Auditor General of Canada
Vérificatrice générale du Canada

AUDITOR'S REPORT

To the Minister responsible for the Qulliq Energy Corporation

I have audited the statement of financial position of the Qulliq Energy Corporation as at March 31, 2005 and the statements of income and retained earnings and cash flow for the year then ended. These financial statements are the responsibility of the Corporation's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with Canadian generally accepted auditing standards. Those standards require that I 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 my opinion, these financial statements present fairly, in all material respects, the financial position of the Corporation as at March 31, 2005 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles. As required by the *Financial Administration Act*, I report that, in my opinion, these principles have been applied, after giving retroactive effect to the change in the classification of the provision for future removal and site restoration as explained in Note 3 to the financial statements, on a basis consistent with that of the preceding year.

Further, in my opinion, proper books of account have been kept by the Corporation and the financial statements are in agreement therewith. In addition, the transactions of the Corporation that have come to my notice during my audit of the financial statements have, in all significant respects, been in accordance with Part IX of the *Financial Administration Act* and regulations, the *Qulliq Energy Corporation Act* and the by-laws of the Corporation.

Ronald C. Thompson, CA
Assistant Auditor General
for the Auditor General of Canada

Ottawa, Canada
August 3, 2005

QULLIQ ENERGY CORPORATION

Statement of Income and Retained Earnings
For the year ended March 31, 2005
($000)

		2005		2004
Revenues				
Sales of power (Note 5)	$	54,997	$	53,337
Other (Note 6)		2,070		1,854
		57,067		55,191
Expenses				
Fuel and lubricants		25,049		22,561
Salaries and wages		14,740		17,124
Supplies and services		10,325		12,052
Amortization of property, plant and equipment		5,576		5,652
Interest expense (Note 7)		4,291		4,694
Travel and accommodation		2,078		2,559
		62,059		64,642
Loss from operations		**(4,992)**		(9,451)
Recovery of increased operating costs (Note 4)		**12,000**		14,000
Gain on settlement of amount due to NTPC (Note 13)		**535**		-
Net income for the year		**7,543**		4,549
Retained earnings, beginning of year		**24,101**		19,552
Retained earnings, end of year	$	**31,644**	$	24,101

The accompanying notes are an integral part of the financial statements.

QULLIQ ENERGY CORPORATION

Statement of Financial Position
For the year ended March 31, 2005
($000)

		2005		2004
ASSETS				
Current assets				
Cash	$	12,129	$	1,800
Accounts receivable and accrued revenue (Note 8)		17,669		16,171
Recovery of increased fuel costs (Note 4)		4,460		10,000
Inventories (Note 9)		7,493		7,074
Prepaid expenses		611		592
		42,362		35,637
Property, plant and equipment, net of accumulated amortization (Note 10)		**118,924**		112,911
	$	**161,286**	$	148,548
LIABILITIES AND SHAREHOLDER'S EQUITY				
Current liabilities				
Accounts payable and accrued liabilities	$	10,196	$	8,234
Due to Petroleum Products Division (Note 12)		2,536		9,914
Due to Government of Nunavut (Note 13)		5,611		-
Due to Northwest Territories Power Corporation (Note 13)		-		5,646
Current portion of long-term debt (Note 14)		17,569		-
		35,912		23,794
Long-term debt (Note 14)		59,431		77,000
Other liabilities (Note 15)		24,299		23,653
		119,642		124,447
Shareholder's equity				
Contributed surplus (Note 4)		10,000		-
Retained earnings		31,644		24,101
		41,644		24,101
	$	**161,286**	$	148,548

Commitments and contingencies (Note 16)
The accompanying notes are an integral part of the financial statements.

