

FORTISBC Inc.

INTERIM MANAGEMENT DISCUSSION & ANALYSIS

For the Three Months and Nine Months Ended September 30, 2009

Dated November 5, 2009

The following material which is unaudited, should be read in conjunction with FortisBC Inc.'s ("the Company" or "FortisBC") unaudited consolidated financial statements and notes thereto for the three months and nine months ended September 30, 2009 and the Management Discussion & Analysis and the audited consolidated financial statements and notes thereto for the year ended December 31, 2008.

Certain statements contained in this Management Discussion & Analysis contain forward-looking information within the meaning of applicable securities laws in Canada ("forward-looking information"). The words "anticipates", "assumes", "believes", "budgets", "could", "estimates", "expects", "forecasts", "intends", "may", "might", "plans", "projects", "schedule", "should", "will", "would" and similar expressions are often intended to identify forward-looking information, although not all forward-looking information contains these identifying words.

The forward-looking information in this Management Discussion & Analysis includes, but is not limited to, statements regarding the Company's expectation of earnings growth in future years given the assumption of a consistently applied regulated capital structure and return on equity, recovery of its cost-of-service components in rates, and growth in rate base assets as a result of its annual capital expenditures.

The forecasts and projections that make up the forward-looking information are based on assumptions, which include but are not limited to receipt of applicable regulatory approvals and requested rate orders; continued electricity demand; absence of adverse weather conditions, natural disasters and equipment breakdown; no significant decline in interest rates; the ability to arrange sufficient and cost effective financing; the ability to maintain and renew collective bargaining agreements on acceptable terms; absence of environmental damage; the First Nations' settlement process does not adversely affect the Company; the adequacy of the Company's existing insurance arrangements; that counterparties do not default on power supply contracts; no weather related demand loss; ability to maintain and obtain applicable permits; climate change does not reduce water flows; and, no material adverse increase in employee future benefit costs.

The forward-looking information is subject to risks, uncertainties and other factors that could cause actual results to differ materially from historical results or results anticipated by the forward-looking information. The factors which could cause results or events to differ from current expectations include, but are not limited to: regulatory approval and rate orders risk; electricity demand risk; weather and natural disasters, equipment breakdown, operating and maintenance risk; interest rates risk; capital resources risk; labour relations risk; environmental matters risk; First Nations' land matters risk; underinsured and uninsured losses; power supply contracts risk; weather related demand loss; permits risk; climate change risk; employee future benefits risk; and, other risks described in the Company's most recent Annual Information Form. For additional information with respect to these risk factors, reference should be made to the section entitled "Business Risk Management" in the Company's Management Discussion & Analysis for the year ended December 31, 2008.

All forward-looking information in this Management Discussion & Analysis is qualified in its entirety by this cautionary statement and, except as required by law, the Company undertakes no obligation to revise or update any forward-looking information as a result of new information, future events or otherwise after the date hereof.

CORPORATE OVERVIEW

FortisBC is an integrated, regulated utility operating in the southern interior of British Columbia, serving approximately 158,000 customers directly and indirectly, focusing on the safe delivery of reliable and cost effective electricity.

The Company's regulated business includes four hydroelectric generating plants with an aggregate capacity of 223 megawatts ("MW"), approximately 7,000 kilometers of transmission and distribution power lines, and a peak demand of 746 MW. Included in FortisBC's non-regulated assets is a 16 MW run-of-river hydroelectric power plant near Lillooet, British Columbia. FortisBC generates approximately 45% of its electricity requirements with the balance met through power purchase agreements.

The Company is regulated by the British Columbia Utilities Commission ("BCUC"). The BCUC administers, acts and regulates, pursuant to the *Utilities Commission Act* (British Columbia) covering such matters as tariffs, rates, construction, operations, financing and accounting.

FortisBC operates primarily under a cost of service regulation as prescribed by the BCUC. The Company applies to the BCUC for annual revenue requirements based on estimated costs of service, including, but not limited to, operating expenses, power purchases, depreciation and amortization, income taxes, interest on debt and a return on equity ("ROE"). In addition, the regulatory framework includes some performance-based rate setting ("PBR") attributes. PBR is subject to change as the Company's regulatory framework evolves.

The Company is an indirect, wholly-owned subsidiary of Fortis Inc. ("Fortis"), a diversified, international utility holding company having investments in distribution, transmission and generation utilities, as well as commercial real estate and hotel operations.

REVENUE REQUIREMENTS

PBR

On April 19, 2006, FortisBC and a group of intervenors concluded negotiations on the Company's 2006 Revenue Requirement application. In addition to an agreement on the increase to customer rates required for 2006, the settlement agreement set 2006 as the base year for a PBR term from 2006 to 2008, with an option to extend the term to 2009. The settlement agreement was approved by the BCUC on May 23, 2006.

The significant terms of the PBR agreement are as follows:

- annual gross operating and maintenance expenses before capitalized overhead will be set by formula incorporating customer growth and inflation (CPI for British Columbia) minus a productivity improvement factor ("PIF") of 2% in 2007, 2% in 2008 and, if applicable, 3% in 2009;
- annual capitalized overhead will be set at 20% of the BCUC approved gross operating and maintenance expense;
- other components of revenue requirements will be forecast annually; and
- a 2% collar has been set around the allowed ROE whereby variances (adjusted for certain revenue and cost variances which flow through to customers) as a result of actual financial performance, positive or negative, will be shared equally between customers and the shareholder. If the variance exceeds the 2% collar, the excess will be placed in a deferral account for review and disposition during the next rate setting process. The Company's portion of the incentive is subject to the Company meeting certain performance standards and BCUC approval.

As part of the approval of 2009 Revenue Requirements on December 11, 2008, the PBR agreement was

extended for 2009 to 2011. The terms of the settlement are consistent with the May 23, 2006 PBR agreement except that annual gross operating and maintenance expenses before capitalized overhead will be set by formula incorporating customer growth and inflation (CPI for British Columbia) minus a PIF of 3% in 2009, 1.5% in 2010 and 1.5% in 2011. Should inflation be in excess of 3%, the excess is added to the PIF which effectively caps the CPI at 3%.

2009 Revenue Requirements

FortisBC filed its Preliminary 2009 Revenue Requirements Application on September 26, 2008 which was updated by the Company on November 3, 2008. Following a negotiated settlement process with intervenors, the BCUC approved the settlement agreement on December 11, 2008 resulting in a rate increase of 4.6% effective January 1, 2009.

The 4.6% rate increase is primarily the result of the Company's ongoing investment in infrastructure and increasing power purchases driven by customer growth and increased demand for electricity. Rates for 2009 reflect an allowed ROE of 8.87%.

In August of 2009, FortisBC applied for and received BCUC approval for a 2.2% rate increase effective September 1, 2009. This increase is due to increased power purchase costs charged by BC Hydro to the Company relating to their BCUC approved 2008 and 2009 rate increases.

Preliminary 2010 Revenue Requirements

On October 1, 2009 FortisBC filed its Preliminary 2010 Revenue Requirements Application with the BCUC to set customer electricity rates for 2010. The Company has requested a general 4.6% rate increase, effective January 1, 2010. The application is subject to intervenor input and BCUC approval. The rate increase is required due to ongoing investment in electrical infrastructure and increasing power purchases driven by customer growth and increased demand for electricity.

Further information on the terms of the PBR agreement and the 2009 Revenue Requirements and 2010 Preliminary Revenue Requirement can be found on the BCUC website (www.bcuc.com).

