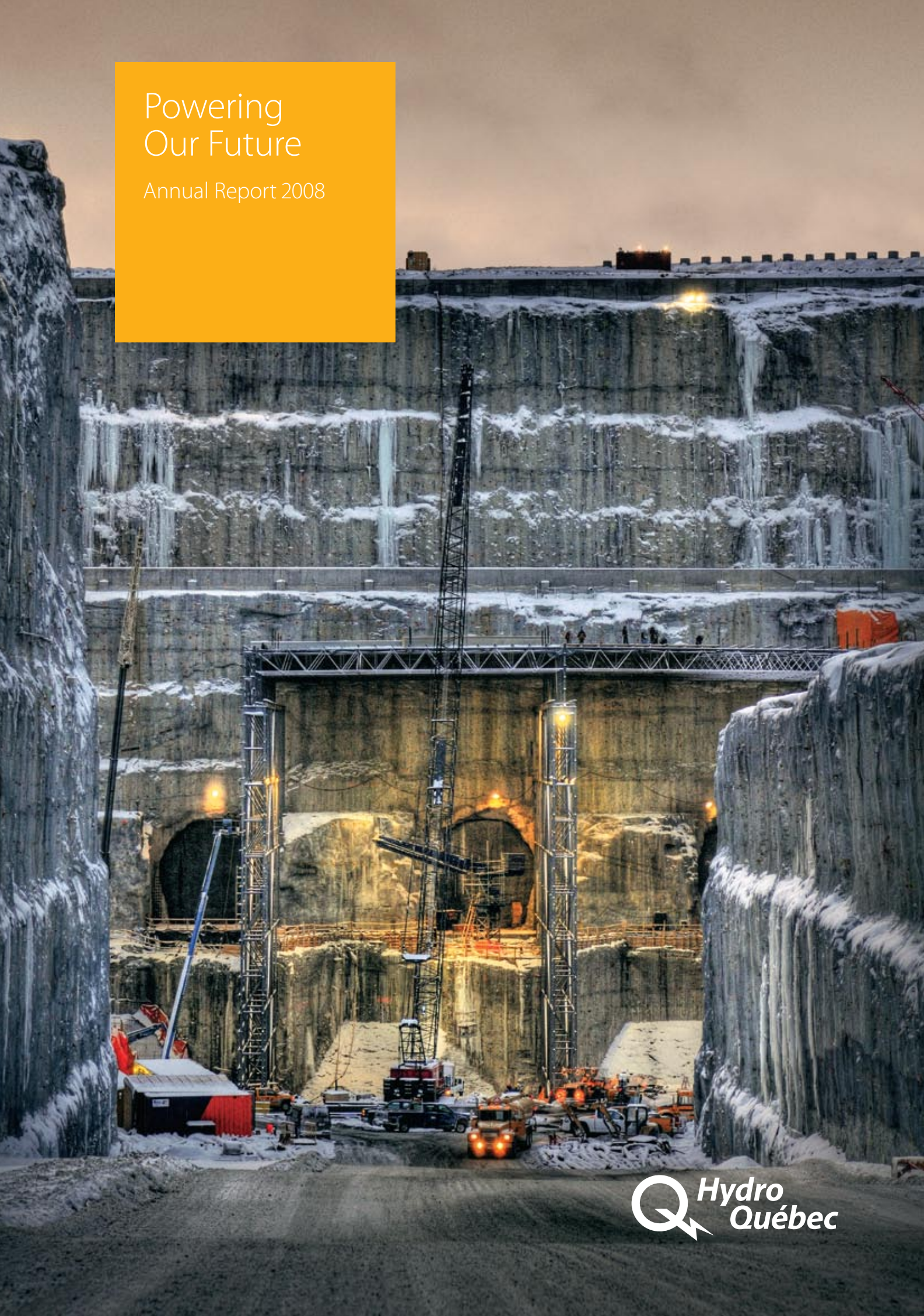
Powering Our Future

Annual Report 2008



Hydro Québec

Hydro-Québec

Hydro-Québec generates, transmits and distributes electricity. Its sole shareholder is the Québec government. It uses mainly renewable generating options, in particular hydropower, and supports the development of wind energy through purchases from independent power producers. It also conducts research in energy-related fields such as energy efficiency. The company has four divisions:

Hydro-Québec Production generates power for the Québec market and sells its surpluses on wholesale markets. It is also active in arbitraging and purchase/resale transactions.

