



An **ATCO** Company

MANAGEMENT'S DISCUSSION AND ANALYSIS

**FOR THE THREE MONTHS ENDED
MARCH 31, 2009**

CU Inc.
Management's Discussion and Analysis (MD&A)
For the Three Months Ended March 31, 2009

This MD&A should be read in conjunction with the Company's unaudited interim consolidated financial statements for the three months ended March 31, 2009, and the audited consolidated financial statements and MD&A for the year ended December 31, 2008 (2008 MD&A). **Information contained in the 2008 MD&A that is not discussed in this document remains substantially unchanged.** This MD&A is dated April 30, 2009. Additional information relating to the Company, including the Company's annual information form, is available on SEDAR at www.sedar.com.

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Glossary

Adjusted Earnings means earnings attributable to Class A and Class B Shares after adjustment for items that are not in the normal course of business or day-to-day operations. These items are usually of a non-recurring or one-time nature.

AESO means the Alberta Electric System Operator.

AFUDC means an allowance for funds used during construction at rates approved by the AUC for debt and equity capital. AFUDC is included in interest and other income.

Alberta Power Pool means the market for electricity in Alberta operated by AESO.

ATCO Midstream means ATCO Midstream Ltd., a wholly owned subsidiary of Canadian Utilities;

AUC means the Alberta Utilities Commission and its predecessor, the Alberta Energy and Utilities Board.

Availability is a measure of time, expressed as a percentage of continuous operation, that a generating unit is capable of producing electricity, regardless of whether the unit is actually generating electricity.

Canadian Utilities means Canadian Utilities Limited

Class A Shares means Class A non-voting shares of the Company.

Class B Shares means Class B common shares of the Company.

Company means CU Inc. and, unless the context otherwise requires, includes its subsidiaries.

GAAP means Canadian generally accepted accounting principles.

GHG means any greenhouse gas which has the potential to retain heat in the atmosphere, including water vapour, carbon dioxide, methane, nitrous oxide and hydrofluorocarbons.

Gigajoule (GJ) means a unit of energy equal to approximately 948.2 thousand British thermal units.

Megawatt (MW) is a measure of electric power equal to 1,000,000 watts.

Megawatt hour (MWh) means a measure of electricity consumption equal to the use of 1,000,000 watts of power over a one-hour period.

Petajoule (PJ) means a unit of energy equal to approximately 948.2 billion British thermal units.

Placeholder means an AUC approved interim cost which has been included in utility customer rates pending an AUC review in a separate or future proceeding. This cost is subject to adjustment once the separate or future proceeding is completed and may result in refunds to or recoveries from customers.

PPA means Power Purchase Arrangements that became effective on January 1, 2001, as part of the process of restructuring the electric utility business in Alberta. The PPAs are legislatively mandated and approved by the AUC.

Company Overview

The consolidated financial statements include the accounts of CU Inc. and all of its subsidiaries. The consolidated financial statements have been prepared in accordance with GAAP and the reporting currency is the Canadian dollar.

The Company operates in the following business segments:

The **Utilities** Business Group includes:

- the regulated distribution of natural gas by ATCO Gas;
- the regulated transmission and distribution of water by CU Water;
- the regulated transmission of natural gas by ATCO Pipelines; and
- the regulated distribution and transmission of electric energy by ATCO Electric and its subsidiaries, Northland Utilities (NWT), Northland Utilities (Yellowknife) and Yukon Electrical.

The **Power Generation** Business Group includes:

- the regulated supply of electricity by Alberta Power (2000).

Transactions between business segments are eliminated in all reporting of the Company's consolidated financial information. For additional information on the Company's business segments, refer to Note 9 to the unaudited interim consolidated financial statements for the three months ended March 31, 2009.

FINANCIAL MARKETS

Significant challenges are currently being experienced in domestic and international financial markets. These challenges are having an impact on the ability of certain borrowers to finance existing operations and capital expenditure programs. As discussed elsewhere in this MD&A, the Utilities Business Group has a capital expenditure program of \$2.0 billion and, depending on infrastructure spending, could be as much as \$4.0 billion over the next three years. The Company completed a \$270 million debenture issue and a \$160 million preferred share issue in March 2009 to fund the 2009 portion of the Utilities Business Group's capital expenditure program and to fund scheduled maturities of previous debenture issues. In addition, the Company has cash balances of approximately \$0.4 billion and available committed and uncommitted lines of credit of approximately \$0.3 billion which can be utilized for general corporate purposes.

While the current financial situation has not directly impacted the Company's ability to fund capital projects and ongoing operations, future borrowing may be impacted by these financial markets through increased carrying costs and the ability to raise debt and equity capital. The Company is unable to determine what future changes in the financial markets could occur and how these changes could affect the Company. Deterioration in domestic and international economic activity may impact the operations of the Company.

PENSION PLANS

Employees are required to contribute a percentage of their salary to registered pension plans. The Company is required to contribute its share of contributions on behalf of the defined contribution members of the pension plans and to provide the balance of the funding necessary to ensure that benefits will be fully provided for at retirement for the members of the defined benefit pension plans.

Recent declines in stock and bond markets have resulted in a reduction in the value of the defined benefit pension plans' assets, creating funding deficits. The Company has not made material contributions since April 1, 1996, as a result of the defined benefit plans' surplus positions which have been used to fund the employer's contributions to the defined contribution component of the pension plans. Based on the most recent actuarial valuations for funding purposes dated December 31, 2006, and December 31, 2007, and recent changes in government regulations resulting from the white paper issued by the government of Alberta in 2008, the Company does not anticipate that it will be required to make material contributions to its pension plans in 2009.

Depending on the outcome of future actuarial valuations, material current service and deficit funding contributions will likely be required to resume in 2010. The amounts are not known at this time. For purposes of any funding requirements pertaining to utility operations, the AUC has directed that the cash basis of accounting be used in customer rate applications. Accordingly, the Company includes the cost of funding in its rate applications to the AUC, thereby, with the consent of the AUC, recovering the costs of funding its pension plans for utility operations from utility customers.

