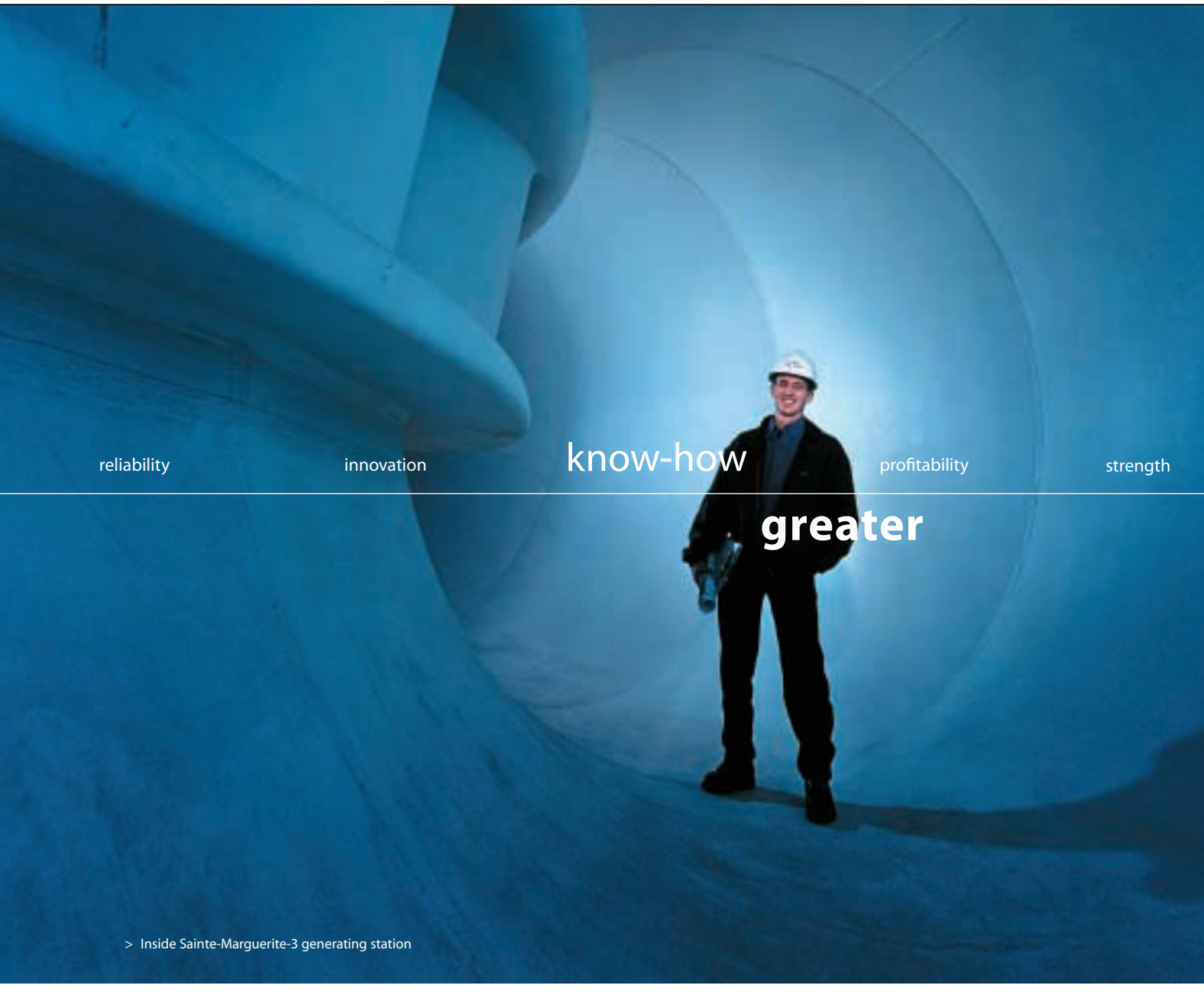
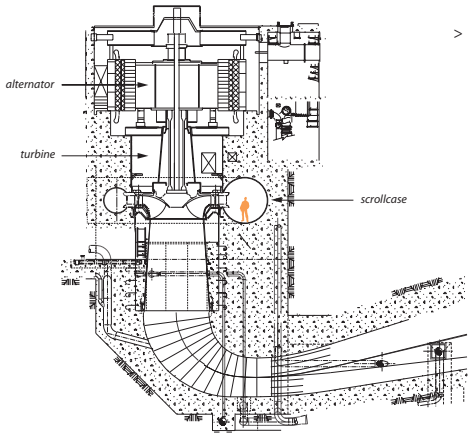
Hydro Québec




> Inside Sainte-Marguerite-3 generating station




> Cross-section of the generating unit and scrollcase shown on the cover

foresight diligence integrity leadership presence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**greater**

commitment determination **expertise** depth knowledge

The deregulation of the North American power market, combined with the fast pace of technological innovation and the widespread use of information technologies, has radically altered the power industry.

More than ever before, Hydro-Québec brings together such qualities as rigor, imagination, daring and commitment to meet the challenge of competition.

With its increasingly efficient, profitable organization, it is in a position to provide all Quebecers with the benefit of clean energy, at highly competitive costs and conditions.

Making the most of its world-class expertise also allows the company to generate additional revenue and to contribute, along with all its partners, to the growth of the Québec economy.

Hydro-Québec is a leading producer of energy and a major North American distributor. Its system includes 32,283 kilometres of transmission lines and 106,448 kilometres of distribution lines.

The company offers its customers energy services either directly or through its TransÉnergie division, its subsidiaries or other companies in which it has a stake.

Most of Hydro-Québec's generating output is sold on the Québec market, under conditions that are set by law. This market has a customer base of over 3.5 million and enjoys low, stable rates.

Hydro-Québec also has dealings with dozens of electric utilities in the northeastern United States, Ontario and New Brunswick.

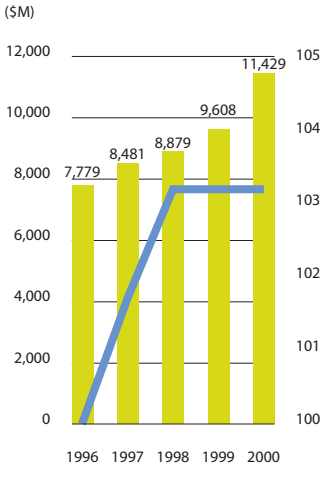
Known worldwide for its expertise, Hydro-Québec has numerous major projects to its credit, mainly in the areas of hydroelectric generation, transmission and distribution.

Hydro-Québec has a single shareholder, the Québec government.

**greater**

| ($M) | 2000 | 1999 | Change (%) |
|---|---|---|---|
| **Operations and Dividends** | | | |
| Revenue | **11,429** | 9,608 | 19 |
| Net income | **1,078** | 906 | 19 |
| Dividends | **539** | 453 | 19 |
| **Balance Sheet** | | | |
| Total assets | **59,111** | 56,836 | 4 |
| Long-term debt | **34,887** | 36,011 | (3) |
| Shareholder's equity | **14,280** | 13,741 | 4 |
| **Cash Flows** | | | |
| Operating activities | **3,345** | 2,884 | 16 |
| Investing activities | **(3,621)** | (2,227) | 63 |
| Financing activities | **353** | 590 | (40) |
| Cash and cash equivalents at end of year | **177** | 100 | 77 |
| **Ratios (%)** | | | |
| Return on equity | **7.7** | 6.7 | 15 |
| Return on revenue | **9.4** | 9.4 | – |
| Capitalization | **26.2** | 26.2 | – |
| Self-financing | **49.8** | 59.5 | (16) |

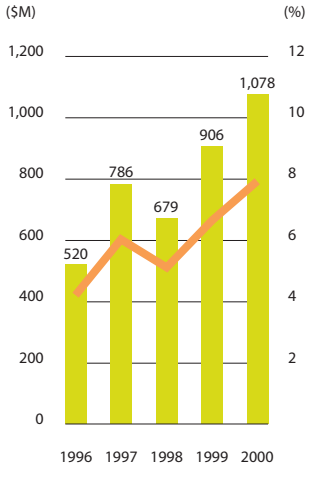
**Sales and average rate increase index**




Sales
Average rate increase index

For the past two years, we have increased sales while still fulfilling our commitment to freeze rates for Québec customers since May 1998. This growth has been driven by electricity sales in Québec and the United States.

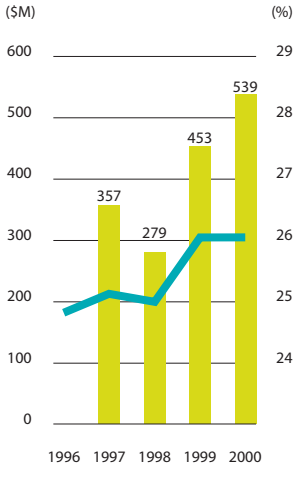
**Net income and return on equity**




Net income
Return on equity

This year, net income topped $1 billion for the first time. Return on equity reached 7.7%, drawing closer to the 9.8% target set in the *Strategic Plan 2000-2004*. While taking steps to improve customer service, we have consistently increased the return to our shareholder.

**Dividends paid and capitalization**




Dividends paid
Capitalization

Once again this year, our improved financial position is reflected in our capitalization rate of 26.2%, which allows us to pay dividends. We paid our shareholder, the Québec government, a fourth consecutive dividend, for a cumulative amount of $1.6 billion.

**04**

> L. Jacques Ménard
> André Caillé

In 2000, Hydro-Québec continued to progress toward achieving the objectives in the *Strategic Plan 2000-2004*.

**RENEWED COMMITMENT**

As stated in our commitment, rates have remained unchanged since 1998 for all of our Québec customers. And we hope to maintain these low rates through improved profitability.

Ongoing improvement in customer service is still a top priority. Following an in-depth analysis of the needs and expectations of our various clienteles, we established a business strategy and focus aimed at broadening our service offering.

We launched several projects to strengthen the entire distribution system in order to assure our customers of a continuous power supply—a central component of our mission.

Major work proceeded on the transmission system to improve the security of supply. The loops serving downtown Montréal, the Mauricie region, downtown Québec City and the Gaspé peninsula were completed and commissioned.

As a result of all the initiatives taken during the year, the average number of hours of service interruption was reduced by about 17%.

**READILY ACCESSIBLE SERVICES**

Considerable effort went into improving our response to customer expectations. For new connections, the percentage of requests filled on schedule was 88%—up from 71% in 1999. We also continued to make our services more readily accessible, upgrade the quality of information provided and diligently follow up on customer requests.

Our large-power customers, who account for more than 40% of our Québec sales, continue to enjoy rates that are among the most competitive in the world. The quality partnership meetings bolstered our advisory role with these customers, resulting in a very high level of satisfaction.

**MORE AUTONOMOUS BUSINESS UNITS**

In organizational terms, we unbundled our distribution and generation activities as required by the *Act to amend the Act respecting the Régie de l'énergie*, adopted in 2000, which deregulates power production in Québec. The main purpose of this law is to preserve the social pact on electricity and to guarantee that Québec consumers will continue to benefit from low rates, particularly in the residential sector. To this end, the government established a heritage pool giving Québec consumers access to a maximum of 165 TWh/year of Hydro-Québec's generating output and existing long-term supply contracts at a fixed price of 2.79¢/kWh. Beyond that volume, the law opens the wholesale market up to competition. Hydro-Québec's transmission and distribution costs, which are still set by the Régie de l'énergie, are added to the cost of supply.

We also proceeded to restructure various responsibilities into three main business units: the Generator, the Transmission Provider and the Distributor. With recognized expertise in their respective fields, these units will be better able than ever to play a part in achieving our objectives.

Each business unit must now define its own portfolio of technological innovation projects. Since 1999, each unit has also been responsible for carrying out international projects in its area of activity.We will continue restructuring our operations in other business units, for example, in engineering and construction.

**PROFITS THAT MEASURE UP TO OUR EFFORTS**

The results achieved in 2000 clearly confirm the relevance of the orientations defined in our *Strategic Plan 2000-2004*, which was approved by the Québec government at the start of the year, and of the actions we have undertaken.

Consolidated net income rose 19% to reach $1,078 million, up $172 million over last year. This increase is mainly attributable to increased revenue from electricity sales on American markets and, in particular, purchase/resale operations on the short-term market. It also stems from the healthy state of our economy—currently experiencing the longest period of continuous growth in the last 50 years—which brought about an increase in sales in Québec, especially to commercial and industrial customers.

The rise in income enabled us to substantially improve our financial health, resulting in an increase in return on equity from 6.7% to 7.7%. We are pursuing our efforts to reach the 9.8% target set for 2004. It should be noted, as well, that the company paid an average weighted interest rate of 9% on its $38-billion debt.

To achieve this goal while maintaining low, stable rates for all our Québec customers, we must keep up strict management practices, improve our methods and take advantage of new business opportunities resulting from industry restructuring.

**RICH POTENTIAL TO BE DEVELOPED**

In Québec, a number of projects are under way to generate the electricity required so that we can meet our customers' needs at all times and on competitive terms, while continuing to meet the most stringent environmental standards.

The construction of Sainte-Marguerite-3 generating station, which will add up to 2.8 TWh to Hydro-Québec's annual output, is nearly complete. We finished refurbishing La Gabelle, La Tuque and Tracy generating stations, and other improvements are proceeding to maintain the reliability of our generating facilities.

In addition, the Québec government issued a decree authorizing the construction of the new Grand-Mère hydroelectric facility, which will replace the existing plant. This project has the backing of the local community.

**SOUGHT-AFTER EXPERTISE**

The restructuring of the world power market affords us an opportunity to sell our recognized expertise abroad, in particular in the design, construction and operation of power transmission lines and hydroelectric generating facilities.

Some bold projects were either started or completed in 2000. Hydro-Québec did the engineering and construction work for the Mantaro-Socabaya interconnection in Peru, carried out in partnership with Québec and Peruvian companies. The 600-km line linking the country's two largest transmission grids was built in exceptionally challenging terrain and called for unique expertise. In Australia, the 65-km link built under the supervision of TransÉnergie went into operation.

As well, Hydro-Québec acquired the assets of Transelec, in Chile, for $1.6 billion. This is the largest international deal ever completed by Hydro-Québec. It means the company is now well positioned on a fast-growing market.

These operations and investments give us the opportunity to make the most of our expertise on the international scene.

**COMMUNITY SUPPORT**

Following the agreements signed in 1999 with the Betsiamites and Essipit Montagnais band councils and with the regional county municipalities concerned, we continued working to obtain government approval for partial diversion of the Sault aux Cochons, Portneuf and Manouane rivers. In addition, the project to build a 517-MW generating station on the Toulnustouc River made progress, and construction should begin in the summer of 2001. Discussions are also going on with the local communities to allow other hydropower projects to start up, including Tabaret generating station.

Hydro-Québec is upholding its commitment to build new projects that meet its profitability objectives, are environmentally acceptable and are well received by local communities.

During the year, we set up a joint committee with the Crees in order to find common ground for settling a number of outstanding issues. We also reached an agreement whereby the Crees, with Hydro-Québec's support, will analyze the proposed Eastmain-1 hydro project, which includes diverting part of the Rupert River into the Eastmain River. In addition, we met with representatives of the communities of Chisasibi and Eastmain on numerous occasions to discuss projects for improving their drinking water supply. In close cooperation with the communities of Waskaganish and Mistissini, we are also cleaning up the sites used for the studies on the Nottaway-Broadback-Rupert project.

At a conference in Hong Kong in June, Hydro-Québec and Makivik Corporation, which represents the cultural, economic and political rights of the Inuit of Nunavik, were the joint recipients of the Indigenous Peoples Corporate Industry Award for their contribution to the advancement of relations between industry and Aboriginal peoples. This award also recognizes the spirit of partnership developed by the two organizations, along with their mutual interest in protecting the natural and social environments.

**EMPLOYEE MOTIVATION: THE KEY TO SUCCESS**

We owe our success mainly to our employees. With their expertise, their skill and their daily commitment, they all contribute, in their own fields, to making Hydro-Québec a company recognized for its ability to meet remarkable challenges. We thank them for their tireless efforts.

To rally all employees around the strategic plan, we invited them to small group meetings intended to foster a shared understanding of the company's issues and strategies.

In the longer term, our success depends on our ability to maintain our know-how with the help of a well-trained, highly motivated new generation of employees. Consequently, we have formulated a management training program to provide for successors to those who will retire in the coming decade.

We wish to express our gratitude to all the members of the Board of Directors and, in particular, to Simon Paré, who left the Board in 2000. We would also like to welcome Alain Forand, Pierre Grand'Maison and Claude Munger, who joined the Board during the year.

We want to pay special tribute to Joseph Bourbeau, who passed away in December 2000. Chairman of the Board from 1980 to 1985, Mr. Bourbeau played a major role in the development of Hydro-Québec for 37 years, through his energy, his visionary qualities and his sense of innovation.

As the year 2000 comes to a close, Hydro-Québec has its sights set on the future. Backed by our considerable achievements, we remain faithful to our core mission: to generate, transmit and distribute energy to meet the needs of all Quebecers. However, we must unite our efforts to remain a leader in an industry that is changing rapidly. To achieve our goals, we must consolidate our gains, continue building our expertise and carefully managing our resources, seize new business opportunities and even initiate change in an environment where new challenges constantly arise.

L.Jacques Ménard
Chairman of the Board

André Caillé
President and Chief Executive Officer

**greater**

awareness balance efficiency quality passion

> Customers can contact us through our HydroDirect call centre or our Web site.

## > greater attention to customer needs

As set out in the *Strategic Plan 2000-2004*, Hydro-Québec has made substantial efforts to improve service quality.

Rate stability was maintained, allowing a great many customers to achieve real savings against other energy sources with more volatile prices. The attainment of this objective was made possible largely by the company's increased profitability.

After a slight dip in the past two years, the overall rate of customer satisfaction rose steadily in 2000. Customers' appreciation of service quality showed an especially marked improvement in the residential and commercial sectors.

Hydro-Québec added new services to meet the specific needs of its business customers. It plans to continue improving its services on the basis of the changing needs and expectations of each customer category.

#### EXPANDED SERVICES

To serve customers better, the company opened new Hydro*Direct* call centre locations: two for residential customers (in Québec City and Saint-Hyacinthe), one for business customers in Montréal and three collection centres—in Montréal, Thetford Mines and Valleyfield. Call centre personnel are increasingly well versed in more efficient technologies that allow them to provide rapid, complete answers to customer requests. Hydro*Direct* showed improved performance in 2000, responding to 91% of calls received, 58% of them in under 20 seconds, thus bettering the year's target by 8%.

Hydro-Québec also offered new services in other customer categories. For example, it met with groups of business customers in various regions to better understand their expectations and play a more effective advisory role. Researchers at Hydro-Québec's electrochemical and electrotechnologies laboratory, LTEE, in cooperation with regional sales representatives and technicians, continued their efforts to offer these customers made-to-measure solutions, particularly in the areas of cooking, geothermal technology, lighting, infrared heating and load management.

For residential customers, we introduced a new sales and installation service for all-electric or dual-energy (electricity/oil) hot-air central heating systems.

The company also began installing modem-connected meters for business customers with more than one account. These meters provide them with access to new services that facilitate account management.

#### A FLEXIBLE COLLECTION APPROACH

The efforts made in 1999 to maintain a fair balance between stringency and flexibility in bill collection bore fruit. As a result of our collection activities, financial losses from outstanding accounts were reduced by $11.4 million in 2000.

The one-year pilot project for household budget planning, which concluded in 2000, was evaluated. Conducted jointly with two consumer associations, it was intended for low-income customers in Montréal and the Mauricie region. By the time the project ended, 68% of the 576 participants who had signed agreements with Hydro-Québec had fulfilled their commitments, and a good many of them had fully discharged their debts to the company. Hydro-Québec is now studying options for a permanent mechanism to help customers in difficulty pay off their debts.

> The Hydro*Direct* call centre offers rapid, efficient service.
> Winter is no problem for this open-air café, thanks to electric infrared heating.
> New: sales and installation of hot-air central heating systems.

In light of rising oil and gas prices, electricity remains one of the most attractive energy sources, both for its low, stable rates and for its limited environmental impact.

> Training abroad: shared knowledge.

**TARGETED R&D**

Research and development has been reoriented with a view to determining what projects are most likely to contribute to improving customer services and products.

The research projects selected concern such subjects as electrotechnologies used in the lumber industry and in food processing, as well as ways to reduce the environmental costs of treatment and disposal of industrial effluent and disposal of municipal sludge.

**PROJECTS OUTSIDE QUÉBEC**

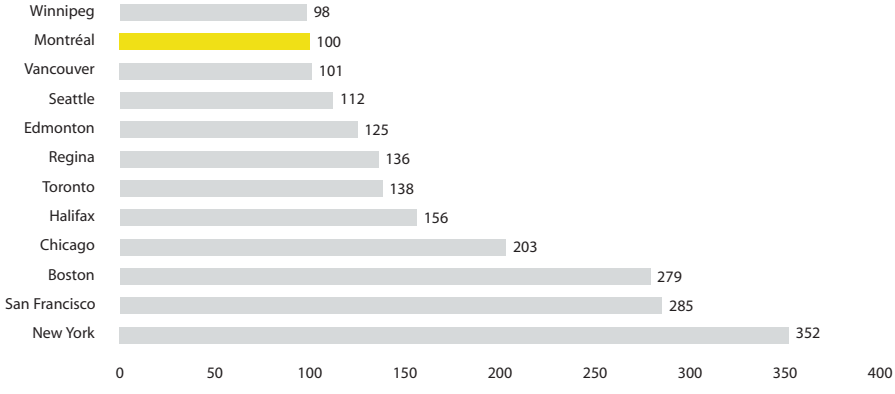
In Libya, Hydro-Québec was awarded a $12-million service contract for technical assistance in restructuring the General Electricity Company of Libya (GECOL) and setting up new information systems for administrative and financial management. This contract requires the participation of several Hydro-Québec business units, as well as the expertise of Famic Technologies 2000, a Québec information technology firm.

Hydro-Québec and Éconoler, a subsidiary of Hydro-Québec International and Dessau-Soprin, signed two major contracts worth a total of $2.6 million with Vietnam's Department of Industry. These projects got under way in fall 2000 and will continue through 2003. They cover load analysis, the planning and implementation of an energy conservation pilot project, and the establishment of efficiency standards for lighting and engines.

Several other international projects were carried out in 2000, including an ongoing technical-assistance contract for the installation of metering and pre-payment systems (Kuwait), training in customer approaches and satisfaction evaluation methods (Algeria and Morocco), and participation in producing master plans for facility construction (Ivory Coast and China).

In the realm of home automation, Hydro-Québec and Microtec signed an agreement in principle to create General Domotic, a business venture specializing in the design and marketing of home automation products. These products comply with CEBus, the recognized North American communications protocol for residential network management.

**Comparative Index of Electricity Prices—Residential Customers—May 1, 2000 (Montréal = 100)**




Monthly bill (taxes excluded) for a consumption of 1,000 kWh.
Source: Hydro-Québec, *Comparison of Electricity Prices in Major North American Cities at May 1, 2000.*

## > greater customer satisfaction

Through its business exploration activities targeting large corporations on the national and international scene, Hydro-Québec promotes Québec's industrial development.

Sales to large-power customers totaled 63.4 TWh in 2000, representing 41.5% of Québec consumption and generating revenue of $2.1 billion—$20 million more than forecast in the company's 2000 business plan. This increase stems from the strength of the Québec economy and the fact that companies established elsewhere in Canada or in the United States moved production here because of the competitive price of electricity in Québec.

Hydro-Québec continued to support its large-power customers' competitive edge by keeping its base rates at the same level as in 1998. In addition, real-time rates remained very attractive, in spite of the sharp increase in electricity prices on the American short-term market.

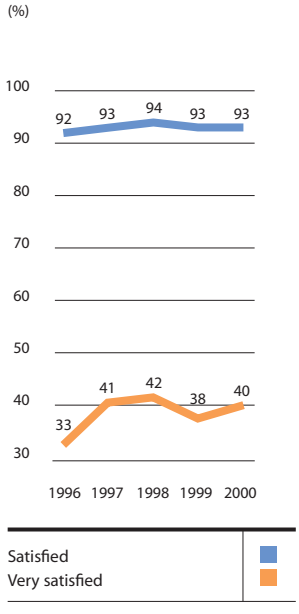
### A BUSINESS PARTNER

The service offered to large corporations is increasingly well suited to these customers' expectations. Their satisfaction with the power supply and service quality has improved steadily, from a rating of 7.6 out of 10 in 1996 to 8.5 out of 10 in 2000. These results are the product of several years of effort. Major customers can count on attentive service, sales representatives who are available every day of the week, direct communication with system planners and operators, and a permanent electronic communications link.

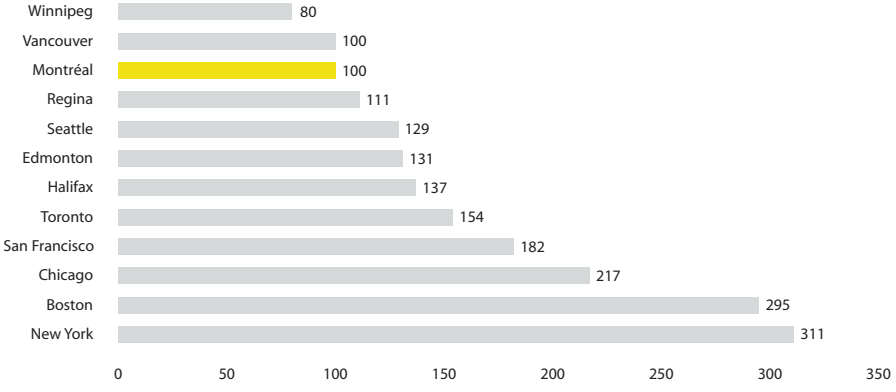
Hydro-Québec promoted its services mainly with large industrial companies in the pulp and paper, smelting and refining, iron and steel, mining, chemicals and manufacturing sectors, as well as commercial enterprises, institutions and municipal power systems. In addition, trade missions were conducted in Europe, the United States and Asia for projects in the chemical and metallurgical fields.

Some $3 million was invested in R&D activities intended to support specific projects likely to be of interest to large industry, such as the treatment of sludge produced by the pulp and paper industry, water treatment using ozone, electric drying of ore concentrates and electrical firing for electrode manufacture.