FINANCIAL RESULTS

Consolidated Financial Results (Unaudited)

| Period Ended September 30 | Quarter | | Year to Date | |
|---------------------------------|---------------|-------------------|----------------|-------------------|
| | 2009 | 2008 ² | 2009 | 2008 ² |
| Electricity Sales (GWh) | 731 | 710 | 2,323 | 2,273 |
| (\$000s) | | | | |
| Electricity Revenue | 54,481 | 50,452 | 174,582 | 162,007 |
| Other Revenue | 1,558 | 3,043 | 4,334 | 6,372 |
| Power Purchases | 15,349 | 13,784 | 50,017 | 47,027 |
| Operating Expenses ¹ | 14,335 | 13,803 | 44,839 | 43,205 |
| Depreciation and Amortization | 9,265 | 8,424 | 27,845 | 25,266 |
| Interest Expense | 8,492 | 7,504 | 24,342 | 22,383 |
| Income Taxes | 322 | 1,447 | 3,039 | 4,011 |
| Net Earnings | 8,276 | 8,533 | 28,834 | 26,487 |

¹ Includes operating and maintenance, property taxes, water fees and wheeling.

² Certain comparative figures have been reclassified to comply with the current period's classification.

Net Earnings

Net earnings for the third quarter of 2009 were \$8.3 million, a decrease of \$0.2 million over the same period last year. The lower earnings were attributable to a decrease in other revenue and increases in power purchases, operating expenses, depreciation and amortization, and interest expense partially offset by an increase in electricity revenue and a decrease in income taxes.

Year to date, net earnings of \$28.8 million for 2009 were \$2.3 million higher than the same period last year. The increase in net earnings was attributable to increased electricity revenue and decreased income taxes, partially offset by a decrease in other revenue and increases in power purchases, operating expenses, depreciation and amortization, and interest expense.

Electricity Sales

Electricity sales in the third quarter of 2009 were 731 gigawatt hours (“GWh”), an increase of 21 GWh compared to 710 GWh in the third quarter of 2008. On a year-to-date basis, electricity sales were 2,323 GWh, an increase of 50 GWh compared to 2,273 GWh for the same period last year. The increase in electricity sales for both comparable periods was primarily due to growth in residential and general service customers, partially offset by a decrease in industrial customers.

Electricity Revenue

Electricity revenue for the third quarter of 2009 was \$54.5 million, an increase of \$4.0 million over the \$50.5 million in the third quarter of 2008. On a year-to-date basis, electricity revenue was \$174.6 million, an increase of \$12.6 million over the \$162.0 million in the first nine months of 2008. The increase in revenue for the comparative periods was primarily due to a 4.6% rate increase effective January 1, 2009 and a 2.2% rate increase effective September 1, 2009 and an increase in electricity sales.

Other Revenue

Other revenue includes incentive adjustments associated with the PBR framework under which FortisBC operates. Under the terms of the PBR agreement, variances in certain revenues and costs as compared to the forecast will be recovered from (refunded to) customers. In addition, the ROE resulting from actual financial performance is compared to the Company’s allowed ROE and variances, positive or negative (adjusting for certain revenue and cost variances which flow through to customers), up to a 2% collar, will be shared equally between customers and FortisBC. The remainder of other revenue consists of management fees for third party contract work, pole attachment revenue, interest income, surplus electricity sales and other miscellaneous rental revenues.

Other revenues for the third quarter of 2009 were \$1.6 million compared to \$3.0 million for the same period of 2008. The decrease of \$1.4 million was primarily due to an increase in the PBR incentive adjustment owing to customers and decreases in surplus electricity sales and pole attachment revenue compared to the same quarter in 2008.

Year to date, other revenues were \$4.3 million compared to \$6.4 million for the same period last year. The decrease of \$2.1 million was attributable to an increase in the PBR incentive adjustment owing to customers and decreases in surplus electricity sales and management fees, partially offset by an increase in pole attachment revenue compared to the same period in 2008.

Power Purchases

Power purchases represent the cost of purchasing energy and capacity from third parties. Hydroelectric generating facilities owned by FortisBC generate approximately 45% of the energy and 30% of the capacity necessary to meet existing customer demand. The majority of the additional energy and capacity required to meet existing customer demand is purchased under firm, long-term power purchase contracts. Any remaining

energy and capacity required to meet customer needs is purchased on the open market and is subject to fluctuations in market rates.

Power purchases were \$15.3 million for the third quarter of 2009 compared to \$13.8 million for the same period in 2008. The \$1.5 million increase in power purchases was primarily attributable to increased electricity sales and higher average power purchase prices.

Year to date, power purchases were \$50.0 million compared to \$47.0 million for the first nine months of 2008. The \$3.0 million increase in power purchases was primarily attributable to:

- increased electricity sales,
- higher average power purchase prices,
- a higher proportion of purchased power versus generated power, and
- the receipt of \$0.6 million of insurance proceeds in the second quarter of 2008 in excess of amounts accrued relating to power purchase costs incurred in 2006 due to a turbine failure at the Lower Bonnington generation plant.

Operating Expenses

Operating expenses consist of operating and maintenance expenses, property taxes, water fees and wheeling. Operating expenses were \$14.3 million in the third quarter of 2009, an increase of \$0.5 million compared to \$13.8 million for the same period of 2008. The \$0.5 million increase in operating expenses was primarily a result of:

- a \$0.2 million increase in property taxes due to a larger assessment base,
- a \$0.2 million increase in water fees, and
- a \$0.2 million increase in wheeling fees,
- partially offset by a \$0.1 million increase in capitalized overhead.

Year to date, operating expenses of \$44.8 million have increased \$1.6 million over \$43.2 million recorded in the same period last year. The \$1.6 million increase in operating expenses was primarily a result of:

- a \$0.5 million increase in operating and maintenance costs due to timing of certain 2009 maintenance projects and their related expenditures, as well as labour escalation and general inflationary increases,
- a \$0.4 million increase in property taxes due to a larger assessment base,
- a \$0.5 million increase in water fees, and
- a \$0.4 million increase in wheeling fees,
- partially offset by a \$0.2 million increase in capitalized overhead.

Depreciation and Amortization

Depreciation and amortization expense for the third quarter of 2009 was \$9.3 million, an increase of \$0.9 million compared to \$8.4 million for the same period in 2008. Year to date, depreciation and amortization expense was \$27.8 million, an increase of \$2.5 million compared to \$25.3 million for the same period last year. These increases were due to increases in the depreciable asset base resulting from the Company's capital expenditure program.

Interest Expense

Interest expense, net of allowance for funds used during construction (capitalized financing costs) in the third quarter of 2009 was \$8.5 million, an increase of \$1.0 million compared to \$7.5 million for the same period in

2008. The increase was primarily due to an increase in gross interest expense resulting from increased borrowings to finance the capital expenditure program, partially offset by lower borrowing interest rates on bank operating credit facilities and increased capitalized financing costs relating to more assets under construction compared to the same period in 2008.

Year to date, interest expense net of capitalized interest was \$24.3 million, an increase of \$1.9 million over the \$22.4 million recorded in the same period last year. The increase was primarily due to an increase in gross interest expense resulting from increased borrowings to finance the capital expenditure program and increased bank operating credit facility renewal fees, partially offset by lower borrowing interest rates on bank operating credit facilities and increased capitalized financing costs relating to more assets under construction compared to the same period in 2008.

Income Taxes

Prior to January 1, 2009, the Company used the taxes payable method of accounting for income taxes on regulated earnings as ordered by the BCUC. Effective January 1, 2009, Canadian Generally Accepted Accounting Principles (“GAAP”) for rate-regulated operations has been amended to require the recognition of future income tax liabilities and assets as well as a regulatory asset or liability for the amount of future income taxes expected to be recovered from or returned to customers in future rates. In addition, certain regulatory assets and deferred charges are recorded net of their income tax impact, with the offset charged to income tax expense.

The Company follows the asset and liability method of accounting for income taxes on its non-regulated earnings which results in future income taxes expensed or recovered in the period that the temporary differences are incurred or reversed.

For the three months ended September 30, 2009, income tax expense was \$0.3 million, a \$1.1 million decrease compared to \$1.4 million for the same period in the prior year. The decrease was primarily due to a decrease in earnings before income taxes, an increase in income tax timing differences and a reduction in the Federal and Provincial income tax rates.