Forward-Looking Information

Certain statements contained in this MD&A constitute forward-looking information. Forward-looking information is often, but not always, identified by the use of words such as “anticipate”, “plan”, “estimate”, “expect”, “may”, “will”, “intend”, “should”, and similar expressions. Forward-looking information involves known and unknown risks, uncertainties and other factors that may cause actual results or events to differ materially from those anticipated in such forward-looking information. The Company believes that the expectations reflected in the forward-looking information are reasonable, but no assurance can be given that these expectations will prove to be correct and such forward-looking information should not be unduly relied upon.

Non-GAAP Measures

The Company uses the measures “funds generated by operations” and “Adjusted Earnings” in this MD&A. These measures do not have any standardized meaning under GAAP and might not be comparable to similar measures presented by other companies.

Funds generated by operations is defined as cash flow from operations before changes in non-cash working capital. In management’s opinion, funds generated by operations is a significant performance indicator of the Company’s ability to generate cash during a period to fund its capital expenditures without regard to changes in non-cash working capital during the period.

Adjusted Earnings is defined as earnings attributable to Class A and Class B Shares after adjustment for items that are not in the normal course of business or day-to-day operations. These items are usually of a non-recurring or one-time nature. Management believes Adjusted Earnings allow for a more effective analysis of operating performance and trends.

Internal Control Over Financial Reporting

There was no change in the Company’s internal control over financial reporting that occurred during the period beginning on January 1, 2009, and ended on March 31, 2009, that has materially affected, or is reasonably likely to materially affect, the Company’s internal control over financial reporting.

Results of Operations

SELECTED QUARTERLY INFORMATION

(\$ millions)	For the Three Months Ended ^{(1) (2) (3) (4)}			
	Mar. 31	Jun. 30	Sep. 30	Dec. 31
2009				
Revenues	476.1	-	-	-
Earnings attributable to Class A and Class B Shares	90.3	-	-	-
Adjusted Earnings	90.3	-	-	-
2008				
Revenues	443.4	363.9	352.6	413.5
Earnings attributable to Class A and Class B Shares	77.7	33.5	30.9	58.2
Adjusted Earnings	77.7	33.5	27.9	53.4
2007				
Revenues	-	341.4	262.9	394.2
Earnings attributable to Class A and Class B Shares	-	38.3	25.4	53.4
Adjusted Earnings	-	32.8	25.4	44.8

Notes:

- ⁽¹⁾ There were no discontinued operations or extraordinary items during these periods.
- ⁽²⁾ Due to certain factors, revenues, earnings and Adjusted Earnings for any quarter are not necessarily indicative of operations on an annual basis. These factors include the seasonal nature of the Company's operations, changes in electricity prices in Alberta and the timing of rate decisions.
- ⁽³⁾ The above data (other than Adjusted Earnings) has been extracted from the financial statements, which have been prepared in accordance with GAAP, and the reporting currency is the Canadian dollar.
- ⁽⁴⁾ As all the Class A and Class B Shares of the Company are owned by Canadian Utilities, the disclosure of earnings per share is not provided as it is not considered to be meaningful.

The principal factors that caused variations in **financial condition** and **results of operations** over the past eight quarters necessary to understand general trends that have developed and the seasonality of the businesses disclosed in the 2008 MD&A remain substantially unchanged, except for:

- the impact of adopting new accounting standards for the recognition of revenues and expenses for regulated assets in ATCO Electric, ATCO Gas and ATCO Pipelines (refer to Changes in Accounting Policies – Rate Regulated Operations section).

CONSOLIDATED REVENUES AND EARNINGS

Revenues for the three months ended March 31, 2009, **increased** by \$32.7 million (7%) compared to the same period in 2008. This increase was primarily attributable to a \$27.9 million (8%) increase in revenues in the Utilities segment and a \$4.8 million (6%) increase in revenues in the Power Generation segment.

The **increase** in **revenues** was primarily attributable to AUC approved interim customer rates in ATCO Electric (ATCO Electric GTA), the impact of the ATCO Gas 2008/2009 general rate application decision (ATCO Gas GRA), and higher AUC approved customer rates resulting from ATCO Pipelines' negotiated settlement decision for 2008 and 2009 (ATCO Pipelines Negotiated Settlement). These increases were partially offset by the impact of applying new accounting standards in ATCO Electric, ATCO Gas and ATCO Pipelines relating to the recognition of revenues for rate regulated assets (refer to Changes in Accounting Policies – Rate Regulated Operations section).

Earnings and Adjusted Earnings for the three months ended March 31, 2009, were \$90.3 million, an **increase** of \$12.6 million (16%) over the same period of 2008. The primary reasons for the increased earnings were the impact of higher AFUDC associated with increased investment in transmission infrastructure in Alberta in ATCO Electric, the impact of the ATCO Gas GRA, and the impact of the ATCO Pipelines Negotiated Settlement.

Interest and other income for the three months ended March 31, 2009, **increased** by \$0.7 million to \$4.8 million, mainly due to higher AFUDC associated with increased investment in transmission infrastructure in Alberta in ATCO Electric.

CONSOLIDATED EXPENSES

(\$ millions)	For the Three Months Ended March 31		
	2009	2008	Change to 2009 (2009-2008)
Operating expenses:			
Natural gas supply	0.4	0.7	(43%)
Purchased power	15.7	15.3	3%
Operation and maintenance	113.9	92.8	23%
Selling and administrative	60.6	55.3	10%
Franchise fees	62.3	62.7	(1%)
	252.9	226.8	12%
Depreciation and amortization	59.6	69.7	(14%)
Interest	47.0	43.6	8%
Income taxes	28.1	26.9	4%
Dividends on equity preferred shares	3.0	2.8	7%

Operating expenses for the three months ended March 31, 2009, **increased** by \$26.1 million (12%) over the same period in 2008. Operation and maintenance expenses were higher primarily as a result of growth in ATCO Electric, ATCO Gas and ATCO Pipelines. Selling and administrative expenses increased primarily as a result of the impact of inflation and increased employment costs resulting from increased growth.