Hydro-Québec TransÉnergie operates the most extensive transmission system in North America for the benefit of customers inside and outside Québec.

Hydro-Québec Distribution provides Quebecers with a reliable supply of electricity. To meet needs beyond the annual heritage pool which Hydro-Québec Production is obligated to supply at a fixed price, it mainly uses a tendering process. It also encourages its customers to make efficient use of electricity.

Hydro-Québec Équipement and Société d'énergie de la Baie James (SEBJ), a subsidiary of Hydro-Québec, design, build and refurbish generation and transmission facilities, mainly for Hydro-Québec Production and Hydro-Québec TransÉnergie.

CONTENTS

2 Hydro-Québec at a Glance
4 Message from the Chairman of the Board
6 Message from the President and Chief Executive Officer

Review of Operations
8 Hydro-Québec Production – Hydropower: The Driving Force Behind Our Development
14 Hydro-Québec TransÉnergie – An Evolving System
20 Hydro-Québec Distribution – Reliable, Efficient Service
28 Hydro-Québec Équipement and SEBJ – Expertise and Innovation: A Winning Combination
34 Preparing for the Future with Innovation
38 Powering a Better Future
42 Powering the Québec Economy
48 Investing in Culture and Society

Financial Review
52 Management's Discussion and Analysis
74 Consolidated Financial Statements
103 Five-Year Review
106 Consolidated Results by Quarter

Corporate Administration
107 Corporate Management
108 Board of Directors
112 Activity Report of the Board of Directors and Board Committees
116 Corporate Governance
120 Code of Ethics and Rules of Professional Conduct for Directors, Executives and Controllers of Hydro-Québec
124 Generating and Transmission Facilities
125 Major Facilities (map)

On the cover:
Excavating the tailrace for Eastmain-1-A powerhouse (Baie-James). Water will enter the tailrace after flowing through the turbines.

Opposite:
Kevin Drouin and Jean Gagné, of the Québec joint venture Neilson-EBC, excavating the intake, which will channel the water into the powerhouse.

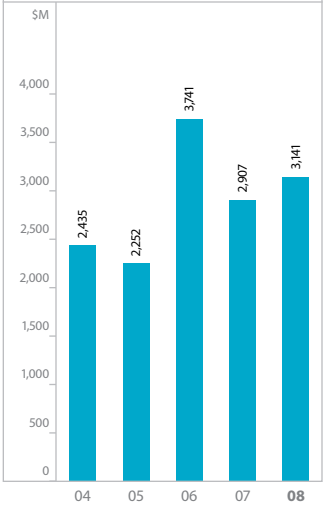
Powering a Clean and Sustainable Future

At Hydro-Québec, we use primarily renewable energy—mainly hydropower, complemented by wind power—to meet the present and future needs of our customers. Our hydropower projects and wind power supply contracts are informed by our concern for environmental protection, social acceptability and regional economic development. Our commitment to sustainability is further expressed through our energy efficiency programs and the importance we attach to technological innovation as a means of improving our performance and inventing solutions for the future.

Hydro-Québec at a Glance

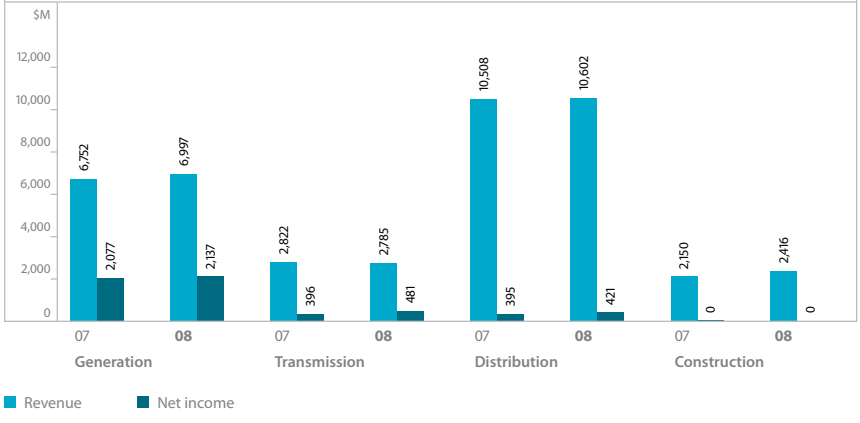
	2008	2007
Operations and Dividends ($M)		
Revenue	**12,717**	12,330
Operating income	**5,457**	5,394
Income from continuing operations	**3,012**	2,882
Income from discontinued operations	**129**	25
Net income	**3,141**	2,907
Dividends declared	**2,252**	2,095
Balance Sheets ($M)		
Total assets	**66,774**	64,866
Long-term debt, including current portion and perpetual debt	**36,415**	34,534
Equity	**22,062**	20,892
Cash Flows ($M)		
Operating activities	**5,015**	5,159
Investing activities	**(4,210)**	(3,406)
Financing activities	**(507)**	(1,744)
Cash and cash equivalents	**370**	54
Ratios		
Interest coverage	**2.12**	2.13
Return on equity (%)	**15.4**	15.0
Profit margin from continuing operations (%)	**23.7**	23.4
Capitalization (%)	**37.7**	37.5
Self-financing (%)	**44.9**	61.9

