, Genesee and Clover Bar PPAs. Through a number of contracts that covered periods to 2006, the Balancing Pool transferred electricity capacity and ancillary services associated with these generation assets into the hands of market participants.

The Balancing Pool may sell the Genesee PPA when market conditions are such that a competitive sale will result in the Balancing Pool receiving fair market value, or may terminate a PPA when it proves to be uneconomical. In 2005 the Balancing Pool sold the Sheerness PPA to TransCanada Energy Ltd. and terminated the uneconomical Clover Bar PPA.

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STAKEHOLDER RECEPTION

Monday, May 10, 2010
4:00 p.m. to 7:00 p.m.

Centini Restaurant
160 – 8th Avenue S.E.
Calgary, Alberta



MESSAGE TO STAKEHOLDERS FROM THE BOARD CHAIR

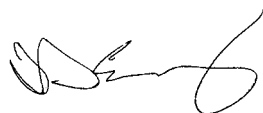
Balancing Pool cash flows were affected in 2009 by significantly softer electricity prices in Alberta, and we expect these market conditions to continue into 2010. Our cash flows provide us the basis to set the annual Consumer Allocation, which has paid out more than \$830 million from 2006 to 2009.

Strong cash flows in 2008 allowed us to set the allocation for 2009 at \$6.50 per megawatt hour (MWh) or more than \$340 million—a healthy rebate for consumers despite the soft market conditions. In 2009 we reduced the allocation to \$4 per MWh for 2010 due to lower electricity price forecasts.

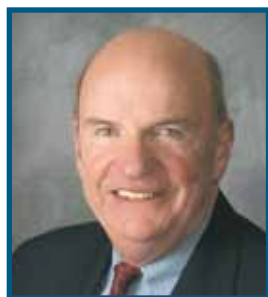
In 2009 the Balancing Pool introduced two new members to our Board: Mary Ritchie FCA and Rafi G. Tahmazian. These new members bring extensive backgrounds in the energy industry and financial markets, complementing the skills and experience of our existing Board members. This year the Balancing Pool's Board and management will focus on reviewing our long-term strategy to ensure we continue to generate value for Alberta's electricity consumers.

New Provincial Government legislation passed in 2009 has removed specific reference to June 30, 2021 as a wind-up date for Balancing Pool operations. This change provides flexibility in dealing with our legislated duties in the future. Otherwise our mandate is unchanged.

We look forward to working with the Honorable Ronald Liepert, the new Minister of Energy, who oversees the Balancing Pool's operations. Our Board and staff appreciate the opportunity of working co-operatively with government officials and stakeholders in managing the assets we hold on behalf of Alberta's consumers.



Thomas Cumming
Chair



Thomas Cumming

"This year the Balancing Pool's Board and management will focus on reviewing our long-term strategy to ensure we continue to generate value for Alberta's electricity consumers."



GOVERNANCE OF THE BALANCING POOL

Adhering to the *Electric Utilities Act (2003)*, the Minister of Energy must appoint as members of the Balancing Pool not more than nine individuals who are independent of any person who has a material interest in the Alberta electric industry. Members are appointed by the Minister on the basis of their cumulative expertise in order to enhance the performance of the Balancing Pool in exercising its powers and carrying out its duties, responsibilities and functions. The term of office of a member is three years; a member is eligible to be appointed for a maximum of three terms of office.



Thomas Cumming, Chair, was previously a member of the Power Pool Council, and served as the Market Surveillance Administrator from 2000 to 2003. Tom is also a Director of Pengrowth Corporation. From 1988 to 2000, he was the President and CEO of the Alberta Stock Exchange. Prior to that, he spent 24 years with the Bank of Nova Scotia in Canada, Ireland and England. Tom has a Bachelor of Applied Science degree in Engineering and Business and has been designated a life member of the Association of Professional Engineers, Geologists and Geophysicists of Alberta.



Peter Flynn held the Poole Chair in Management for Engineers in the Department of Mechanical Engineering at the University of Alberta. Peter's experience includes senior executive positions in leading telecommunications, energy and industrial management companies. He also has served as Director on several corporate and community boards, including the Board of EPCOR Utilities Inc. for 10 years and Plutonic Power Corporation. Peter holds a Ph.D. in Chemical Engineering from the University of Alberta.



Mary Ritchie is President and Chief Executive Officer of Richford Holdings Ltd. an accounting and investment advisory services firm. She is a member of the Board of Directors and Audit Committees of Industrial Alliance Insurance and Financial Services Inc. and Alaris Royalty Corp. She is also a member of the Board of Governors and Chairman of the Audit Committees of RBC Funds Inc. and RBC Advisor Global Fund Inc., as well as a member of the Independent Oversight Committee for RBC Funds and Phillips Hager & North. Mary is a fellow of the Canadian Institute of Chartered Accountants (FCA) and recently completed two terms as a member of the Institute's Accounting Standards Oversight Council.



Rafi G. Tahmazian has more than 20 years of experience in the energy sector and financial services industry. He is currently a Managing Director of Canoe Financial LP and holds positions as both director and advisory board member of several private resource entities and energy-specific investment funds. After positions with First Marathon Securities and LL&E Canada, Rafi was a partner from 1996 to 2008 at First Energy Capital Corp., where he also held the positions of Vice-Chairman and Managing Director. He has a Bachelor of Economics from the University of Calgary.



Stella Thompson, a co-founder and principal of Governance West Inc. from 1996 to 2008, has wide-ranging board experience and currently serves on the Boards of Atomic Energy of Canada Ltd., Calgary Airport Authority, Genome Alberta, the Provincial Audit Committee, Reservlogix Corp., and Talisman Energy Inc. She was involved in the deregulation of energy commodities from the early days as a Vice-President at Petro-Canada and has extensive experience in many aspects of the oil and gas and electricity industries. Stella previously served on the Board of ENMAX Corporation for five years. She has a Masters degree in Economics and has been awarded the designation of ICD.D by the Institute of Corporate Directors.

The Balancing Pool's Audit and Finance Committee is chaired by Dr. Flynn, and the Governance and Human Resources Committee is chaired by Ms. Thompson.



REPORT FROM THE PRESIDENT AND CEO

“The Balancing Pool’s Board members, management team and staff manage and meet a wide range of obligations on behalf of Alberta’s electricity consumers.”



Gary Reynolds

Among the Balancing Pool’s obligations on behalf of Alberta’s electricity consumers is the management of cash flows related to the Power Purchase Arrangements (PPAs) we hold. In 2009 these cash flows were significantly impacted by softer electricity prices in Alberta. Net cash flows from PPAs in 2009 were \$101 million, as compared to more than \$425 million in 2008.

The major source of Balancing Pool cash flows are from the Genesee and Hydro PPAs which together are comprised of approximately 950 megawatts (MW) of electricity capacity and ancillary services. We continue to sell this capacity into the spot and forward energy markets in a competitive manner.

Electricity prices in Alberta dropped by approximately 47% from 2008 averages to average about \$47 per megawatt hour (MWh) in 2009. A combination of lower natural gas prices, extra supply coming onto the grid, and flat year-over-year average energy demand were the primary fundamentals that contributed to the softening of prices. We anticipate that these market conditions will continue in 2010.

Overview of Balancing Pool Inflows and Outflows

The accompanying chart gives an overview of 2009 cash flows from the PPA assets, other revenues, as well as primary expenditures. At the end of 2009, the Balancing Pool had net revenues of some \$331 million and managed more than \$1.7 billion in assets on behalf of Alberta’s electricity consumers.



Impact of Cash Flows on the Consumer Allocation

With anticipated softer electricity prices, and in turn expected lower Balancing Pool cash flows, we reduced the 2010 Consumer Allocation from the 2009 high of \$6.50 per MWh of consumption.

As noted in our Chair's message, consumers in 2009 benefited by more than \$340 million in allocations despite the soft market conditions. Approximately 80% of the allocation goes to commercial and industrial electricity consumers, and the remainder to the residential and farm sectors.

The Balancing Pool announced in 2009 that the allocation to power consumers in 2010 would be \$4.00 per MWh of consumption. The table below summarizes the Consumer Allocations since the Balancing Pool began making payments. PPA sale proceeds, revenues from sales of assets, contracts for energy capacity and ancillary services, and investment income have all contributed to the annual allocations. In 2001 as the province made the transition to competition in Alberta's electric industry, the Balancing Pool also paid out more than \$2 billion to consumers in a rebate program based on PPA auction proceeds and other related revenues.

Summary of Consumer Allocations 2006 – 2009		
Year	\$/MWh	(thousands of dollars) Total
2006	1.00	53,814
2007	3.00	161,704
2008	5.00	271,444
2009	6.50	343,729
Total		830,691

We anticipate Alberta's consumers will continue to benefit from positive allocations into the future from cash flows generated by the Genesee and Hydro PPAs. Our legislated requirement under the *Electric Utilities Act (2003)* is to allocate any forecasted cash surplus to consumers on an annual basis. The forecast is determined by current power prices, future price expectations, decommissioning costs and potential costs associated with PPAs.