Year to date, income tax expense was \$3.0 million, a decrease of \$1.0 million compared to \$4.0 million for the same period last year. The decrease was primarily due to an increase in income tax timing differences and a reduction in the Federal and Provincial income tax rates, partially offset by an increase in earnings before income taxes.

Included in the income tax expense for the three and nine months ended September 30, 2009, are future income tax expenses of \$3.1 million and \$4.2 million respectively. Both future income tax expenses are offset by the expected amounts to be recovered from customers in the future, resulting in no earnings impact for the three and nine months ended September 30, 2009.

FINANCIAL POSITION

The following table outlines the significant changes in the consolidated balance sheets as at September 30, 2009 as compared to December 31, 2008.

Significant Changes in Consolidated Balance Sheets (Unaudited)

As at September 30, 2009 compared to December 31, 2008

| Balance Sheet Item | Increase (Decrease) |
|----------------------------------|---------------------|
| (\$ millions) | |
| Accounts receivable | (6.1) |
| Prepaid expenses | 6.1 |
| Regulatory assets | 79.8 |
| Property, plant and equipment | 60.0 |
| Current and long-term debt | 22.1 |
| Regulatory liabilities | 15.2 |
| Future income taxes ¹ | 78.0 |
| Share capital | 5.0 |
| Retained earnings | 18.3 |

¹ Net of future income tax assets.

Explanation of Significant Changes

Accounts receivable

The decrease in accounts receivable of \$6.1 million from December 31, 2008 was primarily due to the seasonal reduction in sales and the corresponding reduction to receivables, partially offset by the increase in receivables relating to pole attachment revenue.

Prepaid expenses

The increase in prepaid expenses of \$6.1 million from December 31, 2008 was due to the timing of the payment of prepaid expenses including insurance, property taxes and water fees.

Regulatory assets

The increase of \$79.8 million in regulatory assets from December 31, 2008 was primarily due to the amendments to GAAP for rate-regulated operations effective on January 1, 2009 which required the recognition at September 30, 2009 of \$78.0 million in future income taxes (net of future income tax assets), offset by a regulatory asset of the same amount.

Property, plant and equipment

The increase of \$60.0 million in property, plant and equipment from December 31, 2008 was comprised of additions to property, plant and equipment of \$69.0 million less depreciation expense of \$20.6 million (total depreciation expense of \$23.3 million includes a provision for future removal and site restoration of \$2.7 million) and depreciation expense of \$0.7 million relating to the Brilliant Terminal Station (“BTS”) asset under a capital lease, the offset of which has been recognized in regulatory assets. Due to amendments to GAAP for rate-regulated operations effective January 1, 2009, the Company reclassified future removal and site restoration costs of \$12.3 million from accumulated depreciation to regulatory liabilities at January 1, 2009.

Current and long-term debt

The \$22.1 million increase in debt from December 31, 2008 to September 30, 2009 was primarily due to the June 2, 2009 issuance of \$105.0 million of senior unsecured Medium Term Note Debentures (“MTN Debentures”). The net proceeds of \$104.5 million were used to repay existing indebtedness, including bank debt and the maturing Series J - \$50.0 million unsecured debenture due July 31, 2009, as well as finance the capital expenditure program and working capital requirements.

Regulatory liabilities

The increase of \$15.2 million in regulatory liabilities from December 31, 2008 was primarily due to the amendments to GAAP for rate-regulated operations effective January 1, 2009 which required the reclassification of \$12.3 million in future removal and site restoration costs from accumulated depreciation to regulatory liabilities at January 1, 2009.

Future income taxes

The increase of \$78.0 million in future income taxes (net of future income tax assets) from December 31, 2008 was primarily due to the amendments to GAAP for rate-regulated operations effective January 1, 2009 which required the recognition at September 30, 2009 of \$78.0 million in future income taxes (net of future income tax assets), offset by a regulatory asset of the same amount.

Share capital

The increase in share capital of \$5.0 million resulted from the issuance of 50,000 common shares for cash consideration of \$5.0 million in the third quarter of 2009.

Retained earnings

The increase of \$18.3 million in retained earnings from December 31, 2008 was due to net earnings in the period of \$28.8 million less dividends paid of \$10.5 million.

CAPITAL RESOURCES & LIQUIDITY

Summary of Consolidated Cash Flows (Unaudited)

| Period Ended September 30 | Quarter | | Year to Date | |
|-------------------------------------|-----------------|----------|-----------------|----------|
| | 2009 | 2008 | 2009 | 2008 |
| (\$000s) | | | | |
| Cash, Beginning of Period | 39,871 | 451 | 40 | - |
| Cash Provided From (Used in) | | | | |
| Operating activities | 30,206 | 16,158 | 63,034 | 64,355 |
| Investing activities | (27,855) | (26,311) | (79,062) | (76,579) |
| Financing activities | (42,062) | 9,761 | 16,148 | 12,283 |
| Cash, End of Period | 160 | 59 | 160 | 59 |

Sources of Capital Resources and Liquidity

FortisBC’s primary sources of liquidity and capital resources are the following:

- funds generated from operations;
- issuances of long-term debt;
- bank financing and operating lines of credit; and

- equity contributions from its parent.

Operating Activities

Cash provided from operating activities was \$30.2 million in the third quarter of 2009, an increase of \$14.0 million compared to \$16.2 million provided by operating activities in the third quarter of 2008. The increase was primarily due to increases in cash provided from non-cash working capital and depreciation.

Year to date, cash provided from operating activities was \$63.0 million, a decrease of \$1.4 million compared to \$64.4 million provided by operating activities for the same period last year. The decrease was primarily due to decreases in cash provided from non-cash operating working capital, partially offset by increases in net earnings and depreciation.

Investing Activities

Cash used for investing activities in the third quarter of 2009 was \$27.9 million, a \$1.6 million increase compared to \$26.3 million invested in the third quarter of 2008. The increased cash used in investing activities was primarily due to an increase in intangible expenditures compared to the same period in 2008.

Year to date, cash used in investing activities was \$79.1 million, a \$2.5 million increase compared to \$76.6 million invested during the same period last year. The increased cash used in investing activities was primarily due to an increase in property, plant and equipment and intangible expenditures, partially offset by a decrease in cash used for non-cash working capital compared to the same period in 2008.

Financing Activities

Cash used in financing activities was \$42.1 million in the third quarter of 2009, a \$51.9 million increase compared to \$9.8 million in cash provided from financing activities in the third quarter of 2008. The increase in cash used in financing activities was primarily due to the repayment of the Series J - \$50.0 million unsecured debenture on July 31, 2009.

Year to date, cash provided by financing activities was \$16.1 million, an increase of \$3.8 million compared to \$12.3 million provided by financing activities during the same period last year. The increase in cash provided by financing activities was primarily due to the June 2, 2009 issuance of \$105.0 million of senior unsecured MTN Debentures. The net proceeds were used for the repayment of the Series J - \$50.0 million unsecured debenture and bank debt, as well as fund the increase in investing activities.

During the three and nine months ended September 30, 2009, the Company paid common share dividends of \$3.5 million (three months ended September 30, 2008 - \$3.5 million) and \$10.5 million (nine months ended September 30, 2008 - \$9.9 million) respectively to its parent, Fortis Pacific Holdings Inc. ("Fortis Pacific"). For the three and nine months ended September 30, 2009, FortisBC issued common shares for proceeds of \$5.0 million, a \$5.0 million decrease compared to the \$10.0 million issued in the comparative periods in 2008.

Capital Structure

FortisBC's business requires the Company to have ongoing access to capital to allow it to build and maintain the electrical systems in its service territory. In accordance with the BCUC's directives and to support investment grade credit ratings, the Company targets a long-term capital structure of 40% equity and 60% debt.