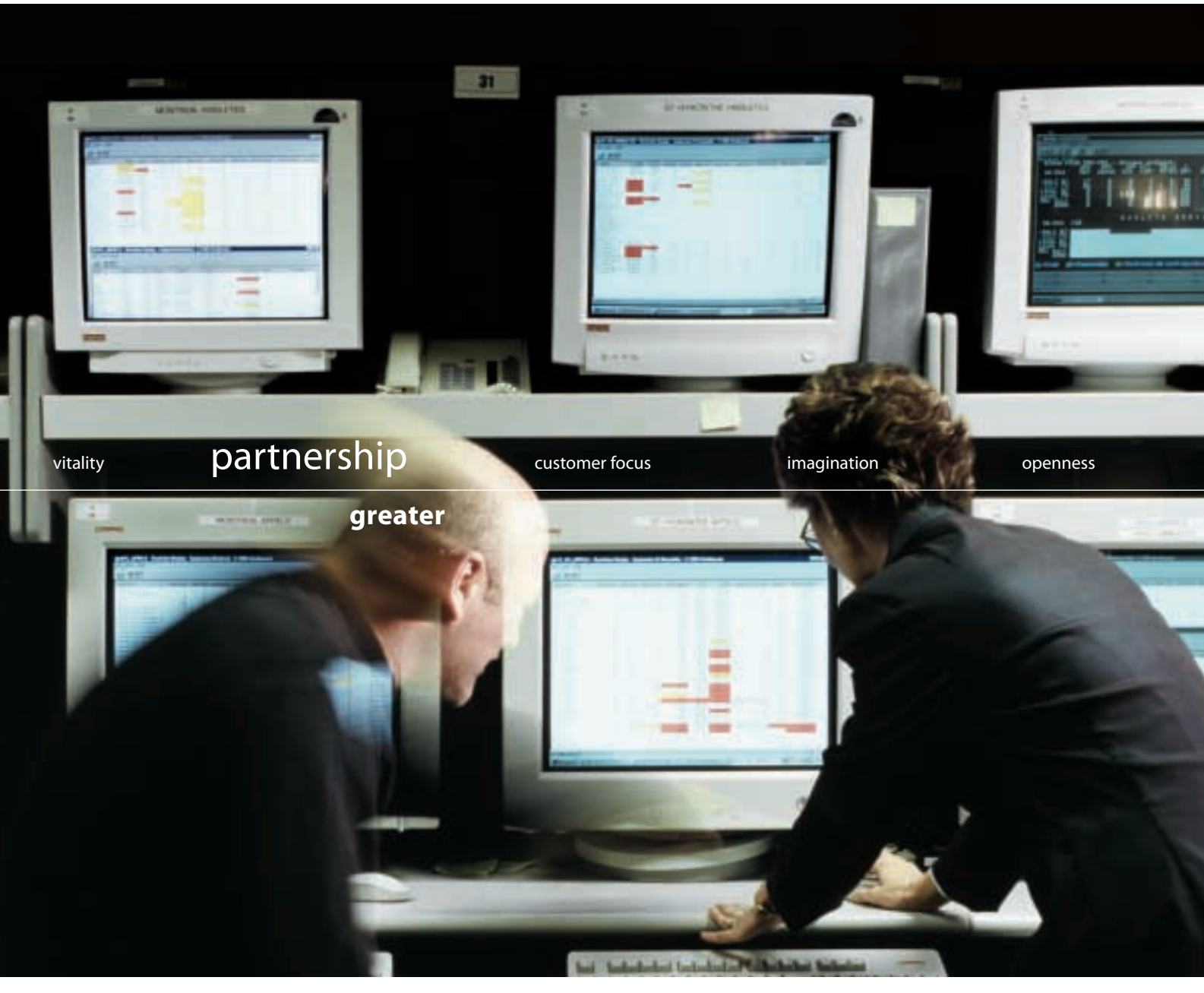
**Customer Satisfaction**




**Comparative Index of Electricity Prices—Industrial Customers—May 1, 2000 (Montréal = 100)**




Monthly bill (taxes excluded) for a demand of 5 MW, a consumption of 3,060 MWh and a load factor of 85%.
Source: Hydro-Québec, *Comparison of Electricity Prices in Major North American Cities at May 1, 2000.*




> The command centre for Hydro*Direct*: our employees are constantly improving their mastery of highly advanced technologies.

Hydro-Québec also worked to improve the quality of power delivered to these customers, in order to protect industrial equipment that is sensitive to voltage fluctuations.

**PROVIDING INFORMATION THROUGH ELECTRONIC CHANNELS**

Hydro-Québec has improved its services to large-power customers with the help of a special Web site. This site gives them access, in real time, to the information they consider most important: their billing, consumption pattern, changes in their contracts, and prices for transactions outside Québec. As well, each customer can communicate with its sales representative by e-mail.

## > greater reliability

In view of the climatic conditions in Québec and the vast area occupied by its customers, the average number of hours of service interruption is an important factor in measuring Hydro-Québec's success at achieving its first objective: ensure a reliable power supply for Quebecers.

Service continuity improved appreciably in 2000, with an average service interruption of 1.97 hours per customer, compared to 2.16 hours last year. A standardized index is used; in other words, it does not include exceptional events that exceed system design criteria. The good results in 2000 were due to less severe weather, as well as efficient management of system performance.

Customer satisfaction with the reliability of the power supply was rated at 7.7 out of 10, up 0.3 from 1999.

**AVERAGE NUMBER OF HOURS OF DISTRIBUTION SERVICE INTERRUPTION PER CUSTOMER***

| 1996 | 1997 | 1998 | 1999 | **2000** | 2004 target |
|---|---|---|---|---|---|
| 2.4 | 2.02 | 2.66 | 2.16 | **1.97** | 1.7 |

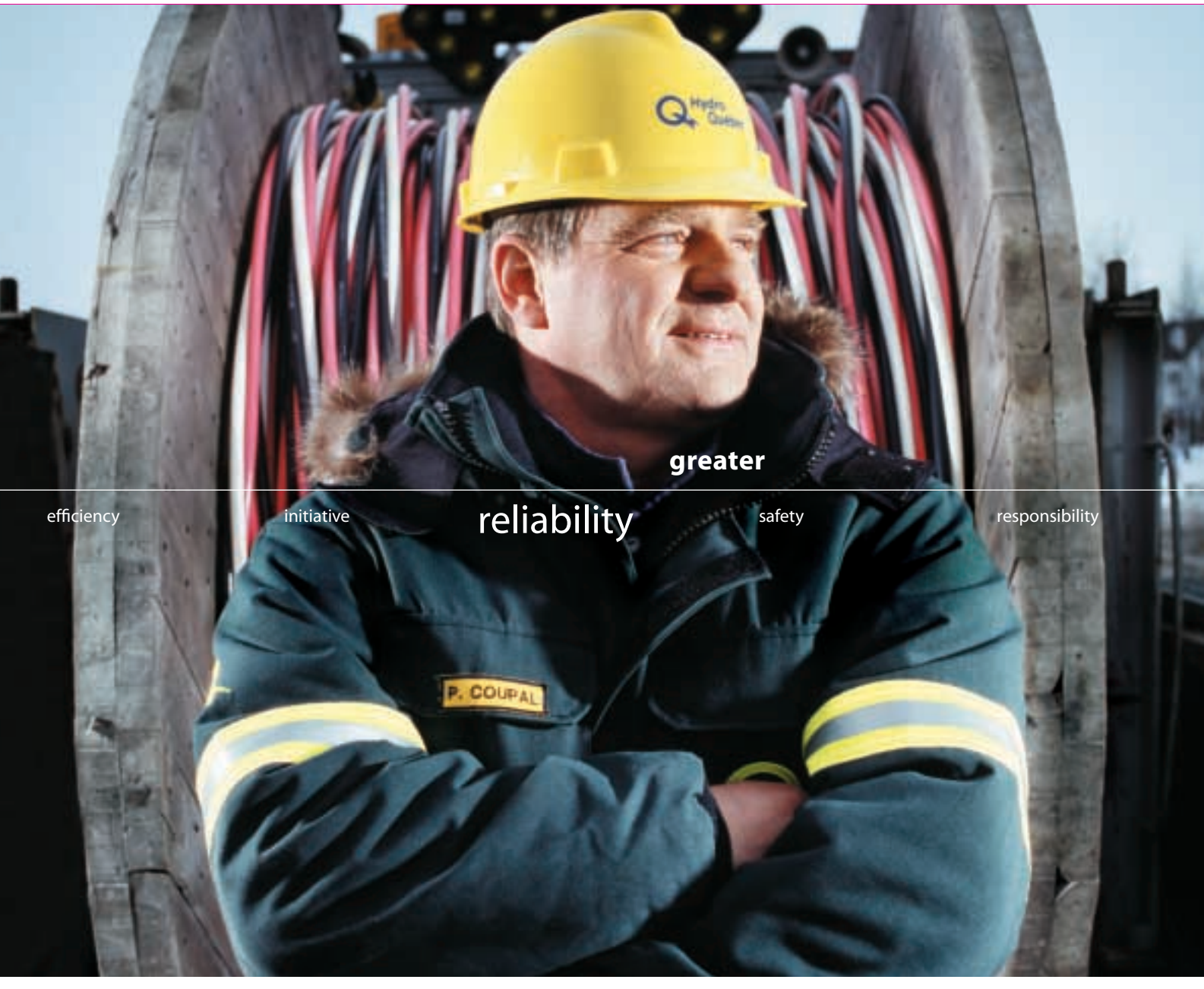
* Not including interruptions related to exceptional weather events.

**STEPPED-UP VEGETATION CONTROL**

Since vegetation is the cause of approximately 31% of service interruptions, Hydro-Québec stepped up its efforts to improve the quality of its pruning. The budget earmarked for this activity rose from $25 million to $40 million a year.

Hydro-Québec also systematically reviewed its dealings with pruning companies. By awarding longer-term contracts and requiring ISO 9002 certification, it helped enhance the quality of the work carried out by these companies and consolidate the pruning industry.

> Molten metal being poured at a smelter.
> Fewer service interruptions, thanks to stepped-up pruning activities.




> Undergrounding of the distribution system offers numerous advantages, including protection against bad weather and improvement of the urban landscape.

**OPTIMIZED DISTRIBUTION**

The four-year program for reinforcing the distribution system, instituted in 1999, will cost a total of $175 million. It is designed to ensure that lines considered top priorities are better able to withstand extreme weather conditions and that service is restored quickly in the event of an outage. A further goal of the program is to reinforce all distribution lines in these priority areas, in order to prevent poles from cascading.

**SYSTEM UNDERGROUNDING**

In accordance with its strategic plan, Hydro-Québec launched a program for undergrounding the distribution system. In addition to reducing exposure to the vagaries of weather, this program will contribute to better integrating the system into the urban environment.

The undergrounding program comprises three parts. The first involves extending the underground grid into new residential neighborhoods. The second is aimed at supporting municipalities that wish to bury their overhead lines. Finally, the third part is devoted to undergrounding the existing system in heritage sites.

**MAJOR URBAN CENTRES: A PRIORITY**

Because of their demographic and economic importance, major downtown areas were studied with a view to improving reliability and service continuity. As well, the strategic plan indicates Hydro-Québec's intention of reducing the average interruption time on this portion of the distribution system to a maximum of one hour by 2004.

Downtown Montréal received particular attention, and a $108-million, three-year program for rehabilitating and automating the underground portion of the system was approved.

**IN HARMONY WITH THE ENVIRONMENT**

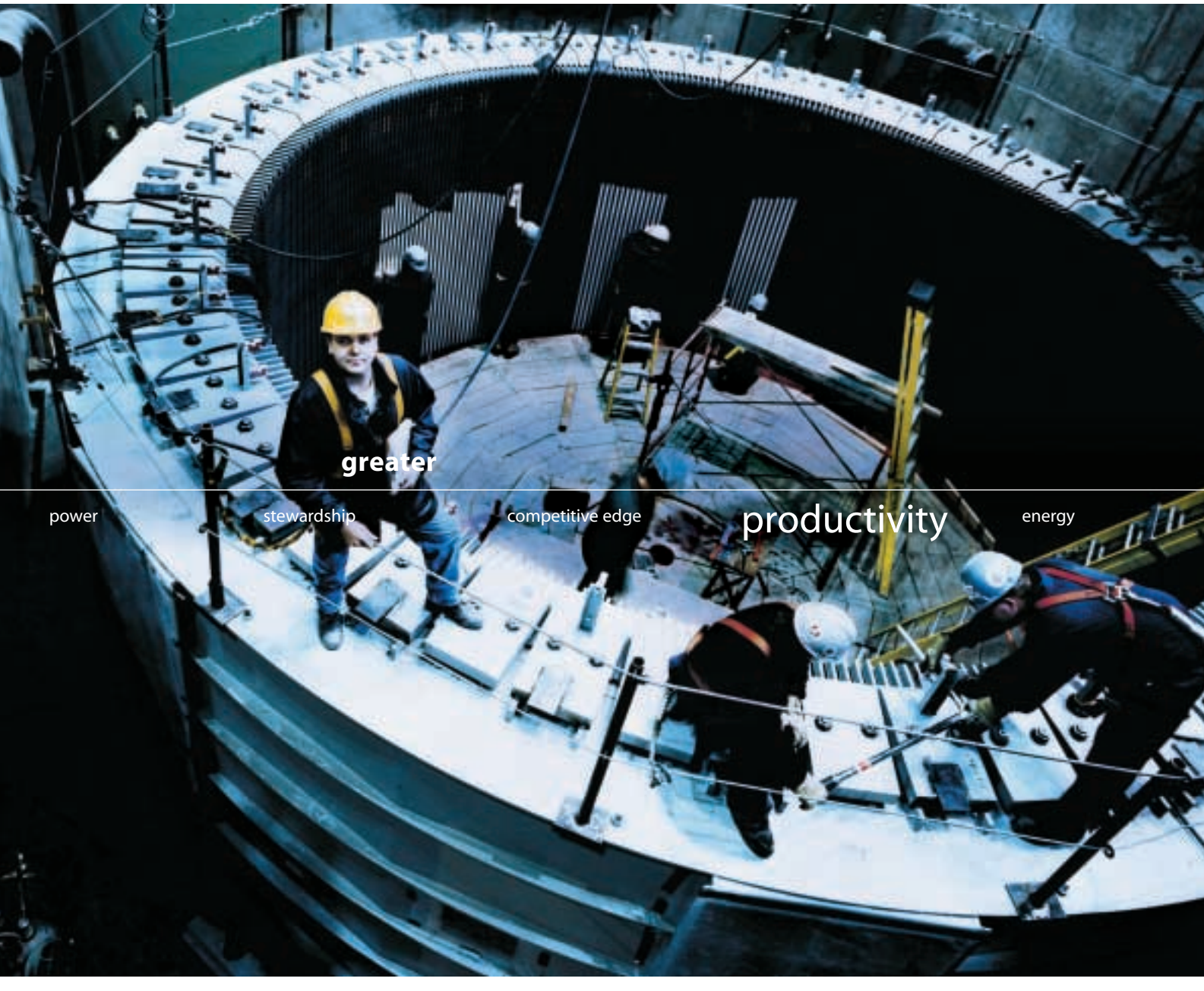
Hydro-Québec sees to it that its projects are carried out with proper respect for the environment. Following a three-year process, the Distribution unit obtained its certificate of ISO 14001 registration. It is the company's first administrative unit to obtain this certification for all of its activities. This recognition is all the more important since the unit is active throughout the province and its employees have frequent, direct contact with customers.

**EMPLOYEE COMMITMENT**

To reach our performance targets, the commitment of our personnel is vital. For more than two years, the 3,700 or so Distribution employees have taken part in a plan which basically provides for structured meetings between employees and managers. The goal is to make managers more aware of the need for good communications with their personnel.

The distribution control centres are responsible for fully integrating all applications related to real-time system operation.

> A wire-free landscape in a new residential neighborhood.




> Sainte-Marguerite-3 generating station,
with an installed capacity of 882 MW,
will come on stream in 2001.

## > greater efficiency in generation

The power market underwent major changes in the past year, both in Québec and throughout North America. These developments were especially rapid in the electric generation sector. In Québec, the *Act to amend the Act respecting the Régie de l'énergie* deregulated power production, although Hydro-Québec retains sole responsibility for developing sites with a capacity of over 50 MW.

### A RELIABLE SUPPLY THAT BENEFITS QUÉBEC

With the output of its generating stations and through purchase contracts, Hydro-Québec ensures a reliable power supply, on favorable terms, for all its Québec customers. In 2000, it continued to operate its generating facilities with optimum efficiency. The company generated or purchased a little over 207 TWh during the year. Its own generating facilities in Québec and Churchill Falls power plant produced 185 TWh of this total, 97% of it by water power.

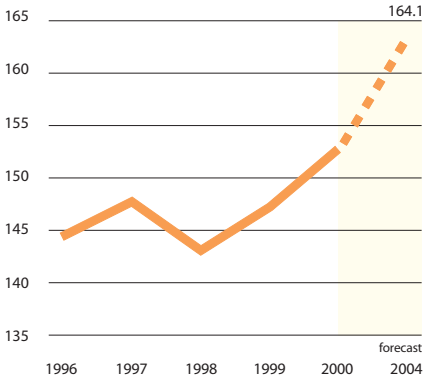
A number of projects continued in 2000 with a view to maintaining the reliability of our generating facilities. Rehabilitation of La Gabelle, La Tuque and Tracy generating stations was completed. Other improvements proceeded at Bersimis-1, Manic-2, Shawinigan-2, Shawinigan-3 and Beauharnois, while upgrading projects at Outardes-3 and Rapides-des-Quinze will be studied in the coming years. In the medium term, the company is also planning a major overhaul of Gentilly-2 nuclear power plant. The Canadian Nuclear Safety Commission gave unrestricted approval for the renewal of the plant's operating permit.

Construction of Sainte-Marguerite-3 is nearly finished. This underground powerhouse, which contains the two most powerful generating units in Québec, is scheduled for commissioning in 2001.

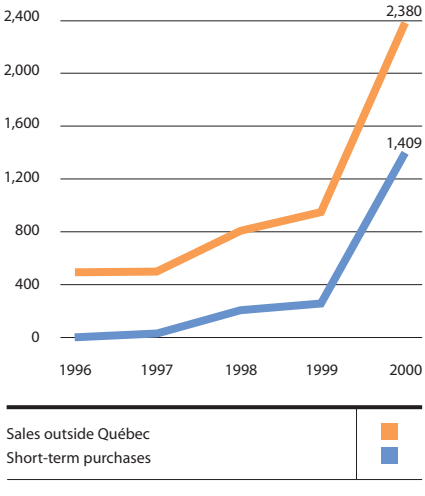
Hydro-Québec maintains a sufficient energy reserve at all times to offset a potential runoff deficit of 64 TWh over two consecutive years, and a capacity reserve representing 10% to 12% of demand under its contracts both inside and outside Québec.

> Rapides-des-Quinze generating station in the Abitibi-Témiscamingue region, in service since 1923.

**Québec—Electricity Sales to the Distributor**
(TWh)




**Sales Outside Québec and Short-Term Purchases***
($M)




* Short-term electricity purchases in the last few months of 2000 include a $77-million charge for structured energy transactions concluded in 1998 and 1999.

In 2000, 97% of the power generated came from water.

> Work has begun on the new Grand-Mère generating station.

With strong backing from the local community, Hydro-Québec also started preliminary work for the construction of a new, $450-million generating facility at Grand-Mère. This 220-MW power station will go into operation in 2004 and will optimize all existing production along the Saint-Maurice River. At the peak of construction, some 430 workers will be on the site.

We continued working to obtain approval for a partial diversion of the Portneuf, Manouane and Sault aux Cochons rivers, which will increase power production on the Betsiamites River. The project to build a large, 517-MW hydroelectric generating station on the Toulnustouc River also advanced by several stages. The company expects to break ground on this facility in 2001. It is also planning to build a powerhouse at the foot of Mercier dam, downstream from Baskatong reservoir.

Finally, several other projects are currently in the planning or discussion stage, including the construction of Eastmain-1 generating station (1,280 MW) and partial diversion of the Rupert River, in the James Bay region, and the construction of Tabaret generating station in the Témiscamingue region and Romaine-1 in the Mingan Islands. Hydro-Québec hopes to carry out these profitable projects in partnership with the local communities.

#### CLEAN ENERGY

Hydro-Québec continued integrating concern for the environment into all of its generating activities, from powerhouse operation to construction project studies. It also took further action to increase awareness of the environmental benefits of hydropower.

With implementation of the environmental management system now complete, the Generation Group should receive ISO 14001 certification during 2001. Continuous-improvement objectives for environmental performance are now an integral part of the business plan, notably with respect to management of emissions, effluents and hazardous materials, as well as water management.

#### PROFITABLE RESEARCH PROJECTS

In accordance with the *Strategic Plan 2000-2004*, Hydro-Québec finished outlining the research avenues and projects most likely to increase its profitability while fitting in with its vision and strategic objectives. The goals of the selected research projects are mainly to maximize the economic potential of facilities and reservoirs, reduce the costs and time required for work on the company's existing and future installations, ensure the continued reliability and security of generating facilities, and remain on the lookout for new technologies, particularly in the area of distributed generation.

**A HIGHER PROFILE INTERNATIONALLY**

Hydro-Québec also kept up its efforts to expand its international presence in power generation. Its activities in a number of countries included participation in the financing and management of infrastructure projects, mainly in China and Central America.

In Panama, Hydro-Québec continued operating the country's largest hydroelectric facility, Fortuna, in which it has a 16.66% stake. During the year, the company successfully optimized production at this plant in a highly competitive market.

In China, Hydro-Québec holds a 20% interest in Meiya Power Company. Meiya currently has seven generating stations in operation or under construction, making it a major independent power producer in that country.

Also in China, Hydro-Québec has a stake in the 20-MW Qingshan power plant on the Lishui River in northern Hunan province. This plant is slated for commissioning in the first quarter of 2001.

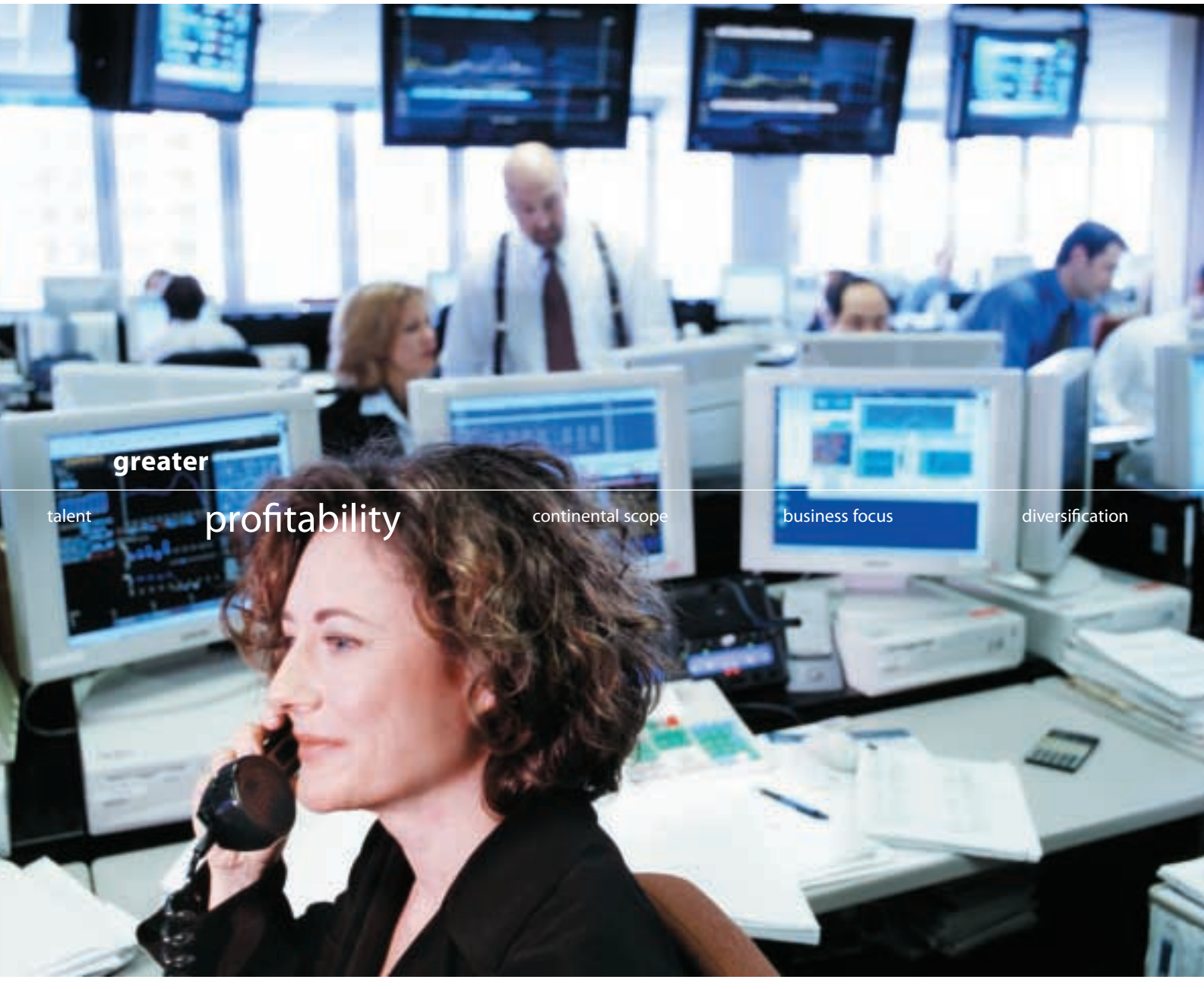
In the area of professional services, projects located mainly in Panama, Venezuela, Iran, Cameroon and China generated close to $10.6 million in revenue.

In Venezuela, the company is providing technical assistance to Electrificación del Caroní (Edelca) for the overhaul or replacement of all 10 generating units, with a capacity of 700 MW each, at Guri II power plant, currently one of the most powerful hydroelectric generating stations in the world. Similar work has begun at Guri I and Macagua.

Lastly, Atomic Energy of Canada Limited put the company in charge of a training program for Chinese specialists; courses in the maintenance and operation of a CANDU-type nuclear power plant were given at Gentilly-2.

Hydro-Québec aims for solid profitability in its international projects, as stipulated in the *Strategic Plan 2000-2004*.

> Fortuna generating station in Panama: even more productive.
> China: Qingshan generating station, now under construction.




> In 2000, Hydro-Québec set up an energy trading floor to conduct transactions on the wholesale power market.

## > greater presence on North American markets

With the competitive edge and flexibility provided by its reservoirs, Hydro-Québec ranks as a major player on power markets in Eastern North America.

The restructuring of the North American power industry has created an environment favorable to energy exchanges and fostered the emergence of new markets and competitors. This has meant unbundling electric generation, transmission and distribution activities. It is closely linked to the growth in e-commerce made possible by the new information technologies and the Internet.

**IN QUÉBEC**

The Québec government adopted the *Act to amend the Act respecting the Régie de l'énergie* this year. The new law has had a huge impact on Hydro-Québec. It removes electricity generation from the jurisdiction of the Régie de l'énergie (Energy Board) and establishes a heritage electricity pool for Québec consumers. At Hydro-Québec, the Generator will consequently supply the Distributor with a maximum of 165 TWh/year for Québec customers, at a set price of 2.79¢/kWh. This pool will form the basic long-term nucleus of Québec's power supply.

The Act also introduces competition into the Québec wholesale market for all needs in excess of the heritage pool. To meet these needs, the Distributor will solicit tenders. It will have to submit a procedure for tendering and awarding contracts as well as a code of ethics to the Régie de l'énergie for approval.

**OUTSIDE QUÉBEC**

The United States has opened up its wholesale power market to promote competition in electric generation and bulk sales. This has brought about the deregulation of the generating industry, and led to the establishment of Regional Transmission Organizations. The RTOs ensure balance in regional wholesale markets by organizing power transactions for a large group of participants on spot markets (on an hourly or daily basis). The futures markets, on the other hand, offer the option of reducing risks related to price fluctuations through two-way deals made mainly by power brokers.

Today, Hydro-Québec is active on all these markets, mainly through its subsidiary H.Q. Energy Services (U.S.), which has had a power marketer licence since 1997 allowing it to operate under U.S. market conditions. H.Q. Energy Services (U.S.) buys and sells electricity in the United States. It also sells power generated by Hydro-Québec at the Québec border, and buys U.S.-generated power at certain times of day for the Québec market, particularly during off-peak hours at night.

To play a greater role on these markets, Hydro-Québec set up an energy trading floor in Montréal in 2000.

The company posted strong growth in its volume of power purchases and sales on all markets outside Québec in the past year even though, in net terms, it generated and delivered to the border essentially the same quantities as last year. Transactions outside Québec generated revenue of more than $2,380 million, or nearly 21% of Hydro-Québec's total sales. The company adopted stringent risk management measures for all these operations.

> Manicouagan reservoir, covering nearly 2,000 km$^2$.

> Building the Mantaro-Socabaya interconnection in Peru made use of Hydro-Québec's expertise in transmission system planning, engineering, construction and operation as well as in alternating-current interconnection and series compensation technologies.

## > greater system strength

Hydro-Québec's interconnections with neighboring systems increase the reliability of the power supply in Québec while also allowing TransÉnergie customers to conduct transactions with their own partners.

TransÉnergie and Engineering, Procurement and Construction carried out major improvements to consolidate Hydro-Québec's transmission system in order to increase its ability to withstand severe weather events and improve service continuity.

The Montréal loop was completed. The project called for the construction of a 315-kV line between Duvernay and Anjou substations, another 315-kV line between Aqueduc and Viger substations and an underground line between Atwater and Hadley substations. In addition, Hydro-Québec can bring back part of Beauharnois's generating output, if needed.

Work to reinforce Mauricie, Deschambault, Jacques-Cartier, Neufchâtel, Laurentides and Leneuf substations also concluded, and the 315-kV Portneuf loop was finished, increasing transfer capacity between Québec City and the Mauricie region by 500 MW.

The installation of a new transformer at Laurentides substation and the reconstruction of the 230-kV lines supplying Québec and La Suète substations helped bolster the security of the power supply to the Greater Québec City area in the event of extreme weather conditions.

In the Gaspé peninsula, the company built a 161-kV line between Percé and Gaspé substations. This new line forms a loop securing the power supply to this region in the event of a lengthy interruption on the only existing line between Gaspé and Micmac substations.