Approved on behalf of the Board:

Simon Merkosak
Chairman of the Board

Colin Low-A-Chee
Director

QULLIQ ENERGY CORPORATION

Statement of Cash Flow
For the year ended March 31, 2005
($000)

		2005		2004
Operating activities				
Cash received from customers	$	55,519	$	57,175
Cash paid to suppliers and employees		(57,812)		(48,279)
Interest paid		(4,970)		(4,978)
Recovery of increased operating costs (Note 4)		17,540		4,000
Cash provided by operating activities		**10,277**		7,918
Financing activities				
Proceeds from long-term debt		-		8,638
Contributed surplus (Note 4)		10,000		-
Cash provided by financing activities		10,000		8,638
Investing activities				
Additions to property, plant and equipment		(9,948)		(5,580)
Insurance proceeds received		-		250
Cash used for investing activities		**(9,948)**		(5,330)
Increase in cash		**10,329**		11,226
Cash (bank indebtedness), beginning of year		**1,800**		(9,426)
Cash, end of year	$	**12,129**	$	1,800

The accompanying notes are an integral part of the financial statements.

QULLIQ ENERGY CORPORATION

Notes to the Financial Statements
For the year ended March 31, 2005
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1. The Corporation

Background

Effective April 1, 2001, the Nunavut Power Corporation commenced operations providing energy to customers resident in Nunavut.

Effective April 1, 2003 the *Nunavut Power Utilities Act* was amended and renamed the *Qulliq Energy Corporation Act* (the "Act") and the Nunavut Power Corporation was renamed the Qulliq Energy Corporation (the "Corporation").

The Act allows the Corporation to establish one or more subsidiaries to carry out its objects, if authorized to do so by order of the Commissioner in Executive Council.

Authority

The Corporation is a territorial Crown corporation and operates in accordance with Part IX of the *Financial Administration Act* and the *Qulliq Energy Corporation Act*. The Corporation is exempt from the payment of income taxes.

Mandate

The Corporation's mandate is to provide energy to residents and businesses in Nunavut on a safe, reliable and efficient basis and in a manner which minimizes the impact on the environment.

The Corporation supplies electricity to its customers through the operation of independent diesel generation plants and distribution systems in 25 communities in Nunavut.

Economic dependence

The Corporation is economically dependent on the Government of Nunavut, which directly and indirectly, accounts for the majority of the Corporation's sales of power. The Government of Nunavut also guarantees the Corporation's debt.

Additional details on the transactions and balances related to the Government of Nunavut are provided in the notes to the financial statements below.

2. Significant accounting policies

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

The regulatory accounting practices adopted by the Corporation may differ from the accounting practices otherwise applied by unregulated enterprises. The Corporation recognizes a regulatory asset or liability when, based on the decisions of the rate-regulator, there is reasonable assurance that it will be able to recover from or be required to refund certain amounts to customers in the future. The accounting effects of rate regulations are described in Note 4.

A summary of significant accounting policies are as follows:

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Use of estimates

The preparation of financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the reported amounts in the financial statements and accompanying notes. Actual results could materially differ from these estimates.

The more significant management estimates relate to the determination of the allowance for doubtful accounts and the estimated useful service life of property, plant and equipment, and the provision for employee future benefits.

Revenues

Revenues are recognized on the accrual basis and include an accrual for services provided but not billed.

Inventories

Fuel, lubricants, materials and supplies are recorded at average cost.

Property, plant and equipment

Property, plant and equipment is recorded at cost which consists of contracted services, direct labor, materials and supplies, a proportionate share of overhead costs and an allowance for interest expense incurred to finance construction. Property, plant and equipment transferred on Division were recorded at their net book value. Amortization of property, plant and equipment is provided on a straight-line average group useful life basis using the following range of rates:

	Estimated Useful Life	Rates
Generation assets	20 – 40 years	2.6% - 5.2%
Distribution assets	20 – 40 years	2.6% - 5.0%
Other assets	5 - 40 years	2.6% - 20.0%

Contributions in aid of construction

Contributions are required from customers whenever the costs of extending services exceed specified construction allowances. Contributions are amortized on the same basis as the related property, plant and equipment and the resulting credit is offset against the corresponding provision for amortization of property, plant and equipment.