Recovery within Our Investment Portfolio

In 2009 we saw a recovery of 16% in our investment portfolio as compared to our 2008 equity position which was impacted by a severe worldwide global recession. The Balancing Pool portfolio enjoyed strong Canadian equity returns in addition to a stable capital recovery from international equities.

At year-end, the total funding of the investment portfolio and money market was \$828 million.

The asset mix allocation within the investment portfolio is as follows:

	Asset Mix	Balances at Year-End
Cash and Money Market	3%	\$27 million
Fixed Income	42%	\$346 million
Canadian Equities	27%	\$226 million
Non-Canadian Equities	28%	\$229 million
Total		\$828 million

Our investment strategy is reviewed on a regular basis by the Board, and is based on prudent investment standards and generally focuses on achievement of a fair return on investments with diversification of the portfolio to reduce risk. The performance of all external Investment Managers is reviewed on a regular basis.

Decommissioning and Reclamation Activities

The Balancing Pool has monetary obligations related to decommissioning and reclamation activities associated with legacy-regulated generating units. In 2009 costs were incurred with respect to decommissioning work on the Wabamun generating plant as well as at various Isolated Generation sites throughout Alberta.

In 2009 we completed our obligations related to the decommissioning and related reclamation of Wabamun plant Units 1, 2 and 3. Under the terms of the Wabamun Negotiated Settlement Agreement, the Balancing Pool was actively involved in this undertaking during 2007 – 2009 to ensure costs were reasonable and in compliance with the agreement. The Balancing Pool directed more than \$5.6 million in 2009 to complete the work, for a total Balancing Pool contribution of approximately \$12 million. Work was completed on schedule and on budget.

In 2009 the Balancing Pool provided \$5 million to ongoing reclamation costs for former Isolated Generation sites in Alberta. Since 2003 the Balancing Pool has paid over \$62 million for remediation of the Isolated Generation sites. To complete the remediation we expect to pay an additional \$24 million for the five remaining ATCO Electric locations. The costs of the reclamation are reviewed by a review committee consisting of consumer groups. Work is expected to continue into 2012.

Genesee Environmental Obligations

The Balancing Pool has ongoing environmental obligations related to our management of the Genesee PPA. These costs include expenditures to meet provincial greenhouse gas reduction regulations that require Alberta facilities that emit more than 100,000 tonnes of greenhouse gases a year to reduce emissions intensity by 12%.

In 2007 we began to make annual payments for greenhouse gas compliance of approximately \$5 million. In order to satisfy our compliance obligations under the regulation, we utilize both offset credits and payments to the Climate Change and Emissions Management Fund. We estimate additional expenditures of more than \$55 million to meet the regulatory requirements through 2020 under the Genesee PPA.

The Balancing Pool also funded a capital project to ensure regulatory compliance related to mercury reduction which includes activated carbon injection and continuous emissions monitoring equipment associated with the Genesee PPA. In 2009 these costs amounted to \$3 million; estimated costs for 2010 are \$1 million.

Contractual Matters

We continued to fulfill our mandated responsibilities in assessing and resolving claims of force majeure from PPAs. In 2009 we were involved in arbitration related to a 2007 force majeure claim associated with the Battle River PPA as well as contractual matters related to the Hydro PPA. We expect these matters to be resolved in 2010.

Our Long-Term Strategy

Our priorities for the future are to continue to maintain and generate value for Alberta's consumers—through sound management of our PPAs, prudent investment strategy, and effective risk management. As noted in our Chair's report, the Board and our management team will be updating our long-term strategy in 2010 to continue to meet these priorities.

I would like to thank our Board members, our management and staff, government officials and agencies, and stakeholders for their contributions and support of our work.



Gary Reynolds

President and Chief Executive Officer



Management's Discussion and Analysis

Year ended December 31, 2009



MANAGEMENT'S DISCUSSION AND ANALYSIS

This Management's Discussion and Analysis ("MD&A"), dated March 23, 2010, should be read in conjunction with the audited financial statements of the Balancing Pool for the years ended December 31, 2009 and 2008. The Audit and Finance Committee reviewed the contents of the MD&A and recommends its approval to the Board.

Results at a Glance

<i>Year ended December 31 (thousands of dollars)</i>	2009	2008
Revenues and funding	331,258	706,679
Operating Income	57,453	467,293
Net results of operations and comprehensive income	(12,280)	219,778
Consumer Allocation	343,729	271,444
Net change in cash, cash equivalents and investments	(98,320)	(20,299)
Cash, cash equivalents and investments	828,310	926,630
Ending deferral account balance	969,363	1,325,372
Total assets/liabilities	1,797,656	2,179,450
<i>Other Information</i>		
Total Volumes (gigawatt hours [GWh])	8,000	7,600
Average Pool price per megawatt hour (MWh)	\$47.81	\$89.95

Operations

Revenues and Funding

Details of Revenues and Funding (thousands of dollars)	2009	2008
Sale of electricity – Genesee power purchase arrangement	337,441	522,627
Hydro power purchase arrangement (PPA)	11,415	139,500
Investment income – Interest and dividends	30,391	32,135
Investment income – Realized gains (losses) on sale of investments	(66,186)	(6,945)
Payments in lieu of taxes (PILOT)	18,197	19,362
Total revenues and funding	331,258	706,679

Change in Cash, Cash Equivalents and Investments

<i>(thousands of dollars)</i>	2009	2008
Operations (excluding items listed below)	143,214	404,538
Investment income – Interest and dividends	30,391	32,135
Investment net gains (losses)	71,804	(185,528)
Consumer Allocation	(343,729)	(271,444)
Net change in cash, cash equivalents and investments	(98,320)	(20,299)

Sale of Electricity – Genesee Power Purchase Arrangement

Revenue from the sale of electricity under the Genesee Power Purchase Arrangement (“PPA”) decreased in 2009 versus 2008 by \$185.2 million largely as a result of decreased pricing year-over-year. Annual average Pool prices dropped year-over-year by approximately 47%. 2009 electricity sales include \$42.7 million (2008 – \$22.6) realized gains on forward sales transactions; during 2009, 33% of total electricity sales volumes were sold at fixed prices with use of forward sale transactions.

Hydro Power Purchase Arrangement (“PPA”)

Revenue from the Hydro PPA represents annual accretion of the value of the Hydro PPA asset, the difference between the actual cash receipts or payments and the estimated cash receipts or payments used in the valuation of the Hydro PPA asset at the beginning of the year. Hydro PPA revenues decreased in 2009 versus 2008 by \$128.1 million as a result of market price decreases as discussed above.

Investment Income (Loss)

a) Interest and Dividends

Details of Investment Income – Interest and Dividends <i>(thousands of dollars)</i>	2009	2008
Interest income	19,532	18,557
Dividend income	12,064	15,186
Fund management fees	(1,205)	(1,608)
Total investment income	30,391	32,135

Investment income resulted from continued investment of surplus cash flows from operations during 2009. The year-over-year decrease in investment income of \$1.7 million is primarily as a result of:

- a \$1.0 million increase in interest income, due to additional Fixed Income investments;
- a \$3.1 million decrease in dividend income resulting from reduced investments in equity securities during 2009.

b) Realized Gains and Losses on Sale of Investments

During 2009, the Balancing Pool sold investments having an original book value of \$154.1 million. Net proceeds from these sales were \$87.9 million and capital losses of \$66.2 million (2008 – \$6.9 million) were realized. The sale of investments occurred in order to reallocate a portion of the investment portfolio to higher performing investment managers.

Payments In Lieu of Tax (“PILOT”)

During 2009, the Balancing Pool received PILOT instalments from the ENMAX group of companies, City of Medicine Hat and City of Lethbridge. Net funding from payments in lieu of tax (“PILOT”) in 2009 was \$18.2 million as PILOT instalment receipts of \$36.8 million (2008 – \$43.0 million) were offset by PILOT refunds and audit costs relating to prior tax years of \$18.6 million (2008 – \$23.7 million). PILOT are based on the taxable income of a municipal entity as defined in the *Payment in Lieu of Tax Regulation of the Act* and are subject to audit by Alberta Revenue. PILOT received in the current year are instalments of 2009 taxes net of adjustments for prior years.

Expenses

Details of Expenses <i>(thousands of dollars)</i>	2009	2008
Cost of sales	230,210	218,618
Amortization and depreciation	19,703	19,715
Office of the Utilities Consumer Advocate	6,268	4,000
General and administrative	2,737	2,522
Other power purchase arrangement expenses	2,146	3,270
Small Power Producer contracts	12,741	(8,739)
Total expenses	273,805	239,386

Cost of Sales

Cost of sales includes PPA capacity payments, variable operating costs, and transmission charges relating to the Genesee PPA. The increase in cost of sales from 2008 of \$11.6 million is due to increased energy and incentive payments offset by lower transmission costs. PPA capacity payments which represent more than 90% of costs of sales vary year-over-year as a result of changes in indices and pass-through charges. Changes to Pool price have a minimal impact on the PPA capacity payments.