For the three months ended March 31, 2009, **depreciation and amortization expenses decreased** by \$10.1 million (14%) over the same period in 2008, primarily due to the impact of applying new accounting standards in ATCO Electric, ATCO Gas and ATCO Pipelines relating to the treatment of future removal and site restoration costs for rate regulated assets (refer to Changes in Accounting Policies – Rate Regulated Operations section). These decreases were partially offset by capital additions in 2008 and 2009 in the Utilities segment.

Interest expense for the three months ended March 31, 2009, **increased** by \$3.4 million (8%) over the same period in 2008, primarily due to increased amounts of debt outstanding (net of redemptions) resulting from new financings issued in 2008 and 2009 to fund capital expenditures in the Utilities segment.

For the three months ended March 31, 2009, **income taxes increased** by \$1.2 million (4%) over the same period in 2008, primarily due to higher earnings before taxes, partially offset by higher tax deductions in

Utilities operations resulting from the flow-through method of income tax accounting, and lower corporate tax rates in 2009.

Dividends on equity preferred shares for the three months ended March 31, 2009, **increased** by \$0.2 million (7%) as a result of the issue of \$160.0 million of 6.70% Cumulative Redeemable Preferred Shares Series 2 on March 27, 2009.

SEGMENTED INFORMATION

(\$ millions)	For the Three Months Ended				Total
	Utilities	Power Generation	Corporate & Other	Intersegment Eliminations	
March 31					
2009					
Revenues	397.1	79.0	-	-	476.1
Earnings attributable to Class A and Class B					
Shares and Adjusted Earnings ⁽¹⁾	80.5	9.9	(0.1)	-	90.3
2008					
Revenues	369.2	74.2	-	-	443.4
Earnings attributable to Class A and Class B					
Shares and Adjusted Earnings ⁽¹⁾	66.4	11.3	-	-	77.7

Note:

⁽¹⁾ There were no adjustments to earnings for the three months ended March 31, 2009, or for the corresponding period in 2008, and consequently earnings and Adjusted Earnings are identical.

Utilities

ATCO Electric, ATCO Gas and ATCO Pipelines are regulated primarily by the AUC, which administers acts and regulations covering such matters as rates, financing, accounting, construction, operation and service area. These utilities are subject to a cost of service regulatory mechanism under which the AUC establishes the revenues required (i) to recover the forecast operating costs, including depreciation and amortization and income taxes, of providing the regulated service, and (ii) to provide a fair and reasonable return on utility investment, or rate base. Rate base for each utility is the aggregate of the AUC approved investment in property, plant and equipment, less accumulated depreciation, and contributions by utility customers for extensions to plant, plus an allowance for working capital. The utilities earn a return on rate base intended to meet the cost of the debt and preferred share components of rate base and to provide share owners with a fair return on the common equity component of rate base.

Utilities **revenues** for the three months ended March 31, 2009, **increased** by \$27.9 million (8%) over the same period in 2008. The increase was primarily due to AUC approved interim customer rates associated with the ATCO Electric GTA, the impact of the ATCO Gas GRA, and higher AUC approved customer rates resulting from the ATCO Pipelines Negotiated Settlement. These increases were partially offset by the impact of applying new accounting standards in ATCO Electric, ATCO Gas and ATCO Pipelines relating to the recognition of revenues for rate regulated assets (refer to Changes in Accounting Policies – Rate Regulated Operations section).

For the three months ended March 31, 2009, **earnings** and **Adjusted Earnings** were \$80.5 million, an **increase** of \$14.1 million (21%) over the same period of 2008. The primary reasons for higher Adjusted Earnings were the impact of higher AFUDC associated with increased investment in transmission

infrastructure in Alberta in ATCO Electric, and the impact of the ATCO Gas GRA and the ATCO Pipelines Negotiated Settlement.

Regulatory Developments

Generic Cost of Capital

In February 2008, the AUC initiated a generic proceeding to determine whether the standardized rate of return methodology and the utility capital structures should be reviewed. A regulatory process has been established by the AUC with a hearing rescheduled for May 19, 2009, to review the generic return on equity formula as well as to review the capital structure for each of the Alberta utilities. The AUC also indicated that any changes which result from this proceeding would be applied beginning in 2009. As ATCO Gas filed a general rate application for 2008 and 2009, a separate module within the generic proceeding will address 2008 cost of capital issues relating to the capital structure for ATCO Gas, as inclusion of these issues was removed from its 2008/2009 general rate application. The changes for 2008 and 2009 will not apply to ATCO Pipelines since cost of capital issues were included in the ATCO Pipelines Negotiated Settlement (refer to ATCO Pipelines – 2008 and 2009 General Rate Application section).

ATCO Electric

2009 and 2010 General Tariff Application

In July 2008, ATCO Electric filed a general tariff application with the AUC for 2009 and 2010 requesting, among other things, increased revenues to recover increased financing, depreciation and operating costs associated with increased rate base in Alberta. ATCO Electric filed an application requesting interim refundable rates pending the AUC's decision on the application. In December 2008, ATCO Electric received a decision from the AUC approving interim refundable rate increases amounting to 50% of the requested increase for transmission operations and 25% of the requested increase for distribution operations. A hearing was held in February 2009, with a decision expected by the third quarter of 2009.

On March 11, 2009, ATCO Electric filed an application requesting an increase to its approved interim refundable rates for its distribution operations. A decision from the AUC was received on April 22, 2009, which resulted in an increase to the interim refundable rates to 67% of the requested rate increase.