Asset retirement obligations

As of April 1, 2004, the Corporation retroactively adopted the recommendations of the Canadian Institute of Chartered Accountants ("CICA") in Section 3110, "Asset Retirement Obligations". The recommendations require the Corporation to identify legal obligations relating to the retirement of tangible long-lived assets. Where a reasonable estimate of the fair value of these obligations can be determined, the total retirement costs are to be recorded as a liability at fair value, with corresponding increase to property, plant and equipment.

The Corporation has determined that it does not have long-lived assets which have future legal obligations for retirement. Therefore, no asset retirement obligations have been recorded.

Provision for future removal and site restoration

The rate regulated liability for the provision for future removal and site restoration represents the estimated costs of removing the property, plant and equipment, net of salvage values and restoring the Corporation's operating sites. These costs are being recognized over the estimated useful life of the assets and are recorded as an increase in the property, plant and equipment and the related provision. The rates used to calculate the annual provision have been approved by the regulator and are applied to the historical cost of the related assets. Actual costs for removal and site restoration are recorded against the provision in the year incurred.

Employee future benefits

(a) Pension plan

Employees participate in the Public Service Pension Plan (the Plan) administered by the Government of Canada. The Corporation's contributions to the Plan are expressed as a percentage of employees' contributions. The percentage may fluctuate from year to year depending on the experience of the Plan. The Corporation's contributions are recorded as an expense on a current year basis and represent the total pension obligations of the Corporation. The Corporation is not required to make contributions with respect to actuarial deficiencies of the Plan.

(b) Non-pension benefits

Under the terms and conditions of employment, employees may earn non-pension benefits for resignation, retirement and removal costs based on years of service. The benefits are paid upon resignation, retirement or death of an employee. The expected cost of providing these benefits is based on management's best estimates and is accrued as a liability as employees render service.

New accounting recommendations

In January 2005, the CICA issued three new standards: Section 3855 "Financial Instruments – Recognition and Measurement", Section 1530 "Comprehensive Income" and Section 3251 "Equity". Section 3855 provides standards on the recognition and measurement of financial assets, liabilities and non-financial derivatives, section 1530 establishes standards on the reporting and display of changes in equity from transactions and other events and circumstances from non-owner sources (comprehensive income), and section 3251 establishes standards for the presentation of equity and changes in the reporting period. The new standards are effective for fiscal years beginning on or after October 1, 2006. The Corporation is currently assessing the impact of the new standards.

In May 2005, the CICA issued Accounting Guideline 19 "Disclosures by Entities Subject to Rate Regulation". The purpose of this guideline is to ensure that financial statement users are better informed about the existence, nature and effects of all forms of rate regulation. This Guideline is effective for fiscal years ending on or after December 31, 2005. The Corporation has implemented some of the disclosures defined in this Guideline in Note 4 of the 2005 financial statements.

3. Change in accounting policy

In accordance with the new CICA recommendations in Section 3110, "Asset Retirement Obligations", the Corporation no longer recognizes a provision for future removal and site restoration under GAAP. However, in accordance with the instructions from the rate-regulator, the Corporation continues to recognize a provision and collect funds from its customers for the future removal of its assets and restoration of its operating sites. Therefore, the Corporation has reclassified the provision for future removal and site restoration of $16,874 as a rate regulated liability (2004 - $16,347).

4. Effects of rate regulation

Utilities Rate Review Council

The Corporation is subject to the *Utilities Rate Review Council Act* for the establishment of rates and terms and conditions of service. The purpose of the Utilities Rate Review Council (URRC) is to advise the Minister of Energy on rates and terms and conditions of service. Final approval of the rates and terms and conditions of service rests with the Minister and the Government of Nunavut.

General rate application

In September 2004, the Corporation filed it first general rate application (GRA) with the Minister of Energy and the URRC. The application was made as there has not been a general rate increase since the Corporation began operations on April 1, 2001 and the Corporation has incurred significant operating losses in the intervening period.

The Minister announced, based on recommendations from the URRC, a 15% general rate increase for all electricity consumption in Nunavut effective April 1, 2005.