Consolidated Capital Structure (Unaudited)

| | September 30, 2009 | | December 31, 2008 | |
|----------------------|--------------------|--------------|--------------------|---------|
| | (\$ millions) | Percent | (\$ millions) | Percent |
| Total Debt | 554.3 ¹ | 58.8 | 531.5 ² | 59.3 |
| Shareholder's Equity | 388.5 | 41.2 | 365.2 | 40.7 |
| Total | 942.8 | 100.0 | 896.7 | 100.0 |

¹ Excludes debt issue costs of \$5.5 million.

² Excludes debt issue costs of \$4.8 million.

The following table discloses the Company's debenture ratings as of September 30, 2009.

| Rating Agency | Rating | Debt Rated |
|----------------------------------|--------------------------|----------------------------------|
| DBRS Limited | BBB (high), Stable Trend | Secured and Unsecured Debentures |
| Moody's Investors Service | Baa2, Stable Outlook | Unsecured Debentures |

Servicing and Repayment of Debt

FortisBC has authorized bank credit facilities of \$160.0 million, comprised of a \$150.0 million operating credit facility and a \$10.0 million demand overdraft facility. As of September 30, 2009, \$6.6 was drawn against these facilities (December 31, 2008 - \$38.2 million) and \$nil (December 31, 2008 - \$3.0 million) was used to support outstanding letters of credit.

On April 30, 2009, the Company amended its operating credit facility provided by a syndicate of Canadian Chartered Banks. The amended operating credit facility is comprised of a \$50.0 million three-year revolving facility maturing on May 9, 2012 ("Facility A") and a \$100.0 million, 364-day revolving facility maturing on May 6, 2010 ("Facility B"). Two years prior to the current Facility A maturity date, the Company may request an extension of the maturity date for Facility A for a further period of 364 days and if the request for extension is not granted, all amounts outstanding under Facility A become due on the Facility A maturity date. Similarly, prior to the current Facility B maturity date, the Company may request the lenders to extend the term for an additional 364 days and if the request for extension is not granted, Facility B will automatically convert into a non-revolving term credit facility that will mature six months from that date. The operating credit facility also allows the Company to request that the lenders provide up to \$50.0 million of additional financing under Facility A or Facility B or a combination of the two facilities.

Borrowings under the Company's operating credit facilities bear interest at prime plus a margin or the certificate of deposit offered rate for bankers' acceptances plus a margin. The margin applied is based on FortisBC's debt ratings provided by its credit rating agencies. Borrowings under the overdraft facility bear interest at prime.

On May 22, 2009 the Company filed a short form base shelf prospectus to establish a MTN Debentures Program and entered into a Dealers Agreement with certain affiliates of a group of Canadian Chartered Banks. Upon filing the shelf prospectus, the Company may time to time during the 25 month life of the shelf prospectus, issue MTN Debentures in an aggregate principal amount of up to \$300.0 million.

On May 28, 2009, FortisBC entered into an agreement with the dealers listed in the Dealers Agreement to sell \$105.0 million of senior unsecured MTN Debentures. The MTN Debentures bear interest at a rate of 6.10% to be paid semi-annually and mature on June 2, 2039. The closing of the issuance occurred on June 2,

2009, with net proceeds of \$104.5 million being used to repay existing indebtedness and finance the capital expenditure program and working capital requirements.

On July 31, 2009, the Company repaid the Series J - \$50.0 million unsecured debenture in full.

FortisBC expects to meet interest payments on outstanding indebtedness from internally generated funds, but may have to rely upon the proceeds of new financings to meet its principal debt obligations when due.

Capital Program

FortisBC's business is capital intensive and is focused on responding to customer growth and enhancing system reliability and safety through its capital program. Due to the size of the forecast capital program relative to the size of the Company, its implementation, financing and customer rate impacts present key challenges to the Company.

It is expected that capital expenditures in 2009 and beyond will be financed by drawing on the revolving lines of credit, utilizing the proceeds from future debt issues, equity contributions from the parent and from funds generated by operating activities.

On June 27, 2008, FortisBC applied to the BCUC for approval of its 2009-2010 Capital Expenditure Plan ("2009-2010 CEP"). On February 27, 2009, the BCUC approved 2009 capital expenditures of approximately \$151.0 million (net of \$14.0 million in customer contributions) and 2010 capital expenditures of approximately \$141.0 million (net of \$15.0 million in customer contributions). The capital expenditures are necessary to ensure the ability to provide service, public and employee safety and reliability of supply to the Company's growing customer base. The most significant areas of expenditure are those required to expand and upgrade the bulk transmission and distribution system to keep pace with load growth, and to continue the life extension program at FortisBC's generating plants.

FortisBC has forecast 2009 capital expenditures of approximately \$112.7 million, net of \$6.5 million in customer contributions. These capital expenditures estimates, as well as the estimates supporting the 2009-2010 CEP, are based upon detailed forecasts which include assumptions such as customer demand, cost of labour and materials, timing of project implementation, as well as other factors which could change and cause actual capital expenditures to differ from forecast capital expenditures.

During the nine months ended September 30, 2009, FortisBC spent \$74.6 million on the capital program (net of \$4.4 million in customer contributions). The significant capital projects and related expenditures for the nine months ended September 30, 2009 are as follows: \$7.1 million for the Black Mountain Substation Project, \$7.1 million for the Okanagan Transmission Reinforcement Project, \$6.9 million relating to new distribution line extensions for customers, \$6.4 million for the Generation Unit Life Extension program, \$3.4 million for the Ellison Substation Project and \$2.3 million for the Benvoulin Substation Project.

FortisBC recovers capital costs through depreciation which is approved by the BCUC on an annual basis. The BCUC also approves the Capital Plans of the Company; therefore, the majority of capital expenditures receive approval prior to the expenditures being made. The BCUC may order a review of cost variances for individual projects prior to inclusion in rate base or certain major projects may be subject to a "cost collar". Also, the Company is generally required to provide a report to the BCUC upon completion of projects that were subject to the Certificate of Public Convenience and Necessity approval process. In these situations, any variance in costs disallowed by the BCUC would be to the account of the shareholder.

Further information relating to the 2009-2010 Capital Expenditure Plan can be found on the BCUC website (www.bcuc.com).

SHARE CAPITAL

FortisBC has issued and outstanding 1,868,510 common shares, all of which are owned by Fortis through its indirect wholly owned subsidiary, Fortis Pacific.

During the three and nine months ended September 30, 2009, FortisBC issued 50,000 common shares (2008 - 100,000 common shares) for cash consideration of \$5.0 million (2008 - \$10.0 million).

During the three and nine months ended September 30, 2009, FortisBC paid dividends of \$3.5 million (2008 - \$3.5 million) and \$10.5 million (2008 - \$9.9 million) respectively to its parent company, Fortis Pacific.

CONTRACTUAL OBLIGATIONS

Contractual Obligations - Payments Due by Period (Unaudited)

As at September 30, 2009

| | Total | Less than 1 Year | 1-3 Years | 4-5 Years | After 5 Years |
|---|----------------|---------------------|--------------|--------------|------------------|
| (\$ millions) | | | | | |
| Building Leases ¹ | 20.7 | 2.0 | 3.9 | 2.7 | 12.1 |
| Vehicle Leases ² | 0.9 | 0.6 | 0.3 | - | - |
| Brilliant Terminal Station Agreement ³ | 61.1 | 2.6 | 5.1 | 5.1 | 48.3 |
| Power Purchase Obligations ⁴ | 2,799.6 | 38.1 | 77.5 | 75.1 | 2,608.9 |
| Debt Retirement ⁵ | 554.3 | 9.2 | 3.9 | 16.2 | 525.0 |
| Totals | 3,436.6 | 52.5 | 90.7 | 99.1 | 3,194.3 |

¹ Under a sale-leaseback agreement, on September 29, 1993 the Company began leasing its Trail, BC office building for a term of 30 years. The terms of the agreement grant the Company repurchase options at approximately year 20 and approximately year 28 of the lease term. During the year ended December 31, 2007, the Company entered into an agreement to lease an office building owned by a related company, Terasen Gas Inc. During the initial five-year term of the lease commencing January 1, 2008, the Company will make annual payments of \$0.2 million. The Company has two options to renew the lease for additional five-year terms. In addition, the Company has entered into various leases within the Kelowna area for office and warehouse space with terms ranging from two to five years.