ATCO Gas

2008 and 2009 General Rate Application

In November 2007, ATCO Gas filed a general rate application with the AUC for 2008 and 2009 requesting, among other things, increased revenues to recover increased financing, depreciation and operating costs associated with increased rate base in Alberta. ATCO Gas also filed an application requesting interim adjustable rates pending the AUC's decision on the general rate application. In December 2007, ATCO Gas received a decision from the AUC approving interim adjustable rate increases amounting to 50% of ATCO Gas' requested revenue increase. On November 13, 2008, the AUC issued a decision on ATCO Gas' 2008 and 2009 general rate application. The decision resulted in an increase to ATCO Gas' 2009 annual earnings of approximately \$3 million as a result of an increase in rate base. In the decision, the AUC used placeholders for common equity capitalization ratios, 2009 information and technology and customer care and billing costs and income tax amounts. The final amounts for these placeholders will be determined by the AUC in subsequent proceedings.

Deferred Gas Account

ATCO Gas filed an application with the AUC to address, among other things, corrections required to historical transportation imbalances (the process whereby third party natural gas supplies are reconciled to amounts actually shipped in the Company's pipelines) that have impacted ATCO Gas' deferred gas account. In April 2005, the AUC issued a decision resulting in a 15% decrease in the transportation imbalance adjustments sought by ATCO Gas. The decision resulted in ATCO Gas recovering \$9.2 million in natural gas supply costs from customers. The City of Calgary filed a leave to appeal the AUC's decision and ATCO Gas filed a cross appeal of the AUC's decision. On July 7, 2006, the Alberta Court of Appeal issued its decision granting the City of Calgary's leave to appeal on the question of whether the AUC erred in law or jurisdiction in assuming that it had the authority to allow recovery in 2005 of costs relating to prior years. At a hearing on April 13, 2007, the Alberta Court of Appeal declined to consider the City of Calgary's appeal and referred the jurisdictional question back to the AUC. On January 3, 2008, the AUC issued a decision confirming its jurisdiction to approve the prior period adjustment it had approved previously. In February 2008, the City of Calgary filed a leave to appeal the AUC's January 3, 2008, decision with the Alberta Court of Appeal. The hearing for this leave to appeal occurred on December 16, 2008 and on April 21, 2009, the Alberta Court of Appeal issued a decision granting the City of Calgary's leave to appeal.

Carbon Natural Gas Storage Facility

ATCO Gas owns a 43.5 petajoule natural gas storage facility located at Carbon, Alberta. ATCO Gas has leased the entire storage capacity of the facility to ATCO Midstream. ATCO Gas has taken the position that the facility is no longer required for utility service and should be removed from regulation.

In the process of obtaining AUC approval, a number of significant events have occurred. In July 2004, the AUC initiated a written process to consider its role in regulating the operations of the facility. In June 2005, the AUC issued a decision with respect to this process. In addition to addressing other matters, the decision found that the AUC has the authority, when necessary in the public interest, to direct a utility to utilize a particular asset in a specific manner, even over the objection of the utility. ATCO Gas filed for leave to appeal the decision with the Alberta Court of Appeal.

In October 2005, the AUC established processes to review the use of the facility for utility purposes. A hearing to review the use of the facility for revenue generation was held in April 2006, and a hearing to review the use of the facility for load balancing was held in June 2006. On October 11, 2006, the AUC issued a decision confirming ATCO Gas' position that the facility is no longer required for utility service with respect to the use of the facility for load balancing purposes. The City of Calgary then filed a leave to appeal and a review and variance application of this decision. On November 3, 2008, the AUC denied the City of Calgary's request that it review and vary its decision that the facility is no longer required for utility service with respect to the use of the facility for load balancing purposes.

On February 5, 2007, the AUC issued a decision in which it determined that a legitimate utility use for the facility is that it be used for purposes of generating revenues to offset customer rates. This decision required ATCO Gas to maintain the status quo with respect to the use of the facility including the lease of the entire facility to ATCO Midstream.

On February 26, 2007, ATCO Gas filed for leave to appeal this decision with the Alberta Court of Appeal. The Alberta Court of Appeal granted ATCO Gas' leave to appeal on October 24, 2007. On May 9, 2008, the Alberta Court of Appeal heard the appeal and subsequently issued a decision on May 27, 2008. The Court found that the AUC had erred in law or jurisdiction when it included the Carbon storage facility in rate base for the purpose of generating revenues to offset customer rates. On August 22, 2008, the City of Calgary filed a leave to appeal this decision with the Supreme Court of Canada. On December

4, 2008, the Supreme Court of Canada dismissed the City of Calgary's application for leave to appeal, thus upholding the Alberta Court of Appeal's May 27, 2008 decision.

As a result of the Alberta Court of Appeal's May 27, 2008 decision, ATCO Gas requested and received approval from the AUC to suspend rate riders to customer rates on an interim basis effective July 1, 2008. These riders were approved by the AUC in the past to distribute net revenues related to the facility to customers. As a result of the suspension of the rate riders, ATCO Gas recognized revenues of \$1.0 million and earnings of \$0.7 million in 2009 for the period January 1, 2009 to March 31, 2009. Due to certain factors, revenues and earnings from this matter for this period are not necessarily indicative of revenues or earnings on an annual basis.

On July 11, 2008, ATCO Gas filed a compliance application with the AUC requesting removal of the facility from the utility rate base and revenue requirement effective April 1, 2005, consistent with the Alberta Court of Appeal decision. Certain aspects of the application were updated on January 15, 2009. This application, in addition to the amounts recognized above, is seeking to recover from customers an additional \$30.3 million, excluding interest, related to those amounts refunded to customers over the April 1, 2005, to June 30, 2008, period. This additional \$30.3 million and related interest has not been recorded in ATCO Gas' earnings and is pending an AUC decision on the compliance application. On September 29, 2008, the AUC suspended ATCO Gas' compliance application pending the completion of the Utility Asset Disposition Rate Review Proceeding. On October 15, 2008, ATCO Gas filed an application with the Alberta Court of Appeal to direct the AUC to comply with its May 27, 2008, decision. ATCO Gas has withdrawn its October 15, 2008, application to the Alberta Court of Appeal as a result of the AUC recommencing the Carbon proceeding. A pre-hearing conference occurred on December 16, 2008, and on January 9, 2009, the AUC issued a decision establishing a final issues list to remove the Carbon facility from rate base. The AUC set a proceeding schedule with a hearing scheduled to commence on March 16, 2009. On March 6, 2009, the AUC suspended the proceeding schedule as previously established due to unanticipated delays in the process. The AUC determined that it would instead consider written submissions on three preliminary questions related to the removal of the Carbon assets from regulation. Once a determination on those questions has been made by the AUC, it will establish a further process to address the remaining outstanding matters. At this time it is unknown what the final outcome of these processes will be.