Recovery of increased operating costs and contributed surplus

In March 2005, the Corporation received $22,000 from the Government of Nunavut. $12,000 of this funding was to off-set the current and prior years' increased operating costs: $8,000 for the current year's increased fuel costs and to offset the fuel stabilization fund balance and $4,000 for other increased operating costs. The remaining $10,000 was to fund the Corporation's capital program for the current fiscal year.

Consistent with the prior year, the Corporation recorded the $12,000 received for the recovery of increased operating costs as income for the current year. The Corporation also recorded the $10,000 received for capital purposes as contributed surplus since it was provided by the Government of Nunavut by virtue of its position as the sole-shareholder of the Corporation.

Fuel stabilization fund

The fuel stabilization fund (the fund) was carried over by the Corporation on Division. Under the fund, increases or decreases in fuel prices over approved amounts are accumulated until the fund reaches $2,000, at which time the Corporation can apply to the URRC for a fuel rate rider to recover from or refund the amounts back to customers to bring the fund back to zero.

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In 2004, the Government of Nunavut agreed to provide the Corporation with $14,000 to reduce the balance in the fund at March 31, 2004. The Corporation received $4,000 in March 2004, and recorded a regulatory asset for $10,000 for the recovery of the increased fuel costs at March 31, 2004.

In March 2005, the Corporation received $8,000 from the Government of Nunavut to reduce the balance in the fund at March 31, 2005. In addition, the Minister issued instructions to the Corporation to reduce the balance in the fund to zero at April 1, 2005 and to reduce the threshold limit of the fund from $2,000 to $1,000.

Accounting effects of rate regulation

The following describes each of the circumstances in which the effects of rate regulation result in financial statement recognition or measurement that differs from what GAAP otherwise requires or permits.

(a) Recovery of increased fuel costs

As discussed above, the Corporation recorded a regulatory asset for $10,000 for the recovery of the increased fuel costs at March 31, 2004. $4,460 of this amount was outstanding at March 31, 2005 and has been subsequently collected by the Corporation.

(b) Property, plant and equipment

The Corporation assesses the likelihood of impairment of its property, plant and equipment on a pooled basis. The recovery of the Corporation's capital costs is factored into the setting of future rates. If the future recovery through rates is no longer considered probable, the net book value of property, plant and equipment not considered recoverable is written off in the period the assessment is made.

(c) Provision for future removal and site restoration

As discussed in Note 3, the Corporation recognizes a provision and collects funds for the future removal of its assets and restoration of its operating sites. This provision is recognized as a rate regulated liability.

5. Sales of power

	2005	2004
Residential customers	$ 8,026	$ 8,550
Commercial customers	30,741	29,869
Territorial power support program	5,757	5,386
Public housing power support program	9,848	9,312
Electrical streetlights and private area lighting	966	1,010
Less bad debt expense	(341)	(790)
	$ 54,997	$ 53,337

The Corporation administers the Territorial Power Support Program for the Government of Nunavut. This program subsidizes qualifying residential customers by reducing the public rate for residential customers to 15.22 cents per kWh on the first 700 kWh consumed each month. The Corporation invoices the Government on a monthly basis for the power subsidies.

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The Corporation administers the Public Housing Power Support Program for the Government of Nunavut. This program subsidizes qualifying residential customers living in public housing by reducing the public rate to 6.0 cents per kWh. The Corporation invoices the Local Housing Associations in Nunavut on a monthly basis for the power subsidies.

6. Other revenue

	2005	2004
Pole rentals	$ 292	$ 288
Sale of residual heat	340	299
Administration and other service fees	630	570
Housing recoveries from employees	808	697
	$ 2,070	$ 1,854

7. Interest expense

	2005	2004
Interest on long-term debt	$ 4,781	$ 4,733
Interest and bank charges	189	254
Interest capitalized on construction projects	(679)	(293)
	$ 4,291	$ 4,694

8. Accounts receivable and accrued revenue

			2005	2004
	Gross	Allowance for doubtful accounts	Net	Net
Accounts receivable:				
Utility	$ 11,054	$ 1,050	$ 10,004	$ 6,778
Government of Nunavut	1,980	-	1,980	2,095
Housing Associations	4,532	-	4,532	3,078
Unbilled sales of power	-	-	-	3,267
Other	2,337	1,184	1,153	953
	$ 19,903	$ 2,234	$ 17,669	$ 16,171

The Corporation billed all of its customers up to March 31, 2005 to facilitate the increase in rates effective April 1, 2005.