Net Income

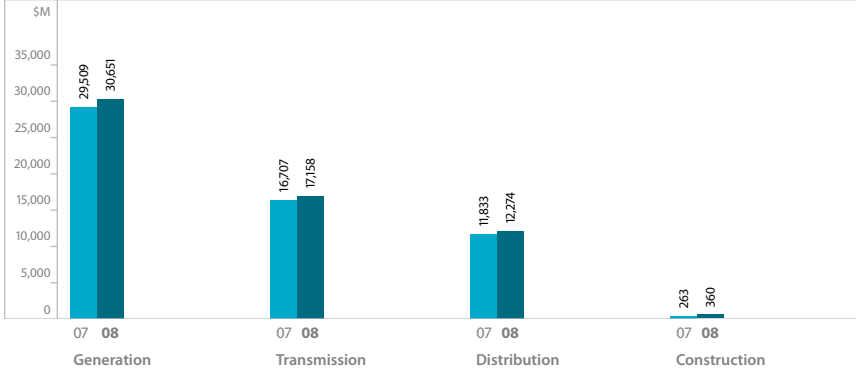


Net income totaled $3.1 billion, up $234 million from 2007. This increase was due to growth of $380 million in net electricity exports and a $126-million gain related to the price adjustments called for in the contract of sale for the interest in Transelec, in Chile. These factors were offset by a $285-million increase in water-power royalties.

Revenue and Net Income by Segment



Total Assets by Segment



Note: Certain comparative figures have been reclassified to reflect the presentation adopted for 2008.

	2008	2007	2006	2005	2004
Customers and Sales					
Total customer accounts in Québec	**3,913,444**	3,868,972	3,815,126	3,752,510	3,701,275
Electricity sales in Québec (TWh)	**170.4**	173.2	167.3	169.2	165.9
Electricity sales outside Québec (TWh)	**21.3**	19.6	14.5	15.3	14.4
Number of Employees[a]					
Permanent as at December 31	**19,297**	19,459	19,116	19,009	18,835
Temporary (year's average)	**4,048**	3,910	3,799	3,577	3,567
Facilities					
Number of hydroelectric generating stations	**59**	57	55	54	53
Total installed capacity (MW)[b]	**36,429**	35,647	35,315	34,571	33,892
Peak power demand in Québec (MW)[c]	**37,230**	35,352	36,251	33,636	34,956
Lines (overhead and underground)					
Transmission (km)	**33,058**	33,008	32,826	32,544	32,487
Distribution (km)[d]	**110,127**	109,618	108,883	108,344	107,423
Number of transmission substations	**510**	509	508	505	506
Power Generation and Purchases					
Renewables (GWh)[e]	**200,109**	194,154	184,379	185,571	177,949
All generating sources (GWh)	**206,603**	208,156	196,236	195,035	190,513
Proportion of renewables (%)	**97**	93	94	95	93

a) Excludes employees of subsidiaries and joint ventures.

b) Hydro-Québec also has access to almost all the output from Churchill Falls generating station (5,428 MW) and purchases all the output from eight privately owned wind farms with a total installed capacity of 530 MW. In addition, 1,277 MW are available under agreements with other independent suppliers.

c) Total power demand at the annual domestic peak for the winter beginning in December, including interruptible power.

d) These figures include off-grid systems but exclude private systems, lines under construction and 44-kV lines (transmission).