Office of the Utilities Consumer Advocate (“UCA”)

The Balancing Pool is obligated to make certain payments as directed by the Minister of Energy which are included in Office of the Utilities Consumer Advocate. The Balancing Pool is responsible for 80% of the UCA costs. In 2009, the Balancing Pool accrued \$6.3 million (2008 – \$4.0 million), as directed by the Minister of Energy.

Small Power Producer Contracts

Under the *Independent Power and Small Power Regulation*, the Balancing Pool is required to make monthly payments to TransAlta Utilities Corporation (“TransAlta”), the utility that administers the Small Power Producer contracts, for the amount by which the Pool price falls below the contracted price for Small Power Producers. If the Pool price is above the contracted price, TransAlta makes a payment to the Balancing Pool. In 2009, the Balancing Pool recorded net expenses of \$12.7 million (2008 – \$8.7 million net revenues), which represents annual accretion of the value of the Small Power Producer contracts and the difference between the actual Pool price and the Pool price used to value the Small Power Producer contracts at the beginning of the year. Annual average Pool prices dropped year-over-year by approximately 47% which had a significant impact on Small Power Producer contract results.

In November 2009, TransAlta acquired Canadian Hydro Developers, Inc. and as a result the Balancing Pool no longer has responsibilities for five of the Small Power Producer contracts. At December 31, 2009 there are 10 contracts subject to the *Independent Power and Small Power Regulation* (December 31, 2008 – 15).

Other Income (Expense)

Details of Other Income (Expense) (thousands of dollars)	2009	2008
Revaluation of Hydro power purchase arrangement	(174,328)	(46,214)
Revaluation of Small Power Producer contracts	(41,445)	–
Reclamation and abandonment	1,742	(5,900)
Unrealized gains (losses) on financial investments	137,990	(178,583)
Unrealized change on financial derivative instruments	6,872	(21,141)
Other income (expense)	(564)	4,323
Total other income (expense)	(69,733)	(247,515)

Revaluation of Hydro Power Purchase Arrangement

The Hydro PPA asset is recorded as a financial instrument calculated as the net present value of estimated cash receipts based on notional energy and reserve (ancillary service) volumes using management's best estimate of Pool price forecast, less PPA obligations over the remaining term of the PPA to 2020. The value of the Hydro PPA is estimated annually. The year-end valuation of the Hydro PPA resulted in a \$174.3 million (2008 – \$46.2 million) revaluation loss. Estimated forward market Pool prices used in the net present value model dropped by approximately 20% from 2008 to 2009 and the discount rate of 4% (2008 – 6%) was reduced to reflect lower market interest rates.

In 2009 the Balancing Pool received, net of PPA obligations and settlement of derivative contracts, \$51.1 million (2008 – \$176.8 million). The Hydro PPA receipts are the amount by which notional energy and reserve (ancillary service) volumes priced at Pool prices exceed PPA obligations. In 2009 there was no hedging activity related to the Hydro PPA (2008 – \$nil).

Revaluation of Small Power Producer Contracts

The Small Power Producer contracts are recorded as a financial instrument calculated as the net present value of payments or receipts based on the difference between the Small Power Producers' contract price and management's best estimate of Pool price forecast. The value of the Small Power Producer contracts asset or liability is estimated annually. The year-end valuations for 2009 were a net liability of \$41.4 million and 2008 \$nil, therefore the valuation adjustment during 2009 was recorded as a loss of \$41.4 million.

In 2009 the Balancing Pool paid \$12.7 million (2008 – received \$8.7 million) under these contracts. An amount paid or received by the Balancing Pool in a given year depends upon the difference between the contract price for the Small Power Producer and the Power Pool price. Estimated forward market Pool prices used in the net present value model dropped by approximately 20% from 2008 to 2009 and the discount rate of 4% (2008 – 6%) was reduced to reflect lower market interest rates.

Reclamation and Abandonment

The reclamation and abandonment provision reflects a reduction of \$1.7 million (2008 – provision of \$5.9 million) due to lower actual costs of decommissioning at Wabamun. In 2009 reclamation and abandonment expenditures were \$10.6 million (2008 – \$12.0 million). During 2009 the Balancing Pool concluded decommissioning for the Wabamun plant with cumulative costs of \$12.4 million incurred from 2008 to 2009.

Gains and Losses on Financial Investments

The economic environment in the second half of 2008 proved challenging as much of the global economy was affected by the global credit crisis. Global markets experienced sharp declines and the valuation of investments at December 31, 2008 resulted in an unrealized loss of \$185.5 million (unrealized losses of \$178.6 million and realized losses of \$6.9 million) which reflects the impact of these financial market issues. During 2009, there was a recovery in the financial markets resulting in reversals of unrealized losses in the amount of \$71.8 million (unrealized gains of \$138.0 million net of realized losses of \$66.2 million).

Unrealized Change on Financial Derivatives

During 2009 the Balancing Pool realized \$42.7 million (2008 – \$22.6 million) on net settlements of financial derivatives and at the end of the year has \$7.6 million in recorded unrealized gains related to forward swaps in place at December 31, 2009.

Assets

Cash and Cash Equivalents

Cash and cash equivalents decreased by \$148.3 million during the year, resulting in an ending balance of \$27.4 million.

Investments

The Balancing Pool continued to invest in fixed-income securities, Canadian and global equities in 2009.

The Balancing Pool's Board has approved a long-term investment strategy to manage the investment funds. The investment strategy is based on prudent investment standards and generally focuses on achievement of a fair return on investments with diversification of the portfolio to reduce risk. The major sources of our investment income include interest, capital gains and dividend income. The strategy, reviewed on a regular basis by the Board, is proving to be effective in meeting our objectives of attaining a fair return over the long-term.

The ranges for asset allocation within the investment portfolio are as follows:

Fixed Income	35-45%
Canadian Equities	25-35%
Global Equities	20-40%

Property, Plant and Equipment

The Genesee PPA is accounted for as an asset acquired by capital lease. At December 31, 2001, based on estimated future electricity market prices at the time, the net book value of the Genesee PPA was written down. At December 31, 2009, the net book value of property, plant and equipment was \$216.4 million (2008 – \$236.1 million). The decline in the net book value from 2009 reflects current year amortization of the Genesee PPA and other assets.

Deferred Charges

Deferred charges include \$10.6 million of amounts with respect to commercial disputes with TransAlta Utilities Corporation ("TransAlta") under the Hydro PPA and \$4.6 million with respect to a claim of force majeure relief from the owner of the Battle River PPA. These issues are in the dispute resolution process and expected to conclude in 2010. Until the claim is resolved, these amounts will be recorded as a deferred charge. Deferred charges are carried net of a \$2.3 million provision for doubtful deferred charges.

Hydro Power Purchase Arrangement

The estimated value of the Hydro PPA asset at December 31, 2009 was \$693.5 million (2008 – \$907.5 million). The Hydro PPA is valued at the present value of estimated amounts to be received by the Balancing Pool, net of estimated PPA obligations, over the remaining term of the PPA to 2020. The Hydro PPA is recorded as a financial asset due to the fact that TransAlta, the owner of the hydro plants, retains operational control of the hydro assets under the terms of this PPA.

Liabilities

Power Purchase Arrangement Lease Obligation

As counterparty to the Genesee PPA, the Balancing Pool is required to make monthly payments to the owner of the generating unit intended to cover fixed and variable costs. The capital component of the monthly payment is accounted for as a capital lease. The year-end balance of \$669.6 million (2008 – \$728.0 million) represents the sum of the capital component of the payments required over the remaining term of the Genesee PPA.

Small Power Producer Contracts

The Balancing Pool's legislated obligation related to Small Power Producer contracts is recorded at the net present value of estimated amounts to be received or paid by the Balancing Pool over the remaining terms of the contracts. This is recorded as a financial asset as the Balancing Pool does not have operational control of the assets. The estimated value of the Small Power Producer contracts at December 31, 2009 was a net liability of \$41.4 million (2008 – \$nil).

Reclamation and Abandonment Provision

The reclamation and abandonment liability at December 31, 2009 of \$35.7 million (2008 – \$48.0 million) represents estimated costs to decommission the H.R. Milner generating station, as well as estimated reclamation costs associated with the Isolated Generation sites. Wabamun decommissioning was completed during 2009.

In 2009 the Balancing Pool paid \$4.9 million (2008 – \$5.4 million) for reclamation costs of the Isolated Generation sites and \$5.6 million (2008 – \$6.6 million) for decommissioning costs related to Wabamun. At December 31, 2009, the reclamation of 98 of 103 Isolated Generation sites was complete, however, a few large sites still require reclamation. As per Energy Utilities Board (EUB) Decisions 2002-102 and 2003-036, costs for the Isolated Generation sites are approved by the Remediation Review Committee. The Remediation Review Committee is comprised of representatives of various consumer groups who were signatories to the Negotiated Settlement Agreement.