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9. Inventories

		2005		2004
Fuel	$	4,303	$	3,921
Supplies and lubricants		3,190		3,153
	$	7,493	$	7,074

10. Property, plant and equipment

	2005						2004	
		Cost		Accumulated amortization		Net book value		Net book value
Generation	$	122,306	$	40,351	$	81,955	$	83,835
Distribution		21,882		9,767		12,115		12,056
Other		16,492		6,476		10,016		10,307
		160,680		56,594		104,086		106,198
Construction in progress		14,838		-		14,838		6,713
	$	175,518	$	56,594	$	118,924	$	112,911

Engineering and direct administration expenses capitalized during the year totaled $1,169 (2004 - $819). Interest on funds used during construction amounted to $679 (2004 - $293).

The estimated cost to complete construction projects in progress as at March 31, 2005 was $1,431, of which $521 was committed under contract. The Corporation expects to invest $7,030 in property, plant and equipment in the upcoming fiscal year.

Included in amortization expense is a $720 (2004 - $711) provision for future removal and site restoration of property, plant and equipment. Total expenditures for site restoration were $193 ($2004 – 208) during the year.

The Corporation has entered into an agreement to sell its telecommunication assets for their estimated net book value of $1,000. The sale is expected to be finalized in the upcoming fiscal year.

11. Bank indebtedness

The Corporation has a bank credit facility with a limit of $12,000. Interest charged on the overdraft is at prime. The balance on the credit facility was nil at March 31, 2005 (2004 - nil). The credit facility is guaranteed by the Government of Nunavut.

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12. Due to Petroleum Products Division

In November 2003, the Financial Management Board (FMB) of the Government of Nunavut directed the Corporation to stop paying the Petroleum Products Division (PPD) of the Government of Nunavut for fuel purchases.

In January 2005, the FMB approved the inclusion of $22,000 (described in note 4) in funding for the Corporation as a supplementary appropriation and directed the Corporation to settle all outstanding fuel purchases with PPD at March 31, 2005. The due to PPD of $2,536 at March 31, 2005 represents fuel deliveries received but not invoiced until after March 31, 2005.

13. Due to Government of Nunavut / Northwest Territories Power Corporation

The Government of the Nunavut paid $5,111 on behalf of the Corporation to the Government of the Northwest Territories to settle a dispute over the allocation of long-term debt and equity between the Northwest Territories Power Corporation and the Corporation at Division. The settlement resulted in a gain of $535 which has been recognized in income for the current year.

The $5,111 due to the Government of Nunavut bears no interest and will be repaid over 10 years with annual payments or $510 starting October 1, 2006 until the final payment of $521 on October 1, 2015.

The Corporation also received $500 from the Government of Nunavut related to the proposed transfer of the Petroleum Products Division. These funds were unspent as at March 31, 2005.

14. Long-term debt

		2005		2004
6.809% redeemable 20 year amortizing debenture, due September 27, 2021. Semi-annual interest only payments of $2,077 due until March 27, 2005 and blended semi-annual payments of $2,848 due thereafter with a balloon payment of $17,502 at the end of the term.	$	61,000	$	61,000
$16,000 floating rate capital loan facility due April 1, 2005. Interest is at bank prime (2005 - 4.25%).		16,000		16,000
Total debt		77,000		77,000
Less current portion of long-term debt		17,569		-
Long-term debt	$	59,431	$	77,000

Subsequent to the year end $15,000 of the $16,000 loan was repaid.

Principal debt repayment amounts are as follows: 2006 - $ 17,569; 2007 - $1,678; 2008 - $1,795; 2009 - $1,919; 2010 - $2,052; and 2011 to 2021- $51,987.