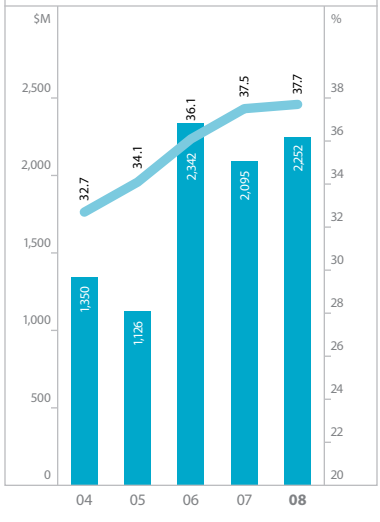
e) Does not include wind energy purchases for which renewable energy certificates were sold to third parties.

Revenue, Average Rate Increase Index and Consumer Price Index

Revenue
Average rate increase index (1998 = 100)
Consumer Price Index (1998 = 100)

Revenue rose by $387 million to $12.7 billion due to electricity sale increases of $77 million in Québec and $302 million outside Québec. Other revenue totaled $353 million, as against $345 million in 2007.

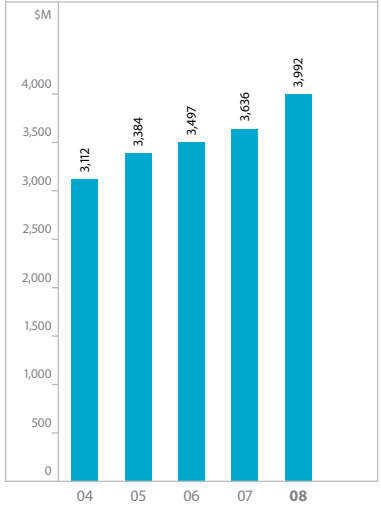
Dividends Declared and Capitalization



Dividends declared
Capitalization

Dividends declared from 2004 to 2008 totaled $9.2 billion.

Investments in Property, Plant and Equipment, Intangible Assets and the EEP[a]



a) EEP: Energy Efficiency Plan

Cash from operations totaled $5.0 billion. This enabled us to pay the dividends of $2,252 million declared for 2007 and to finance a large portion of our investments ($4.0 billion).

Message from the Chairman of the Board

Hard Work Crowned by Success

Hydro-Québec's contributions to Québec society and the economy make it an exemplary corporate citizen.

Michael L. Turcotte

In 2008, Hydro-Québec once again played a critical role in leveraging Québec's energy resources. Extensive experience in the industry enabled the company to make optimum use of the vast power system it has built up over the years to provide top-quality service to all its customers and to increase exports of renewable energy to neighboring markets. In so doing, it has created wealth for all Quebecers.

Given the importance for Hydro-Québec of continuing to develop its generating fleet and transmission capacity while ensuring long-term operability, the Board carefully monitors all of the company's major projects. In 2008, it authorized the company to continue the draft design for the Romaine hydropower project and approved the refurbishment of Gentilly-2 nuclear generating station and the construction of Anne-Hébert substation, among other things.

The Board also took part in working sessions to develop the *Strategic Plan 2009–2013*, which will be filed with the Québec government in the summer of 2009.

With regard to governance, the Board reviewed the mandates of its committees and the expertise and experience profiles used to select new directors. It also received the report on the directors' induction and training program and assessed its own performance. In addition, the Board carefully examined the risk management process and the enterprise risk portfolio.

Apart from the Chairman of the Board and the President and Chief Executive Officer, the Board now has 14 members with different backgrounds, who are active on seven committees. The roles of the directors are many and varied: to advise Management in choosing and implementing strategic directions, to ensure the sound management and profitability of the company, to approve all major projects, and to ensure that such projects remain within budget and comply with the principles of sustainable development. They must also plan for executive succession and oversee the implementation of strategies and policies to maintain qualified personnel in all of the company's lines of business. Lastly, they work closely with the company's executives and, with them, safeguard Hydro-Québec's image and reputation.

I owe a debt of gratitude to all the directors for their great diligence and assiduity; special thanks are due to Hélène F. Fortin, who left the Board in 2008. I am also grateful to Management and to all Hydro-Québec employees for their unfailing commitment and their contribution to the company's strong performance.

Michael L. Turcotte
Chairman of the Board

Hydro-Québec's head office, in Montréal.