² These vehicle leases generally provide for the Company to pay the taxes, maintenance, insurance and certain other operating costs of the leased property, and typically have a lease term of two to five years.

³ On July 15, 2003, the Company began operating the Brilliant Terminal Station ("BTS") under an agreement the term of which expires in 2056 (unless the Company has earlier terminated the agreement by exercising its right, at any time after the anniversary date of the agreement in 2029, to give 36 months' notice of termination). The BTS is jointly owned by the Columbia Power Corporation and the Columbia Basin Trust (the "Owners") and used by the Company on its own behalf and on behalf of the Owners. The agreement provides that FortisBC will pay the Owners a charge related to the recovery of the capital cost of the BTS and related operating costs.

⁴ Power purchase obligations of FortisBC include the Brilliant Power Purchase Agreement (the "BPPA") and the Power Purchase Agreement with BC Hydro (the "PPA"). On May 3, 1996, an Order was granted by the BCUC approving the 60-year BPPA for the output of the Brilliant hydroelectric plant located near Castlegar, BC. The BPPA requires payments based on the operation and maintenance costs and a return on capital for the plant, in exchange for the specified take-or-pay amounts of power. The BPPA includes a market related price adjustment after 30 years of the 60-year term. The PPA, which expires in 2013, provides for any amount of supply up to a maximum of 200 MW but includes a take-or-pay provision based on a 5-year rolling nomination of the capacity requirements.

⁵ Excludes debt issue costs.

RELATED PARTY TRANSACTIONS

In the normal course of business, the Company transacts with its parent and other related companies under common control. The following transactions were measured at the exchange amount.

Inter-corporate Charges (Unaudited)

| Period Ended September 30 | Quarter | | Year to Date | |
|--|---------|-------|--------------|-------|
| | 2009 | 2008 | 2009 | 2008 |
| (\$000s) | | | | |
| Revenue charged to related parties | 135 | 112 | 393 | 426 |
| Operating costs charged by related parties | 449 | 330 | 1,410 | 1,249 |
| Operating costs recovered from related parties | 1,607 | 1,195 | 4,392 | 4,391 |
| Interest revenue on accounts receivable | 2 | 7 | 8 | 20 |
| Capital costs charged from related parties | 43 | - | 43 | 159 |

The revenues charged represent electricity and services sold to related parties.

The operating costs charged consist of information technology expenses, contract and direct labour charges, meter shop charges, stock options, rent, natural gas utility charges consumed in operating the Company's facilities, and corporate governance costs.

The operating costs recovered consist of labour and materials charges to the Company's parent and other related parties.

Included in accounts receivable are amounts due from Fortis Pacific which bear interest at prime. Interest on the related party accounts receivable was recorded in other revenue.

Capital costs charged consist of electrical equipment sold to the Company by a related Fortis subsidiary.

Inter-corporate charges between FortisBC and other related companies under common control are included in accounts receivable and accounts payable and are unsecured and due on demand. Also included in accounts receivable are amounts due from officers of the Company for employee share purchase plan loans and stock option loans which are non-interest bearing and due within one to two years from the grant date.

Amounts due to and from the Company's parent, and other related companies under common control and officers of the Company are as follows:

Inter-corporate Charges (Unaudited)

| | September 30, 2009 | December 31, 2008 |
|--|--------------------|-------------------|
| (\$000s) | | |
| Included in accounts receivable | \$ 723 | 621 |
| Included in accounts payable and accrued liabilities | 374 | 344 |

QUARTERLY RESULTS

The following table sets forth unaudited quarterly information for each of the eight quarters ended December 31, 2007 through September 30, 2009. The information has been obtained from the Company's unaudited

interim consolidated financial statements which, in the opinion of management, have been prepared in accordance with GAAP for rate-regulated entities. The timing of the recognition of certain assets, liabilities, revenues and expenses as a result of regulation may differ from that otherwise expected using GAAP for companies not subject to rate regulation. Past operating results are not necessarily indicative of results for any future period and should not be relied upon to predict future performance.

Summary of Consolidated Quarterly Results (Unaudited)

| Quarter Ended | Electricity Revenue | Net Earnings |
|--------------------|---------------------|--------------|
| (\$000s) | | |
| September 30, 2009 | 54,481 | 8,276 |
| June 30, 2009 | 51,609 | 7,398 |
| March 31, 2009 | 68,492 | 13,160 |
| December 31, 2008 | 60,670 | 6,177 |
| September 30, 2008 | 50,452 | 8,533 |
| June 30, 2008 | 48,547 | 6,346 |
| March 31, 2008 | 63,008 | 11,608 |
| December 31, 2007 | 56,799 | 6,035 |

A summary of the past eight quarters reflects FortisBC's growth as well as the seasonality associated with the Company's business. The operations generally produce higher earnings in the first quarter of the fiscal year due to increased customer load as a result of cooler weather, while certain expenses such as depreciation, interest and operating expenses remain more evenly distributed throughout the fiscal year.

December 2007/2008 - The increase in revenues was primarily due to a 2.9% rate increase effective January 1, 2008 and a 0.8% rate increase effective May 1, 2008. Despite the increase in electricity revenue, net earnings were relatively consistent due to increases in certain other costs during the fourth quarter of 2008 compared to the same period in 2007.

March 2008/2009 - The increase in revenues and earnings was primarily due to a 4.6% rate increase effective January 1, 2009 and increased electricity sales resulting from customer growth and cooler temperatures.

June 2008/2009 - The increase in revenues and earnings was primarily due to a 4.6% rate increase effective January 1, 2009 and increased electricity sales resulting from customer growth.

September 2008/2009 - The increase in revenues was primarily due to a 4.6% rate increase effective January 1, 2009, a 2.2% rate increase effective September 1, 2009 and increased electricity sales resulting from customer growth. Despite the increase in electricity revenue, net earnings were relatively consistent due to increases in certain other costs during the third quarter of 2009 compared to the same period in 2008.

OFF-BALANCE SHEET ARRANGEMENTS

Disclosure is required of all off-balance sheet arrangements such as transactions, agreements or contractual arrangements with unconsolidated entities, structured finance entities, special purpose entities or variable interest entities that are reasonably likely to materially affect liquidity or the availability of, or requirements for, capital resources. The Company has no such off-balance sheet arrangements.

CRITICAL ACCOUNTING ESTIMATES

The preparation of the Company's financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of revenues and expenses during the periods. Certain estimates are also necessary since the regulatory environment in which the Company operates often requires amounts to be recorded at estimated values until finalization and adjustment, if any, is determined pursuant to subsequent regulatory decisions or other regulatory proceedings. Due to the inherent uncertainty in making such estimates, actual results reported in future periods could differ materially from those estimated. Any such adjustments, which could be material, will be recorded in the period they become known.

There were no material changes to the Company's critical accounting estimates during the three and nine months ended September 30, 2009 from those disclosed in the Management Discussion and Analysis for the year ended December 31, 2008 other than noted below.

Effective January 1, 2009, GAAP for rate-regulated operations has been amended to require the recognition of future income tax liabilities and assets. Future income taxes are recognized based upon temporary differences between the accounting and tax basis of existing assets and liabilities, the benefit of income tax reductions or tax losses available to be carried forward and the effects of changes in tax laws. The carrying amounts of assets and liabilities are based upon the amounts recorded in the financial statements and are therefore subject to accounting estimates that are inherent to those balances. The timing of the reversal of temporary differences is estimated based upon assumptions of expectations of future results of operations. The composition of future income tax liabilities is reasonably likely to change from period to period because of changes in the estimation of these uncertainties.