**AVERAGE NUMBER OF HOURS OF TRANSMISSION SERVICE INTERRUPTION PER CUSTOMER***

| 1996 | 1997 | 1998 | 1999 | **2000** | 2004 target |
|---|---|---|---|---|---|
| 0.44 | 0.61 | 0.48 | 0.65 | **0.36**** | 0.65 |

* Not including interruptions related to exceptional weather events.
** Mainly due to less severe weather conditions during the year.

**INNOVATION, A PREREQUISITE FOR CONTINUING PROGRESS**

TransÉnergie reoriented its research and development program to increase the value added for Hydro-Québec and maximize spinoffs. The research projects focus on the division's strategic objectives, and an integrated management process ranging from research to the application of innovations was formulated.

A group made up of representatives of TransÉnergie, Hydro-Québec's research institute IREQ, the Engineering, Procurement and Construction Group and outside firms determined the most profitable research avenues and projects. R&D projects will be aimed mainly at reducing the cost of new facilities, developing alternative solutions for construction projects designed to increase transfer capacity, reducing the impact of severe weather events on the transmission system, and improving system simulation tools.

> The downtown Montréal loop was completed in 2000.

TransÉnergie continued its research projects on various thermal and mechanical de-icing methods to protect the transmission system.

In commercialization of technology, TransÉnergie Technologies signed a contract with the Electric Power Research Institute (EPRI-China) to develop an improved hybrid power system simulator. This is the fifth contract won in China by TransÉnergie Technologies and its subsidiary Teqsim International since they began marketing Hydro-Québec's power system simulators. Another contract was signed with the Electric Power Development Company of Japan for delivery of a similar tool.

The $155-million project to modernize the System Control Centre proceeded. The generation rejection and remote load-shedding system, developed by a team of TransÉnergie and IREQ specialists and commissioned in the fall, is on the leading edge of technology. This automatic system protects the transmission grid from severe disturbances.

Lévis substation was also updated with the installation of the ALCID system, which manages automatic local controls and remote control based on distributed intelligence.

#### NEW REVENUE SOURCES

The opening of the U.S. market and the entry of new power wholesalers have created new business opportunities. The use of the transmission system by other electric utilities generated additional transmission revenue. Of the 197,861 GWh carried over the system during the year, 12% was bound for markets outside Québec.

The number of customers allowed to transfer their power via the Hydro-Québec system rose from 10 to 16 during the year.

#### THE ENVIRONMENT: AN ASSET TO BE PRESERVED

In view of the importance of the facilities it manages, TransÉnergie continued implementing its environmental management system, designed to reduce the impact of its installations throughout the province. Most work methods were reviewed in light of environmental requirements.

TransÉnergie is aiming for ISO 14001 registration in 2002. This recognition will help confirm its reputation as a reliable transmission provider and a careful manager concerned with preserving the quality of the environment.

#### TARGETED INTERNATIONAL ACTION

The 600-km Mantaro-Socabaya interconnection in Peru was commissioned by the deadline agreed upon with the Peruvian government, in spite of the sizable challenges of building such a transmission line in the Andes. Hydro-Québec was able to carry out this project thanks to its advanced technologies, its expertise in planning, engineering, project management and the operation of extensive transmission systems, and its innovative capability.

> The ALCID system's four consoles will replace the mimic boards covering two walls in the background.

Construction also concluded on a 65-km interconnector in Australia. A new technology developed by equipment manufacturer ABB was used to link two transmission grids. The project was carried out in partnership with a local distributor.

TransÉnergie U.S., Hydro-Québec's American transmission subsidiary, signed an agreement with the Long Island Power Authority (LIPA) to design, build and operate an interconnector that will provide a competitive source of supply for Long Island energy needs, while promoting the economic growth of the region and the protection of the environment. This direct-current interconnector will improve the reliability of the power supply to New York and Connecticut.

TransÉnergie U.S. won Federal Energy Regulatory Commission (FERC) authorization to base its transmission rates on the energy price differential between the interconnected markets rather than on a fixed rate. It has sold the transmission rights on this interconnector to LIPA for 20 years.

Finally, Hydro-Québec acquired Transelec, in Chile. This company operates the country's main transmission system and delivers energy to local distributors that serve 93% of Chile's electricity customers. The system includes 348 substations and nearly 7,300 km of transmission lines with voltage levels ranging from 66 kV to 500 kV.

**MAINTAINING LEADING-EDGE EXPERTISE**

The success enjoyed by TransÉnergie is largely due to the skill of its employees. Over the years, they have taken part in a wide variety of major projects making good use of their knowledge and innovative abilities.

After conducting an analysis of its work force, TransÉnergie reviewed its succession plan to ensure the continuity of its expertise. This exercise will continue in 2001.

Employee motivation was also fostered. To recognize the contribution of its specialists in designing the products and services on which the division's reputation is based, TransÉnergie organized the TransÉnergie 2000 exhibition at Montréal's convention centre. This event showcased the know-how of TransÉnergie's employees and partners, for other Hydro-Québec employees.

> New acquisition: Chile's largest transmission provider.
> TransÉnergie 2000: showcasing our employees' expertise.

**greater**

ingenuity drive mastery breakthroughs productivity

In expanding its business internationally, Hydro-Québec is backed by over half a century of know-how in the design, construction and management of generation and transmission projects.

## > engineering, procurement and construction

Engineering, Procurement and Construction offers a wide range of integrated services along with strategic energy-related advice. Over the past year, the Group carried out engineering and construction projects worth over $1 billion. The work included all rehabilitation projects and new plant for the Generator and the Transmission Provider.

In the field of generation, the Group almost completed construction of Sainte-Marguerite-3 generating station and received a turnkey assignment to build the new Grand-Mère power station. It prepared many draft designs, including studies for the construction of Toulnustouc and the partial diversion of the Portneuf and Sault aux Cochons rivers.

In addition, following the exceptional flooding in the Saguenay region in 1996, the Group was asked by the Québec government to carry out studies and produce the draft design for a hydropower project in the region, as part of the Kénogami development.

In transmission, the Group completed the Montréal and Québec City loops as well as construction of a 71-km line between Sainte-Marguerite-3 generating station and Arnaud substation. It also commissioned a 4.6-km underwater line between Les Éboulements and Île aux Coudres; this is a particularly challenging environment because of the tides and strong currents.

On the procurement side, the Group acquired goods and services totaling $1,570 million. Hydro-Québec's sizable purchasing power yielded savings of over 20% on certain products.

#### SOCIÉTÉ D'ÉNERGIE DE LA BAIE JAMES

The Société d'énergie de la Baie James (SEBJ)—a subsidiary that reports to Engineering, Procurement and Construction—acted as project manager and carried out half the construction work on the 220-kV Mantaro-Socabaya interconnection in Peru, commissioned in October.

In Brazil, SEBJ signed a partnership agreement with a local company and a Canadian supplier for the live-line installation of optical-fibre ground wires using Hydro-Québec's cradle-block method.

> Building a line in the Andes is quite a challenge.
> Using Hydro-Québec's cradle-block system in Brazil.
> Tubular steel pole, chosen for its aesthetic qualities.

**BREAKDOWN OF SALES BY CUSTOMER ($M)**

| Customer | Engineering and Construction | Procurement and Services |
|---|---|---|
| Generator | 567 | 60.9 |
| Transmission Provider | 403 | 70.2 |
| Distributor | N/A | 113.5 |
| Other customers | 55 | 103.3 |
| **Total** | **1,025** | **347.9** |

The subsidiary broadened its scope in the Middle East and submitted a number of proposals for transmission services in countries such as Libya, Algeria and Saudi Arabia. It also began upgrading a transmission system control centre for the Bangladesh Power Development Board.

In Québec, SEBJ conducted technical and feasibility studies on the proposed Eastmain-1 hydro development in the James Bay region. The subsidiary also secured a contract to replace the 120-kV line between Les Cèdres generating station and the Ontario grid with a 230-kV line to be commissioned in 2002.

To achieve its objectives, Hydro-Québec must be able to count on employees who keep up with the very latest developments in their field.

## > human resources

Renewing our work force and training the next generation of employees in the necessary skills are vital to Hydro-Québec, which must ensure the continuity of the expertise acquired over the years by its employees. A number of initiatives were taken to achieve this goal.

Hydro-Québec adopted an integrated skill management approach to develop the know-how of its personnel and ensure that it is passed on.

A detailed analysis was done of work force needs for the next 10 years. A succession program designed to fill management positions is being formulated in consultation with the business units, and a management training program was introduced.

Hydro-Québec's training institute held 270 sessions involving more than 3,000 executives and professionals. The institute's courses are now recognized and accredited, following an agreement in principle with the business faculty of the Université du Québec à Montréal to validate course content and instructors' qualifications. Each business unit is responsible for its personnel's technical training.

Under a program launched in 1999, Hydro-Québec hired 56 new graduates this year, mainly in engineering and finance. This program is developing less quickly than expected, however, due to the shortage of graduates in energy-related professions and technologies, among other factors.

> A discussion of business issues.
> Telecommunications: a tool in daily use.

**WORKING CONDITIONS**

During the year, Hydro-Québec made substantial progress in applying the *Pay Equity Act*. Since each union asked for its own pay equity program, as the Act allows, several joint committees were formed. All the committees determined which job classes were predominantly female. Some also laid out the method and tools to be used and established a value determination procedure. The other steps specified in the Act will proceed in 2001.

The incentive pay plan launched in 1999 was maintained. This year it was applied to all employees on the basis of the attainment of the company's objectives.

In labor relations, Hydro-Québec signed a collective agreement at the end of the year with the union representing the researchers at IREQ. The agreement runs to the end of 2003.

As regards occupational health and safety, 4.39 work accidents were recorded for every 200,000 hours worked, falling short of the year's overall corporate target of 3.89. Although the company's results are comparable to those generally found in the industry, this situation is still cause for concern and shows that our safety efforts will have to be stepped up.

**MOTIVATION CAMPAIGN**

Hydro-Québec implemented several programs over the year to encourage employees to support its initiatives and work to achieve its objectives.

To remain in tune with its employees, Hydro-Québec conducted a survey to find out their satisfaction level in terms of certain job- and company-related expectations. The poll results indicate that employees' expectations are being better met. The overall employee motivation index was 6.33 out of 10, up 0.19 from 1999.

In addition, as part of a motivation campaign, the company held meetings of small groups of employees from different units. The goal of the meetings was for all employees to become more fully acquainted with the company's business environment and financial reality, to gain a better understanding of the importance of reaching specific financial targets and to commit themselves to the company's main objectives. Over the year, nearly half our personnel took part in this activity, which will continue in 2001.

For the past 10 years, Hydro-Québec has exported more hydropower to its U.S. and Canadian neighbors than the amount of thermally generated power it has bought from them, a practice that contributes to reducing acid rain and smog.

Fondation Hydro-Québec pour l'environnement

## > environment

Hydro-Québec integrates environmental protection and corporate growth. In view of the diversity of environment-related issues, each business unit has adopted its own environmental commitments.

In 1997, the company decided to implement the ISO 14001 international standard in all units whose activities are likely to generate significant environmental impacts. Implementation is to be completed in 2002.

In connection with its projects and facility operations, this year the company signed over 20 agreements with the local communities concerned. Many of these agreements will lead to reduced environmental impacts or improved mitigative or compensation measures.

As well, to foster long-term environmental protection and enhancement, the company established a special foundation for the environment.

### INTERNATIONAL DIALOGUE

Like other major organizations, Hydro-Québec took part in a number of international committees that debated issues related to climate change, further to the commitments given by the industrialized countries at the Kyoto Summit in 1997.

Hydro-Québec plays an active role in the International Energy Agency, which is associated with the Organisation for Economic Co-operation and Development (OECD). This year, the company was in charge of preparing a summary of OECD studies on hydropower and the environment over the past five years.

Increased participation in the activities of the International Hydropower Association (IHA) Environment Committee allowed Hydro-Québec to highlight the advantages of hydropower and share its environmental expertise with the representatives of the IHA's 60 or so member countries.

Hydro-Québec's relations with Aboriginal communities, as well as its partnership approaches, elicited considerable interest from the commissioners of the World Commission on Dams (WCD). Hydro-Québec also defended the positions of the hydropower industry as a member of the WCD Forum and as a financial contributor to the WCD, along with manufacturer ABB.

> Hydro-Québec: a leader in environmental management for close to 30 years.

Technological innovation plays a strategic role in ensuring the long-term growth of the company's business units.

## > technological innovation and venture capital

**TECHNOLOGICAL INNOVATION**

As part of a new integrated innovation management process, designed to maximize the value added through technological innovation, Hydro-Québec has built a portfolio of 65 projects incorporating the proposals of its researchers and engineers and budgeted at $63 million for 2001.

Projects directly affecting the company's core business include improvements to electrical insulation under icing conditions, automated fault location on overhead and underground lines, and the development of diagnostic tools for determining facilities' remaining useful life. In addition, TransÉnergie assigned a five-year, $8-million project to IREQ for the development of a real-time, digital transmission system simulator. This advanced technology will allow network topology to be represented in graphic form and to be tested under various difficult conditions.

Two examples of the use of new products created through innovation are a portable device for acoustic fault detection in tap changers on large transformers and the VAT-2000 no-voltage detector used in 14 facilities on the Hydro-Québec distribution system. Discussions on marketing these new technologies are under way with strategic partners.

Some other innovations are on the verge of being marketed with partners: the integrated ventilation and heating system, the plasma-assisted wet oxidation process, metal hydrides for safe storage of hydrogen molecules, and the ACEP battery for the telecommunications market.

Hydro-Québec sponsored the 17th edition of the International Electric Vehicle Symposium in Montréal, which brought together 1,600 experts from around the world. At this event, Hydro-Québec CapiTech's subsidiary AVESTOR, together with its partners, presented the lithium-metal-polymer battery developed by Hydro-Québec and used in Ford's TH!NK city electric vehicle.

> Lithium-metal-polymer battery for telecommunications: a technology of the future

> The VAT-2000, a reliable and high-performance tool

> The Capstone microturbine for transportation, air conditioning, food processing and greenhouse operation.
> TH!NK city, the little car that's environmentally friendly.

**VENTURE CAPITAL**

Hydro-Québec CapiTech, Hydro-Québec's venture capital subsidiary in the energy technology field, held course toward its target of a 20% financial return over the life of its investment fund, in line with Hydro-Québec's *Strategic Plan 2000-2004*. This target applies to the first fund, totaling $108 million, set up in 1998. Two companies in the Hydro-Québec CapiTech portfolio—Capstone Turbine Corporation and H Power Corporation—went public, a development that will make a real contribution to achieving this goal, as together they represent nearly 25% of direct investments.

Since its inception, Hydro-Québec CapiTech has invested close to $80 million directly in companies with energy-related products and services. Through the partnerships formed in North American venture capital circles, it has been able to target profitable investment opportunities in companies offering technologies of strategic interest to Hydro-Québec.

Given the anticipated return on the first Hydro-Québec CapiTech fund and the favorable market conditions, Hydro-Québec's Board of Directors authorized the creation of a second investment fund with a value of $192 million.

Another highlight of the year was the decision by Hydro-Québec CapiTech to establish Hydro-Québec CapiTech Innovation, a $20-million fund incorporating the activities of Énergie Capital Innovation. This new entity invests in technological business ventures that will help create new value for the products of Hydro-Québec's research.

**TARGETED INVESTMENTS**

Hydro-Québec CapiTech took advantage of the thriving venture capital market in the energy sector to consolidate and expand its portfolio of holdings in companies offering products and services likely to contribute to the growth of Hydro-Québec's business units.

Hydro-Québec CapiTech made nine new direct investments and eight reinvestments during the year, most of them in companies identified through its partner network. Six Québec companies benefited from these investments or reinvestments: ECI Composites (Saint-Jérôme), AlterSys (Longueuil), HydroSoft Énergie (Montréal), Galvacor (Québec City), Domosys Corporation (Québec City) and Comaintel (Grand-Mère). In addition, in keeping with its investment policy, it wound up its interest in VibroSystM, which had become sufficiently autonomous to take over its own capitalization. It also contributed to the creation of Acres Productive Technologies International, with which it integrated the operations of HydroSoft Énergie.

Hydro-Québec CapiTech continued to monitor the energy market for business opportunities with a view to keeping the business units informed about the latest technological developments and contributing to the innovation process. During the year, it conducted studies on e-commerce and energy, energy management, the use of carrier current for voice and data transmission, and superconductivity. These studies enable it to pinpoint emerging enterprises that design new technologies in these fields, and to target potential investments.

Information Technologies works to achieve the objectives of the company's strategic plan by helping its customers tap the full potential of information technologies.

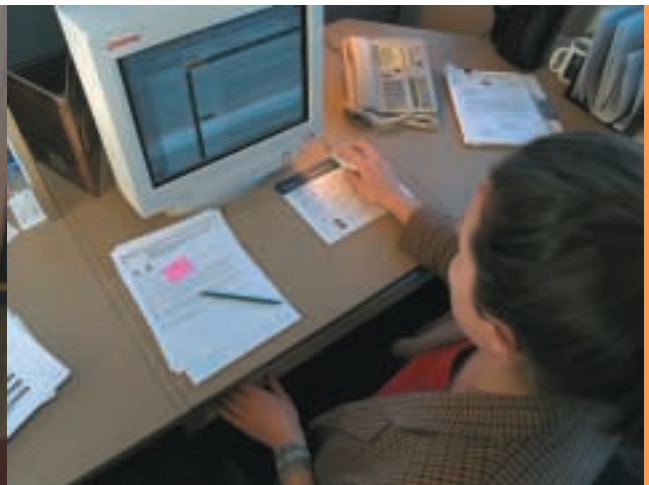
## > information technologies

The year 2000 date changeover took place safely and without inconveniencing customers. During the year, Information Technologies installed a number of computer tools of strategic importance to the business units. It also inaugurated a trading floor to enable Hydro-Québec to broker electricity on the wholesale power market.

Internet use has expanded, mainly to facilitate communications with customers. In addition, Web sites have been created for large-power customers. Hydro-Québec has also implemented information security measures.

#### CONNEXIM ON THE LOOKOUT FOR NEW BUSINESS OPPORTUNITIES

Connexim—a joint interest of Hydro-Québec and Bell Canada in operation since 1999—manages internal telecommunications networks (voice and data) for large and medium-sized businesses, in addition to the networks of its two parent companies. This will promote the development of synergy and expertise that will benefit all of its customers as well as its shareholders.



> Using a microprocessor-equipped interactive terminal, field personnel can consult the company's intranet.
> The intranet, an indispensable tool.

> March for Centraide, an organization that is close to Hydro-Québec's heart.
> Young people benefit from Hydro-Québec's community involvement.

## > community involvement

**SUPPORT FOR ORGANIZATIONS AND ASSOCIATIONS**

Hydro-Québec plays an important role in Québec society. In addition to the substantial economic spinoffs generated by its activities in all of the province's regions, it lends support to a great many causes in the spheres of health, education, and social and humanitarian aid.

In health care, Hydro-Québec supports research projects on mental health, children's health and the environment. These projects are referred by Québec's health-care research fund.

Hydro-Québec has also signed a three-year agreement with the Québec mental health foundation, in connection with a program for preventing depression in high school students.

Through its donations, the company continues to support such major health institutions as the Montréal Heart Institute, the Clinical Research Institute of Montréal and the Montréal Neurological Institute and Hospital.

In education, Hydro-Québec's support for Québec universities helped finance teaching and research activities as well as scholarships awarded to students at the undergraduate and postgraduate levels.

Hydro-Québec contributed to the basic funding for 17 research chairs, five of which were new this year: three at Université Laval—the chair in electric-energy economics, the chair in corporate occupational health and safety management, and the industrial chair in shotcrete and concrete repairs—and two at the Université de Montréal—the research chair in conducting polymers and the chair in process integration for the pulp and paper industry. The company's support amounts to approximately $1.5 million.

As in the past, Hydro-Québec supported a number of community organizations that assist young people.

And Hydro-Québec is still the largest donor to Centraide (the United Way). Donations collected from employees and pensioners, which were then matched by the company's contribution, totaled over $3.6 million—around 13% more than in 1999.

> *Symphony of the Millennium*, a memorable event.
> Hydro-Québec encourages young amateur athletes.

**SPONSORSHIP OF PROJECTS AND EVENTS**

Hydro-Québec also helped make numerous projects and events possible through its sponsorships.

The company presented its inaugural Énergie Hydro-Québec award as part of the Bell Super Science Fair and regional science fairs. This award was given out to 10 teams of young students who submitted the best energy-related projects.

Hydro-Québec once again demonstrated its support for Québec culture through its association with various events, including the *Symphony of the Millennium* and free Wednesdays at the Musée du Québec.

The company also renewed its commitment to the Journées de la culture through 2002. It remains one of the main sponsors of this activity, which was launched in 1997 by the Chantier de l'économie sociale. The agreement with the Abitibi-Témiscamingue international film festival was renewed for two years. As well, Hydro-Québec is the sponsor of the Pro Musica orchestra and the first official sponsor of the Orchestre symphonique de Montréal. And at the Montréal book fair, it awarded the $5,000 Marcel-Couture prize. This new prize recognizes a groundbreaking literary work.

Other Hydro-Québec-sponsored organizations and events include the Québec association of student entrepreneur clubs, an association called Les Jeunes Entreprises du Québec, Earth Day, the 6th Canadian and Québec Olympiad for technical training, the Grands prix du tourisme and a competition for disabled athletes. Together with the Québec foundation for excellence in sports, it also presented 18 awards of excellence, worth $3,000 each, to amateur athletes aged 15 to 23.

In addition, the company presented six awards of excellence to Aboriginal students at the college and university levels to encourage them to pursue their education, and sponsored the 10th edition of the First Peoples' Festival.

Through a special program, Hydro-Québec also encourages its employees to provide volunteer support for causes that are not funded by Centraide. This past year, the company devoted some $200,000 to the program, helping more than 200 organizations throughout Québec.

#### INTERNATIONAL COOPERATION

On the international scene, Hydro-Québec is actively engaged in cooperation with developing countries. As a member of the E7 group, the company contributes to various technical-assistance projects to promote sustainable development in such countries. This year, the focus was on South Africa, Laos, Bangladesh and Jordan. Hydro-Québec also allotted $1 million to cooperative projects with countries in the French-speaking world.

## > industry role

In 2000, Hydro-Québec chaired the E7, a body set up in 1992 and comprising 8 of the 15 largest electric utilities in the world: Edison Electric (United States), Électricité de France, Enel (Italy), Kansai (Japan), Ontario Power Generation, RWE (Germany), Tepco (Japan) and Hydro-Québec. The E7's mission is to play an active role in the international debate on the environment and sustainable development, particularly in the area of global warming.

During its chairmanship, Hydro-Québec headed the Regional Electricity Co-operation and Integration Working Group for developing countries. The group's list of problems and potential solutions was published under the title *E7 Guidelines for the Pooling of Resources and the Interconnection of Electric Power Systems*. The company also hosted the annual E7 summit, which took place in Québec City in October 2000.

In addition, Hydro-Québec took part in the Forum on Hydropower, an annual event organized by the Canadian Hydropower Association. This year's theme was the future of hydropower in Canada.

> Ceremony held at James Bay to honor the E7 founders: Richard Drouin, then Chairman of the Board and Chief Executive Officer of Hydro-Québec, and Pierre Delaporte, then Chairman of Électricité de France, accompanied by L. Jacques Ménard (left).

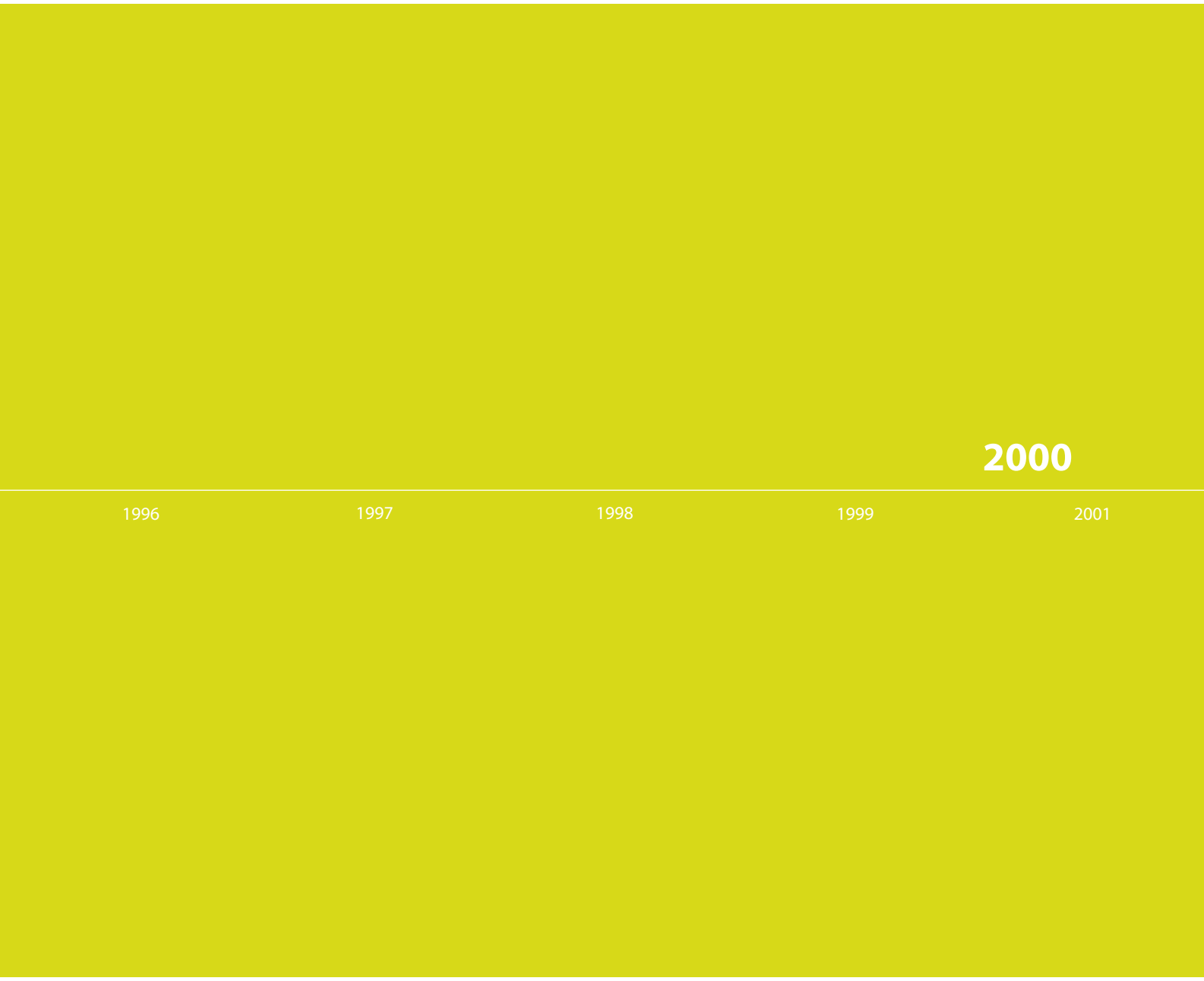
> Town crier at the *Electricity, the New Millennium* conference.

The 1st World Forum on Energy Regulation, held in Montréal, brought together more than 1,000 delegates from every continent. Hydro-Québec was one of the principal sponsors of this event, organized by Québec's Régie de l'énergie, the Canadian Association of Members of Public Utility Tribunals and the U.S. National Association of Regulatory Utility Commissioners.

The company also participated in the 6th International Business Alliances Forum, FuturAllia 2000, in Sherbrooke—an event that drew nearly 1,000 company managers, half of them from Europe and the United States.

The public relations association of Québec awarded Hydro-Québec its Équinoxes prize, interactive communication category, for the company's intranet.

Finally, Hydro-Québec hosted the conference-exposition *Electricity, the New Millennium*, attended by a large number of senior executives representing the electric industry in 65 countries. This event, held in Montréal, allowed the 2,000-plus participants to explore the challenges and business opportunities available worldwide.