Message from the President and Chief Executive Officer

Results We Can Build On

For Hydro-Québec, the keynote of 2008 was outstanding performance, manifested by steadily improving results and achieved against a backdrop of intense activity. The company continued to play a central role in Québec's economic development, particularly in the regions hosting its infrastructure projects.

Net income rose to $3,141 million from $2,907 million in 2007. This 8% increase is mainly attributable to higher net electricity exports, which were up $380 million. In addition, our sales figure grew 3% to reach $12,717 million. These results will enable us to pay dividends of $2,252 million to our shareholder, the Québec government.

Our performance was noteworthy in several other respects: risk management that has proven its worth, smoothly running projects, customers' growing interest in our energy efficiency programs, and the remarkable dedication shown by our employees. In labor relations, seven of the eight unions at Hydro-Québec, representing 91% of our unionized employees, signed new collective agreements. This ensures another five years of the stability we need to achieve our objectives.

Opting for sustainable development

Sustainable development is a critical component of all aspects of our activities: our energy choices, our approach to hydropower development, the integration of wind power into our portfolio of supply options, our careful management and our social commitment. The name of Hydro-Québec has become synonymous with sustainable energy.

Hydroelectricity: A collective resource

To fulfill its responsibility for ensuring Québec's energy future, the company invests several billion dollars every year in developing its generating fleet. In 2008, for example, we commissioned the last generating units at Péribonka (Saguenay–Lac-Saint-Jean) and the first units at Chute-Allard and Rapides-des-Cœurs (Mauricie) generating stations. As well, work at the Eastmain-1-A/Sarcelle/Rupert jobsite, in the Baie-James region, moved ahead according to schedule. This project will enable us to add 8.7 TWh per year to our supply of green energy by 2012. We also completed several key stages in another major project, the Romaine complex (Minganie), with four hydroelectric generating stations slated to come on stream between 2014 and 2020. We filed the environmental impact statement in January, a public hearing on the project was held in the fall, and the review bodies issued a positive recommendation at the beginning of March 2009. We hope to break ground in the second quarter of 2009 on what will then be Canada's largest infrastructure project.

Wind power: A logical complement

Hydro-Québec considers wind power a logical complement to its hydroelectric output. Like hydropower, wind power is a clean, renewable generating option, and one that also provides valuable spinoffs for the communities concerned.

Transmission: Growth combined with reliability

To handle the expansion of our hydroelectric fleet, integrate wind farm output and bolster our transmission capacities, we clearly must develop the grid. In 2008, we invested $559 million in this undertaking, including $249 million to build a 1,250-MW interconnection with Ontario that will allow us to increase our interchanges with neighboring markets starting in 2009. This project alone represents a capital outlay of $654 million. We also devoted $538 million to rolling out state-of-the-art technologies and to efforts to ensure the reliability and long-term operability of our transmission assets.

Hydro-Québec posted outstanding performance in 2008, manifested by steadily improving results and achieved against a backdrop of intense activity.

Thierry Vandal

Being energy-wise: Our customers rise to the challenge

An increasing number of customers are taking advantage of our energy efficiency programs. The response has been so strong that we surpassed our forecasts for the fifth year in a row, with new energy savings of 1.1 TWh; the savings achieved since the Energy Efficiency Plan was introduced in 2003 now total 3.4 TWh. These results attest to the sizable effort we have made to reach our target, which was raised from 4.7 TWh to 5.8 TWh for 2010, and from 8 TWh to 11 TWh for 2015. It bears repeating that every kilowatthour saved represents a gain for all our customers.

Customer satisfaction: An ongoing priority

In January 2008, Hydro-Québec Distribution rolled out the residential portion of the Customer Information System, the last phase in a project to upgrade our information systems. This initiative paves the way for a more thorough integration of customer records and business processes. The division also continued to improve its efficiency with an approach that combines service quality, customer satisfaction and evolving practices. This approach, which has been approved by the Régie de l'énergie, will generate recurring savings. A final highlight was the launch of the Time It Right rate project in four cities. The goal of this pilot project is to determine whether a rate option based on time and season of use encourages customers to shift part of their consumption to low-demand periods.