CHANGES IN ACCOUNTING POLICIES

Effective January 1, 2009, FortisBC adopted the following new accounting standards issued by the Canadian Institute of Chartered Accountants ("CICA").

- a) Amendments to Section 1100, *Generally Accepted Accounting Principles* and Section 3465, *Income Taxes* which resulted from a Decision Summary issued by the Accounting Standards Board ("AcSB") in August 2007. The standards prior to the amendments were intended to reflect the unique characteristics of rate-regulated operations, specifically how rate regulation may result in assets and liabilities which meet the asset and liability definitions of the CICA Handbook. The Decision Summary determined that prospectively for fiscal years beginning on or after January 1, 2009:
 - The temporary exemption in Section 1100, *Generally Accepted Accounting Principles*, providing relief to entities subject to rate regulation from the requirement to apply Section 1100 to the recognition and measurement of assets and liabilities arising from rate regulation has been removed.
 - Section 3465, *Income Taxes*, has been amended to require the recognition of future income tax liabilities and assets as well as a regulatory asset or liability for the amount of future income taxes expected to be recovered from or returned to customers in future rates.

The AcSB also decided that the current guidance pertaining to rate-regulated operations in Section 1600, *Consolidated Financial Statements*, Section 3061, *Property, Plant and Equipment*, Section 3475, *Disposal of Long Lived Assets and Discontinued Operations*, and AcG-19, *Disclosures by Entities Subject to Rate Regulation* be retained.

Effective January 1, 2009, the Company applied the amended Section 1100 to the recognition and measurement of assets and liabilities arising from rate regulation. Certain assets and liabilities arising

from rate regulation continue to have specific guidance under a primary source of GAAP that applies only to the particular circumstances described therein, including those arising under Sections 1600, 3061 and 3475. Certain of the Company's assets and liabilities arising from rate regulation do not have specific guidance under a primary source of GAAP. In absence of primary sources of GAAP, Section 1100 directs the Company to adopt accounting policies that are developed through the exercise of professional judgment and the application of concepts described in Section 1000, *Financial Statement Concepts*. In developing these accounting policies, Section 1100 directs entities to consult other sources, including pronouncements issued by bodies authorized to issue accounting standards in other jurisdictions. In accordance with Section 1100, the Company has determined that certain of its assets and liabilities qualify for recognition under GAAP and this recognition is generally consistent with the accounting prescribed by the U.S. Financial Accounting Standards Board's Statement of Accounting Standards Codification No.980, *Regulated Operations* ("ASC 980"), formerly known as Financial Accounting Standards No. 71, *Accounting for the Effects of Certain Types of Regulation*. ASC 980 is the prevailing guidance to which the Company will refer to for the development of accounting policies and disclosures relating to certain of its assets and liabilities arising from rate regulation where there are no primary sources of GAAP available. The Company has determined that its regulatory assets and liabilities recognized in the financial statements prior and subsequent to January 1, 2009 comply with the recognition and presentation criteria under Section 1000 and ASC 980 and therefore will continue to exist under GAAP. Adoption of the amended Section 1100 standard resulted in the balance sheet changes discussed below.

Future Removal and Site Restoration

Included in FortisBC's depreciation rates is a provision for future removal and site restoration costs. Prior to January 1, 2009, actual costs of removal and site restoration incurred were recorded against accumulated depreciation as the assets were disposed of. In the absence of rate regulation, the removal and site restoration costs would be expensed in the period incurred. Effective January 1, 2009, the Company has prospectively applied the practice, consistent with other rate-regulated companies that follow ASC 980, of removing the net future site restoration provision from accumulated depreciation and reclassifying it as a long-term regulatory liability. Effective January 1, 2009, the Company reclassified \$12.3 million with no impact on earnings.

Future Income Tax

Effective January 1, 2009, the impact on FortisBC of the amendments to Section 3465, is the prospective recognition of future income taxes and a separate regulatory asset or liability for the amount of future income taxes expected to be included in future rates and recovered from or returned to customers. Prior to January 1, 2009, the Company used the taxes payable method of accounting for income taxes on regulated earnings. As a result of the Company adopting the amendment to Section 3465, the Company has changed its accounting policy to account for income taxes using the asset and liability method. Under this method, future tax assets and liabilities are recognized for temporary differences between the accounting and tax basis of existing assets and liabilities, the benefit of income tax reductions or tax losses available to be carried forward and the effects of changes in tax laws and enacted or substantially enacted tax rates. The effect to the Company's September 30, 2009 interim financial statements is an increase to future income taxes (net of future income tax assets) of \$78.0 million (January 1, 2009 - \$73.8 million), including an amount associated with income taxes that will become payable on future revenues as they are collected from customers when the tax timing differences reverse. There is a corresponding increase in regulatory assets of \$78.0 million (January 1, 2009 - \$73.8 million) and no impact to earnings.

- b) Section 3064, *Goodwill and Intangible Assets*, converges GAAP for goodwill and intangible assets with International Financial Reporting Standards. The new standard provides more comprehensive guidance on intangible assets, particularly for internally developed intangible assets. Under Section 1506, *Changes in Accounting Policy*, the adoption of this new Section is to be applied retrospectively in the Company's

financial statements. Effective January 1, 2009 and December 31, 2008, the Company reclassified \$14.9 million in software costs and \$20.5 million in right of way costs from property, plant and equipment to intangibles. The reclassification resulted in no impact on earnings.

- c) Emerging Issues Committee-173 (“EIC-173”), *Credit Risk and the Fair Value of Financial Assets and Financial Liabilities*, requires that the Company’s own credit risk and the credit risk of its counterparties be taken into account in determining the fair value of a financial instrument. There was no effect on the Company’s financial statements as a result of adopting EIC-173.

FUTURE ACCOUNTING PRONOUNCEMENTS

International Financial Reporting Standards (“IFRS”)

In February 2008, the Accounting Standards Board (“AcSB”) confirmed that the use of IFRS will be required in 2011 for publicly accountable enterprises in Canada. In March 2009, the AcSB issued a second IFRS Omnibus Exposure Draft confirming that publicly accountable enterprises be required to apply IFRS, in full and without modification, on January 1, 2011. The transition date of January 1, 2011 will require the restatement, for comparative purposes, of amounts reported by the Company for its year ended December 31, 2010, and of the opening IFRS balance sheet as at January 1, 2010.

The Company is continuing to assess the financial reporting impacts of adopting IFRS in 2011. While the impact on future financial position and results of operations is not fully determinable or estimable at this time, proposals put forth by the International Accounting Standards Board (“IASB”) in its July 2009 Exposure Draft on *Rate-regulated Activities*, if adopted, should reduce earnings volatility that may have otherwise resulted under IFRS in the absence of an accounting standard for rate-regulated activities. The Company also anticipates a significant increase in disclosure resulting from the adoption of IFRS and is continuing to assess the additional disclosure requirements as well as information systems changes that will be necessary to gather and compile the required disclosure.

Differences between IFRS and GAAP, in addition to those referred to below under “Accounting Policy Impacts and Decisions”, may continue to be identified based on further detailed analysis by the Company, the outcome of a final standard on accounting for rate-regulated activities and other changes in IFRS prior to the Company’s conversion to IFRS in 2011.

IFRS Conversion Project: Fortis and its subsidiaries, including FortisBC, commenced an IFRS conversion project in 2007 and have established a formal project governance structure. Reporting on the IFRS conversion project occurs to senior executive management and the Audit and Risk Committee of the Board of Directors of FortisBC.

The IFRS conversion project consists of three phases: Scoping and Diagnostics, Analysis and Development, and Implementation and Review.