As part of the 2008-2009 general rate application, in a compliance application submitted to the AUC on January 19, 2009, ATCO Gas reduced its rate increase applicable to its south customers by \$7.6 million related to the production and storage charge that was included in ATCO Gas' rates from January through June 2008 as a result of excluding any costs for the Carbon facility in its general rate application. The impact of this \$7.6 million reduction to revenues could be a \$5.3 million decrease to ATCO Gas' earnings when a decision on the Carbon compliance application is received.

ATCO Pipelines

2008 and 2009 General Rate Application

In November 2008, ATCO Pipelines filed an application requesting the AUC approve a negotiated settlement with its customers of ATCO Pipelines' 2008 and 2009 revenue requirements. On March 18, 2009, the AUC issued a decision approving the negotiated settlement, including, among other things, a rate of return on common equity of 8.75% and a common equity ratio of 43% for each of 2008 and 2009. As a result of the decision, ATCO Pipelines recognized additional earnings over existing interim rates of \$4.5 million in the first quarter of 2009, of which \$3.7 million related to 2008.

2010, 2011 and 2012 Negotiated Settlement

On January 29, 2009, ATCO Pipelines filed a request with the AUC to negotiate with customers the settlement of the revenue requirements for the years 2010, 2011 and 2012.

Other Matters

The Company has a number of other regulatory filings and regulatory hearing submissions before the AUC for which decisions have not been received. The outcome of these matters cannot be determined at this time.

Power Generation

Power Generation **revenues** for the three months ended March 31, 2009, **increased** by \$4.8 million (6%) over the corresponding period in 2008, primarily as a result of GHG emission fees recovered from customers in accordance with the PPAs.

Earnings and **Adjusted Earnings** for the three months ended March 31, 2009, were \$9.9 million, a **decrease** of \$1.4 million (12%) over the corresponding period in 2008. This decrease was primarily due to a planned maintenance outage at the Sheerness generating plant in Alberta Power (2000).

Availability of the Power Generation generating plants by geographic region is set forth below:

	For the Three Months Ended		
	March 31		
	2009	2008	Change to 2009 (2009-2008)
Alberta Power (2000) ⁽¹⁾⁽²⁾ :			
Canada	85.9%	92.0%	(6.1%)

Notes:

⁽¹⁾ *Generating plant availability will fluctuate due to the timing and duration of outages.*

⁽²⁾ *The lower availability for the three months ended March 31, 2009, reflects a planned outage at the Sheerness generating plant.*

Alberta Power (2000)

Under the terms of the PPAs, Alberta Power (2000) is subject to an incentive/penalty regime related to generating unit availability. Incentives are payable by the PPA counterparties for availability in excess of predetermined targets, and penalties are payable by Alberta Power (2000) when the availability targets are not achieved. These amounts are amortized based on estimates of future generating unit availability and future electricity prices over the term of the PPAs.

During the three months ended March 31, 2009, the **deferred availability incentive** account **decreased** by \$0.5 million to \$60.8 million, mainly due to a planned outage at the Sheerness generating plant. During the three months ended March 31, 2009, the amortization of deferred availability incentives, recorded in revenues, increased by \$1.5 million to \$4.5 million, primarily as a result of changes in assumptions related to the terms of the PPAs. Previous assumptions were based on a single term for the PPAs at the Battle River generating plant. These assumptions have been revised to coincide with the term of the Battle River individual unit PPAs. The change is expected to increase 2009 revenues by approximately \$3 million.

Liquidity and Capital Resources

A major portion of the Company's operating income and funds generated by operations is generated from its utility operations. The Company uses short term bank loans and commercial paper borrowings to provide flexibility in the timing and amounts of long term financing.

SUMMARY OF CASH FLOW

(\$ millions)	For the Three Months Ended March 31		
	2009	2008	Change to 2009 (2009-2008)
Cash position, beginning of period	(9.0)	0.3	(3,100%)
Cash provided by (used in)			
Operating activities:			
Funds generated by operations	164.3	151.9	8%
Changes in non-cash working capital	38.1	24.5	56%
Cash flow from operations	202.4	176.4	15%
Investing activities	(228.7)	(105.9)	116%
Financing activities	424.8	(15.0)	2,932%
Cash position, end of period	389.5	55.8	598%

OPERATING ACTIVITIES

For the three months ended March 31, 2009, **funds generated by operations** were \$164.3 million, an **increase** of \$12.4 million (8%) over the same period in 2008, primarily due to higher cash earnings. For the three months ended March 31, 2009, **cash flow from operations** was \$202.4 million, an **increase** of \$26.0 million (15%) over the same period in 2008. This increase was primarily due to changes in non-cash working capital and increases in funds generated by operations.

INVESTING ACTIVITIES

For the three months ended March 31, 2009, **cash used in investing activities increased** by 116%, primarily due to changes in non-cash working capital, higher capital expenditures, and lower contributions by utility customers for extensions to plant. **Capital expenditures increased** by \$27.3 million, primarily due to increased investment in electric projects.

Capital expenditures to maintain capacity, meet planned growth, and fund future development activities are expected to be approximately \$0.9 billion in 2009, **unchanged** from 2008. The majority of these expenditures relate to the Utilities segment. For the 2009 to 2011 period, capital expenditures in the Utilities segment are expected to be \$2.0 billion and, depending on infrastructure spending, could be as much as \$4.0 billion.