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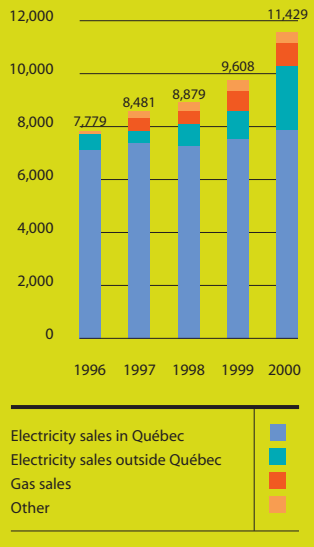
## > overview

**Sales**
($M)




**Net income** topped $1 billion to stand at $1,078 million, an increase of $172 million or 19% over last year. This performance exceeds the target of $950 million for 2000 set in the *Strategic Plan 2000-2004*.

**Revenue** surpassed $10 billion for the first time to reach $11,429 million, up 19% from 1999. This growth was largely driven by increased electricity transactions in the United States. We also benefited from sustained economic growth in Québec, which has stimulated electricity demand in the province since the start of 2000.

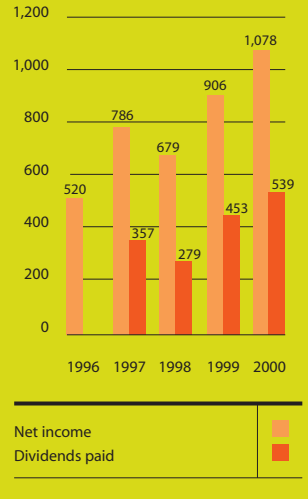
**Dividends** to our shareholder amounted to $539 million and constituted the fourth consecutive payment. The cumulative amount remitted to the Québec government since 1997 is $1.6 billion.

**Return** continued to improve in 2000, drawing closer to the targets in the *Strategic Plan 2000-2004*. Return on revenue stood at 9.4%, identical to 1999. Return on equity rose to 7.7% from 6.7% last year.

**The acquisition** of Transelec, Chile's largest power transmission company, represents approximately $1.6 billion. Investments like this one serve to solidify Hydro-Québec International's South American presence.

**Paying down the debt,** for the second consecutive year, will help to lower financial expenses over the long term.

**Net income and dividends paid**
($M)



Management's Discussion and Analysis reports on Hydro-Québec's consolidated and segmented results and consolidated financial position. Our analysis concludes with a brief discussion of our risk management strategy and outlook.

In our analysis, the consolidated group (Hydro-Québec) means the publicly owned corporation Hydro-Québec (the Corporation) and the companies in which it holds an interest, including its subsidiaries.

## > results

### CONSOLIDATED RESULTS

In 2000, Hydro-Québec maintained its forward momentum, with results reaching new heights. Consolidated net income totaled $1,078 million, up $172 million or 19.0% from the previous year. Hydro-Québec thus kept its commitment to better its financial position without lifting its rate freeze.

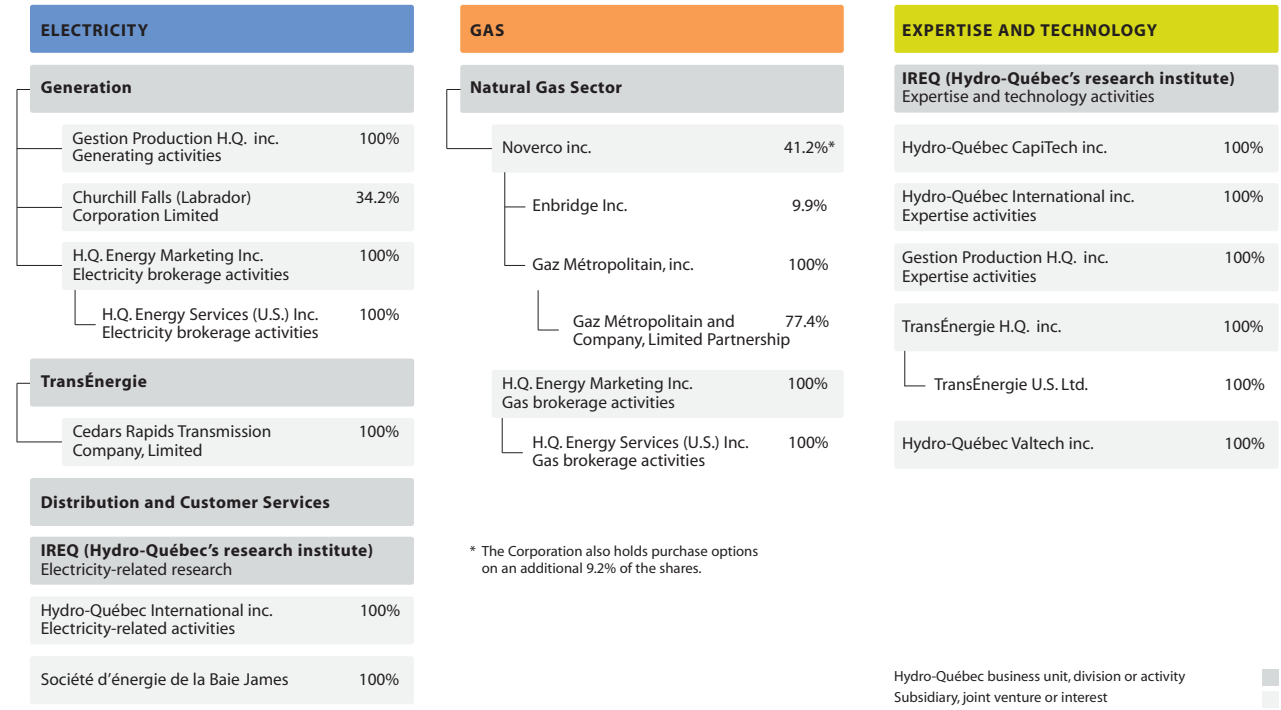
Consolidated sales continued their steady climb, growing by $1.8 billion or 19.0% to $11.4 billion. Total expenditure also grew, reaching $7.0 billion for a $1.6 billion increase, $1.2 billion of which is traceable to short-term electricity purchases. Financial expenses were comparable to the previous year, totaling $3.4 billion.

### OPERATING SEGMENTS

Hydro-Québec's activities fall into three energy-related operating segments:

- Electricity, Hydro-Québec's core business, encompasses the generation, transmission and distribution of electricity;
- Gas, which covers brokerage and natural gas transmission and distribution activities, carried on primarily through our interest in Noverco;
- Expertise and Technology, which comprises the development and marketing of technology and know-how, carried on through our main subsidiaries and the Hydro-Québec research institute.

## > operating segments (principal components)



**SEGMENTED INFORMATION**

| | 2000 | Change 1999-2000 | | 2000 | Change 1999-2000 | |
|---|---|---|---|---|---|---|
| | Revenue | | | Net income (loss) | | |
| | $M | $M | % | $M | $M | % |
| Electricity | **10,417** | 1,700 | 19.5 | **1,174** | 259 | 28.3 |
| Gas | **924** | 146 | 18.8 | **(11)** | (47) | (130.6) |
| Expertise and Technology | **97** | (41) | (29.7) | **(85)** | (40) | (88.9) |
| Intersegment eliminations for consolidation purposes | **(9)** | 16 | 64.0 | | | |
| **Total** | **11,429** | 1,821 | 19.0 | **1,078** | 172 | 19.0 |

With more than $10 billion in sales, or 91% of consolidated revenue, the Electricity segment continued to be the dominant sales contributor. In 2000, it accounted for 97% of Hydro-Québec's assets, a level identical to 1999, and experienced the most pronounced growth in terms of both revenue and net income generated.

The Gas segment recorded $924 million in sales, up 18.8% from the preceding year. The segment posted a net loss of $11 million, compared with net income of $36 million in 1999, mainly due to a dilution gain realized by Gaz Métropolitain in 1999 combined with the higher price of natural gas in 2000.

The Expertise and Technology segment, with total revenue of $97 million, posted an $85 million net loss in 2000, mirroring to some extent the reevaluation of its projects portfolio. These results are in keeping with the nature of the segment's activities, and the amounts invested, particularly in technology development, will yield a potential gain in the medium to long term.

### ELECTRICITY

**Record Electricity Sales**

Topping $10 billion for the first time, revenue from electricity sales catapulted $1,675 million or 19.7%, to reach $10,174 million. The corresponding total volume of sales stood at 190.1 TWh, up 18.4 TWh or 10.7% from the preceding year. This growth was mainly driven by increased transactions on U.S. markets at favorable prices and the growing demand for electricity in Québec, fueled by the province's strong economic performance.

— Growth in Electricity Sales in Québec

Electricity sales in Québec grew significantly, reflecting, in particular, increased demand from industrial customers and colder temperatures than in 1999. Revenue was up $346 million or 4.6% at $7,794 million, while the volume of sales totaled 152.8 TWh, an increase of 5.8 TWh or 3.9%.

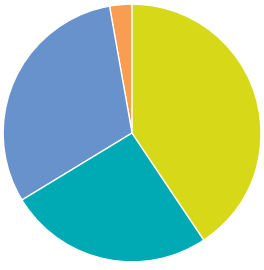
**ELECTRICITY SALES IN QUÉBEC, BY CATEGORY**

| | 2000 | Change 1999-2000 | | 2000 | Change 1999-2000 | |
|---|---|---|---|---|---|---|
| | Sales | | | Sales revenue | | |
| | TWh | TWh | % | $M | $M | % |
| Residential and farm | **51.7** | 2.4 | 4.8 | **3,167** | 133 | 4.4 |
| General and institutional | **30.5** | 0.7 | 2.4 | **2,002** | 39 | 2.0 |
| Industrial | **66.0** | 2.6 | 4.1 | **2,405** | 169 | 7.6 |
| Other | **4.6** | 0.1 | 2.2 | **220** | 5 | 2.3 |
| **Total** | **152.8** | 5.8 | 3.9 | **7,794** | 346 | 4.6 |

**1999-2000 SALES VARIATION FACTORS, BY CATEGORY**

| | Demand | | Temperature | | February 29 | | Other changes |
|---|---|---|---|---|---|---|---|
| | TWh | $M | TWh | $M | TWh | $M | $M |
| Residential and farm | 0.8 | 42 | 1.4 | 84 | 0.2 | 11 | (4) |
| General and institutional | 0.5 | 28 | 0.1 | 7 | 0.1 | 5 | (1) |
| Industrial | 2.4 | 119 | 0.0 | 0 | 0.2 | 6 | 44 |
| Other | 0.0 | 1 | 0.1 | 3 | 0.0 | 1 | 0 |
| **Total** | **3.7** | **190** | **1.6** | **94** | **0.5** | **23** | **39** |

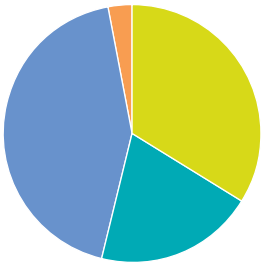
**Revenue from electricity sales in Québec**
(%)



**2000**

| | |
|---|---|
| Residential and farm | 40.6 |
| General and institutional | 25.7 |
| Industrial | 30.9 |
| Other | 2.8 |

**Electricity sales in Québec**
(%)



**2000**

| | |
|---|---|
| Residential and farm | 33.8 |
| General and institutional | 20.0 |
| Industrial | 43.2 |
| Other | 3.0 |

*Growth in Demand*

Stimulated by the still-robust Québec economy, demand rose by 3.7 TWh. This increase alone accounts for $190 million, or more than 50%, of the additional revenue from electricity sales in Québec.

Growth was most vigorous in the industrial sector, where sales rose by 2.4 TWh and revenue by $119 million. Nearly half of this increase was derived from small- and medium-power customers. In addition to benefiting from an export-favorable economy, Québec's chemical, smelting and metal-refining industries won new customers and saw production transferred from plants elsewhere in North America.

Sales in the residential and farm sector and the general and institutional sector grew by 0.8 TWh and 0.5 TWh respectively, generating additional revenue of $42 million and $28 million. In 2000, intense economic activity in Québec was reflected in increased housing starts early in the year and a higher commercial occupancy rate. This rate improved primarily on the strength of the new economy, particularly in Montréal. Lastly, higher heating oil and natural gas prices drove up electricity demand among our customers, who tended to make greater use of dual-energy rates.

*More Seasonal Temperatures*

Colder temperatures than in 1999 sent revenue up by $94 million over the preceding year. The residential and farm sector, the most sensitive to climatic changes because of its heating requirements, recorded a 1.4 TWh increase in sales volume, for additional revenue of $84 million.

However, a shortfall of $50 million was recorded for 2000 because of above-average temperatures, mainly in the first quarter.

*Leap Year*

The extra day of consumption on February 29 accounted for additional sales of 0.5 TWh and added revenue of $23 million.

*Other Factors*

Sales contracts with rates based on the price of aluminum contributed an additional $47 million to industrial-sector revenue, reflecting the 16.5% rise in the average price of the metal. This revenue increase includes the impact of derivative instruments used to offset the effect of aluminum price fluctuations on sales revenue. In comparison with 1999, the exchange-rate effect on sales concluded in U.S. dollars was reflected in slightly higher revenue.

| ELECTRICITY SALES OUTSIDE QUÉBEC | 2000 | Change 1999-2000 | |
|---|---|---|---|
| | $M | $M | % |
| Sales in Canada and the United States | | | |
| Long-term sales | **346** | (46) | (11.7) |
| Short-term sales | **2,003** | 1,379 | 221.0 |
| | **2,349** | 1,333 | 131.2 |
| Sales, other countries* | **31** | (4) | (11.4) |
| **Total** | **2,380** | 1,329 | 126.5 |

* Sales by Fortuna generating station in Panama covered a nine-month period in 2000.

— Marked Rise in Electricity Sales Outside Québec

In 2000, market restructuring in the North American electrical industry intensified. With the introduction of new regional energy exchanges, market players can now conclude short-term electricity sales and purchases on a real-time basis. Forward financial markets for electricity also continued to flourish. Hydro-Québec set up an energy trading floor so that it could participate more fully in these markets, particularly in electricity brokerage and sale and purchase transactions, by taking advantage of the flexibility provided by its hydropower facilities.

This environment joined with higher market prices for electricity to dramatically lift electricity sales outside Québec. The additional sales commitments were met using short-term electricity purchases and our surplus generating capacity. In carrying out these transactions, Hydro-Québec ensured careful and optimal management of its reservoirs over a horizon of several years.

Electricity sales outside Québec consequently gained $1,329 million or 126.5% to reach $2,380 million. The corresponding volume totaled 37.3 TWh, up 12.6 TWh from the preceding year. With the changes in the market, short-term sales therefore increased by $1,379 million or 14.5 TWh, while long-term sales declined by 1.8 TWh, which was reflected in a $46 million decrease in revenue.

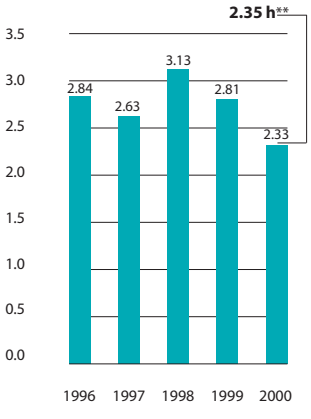
Lastly, we continued to assert our presence on international markets through our interests in Panama and Costa Rica. We thus posted revenue of $31 million in 2000.

**Operating Expenses**

In keeping with our commitment to improve service quality and reliability for all our customers, we stepped up routine maintenance and system enhancement activities. This commitment was mirrored in a $219 million or 12.8% increase in operating expenses, which stood at $1,934 million. Moreover, average interruption time per customer, a system performance indicator, was 2.33 hours in 2000, exceeding the goal for 2004 of 2.35 hours set in the *Strategic Plan 2000-2004*.

Labor costs, which have declined steadily over the past several years, accounted for 60% of total expenses in 2000, compared with an average of 68% over the past five years. The decrease includes the positive effect of the pension credit recorded since 1999. Although our total work force increased slightly from 1999, it was still below our target of 19,500 employees as at December 31, 2000.

**Average hours of service interruption per customer***




* Excluding unusual major climatic events.
** Target for 2004 according to the *Strategic Plan 2000-2004*.

This year we focused on system reinforcement and looping. As a result, the proportion of expenses capitalized to investment projects reached 23% in 2000, up from 22%. The 1999 labor dispute had resulted in a decline in capitalizable projects, as priority was given to readying the system for the winter months.

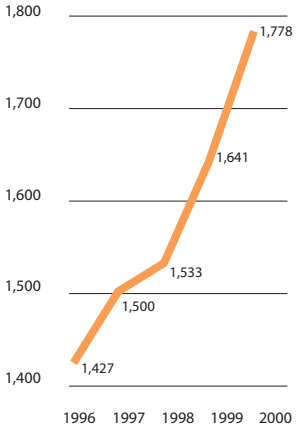
**Electricity and Fuel Purchased**

Our increased transactions on North American markets elevated electricity purchases by $1,171 million to $1,715 million. This substantial growth was almost entirely attributable to short-term electricity purchases, which increased by $1,151 million to $1,409 million in 2000. We stepped up electricity purchases for use either in brokerage transactions or future resale during peak periods. In addition to short-term electricity purchases, the last months of 2000 saw expenses of $77 million relating to structured energy transactions concluded in 1998 and 1999.

Regular electricity purchases increased by $18 million from the previous year to reach $302 million. Price adjustment clauses in the various contractual agreements signed with private producers and Churchill Falls (Labrador) Corporation accounted for this increase.

Fuel purchases were down by $39 million from the previous year to $53 million, due notably to limited use of Tracy thermal power plant.

**Change in depreciation, amortization and decommissioning expense**
($M)




**Depreciation, Amortization and Decommissioning**

Depreciation, amortization and decommissioning expense increased by $137 million or 8.3% in 2000 to reach $1,778 million, due mainly to fixed-asset depreciation and project write-offs.

The sinking fund method of depreciation, which results in a depreciation expense for fixed assets that grows over time, is a natural factor in the increase. Other factors, however, also played a part: the downward adjustment to the life span of certain assets as part of the five-year life review program; current-year commissionings; and the impact, over a full year, of prior-year commissionings.

Expenses related to project write-offs specifically reflect the $33 million write-off of environmental and engineering studies for the Lower Churchill River hydropower development project, in Labrador. This amount is for feasibility studies related to generation in Labrador and takes account of recent discussions between the Corporation and its partner, Newfoundland and Labrador Hydro, concerning the possible configuration of any future project. Deferred charges and draft-design studies totaling $30 million were written off after the potential of our projects portfolio was reevaluated as part of an annual review process.

**Tax**

In May 2000, a technical amendment announced in the Québec Budget changed the basis for calculating capital tax. The measure, which applies retroactively as of 1995, brought about a reduction of the expense for 2000.

**Financial Expense Stability**

Financial expenses held steady in 2000 at $3,263 million compared with $3,242 million the preceding year, an increase of just $21 million or 0.6%.

— Changes in Financial Variables

As expected, the significant tightening of monetary conditions initiated in mid-1999 by the U.S. Federal Reserve had an appreciable impact on the three-month U.S. dollar LIBOR, which increased, on average, from 5.4% in 1999 to 6.5% in 2000. In Canada, the rate for three-month Canadian bankers' acceptances was also up, gaining almost 1.0% compared with 1999.

The Canadian dollar, after recovering early in the year, slid in value against the U.S. dollar, only to rally at the very end of the year. After fluctuations, the Canadian dollar averaged out to US$0.673, the same as in 1999.

— Management of Risks Arising from Financial Variables

Considering that 26% of our debt is subject to variable rates and 43% is denominated in U.S. dollars, we are exposed to risks related to fluctuations in short-term interest rates and the value of the Canadian dollar. In order to reduce operating results volatility, we use an active, integrated approach to manage these risks and the risk associated with fluctuations in the price of raw materials. When there is movement in the markets, our objective is to keep the maximum loss below the risk threshold set by the Board of Directors early in the year, while maximizing potential gains.

— Interest

Despite interest-rate fluctuations during the year, interest expense remained stable at $2,902 million compared with $2,911 million in 1999, a decrease of $9 million. This result is partly explained by favorable long-term rates obtained in refinancing debt according to new maturities. Moreover, some debt was repaid out of funds from operations, which reduced debt and the related financial expenses for recurring annual savings of approximately $95 million, excluding the exchange-rate effect.

Increases in short-term interest rates, however, drove up interest expense on the variable portion of long-term debt by $131 million compared with 1999, including the offsetting effect of managing rates with derivative instruments.

— Exchange Loss

The exchange loss rose to $174 million from $134 million in 1999, primarily due to the volume of maturing U.S.-dollar-denominated debt, which is hedged by future revenue streams in this currency.

— Loan Guarantee Fees

Under the *Hydro-Québec Act*, loans are approved and guaranteed by the government of Québec. In exchange, we are required to pay an annual amount equal to 0.5% of the guaranteed-debt balance at the preceding year-end. In 2000, these fees totaled $187 million, down $10 million from 1999. This decrease is explained by the favorable exchange-rate effect and the net repayment of debt in 1999.

**GAS**

In 2000, the Gas segment recorded a net loss of $11 million, compared with net income of $36 million in 1999. Gas sales, however, stood at $924 million, an increase of $146 million or 18.8% over 1999.

Net income from our interest in Noverco totaled $15 million, a decline of $10 million from the previous year. It is important to remember that Gaz Métropolitain realized a dilution gain in 1999 on an issue of units of Gaz Métropolitain and Company, Limited Partnership (GMCLP). Noverco's net income, excluding this gain, was up from the previous year due to favorable changes in the operating results of GMCLP and Enbridge.

Other than the interest in Noverco, Gas segment activities—consisting mainly of brokerage operations in the Québec and U.S. markets—resulted in a net loss of $26 million in 2000, compared with net income of $11 million in 1999. The net loss is mainly attributable to a pre-2000 fixed-price sale contract for which the supply costs, at market prices, were up sharply.

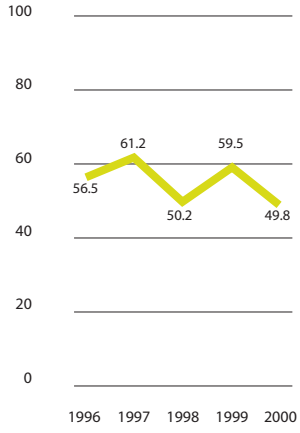
**EXPERTISE AND TECHNOLOGY**

The Expertise and Technology segment reported an $85 million loss at year-end, $40 million higher than in the previous year. In addition to the operating results of subsidiaries involved in technological development and marketing, this sector's results now include amounts relating to capitalized development expenses in high-technology sectors formerly presented in the Electricity segment.

Amounts invested in technological development are capitalized and amortized over a five-year period. Moreover, deferred amounts are reviewed each year to determine their recoverability. Because of the nature of this segment's activities and our cautious management approach, the Corporation generally incurs significant start-up costs in the initial years of a project which offset medium and long-term potential gains. Accordingly, the results for 2000 reflect the impact of substantial amounts spent on projects in the last few years, in particular the ACEP initiative. In addition, a number of projects, including the motor-wheel, were written off following a review of current projects according to their market potential.

Development and marketing activities by subsidiaries posted an $18 million loss, $10 million more than in 1999, due principally to stepped-up solicitation efforts by Hydro-Québec International (HQI) for the purpose of building new markets. The expenses related to these development activities adversely affected the year's results, but should result in future growth for the subsidiary's operations. In terms of overall performance, the marketing activities of the business units' holding companies continued to record net income, which in 2000 totaled $5 million.

**Self-financing ratio**
(%)




# > financial position

**OPERATING ACTIVITIES**

Growth in our operations added $461 million or 16.0% to cash from operating activities compared with 1999, bringing the total to $3,345 million. The increase in electricity transactions in the United States and growth in electricity sales in Québec were the main factors resulting in additional cash.

The cash generated was used to finance the Corporation's investment program and pay down long-term debt. Lastly, the acquisition of Transelec, in Chile, which represents approximately $1.6 billion, reduced the self-financing ratio to 49.8% at year-end 2000, down 16.3% from the ratio of 59.5% recorded in 1999.

**INVESTING ACTIVITIES**

The investment program in 2000 totaled $3,563 million, up $1,465 million or 69.8% from the preceding year. The increase stemmed mainly from the acquisition of Transelec, a leading South American power transmission company.

Investing activities fall into three broad categories: ongoing operations encompass amounts invested in the normal course of the Corporation's business; development activities cover amounts invested to develop new business; and the third category comprises amounts invested through Hydro-Québec's interests.

**Ongoing Operations**

Amounts invested as part of ongoing operations totaled $1,509 million and are divided into three types according to their objective.

— Prolonging Asset Service Life

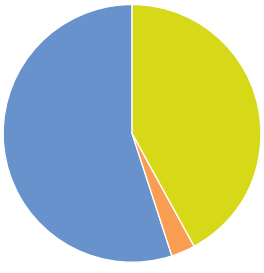
We invested $683 million to prolong the service life of our facilities and equipment, increase their production capacity, or replace them.

The Grand-Mère hydroelectric development project, one of the largest, will boost capacity to 220 MW, a 46.7% increase compared with the existing generating station, which will be dismantled. This work, which was begun in 2000, represents $40 million of a projected total investment of $460 million and is expected to continue into 2004.

Major rehabilitation projects designed to prolong the useful life and enhance the reliability of generating facilities are still under way. The Beauharnois project, in particular, was allocated $82 million this year, mainly for infrastructure work, modernization, generating unit overhauls and construction of auxiliary buildings. Since 1994, commissionings have been undertaken according to degree of completion.

This year we invested $37 million in Shawinigan-2 and Shawinigan-3 generating stations, specifically to overhaul and modernize three generating units commissioned in the final months of 2000. The work should be completed in 2001.

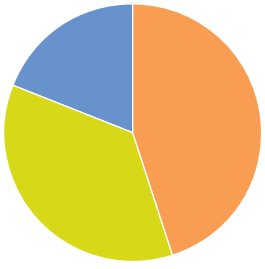
**Investments by type of activity**



| 2000 | $M | % |
|---|---|---|
| Ongoing operations | 1,509 | 42 |
| Development activities* | 113 | 3 |
| Hydro-Québec's interests** | 1,941 | 55 |

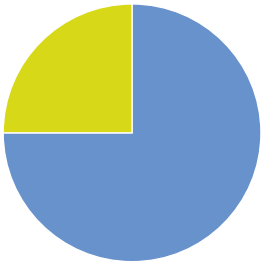
* Not including an amount of $690 million for the Corporation's investment in its interests, eliminated during consolidation.
** Including eliminations for purposes of consolidation.

**Ongoing operations**



| 2000 | $M | % |
|---|---|---|
| Prolonging asset service life | 683 | 45 |
| Growth in the Québec customer base | 547 | 36 |
| Quality maintenance and enhancement | 279 | 19 |

**Development activities***



| 2000 | $M | % |
|---|---|---|
| Business and technology development | 204 | 25 |
| International development | 599 | 75 |

* Excluding eliminations of $690 million.

Lastly, the bulk of the $37 million earmarked for rehabilitation and modernization of Bersimis-1 generating station was allocated to two generating units. Commissionings have taken place since 1997 and the project should continue into 2005.

We also earmarked $152 million for the renewal of aging or inadequate distribution system equipment in order to respond to the larger electrical load.

— Growth in the Québec Customer Base

Of the $547 million invested to meet the growing needs of Québec customers, $294 million was spent on the ongoing construction of Sainte-Marguerite-3 generating station. With this project, 882 MW of power will be added to the grid to meet future demand. In 2000, we installed the main equipment and are conducting tests and inspections required for commissioning, scheduled for the fall of 2001. We also injected $117 million into projects to ensure power supply to customers, mainly in the form of system extensions to connect new customers.

— Quality Maintenance and Enhancement

We spent $219 million to strengthen the grid by optimizing operational processes and developing our equipment. Activities in 2000 included $68 million in reinforcement and looping work on the transmission system to bolster electrical supply security for areas affected by the 1998 ice storm and diversify supply sources. The downtown Montréal, downtown Québec City and Québec-Mauricie loops were completed in 2000. Other loop projects are following the usual process for approval by the competent authorities and should be completed between 2002 and 2003. The Corporation also invested $19 million in the interconnection project with Ontario, which will heighten interconnected system security and increase electricity exchanges while allowing for profitable commercial transactions. Work began on the new 1,250-MW interconnection after the 1998 ice storm and is expected to be completed in 2003.

In addition, $60 million was invested to fulfill various contractual, legal, environmental or other obligations. More than half of this amount relates to system modification and relocation work to comply with the requests of municipal administrations and the government of Québec.

**Development Activities**

The Corporation invested $803 million in business and technology development as well as in international development. These two categories include the Corporation's investments in its holdings.