Phase One: Scoping and Diagnostics, which involved project planning and staffing and identification of differences between current GAAP and IFRS, has been completed. The resulting identified areas of accounting difference of highest potential impact to the Company, based on existing IFRS at the time, were identified to include rate-regulated accounting; property plant and equipment; provisions and contingent liabilities; employee benefits; impairment of assets; income taxes; and, initial adoption of IFRS under the provisions of IFRS 1, *First-Time Adoption of International Financial Reporting Standards*.

Phase Two: Analysis and Development is nearing completion, and involves detailed diagnostics and evaluation of the financial impacts of various options and alternative methodologies provided for under IFRS; identification and design of operational and financial business processes; initial staff training and audit

committee orientation; analysis of IFRS 1 optional exemptions and mandatory exceptions to the general requirement for full retrospective application upon transition to IFRS; summarization of 2011 IFRS disclosure requirements; and development of required solutions to address identified issues.

Phase Three: Implementation and Review has commenced and involves the execution of changes to information systems and business processes; completion of formal authorization processes to approve recommended accounting policy changes; and further training programs across the Company's finance and other affected areas, as necessary. It will culminate in the collection of financial information necessary to compile IFRS-compliant financial statements and reconciliations; embedding of IFRS in business processes; and audit committee approval of IFRS-compliant interim and annual financial statements for 2011.

Accounting for Rate-Regulated Activities under IFRS: IFRS does not provide specific guidance with respect to accounting for rate-regulated activities. However, in December 2008, the IASB initiated a project on accounting for rate-regulated activities and whether or not rate-regulated entities could or should recognize assets or liabilities as a result of rate-regulation imposed by a regulatory body.

On July 23, 2009, the IASB issued an Exposure Draft on *Rate-regulated Activities*. Comments on the Exposure Draft are to be submitted for consideration by the IASB by November 20, 2009. Based on the current project timeline of the IASB, a final standard is expected to be issued in the second quarter of 2010.

Based on the Exposure Draft as it currently exists, regulatory assets and liabilities arising from activities subject to cost-of-service regulation may be recognized under IFRS when certain conditions are met. The ability to record regulatory assets and liabilities, as proposed in the Exposure Draft, could reduce the Company's earnings volatility that may have otherwise resulted under IFRS, however it will result in the requirement to provide enhanced balance sheet presentation and note disclosures. However, uncertainty as to the final outcome of this Exposure Draft, and the final standard on accounting for rate-regulated activities under IFRS, has resulted in FortisBC being unable to reasonably estimate and conclude on the impact on the Company's future financial position and results of operations with respect to differences, if any, in accounting for rate-regulated activities under IFRS versus GAAP.

During the second quarter of 2009, FortisBC, along with the other primary regulated utilities in British Columbia, drafted a set of IFRS guidelines for use in regulatory applications being submitted by the utilities to the BCUC. On October 1, 2009 FortisBC filed its Preliminary 2010 Revenue Requirements Application with the BCUC to set customer electricity rates for 2010. Included in the application are the IFRS issues expected to affect the Company on transition to IFRS.

The Company will continue to work with the BCUC to identify IFRS transitional issues and suggest how the issues might be addressed.

Accounting Policy Impacts and Decisions: The Company has completed an initial assessment of the impacts of adopting IFRS, based on the standards as they currently exist, and has identified the following as having the greatest potential to impact the Company's accounting policies, financial reporting and information systems requirements upon conversion to IFRS. Final conclusions cannot be reached at this time with respect to the Company's rate-regulated operations pending further certainty as to a final IFRS standard on accounting for rate-regulated activities.

(a) *Property Plant and Equipment*

IFRS and GAAP contain the same basic principles of accounting for property, plant and equipment; however, differences in application do exist. For example, capitalization of directly attributable costs in accordance with IAS 16, *Property Plant and Equipment* may require measurement of an item of

property, plant and equipment upon initial recognition to include or exclude certain previously recognized amounts under GAAP. Specifically, there may be changes in accounting for:

- i) the amount of capitalized overheads;
- ii) the capitalization of major inspections that were previously expensed under GAAP;
- iii) the capitalization of depreciation for which the future economic benefits of that asset are absorbed in the production of another asset; and
- iv) the capitalization of borrowing costs in accordance with IAS 23, *Borrowing Costs*.

However, the IASB's Exposure Draft on *Rate-regulated Activities* proposes that, in the case of qualifying rate-regulated entities, amounts approved by the regulator for inclusion in the cost of self-constructed property, plant and equipment for rate-making purposes shall also be included in the cost of these assets for financial reporting purposes, even if the entity would not otherwise be permitted to include these costs in the cost of its property, plant and equipment based on application of IAS 16.

IAS 16 also requires an allocation of the amount initially recognized in respect of an item of property, plant and equipment to its significant parts and the depreciation of each such part separately. This method of componentizing property, plant and equipment may result in an increase in the number of component parts that are recorded and depreciated and, as a result, may impact the calculation of depreciation expense.

The Exposure Draft on *Rate-regulated Activities* proposes a new transitional exemption for qualifying rate-regulated entities that will allow them to use, as of the date of transition, the carrying amount of property, plant and equipment under GAAP as the deemed cost under IFRS. The Company will likely avail of this exemption, should the Exposure Draft be adopted as proposed.

The final extent of the impact of applying IAS 16 by the Company, and elective options with respect to accounting for property, plant and equipment upon transition to IFRS, cannot be made at this time pending further certainty as to a final standard on accounting for rate-regulated activities.

(b) *Provisions and Contingent Liabilities*

IAS 37, *Provisions, Contingent Liabilities and Contingent Assets* requires a provision to be recognized when (i) there is a present obligation as a result of a past transaction or event; (ii) it is probable that an outflow of resources will be required to settle the obligation; and (iii) a reliable estimate can be made of the obligation. The threshold for recognition of a provision under GAAP is higher than under IFRS. It is possible, therefore, that some contingent liabilities which would not have been recognized under GAAP may meet the criteria for recognition as a provision under IFRS.

(c) *Employee Benefits*

IAS 19, *Employee Benefits* requires the past service cost element of defined benefit plans to be expensed on an accelerated basis, with vested past service costs being expensed immediately and unvested past service costs being recognized on a straight-line basis until the benefits become vested. In addition, actuarial gains and losses are permitted under IAS 19 to be recognized directly in equity rather than through earnings, and IFRS 1 also provides an option to recognize immediately in retained earnings all cumulative actuarial gains and losses existing as at the date of transition to IFRS.

Under GAAP, past service costs are generally amortized on a straight-line basis over the expected average remaining service period of active employees in the defined benefit plan.

The Company maintains defined benefit pension plans, defined contribution pension plans and supplementary and other post-employment benefit plans which will be subject to different accounting treatment under IFRS as compared to GAAP. The full extent of the impact of applying IAS 19 cannot be

made at this time, pending further certainty as to a final standard on accounting for rate-regulated activities.

(d) *Impairment of Assets*

IAS 36, *Impairment of Assets* uses a one-step approach for testing and measuring asset impairments, with asset carrying values being compared to the higher of value in use and fair value less costs to sell. Value in use is defined as being equal to the present value of future cash flows expected to be derived from the asset. In the absence of an active market, fair value less costs to sell may also be determined using discounted cash flows. The use of discounted cash flows under IFRS to test and measure asset impairment differs from GAAP where undiscounted future cash flows are used to compare against the asset's carrying value to determine if impairment exists. This may result in more frequent write-downs in the carrying value of assets under IFRS since asset carrying values that were previously supported under GAAP based on undiscounted cash flows may not be supported on a discounted cash flow basis under IFRS. However, under IAS 36, previous impairment losses may be reversed where circumstances change such that the impairment has reduced. This also differs from GAAP, which prohibits the reversal of previously recognized impairment losses.

The majority of the Company's assets are rate-regulated and the potential for and extent of impairment losses on these assets will be primarily subject to the continued ability of the Company to recover costs through the regulatory process.

The Company's other non-regulated assets will be subject to the one-step approach under IFRS for testing and measuring asset impairments which may result in some impairments being recognized or reversed under IFRS that would not have been required or permitted under GAAP.