Balancing Pool Deferral Account

The deferral account at December 31, 2009 was \$969.3 million (2008 – \$1,325.4 million).

2009 changes to the deferral account include:

- a) a Net Assignment from equity of \$12.3 million loss (2008 – \$236.6 million gain); and
- b) Consumer Allocation payments of \$343.7 million (2008 – 271.4 million).

Consumer Allocation

Under the *Electric Utilities Act*, the Balancing Pool is mandated to allocate any forecasted cash surplus (or deficit) to electricity consumers in Alberta in annual amounts. In 2009 the Balancing Pool continued an allocation of its surplus to electricity consumers in Alberta in the amount of \$6.50 per megawatt hour (“MWh”) of consumption (2008 – \$5.00). For the year ending December 31, 2009, this allocation was \$343.7 million (2008 – \$271.4 million). Effective January 1, 2010, this allocation was decreased to \$4.00 per MWh of consumption; this allocation will continue to be reviewed on an annual basis.

Commitments and Contingencies

See discussion of force majeure claims in deferred charges above as well as PILOT.

Accounting Policy Changes

On January 1, 2009, the Balancing Pool adopted the amendments to Canadian Institute of Chartered Accountants (“CICA”) Handbook Section 3862, Financial Instruments – Disclosure. The standard was amended to include additional disclosure requirements about fair value measurements of financial instruments and to enhance the liquidity risk disclosure requirements. These amendments require fair values to be assessed based on a three-level hierarchy that reflects the significance of the inputs used in making the fair value measurements.

During 2009, the Balancing Pool adopted the requirements of CICA Emerging Issues Committee (“EIC”) 173 Credit Risk and the Fair Value of Financial Assets and Financial Liabilities. Under EIC-173 an entity’s own credit risk and the credit risk of the counterparty should be taken into account in determining the fair value of financial assets and liabilities, including derivative instruments. Application of EIC-173 did not result in any material adjustments to the fair value of financial assets or liabilities.

Future Accounting Changes

International Financial Reporting Standards (IFRS)

In 2005, the Accounting Standards Board (AcSB) announced that accounting standards in Canada are to converge with IFRS. On February 13, 2008 the AcSB confirmed that the use of IFRS for publicly accountable enterprises will be required on January 1, 2011 with appropriate comparative financial data for 2010.

The Balancing Pool has developed an IFRS convergence plan which takes into consideration, among other things:

- identification of differences in Canadian GAAP and IFRS accounting policies and their impact;
- selection of our continuing IFRS accounting policies;
- changes in financial statement notes disclosures;
- information technology and data system requirements;
- disclosure controls and procedures and internal controls over financial reporting;
- financial reporting expertise and training; and
- impacts on other business activities that may be influenced by GAAP measures.

During December 2009, the Balancing Pool has completed the initial identification of differences in Canadian GAAP and IFRS accounting policies and their impact. A diagnostic assessment was prepared by management, discussed with our external auditors and reviewed by the Audit and Finance Committee. No decisions were taken at this stage as the process focused on issue identification.

Efforts continue on the next phases of IFRS conversion which include management's recommendation on selection of IFRS accounting policies, the quantification of the impact of changes on our existing accounting policies, on our opening IFRS balance sheet, and the development of draft IFRS financial statements.

Critical Accounting Estimates

Since a determination of some assets, liabilities, revenues and expenses is dependent upon future events, the preparation of these financial statements requires the use of estimates and assumptions which have been made using careful judgment. Actual results will differ from these estimates. In particular, there were significant accounting estimates in relation to the following items:

Reclamation and Abandonment Provision—Engineering estimates are used to calculate the anticipated future costs of reclamation and abandonment.

Hydro Power Purchase Arrangement and Small Power Producer Contracts—The net present value of future cash flows is estimated using:

- forward market Pool electricity prices, discounted for risk of volatility;
- escalated costs as per contract term; and
- future cash flows discounted to net present value at 4% (2008 – 6%).

In the opinion of management, these financial statements have been properly prepared within reasonable limits of materiality and within the framework of the significant accounting policies.

Outlook

Based on forecasted cash flow and expected financial position for 2009, effective January 1, 2010, the Balancing Pool decreased the allocation of its surplus to electricity consumers in Alberta to \$4.00 per MWh of consumption, estimated at approximately \$210 million during the year. The Consumer Allocation is reviewed on an annual basis.

Under the *Electric Utilities Act*, the Balancing Pool is mandated to sell generation assets when market conditions are such that a fair market value will be obtained in a competitive sale process. At present, there continues to be a major area of uncertainty due to the pending federal legislation with respect to greenhouse gas emission standards that may impact the cost structure of the Genesee PPA. Given this element of high uncertainty, the Balancing Pool deems it inappropriate to conduct any PPA auction process until this major issue is finalized.

Forward-Looking Information

Certain information in this MD&A is forward-looking information and relates to, among other things, anticipated financial performance, operational prospects and strategies. Forward-looking information typically contains statements with words such as “anticipate,” “believe,” “expect,” “target” or similar words suggesting future outcomes. By their nature, such statements are subject to various risks and uncertainties that could cause the Balancing Pool’s actual results and experience to differ materially from the anticipated results. Such risks and uncertainties include, but are not limited to: availability and price of energy commodities; regulatory decisions; the ability of the Balancing Pool to successfully implement the initiatives referred to in this MD&A; and electricity market factors.



Financial Statements

Year ended December 31, 2009



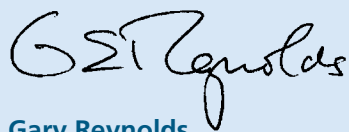
MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING

The financial statements included in the Annual Report are the responsibility of management and have been approved by the Board members of the Balancing Pool. These financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles (GAAP) and include the use of estimates and assumptions. Estimates and assumptions have been made using careful judgment and with all information available up to March 23, 2010. Financial information contained elsewhere in this Annual Report is consistent with that in the financial statements.

To discharge its responsibility for financial reporting, management maintains a system of internal controls designed to provide reasonable assurance that the Balancing Pool's assets are safeguarded, that transactions are properly authorized and that financial information is relevant, accurate and available on a timely basis.

The Balancing Pool Board members have appointed an Audit and Finance Committee that reviews the financial statements with management and the external auditors before the financial statements are submitted to the Balancing Pool Board members for approval. The external auditors have full and open access to the Audit and Finance Committee without obtaining prior management approval.

The financial statements have been examined by PricewaterhouseCoopers LLP, the Balancing Pool's external independent auditors. The responsibility of these external auditors is to examine the financial statements and to express an opinion on the fairness of the financial statements in accordance with Canadian GAAP. The auditors' report outlines the scope of their examination and states their opinion.



Gary Reynolds
President and Chief Executive Officer

March 23, 2010

AUDITORS' REPORT TO THE BOARD MEMBERS OF THE BALANCING POOL

We have audited the Balance Sheets of the Balancing Pool as at December 31, 2009 and 2008 and the Statements of Operations and Comprehensive Income (Loss), Equity and Cash Flows for the years then ended. These financial statements are the responsibility of the Balancing Pool'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 Balancing Pool as at December 31, 2009 and 2008 and the results of its operations and cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

PricewaterhouseCoopers LLP


Chartered Accountants
Calgary, Alberta

March 23, 2010

BALANCE SHEETS

<i>As at December 31 (in thousands of dollars)</i>	2009	2008
Assets		
Current assets		
Cash and cash equivalents	27,386	175,725
Accounts receivable	38,858	99,319
Current portion of Hydro power purchase arrangement (Note 4 b i)	48,975	94,094
Risk management asset (Note 4 b iii)	7,599	2,039
	122,818	371,177
Investments (Note 5)	800,924	750,905
Property, plant and equipment (Note 6)	216,439	236,143
Deferred charges (Note 9)	12,915	7,812
Hydro power purchase arrangement (Note 4 b i)	644,560	813,413
	1,797, 656	2,179,450
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities	81,491	76,798
Risk management liabilities (Note 4 b iii)	–	1,312
Current portion of power purchase arrangement lease obligation (Note 6 b)	57,844	58,309
Current portion of Small Power Producer contracts (Note 4 b ii)	11,362	–
Current portion of reclamation and abandonment provision (Note 7)	7,000	13,217
	157,697	149,636
Genesee power purchase arrangement lease obligation (Note 6 b)	611,803	669,647
Small Power Producer contracts (Note 4 b ii)	30,083	–
Reclamation and abandonment provision (Note 7)	28,710	34,795
Balancing Pool deferral account (Note 1, 8)	969,363	1,325,372
	1,797,656	2,179,450
Equity (Note 1)	–	–
Contingencies and commitments (Note 9)		
	1,797,656	2,179,450

On behalf of the Balancing Pool:



Thomas Cumming
Chair



Peter Flynn
Audit and Finance Committee Chair

The accompanying notes are an integral part of these financial statements

STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME (LOSS)

<i>For the year ended December 31 (in thousands of dollars)</i>	2009	2008
Revenues and funding		
Sale of electricity	337,441	522,627
Hydro power purchase arrangement (Note 4 b i)	11,415	139,500
Investment income – interest and dividends	30,391	32,135
Investment income – realized gains (losses) on sale of investments	(66,186)	(6,945)
Payments in lieu of tax	18,197	19,362
	331,258	706,679
Expenses		
Cost of sales	230,210	218,618
Small Power Producer contracts (Note 4 b ii)	12,741	(8,739)
Amortization and depreciation	19,703	19,715
Office of the Utilities Consumer Advocate	6,268	4,000
General and administrative	2,737	2,522
Other power purchase arrangement expenses	2,146	3,270
	273,805	239,386
Operating income	57,453	467,293
Other income (expense)		
Revaluation of Hydro power purchase arrangement (Note 4 b i)	(174,328)	(46,214)
Revaluation of Small Power Producer contracts (Note 4 b ii)	(41,445)	–
Unrealized gains (losses) on financial investments (Note 5)	137,990	(178,583)
Unrealized change on financial derivative instruments (Note 4 b iii)	6,872	(21,141)
Reclamation and abandonment provision (Note 7)	1,742	(5,900)
Other income (expense)	(564)	4,323
	(69,733)	(247,515)
Net results of operations and net comprehensive income (loss)	(12,280)	219,778

STATEMENTS OF EQUITY

<i>For the year ended December 31 (in thousands of dollars)</i>	2009	2008
Equity, beginning of year	–	–
Net results of operations	(12,280)	219,778
Adjustment for change in accounting policy (Note 4 d)	–	16,852
Assigned to Balancing Pool deferral account (Note 8)	12,280	(236,630)
Equity, end of year (Note 1)	–	–

The accompanying notes are an integral part of these financial statements

STATEMENTS OF CASH FLOWS

<i>For the year ended December 31 (in thousands of dollars)</i>	2009	2008
Operating activities		
Net results of operations	(12,280)	219,778
Adjustment for change in accounting policy – opening gain on financial derivatives	–	21,868
Items not affecting cash		
Amortization and depreciation	19,703	19,715
Reclamation and abandonment provision	(1,742)	5,900
(Increase) decrease in Small Power Producer contracts	54,186	(8,739)
(Increase) decrease in Hydro power purchase arrangement	162,913	(93,286)
Unrealized gains on financial derivative instruments	(6,872)	(727)
Unrealized (gain) loss on financial investments	(137,990)	178,583
Reclamation and abandonment expenditures	(10,560)	(11,993)
Net change in non-cash working capital	65,155	(19,391)
	132,513	311,708
Investing activities		
Sale (purchase) of investments	87,972	(135,493)
Deferred charges	(5,103)	(6,960)
Net additions to property, plant and equipment	–	(8)
	82,869	(142,461)
Financing activities		
Net Hydro power purchase arrangement receipts (Note 4 b i)	51,058	176,803
Power purchase arrangement lease obligation	(58,309)	(55,539)
Net Small Power Producer contracts receipts (outflows)	(12,741)	8,739
Consumer Allocation (Note 8)	(343,729)	(271,444)
	(363,721)	(141,441)
Change in cash and cash equivalents	(148,339)	27,806
Cash and cash equivalents, beginning of year	175,725	147,919
Cash and cash equivalents, end of year	27,386	175,725

The accompanying notes are an integral part of these financial statements

NOTES TO FINANCIAL STATEMENTS

1. Nature of Operations

Formation and Duties of the Balancing Pool

The Balancing Pool was created by the Government of Alberta to help manage certain assets, revenues and expenses arising from the transition to competition in Alberta's electric industry. The Balancing Pool was originally established in 1998 as a separate financial account of the Power Pool Council ("the Council") and commenced operations in 1999. The Council was a statutory corporation established under the *Electric Utilities Act of Alberta (1995)*. The requirement to establish the Balancing Pool was set out in the *Balancing Pool Regulation*.

With the proclamation of the *Electric Utilities Act (2003)* (the "Act") on June 1, 2003 the Balancing Pool was established as a separate statutory corporation. The assets and liabilities of the Council that related to the duties, responsibilities and powers of the Balancing Pool were transferred to the Balancing Pool.

Under the Act the corporation is required to operate with no profit or loss and no share capital for the corporation has been issued. The Balancing Pool Board consists of individual members independent of persons having a material interest in the Alberta electric industry. The members of the Board are appointed by the Minister of Energy of the Government of Alberta.

The Balancing Pool acted as Buyer of the Power Purchase Arrangements ("PPAs") that were not sold at the public auction held by the Government of Alberta in August 2000, assuming all rights and obligations of a buyer of these PPAs. Under the Act the Balancing Pool is required to manage generation assets in a commercial manner. The Balancing Pool is also required to respond to certain extraordinary circumstances during the operating period of all of the PPAs such as force majeure, unit destruction, buyer or owner default or a change in law resulting in termination of a PPA. In situations resulting in termination of a PPA, the Balancing Pool will assume all remaining rights and obligations pursuant to the PPA.

During 2009, the Alberta Government enacted amendments to the *Electric Utilities Act (2003)* that removed the requirement for the winding-up of the Balancing Pool by June 30, 2021.

Activities of the Balancing Pool

The initial allocation of assets and liabilities to the Balancing Pool was charged to the deferral account. Differences between annual revenues and expenditures are also charged or credited to the Balancing Pool deferral account. The Act requires that the Balancing Pool forecast its revenues and expenses. Any excess or shortfall of funds in the accounts is to be allocated to, or provided by, electricity consumers in annualized amounts.

Use of Estimates

The timely preparation of the financial statements in conformity with Canadian generally accepted accounting principles ("GAAP") requires that management make estimates and assumptions and use judgment regarding the reported amounts of assets

and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the year. Such estimates represent management's best estimate of future events as of the date of the financial statements. Accordingly, actual results will differ from estimated amounts as future confirming events occur. (See Note 2 for a discussion of significant estimates.)

Revenue and Funding

The Balancing Pool has five primary sources of revenue and funding:

i) Sale of electricity

The Balancing Pool earns revenue from the sale of electricity.

Electricity that is not otherwise contracted is sold into the spot market. Ancillary services from the Genesee PPA are sold to the Alberta Electric System Operator ("AESO") through a competitive exchange.

ii) Hydro PPA

Under the terms of government legislation, the Balancing Pool has obtained the right to a stream of payments from the owner of certain hydro plants in the province of Alberta. These payments are calculated based on the Pool price multiplied by a notional amount of production as outlined in the PPA less PPA obligations. The net present value of these estimated payments is recorded as an asset on the Balance Sheet and any revaluation adjustment included in net operating income.

iii) Investment income

Cash, cash equivalents and investments held by the Balancing Pool generate investment income consisting of interest, dividends and realized capital gains and losses.

iv) Payments in lieu of tax ("PILOT")

Pursuant to Section 147 of the Act, the Balancing Pool collects from electricity companies controlled by municipalities a notional amount of tax that would otherwise be payable if these entities were subject to tax. The Balancing Pool does not calculate instalment payments and it does not audit PILOT findings. PILOT instalments are calculated by the payor and are subject to audit by Alberta Revenue; adjustments, if any, arising from audits will be recorded in the current year.

v) Small Power Producer ("SPP") contracts

Under the *Independent Power and Small Power Regulation*, any surplus or deficit from contracts that a utility company entered into with Small Power Producers pursuant to the *Small Power Research and Development Act* will be paid to or received from the Balancing Pool. The net present value of these estimated payments is recorded as a liability on the Balance Sheet and any revaluation adjustment included in net results of operations.

Expenses and Disbursements

The Balancing Pool has expenditures which include:

i) Cost of sales

The Balancing Pool is obligated to pay certain fixed and variable costs to the owner of the generation asset that is operated under the terms of the Genesee PPA. Transmission costs are included in cost of sales. Under the terms of government legislation, the Balancing Pool is obligated to make payments to certain entities for such matters as force majeure.

ii) Other costs

Under the terms of government legislation, the Balancing Pool is obligated to make payments to certain entities for such matters as reclamation and abandonment costs which are included in Other Income (Expense). The Minister of Energy may direct the Balancing Pool to fund specific payments under Section 148 of the Act which are included in Office of the Utilities Consumer Advocate.