— Business and Technology Development

Business and technology development accounted for $204 million of the total amount invested. Business development projects cover amounts invested to generate new sales or maintain or develop new markets in Québec or elsewhere. This year, $44 million was invested in H.Q. Energy Marketing to support expansion of its activities. H.Q. Energy Marketing, through its subsidiary H.Q. Energy Services (U.S.), contributes to the Corporation's business development through power purchase-resale activities on the U.S. market.

Technology development projects comprise investments aimed at marketing new products or processes. The Corporation earmarked $28 million for the ACEP project to develop, industrialize and market rechargeable lithium-metal-polymer batteries for the telecommunications and automotive markets. Also, additional capitalization of $37 million was provided to Hydro-Québec CapiTech, which manages Hydro-Québec's technology-related venture capital investments. The funds were added as part of the first venture capital portfolio of $108 million, authorized by the Corporation in 1998.

— International Development

During the year, the Corporation invested $599 million in international development activities in markets other than those of neighboring power grids. The main focus of our expertise was on hydroelectric generating station construction and management and high-voltage transmission. The investments were chiefly made through our subsidiary HQI, which is dedicated to market prospecting, and were primarily used to ensure the success of the largest transaction ever completed by HQI in international development, the acquisition of Transelec.

**Hydro-Québec's Interests**

Amounts invested by Hydro-Québec's interests totaled $1,940 million over the year and mainly relate to investments and fixed assets.

— Investments

Investments totaled $1,685 million at year-end. During the last quarter, HQI completed a $1,631 million transaction to acquire all shares of Transelec, the largest power transmission company in Chile. This strategic acquisition, in a field where Hydro-Québec has high-level expertise, affords opportunities for future expansion in South America.

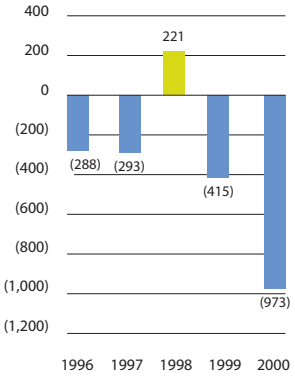
Investments acquired by the Corporation's other interests reached $54 million in 2000. Transactions included the addition of $40 million to Hydro-Québec CapiTech's venture capital portfolio through equity participation or reinvestment in companies offering energy-related technological products and services.

— Fixed Assets

During the year, $198 million was used to acquire fixed assets through Hydro-Québec's interests, including $89 million by its subsidiary, HQI. The subsidiary added to its fixed assets mainly in order to complete power transmission lines in Peru and Australia and construct the Bucksport thermal generating station in the United States. Also, TransÉnergie H.Q., through its American subsidiary, TransÉnergie U.S., spent $49 million as part of a project to build and operate an interconnection line between the New York State and Connecticut power grids.

Lastly, our share of amounts invested by GMCLP, which we hold through Noverco, amounted to $43 million.

**Changes in long-term financing**
($M)




| ($M) | 1996 | 1997 | 1998 | 1999 | 2000 |
|---|---|---|---|---|---|
| Issues | 1,893 | 1,931 | 2,472 | 2,208 | 2,069 |
| Redemptions | (2,181) | (2,224) | (2,251) | (2,623) | (3,042) |

**FINANCING ACTIVITIES**

**Long-Term Financing**

The following analysis focuses on the Corporation's long-term financing activities, which represent substantially all such activities of Hydro-Québec. At year-end 2000, permanent financing of the Transelec acquisition was not yet complete and is therefore included in short-term financing.

For the second consecutive year, the Corporation made a net repayment of long-term debt. The repayment amounted to $973 million, an increase of $558 million from 1999. Higher-than-forecast funds from operations and lower-than-expected allocations to investment projects meant that we only had to complete 75% of our borrowing program, initially set at $2,769 million, for total borrowed capital of $2,069 million.

To guide its financial decisions, the Corporation adopted a financing policy that requires it to secure, at the lowest possible cost, the funds needed to finance its activities. This policy also promotes long-term rate stability by minimizing the risk associated with debt refinancing. The Corporation's four objectives are to diversify funding sources, minimize foreign exchange risk, stagger debt maturities and maintain short-term variable-rate debt at around 25%.

As in 1999, all transactions under our borrowing program in 2000 were in Canadian dollars. The rates of return sought by Canadian investors were more favorable than those demanded in other capital markets where the larger offering drove up the cost of borrowing.

The beginning of the year, when the markets were nervously anticipating a hike in U.S. long-term interest rates, was an excellent time to launch a floating-rate issue. In January, we floated an international issue of floating-rate debentures in the amount of CDN$500 million, maturing in 2005. The issue was well received and provided us with an opportunity to assert our presence on the European and U.S. markets.

In early June, we marketed a new $400 million series of debentures, maturing in February 2011. In late August, renewed investor demand, which had been fairly moderate during the summer months, prompted us to reopen the series. The amount outstanding subsequently doubled from $400 million to $800 million, increasing the security's market liquidity.

The Canadian Medium-Term Note Program enabled us to complete our financing. We issued $397 million in notes with maturities of 2035 or later. Notes with earlier maturities, between 2003 and 2006, were also issued for a similar amount.

Lastly, we decided to exercise two early redemption options on bonds with a face value of $660 million and bearing interest at an average annual rate of 12.8%. We financed these redemptions through issues with an average rate under 6.5%.

**Short-Term Financing**

The acquisition of Transelec, at the end of 2000, was temporarily financed using a short-term loan. The Corporation borrowed part of the amount, US$376 million, and a subsidiary of Hydro-Québec International assumed the balance of US$724 million. Long-term permanent financing of these amounts is expected to be secured during 2001.

For cash flow purposes, the Corporation has access to the following pre-authorized funding sources:

| Type of financing | Authorized volume | Market | **Outstanding December 31, 2000** |
|---|---|---|---|
| Credit | CDN$365M or US$350M | Canada | – |
| | US$50M | United States | – |
| Standby credit | US$1,800M | Eurodollar | – |
| Commercial paper | US$2,750M or equivalent in CDN$ | United States Canada | **$46M** |

**Dividends, Capitalization and Interest Coverage**

With a year-end capitalization rate of 26.9%, Hydro-Québec was able to declare dividends of $539 million, or 50% of net income. After the dividends were paid to the shareholder, the capitalization rate stood at 26.2%, the same as in 1999.

Moreover, growth in revenue once again resulted in better interest coverage. From its level of 1.25 times interest expense in 1998, the ratio improved appreciably, reaching 1.33 in 1999 and 1.37 in 2000.

**Credit Ratings**

The following table summarizes Hydro-Québec's credit ratings:

| | **2000** | 1999 |
|---|---|---|
| U.S. agencies | | |
| Moody's | **A2 positive** | A2 positive |
| Fitch IBCA, Duff & Phelps | **AA-** | AA- |
| Standard & Poor's | **A+ stable** | A+ stable |
| Canadian agency | | |
| DBRS | **A stable** | A (low) stable |

## > risks and outlook

### RISK MANAGEMENT

Hydro-Québec has opted for an integrated business risk management strategy, which it is implementing on a gradual basis. The strategy covers all business units and activities and enables the determination of key risk factors for each one. The most significant risks are then incorporated into the Hydro-Québec risk portfolio.

Senior management has developed a progressive implementation plan based on priority management activities such as risk management systematization (across all operations and management levels), risk assessment and integrated risk management within a portfolio perspective, and preparation of periodic status reports to track risk management progress.

Business risk analysis is integral not only to our strategic and business plans, but also to management of projects and ongoing operations. It also results in specific issues being addressed, such as runoff risk management and work process improvement, on an as-needed basis. Accordingly, the recommendations retained by Hydro-Québec concerning the investment portfolio include the adoption of project selection criteria ensuring a more balanced portfolio, reinforcement of pre- and post-performance assessment mechanisms and quicker adaptation of training to user needs.

We have also fine-tuned our sensitivity analyses for outside risks arising from unusual natural events and changes in temperature, demand, runoff, foreign exchange rates and interest rates. We are also planning to use a stochastic optimization technique to help us select the best strategies for dealing with uncertainty that arises when several issues are present at the same time.

### OUTLOOK

**Business Environment**

The opening of North American electricity markets and sustained growth in energy demand have unquestionably shaped the course of the electricity industry over the past three years. Like 1999, the year 2000 was characterized by an appreciable increase in purchase-resale transactions on U.S. markets. Our reservoir storage capacity gives us a competitive edge, allowing us to capitalize on good price conditions in the Northeastern U.S. market through favorable price arbitraging. These transactions do not affect security of electricity supply for Québec customers.

Since December 1996, the Régie de l'énergie du Québec has regulated the distribution and transmission of electricity. On August 15, 2000, Hydro-Québec submitted a rate proposal to the Régie for electricity transmission rates for 2001. The rates paid by Québec customers will not increase as a result of the Régie's decision, which is expected by the end of 2001. We have confirmed our commitment to freeze electricity rates until April 2002, pursuant to our *Strategic Plan 2000-2004*.

In June 2000, the government of Québec passed the *Act amending the Act respecting the Régie de l'énergie and other legislative provisions*. The Act is designed to preserve the social pact which guarantees that Québec consumers will continue to benefit from low electricity rates, particularly in the residential sector. As such, the government has established a heritage electricity pool for Hydro-Québec's hydroelectric production and existing long-term supply contracts. The pool corresponds to annual consumption of up to 165 TWh per year, for which the price is set at 2.79 cents per kWh. Beyond the heritage pool amount, the Act opens up the wholesale market to competition.

**2001 Financial Outlook**

For the past two years, Québec has enjoyed outstanding economic growth. In 1999, Québec's real gross domestic product grew by 4.7%, the best performance since 1984. The third quarter of 2000 marked the twentieth consecutive quarter of growth for this economic indicator. The Québec economy owes much of its strength to a vital local manufacturing industry and the vigorous U.S. economy.

The favorable economic environment and high fuel prices are having a positive impact on electricity sales. For 2001, the assumption underlying our financial forecasts is that there will be an economic slowdown. Consequently, electricity demand in Québec will grow at a more moderate pace in 2001 compared with the last two years.

Our resolve to enhance corporate profitability will be reflected in a sustained drive to increase sales and control costs. However, weakness in the Canadian dollar should continue to adversely affect our financial expenses in 2001. We nonetheless expect net income to top $1 billion in 2001 for the second straight year.

The 2001 investment program is approximately $2.4 billion. Aside from investments to prolong the service life of our assets, including Beauharnois and Grand-Mère generating stations, we will invest in reinforcing and enhancing the transmission and distribution systems. The year 2001 will see the commissioning of Sainte-Marguerite-3 generating station. Lastly, the Corporation's borrowing program, including the refinancing of Transelec, will total $3.9 billion, higher than in 2000. These funds will also be used to refinance major debt maturing in 2001.

## > management report

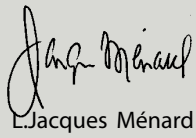
Hydro-Québec's consolidated financial statements and all additional information contained in the Annual Report are the responsibility of Management and are approved by the Board of Directors. Management's responsibility also includes the selection of appropriate accounting practices in accordance with Canadian generally accepted accounting principles, taking into account generally accepted accounting methods and practices of regulatory bodies. As required, Management makes informed judgments and prepares the most appropriate estimates of the outcome of events and transactions, with due consideration given to materiality. Financial information contained elsewhere in the Annual Report is consistent with that in the financial statements.

Management, in keeping with its responsibilities, maintains a control system, designed among other things to provide reasonable assurance that the assets of Hydro-Québec are adequately recorded and safeguarded and that the accounting records form an appropriate basis for the preparation of reliable financial statements. An internal auditing process allows evaluation of the sufficiency and efficiency of control, as well as of Hydro-Québec's policies and procedures. Recommendations ensuing from this process are submitted to Management and the Audit Committee.

The Board of Directors assumes its responsibility for the consolidated financial statements principally through its Audit Committee, composed solely of directors who do not hold full-time positions within the Corporation or in one of its subsidiaries. This committee's mandate is to ensure that the financial statements present fairly Hydro-Québec's financial position, the results of its operations and its cash flows. The Audit Committee meets regularly with Management, the General Auditor and the external auditors to review the results of their audits and the reports on Hydro-Québec's accounting methods and policies and on the control systems. The General Auditor and the external auditors have full and unrestricted access to the Audit Committee, with or without Management's presence.

Hydro-Québec has also established a code of ethics and a code of conduct primarily to ensure the proper management of its resources and the orderly conduct of business.

The consolidated financial statements have been audited jointly by accounting firms Samson Bélair/Deloitte & Touche and PricewaterhouseCoopers.



L. Jacques Ménard
Chairman of the Board

André Caillé
President and
Chief Executive Officer

Daniel Leclair
Vice President – Finance
and Chief Financial Officer

Montréal, Québec
February 23, 2001

## > auditors' report

To the Minister of Finance of Québec:

We have audited the consolidated balance sheet of Hydro-Québec as at December 31, 2000, and the consolidated statements of operations, retained earnings and cash flows for the year then ended. These financial statements are the responsibility of Hydro-Québec's Management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of Hydro-Québec as at December 31,2000,and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles as described in note 1. As required by the *Auditor General Act* (R.S.Q., c. V-5.01), we report that, in our opinion,these principles have been applied on a basis consistent with that of the preceding year.

Samson Bélair
Deloitte & Touche

Chartered Accountants

Montréal, Québec
February 23,2001

Chartered Accountants

## > consolidated statement of operations

| For the year ended December 31 | | 2000 | 1999 |
|---|---|---|---|
| In millions of dollars | notes | | |
| **Revenue** | | **11,429** | 9,608 |
| **Expenditure** | | | |
| Operations | | **2,135** | 1,912 |
| Electricity and fuel purchased | | **2,408** | 1,109 |
| Depreciation, amortization and decommissioning | 2 | **1,896** | 1,731 |
| Taxes | 3 | **525** | 592 |
| | | **6,964** | 5,344 |
| **Operating income** | | **4,465** | 4,264 |
| Financial expenses | 4 | **3,369** | 3,345 |
| Income before non-controlling interest | | **1,096** | 919 |
| Non-controlling interest | | **18** | 13 |
| **Net income** | | **1,078** | 906 |

## > consolidated statement of retained earnings

| For the year ended December 31 | | 2000 | 1999 |
|---|---|---|---|
| In millions of dollars | note | | |
| Balance at beginning of year | | **9,367** | 8,914 |
| Net income | | **1,078** | 906 |
| | | **10,445** | 9,820 |
| Dividends | 16 | **539** | 453 |
| Balance at end of year | | **9,906** | 9,367 |

## > consolidated balance sheet

| As at December 31 | | 2000 | 1999 |
|---|---|---|---|
| In millions of dollars | notes | | |
| **ASSETS** | | | |
| **Fixed assets** | 5 | **49,640** | 48,226 |
| **Current assets** | | | |
| Cash | | **134** | 88 |
| Investments | | **612** | 400 |
| Accounts receivable | | **1,861** | 1,875 |
| Financial assets related to debt | | **89** | 191 |
| Materials, fuel and supplies | | **407** | 381 |
| | | **3,103** | 2,935 |
| **Other long-term assets** | | | |
| Investments | 6 | **750** | 702 |
| Deferred charges | 7 | **4,309** | 3,874 |
| Financial assets related to debt | 8 | **372** | 418 |
| Other assets | 9 | **937** | 681 |
| | | **6,368** | 5,675 |
| | | **59,111** | 56,836 |
| **LIABILITIES AND EQUITY** | | | |
| **Long-term debt** | 10 | **34,887** | 36,011 |
| **Current liabilities** | | | |
| Borrowings | | **1,774** | 107 |
| Dividends payable | | **539** | 453 |
| Accounts payable | | **1,471** | 1,236 |
| Accrued interest | | **1,264** | 1,277 |
| Current portion of long-term debt | | **3,484** | 2,598 |
| | | **8,532** | 5,671 |
| **Other long-term liabilities** | 11 | **673** | 671 |
| **Perpetual debt** | 12 | **552** | 552 |
| **Non-controlling interest** | | **187** | 190 |
| **Shareholder's equity** | 16 | | |
| Share capital | | **4,374** | 4,374 |
| Retained earnings | | **9,906** | 9,367 |
| | | **14,280** | 13,741 |
| | | **59,111** | 56,836 |

Yvon Lamontagne
Chairman of the Audit Committee

L.Jacques Ménard
Chairman of the Board

## > consolidated statement of cash flows

| For the year ended December 31 | | 2000 | 1999 |
|---|---|---|---|
| In millions of dollars | notes | | |
| **Operating activities** | | | |
| Net income | | **1,078** | 906 |
| Depreciation of fixed assets | | **1,587** | 1,538 |
| Amortization of deferred charges | | **449** | 382 |
| Change in non-cash working capital items | 17 | **89** | 105 |
| Other | | **142** | (47) |
| | | **3,345** | 2,884 |
| **Investing activities** | | | |
| Fixed assets | | **(1,812)** | (1,642) |
| Acquisition of joint ventures | 15 | **(1,576)** | (95) |
| Long-term investments | | **(65)** | (216) |
| Net change in short-term investments | | **(131)** | (129) |
| Other | | **(37)** | (145) |
| | | **(3,621)** | (2,227) |
| **Financing activities** | | | |
| Issue of long-term debt | | **2,200** | 2,302 |
| Maturity of long-term debt and sinking fund redemption | | **(2,317)** | (2,279) |
| Repayment in advance of long-term debt | | **(737)** | (406) |
| Net change in short-term borrowings | | **1,678** | 40 |
| Dividends paid | | **(453)** | (279) |
| Other | | **(18)** | 32 |
| | | **353** | (590) |
| **Net change in cash and cash equivalents** | | **77** | 67 |
| **Cash and cash equivalents at beginning of year** | | **100** | 33 |
| **Cash and cash equivalents at end of year** | | **177** | 100 |

| | | |
|---|---|---|
| **Supplementary information** | | |
| Interest paid | **2,967** | 3,004 |

Cash and cash equivalents comprise cash and liquid short-term investments with maturities generally less than or equal to three months from the date of acquisition.

## > note 1. significant accounting policies



Under the provisions the *Hydro-Québec Act*, the publicly owned corporation Hydro-Québec (the "Corporation") is mandated to supply power and to pursue endeavors in energy-related research and promotion, energy conversion and conservation, and any field connected with or related to power or energy.

The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles and take into account generally accepted accounting methods and practices of regulatory bodies. The regulatory accounting practices adopted by the Corporation, which differ from the accounting practices otherwise applied in unregulated enterprises, are in particular related to certain deferred charges, including those concerning major projects canceled or postponed and personnel reduction and renewal measures, as well as depreciation of fixed assets disposed of.

**CONSOLIDATION**

The consolidated financial statements include the accounts of the Corporation, its subsidiaries, all of which are wholly owned, and its interests in jointly controlled enterprises (collectively "Hydro-Québec").

The interests in jointly controlled enterprises, that is, joint ventures, are accounted for using the proportionate consolidation method. Investments in companies over which Hydro-Québec can exercise a significant influence are accounted for on an equity basis, whereas venture capital investments are generally recorded at cost. Other long-term investments are also recorded at cost.

**GOODWILL**

The excess of the cost of the investments in subsidiaries and joint ventures over the share of the net assets acquired is recorded as consolidated goodwill and amortized on a straight-line basis over a period not exceeding 40 years. Each year, Hydro-Québec reviews the book value of goodwill to determine if there has been a permanent impairment in value by measuring the estimated fair value of the investments using the discounted cash flow method.

**REGULATION**

Under the *Act respecting the Régie de l'énergie*, assented to on December 23, 1996, and amended on June 16, 2000, the Régie de l'énergie has exclusive jurisdiction to determine or modify the rates and conditions under which electricity is transmitted and distributed by Hydro-Québec.

The joint venture Noverco inc. wholly owns Gaz Métropolitain, inc., whose main subsidiary, Gaz Métropolitain and Company, Limited Partnership, is involved primarily in the distribution of natural gas by pipeline. Most aspects of its operations are monitored and controlled by the Régie de l'énergie. In exercising its authority, the Régie de l'énergie makes decisions that influence the adoption and use of certain accounting policies.

**REVENUE**

Revenue from sales of electricity is recorded on the basis of cyclical billings and also includes revenue accrued in respect of electricity delivered but as yet unbilled.

**FOREIGN CURRENCY TRANSLATION**

Revenue and expenditure resulting from transactions in foreign currencies are translated into the Canadian dollar equivalent at exchange rates in effect at the transaction date. Monetary assets and liabilities are translated into Canadian dollars at exchange rates in effect at the balance sheet date, and non-monetary items are translated into Canadian dollars at exchange rates in effect at the transaction date.

The exchange gains or losses resulting from the translation of current monetary items are included in the consolidated statement of operations. Those resulting from the translation of long-term monetary items are deferred and amortized on a straight-line basis over the remaining term of the asset or liability, except when they relate to liabilities hedged by future revenue streams in United States dollars, in which case they are deferred until the date of repayment of such liabilities.

**> note 1. significant accounting policies (continued)**

Currency swaps used to manage exchange risk related to the repayment of the principal amount of long-term debt are presented at rates in effect at the balance sheet date. Those that constitute financial assets are presented as Financial assets related to debt, while those representing financial liabilities are presented as Long-term debt. Gains or losses on these currency swaps are deferred and amortized on a straight-line basis over their remaining terms.

#### FIXED ASSETS

Fixed assets are carried at cost, which comprises materials, labor, other costs directly contributing to construction activities and borrowing costs capitalized during construction. Capitalized borrowing costs are based on the previous year's average cost of long-term debt issued by the Corporation.

The costs of fixed assets in progress are transferred to fixed assets in service when construction is completed and the facilities are in commercial operation. As for generating facilities, the costs are transferred in installments as generating units of the facilities are completed and commissioned.

Fixed assets are depreciated over their useful life. Under the *Hydro-Québec Act*, the depreciation period is restricted to a maximum of 50 years. The depreciation periods for the main classes of fixed assets are as follows:

| | |
|---|---|
| Hydraulic generation | 45 to 50 years |
| Nuclear generation | 25 to 30 years |
| Thermal generation, other than nuclear | 15 to 30 years |
| Transmission | 30 to 50 years |
| Distribution | 25 to 40 years |
| Administrative and service buildings | 50 years |
| Construction, operating and research equipment | 3 to 30 years |

Fixed assets are depreciated according to the sinking fund method at the rate of 3%, with the exception of construction, operating and research equipment, which is depreciated according to the straight-line method.

Upon disposal, the cost of fixed assets and the cost of their dismantlement, net of accumulated depreciation and salvage value, are charged to a separate account and amortized over a maximum period of 10 years, according to the sinking fund method, at the rate of 3%. However, when the fixed assets are replaced, the cost of dismantlement, less the salvage value, is added to the cost of the new fixed assets and then depreciated according to the method appropriate to the new asset.

#### SHORT-TERM INVESTMENTS

Short-term investments are shown at amortized cost. The book value of the investments approximates their fair value.

#### DEFERRED CHARGES

**Marketing programs and development expenses**

Deferred charges related to marketing programs and deferred development expenses are amortized on a straight-line basis over a maximum of five years after the year in which they were incurred.

**Cancellation or postponement of major projects**

Project costs are reviewed periodically. Costs deemed irretrievable at the time of cancellation of a major project or its postponement to a later date are deferred and amortized on a straight-line basis over a period of three years.

**> note 1. significant accounting policies (continued)**

**PERSONNEL REDUCTION AND RENEWAL MEASURES**

The Corporation introduced various temporary measures to facilitate the reduction and renewal of its personnel from 1997 to 2000. The most significant of these measures were improvements to the Pension Plan and severance pay. The cost of measures relating to the Pension Plan is included in the accrued benefit obligation of the Pension Plan, while the cost of severance pay is presented as Deferred charges. The cost of these measures is amortized on a straight-line basis over a period of 60 months, beginning the month following each individual commitment. The amortization is recorded in Expenditure – Operations.

**SINKING FUNDS**

Sinking funds are created through the purchase of the Corporation's debentures, Government of Canada bonds, or bonds issued or guaranteed by the Québec government. The Corporation's debentures are deducted from long-term debt. Government issued or guaranteed bonds are presented as Financial assets related to debt.

Sinking fund securities are carried at unamortized cost, a method whereby the difference between the cost and the par value at maturity is amortized over the remaining term of the security. The book value of the securities does not necessarily approximate their fair value.

**DERIVATIVE INSTRUMENTS**

Hydro-Québec uses various derivative instruments to mitigate foreign exchange and interest rate risk related to long-term debt, as well as risk of changes in energy and raw material prices.

Interest exchanges, which arise from swap agreements used to change long-term interest rate exposure, are matched to interest expense on the borrowings to which they are related.

Derivative instruments used in the short term to manage financial risk over a period of no more than three years are recorded at cost. Gains or losses realized are deferred and charged to operations on a basis consistent with the recognition of the gains or losses of the underlying position.

The instruments used to manage risks related to energy-price fluctuations constitute hedges. Gains or losses related to these instruments are deferred and charged to operations on a basis consistent with the recognition of the gains or losses of the underlying position.

**DECOMMISSIONING OF NUCLEAR GENERATING STATION**

The future costs of decommissioning Gentilly-2 nuclear generating station are charged progressively to operations and reflected in Other long-term liabilities. These estimated costs essentially relate to dismantling of the station and removal of the irradiated fuel.

The Corporation revises these costs periodically based on the various assumptions and estimates underlying the calculations, possible technological advances and changes in the standards and regulations governing the decommissioning of nuclear generating stations.

**USE OF ESTIMATES**

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires Management to make estimates and assumptions which affect the amounts reported in the financial statements. Actual amounts could differ from those estimates.

**RECLASSIFICATION**

Some figures of the previous year have been reclassified in order to respect the presentation adopted in the current year.

## > note 2. depreciation, amortization and decommissioning

| | 2000 | 1999 |
|---|---|---|
| Depreciation of fixed assets | **1,587** | 1,538 |
| Amortization of marketing programs | **67** | 58 |
| Amortization of major projects canceled or postponed | **43** | 44 |
| Amortization of development expenses | **33** | 29 |
| Write-off of projects | **81** | 7 |
| Decommissioning of nuclear generating station | **12** | 10 |
| Other | **73** | 45 |
| | **1,896** | 1,731 |

## > note 3. taxes

| | 2000 | 1999 |
|---|---|---|
| Capital tax | **243** | 320 |
| Tax on gross revenue as municipal real estate tax on certain immovables | **218** | 211 |
| Municipal, school and other taxes | **64** | 61 |
| | **525** | 592 |

## > note 4. financial expenses

| | 2000 | 1999 |
|---|---|---|
| **Interest** | | |
| Interest on debt securities | **3,231** | 3,177 |
| Amortization of borrowing discount and expenses | **58** | 54 |
| | **3,289** | 3,231 |
| Less | | |
| Capitalized borrowing costs | **239** | 198 |
| Net investment income | **42** | 19 |
| | **281** | 217 |
| | **3,008** | 3,014 |
| **Exchange loss** | **174** | 134 |
| **Loan guarantee fees** | **187** | 197 |
| | **3,369** | 3,345 |

## > note 5. fixed assets

**2000**

| | In service | Accumulated depreciation | In progress | Total |
|---|---|---|---|---|
| **Generation** | | | | |
| Hydraulic | 24,082 | 5,106 | 2,472 | **21,448** |
| Nuclear | 1,638 | 724 | 11 | **925** |
| Thermal, other than nuclear | 1,091 | 566 | 76 | **601** |
| | 26,811 | 6,396 | 2,559 | **22,974** |
| **Transmission** | 19,418 | 4,099 | 925 | **16,244** |
| **Distribution** | 9,640 | 2,711 | 255 | **7,184** |
| **Other** | | | | |
| Administrative and service buildings | 1,720 | 421 | 10 | **1,309** |
| Construction, operating and research equipment | 1,926 | 1,336 | 130 | **720** |
| Sundry | 1,880 | 797 | 126 | **1,209** |
| | 5,526 | 2,554 | 266 | **3,238** |
| | 61,395 | 15,760 | 4,005 | **49,640** |

1999

| | In service | Accumulated depreciation | In progress | Total |
|---|---|---|---|---|
| **Generation** | | | | |
| Hydraulic | 23,743 | 4,693 | 2,302 | 21,352 |
| Nuclear | 1,630 | 655 | 15 | 990 |
| Thermal, other than nuclear | 1,121 | 552 | 26 | 595 |
| | 26,494 | 5,900 | 2,343 | 22,937 |
| **Transmission** | 17,732 | 3,736 | 916 | 14,912 |
| **Distribution** | 9,304 | 2,441 | 220 | 7,083 |
| **Other** | | | | |
| Administrative and service buildings | 1,731 | 377 | 7 | 1,361 |
| Construction, operating and research equipment | 1,877 | 1,191 | 100 | 786 |
| Sundry | 1,632 | 648 | 163 | 1,147 |
| | 5,240 | 2,216 | 270 | 3,294 |
| | 58,770 | 14,293 | 3,749 | 48,226 |

**> note 5. fixed assets (continued)**

As at December 31, 2000, the Corporation had cumulative costs related to suspended draft-design projects amounting to $509 million ($553 million as at December 31, 1999), recorded under Fixed assets in progress. The Corporation has therefore ceased capitalizing the related borrowing expenses.