Intense activity

In 2008, Hydro-Québec Équipement and Société d'énergie de la Baie James were involved in the construction of five hydroelectric generating stations (Péribonka, Eastmain-1-A, Sarcelle, Chute-Allard and Rapides-des-Cœurs) and in about 80 projects to refurbish or refit generating facilities. Their transmission-related workload grew, with a volume of activity of $816 million for about a thousand projects of all types and sizes: building lines and substations, increasing transmission capacities, particularly for interchanges with Ontario, and ensuring long-term operability. Through careful project management, they were able to move up the commissioning dates of several facilities.

Innovation, an important strategic tool

Technological innovation is one of our key strategic orientations. That is the reason we invest $100 million a year in R&D directed by our research institute. In 2008, the institute focused its energies on a hundred or so innovation projects aimed, in particular, at helping our divisions improve the performance of their generating, transmission and distribution facilities.

A joint effort

After such a productive year, it gives us great pride to report on our accomplishments, on the progress made on our projects, and on the continued improvement in our financial results. We owe this outstanding performance to our employees, the energetic men and women across the province who are all working hard to achieve the same goal: to provide Quebecers with a reliable, high-quality supply of electricity. On behalf of Management, I would like to express my heartfelt gratitude for their contribution.

In closing, I would also like to thank the members of the Board of Directors for their commitment to the success of Hydro-Québec.

Thierry Vandal
President and Chief Executive Officer

Hydro-Québec Production

Powering a Future Generated Here

At La Tuque generating station in the Mauricie region, powerhouse mechanic supervisor Alain Drouin and powerhouse mechanic René Marchand use a 36-tonne, digitally controlled tool to perform machining work in a turbine pit. This state-of-the-art machine tool offers an exceptional degree of precision and substantial time savings.

Hydropower: The Driving Force Behind Our Development

Hydro-Québec Production posted another strong performance in 2008. The solid contribution made by our employees allowed several major hydropower projects to reach important milestones—the last generating units at the Péribonka development and the first units at Chute-Allard and Rapides-des-Cœurs came on stream—while work proceeded on a number of fronts at the Eastmain-1-A/Sarcelle/Rupert jobsite. Alongside these construction projects, our teams carried out extensive rehabilitation and maintenance operations needed to ensure the long-term operability of our generating fleet. We also reached agreements with the regional county municipality of Minganie and three Innu communities affected by the planned Romaine complex. A further highlight of the year was Hydro-Québec's announcement of the decision to move ahead with the refurbishment of Gentilly-2 nuclear generating station.

In 2008, we recorded net income of $2,137 million and paid water-power royalties totaling $552 million. Through careful management of our energy reserves, net exports grew to $1,484 million, while our hydraulic reserves remained essentially stable at 116.5 TWh. Once again, our employees played a key role in helping us reach our business objectives, both here in Québec and on neighboring markets.

Our employees' know-how is the key to ensuring that we achieve our goals.

Richard Cacchione
President, Hydro-Québec Production

OUR MISSION Hydro-Québec Production generates electricity to supply the domestic market and sells its excess output on wholesale markets. We also offer balancing and firming capacity services to Hydro-Québec Distribution to offset variations in wind farm output and thereby facilitate the integration of this energy source.

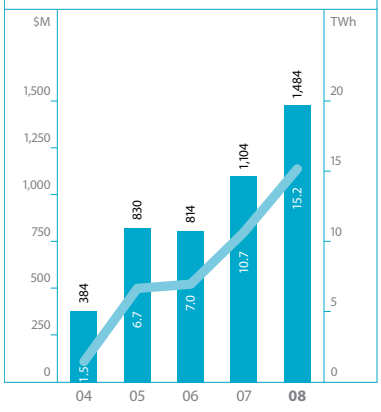
OUR FACILITIES Our generating fleet comprises 58 hydroelectric generating stations, 1 nuclear generating station, 4 thermal generating stations and 1 wind farm, representing assets worth $25.6 billion and installed capacity of 36.3 GW. We also have 26 large reservoirs with a storage capacity of 175 TWh, and more than 570 dams and control structures.

OUR ACTIVITIES We supply Hydro-Québec Distribution with a heritage pool of 165 TWh of electricity per year at 2.79¢/kWh. Above this volume, we sell our output in response to tender calls or short-term needs inside and outside Québec.