The planned capital expenditures for the Utilities segment are based on the following assumptions:

- the AESO projects approved in principle by the AUC will proceed as currently scheduled;
- the remaining planned capital expenditures in the Utilities segment are required to maintain capacity and meet planned growth in the Company's service areas. These expenditures are

consistent with the anticipated growth in the Alberta economy and in the Company's service areas; and

- the regulatory system in Alberta will remain substantially unchanged.

In the opinion of the Company, these assumptions are reasonable, but no assurance can be given that these assumptions will prove to be correct.

ATCO Electric, ATCO Gas and ATCO Pipelines are regulated primarily by the AUC, which administers acts and regulations covering such matters as rates, financing, accounting, construction, operation and service area. The AUC approves customer rates based on the revenue required to recover estimated costs of service, including a fair return on rate base, estimated operating expenses, depreciation and taxes, all in respect of a future test year. Return on rate base is designed to meet the cost of interest on long term debt and dividends on preferred shares and to provide the shareowners with a reasonable opportunity to earn a fair return on their investment.

ATCO Electric, ATCO Gas and ATCO Pipelines are subject to the normal risks faced by companies that are regulated. These risks include the approval by the AUC of customer rates that permit a reasonable opportunity to recover on a timely basis the estimated costs of providing service, including a fair return on rate base. In addition, these risks include the disallowance of capital expenditures incurred if the AUC determines that such costs were not prudently incurred. This risk is mitigated by the inclusion of capital expenditures in general rate applications approved by the AUC. Furthermore, all major electric transmission projects assigned by the AESO to ATCO Electric are required to be approved by the AUC prior to commencing construction.

Tightness in labour and materials markets in Alberta in recent years has resulted in substantial growth in costs of many construction projects, and while the Company attempts to mitigate the risk of delays and cost overruns by careful planning and entering into long term contracts when possible, there can be no assurance that significant cost overruns or delays will not occur.

On September 9, 2008, ATCO Electric announced it had entered into an agreement with UK-based Balfour Beatty and Australia-based United Group Limited for engineering, construction, procurement and project management services to provide these services for required capital projects in the extremely tight labour market for such services available in Alberta. Individual projects assigned pursuant to this agreement will be jointly estimated and a target project cost agreed to before construction commences. The agreement provides ATCO Electric full discretion to assign or remove projects on an individual basis. Projects will be undertaken with a full disclosure to the AUC of actual costs, with any savings or overruns relative to target project costs shared equally.

FINANCING ACTIVITIES

For the three months ended March 31, 2009, the Company had **net debt increases** of \$270.0 million. Issuance of debt consisted of \$150.0 million of 6.50% Debentures due March 7, 2039, and \$120.0 million of 6.215% Debentures due March 6, 2024. There were no redemptions during the three months ended March 31, 2009.

For the three months ended March 31, 2009, the Company **issued** \$160.0 million of 6.70% Cumulative Redeemable Preferred Shares Series 2 (for additional details on these shares, refer to Note 6 to the unaudited interim consolidated financial statements for the three months ended March 31, 2009). The Company had no issues or redemptions of equity preferred shares in the corresponding period of 2008.

Total **dividends** for the three months ended March 31, 2009, **decreased** by \$15.0 million to nil, compared to the same period in 2008. The payment of any dividend is at the discretion of the Board of Directors and depends on the financial condition of the Company and other factors.

SHORT TERM INVESTMENT POLICY

The Company has a long-standing policy not to invest any of its cash balances in asset-backed securities; consequently, the recent turmoil in the asset-backed commercial paper market has had no impact on the Company. Cash and short term investment credit risk is reduced by investing 100% in short term money market instruments of Canadian financial institutions and Government of Canada treasury bills as at March 31, 2009.

LINES OF CREDIT

At March 31, 2009, the Company had the following credit lines that enable it to obtain funding for general corporate purposes.

	Total	Used	Available
(\$ millions)			
Short term committed	300.0	31.0	269.0
Uncommitted	28.7	1.0	27.7
Total	328.7	32.0	296.7

The amount and timing of future financings will depend on market conditions and the specific needs of the Company.

CONTRACTUAL OBLIGATIONS

Contractual obligations disclosed in the 2008 MD&A remain substantially unchanged as at March 31, 2009.

NET CURRENT AND LONG TERM FUTURE INCOME TAXES

Net current and long term future income taxes at March 31, 2009, were \$271.4 million, an increase of \$244.4 million (905%) over the same period of 2008. This increase was primarily due to changes in accounting policies relating to rate regulated operations (refer to Changes in Accounting Policies – Rate Regulated Operations section).

Future income taxes are attributable to differences between the financial statement carrying amounts of assets and liabilities and their tax bases. These differences result primarily from recognizing revenue and expenses in different years for financial and tax reporting purposes. Future income taxes will become payable when such differences are reversed through the settlement of liabilities and realization of assets.

BASE SHELF PROSPECTUS

On May 16, 2008, CU Inc. filed a **base shelf prospectus** that permits CU Inc. to issue up to an aggregate of \$1,500.0 million of debentures over the twenty-five month life of the prospectus. During the three months ended March 31, 2009, the following debentures were issued:

- on March 6, 2009, CU Inc. issued \$150.0 million of 6.50% Debentures due March 7, 2039, and
- on March 6, 2009, CU Inc. issued \$120.0 million of 6.215% Debentures due March 6, 2024.

The proceeds of these issues were advanced to ATCO Electric, ATCO Gas and ATCO Pipelines to be used to fund capital expenditures, to repay indebtedness and for other general corporate purposes.

Under its base shelf prospectus, the Corporation has issued \$0.6 billion of debentures to date, leaving \$0.9 billion remaining.

Share Capital

The equity securities of the Company consist of Class A Shares and Class B Shares.

At April 29, 2009, the Company had outstanding 3,286,124 Class A Shares, 2,014,076 Class B Shares, all of which are owned by Canadian Utilities.

Business Risks

Information contained in the 2008 MD&A related to Business Risks which is not discussed in this section remains substantially unchanged.