As certain projects have longer completion timelines, their cumulative costs are periodically reviewed.

During such reviews, Management must use estimates and make assumptions that have an impact on the amounts reported for draft-design projects at the balance sheet date. Such projects are assessed in terms of profitability based on prevailing market conditions at the time of their commissioning, compliance with sustainable development principles and how well local communities receive them. A significant change in the assessment of these criteria could result in a reduction of the balance for draft-design projects.

## > note 6. investments

| | **2000** | 1999 |
|---|---|---|
| **At cost** | | |
| Noverco inc. (note 14) | | |
| Notes[a] | **141** | 141 |
| Churchill Falls (Labrador) Corporation Limited (note 19) | | |
| Bonds[b] | **59** | 61 |
| Other[c] | **181** | 152 |
| | **381** | 354 |
| **At equity** | | |
| Enbridge Inc. | **207** | 193 |
| Churchill Falls (Labrador) Corporation Limited (note 19) | **35** | 33 |
| Connexim, Limited Partnership | **41** | 40 |
| Meiya Power Company Limited | **86** | 82 |
| | **369** | 348 |
| | **750** | 702 |

*a) Subordinate debentures, interest rate based on the annual average rate of Government of Canada bonds with terms of over 10 years plus 4.45%, due in 2031, redeemable.*

*b) General mortgage, 7½ %, due 2001 through 2010 (par value of $65 million in 2000 and $67 million in 1999).*

*c) Comprises venture capital investments at a cost of $90 million and with a fair value of $143 million as at December 31, 2000 ($48 million and $48 million as at December 31, 1999). The fair value of listed shares is determined based on the weighted average trading price as at December 31, 2000; the fair value of unlisted shares is cost.*

## > note 7. deferred charges

| | 2000 | 1999 |
|---|---|---|
| Deferred charges related to debt[a] | **3,191** | 2,634 |
| Employee future benefit asset (note 18) | **545** | 466 |
| Marketing programs | **49** | 100 |
| Development expenses | **91** | 109 |
| Major projects canceled or postponed | **44** | 87 |
| Personnel reduction and renewal measures | **117** | 151 |
| Other | **272** | 327 |
| | **4,309** | 3,874 |

*a) Mainly comprises a deferred exchange loss of $3,063 million ($2,517 million as at December 31, 1999).*

## > note 8. financial assets related to debt

| | 2000 | 1999 |
|---|---|---|
| Currency swaps | **232** | 378 |
| Sinking funds | **229** | 231 |
| | **461** | 609 |
| Less | | |
| Current portion | **89** | 191 |
| | **372** | 418 |

## > note 9. other assets

| | 2000 | 1999 |
|---|---|---|
| Goodwill | **557** | 291 |
| Government reimbursement for the 1998 ice storm[a] | **380** | 390 |
| | **937** | 681 |

*a) Corresponds to the reimbursement of the cost of emergency measures, an amount of $186 million, receivable in 2002, and the compensation payments, from 2002 to 2007, for the net cost of restoring the system, an amount of $194 million ($186 million and $204 million, respectively, as at December 31, 1999).*

## > note 10. long-term debt

**COMPOSITION AND MATURITIES**

Debentures, other long-term debt and currency swaps representing financial liabilities, translated into Canadian dollars at the exchange rates in effect at the balance sheet date, are summarized in the following table. These amounts are presented by year of maturity, and take into account the requirements of the sinking funds.

| | | | | | | **2000** | 1999 |
|---|---|---|---|---|---|---|---|
| | | | | Debt of the Corporation | | | |
| Years of maturity | Canadian dollars | U.S. dollars | Other currencies | Total | Subsidiaries and joint ventures | Total | Total |
| 2000 | — | — | — | — | — | **—** | 2,598 |
| 2001 | 1,682 | 679 | 1,112 | 3,473 | 11 | **3,484** | 3,492 |
| 2002 | 535 | 1,942 | 430 | 2,907 | 104 | **3,011** | 2,827 |
| 2003 | 1,218 | 1,101 | 276 | 2,595 | 296 | **2,891** | 2,633 |
| 2004 | 1,142 | 3 | 52 | 1,197 | 6 | **1,203** | 1,154 |
| 2005 | 1,328 | 617 | 166 | 2,111 | 191 | **2,302** | — |
| 1 to 5 years | 5,905 | 4,342 | 2,036 | 12,283 | 608 | **12,891** | 12,704 |
| 6 to 10 years | 1,607 | 1,846 | 1,531 | 4,984 | 268 | **5,252** | 7,217 |
| 11 to 15 years | 2,514 | 1,840 | 586 | 4,940 | 22 | **4,962** | 3,761 |
| 16 to 20 years | 1,613 | 990 | 99 | 2,702 | 66 | **2,768** | 1,664 |
| 21 to 25 years | 3,057 | 3,045 | — | 6,102 | 50 | **6,152** | 7,402 |
| 26 to 30 years | 86 | 3,761 | — | 3,847 | 33 | **3,880** | 2,352 |
| 31 to 35 years | 2,171 | — | — | 2,171 | — | **2,171** | 2,484 |
| 36 to 40 years | 209 | — | — | 209 | — | **209** | 844 |
| 41 to 45 years | 4 | — | — | 4 | — | **4** | 181 |
| 46 to 50 years | 50 | — | — | 50 | — | **50** | — |
| 56 to 60 years | 32 | — | — | 32 | — | **32** | — |
| | 17,248 [a] | 15,824 | 4,252 | 37,324 | 1,047 | **38,371** | 38,609 |
| Less | | | | | | | |
| Current portion | 1,682 | 679 | 1,112 | 3,473 | 11 | **3,484** | 2,598 |
| | 15,566 | 15,145 | 3,140 | 33,851 | 1,036 | **34,887** | 36,011 |

*a) Includes $101 million and $225 million in zero-coupon bonds, reported at their discounted value at an interest rate compounded semiannually of 10.95% and 10.67% respectively. Their par value will reach $282 million and $1,729 million in 2010 and 2020 respectively. Other bonds, reported at their discounted value and amounting to $864 million, will reach a par value of $1,122 million on maturity.*

The debentures of the Corporation are guaranteed by the Québec government. Other long-term debt of the Corporation, which is not guaranteed by the government, totaled $223 million as at December 31, 2000 ($231 million as at December 31, 1999).

**> note 10. long-term debt (continued)**

**ALLOCATION OF DEBT BY CURRENCY AT TIME OF ISSUE AND IMPACT OF FINANCIAL ASSETS RELATED TO DEBT**

The following table summarizes long-term debt, including the current portion, in Canadian dollars and currency units. Also shown are the effects of currency swaps and sinking funds allocated to repay debt, which are presented on the balance sheet under Financial assets related to debt.



| | | | | **2000** | 1999 |
|---|---|---|---|---|---|
| | | Long-term debt | Financial assets related to debt | | |
| | In Canadian dollars and currency units | At the closing exchange rates at the balance sheet date[a] | Currency swaps and sinking funds | Total | Total |
| **Debt of the Corporation** | | | | | |
| Canadian dollars | 17,248 | 17,248 | — | **17,248** | 16,662 |
| U.S. dollars[b] | 10,595 | 15,824 | (290) | **15,534** | 15,590 |
| Other currencies[c] | | | | | |
| Japanese yen | 65,500 | 966 | (84) | **882** | 975 |
| Deutsche marks | 1,574 | 1,377 | (60) | **1,317** | 1,627 |
| Pounds sterling | 400 | 1,009 | (10) | **999** | 986 |
| Swiss francs | 247 | 246 | (17) | **229** | 535 |
| French francs | 2,500 | 654 | — | **654** | 629 |
| Belgian francs | — | — | — | **—** | 43 |
| | | 4,252 | (171) | **4,081** | 4,795 |
| | | 37,324 | (461) | **36,863** | 37,047 |
| **Subsidiaries and joint ventures**[d] | | 1,047 | — | **1,047** | 953 |
| | | 38,371 | (461) | **37,910** | 38,000 |

*a) Includes $765 million of financial liabilities composed of currency swaps ($540 million as at December 31, 1999).*

*b) These balances are 77% hedged by future revenue streams in U.S. dollars and 1% by currency swaps (77% and 2% as at December 31, 1999).*

*c) These balances are 43% hedged by currency swaps that translate the balances into Canadian dollars and 50% hedged by currency swaps that translate the balances into U.S. dollars (53% and 41%, respectively, as at December 31, 1999).*

*d) Comprises $809 million issued in Canadian dollars, $236 million in U.S. dollars and $2 million in other currencies ($744 million in Canadian dollars, $154 million in U.S. dollars, $18 million in Australian dollars and $37 million in Senegalese francs as at December 31, 1999).*

**> note 10. long-term debt (continued)**

**ALLOCATION OF DEBT BY CURRENCY AT TIME OF ISSUE AND AT TIME OF REPAYMENT**

The following table shows the allocation of debt, net of sinking funds, converted into Canadian dollars after taking swaps into account, according to the currency at time of issue and the currency at time of repayment.

| | 2000 | | 1999 | |
|---|---|---|---|---|
| | At time of issue | At time of repayment | At time of issue | At time of repayment |
| **Debt of the Corporation** | | | | |
| Canadian dollars | **17,248** | **17,477** | 16,662 | 17,881 |
| U.S. dollars | **15,534** | **19,099** | 15,590 | 18,869 |
| Other currencies | **4,081** | **287** | 4,795 | 297 |
| | **36,863** | **36,863** | 37,047 | 37,047 |
| **Debt of the subsidiaries and joint ventures** | | | | |
| Canadian dollars | **809** | **809** | 744 | 762 |
| U.S. dollars | **236** | **236** | 154 | 154 |
| Other currencies | **2** | **2** | 55 | 37 |
| | **1,047** | **1,047** | 953 | 953 |
| | **37,910** | **37,910** | 38,000 | 38,000 |

**INTEREST RATES**

The Hydro-Québec interest rates presented in the following table take into account nominal interest rates on borrowings, the related discounts and expenses, and the effect of interest rate swaps.

| | | | | 2000 | 1999 |
|---|---|---|---|---|---|
| Years of maturity | Canadian dollars | U.S. dollars | Other currencies | Weighted average | Weighted average |
| 1 to 5 years | 6.32 | 8.11 | 8.30 | **7.08** | 7.30 |
| 6 to 10 years | 7.00 | 8.86 | 6.30 | **7.37** | 6.89 |
| 11 to 15 years | 9.31 | 9.96 | 10.54 | **9.72** | 10.30 |
| 16 to 20 years | 11.25 | 8.67 | 6.08 | **10.24** | 7.51 |
| 21 to 25 years | 10.29 | 9.25 | — | **9.78** | 10.14 |
| 26 to 30 years | 6.31 | 9.11 | — | **9.03** | 8.62 |
| 31 to 35 years | 6.51 | — | — | **6.51** | 8.54 |
| 36 to 40 years | 6.43 | — | — | **6.43** | 5.83 |
| 41 to 45 years | 6.29 | — | — | **6.29** | 6.41 |
| 46 to 50 years | 6.45 | — | — | **6.45** | — |
| 56 to 60 years | 6.33 | — | — | **6.33** | — |
| Weighted average | 8.65 | 9.13 | 7.88 | **8.82** | 8.71 |

The variable-rate portion of Hydro-Québec's debt amounted to 25.2%, or 26.3% after perpetual debt, as at December 31, 2000 (25.1%, or 26.2% after perpetual debt, as at December 31, 1999). For information purposes, a change of 1% in the interest rate would change net income by $101 million ($100 million in 1999), not including the impact of derivative instruments used to manage short-term financial risk (note 13).

**> note 10. long-term debt (continued)**

**FAIR VALUE**

As at December 31, 2000, the fair value of Hydro-Québec's debt, net of sinking funds and after swaps, amounted to $45,019 million ($43,721 million as at December 31, 1999).



Fair value is obtained by discounting future cash flows, based on term and closing interest rates as at the balance sheet date for similar instruments available on financial markets. The fluctuation in the fair value is explained by its sensitivity to interest rates on such markets. However, Management intends to retain these debt securities until maturity. Therefore, as at December 31, 2000, Hydro-Québec did not foresee any significant debt repayments that could result in the realization of this fair value.

Hydro-Québec has undrawn revolving standby credits totaling US$1,800 million and expiring between 2001 and 2003. Any borrowing under these lines of credit will bear interest at a rate based on the Eurodollar London Interbank Offered Rate (LIBOR).

## > note 11. other long-term liabilities

| | **2000** | 1999 |
|---|---|---|
| Accounts payable | **275** | 324 |
| Employee future benefit liability (note 18) | **311** | 272 |
| Decommissioning of nuclear generating station | **87** | 75 |
| | **673** | 671 |

## > note 12. perpetual debt

Perpetual notes in the amount of US$400 million bear interest at a rate established semiannually based on LIBOR. They are guaranteed by the Québec government and are only redeemable at the Corporation's option. These notes are shown on the balance sheet at the exchange rate in effect on the date of issue ($600 million at the exchange rate in effect at the balance sheet date). As at December 31, 2000, their fair value was $520 million ($592 million as at December 31, 1999). As at December 31, 2000 and 1999, the LIBOR for perpetual notes was 6.88% and 6.06%, respectively.

## > note 13. derivative instruments

Derivative instruments used by Hydro-Québec are always associated with a reverse risk position.

Hydro-Québec concludes currency swaps in order to manage the foreign exchange risk associated with repayments of principal on long-term debt and with interest payments. Some of these currency swaps allow for interest rate exchanges to change long-term exposure to interest rate risk. Interest rate swaps that do not allow for exchanges of principal are also used to manage this risk.

The valuation of these swaps, with terms through 2017, shows a negative fair value of $318 million (positive fair value of $71 million as at December 31, 1999).

The following table shows the notional amount of these swaps, expressed in Canadian dollars or other currencies.

| | **2000** | 1999 |
|---|---|---|
| **Canadian dollars** | **(698)** | (1,676) |
| **U.S. dollars** | **(2,136)** | (1,962) |
| **Other currencies** | | |
| Japanese yen | **65,500** | 75,500 |
| Deutsche marks | **1,456** | 1,956 |
| Pounds sterling | **310** | 310 |
| Swiss francs | **247** | 547 |
| French francs | **2,500** | 2,500 |
| Belgian francs | **—** | 1,000 |
| Australian dollars | **—** | 19 |

Data in brackets represent amounts to be paid.

**> note 13. derivative instruments (continued)**

In managing short-term financial risks, Hydro-Québec assesses the overall impact of variations in exchange rates, interest rates and prices of raw materials on an ongoing basis. Hydro-Québec held options and forward contracts designed to hedge several positions. It also uses derivative instruments to manage market risks resulting from fluctuations in energy prices. The fair value of these instruments is presented by specific risk in the following table. These derivative instruments mature through April 2002.

The fair value of derivative instruments reflects the amount that Hydro-Québec would receive (*financial assets*) or pay (*financial liabilities*) as at the balance sheet date in terminating these instruments.

| | **2000** | 1999 |
|---|---|---|
| **Exchange risk** | | |
| Forward exchange contracts and options | | |
| Financial assets | **39** | 1 |
| Financial liabilities | **(43)** | (50) |
| | **(4)** | (49) |
| **Interest rate risk** | | |
| Forward rate agreements, options and swaps | | |
| Financial assets | **1** | 14 |
| Financial liabilities | **—** | (2) |
| | **1** | 12 |
| **Risk of change in energy and raw material prices** | | |
| Forward contracts, swaps and transmission congestion contracts | | |
| Financial assets | **47** | 1 |
| Financial liabilities | **(21)** | (34) |
| | **26** | (33) |
| | **23** | (70) |

The fair value of derivative instruments is based on the spot rates or forward rates or prices in effect at market closing as at the balance sheet date. Without this information for a given instrument, Management refers to the available forward rate or price for an equivalent instrument. Different valuation models recognized by financial markets are used to estimate the fair value of options.

**CREDIT RISK**

Derivative instruments include an element of risk, since a counterparty might not meet its obligations. However, this risk is moderate as Hydro-Québec deals only with Canadian and international financial institutions with high credit ratings. Credit risk exposure is also reduced by applying a credit policy limiting credit risk concentrations and a customer credit risk evaluation program, as well as by adopting credit limits, where necessary. As at December 31, 2000, Hydro-Québec does not foresee any loss arising from counterparty default.

## > note 14. interests in joint ventures

The share of the principal joint venture items included in the consolidated financial statements is presented in the following table. These joint ventures include the interest in Noverco inc. and the Corporation's interests in various foreign joint ventures through Hydro-Québec International inc. (HQI).

| | **2000** | 1999 |
|---|---|---|
| **Operations** | | |
| Revenue | **873** | 728 |
| Expenditure and financial expenses | **807** | 645 |
| Non-controlling interest | **18** | 17 |
| *Net income* | **48** | 66 |
| **Balance sheet** | | |
| Current assets | **191** | 147 |
| Long-term assets | **1,687** | 1,539 |
| Current liabilities | **256** | 226 |
| Long-term liabilities | **1,028** | 872 |
| Non-controlling interest | **180** | 182 |
| *Net assets* | **414** | 406 |
| **Cash flows** | | |
| Operating activities | **101** | 115 |
| Investing activities | **(144)** | (387) |
| Financing activities | **63** | 190 |
| *Net change in cash and cash equivalents* | **20** | (82) |

#### NOVERCO INC.

Hydro-Québec holds 41% of the outstanding common shares of Noverco inc. and options on an additional 9%. Under the Noverco inc. shareholders' agreement, the Corporation agreed to mechanisms enabling the joint owners to convert their interests into liquidities under certain conditions.

Noverco inc., through its interest in Gaz Métropolitain and Company, Limited Partnership (GMCLP), has unrecorded deferred income taxes on regulated activities of $141 million in 2000 ($145 million in 1999). The Régie de l'énergie and the National Energy Board are expected to allow these deferred income taxes to be included in GMCLP's rates as they become payable.

#### FOREIGN JOINT VENTURES

The Corporation holds interests in joint ventures through HQI. These joint ventures are essentially involved in the construction, ownership and operation of hydroelectric generating stations and transmission systems. They mainly operate in South and Central America, as well as in Australia.

A contract for the sale of Senelec's shares, which takes effect in 2001, was signed on December 29, 2000. As at December 31, 2000, the investment in Senelec is reflected in short-term investments at its fair value of $49 million. Before this transaction, it was recorded using the proportionate consolidation method (cost of $64 million).

## > note 15. business acquisition



On October 23, 2000, the Corporation, through HQI, acquired the aggregate of the outstanding common shares of Compañía Nacional de Transmisión Eléctrica S.A. (Transelec), a major Chilean power transmission company. The purchase, at a cost of $1,631 million, was financed through a short-term loan for which long-term financing may be secured at a later date. The acquisition was recorded using the purchase method.

The fair value of the assets acquired and liabilities assumed are as follows:

| | |
|---|---|
| Cash | 50 |
| Current assets | 13 |
| Long-term assets | 1,282 |
| | **1,345** |
| Current liabilities | (14) |
| Long-term liabilities | (23) |
| Net assets | **1,308** |
| Goodwill | 323 |
| Purchase price | **1,631** |
| Consideration comprises: | |
| Cash, net of cash acquired | 1,576 |
| Other | 5 |
| | **1,581** |

As at December 31, 2000, no results had been recorded, pursuant to Hydro-Québec's practice of consolidating international interests on a quarter lag basis.

## > note 16. shareholder's equity

The authorized share capital comprises 50,000,000 shares with a par value of $100 each, and 43,741,090 shares were issued and paid.

Under the *Hydro-Québec Act*, any dividends to be paid by the Corporation are declared once a year by the Québec government, which also determines the terms and conditions of payment. For a given fiscal year, they cannot exceed the distributable surplus, equal to 75% of the year's operating income and the net investment income, less interest on debt securities and amortization of borrowing discount and expenses. This calculation is made on the basis of the consolidated financial statements.

However, in respect of a given fiscal year, no dividend may be declared in an amount that would have the effect of reducing the rate of capitalization to less than 25% at the end of the year. The government declares the dividends for a given year within 30 days after the Corporation has sent the government the financial data relative to the distributable surplus. On expiry of the time prescribed, any distributable surplus or part thereof that has not been subject to a dividend declaration may no longer be distributed to the shareholder as a dividend.

For 2000, the Québec government declared dividends of $539 million, which is less than the maximum permitted.

Dividends declared are deducted from the retained earnings of the year for which they were declared.

## > note 17. change in non-cash working capital items

| | 2000 | 1999 |
|---|---|---|
| Accounts receivable | **30** | (49) |
| Materials, fuel and supplies | **(24)** | (111) |
| Accounts payable | **96** | 397 |
| Accrued interest | **(13)** | (132) |
| | **89** | 105 |

## > note 18. employee future benefits

The Corporation offers all its employees a contributory defined benefit pension plan, based on final pay. The Corporation's pension plan (the "Pension Plan") is a funded plan that ensures post-retirement benefits based on number of years of service and average five best years of earnings. The Corporation also offers its active and retired employees other employee benefits including group life, medical and hospitalization, and salary insurance plans. However, with the exception of the long-term disability salary insurance plan, for which amounts are set aside with the insurer to guarantee benefit payments to beneficiaries, these plans are unfunded.

The cost of pension benefits and other retirement benefits provided in exchange for services rendered during the year is calculated using the projected benefit method prorated on years of service, and is based on best estimate economic and demographic assumptions as determined by Management.

The following tables present information concerning the defined benefit plans, established by independent actuaries:

| | 2000 | 1999 | 2000 | 1999 |
|---|---|---|---|---|
| | | Pension Plan | | Other plans |
| **Accrued benefit obligation** | | | | |
| *Balance at beginning of year* | 5,988 | 5,938 | 460 | 499 |
| Current service cost | 171 | 166 | 16 | 18 |
| Benefit payments and refunds | (322) | (367) | (26) | (24) |
| Interest on obligation | 436 | 353 | 32 | 29 |
| Actuarial losses (gains) | 647 | (439) | 40 | (62) |
| Adjustments arising from plan amendments | — | 306 | — | — |
| Adjustments arising from personnel reduction programs | 46 | 31 | — | — |
| *Balance at end of year* | **6,966** | 5,988 | **522** | 460 |

**> note 18. employee future benefits (continued)**

| | 2000 | 1999 | 2000 | 1999 |
|---|---|---|---|---|
| | | Pension Plan | | Other plans |
| **Plan assets at fair value** | | | | |
| *Balance at beginning of year* | 8,958 | 8,304 | 31 | 29 |
| Actual return on plan assets during the year | 831 | 1,006 | — | 1 |
| Employee contributions | 3 | 19 | — | — |
| Hydro-Québec contributions | 1 | 14 | 4 | 4 |
| Benefit payments and refunds | (322) | (367) | (4) | (3) |
| Administrative fees | (19) | (18) | — | — |
| *Balance at end of year* | **9,452** | 8,958 | **31** | 31 |
| **Surplus (deficit) at end of year** | **2,486** | 2,970 | **(491)** | (429) |
| Unamortized past service costs[a] | 278 | 300 | — | — |
| Unamortized net gain[b] | (428) | (905) | (19) | (62) |
| Unamortized transitional obligation (asset)[a] | (1,977) | (2,129) | 193 | 209 |
| Unamortized adjustments arising from personnel reduction programs[c] | 186 | 230 | 6 | 10 |
| **Accrued benefit asset (liability)** | **545** | 466 | **(311)** | (272) |
| **Significant actuarial assumptions (%)** | | | | |
| Discount rate | 6.61 | 7.17 | 6.61 | 7.17 |
| Expected rate of return on plan assets[d] | 7.90 | 6.49 | 5.59 | 5.30 |
| Salary escalation rate[e] | 2.95 | 2.23 | — | — |

As at December 31, 2000, health-care costs are based on an annual growth rate of 7.5% in 2001 and 7.1% in 2002. After that time, based on the assumption used, this rate gradually decreases until it reaches the ultimate rate of 3.7% in 2010.

*a) Past service costs arising from plan amendments and transitional balances relating to the Pension Plan and other defined retirement benefits as at January 1, 1999 are amortized on a straight-line basis over the employees' expected average remaining service life. The transitional obligation relating to salary insurance plans is amortized on a straight-line basis over a period of five years.*

*b) Amortization of actuarial gains or losses is recognized in the expense for the year if the unamortized net actuarial gain or loss at the beginning of the year exceeds 10% of the value of the accrued benefit obligation or 10% of the market-related value of the assets of the plan fund, whichever is greater. Amortization corresponds to the excess divided by employees' expected average remaining service life.*

*c) Adjustments arising from personnel reduction programs are amortized on a straight-line basis over a period of 60 months, beginning the month following each individual commitment.*

*d) The expected return on pension plan assets is based on a market-related value determined by using a five-year moving average for equity securities held, and by valuing other asset classes at their fair value.*

*e) This rate is a weighted average which takes salary increases into account as well as promotion opportunities while in service.*

**> note 18. employee future benefits (continued)**

The plan assets include certain securities issued by the Corporation and its related companies. These securities are grouped under the following asset classes:

| | **2000** | 1999 | **2000** | 1999 |
|---|---|---|---|---|
| | | Pension Plan | | Other plans |
| Bonds and debentures | 742 | 532 | — | — |
| Shares | 10 | 17 | — | — |
| Short-term investments | 20 | 10 | 31 | 30 |
| | **772** | 559 | **31** | 30 |
| **Plan expense (credit)** | | | | |
| Current service cost, net of employee contributions[a] | 157 | 136 | 16 | 18 |
| Administrative fees[b] | 19 | 18 | — | — |
| Interest on obligation | 436 | 353 | 33 | 29 |
| Interest on assets | (650) | (529) | (1) | (1) |
| Amortization of transitional obligation (asset) | (152) | (152) | 16 | 16 |
| Amortization of net actuarial gain | — | — | (1) | — |
| Amortization of adjustments arising from personnel reduction programs | 90 | 82 | 4 | 3 |
| Amortization of past service costs | 22 | 6 | — | — |
| **Expense (credit) for the year** | **(78)** | (86) | **67** | 65 |

*a) The value of the contribution holiday granted to employees for the year is disclosed net of service cost of contributions deemed paid and amortized using the method for amortizing actuarial gains and losses. For the long-term disability insurance plan, current service cost corresponds to the cost of new disability cases for the year.*

*b) Administrative fees chargeable to the Pension Plan are fully billed by the Corporation.*

The Corporation and most of its employees have benefited from a Pension Plan contribution holiday since May 10, 1999. Several amendments with a material effect on the obligation of the Pension Plan were also the subject of agreements between the Corporation and the unions during 1999. These amendments are mainly improvements to retirement benefits, including the extension of the "80 clause" to 2003, where 80 is the total of *age and years of contribution*, the introduction of a bridging benefit calculated on service up to 2003 and payable as of the date of retirement up to age 65, the buyback of non-contribution periods up to a maximum of $50 million, and the inclusion of lump sums paid under the profit-sharing plan or certain corporate performance management programs in the definition of pensionable earnings.

## > note 19. commitments and contingent liabilities



**ELECTRICITY PURCHASED**

On May 12, 1969, the Corporation signed a contract with Churchill Falls (Labrador) Corporation Limited (CF(L)Co) whereby the Corporation undertook to purchase substantially all the energy generated at Churchill Falls generating station, which has a nominal capacity of 5,428 MW. Under this agreement, the Corporation could be required to provide additional funding to service the debt of CF(L)Co and to pay its expenses should CF(L)Co be unable to do so. Expiring in 2016, this contract will be automatically renewed for a further 25 years in accordance with existing terms and conditions. On June 18, 1999, the Corporation and CF(L)Co also entered into a contract to guarantee the availability of 682 MW of additional power until 2041 for the November 1 to March 31 winter period.