2008 IN FIGURES

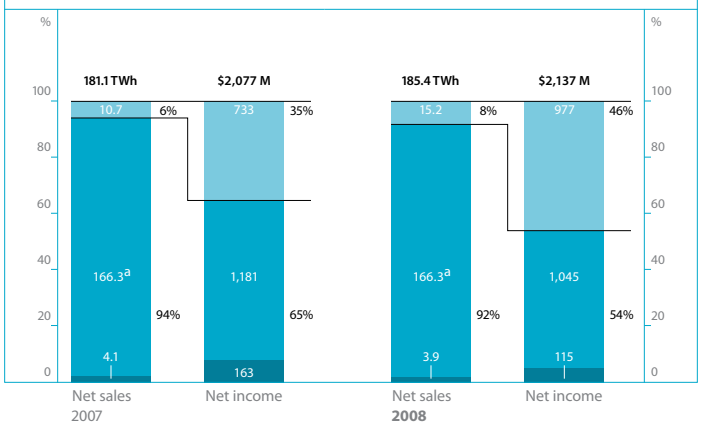
Revenue	$7.0 billion
Net income	$2.1 billion
Customers (% of revenue from electricity sales)	
Hydro-Québec Distribution	72%
Other	28%
Sales volume	
Hydro-Québec Distribution	170.2 TWh
Other	21.1 TWh
Property, plant and equipment as at December 31 (including work in progress)	$29.7 billion
Investments (property, plant and equipment, and intangible assets)	$1.9 billion

Hydro-Québec Production's Net Electricity Exports



- Net contribution (including revenue from energy derivatives) ($M)
- Net reservoir drawdown (TWh)

Hydro-Québec Production's Net Electricity Sales and Income, by Market



- Exports
- Heritage pool – Québec
- Other sales – Québec

a) The difference between this volume and the 165-TWh heritage pool of electricity corresponds to the difference between the actual rate of loss and the rate forecast used in order-in-Council No. 1277-2001.

Making the most of our energy resources

Hydro-Québec Production manages its generating capacity with ever-increasing efficiency in order to maximize profitability. Beyond the heritage pool of electricity reserved for the domestic market, our output may be sold at the best possible price on wholesale markets throughout northeastern North America. Thanks to the flexibility of our hydroelectric generating stations, which can be started up in the space of a few minutes if necessary, we can import electricity when prices on external markets are low and export it when prices are high.

■ Hydro-Québec Production recorded net income of $2,137 million in 2008, up $60 million over 2007, mainly as a result of a $380-million increase in net electricity exports. However, this growth was offset by two factors: an $86-million decline in net results from special contracts with large industrial customers in Québec, and an increase in water-power royalties, which rose to $552 million from $267 million in 2007.

In 2008, net exports by Hydro-Québec Production accounted for only 8% of sales volume, but generated 46% of the division's net income and 32% of the company's income from continuing operations.

■ The volume of electricity sales to Hydro-Québec Distribution totaled 170.2 TWh, down slightly from 171.5 TWh the year before. Net income from the heritage pool and special contracts with large industrial customers in Québec amounted to $1,045 million. Net income from contractual deliveries of baseload and cycling capacity to Hydro-Québec Distribution, spot transactions with this division and other business transactions totaled $115 million.

■ Sales outside Québec generated $1,897 million for 21.1 TWh, versus $1,483 million for 17.5 TWh in 2007. Net exports and the related financial transactions totaled $1,484 million for net reservoir drawdown of 15.2 TWh—a unit contribution of 9.8¢/kWh—compared with $1,104 million and drawdown of 10.7 TWh in 2007. The growth in revenue is largely attributable to the higher volume of sales and favorable market conditions. Net electricity exports and related transactions, less generating, procurement and transmission costs, yielded $977 million in net income, up from $244 million in 2007.

■ As at December 31, 2008, our energy reserves represented 116.5 TWh, comparable to the previous year's level.

■ We operate our facilities in such a way as to maintain a sufficient energy reserve at all times to offset a potential runoff deficit equivalent to 64 TWh over two consecutive years and 98 TWh over four. In compliance with the industry's current reliability criteria, we also keep a capacity reserve approximately 8% higher than our contract commitments.

■ Under the terms of an agreement to integrate the wind power supplied by private producers, we offer Hydro-Québec Distribution

- a balancing service to mitigate the impact of hourly fluctuations in the quantity of wind power carried on the Hydro-Québec TransÉnergie system, and
- firming capacity equal to 35% of the contractual capacity of the wind farms in commercial operation.