2. Significant Accounting Policies

The financial statements of the Balancing Pool have been prepared by management in accordance with Canadian GAAP. Certain comparative figures have been reclassified to conform to the current year's presentation. Since a determination of some assets, liabilities, revenues and expenses is dependent upon future events, the preparation of these financial statements requires the use of estimates and assumptions which have been made using careful judgment. Actual results will differ from these estimates. In particular, there were significant accounting estimates in relation to the following items:

- i) Hydro power purchase arrangement (Note 4 b i)*
- ii) Reclamation and abandonment provision (Note 7)*
- iii) Small Power Producer contracts (Note 4 b ii)*
- iv) Investments (Note 5)*
- v) Risk Management Assets and Liabilities (Note 4 b iii)*

In the opinion of management, these financial statements have been properly prepared within reasonable limits of materiality and within the framework of the significant accounting policies summarized below.

Revenue Recognition

a) Sale of electricity

Revenues from the sale of electricity and ancillary services are recognized on an accrual basis in the period in which generation occurred. Amounts settled under financial derivative contracts are recorded in sale of electricity.

b) Payments in lieu of tax

Payments in lieu of tax ("PILOT") are accrued based on the payors' instalments for a particular tax year. PILOT payments are calculated by payors and are subject to assessment and audit by Alberta Revenue.

c) Hydro power purchase arrangement

The Hydro PPA is recorded at the present value of the estimated future net payments to be received under this PPA. The increase in value of this asset with the passage of time (accretion) is recognized on an accrual basis. Any change in valuation as a result of changes in underlying assumptions is recognized in net operating income.

d) Investment income

Investment income from interest and dividends is recorded on an accrual basis when there is reasonable assurance as to its measurement and collectability. Investment income also includes realized gains and losses on investments sold and realized foreign currency exchange rate gains and losses on sale of foreign investments.

e) Small Power Producer contracts

Small Power Producer contracts are recorded at the present value of the estimated future net payments to be received (or paid) under these contracts. The change in value of this liability with the passage of time (accretion) is recognized on an accrual basis. Any change in valuation as a result of changes in underlying assumptions is recognized in net operating income.

Income Taxes

No provision has been made for income tax as under the Act the Balancing Pool is required to operate so that no profit or loss results.

Cash and Cash Equivalents

Cash and cash equivalents are comprised of cash and highly liquid short-term investments with maturities of three months or less that are classified as held-for-trading and are measured at fair value, which approximates carrying value, due to the short-term nature of these investments.

Accounts Receivable and Prepaid Expenses

Accounts receivable are classified as loans and receivables and are measured at amortized cost using the effective interest method. At each balance sheet date, the Balancing Pool assesses whether loans and receivables are impaired and any impairment is recognized.

Price Risk Management and Financial Instruments

Risk Management Assets and Liabilities

The Balancing Pool utilizes swap contracts to manage its exposure to electricity price fluctuations which require payments to (or receipts from) counterparties based on the differential between fixed and variable prices for electricity and other contractual arrangements. The estimated fair value of all derivative instruments is based on reported values in the electricity forward market. Amounts settled under these contracts are recorded as sale of electricity.

Derivative financial instruments are classified as held-for-trading and are recorded on the balance sheet at fair value. All changes in fair value are included in other income (expense).

Investments

Fixed-income securities are classified as held-to-maturity and valued at amortized cost where cost includes the amortization of the discount or premium using the effective interest rate method over the life of the investment and initial purchase transaction costs.

Equity securities are classified as held-for-trading and recorded in the financial statements at estimated fair value, as of the balance sheet date, measured based on the bid price in active markets, and unrealized gains or losses resulting from changes in fair value are recorded in operating income.

Should any investments be determined to be impaired, any unrealized loss would be recognized in operating income.

Genesee Power Purchase Arrangement (Genesee PPA) and Related Capital Lease Obligation

The Genesee PPA transfers to the Balancing Pool substantially all the benefits and risks of ownership and is therefore treated as if the asset had been purchased outright. The asset is included in property, plant and equipment at an amount not exceeding the estimated net future cash flows arising from operations over the remaining life of the PPA. At December 31, 2001 based upon estimated future electricity prices at the time, the net book value of the Genesee PPA was written down to \$426.8 million. The asset is depreciated over the term of the Genesee PPA. The capital element of the leasing commitment is shown as a Genesee PPA lease obligation.

Reclamation and Abandonment

The Balancing Pool has recorded an estimate of the cost to remediate certain Isolated Generating Unit sites in Alberta. Actual costs incurred to remediate these sites will reduce this liability and any increase in this liability will be charged to expense when estimated costs are known to exceed the remaining liability balance. An amount has

also been provided for the decommissioning of the H.R. Milner generating station which is being accreted annually; revisions to this estimate will be charged or credited to income. During 2009 the decommissioning of the Wabamun plant Units 1, 2, and 3 was completed (see Note 7).

3. Significant Accounting Policy Changes

During 2009, the Balancing Pool adopted the amendments to the Canadian Institute of Chartered Accountants (CICA) Handbook Section 3862, Financial Instruments – Disclosure. The standard was amended to include additional disclosure requirements about fair value measurements of financial instruments and to enhance the liquidity risk disclosure requirements. These amendments require fair values to be assessed based on a three-level hierarchy that reflects the significance of the inputs used in making the fair value measurements (see Note 4 c).

During 2009, the Balancing Pool adopted the requirements of CICA Emerging Issues Committee (“EIC”) 173 Credit Risk and the Fair Value of Financial Assets and Financial Liabilities. Under EIC-173, an entity’s own credit risk and the credit risk of the counterparty should be taken into account in determining the fair value of financial assets and liabilities, including derivative instruments. Application of EIC-173 did not result in any material adjustments to the fair value of financial assets or liabilities.

Future Accounting Changes

International Financial Reporting Standards (IFRS)

In 2005, the Accounting Standards Board (AcSB) announced that accounting standards in Canada are to converge with IFRS. On February 13, 2008 the AcSB confirmed that the use of IFRS for publicly accountable enterprises will be required on January 1, 2011 with appropriate comparative financial data for 2010. The Balancing Pool is currently assessing the impact of the differences in the accounting standards on its future financial reporting requirements.

4. Accounting For Financial Instruments

4. a) Risk Management Overview

The Balancing Pool is exposed to a number of business risks including:

i) PPA Risk: Under terms of the PPAs the Balancing Pool is exposed to longer term risks including change in law, force majeure and PPA termination risks. Risks under change in law could include new provincial and federal legislation relating to environmental emission standards, which if enacted, may result in the PPA becoming unprofitable to the buyer, in which case the PPA could then be terminated and consequently returned to the Balancing Pool. Pursuant to Section 96 of the *Electric Utilities Act (2003)* where a PPA is terminated by the plant owner (“Owner”), except for total destruction of a unit or plant, the PPA is deemed to have been sold to the Balancing Pool. Owner-initiated termination would generally be as a result of a default by the PPA Buyer in performing its obligations; in this instance, the Balancing Pool would be entitled to receive a termination payment from the Buyer

equal to the amount of net profit the Buyer would have lost by continuing to hold the PPA until the end of the effective term. Buyer-initiated termination could be as a result of a change in law making the PPA uneconomic for the Buyer, an event of force majeure lasting greater than six months, Owner default in performing its obligations, or Buyer buyout of the PPA. Termination under these provisions would result in the immediate transfer of the PPA to the Balancing Pool. Identifying, quantifying and devising strategies for mitigating these risks are an ongoing responsibility of the Balancing Pool.

ii) *Fluctuating Market Prices:* Changes in the market price for electricity and ancillary services affect the amount of income that the Balancing Pool receives from the Genesee and Hydro PPAs. Changes in the market price for electricity also affect the amounts paid or received by the Balancing Pool under the Small Power Producer contracts. Electricity prices are highly volatile, and are affected by supply and demand, which in turn are influenced by fuel costs (e.g. natural gas prices), weather patterns, plant availability and power imports or exports. Market price risk can be managed through the use of purchase and sales contracts for electricity.

iii) *Currency and Interest Rate Risk:* The Balancing Pool is exposed to currency risk and interest rate risk in that there is the possibility that investments will change in value due to fluctuations in foreign currency exchange rates and market interest rates. A \$0.01 change in the Canadian Dollar exchange rate versus the United States Dollar would have an estimated \$0.7 million impact on investment valuations and a \$0.01 change in the Canadian Dollar exchange rate versus the Euro would have an estimated \$0.8 million impact on investment valuations. Likewise a 1% change in interest rates would have an estimated \$0.3 million impact on investment annual returns and an estimated \$9.3 million impact on Genesee PPA capacity payments.

iv) *Plant Availability:* Changes in plant availability can impact the expected generation and associated revenues of the Balancing Pool. If the plant output managed by the Balancing Pool is sold forward and the plants are not available to supply delivery obligations, the Balancing Pool would be required to purchase energy at the prevailing market price to cover the shortfall in generation.

v) *Counterparty Credit Risk:* The Balancing Pool is exposed to counterparty credit risk. In the event of a default on payments from counterparties to the Hydro PPA, Small Power Producer contracts or forward sale contracts, a financial loss may be experienced by the Balancing Pool. Credit risk is managed in accordance with the Credit Policy which requires that all counterparties be investment grade level and is regularly monitored by management and the Audit and Finance Committee.

vi) *Liquidity Risk:* Liquidity risk is the risk that the Balancing Pool will not be able to meet its financial obligations as they fall due. To manage this risk, management forecasts cash flows for a period of 12 months and beyond and could make adjustments to the Consumer Allocation and/or liquidate investments as required.

vii) *Risk Management Policy:* The Balancing Pool has developed Risk Management and Credit Policies that defines the organization's tolerance for risk and sets out procedures for quantifying and monitoring exposures. Exposures and compliance with the Policy are regularly monitored by management, the Audit and Finance Committee and the Board.