On May 28, 1990, the Corporation signed a firm power purchase contract with New Brunswick Power Corporation to provide the Corporation with blocks of power of up to 300 MW between 1998 and 2002, and 200 MW between 2002 and 2011.

On April 13, 1999, the Corporation signed an energy purchase agreement with PG&E Energy Trading-Power, L.P. for 2,850 GWh, to be delivered from 2001 until 2004.

As at December 31, 2000, the Corporation had signed contracts with 66 independent power producers for a potential capacity of 435 MW. The Corporation expects to purchase approximately 387 MW of power and energy annually over the initial term of these contracts, which extend through 2024. The majority of these contracts include renewal clauses.

**ENERGY STORAGE**

The Corporation entered into energy banking agreements for a potential of approximately 9 TWh. These agreements cover periods ranging from one to five years and extend through 2004. As at December 31, 2000, the Corporation received approximately 2 TWh which, under these agreements, must be returned. Certain provisions enable the Corporation and/or the counterparty to convert some energy banking contracts into energy purchase/sale contracts.

**GUARANTEES**

Hydro-Québec had issued letters of credit or guarantees for an amount of $2,371 million as at December 31, 2000.

**CAPITAL EXPENDITURES**

The Corporation expects to invest $1,920 million in fixed assets in 2001.

**LITIGATION**

In the normal course of business, Hydro-Québec is party to claims and legal proceedings. Management is of the opinion that the settlement of these legal actions, the outcome of which may be determined with a reasonable degree of certainty, will not have an adverse effect on the financial position or consolidated operating results of Hydro-Québec.

The Corporation also received claims for the 1998 ice storm. Management believes that it is too early to assess the potential impact of these claims on the Corporation's financial position.

## > note 20. segmented information

The activities of Hydro-Québec are divided into three energy-related operating segments, according to products and services: Electricity, Gas, and Expertise and Technology. These segments, based on management practices that support Hydro-Québec's growth and profitability orientations, have their own particular economic characteristics and differ in nature, production processes, and technology, as well as in their target customer base.

The Electricity segment is Hydro-Québec's core business and encompasses the generation, transmission and distribution of electricity.

The Gas segment comprises natural gas transmission and distribution activities, principally through an interest in Noverco inc. shares and debentures.

The Expertise and Technology segment groups together activities related to the marketing of technology and expertise developed both on the national and international stage. The information provided relates chiefly to the subsidiaries in these sectors, namely HQI, Hydro-Québec CapiTech and the holding companies Gestion Production H.Q. inc., TransÉnergie H.Q. inc. and Hydro-Québec Valtech inc.

The following tables contain information related to operations and assets by segment and certain geographical information.

**SEGMENTS**

**2000**

| | Energy | | | |
|---|---|---|---|---|
| | Electricity | Gas | Expertise and Technology | Intersegment eliminations for consolidation purposes | Total |
| Revenue | **10,417** | **924** | **97** | **(9)**[a] | **11,429** |
| Depreciation, amortization and decommissioning | **1,778** | **69** | **49** | **—** | **1,896** |
| Financial expenses | **3,263** | **93** | **13** | **—** | **3,369** |
| Net income (loss) | **1,174** | **(11)** | **(85)** | **—** | **1,078** |
| Capital expenditure | **1,766** | **43** | **3** | **—** | **1,812** |
| Total assets | **57,138** | **1,704** | **320** | **(51)** | **59,111** |

1999

| | Energy | | | |
|---|---|---|---|---|
| | Electricity | Gas | Expertise and Technology | Intersegment eliminations for consolidation purposes | Total |
| Revenue | 8,717 | 778 | 138 | (25)[a] | 9,608 |
| Depreciation, amortization and decommissioning | 1,641 | 61 | 29 | — | 1,731 |
| Financial expenses | 3,242 | 92 | 12 | (1) | 3,345 |
| Net income (loss) | 915 | 36 | (45) | — | 906 |
| Capital expenditure | 1,552 | 89 | 1 | — | 1,642 |
| Total assets | 54,855 | 1,636 | 392 | (47) | 56,836 |

*a) Corresponds to intersegment revenue derived essentially from Expertise and Technology.*

**> note 20. segmented information (continued)**

**GEOGRAPHICAL INFORMATION**

| | 2000 | | 1999 | |
|---|---|---|---|---|
| | Revenue | Fixed assets and goodwill | Revenue | Fixed assets and goodwill |
| Québec | **8,799** | **48,027** | 8,209 | 48,079 |
| Canada, outside Québec | **176** | **—** | 275 | — |
| United States | **2,331** | **226** | 974 | 107 |
| Chile | **—** | **1,605** | — | — |
| Other countries | **123** | **339** | 150 | 331 |
| | **11,429** | **50,197** | 9,608 | 48,517 |

The amounts presented for each segment are based on the financial information used to establish the consolidated financial statements.

## > consolidated financial information

| In millions of dollars | **2000** | 1999 | 1998 | 1997 | 1996 |
|---|---|---|---|---|---|
| **OPERATIONS** | | | | | |
| **Revenue** | **11,429** | 9,608 | 8,879 | 8,481 | 7,779 |
| **Expenditure** | | | | | |
| Operations | **2,135** | 1,912 | 1,681 | 1,724 | 1,619 |
| Electricity and fuel purchased | **2,408** | 1,109 | 899 | 529 | 275 |
| Depreciation, amortization and decommissioning | **1,896** | 1,731 | 1,589 | 1,545 | 1,427 |
| Taxes | **525** | 592 | 610 | 583 | 568 |
| | **6,964** | 5,344 | 4,779 | 4,381 | 3,889 |
| **Operating income** | **4,465** | 4,264 | 4,100 | 4,100 | 3,890 |
| Financial expenses | **3,369** | 3,345 | 3,410 | 3,308 | 3,370 |
| Income before non-controlling interest | **1,096** | 919 | 690 | 792 | 520 |
| Non-controlling interest | **18** | 13 | 11 | 6 | — |
| **Net income** | **1,078** | 906 | 679 | 786 | 520 |
| **SUMMARY OF BALANCE SHEET** | | | | | |
| Total assets | **59,111** | 56,836 | 57,336 | 55,238 | 53,760 |
| Long-term debt | **34,887** | 36,011 | 37,664 | 37,172 | 36,404 |
| Shareholder's equity | **14,280** | 13,741 | 13,288 | 12,888 | 12,459 |
| **ANNUAL INVESTMENTS** | | | | | |
| Fixed assets | **1,812** | 1,642 | 2,092 | 1,590 | 2,056 |
| Other | **1,678** | 456 | 234 | 527 | (9) |
| Total investments | **3,490** | 2,098 | 2,326 | 2,117 | 2,047 |
| **FINANCIAL RATIOS** | | | | | |
| Interest coverage[a] | **1.37** | 1.33 | 1.25 | 1.27 | 1.17 |
| Capitalization (%)[b] | **26.2** | 26.2 | 25.0 | 25.1 | 24.9 |
| Self-financing (%)[c] | **49.8** | 59.5 | 50.2 | 61.2 | 56.5 |
| Return on equity (%)[d] | **7.7** | 6.7 | 5.2 | 6.2 | 4.3 |
| Return on revenue (%)[e] | **9.4** | 9.4 | 7.6 | 9.3 | 6.7 |

*a) Sum of operating income and net investment income divided by gross interest expense.*
*b) Shareholder's equity divided by sum of shareholder's equity, long-term debt, perpetual debt, short-term borrowings and current portion of long-term debt, less financial assets related to debt.*
*c) Cash provided from operations less dividends paid, divided by sum of investments, maturity of long-term debt and sinking fund redemption.*
*d) Net income divided by average shareholder's equity.*
*e) Net income divided by revenue.*

*Note: Throughout the Supplementary Information section, certain figures for previous years have been reclassified to reflect the presentation of the current year.*

## > operating statistics–Electricity

| | 2000 | 1999 | 1998 | 1997 | 1996 |
|---|---|---|---|---|---|
| In millions of kilowatthours | | | | | |
| **ELECTRICITY SALES** | | | | | |
| In Québec | | | | | |
| Residential and farm | **51,666** | 49,315 | 47,701 | 51,246 | 50,294 |
| General and institutional | **30,490** | 29,765 | 28,815 | 29,560 | 29,158 |
| Industrial | **65,950** | 63,409 | 61,773 | 61,837 | 59,797 |
| Other | **4,651** | 4,500 | 4,519 | 4,648 | 5,261 |
| | **152,757** | 146,989 | 142,808 | 147,291 | 144,510 |
| Outside Québec | | | | | |
| Long-term sales | **6,844** | 8,711 | 8,101 | 8,072 | 7,819 |
| Short-term sales | **30,479** | 16,012 | 10,464 | 7,170 | 11,073 |
| | **37,323** | 24,723 | 18,565 | 15,242 | 18,892 |
| Total sales | **190,080** | 171,712 | 161,373 | 162,533 | 163,402 |
| In millions of dollars | | | | | |
| **REVENUE FROM SALES** | | | | | |
| In Québec | | | | | |
| Residential and farm | **3,167** | 3,034 | 2,906 | 3,066 | 2,945 |
| General and institutional | **2,002** | 1,963 | 1,894 | 1,885 | 1,835 |
| Industrial | **2,405** | 2,236 | 2,214 | 2,162 | 2,075 |
| Other | **220** | 215 | 213 | 218 | 226 |
| | **7,794** | 7,448 | 7,227 | 7,331 | 7,081 |
| Outside Québec | | | | | |
| Long-term sales | **377** | 427 | 391 | 350 | 292 |
| Short-term sales | **2,003** | 624 | 423 | 246 | 296 |
| | **2,380** | 1,051 | 814 | 596 | 588 |
| Total revenue from sales | **10,174** | 8,499 | 8,041 | 7,927 | 7,669 |
| At December 31 | | | | | |
| **NUMBER OF CUSTOMER ACCOUNTS** | | | | | |
| In Québec | | | | | |
| Residential and farm | **3,228,610** | 3,206,211 | 3,182,033 | 3,157,096 | 3,127,136 |
| General and institutional | **281,107** | 280,383 | 280,067 | 280,396 | 280,570 |
| Industrial | **13,081** | 12,732 | 12,803 | 13,002 | 13,198 |
| Other | **5,941** | 5,986 | 6,066 | 6,222 | 6,308 |
| Outside Québec | **86** | 88 | 61 | 52 | 48 |
| Total customer accounts | **3,528,825** | 3,505,400 | 3,481,030 | 3,456,768 | 3, 427,260 |
| In kilowatthours/customer | | | | | |
| **AVERAGE ANNUAL CONSUMPTION** | | | | | |
| In Québec | | | | | |
| Residential and farm | **16,058** | 15,381 | 15,050 | 16,309 | 16,154 |
| General and institutional | **108,604** | 106,157 | 102,826 | 105,390 | 104,133 |
| Industrial | **5,109,828** | 4,980,295 | 4,787,677 | 4,720,382 | 4,498,721 |
| Other | **779,911** | 751,720 | 735,514 | 741,899 | 819,917 |

## > operating statistics–Electricity

| In thousands of kilowatts | 2000 | 1999 | 1998 | 1997 | 1996 |
|---|---|---|---|---|---|
| **INSTALLED CAPACITY**[a] | | | | | |
| Hydroelectric | **29,246** | 29,235 | 29,203 | 29,203 | 29,220 |
| Thermal[b] | **2,266** | 2,270 | 2,269 | 2,194 | 2,193 |
| Total installed capacity | **31,512** | 31,505 | 31,472 | 31,397 | 31,413 |

*a) In addition to its own generating stations, Hydro-Québec has access to most of the generation from the Churchill Falls power plant (nominal capacity 5,428 MW). Hydro-Québec also has access to the generation from two power plants in Panama and Costa Rica (nominal capacity 310 MW).*

*b) Includes Gentilly-2 nuclear power station (nominal capacity 675 MW).*

| In millions of kilowatthours | | | | | |
|---|---|---|---|---|---|
| **TOTAL REQUIREMENTS**[a] | **197,861** | 187,999 | 176,236 | 182,263 | 182,679 |

*a) Total requirements include kilowatthours delivered within Québec and to neighboring systems.*

| In thousands of kilowatts | | | | | |
|---|---|---|---|---|---|
| **PEAK POWER REQUIREMENTS**[a] | **33,767** | 35,577 | 35,275 | 32,305 | 34,642 |

*a) Total power requirements at annual peak for the winter beginning in December, including interruptible power. The annual peak for winter 2000-2001 occurred at 7:00 p.m. on December 13, 2000.*

| In kilometres | | | | | |
|---|---|---|---|---|---|
| **LINES (OVERHEAD AND UNDERGROUND)** | | | | | |
| Transmission and subtransmission | **32,283** | 32,227 | 32,144 | 32,036 | 30,557 |
| Distribution | **106,448** | 105,898 | 105,705 | 104,640 | 104,078 |
| | **138,731** | 138,125 | 137,849 | 136,676 | 134,635 |

## > other information

| In % | 2000 | 1999 | 1998 | 1997 | 1996 |
|---|---|---|---|---|---|
| **RATE INCREASES** | | | | | |
| Average increase at May 1 | **0.0** | 0.0 | 1.6 | 1.6 | 1.3 |
| Inflation rate | **2.7** | 1.7 | 0.9 | 1.6 | 1.6 |
| **NUMBER OF EMPLOYEES**[a] | | | | | |
| Permanent at December 31 | **17,277** | 17,277 | 17,468 | 17,164 | 19,553 |
| Temporary (year's average) | **3,399** | 3,126 | 3,379 | 3,252 | 3,767 |
| Women (%) | **28.6** | 27.9 | 27.4 | 27.0 | 25.9 |

*a) Excludes employees of subsidiaries and joint ventures.*

## > consolidated results by quarter

**2000**

| In millions of dollars | 1st quarter | 2nd quarter | 3rd quarter | 4th quarter | 12-month period |
|---|---|---|---|---|---|
| | | | | (unaudited) | (audited) |
| **Revenue** | **2,932** | **2,542** | **2,913** | **3,042** | **11,429** |
| **Expenditure** | | | | | |
| Operations | **464** | **509** | **474** | **688** | **2,135** |
| Electricity and fuel purchased | **352** | **470** | **878** | **708** | **2,408** |
| Depreciation, amortization and decommissioning | **447** | **447** | **463** | **539** | **1,896** |
| Taxes | **157** | **156** | **141** | **71** | **525** |
| | **1,420** | **1,582** | **1,956** | **2,006** | **6,964** |
| **Operating income** | **1,512** | **960** | **957** | **1,036** | **4,465** |
| Financial expenses | **830** | **850** | **842** | **847** | **3,369** |
| Income before non-controlling interest | **682** | **110** | **115** | **189** | **1,096** |
| Non-controlling interest | **7** | **12** | **1** | **(2)** | **18** |
| **Net income** | **675** | **98** | **114** | **191** | **1,078** |

1999

| In millions of dollars | 1st quarter | 2nd quarter | 3rd quarter | 4th quarter | 12-month period |
|---|---|---|---|---|---|
| | | | | (unaudited) | (audited) |
| **Revenue** | 2,697 | 2,111 | 2,130 | 2,670 | 9,608 |
| **Expenditure** | | | | | |
| Operations | 484 | 477 | 461 | 490 | 1,912 |
| Electricity and fuel purchased | 289 | 290 | 235 | 295 | 1,109 |
| Depreciation, amortization and decommissioning | 404 | 408 | 428 | 491 | 1,731 |
| Taxes | 156 | 156 | 148 | 132 | 592 |
| | 1,333 | 1,331 | 1,272 | 1,408 | 5,344 |
| **Operating income** | 1,364 | 780 | 858 | 1,262 | 4,264 |
| Financial expenses | 860 | 802 | 822 | 861 | 3,345 |
| Income (loss) before non-controlling interest | 504 | (22) | 36 | 401 | 919 |
| Non-controlling interest | 5 | 7 | 1 | — | 13 |
| **Net income (net loss)** | 499 | (29) | 35 | 401 | 906 |

1.

Senior Management:
A strong team at the helm of a modern, profitable, innovative corporation focused resolutely on the future.

*— André Caillé*

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1. **Yves Filion**, Deputy Chief Executive Officer
2. **Daniel Leclair**, Vice President – Finance and Chief Financial Officer
3. **Thierry Vandal**, Executive Vice President – Generation
4. **André Caillé**, President and Chief Executive Officer
5. **Marie-José Nadeau**, Executive Vice President – Corporate Affairs and Secretary General
6. **Élie Saheb**, Executive Vice President – Engineering, Procurement and Construction
7. **Jacques Régis**, President – TransÉnergie
8. **Roger Lanoue**, Vice President – Research and Strategic Planning
9. **Michel Gourdeau**, Executive Vice President – Natural Gas Sector
10. **Maurice Charlebois**, Vice President – Human Resources
11. **Daniel Lafleur**, General Auditor

**L. Jacques Ménard** [a, b, d, f, g]
Chairman of the Board of Directors, Hydro-Québec
President, The Bank of Montreal Group of Companies, Québec
Deputy Chairman, BMO Nesbitt Burns

**André Caillé** [a, b, c, d, f, g]
President and Chief Executive Officer, Hydro-Québec

**Jean-Paul Beaulieu**
Deputy Minister of Natural Resources, Gouvernement du Québec

**Daniel Boulard** [f]
Partner, Martin, Boulard et Associés, CA

**Pierre Bourgie** [a, c, f]
Vice Chairman of the Board of Directors, Hydro-Québec
President and Chief Executive Officer, Société financière Bourgie 1996 inc.

**Robert Brouillette** [e]
Senior Partner, Brouillette Charpentier Fortin

**Charles G. Cavell** [a]
President and Chief Operating Officer, Quebecor Printing Inc.

**Alain Forand**
Major-General (retired), Canadian Forces, Department of National Defence

**Éric Gourdeau** [b, c, g]
Director

**Pierre Grand'Maison**
President and Chief Executive Officer, Thermoplast inc.

**Francine Harel Giasson** [b, d, e]
Professor, École des hautes études commerciales, Université de Montréal

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Mission Delegate to the President, AXA Canada

**Gérald Lemoyne**
Mayor of Lebel-sur-Quevillon

**Claude Munger**
Director

**Michèle Poirier** [e, g]
President, Michèle Poirier et Associés

**Serge Racine** [d]
Chairman of the Board and Chief Executive Officer, Shermag inc.

**Francine Ruest-Jutras** [a, d]
Mayor of Drummondville

**Board Committees**

*a* Executive Committee
*b* Environment and Corporate Social Responsibility
*c* Finance
*d* Human Resources
*e* Audit
*f* Pension Fund Management
*g* Ethics and Corporate Governance

## > corporate governance

Hydro-Québec's Board of Directors is concerned with maintaining the highest possible standards for corporate governance. It therefore fully subscribes to the corporate governance guidelines established by Canadian stock exchanges, even though, legally speaking, it is not required to abide by them because it is not a publicly traded company.

**MISSION**

The Board administers the company's business in accordance with the *Hydro-Québec Act*, the *Companies Act* and the energy policies of the Québec government. Its most important functions involve the analysis and adoption of the strategic plan, which describes the company's main orientations, and the annual business plan, which comprises the capital and operating budgets along with the annual performance objectives for members of the management team. Other functions include the monthly review of financial results, the four-month review of management results, the annual evaluation of integrated business risk management, and the selection and evaluation of members of Senior Management. The Board regularly receives and analyzes the subsidiaries' activity reports, financial results and accountability reports.

**INDEPENDENCE**

A majority of members of the Board come from outside the company. In fact, only one director—the President and Chief Executive Officer—is a member of Senior Management. The Board is responsible for compliance, at all times, with the rules stated in the *Code of Ethics and Rules of Professional Conduct for Directors and Executives of Hydro-Québec* based on the *Regulation respecting the ethics and professional conduct of public office holders*.

**INFORMATION**

Directors are all offered a complete information session on the energy sector and Hydro-Québec's business environment and principal activities. They also receive a director's guide describing the company's specific technical, business and regulatory context, along with the roles and responsibilities of a Board member.

**OPERATION**

The Board benefits from the expertise and experience of its members through the analyses done by the six Board committees: Audit, Finance, Human Resources, Ethics and Corporate Governance, Environment and Corporate Social Responsibility, and Pension Fund Management. After every committee meeting, a report by the chair of the committee in question is presented at the next Board meeting. The Ethics and Corporate Governance Committee is responsible for assessing the Board's performance and operation. The Executive Committee may exercise the Board's powers, except those reserved by law.

## > report of activities of the Board of Directors and Board committees

The Board of Directors is composed of a maximum of 16 members appointed by the Québec government for terms of no more than five years, as well as the President and Chief Executive Officer, who is appointed by the Board with government approval. The Deputy Minister of Natural Resources is an ex officio, non-voting member of the Board.

The Board of Directors met 10 times in 2000, with an attendance rate of about 75%. The Executive Committee held 15 meetings, while the other committees held 28 in all.

Owing to the present regulatory and business environment in the energy sector, the Board turned its attention to the issue of independent decision making between the company's business units responsible for generation, transmission and distribution operations.

Under the management mandate entrusted to Hydro-Québec by the Board of Directors of its subsidiary Hydro-Québec International (HQI), the Board looked into HQI's foreign investments, and specifically the acquisition of the Chilean electric transmission company Transelec.

Lastly, the Board followed up on Hydro-Québec's *Strategic Plan 2000-2004*.

### AUDIT

The main role of the Audit Committee is to assure the Board of Directors that the financial statements accurately present the company's financial position, that internal controls are adequate and effective, and that suitable mechanisms are being applied to identify and manage the major internal and external risks to which the company is exposed. The committee reads the internal audit reports and resulting action plans.

In 2000, this committee paid particular attention to matters related to energy theft and the payment of invoices without corresponding work orders. It also studied several action plans, concerning phase two installation of SAP R/3 software, the use of this software in equipment management, maintenance of the overhead distribution grid, implementation of e-commerce, etc.

### FINANCE

The main role of the Finance Committee is to advise the Board on financial matters, especially financing, management of corporate funds, insurance, banking, the business plan and ensuing annual budget, financial risk management and integrated business risk management.

This year, risk management took up much of the agendas of the meetings of this committee, whose responsibilities include monitoring the management of risks associated with power brokerage activities on the American market. The committee concentrated, in particular, on the guarantees issued by Hydro-Québec and its subsidiaries. It also received a detailed accounting of the application of the policy "Our Assets."

### HUMAN RESOURCES

The main role of the Human Resources Committee is to advise the Board on various matters, such as hiring, total compensation, training and succession, including the hiring, appointment, performance review and compensation of the President and Chief Executive Officer and other senior executives.

In 2000, the committee examined the application of the policy "Our Human Resources" throughout the company. It also considered the issue of pay equity and the hiring program for new graduates, and studied various matters related to corporate structure and succession in strategic jobs.

**ETHICS AND CORPORATE GOVERNANCE**

The Ethics and Corporate Governance Committee ensures that Hydro-Québec is well managed in accordance with the highest standards of ethics and corporate governance and with the relevant laws and regulations. The committee also provides advice on the application and enforcement of the *Code of Ethics and Rules of Professional Conduct for Directors and Executives of Hydro-Québec*. It makes recommendations on rules applicable to the company's business.

The committee's activities in 2000 included analyzing accountability reports on the application of corporate policies.

**ENVIRONMENT AND CORPORATE SOCIAL RESPONSIBILITY**

The Environment and Corporate Social Responsibility Committee provides advice on environmental management, public health and safety, community relations, social responsibility and corporate image. The committee receives all reports and violation notices related to environmental incidents.

During the past year, the committee studied matters related to environmental legionella, management of radioactive waste at Gentilly-2 nuclear power plant, and the integration of distribution systems into the landscape. It also defined the operating conditions of Hydro-Québec's foundation for the environment, approved by the Board of Directors in 1999 with a mission to contribute to long-term environmental protection and enhancement. It reviewed the progress made in the implementation of the ISO 14001 standard, and examined the semiannual environmental performance report submitted to the Board.

**PENSION FUND MANAGEMENT**

The role of the Pension Fund Management Committee is to advise the Board on investment management and performance, evaluation of portfolio managers and the management of the pension plan, including changes in pension obligations.

This year, the committee recommended that the Board adopt the new management policy for pension fund investments. The policy needed to be revised as a result of the adoption of a new benchmark portfolio, focusing on the target allocation of long-term assets.

Finally, the committee reviewed the performance of the pension plan portfolio and specialized portfolio managers.

> Board room.

# > Code of Ethics and Rules of Professional Conduct for Directors and Executives of Hydro-Québec



PART I

## Interpretation and application

**1.** In this Code, unless the context indicates otherwise:

a) **"Act"** means the *Hydro-Québec Act,* R.S.Q. c. H-5, as amended from time to time;

b) **"affiliated enterprise"** means a legal person or company in which the Corporation owns, directly or indirectly, securities including shares, conferring more than 10% of voting rights or economic interest;

c) **"Board"** means the Board of Directors of the Corporation;

d) **"Committee"** or **"Ethics and Corporate Governance Committee"** means the Ethics and Corporate Governance Committee established by resolution of the Board of October 17, 1997 (HA-173/97), a copy of which is attached as Schedule D;

e) **"contract"** includes a proposed contract;

f) **"control"** means the direct or indirect ownership of securities, including shares, conferring more than 50% of voting rights or economic interest without this right depending on the occurrence of a particular event or allowing the election of the majority of directors;

g) **"Corporation"** means Hydro-Québec;

h) **"director"** means, with respect to the Corporation, a member of the Board of Directors of the Corporation, whether or not working full-time within the Corporation;

i) **"enterprise"** means any form that can be taken by the organization for the production of goods or services or any other business of a commercial, industrial or financial nature or any group seeking to promote certain values, interests or opinions or to exercise an influence on public officials; however this does not include the Corporation or a non-profit association or group that has no financial link with the Corporation or is not incompatible with the objects of the Corporation;

j) **"executive"** with respect to the Corporation means any contractual manager whose employment conditions are subject to the approval of the Board;

k) **"immediate family"** means spouse and dependent children;

l) **"spouse"** includes marriage partners and persons living as if married for more than one year;

m) **"subsidiary"** means a legal person or corporation controlled directly or indirectly by the Corporation.

**2.** In this Code, the prohibition to perform an act also applies to any attempt to perform it and any participation in it or incitement to perform it.

**2.1** This Code applies to the directors and to the President and Chief Executive Officer and the other executives of the Corporation.

The directors and the President and Chief Executive Officer are also subject to the *Regulation respecting the ethics and professional conduct of public office holders* (Order-in-Council 824-98 of June 17, 1998 as amended).

PART II

## Ethical principles and general rules of professional conduct

**3.** The director or executive is appointed to contribute to the achievement of the mission of the Corporation in the best interest of Québec. Accordingly, he is expected to use his knowledge, abilities and experience in a way that will promote the effective, fair and efficient accomplishment of the objectives assigned to the Corporation by the Act and the good administration of the property it owns as mandatary of the State.

His contribution shall be made in compliance with the law and with honesty, loyalty, prudence, diligence, efficiency, application and fairness.

**3.1** The director or executive respects the following principles in the performance of his duties:

- a vision of the Corporation that seeks to make it a world leader in the energy industry by developing its expertise for the benefit of its customers, employees and shareholder and by working with partners in business ventures;
- the values underlying the activities of the Corporation as a government-owned business corporation, which include customer satisfaction, an understanding of business, respect for employees, quality improvement, respect for the environment, partnership with local communities and protection of the future;
- the principles set out in the basic policies of the Corporation, expressing commitments and conveying a business culture with regard to customers, human resources, acquisition of assets and services, business partners, finance, assets, the environment, social role and corporate governance.

**3.2** The director or executive is required, in the performance of his duties, to respect the ethical principles and rules of professional conduct provided in the Act, the *Regulation respecting the ethics and professional conduct of public office holders* (Order-in-Council 824-98 of June 17, 1998 as amended) as appropriate, and those defined in this Code. In case of discrepancy, the more demanding rules and principles apply.

In case of doubt, act according to the spirit of these principles and rules.

A director or executive who, at the request of the Corporation, serves as director or member of an undertaking or company, is held to the same standards.