FINANCIAL MARKETS

Significant challenges are currently being experienced in domestic and international financial markets. These challenges are having an impact on the ability of certain borrowers to finance existing operations and capital expenditure programs. As discussed elsewhere in this MD&A, the Utilities Business Group has a capital expenditure program of \$2.0 billion and, depending on infrastructure spending, could be as much as \$4.0 billion over the next three years. The Company completed a \$270 million debenture issue and a \$160 million preferred share issue in March 2009 to fund the 2009 portion of the Utilities Business Group's capital expenditure program and to fund scheduled maturities of previous debenture issues. In addition, the Company has cash balances of approximately \$0.4 billion and available committed and uncommitted lines of credit of approximately \$0.3 billion which can be utilized for general corporate purposes.

While the current financial situation has not directly impacted the Company's ability to fund capital projects and ongoing operations, future borrowing may be impacted by these financial markets through increased carrying costs and the ability to raise debt and equity capital. The Company is unable to determine what future changes in the financial markets could occur and how these changes could affect the Company. Deterioration in domestic and international economic activity may impact the operations of the Company.

PENSION PLANS

Employees are required to contribute a percentage of their salary to registered pension plans. The Company is required to contribute its share of contributions on behalf of the defined contribution members of the pension plans and to provide the balance of the funding necessary to ensure that benefits will be fully provided for at retirement for the members of the defined benefit pension plans.

Recent declines in stock and bond markets have resulted in a reduction in the value of the defined benefit pension plans' assets, creating funding deficits. The Company has not made material contributions since April 1, 1996, as a result of the defined benefit plans' surplus positions which have been used to fund the employer's contributions to the defined contribution component of the pension plans. Based on the most

recent actuarial valuations for funding purposes dated December 31, 2006, and December 31, 2007, and recent changes in government regulations resulting from the white paper issued by the government of Alberta in 2008, the Company does not anticipate that it will be required to make material contributions to its pension plans in 2009.

Depending on the outcome of future actuarial valuations, material current service and deficit funding contributions will likely be required to resume in 2010. The amounts are not known at this time. For purposes of any funding requirements pertaining to utility operations, the AUC has directed that the cash basis of accounting be used in customer rate applications. Accordingly, the Company includes the cost of funding in its rate applications to the AUC, thereby, with the consent of the AUC, recovering the costs of funding its pension plans for utility operations from utility customers.

ENVIRONMENTAL MATTERS

The Company's operating subsidiaries and the industries in which they operate are subject to extensive federal, provincial and local environmental protection laws concerning emissions to the air, discharges to surface and subsurface waters, land use activities and the handling, manufacturing, processing, use, emission and disposal of materials and waste products.

Alberta legislation requires most large emitters to reduce GHG emission intensities by 12% annually. For cogeneration and combined cycle facilities, steam production GHG emissions are subjected to the 12% reduction target and electricity production emissions are compared to a deemed emission baseline. Compliance reports with true-up amounts for any obligations must be submitted annually to Alberta Environment by March 31. The compliance reports and obligation amounts for the 2008 reporting year have been submitted to Alberta Environment. PPA counterparties have reimbursed Alberta Power (2000) for amounts paid for their GHG obligations.

Alberta regulation requires coal-fired generating plant operators, including Alberta Power (2000), to monitor mercury emissions and target a capture of at least 70% of the mercury in the coal commencing January 1, 2011. Proposals to monitor and install control equipment on the Battle River and Sheerness generating plants have been submitted to Alberta Environment for approval. Once approval is received, installation of the equipment will be scheduled.

The Clean Air Strategic Alliance (CASA) is conducting a review of air emissions standards (sulphur dioxide, nitrogen oxides, mercury, and particulate matter) for the electricity sector in Alberta. Alberta Power (2000) participates in this process which will develop new air emissions standards for new units and units at the end of their design life (40 years or the end of their PPA term for coal-fired units and 30 years for natural gas-fired units). The new standards are expected to be adopted by Alberta Environment by 2010, and to be effective January 1, 2011.

On March 10, 2008, the federal government released details of its regulatory framework for its "Turning the Corner" legislation originally announced in April 2007. Electricity sector companies must achieve an initial GHG reduction in 2010 of 18% from their company-wide emission intensity, with a 2% continuous improvement required annually thereafter. New facilities (2004 or later) are allowed a three year grace period after which they must improve emission intensity by 2% per year below the clean fuel standard. For cogeneration and combined cycle facilities, GHG emissions are subjected to the 18% reduction target and electricity production emissions are compared to a deemed emission baseline similar to Alberta's legislation. Compliance may be achieved by reduction of emissions intensity, limited investment in a technology fund, emission credit trading, purchase of offset credits, *Kyoto Protocol Clean Development Mechanisms* (maximum 10%) and very limited opportunity for early action credits. A draft regulation has yet to be released.

In May 2008, the federal government and the Canadian Council of Environment Ministers (CCME) sanctioned a tripartite group (federal, provincial and territorial governments, industry and non-government organizations) to develop a new air management system for sulphur dioxide, nitrogen oxides, particulate matter, volatile organic compounds, mercury, and ground level ozone. They propose to have regulations in place by 2010 with implementation by 2015 for new and existing facilities. The three key elements of this proposal are: national ambient air quality standards set by the federal government, base level equipment performance standards and geographically based air quality management zones. No details have been provided on emissions targets.

Alberta Power (2000) continues to monitor these developments and the impact of complying with any resulting regulations.

It is anticipated that the PPAs will allow Alberta Power (2000) to recover most of the costs associated with complying with both the federal and Alberta regulations during the PPA term.

Changes in Accounting Policies

Rate Regulated Operations

Effective January 1, 2009, the Canadian Institute of Chartered Accountants (CICA) removed a temporary exemption in its accounting recommendations that permitted assets and liabilities arising from rate regulation to be recognized and measured on a basis other than in accordance with the primary sources of GAAP. Previously, the Company followed Canadian GAAP recommendations, which were similar to standards issued by the Financial Accounting Standards Board (“FASB”) in the United States, which provide guidance on the recognition and measurement of assets and liabilities arising from rate regulation. As permitted by Canadian GAAP, the Company has applied standards issued by FASB as another source of Canadian GAAP. This change in accounting policy has been adopted prospectively with changes identified below.