4. b) Analysis of Financial Instruments

i) Hydro Power Purchase Arrangement

The Balancing Pool is the counterparty to the Hydro PPA, a financial arrangement recorded as an asset at the present value of estimated amounts to be received, net of Hydro PPA obligations, over the remaining term of the Hydro PPA. The Balancing Pool has no responsibility for the operational control of the hydro generating units and receives from (or pays to) the owner of the hydro plants revenues based on Pool prices and notional energy and reserve (ancillary service) volumes defined in the Hydro PPA, less the Hydro PPA fixed and variable costs.

The notional production of electricity under the Hydro PPA is 1,650 gigawatt hours per annum until 2013 and 1,620 gigawatt hours per annum from 2014 to 2020. Hydro PPA receipts or payments are settled on a monthly basis.

The remaining term of the Hydro PPA is 11 years to 2020. At December 31, 2009, the net present value of the Hydro PPA was estimated at \$694 million (December 31, 2008 – \$908 million). Key assumptions in this valuation are a discount rate of 4% (2008 – 6%) and management's best estimate of market prices for electricity.

Hydro PPA (in thousands of dollars)	2009	2008
Hydro power purchase arrangement, opening balance	907,506	991,024
Accretion and current year change	11,415	139,500
Net cash receipts	(51,058)	(176,803)
Revaluation of Hydro power purchase arrangement asset	(174,328)	(46,214)
	693,535	907,507
Less: Current portion	(48,975)	(94,094)
	644,560	813,413

The estimated value of this asset varies significantly based on the assumptions used and there is a high degree of measurement uncertainty. For example, if the forecasted market price of electricity is decreased by 10% the value is reduced to \$548 million; if the discount rate is reduced to 3% the value is increased to \$737 million.

ii) Small Power Producer Contracts

Under the *Independent Power and Small Power Regulation of the Act*, any surplus or deficit from contracts that a utility company entered into with Small Power Producers pursuant to the *Small Power Research and Development Act* will be paid to or received from the Balancing Pool.

There are 10 (2008 – 15) contracts with total allocated capacity of 82 (2008 – 108) megawatts ("MW"). Contract prices range from \$61.90/megawatt hour ("MWh") to \$79.70/MWh. Contract completion dates range between 2013 and 2019. Under these contracts the price that the Small Power Producer receives from the utility company is either fixed or fixed plus an escalation factor. If the market price is below the contract price, the Balancing Pool must pay the difference to the utility company. If the market price exceeds the contract price, the utility company must pay the difference to the Balancing Pool.

At December 31, 2009, the net present value of cash flows to or from the Balancing Pool for these contracts was estimated to be \$41.4 million liability (2008 – \$nil). The estimated value of this liability varies significantly based on the assumptions used and there is a high degree of measurement uncertainty. Key assumptions in this valuation are a discount rate of 4% (2008 – 6%) and management’s best estimate of market prices for electricity.

Small Power Producer Contracts <i>(in thousands of dollars)</i>	2009	2008
Small power purchase contracts, opening balance	–	–
Accretion and current year change	(12,741)	8,739
(Revenues) expenses	12,741	(8,739)
Revaluation of Small Power Producer contracts	(41,445)	–
Small power producer contracts, ending balance	(41,445)	–
Less: Current portion	11,362	–
	(30,083)	–

The valuation of these contracts varies significantly depending on the assumptions used. For example, if the forecast market price of electricity is decreased by 10% the value is decreased to a \$52.4 million liability; if the discount rate is reduced to 3% the value change is not significant.

iii) Financial Derivatives—Electricity Price Risk Management Activities

At December 31, 2009, the Balancing Pool had derivative swap contracts outstanding to manage its exposure to changes in electricity prices with a net unrealized fair value gain of \$7.6 million (2008 – \$0.7 million). These swap contracts require payments to (or receipts from) counterparties based on the differential between the fixed contract price and variable Pool prices as published by the AESO. The swap contracts require the Balancing Pool to pay a variable price and the counterparty to pay a fixed price. The estimated volume in MWh and weighted average fixed price per MWh is provided below:

Effective Term	MWh	Weighted Average Fixed Price
Q1, 2010	448,230	\$57.61
Q2, 2010	163,800	\$61.36
Q3, 2010	11,040	\$51.00

The following table provides disclosure on the movements in the fair value of the Balancing Pool's net risk management current assets and current liabilities:

Risk Management Assets and Liabilities <i>(in thousands of dollars)</i>	Assets	Liabilities	Net
Outstanding at December 31, 2007	21,868	–	21,868
Changes in value attributable to:			
Market changes	35,750	34,990	760
New contracts entered during the year	2,039	1,312	727
Net realized gains on contracts settled during the year ^a	(57,618)	(34,990)	(22,628)
Net changes in value during 2008	(19,829)	1,312	(21,141)
Outstanding at December 31, 2008	2,039	1,312	727
Changes in value attributable to:			
Market changes	60,415	18,413	42,002
New contracts entered during the year	7,599	–	7,599
Net realized gains on contracts settled during the year ^a	(62,454)	(19,725)	(42,729)
Net changes in value during 2009	5,560	(1,312)	6,872
Outstanding at December 31, 2009	7,599	–	7,599

^a Amounts settled under financial derivative contracts are recorded on an accrual basis in revenue against the applicable exposure. During 2009, the Balancing Pool realized \$42.7 (2008 – \$22.6) million in financial derivatives gains which have been included in sale of electricity.

4. c) Fair Value Hierarchy

Financial Instruments carried at fair value are categorized as follows:

<i>(in thousands of dollars)</i>	Quoted prices in active markets for identical assets	Significant other observable inputs	Significant unobserv- able inputs	Total
	Level 1	Level 2	Level 3	
Assets				
Cash and cash equivalents	27,386	–	–	27,386
Risk management assets	–	7,599	–	7,599
Investments – Equity Securities	455,238	–	–	455,238
Hydro PPA	–	–	693,535	693,535
	482,624	7,599	693,535	1,183,758
Liabilities				
SPP Contracts	–	–	41,445	41,445
			41,445	41,445
	482,624	7,599	652,090	1,142,313

Fair values of assets and liabilities included in Level 1 are determined by reference to quoted prices in active markets for identical assets and liabilities. Assets and liabilities in Level 2 include valuations using inputs other than Level 1 quoted prices for which all significant inputs are observable, either directly or indirectly. Level 3 valuations are based on inputs that are unobservable and significant to the overall fair value measurement. Changes in valuation methods may result in transfers into or out of an assigned level.

Cash and cash equivalents—are comprised of cash and highly liquid short-term investments with maturities of three months or less and are measured at fair value, which approximates carrying value, due to the short-term nature of these investments.

Risk management assets and liabilities—the estimated fair value of all derivative instruments is based on reported values in the electricity forward market as at December 31, 2009. Derivative financial instruments can result in exposure to credit risk being the risk a counterparty will default on its contractual obligations. Derivative financial instruments transactions are entered only with institutions that are rated investment grade by recognized credit ratings agencies.

Investments – Equity Securities—are recorded in the financial statements at estimated fair value, as of the balance sheet date measured based on the bid price in active markets and unrealized gains or losses resulting from changes in fair value are recorded in operating income. Should the investment be determined to be impaired, any unrealized loss would be recognized in operating income.

Hydro power purchase arrangement (PPA) and Small Power Producer contracts—are recorded at the present value of the estimated future net payments to be received or paid under the contracts and reflect management’s best estimates based on generally accepted valuation techniques or models and supported by observable market prices and rates when available. Given the long-term nature of these contracts, observable market prices are not available beyond the first few years. Methodologies have been developed to determine the fair value for these contracts based on extrapolation of observable future prices and rates.

4. d) Analysis of Accounting Policy Change Adjustment

Further to the implementation of CICA Handbook Section 3855 on January 1, 2008, adjustments were made to the opening investment and risk management assets and liabilities in order to reflect the effect on financial derivatives and investments held at December 31, 2007.