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Section 25 of the *Qulliq Energy Corporation Act* requires the Corporation's borrowings not to exceed three times its equity at any time. The Corporation's borrowings were 1.85 times its equity at March 31, 2005 (2004 - 3.2 times).

The long-term debt is guaranteed by the Government of Nunavut.

15. Other liabilities

		2005		2004
Provision for future removal and site restoration	$	16,874	$	16,347
Contributions in aid of construction		6,877		6,685
Employee future benefits		548		621
	$	24,299	$	23,653

The Corporation and all eligible employees contribute to the Public Service Pension Plan (Plan). The Plan provides benefits based on years of service and average earnings at retirement. The benefits are fully indexed to the increase in the Consumer Price Index.
Contributions to the Plan were as follows:

		2005		2004
Employer's contributions	$	1,070	$	999
Employee's contributions		496		440
	$	1,566	$	1,439

The Corporation also provides severance and removal benefits to its employees based on years of service and final salary. These benefits are not pre-funded. The liability for these benefits is as follows:

		2005		2004
Balance, beginning of year	$	1,764	$	908
Costs for the year		116		1,300
Benefits paid		(725)		(444)
Balance, end of year		1,155		1,764
Less current portion included in accrued liabilities		(607)		(1,143)
	$	548	$	621

16. Commitments and contingencies

Operating leases

The Corporation has leased property and equipment under various long-term operating leases. The minimum annual payments for these leases are as follows: 2006 - $1,857; 2007 - $1,630; 2008 - $1,403; 2009 - $1,067; 2010 - $686; and 2011 – 2012 - $728.

Litigation

In the normal course of operations, the Corporation could become party to future claims and legal proceedings. Management is of the opinion that adequate provisions have been made for any disbursements that could stem from future legal actions and does not foresee any adverse affect of such liabilities on the financial position or operating results of the Corporation.

Environmental liabilities

The Corporation's activities are subject to various federal and territorial laws and regulations governing the protection of the environment or to minimize any adverse impact thereon. The Corporation conducts its operations so as to protect public health and the environment and believes its operations are materially in compliance with all applicable laws and regulations. Liabilities will be recorded when the occurrence of an environmental expenditure, related to past or present activities of the Corporation, is considered probable and the costs can be reasonably estimated. To date, no such costs have been incurred by the Corporation.

17. Fair values

The estimated fair value of the Corporation's $61,000 debenture at March 31, 2005 is $68,135 (March 31, 2004 - $67,509) and is based on market prices for similar instruments.

The Corporation's financial instruments consist of cash, accounts receivable and accrued revenue, recovery of increased fuel costs, accounts payable and accrued liabilities, due to Petroleum Products Division, due to Government of Nunavut, capital loan facility and debentures. It is management's opinion that the Corporation is not exposed to significant interest or credit risk arising from these financial instruments. Except for the debentures disclosed above, management estimates that the carrying values of the financial instruments approximate their fair value due to their impending maturity.

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18. Related party transactions

Qulliq Energy Corporation is a territorial Crown corporation and consequently is related to the Government of Nunavut and its agencies and territorial corporations. The Corporation provides utility services to, and purchases fuel, materials, supplies and other services from these related parties. These transactions are at the same rates and terms as those with similar unrelated customers.

Transactions with related parties and balances at year end, not disclosed elsewhere in the financial statements, are as follows:

		2005		2004
Sale of power, heat and other	$	14,276	$	12,507
Territorial and housing subsidies included in revenue		15,605		14,698
Purchase of fuel		21,742		9,095
Fuel tax		1,240		1,218
Other		532		541
Balances at year-end:				
Accounts receivable - Utility		3,063		2,000
Accounts receivable – Territorial and housing subsidies		6,512		5,173
Accounts payable		2,776		1,519
Due to Petroleum Products Division		2,536		9,914

19. Comparative figures

Certain 2004 comparative figures have been reclassified to conform with the current year's presentation.