**4.** The director or executive shall not merge the assets of the Corporation with his own; he may not use the assets of the Corporation or information he obtains as a result of his duties for his own profit or the profit of others. These obligations continue even after the director or executive has ceased to hold his position.

**5.** The director or executive shall seek, in the performance of his duties, only the interest of the Corporation to the exclusion of his own interest or that of others.

**5.1** The director or executive is bound to discretion in regard to anything that comes to his knowledge in or during the performance of his duties and is at all times bound to maintain the confidentiality of such information.

**5.2** In the performance of his duties, the director or executive shall make decisions without regard for any partisan political considerations.

The Chairman of the Board, the director working full-time within the Corporation and the executive shall demonstrate reserve in the public expression of their political opinions.

**6.** The director or executive may not directly or indirectly grant, solicit or accept a favor or an undue advantage for himself or for a third party.

In particular, he may not accept or solicit an advantage from a person or undertaking doing business with the Corporation or a subsidiary or acting in the name of or on behalf of such a person or undertaking if this advantage is intended or likely to influence him in the performance of his duties or generate expectations of this nature.

**6.1** The director or executive shall, in making decisions, avoid allowing himself to be influenced by offers of employment.

**6.2** The director or executive may not accept any gift or hospitality except what is customary and modest in value.

Any other gift or hospitality shall be returned to the giver.

**7.** The director may not make a commitment to a third party or grant them any guarantee relative to a vote he may be asked to make or any decision whatsoever that the Board may be asked to make.

**7.1** The director or executive may not, in the performance of his duties, deal with a person who has ceased to be a director or executive of the Corporation for less than one year if this person is acting on behalf of a third party with respect to a proceeding, negotiation or other transaction to which the Corporation is a party and about which he has information not available to the public.

**7.2** After ceasing his duties, no director or executive may disclose confidential information he has obtained or give anyone advice based on information not available to the public concerning the Corporation or any other undertaking or company with which he had direct and substantial dealings during the year preceding the date on which he ceased his duties.

In the year following that date, he may not act on behalf or on account of another party with respect to a procedure, negotiation or other transaction to which the Corporation is a party and about which he has information not available to the public.

**8.** The director or executive shall collaborate with the Chairman of the Board or the Ethics and Corporate Governance Committee on an issue of ethics or professional conduct when asked to do so.

**8.1** A director or executive who intends to be a candidate for elected office shall inform the Chairman of the Board of this intention.

The Chairman of the Board or President and Chief Executive Officer with the same intention shall inform the Secretary General of the Executive Committee.

PART III

## Duties and obligations of directors and executives with respect to conflicts of interest

### *Prevention of conflicts of interest*

**9.** The director or executive shall avoid placing himself in a situation in which his personal interest is in conflict with the duties of his position or in which reasonable doubt is cast on his ability to perform these duties with undivided loyalty.

A director who is employed full-time within the Corporation or one of its subsidiaries shall also avoid performing duties or being bound by commitments that prevent him from devoting the time and attention that the normal exercise of his duties requires.

As for other directors, they shall be sure to devote the time and attention reasonably required in the circumstances for the execution of their duties.

**10.** No director holding a full-time office with the Corporation, under pain of forfeiture of office, may have any direct or indirect interest in an undertaking, company or association that puts his personal interest in conflict with that of the Corporation.

However, such forfeiture is not incurred if that interest devolves to him by succession or gift, provided that he renounces or disposes of it with all possible dispatch. Meanwhile, sections 12, 13, 15 and 18 apply to this director.

Every other director who has an interest in an undertaking shall, on pain of forfeiture of his office, comply with the provisions of sections 12, 13, 15 and 18.

**11.** A director or executive of the Corporation who serves as director or executive of an affiliated enterprise shall be specifically authorized by the shareholder or shareholders who control the enterprise concerned to:

a) hold shares, rights or any other security issued by such enterprise and conferring voting rights or economic interest in it or the right to subscribe or buy such shares, rights or securities;

b) benefit from any profit-sharing program, unless he works full-time for the enterprise and the profit-sharing program is closely linked with the individual performance of the director or executive within the affiliated enterprise;

c) benefit from a pension plan granted by the affiliated enterprise if he does not hold a full-time position within the enterprise; or

d) benefit from any advantage granted in advance in the case of a change of control of the affiliated enterprise.

**12.** A director or executive who:

a) is party to a contract with the Corporation or a subsidiary; or

b) has a direct or indirect interest in an enterprise that is a party to a contract with the Corporation or a subsidiary or is a director, executive or employee of this enterprise;

shall disclose the nature and extent of his interest in writing to the Chairman of the Board.

The same applies to a director who has a direct or indirect interest in any issue being considered by the Board of Directors.

The director shall at all times abstain from conveying information of any kind to any employee, executive or director of the Corporation with respect to this contract or interest.

The director shall abstain from deliberating or voting on any question linked to this interest and avoid trying to influence the related decision. The director shall also withdraw from the meeting for the duration of deliberations and voting on this question.

**13.** The disclosure required by section 12 occurs, in the case of a director, during the first meeting:

a) in the course of which the contract or question concerned is under study;

b) following the time at which the director who had had no interest in the contract or question concerned acquires such interest;

c) following the time at which the director acquires an interest in the already concluded contract; or

d) following the time at which any person with an interest in a contract or a question under study becomes a director.

**14.** An executive who is not a director shall make the disclosure required in section 12 immediately after:

a) having learned that the contract or question concerned was or will be studied at a meeting;

b) having acquired the interest, if it is acquired after the contract was concluded or the decision made;

c) having become an executive, if he becomes one after acquiring the interest.

The executive may not try to influence the directors' decision in any way.

**15.** The director or executive shall make the disclosure required in section 12 as soon as he has knowledge of a contract contemplated by this section which, as part of the normal business of the Corporation, does not require the approval of the directors.

**16.** Sections 12 to 15 apply also when the interest concerned is held by a member of the immediate family of the director or executive.

**17.** The director or executive shall notify the Chairman of the Board in writing of the rights he may invoke against the Corporation, by indicating their nature and their value, as soon as these rights come into existence or when he acquires knowledge of them.

**18.** The director or executive shall submit to the Chairman of the Board within 60 days of being appointed and on January 31 of each year in which he remains in office, an attestation in the form provided in Schedule A and containing the following information:

a) the name of any enterprise in which the director or executive owns, directly or indirectly, securities or assets, including common shares, specifying the nature and quantity in number and proportion of securities owned and value of assets;

b) the name of any enterprise for which he performs functions or in which he has an interest in the form of a debt, right, priority, mortgage or significant commercial or financial benefit; and

c) to the best of his knowledge, the information specified in the preceding paragraphs concerning his employer and the corporation, company or enterprise of which he is owner, shareholder, director or executive.

A director or executive to whom the provisions of paragraphs a) to c) do not apply shall fill out an attestation to that effect and present it to the Chairman of the Board.

The director or executive shall also produce such an attestation within 60 days of the occurrence of a significant change in its content.

The attestations presented pursuant to this section are treated as confidential.

**19.** The Chairman of the Board submits the attestations received pursuant to sections 12 to 18 to the Secretary of the Corporation, who keeps them at the disposal of the members of the Board and the Ethics and Corporate Governance Committee.

Moreover, the Secretary of the Corporation notifies the Ethics and Corporate Governance Committee of any failure to satisfy the obligations provided for in sections 12 to 18 as soon as the Secretary becomes aware of them.

### *Waivers*

**20.** This Code does not apply:

a) to owning securities when the size of the holding probably does not place the director or executive in a conflict of interest;

b) to owning an interest by way of a mutual fund in whose management the director or executive plays no role directly or indirectly;

c) to owning interests through a blind trust whose beneficiary cannot know its make-up;

d) to owning a minimum number of shares required to be eligible as director of a corporation;

e) to an interest which, by its nature and extent, is common to the public at large or a particular sector in which the director or executive operates;

f) to a directors' liability insurance agreement; or

g) to the owning of shares issued or guaranteed by the Corporation, a government or municipality under the same conditions for everyone.

### *Attestation*

**20.1** Within sixty days of the adoption of this Code by the Board, each director shall submit to the Chairman of the Board and the Secretary of the Corporation the attestation appearing in Schedule B.

Each new director shall do the same within sixty days of his appointment to this position.

## PART IV
## **Remuneration**

**20.2** The director or executive, for the exercise of his duties, is entitled solely to the remuneration related to those duties. Such remuneration may not include, even partially, monetary advantages such as those established, in particular, by a profit-sharing plan based on the variation in the value of shares or on a stake in the capital stock of the Corporation.

**20.3** A director or executive dismissed for just and sufficient cause may not receive a severance allowance or payment.

**20.4** A director or executive who quits his duties, who has received or is receiving a severance allowance or payment and who holds an office, employment or any other remunerated position in the public sector during the period corresponding to that allowance or payment shall refund the part of the allowance or payment covering the period for which he receives a salary or shall cease to receive it during that period.

However, if the salary he receives is lower than that he received previously, he shall be required to refund the allowance or payment only up to the amount of his new salary or he may continue to receive the part of the allowance or payment that exceeds his new salary.

**20.5** Anyone who has received or is receiving a severance allowance or payment from the public sector and receives a salary as director or executive during the period corresponding to that allowance or payment shall refund the part of the allowance or payment covering the period for which he receives a salary or shall cease to receive it during that period.

However, if the salary he receives as director or executive is lower than that he was receiving previously, he shall be required to refund the allowance or payment only up to the amount of his new salary or he may continue to receive the part of the allowance or payment that exceeds his new salary.

**20.6** A President and Chief Executive Officer who has ceased to perform his duties, who has received so-called assisted departure measures and who, within two years after his departure, accepts an office, employment or any other remunerated position in the public sector shall refund the sum corresponding to the value of the measures received by him, up to the amount of the remuneration received, by the fact of his return to the public sector, during that two-year period.

**20.7** Part-time teaching by a director or executive is not covered by sections 20.2 to 20.6

**20.8** For the application of sections 20.2 to 20.6, "public sector" means the bodies, institutions and corporations referred to in Schedule C.

The period covered by the severance allowance or payment referred to in subsections 20.4 and 20.5 shall correspond to the period that would have been covered by the same amount if the person had received it as a salary in his former office, employment or position.

PART V
## Application of the Code

### *Competent authorities*

**20.9** The Associate Secretary General for Senior Positions of the Ministère du Conseil Exécutif is the competent authority for the application of this Code with respect to the Chairman of the Board and the other directors of the Corporation appointed by the Government.

The Chairman of the Board is the competent authority with respect to other directors or executives of the Corporation.

The Chairman of the Board shall ensure observance of the ethical principles and rules of professional conduct by the directors and the executives of the Corporation.

**21.** The Ethics and Corporate Governance Committee has as its mission to advise the competent authority with respect to ethics and professional conduct.

The Committee also performs the duties invested in it by the resolution appearing in Schedule D and performs any other duties related to ethics entrusted to it by the Board.

In the performance of its duties, the Ethics and Corporate Governance Committee may become acquainted with the attestations contemplated by section 19.

**22.** When a director or executive is accused of a violation of ethics or the rules of professional conduct, the Committee is responsible for collecting all relevant information. It makes a report of its findings to the competent authority and recommends appropriate measures, if any.

The competent authority notifies the director or executive of the alleged violations and the possible penalties. It informs him that he has seven days in which to respond and if he requests, to be heard on this matter.

**23.** The Committee may render advisory opinions on the provisions of this Code and their application to specific cases, even hypothetical ones. It is not required to limit its views to the terms contained in the request.

**23.1** In order to allow an appropriate decision to be made in the case of an urgent situation requiring fast response or in an alleged case of serious misconduct, the competent authority may temporarily relieve of his duties, with remuneration, the director or executive who is accused of violations of ethics or the rules of professional conduct.

**24.** The Secretary of the Corporation keeps records in which are stored the statements, disclosures and attestations that must be submitted to it under this Code, the reports, decisions and advisory opinions of the Committee and the decisions of the competent authority with respect to ethics and professional conduct.

The Secretary shall also take the necessary steps to ensure the confidentiality of the information provided by the directors and executives pursuant to this Code.

**25.** The Committee may consult and receive opinions from outside counsel or experts on any issue it considers appropriate.

**26.** A director or executive does not violate the provisions of this Code if he has obtained in advance a favorable decision from the Committee, on the following conditions:

a) the decision was obtained before the facts on which it was based became a reality;

b) the decision was submitted to the Board;

c) all of the relevant facts were fully disclosed to the Committee exactly and completely; and

d) the director or executive has complied with all the requirements of the decision.

**27.** The Committee and the competent authority preserve the anonymity of complainants, applicants and informers unless there is a clear intention to do otherwise. They may not be forced to reveal information likely to disclose their identity except if the law or a court so requires.

### *Penalties*

**28.** Upon concluding that a provision of the law, the *Regulation respecting the ethics and professional conduct of public office holders* or this Code has been violated, the competent authority may impose either of the following penalties:

a) for an executive, the appropriate penalty, which can extend as far as termination of employment; and

b) for a director, reprimand, suspension without remuneration for a maximum of three months, or removal from the Board.

However, when the competent authority is the Associate Secretary General contemplated by section 20.9, the penalty is imposed by the Secretary General of the Executive Committee. If the penalty proposed consists of the removal of a public office holder appointed or designated by the Government, it can only be imposed by the latter; in this case, the Secretary General of the Executive Committee may immediately suspend the public office holder without remuneration for a period not exceeding 30 days.

Any penalty imposed on a director and the decision to temporarily relieve him of his duties must be in writing and give the reasons therefor.

**29.** In the case of a violation of section 10, the competent authority records in writing the forfeiture of office of the violator.

**30.** The director or executive shall render an account and restore to the Corporation any profits earned or benefits received as a result of or on the occasion of a violation of the provisions of this Code.

**31.** A director's vote shall not be a casting vote if it is made in violation of the provisions of this Code or associated with such a violation, or if the director fails to produce the attestation contemplated by section 18.

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The schedules may be consulted on Hydro-Québec's Web site (www.hydroquebec.com).

> Plaque presented by the OLF attesting to the quality of French used in the company.

## > language guidelines

In applying its language guidelines, Hydro-Québec emphasized improving the quality of French. A dozen or so made-to-measure courses were offered to the company's personnel this past year, in grammar, business correspondence, report writing, and other subjects. Close to 750 employees signed up, and some 50 training sessions were given.

To promote the use of French in new activity sectors, the company drafted an e-commerce vocabulary. A preliminary edition of this new tool was made available to personnel.

Various other promotional and awareness activities were organized within the company to mark a week-long event celebrating the French language and the French-speaking world.

Hydro-Québec presented the Office de la langue française with its annual report on the application of the government's policy on the use of French in information technologies.

Finally, Hydro-Québec's standing committee on language continued its work, meeting twice in 2000.

## > acquisition of goods and services

During the year, Hydro-Québec worked to fulfill the commitments stated in the policy "Our Acquisition of Goods and Services," adopted in 1998.

Accordingly, the company maintained its strategy to ensure security of supply. For most goods and services, it uses several suppliers. In cases where it has only one supplier, it endeavors to reduce the risk by searching for new suppliers, approving alternate products and formulating emergency plans. Three new partnership agreements help ensure that suppliers develop other markets so they are less vulnerable to fluctuations in the volume of Hydro-Québec's purchases. There are currently 10 such partnerships with Québec suppliers.

In addition, the company takes every possible measure to ensure quality; for example, by demanding that suppliers of strategic goods and services have ISO 9000–compliant quality systems and by establishing quality management and control mechanisms. During the year, mandatory ISO 9000 compliance was implemented for vegetation control, which previously had been the only strategic sector of the company's activities not yet subject to ISO standards.

With a view to efficiency, Hydro-Québec followed an approach of grouping its needs, which allows it to secure better market conditions, as well as strategies for reducing supply costs and lead times and improving the quality of goods and services purchased. These strategies, and the long-term business relations with suppliers made possible by supply agreements, have led to sizable savings: about $23 million in 2000 and $117 million altogether since 1997.

The impacts of the company's activities remain considerable in terms of economic spinoffs in Québec: 94% of our total $1,570 million in purchases were made from Québec-based companies.

As well, Hydro-Québec cooperated with Sous-traitance industrielle Québec in setting up a Web site for Québec suppliers. This additional tool will make it easier for the company to obtain information on prospective suppliers in the various regions of Québec.

**PURCHASES BY ADMINISTRATIVE REGION ($'000)**[a]

| Administrative region of Québec | Goods[b] | Services[c] | Total |
|---|---|---|---|
| Bas-Saint-Laurent (01) | 2,218 | 3,531 | 5,749 |
| Saguenay–Lac-Saint-Jean (02) | 6,812 | 28,271 | 35,083 |
| Capitale-Nationale (03) | 34,451 | 58,359 | 92,810 |
| Mauricie (04) | 22,877 | 55,671 | 78,548 |
| Estrie (05) | 3,651 | 5,737 | 9,388 |
| Montréal (06) | 356,012 | 347,197 | 703,209 |
| Outaouais (07) | 10,270 | 3,484 | 13,754 |
| Abitibi-Témiscamingue (08) | 7,789 | 27,629 | 35,418 |
| Côte-Nord (09) | 6,464 | 43,039 | 49,503 |
| Nord-du-Québec (10) | 1,853 | 6,728 | 8,581 |
| Gaspésie–Îles-de-la-Madeleine (11) | 760 | 4,171 | 4,931 |
| Chaudière-Appalaches (12) | 10,770 | 37,989 | 48,759 |
| Laval (13) | 8,931 | 63,333 | 72,264 |
| Lanaudière (14) | 31,269 | 13,962 | 45,231 |
| Laurentides (15) | 8,372 | 18,330 | 26,702 |
| Montérégie (16) | 139,972 | 61,603 | 201,575 |
| Centre-du-Québec (17) | 10,686 | 33,062 | 43,748 |
| **Total** | **663,157** | **812,096** | **1,475,253** |

*a) Amounts billed by suppliers located in the administrative region.*
*b) Strategic goods, miscellaneous goods, rental of goods.*
*c) Specialized services, professional services and other work.*

**HYDROELECTRIC**

| | Installed capacity (kW) | | Installed capacity (kW) | | Installed capacity (kW) |
|---|---|---|---|---|---|
| Robert-Bourassa | 5,328,000 | Brisay | 446,500 | Rapides-des-Quinze | 94,560 |
| La Grande-4 | 2,650,500 | Laforge-2 | 304,000 | Chute-des-Chats | 89,300 |
| La Grande-3 | 2,304,000 | Trenche | 302,400 | Bryson | 61,000 |
| La Grande-2-A | 1,998,000 | Paugan | 250,100 | Hart-Jaune | 48,450 |
| Beauharnois | 1,656,860 | Beaumont | 243,000 | Rivière-des-Prairies | 48,300 |
| Manic-5 | 1,528,000 | La Tuque | 224,000 | Rapide-2 | 48,000 |
| La Grande-1 | 1,368,000 | Shawinigan-2 | 202,601 | Rapide-7 | 48,000 |
| Manic-3 | 1,183,200 | Rapide-Blanc | 201,600 | Chute-Hemmings | 28,800 |
| Manic-5-PA | 1,064,000 | Manic-1 | 184,410 | Hull-2 | 27,280 |
| Manic-2 | 1,015,200 | Shawinigan-3 | 171,900 | Lac-Robertson | 23,760 |
| Bersimis-1 | 936,000 | Les Cèdres | 153,000 | Sept-Chutes | 21,600 |
| Laforge-1 | 837,900 | Chelsea | 150,700 | Drummondville | 16,200 |
| Bersimis-2 | 798,000 | Grand-Mère | 149,575 | Saint-Narcisse | 15,000 |
| Outardes-3 | 756,200 | Rapides-des-Îles | 146,520 | Chute-Bell | 9,900 |
| Carillon | 654,500 | La Gabelle | 136,580 | Mitis-1 | 6,400 |
| Outardes-4 | 632,000 | Première-Chute | 124,200 | Mitis-2 | 4,250 |
| Outardes-2 | 453,900 | Rapides-Farmers | 98,250 | Chute-Burroughs | 1,600 |

**THERMAL**

| | Installed capacity (kW) | | Installed capacity (kW) | | Installed capacity (kW) |
|---|---|---|---|---|---|
| **Nuclear** | | Kuujjuaq | 3,935 | Akulivik | 850 |
| Gentilly-2 | 675,000 | Kuujjuarapik | 3,405 | Tasiujaq | 850 |
| **Oil** | | Inukjuak | 2,990 | Aupaluk | 550 |
| Tracy | 600,000 | Povungnituk | 2,870 | Clova | 530 |
| **Gas-turbine** | | Port-Menier | 2,790 | Saint-Augustin* | 400 |
| Bécancour | 428,200 | Weymontachie | 2,220 | | |
| La Citière | 280,000 | Salluit | 2,000 | **Total installed capacity** | |
| Cadillac | 162,000 | Kangiqsualujjuaq | 2,000 | **at December 31, 2000**** | **(kW)** |
| **Diesel** | | Kangiqsujuaq | 1,520 | Hydroelectric generating | |
| Îles-de-la-Madeleine | 67,200 | L'Île-d'Entrée | 1,190 | stations (51) | 29,245,996 |
| La Tabatière* | 6,800 | Ivujivik | 1,050 | Thermal generating | |
| La Romaine | 4,934 | Kangirsuk | 1,050 | stations (29) | 2,266,129 |
| Obedjiwan | 4,900 | Umiujaq | 1,050 | **Total generating** | |
| Blanc-Sablon* | 4,800 | Quaqtaq | 1,045 | **stations (80)** | **31,512,125** |

**UNDER CONSTRUCTION**

| | Commissioning date | Installed capacity (kW) |
|---|---|---|
| Sainte-Marguerite-3 hydroelectric generating station | 2001 | 882,000 |

* Kept in reserve since the commissioning of Lac-Robertson generating station.

** Hydro-Québec also has access to most of the generation from Churchill Falls power plant, which has a nominal capacity of 5,428 MW.

Generating station rated 300 MW or more
Generating station rated 300 MW or more under construction
735-kV substation
735-kV line
450-kV direct-current (DC) line
Alternating-current (AC) interconnection
Direct-current (DC) interconnection
Neighboring system
HUDSON BAY
QUÉBEC
JAMES BAY
La Grande-2-A
Robert-Bourassa
La Grande-1
La Grande-3
La Grande-4
Laforge-2
Brisay
Laforge-1
to Churchill Falls
Sainte-Marguerite-3
Manic-5-PA
Manic-5
Manic-3
Outardes-4
Outardes-3
Manic-2
Outardes-2
Bersimis-1
Bersimis-2
ST. LAWRENCE RIVER
Trenche
Gentilly-2
Bécancour
Tracy
Carillon
Beauharnois
ONTARIO
LAKE ONTARIO
NEW BRUNSWICK
PRINCE EDWARD ISLAND
NOVA SCOTIA
MAINE
VERMONT
NEW YORK
NEW HAMPSHIRE
UNITED STATES
MASSACHUSETTS
CONNECTICUT
R.I.
PENNSYLVANIA
NEW JERSEY
ATLANTIC OCEAN

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**Hydro-Québec International** (HQI) is responsible for investments and the sale of professional services outside Canada and the United States. Since HQI has entrusted Hydro-Québec with the management of its operations, each Hydro-Québec business unit is responsible for foreign operations in its spheres of competence.

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**Hydro-Québec CapiTech** is a corporate venture capital company that invests in companies with technology-based products and services related to the energy industry.

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The **Société d'énergie de la Baie James** chiefly provides world-class services in engineering and in carrying out construction projects in the energy industry, both locally and internationally.

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**H.Q. Energy Marketing** conducts energy transactions, including sales, purchases and exchanges in Canada as well as in the United States through H.Q. Energy Services (U.S.).

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**Noverco**, a holding company in which Hydro-Québec has a stake, controls a large number of companies involved primarily in the transmission and distribution of natural gas.

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**Units of Measure**

| | |
|---|---|
| **$M** | millions of dollars |
| **MW** | megawatt (one million watts) |
| **GW** | gigawatt (one million kilowatts) |
| **GWh** | gigawatthour (one million kilowatthours) |
| **TWh** | terawatthour (one billion kilowatthours) |

The following publications may be obtained at our Web site (www.hydroquebec.com) or by calling 1 800 363-7443:

*Strategic Plan 2000-2004*
*Annual Report 2000* (this document)
*Environmental Performance Report 2000*
*Financial Profile 2000*

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Hydro-Québec wishes to thank all the employees whose photos appear in this Annual Report.

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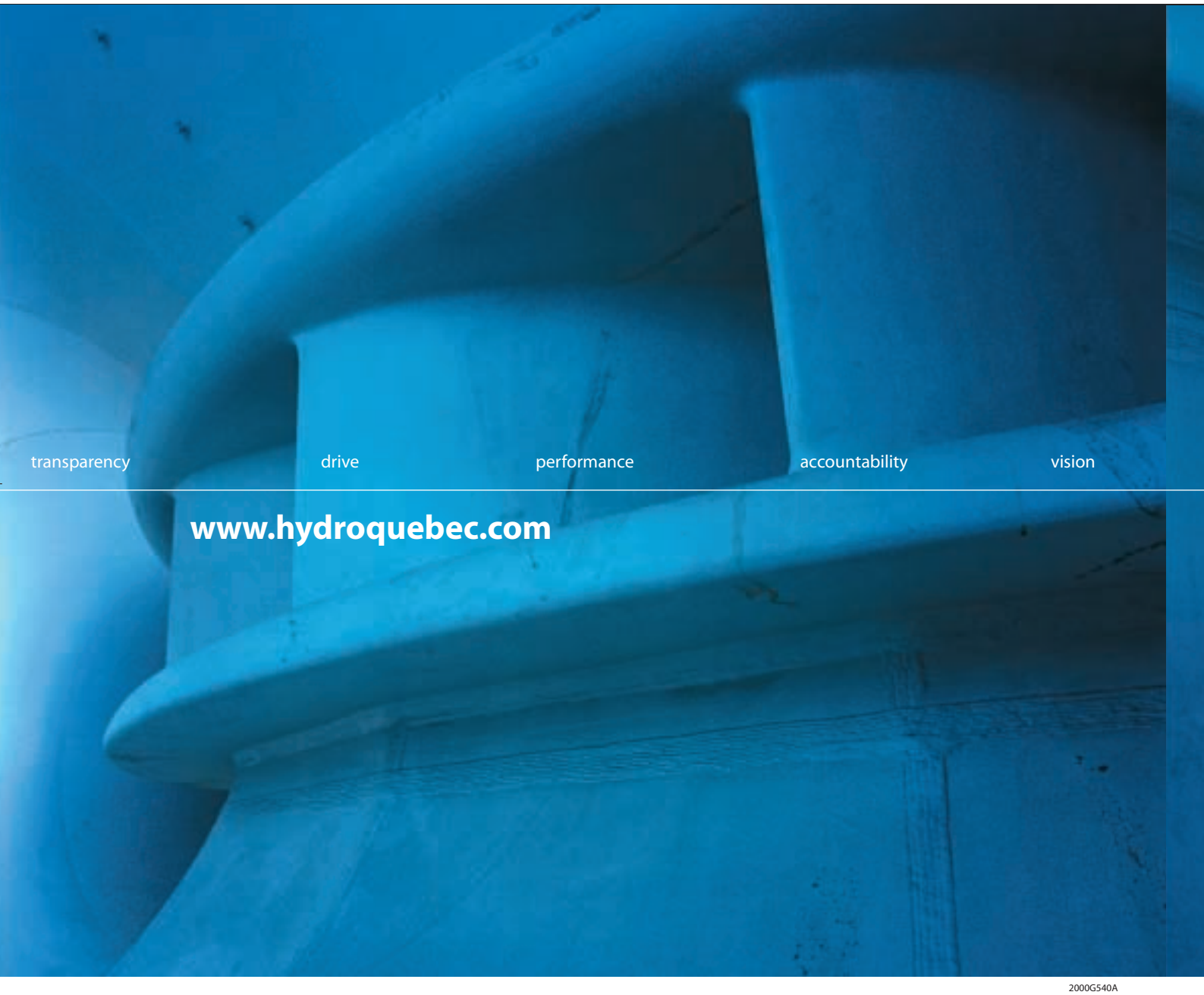
*Ce document est également publié en français.*

> In 2001, I'll be one of the last people to walk through the scrollcase before the water starts rushing in. I'm very proud to have been a part of the Sainte-Marguerite-3 construction project.

*— Frédéric Prévost, mechanical engineer*

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