The following table provides details of these adjustments at January 1, 2008:

Adjustments <i>(in thousands of dollars)</i>	2008
Fair value adjustment unrealized gain on financial derivatives	21,866
Fair value adjustment unrealized loss on equity securities	(5,014)
Net adjustment for accounting policy change	16,852

5. Investments

<i>(in thousands of dollars)</i>	2009		2008	
	Amortized Cost		Amortized Cost	
Fixed-income securities	345,687		334,374	
	Market Value	Cost	Market Value	Cost
Canadian equities	226,016	240,786	166,129	242,471
Global equities	229,221	262,256	250,402	359,855
	455,237	503,042	416,531	602,326
Total investments	800,924		750,905	

Fair value of fixed-income securities investments is estimated to be \$360.9 million as at December 31, 2009.

The following table provides disclosure on the movements in the fair value of the investments in equity securities:

Equity Securities Unrealized Gains (Losses) <i>(in thousands of dollars)</i>	Canadian Equities	Global Equities	Totals
Unrealized market gain (loss), Jan. 1, 2008	2,362	(7,376)	(5,014)
Unrealized foreign exchange loss, Jan. 1, 2008	–	(2,198)	(2,198)
Change during the year	(78,704)	(99,879)	(178,583)
Unrealized market loss, Dec. 31, 2008	(76,342)	(109,453)	(185,795)
Change during the year gains (losses)	53,013	18,791	71,804
Realized (gains) losses on sales of investments	8,559	57,627	66,186
Net change during the year	61,572	76,418	137,990
Unrealized market loss, December 31, 2009	(14,770)	(33,035)	(47,805)

6. Property, Plant and Equipment and Related Lease Obligation

a) Property, Plant and Equipment

<i>(in thousands of dollars)</i>	2009	2008
Power purchase arrangement	426,819	426,819
Less: Accumulated amortization	(210,485)	(190,819)
	216,334	236,000
Other assets	464	464
Less: Accumulated amortization	(359)	(321)
	105	143
	216,439	236,143

b) Power Purchase Arrangement Lease Obligation

Under the terms of the Act, the Balancing Pool assumed the role of the counterparty to the Genesee PPA, which has been accounted for as a capital lease. The estimated future annual lease payments (capital component of the Genesee PPA payments) are as follows:

<i>(in thousands of dollars)</i>	
2010	57,844
2011	58,874
2012	59,948
2013	60,081
2014	59,244
Thereafter	373,656
	669,647
Less: Current portion	(57,844)
	611,803

7. Reclamation and Abandonment Provision

<i>(in thousands of dollars)</i>	2009	2008
Isolated Generation sites ^a	18,910	23,895
H.R. Milner generating station ^b	16,800	15,900
Wabamun plant Units 1, 2, 3 ^c	–	8,217
	35,710	48,012
Less: Current portion	(7,000)	(13,217)
	28,710	34,795

A reconciliation between the opening and closing reclamation and abandonment provisions is provided below:

<i>(in thousands of dollars)</i>	2009	2008
Balance, beginning of year	48,012	54,105
Net increase (decrease) in liability provision	(2,642)	5,000
Liabilities paid in period	(10,560)	(11,993)
Accretion expense	900	900
Balance, end of year	35,710	48,012

a) Isolated Generation Sites

Under the *Isolated Generating Units and Customer Choice Regulations of the Act*, the Balancing Pool is liable for certain amounts relating to the reclamation costs associated with Isolated Generation units. In 2009 \$5.0 million (2008 – \$5.4 million) expenditures were incurred.

<i>(in thousands of dollars)</i>	2009	2008
Isolated Generation sites	18,910	23,895
Less: Current portion	(7,000)	(5,000)
	11,910	18,895

Pursuant to the Negotiated Settlement Agreements approved by the Alberta Utilities Commission, the ultimate payment of these costs must be reviewed and approved by the Remediation Review Committee.

b) H.R. Milner Generating Station

Under the Negotiated Settlement Agreement for the H.R. Milner generating station in 2001, the Balancing Pool assumed liability for the costs of decommissioning the station at the end of the contract period. When the asset was sold in 2004, the Balancing Pool retained the liability for decommissioning the generating station.

c) Wabamun Plant

The Negotiated Settlement Agreement (NSA) to decommission Wabamun Units 1, 2, and 3, was approved by the Energy and Utilities Board (EUB) on December 19, 2006 under Decision 2006-129. The NSA specifies the decommissioning cost categories for which the Balancing Pool and TransAlta Utilities Corporation respectively will be responsible. In 2009 \$5.6 million (2008 – \$6.0 million) expenditures were incurred. In 2008 the provision for decommissioning was increased by \$5.0 million and in 2009 there was a recovery of the provision in the amount of \$2.6 million on completion of reclamation.

8. Capital Management

The Balancing Pool's objective when managing capital is to operate as per the requirements of the *Electric Utilities Act (2003)* which requires the Balancing Pool to operate with no profit or loss and no share capital and forecast its revenues, expenses, and cash flows. Any excess or shortfall of funds in the accounts is to be allocated to, or provided by, electricity consumers in annual amounts. During 2009, the Alberta Government enacted amendments to the *Electric Utilities Act (2003)* that have removed the requirement for the winding-up of the Balancing Pool by June 30, 2021.

A reconciliation of the opening and closing Balancing Pool deferral account is provided below:

Balancing Pool Deferral Account <i>(in thousands of dollars)</i>	2009	2008
Deferral account, beginning of year	1,325,372	1,360,186
Assigned from equity	(12,280)	236,630
Consumer Allocation	(343,729)	(271,444)
Deferral account, end of year	969,363	1,325,372

Effective January 1, 2010, the Balancing Pool decreased the allocation to Alberta's electricity consumers to \$4.00 per MWh of consumption, an estimated \$213 million per annum (January 1, 2009 – \$6.50 per MWh, \$344 million per annum). The Consumer Allocation is reviewed and approved by the Board of Directors of the Balancing Pool on an annual basis.

9. Contingencies and Commitments

Other Power Purchase Arrangements

Pursuant to Section 96 of the Act, where a PPA is terminated by the plant owner ("Owner"), except for total destruction of a unit or plant, the PPA is deemed to have been sold to the Balancing Pool. Owner-initiated termination would generally be as a result of a default by the Buyer in performing its obligations. Buyer-initiated termination could be as a result of a change in law making the PPA uneconomic for the Buyer, an event of force majeure lasting greater than six months, Owner default in performing its obligations, or Buyer buyout of the PPA. Termination under these provisions would result in the immediate transfer of the PPA to the Balancing Pool.

Decommissioning Costs

Pursuant to Section 7 of the *Power Purchase Arrangements Regulation of the Act*, the owner of a generating unit who applies to the Alberta Utilities Commission ("AUC") to decommission a unit within one year of the termination of the PPA is entitled

to receive from the Balancing Pool the amount by which the decommissioning costs exceed the amount the owner collected from consumers before January 1, 2001 and subsequently through a PPA, provided that the unit has ceased generating electricity and subject to AUC approval.

Deferred Charges

a) Hydro PPA Disputes

Deferred charges include \$10.6 million of amounts with respect to commercial disputes with TransAlta Utilities Corporation ("TransAlta") under the Hydro PPA which are in the dispute resolution process and expected to conclude in 2010. Until the matters are resolved, the payments will be recorded as deferred charges.

b) Battle River Force Majeure

In February 2008, Alberta Power (2000) Ltd. claimed force majeure relief from its obligations under the Battle River PPA. As required under the *Balancing Pool Regulation*, the Balancing Pool paid \$4.6 million of capacity payments to Alberta Power (2000) Ltd. for the force majeure claims; however the Balancing Pool subsequently reviewed and rejected the claims. The repayment of the \$4.6 million is now subject to the dispute resolution process under the PPA which is expected to conclude in 2010. Until the claim is resolved, this amount will be recorded as deferred charges.

These deferred charges are presented net of a \$2.3 million provision for doubtful deferred charges.

Payments In Lieu of Tax

ENMAX Energy Corporation ("ENMAX") filed Notice of Objection related to the 2002 taxation year. The amount under dispute that was paid to the Balancing Pool is \$14.2 million. Due to the uncertainty of the outcome of the appeal process, no provision has been made in the financial statements.

In 2008, Alberta Finance, Tax and Revenue Administration issued Notice of Reassessments to ENMAX related to its 2003, 2004 and 2005 taxation years. The reassessments required a payment to the Balancing Pool of \$20.2 million, \$19.4 million and \$7.7 million respectively. The Balancing Pool has not received any amounts payable under these Notices of Reassessment and ENMAX has filed a Notice of Objection related to these taxation years. Due to the uncertainty of the outcome of the appeal process, no amount has been recorded in the financial statements in this regard.

Credit Facility

At December 31, 2009, the Balancing Pool had \$4 million of unsecured Letters of Credit issued and an uncommitted credit facility available to issue Letters of Credit up to a maximum of \$90 million.

CORPORATE INFORMATION

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Photo by Studio Concepts

About the Cover: The Ghost plant is one of TransAlta Utilities Corporation hydro plants located on the Bow River. The plant was originally built in 1929. The Balancing Pool is counterparty to the Hydro Power Purchase Arrangement, covering the output of 13 hydroelectric plants, including the Ghost facility.