The reserves for future removal and site restoration costs for the utility operations, which were previously netted against property plant and equipment, have been reclassified to non-current regulatory liabilities, resulting in an increase to the Company’s total assets and total liabilities. The Company reclassified \$376.2 million at January 1, 2009, corresponding to these reserves.

Previously, depreciation expense for property, plant and equipment included a provision for future removal and site restoration costs for the utility operations. An amount corresponding to this provision is incorporated into rates charged to customers and was previously recognized in revenues. Under the new method of accounting, the Company does not recognize this amount in depreciation and amortization expense and revenues. The Company now recognizes operation and maintenance expense and revenues as actual removal and site restoration costs are incurred. As a result of the change in accounting, depreciation and amortization expense and revenues for the three months ended March 31, 2009, were \$13.9 million lower, resulting in no change in earnings.

Effective January 1, 2009, the Company also adopted the CICA recommendations requiring the recognition of future income tax assets and liabilities as well as a separate regulatory asset or liability for the amount of future income taxes expected to be included in future rates and recovered from or paid to future customers in the Company’s utility operations. As a result of adopting these recommendations, the Company recorded future income tax liabilities and non-current regulatory assets of \$255.6 million at January 1, 2009.

Concurrent with the changes in accounting for rate regulated operations noted above, the Company changed its presentation of changes in regulatory accounts within the statement of cash flows. Certain items relating to changes in rate regulated assets and liabilities that were previously included in investing and financing activities are now reported in operating activities. The inclusion of changes in the non-current regulatory assets and liabilities in operating activities provides more relevant information on the activities of the Company.

Goodwill and Intangible Assets

Effective January 1, 2009, the Company adopted the CICA recommendations for goodwill and intangible assets which established standards for the recognition, measurement, presentation and disclosure of goodwill and intangible assets (including internally developed intangible assets).

This change in accounting has been adopted retrospectively and had the following effect on the consolidated financial statements for the three months ended March 31, 2009 and March 31, 2008:

- (a) Restatement of opening retained earnings at January 1, 2008, to recognize the prior years' earnings effect of amounts capitalized prior to 2008 that do not meet the definition of intangible assets as now defined by GAAP (refer to Note 2 to the unaudited interim consolidated financial statements for the three months ended March 31, 2009).
- (b) Reclassification of \$174.1 million included in property, plant and equipment and other assets to intangible assets on the balance sheet at March 31, 2008.
- (c) Reclassification within investing activities of \$7.9 million from purchases of property, plant and equipment to purchases of intangibles for 2008.

Intangible assets mainly include computer software not directly attributable to the operation of property, plant and equipment and land rights and are recorded at cost less accumulated amortization and unamortized contributions by utility customers. The assets are amortized over their useful lives; which are not longer than 10 years for computer software and between 75 and 100 years for land rights. Intangible assets with finite lives are tested for recoverability whenever events or changes in circumstances indicate a possible impairment. An impairment of intangible assets with finite lives is recognized in earnings when the asset's carrying value exceeds the total cash flows expected from its use and eventual disposition. The impairment loss is then calculated as the difference between the asset's carrying value and its fair value, which is determined using discounted future cash flows.

FUTURE ACCOUNTING CHANGES

International Financial Reporting Standards

The Canadian Accounting Standards Board confirmed in 2008 that the use of International Financial Reporting Standards (IFRS) by publicly accountable enterprises will be required in 2011. The Company will need to begin reporting under IFRS in the first quarter of 2011 with comparative data for the prior year. IFRS uses a conceptual framework similar to Canadian GAAP, but there could be significant differences in recognition, measurement and disclosures that will need to be addressed.

The Company has established a Steering Committee, a project team, and working groups to review the adoption of IFRS. The project team and working groups provide position papers and regular updates to management, the Steering Committee and the Audit Committee. Education sessions have been, and will continue to be, provided for employees, senior management and the Audit Committee to increase knowledge and awareness of IFRS and its impacts.

The Company is participating in various industry groups, including the Canadian Energy Pipeline Association, the Canadian Gas Association and the Canadian Electricity Association. The Company

participated in a collaborative process which culminated in the AUC issuing a draft document that summarizes the rate making accounting procedures and requirements to be used by utilities as a result of adopting IFRS. The direction provided in the AUC document will allow the Company to proceed with cost efficient changes to its financial reporting computer systems. This document has not yet been approved by the AUC. The AUC announced that it will periodically review and amend the material contained in this document as circumstances warrant.

The Company's IFRS Conversion Project consists of three phases: Assessment and Diagnostic; Design and Planning; and Implementation and Review. Position papers are being prepared on issue-specific accounting differences between Canadian GAAP and IFRS and the impact on financial reporting computer systems. These position papers are currently being reviewed with the Company's auditor. As a number of the IFRS standards are changing, the position papers will be updated to reflect any changes resulting from the final standards. The Company has developed a plan to make changes to its financial reporting computer systems. The Company is also evaluating the potential impact of IFRS on financial covenants, business contracts and internal control over financial reporting.

The Company reviews discussion papers, exposure drafts and standards released by the International Accounting Standards Board and the International Financial Reporting Interpretations Committee. The Company will continue to assess the impact of the proposed standards on its financial statements and disclosure as additional information becomes available. Financial impacts cannot be reasonably determined at this time.

Based on initial assessments, the Company has identified that the following areas have the greatest potential impact to the Company's accounting: property, plant and equipment, rate regulated operations, deferred availability incentives, and employee benefits. There will also be a significant amount of effort to comply with the IFRS' requirements for initial adoption of IFRS.

A more detailed analysis and evaluation of the financial impact of the issues identified in the assessment and diagnostic phase and the impact on and implementation of financial reporting computer systems will be completed in 2009.