(e) *Income Taxes*

IAS 12, *Income Taxes* prescribes that an entity account for the tax consequences of transactions and other events in the same way that it accounts for the transactions and other events themselves. Therefore, where transactions and other events are recognized in earnings, the recognition of deferred tax assets or liabilities which arise from those transactions should also be recorded in earnings. For transactions that are recognized outside of the statement of earnings, either in other comprehensive income or directly in equity, any related tax effects should also be recognized outside of the statement of earnings.

The most significant impact of IAS 12 on the Company will be derived directly from the accounting policy decisions made under IAS 16. In addition, the Company currently accounts for income taxes based on regulatory decisions. Therefore, the impact on the Company of accounting for the tax consequences of transactions and other events under IFRS versus GAAP cannot be fully determined at this time pending further certainty as to a final IFRS standard on accounting for rate-regulated activities.

(f) *IFRS 1, First-Time Adoption of International Financial Reporting Standards*

IFRS 1 provides the framework for the first time adoption of IFRS and specifies that, in general, an entity shall apply the principles under IFRS retrospectively. IFRS 1 also specifies that the adjustments that arise on retrospective conversion to IFRS from other GAAP should be directly recognized in retained earnings. Certain optional exemptions and mandatory exceptions to retrospective application are provided for under IFRS 1.

The Company has completed an analysis of IFRS 1. While preliminary decisions have been made with respect to the elective exemptions available upon transition, final decisions cannot be made at this time pending further certainty as to a final IFRS standard on the accounting for rate-regulated activities.

(g) *Internal Controls over Financial Reporting and Disclosure*

In accordance with the Company's approach to certification of internal controls required under Canadian Securities Administrators' National Instrument 52-109, all entity level, information technology, disclosure and business process controls will require updating and testing to reflect changes arising from the Company's conversion to IFRS. Where material changes are identified, these changes will be mapped and tested to ensure that no material deficiencies exist as a result of the Company's conversion to these new accounting standards.

(h) *Information Systems*

It is anticipated that the adoption of IFRS will have an impact on information systems requirements. The Company has assessed the need for systems upgrades or modifications to ensure an efficient conversion to IFRS. The extent of the impact on the Company's information systems is largely dependent upon certainty as to a final IFRS standard on accounting for rate-regulated activities and is, therefore, not fully determinable at this time.

The IASB has a number of on-going projects on its agenda, in addition to the project on accounting for rate-regulated activities, that may result in changes to existing IFRS prior to the Company's conversion in 2011. The Company continues to monitor these projects and the impact that any resulting IFRS changes may have on its anticipated accounting policies, financial position or results of operations under IFRS for 2011 and beyond.

Section 3862, *Financial Instruments - Disclosures*

This Section was amended in June 2009 to improve the disclosure surrounding fair value and liquidity risk. The amendment was a response to calls by users of financial statements and others for enhanced disclosures in light of current market conditions and concerns that the nature and extent of liquidity risk disclosure requirements were unclear and difficult to apply. The amended section clarifies that liquidity risk disclosures are required only for financial liabilities that result in the outflow of cash or another financial asset; require entities to provide quantitative disclosures based on how they manage liquidity risk for derivative financial liabilities; require entities to disclose the remaining expected maturities of non-derivative financial liabilities if they manage liquidity risk on the basis of expected maturities; and strengthen the relationship between qualitative and quantitative disclosures about liquidity risk. The amended section is to be applied prospectively and is effective for FortisBC's annual financial statements for the year ended December 31, 2009. This amended accounting policy is not expected to have a significant impact on FortisBC's annual financial statements.

BUSINESS OUTLOOK

Regulatory

The Company would expect earnings to grow in future years assuming a consistently applied regulated capital structure, no material reduction in the allowed return on equity, recovery of its cost-of-service components in rates, and growth in rate base assets as a result of its annual capital expenditures.

The BC Energy Plan

The British Columbia provincial government released its Energy Plan on February 27, 2007. The plan is a natural progression from the previous plan with consistent principles and a strong focus on environmental leadership, energy conservation and efficiency, and investing in innovation. This focus manifests itself by setting specific goals and timelines in these three areas. In particular, the Energy Plan outlines various measures to address the challenges of global warming including that all electricity produced in British Columbia will be required to have zero net greenhouse gas emissions by 2016. The plan places a great deal of responsibility on British Columbians to conserve energy by acquiring 50% of the province's incremental

resource needs through conservation by 2020. The plan emphasizes efficiency by requiring BC Hydro to eliminate electricity imports and become fully self-sufficient by 2016. The Energy Plan also states that 90% of British Columbia's electricity will come from renewable resources and that British Columbia will become the first jurisdiction in North America to require 100% carbon sequestration for any coal-fired electricity project. FortisBC continues to assess the impacts and opportunities provided by the plan, and will consider which policy actions it may support. Many of the principles of the Energy Plan were adopted when Bill 15-2008, the *Utilities Commission Amendment Act, 2008*, received Royal Assent by the Legislative Assembly of British Columbia on May 1, 2008. The Energy Plan is available on the following website: www.energyplan.gov.bc.ca.

Collective Agreements

The Collective Agreement between the Company and Local 213 of the International Brotherhood of Electrical Workers ("IBEW") expires on January 31, 2013. IBEW represents employees in specified occupations in the areas of generation, transmission and distribution. The Collective Agreement between the Company and Local 378 of the Canadian Office and Professional Employees Union expires January 31, 2011.

Business Risk Management

For more information with respect to risks and uncertainties, reference is made to the subsection entitled "Business Risk Management" in the Company's Management Discussion and Analysis for the year ended December 31, 2008.

Contingency

The Province of British Columbia has alleged breaches of the Forest Practices Code and negligence relating to a forest fire near Vaseux Lake and has filed and served a Writ and Statement of Claim against FortisBC. In addition, private land owners have filed a separate Writ and Statement of Claim in relation to the same matter. FortisBC is communicating with its insurers and has filed a Statement of Defence in relation to both of the actions. The outcome cannot be reasonably determined and estimated at this time, and accordingly no amount has been accrued in the financial statements.

STRATEGY AND VISION

FortisBC is an electric utility company, generating, transmitting and distributing electricity to homes and businesses in the southern interior of British Columbia. FortisBC employees are committed to safety, providing excellent customer service, and conducting business in an environmentally responsible manner.

CORPORATE INFORMATION

All the common shares of FortisBC are owned by Fortis Inc. (“Fortis”) through its indirect wholly owned subsidiary, Fortis Pacific Holdings Inc. Fortis is the largest investor-owned distribution utility in Canada. Its regulated holdings include a natural gas utility in British Columbia and electric utilities in five Canadian provinces and three Caribbean countries. Fortis owns non-regulated hydroelectric generation assets across Canada and in Belize and upper New York State. It also owns hotels and commercial real estate in Canada. Fortis shares are listed on the Toronto Stock Exchange and trade under the symbol FTS. Additional information can be accessed at www.fortisinc.com or www.sedar.com.

Board of Directors:

Beth Campbell, William J. (Bill) Daley, Walter Gray, R.L. (Randy) Jespersen, Stanley Marshall, Roger Mayer, John McCallum, Harry McWatters and John Walker.

Executive Team:

| | |
|-----------------|---|
| John Walker | <i>President and Chief Executive Officer</i> |
| Don Debiegne | <i>Vice President, Power Supply and Strategic Planning</i> |
| Doyle Sam | <i>Vice President, Engineering and Operations</i> |
| Michele Leeners | <i>Vice President, Finance and Chief Financial Officer</i> |
| Michael Mulcahy | <i>Vice President, Customer and Corporate Services</i> |
| David Bennett | <i>Vice President, Regulatory Affairs and General Counsel</i> |

Additional information about FortisBC Inc. is available on Sedar at www.sedar.com.

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