The average cost of a kilowatthour in 2008 was 2.2¢. This corresponds to the sum of our generating, procurement and sales costs divided by the net sales volume.

Péribonka hydropower development, in the Saguenay–Lac-Saint-Jean region.

Signing ceremony held in July 2008 for the Nanemessu-Nutashkuan agreement concerning the planned Romaine hydropower complex. Daniel Malec, Negotiator for Nutashkuan, François Bellefleur, Council of the Innu of Nutashkuan, Julie Boulet and Benoît Pelletier, Québec government, and Richard Cacchione, Hydro-Québec Production.

Constantly expanding our generating fleet

In its ongoing development of Québec's hydropower potential, Hydro-Québec Production has commissioned a number of generating facilities in the past few years: Sainte-Marguerite-3 and Rocher-de-Grand-Mère in 2004, Toulnustouc in 2005, Eastmain-1 in 2006, Mercier in 2007, and the last generating units at Péribonka as well as the first units at Chute-Allard and Rapides-des-Cœurs in 2008. All our development projects must meet three fundamental criteria before they can proceed: they must be profitable, environmentally acceptable and favorably received by the communities concerned.

By continuing to develop hydropower, a renewable energy source, we will be able to meet the needs of future generations.

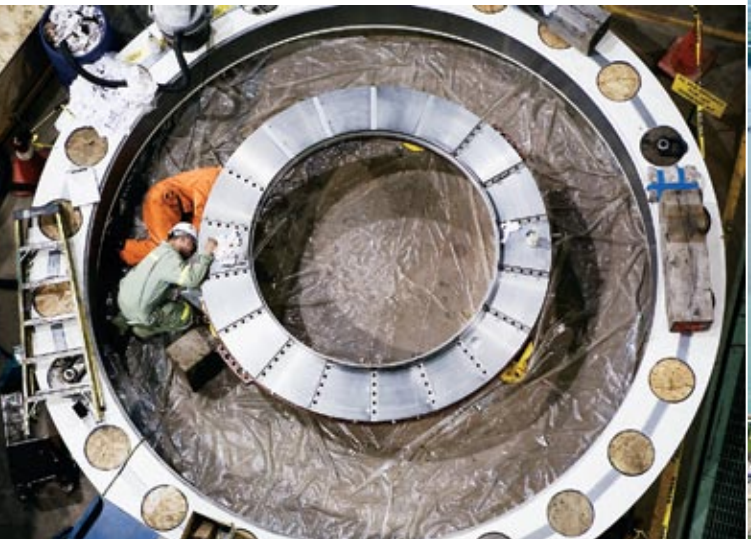
■ In March 2008, the last of the three generating units at Péribonka, in the Saguenay–Lac-Saint-Jean region, went into operation. The total cost of this 385-MW, 2.2-TWh project is $1.4 billion.

■ The Chute-Allard and Rapides-des-Cœurs developments on the Saint-Maurice are nearing completion. Four units have already come on stream: three at Chute-Allard in July, October and December, and one at Rapides-des-Cœurs in October. The eight remaining units will be commissioned in 2009. The two facilities will provide a combined capacity of 138 MW and annual output of 0.9 TWh, and represent a total investment of $1.0 billion.

■ Construction of Eastmain-1-A and Sarcelle powerhouses and the Rupert diversion (Baie-James) is moving forward according to schedule. This project, which will cost $5.0 billion to build, will add 918 MW in installed capacity and 8.7 TWh in annual output, including additional output stemming from the diversion of part of the flow of the Rupert to the La Grande complex. The various structures will commence operation in stages from the end of 2009 to early 2012.

■ Hydro-Québec is planning to build four generating stations with a total installed capacity of 1,550 MW and annual output of 8.0 TWh on the Romaine, north of Havre-Saint-Pierre (Minganie). This $6.5-billion project reached some major milestones in 2008:

- In January, Hydro-Québec filed the environmental impact statement for the project with the authorities concerned. It also signed a partnering agreement with the regional county municipality (RCM) of Minganie intended to maximize project spinoffs for the host communities. Under this agreement, the RCM will receive royalties to be paid in installments until 2070.
- The company went on to sign two similar agreements with local Innu communities: the first in July, with Nutashkuan, and the second in October, with Pakua Shipi and Unamen Shipu. These agreements, likewise set to run until 2070, call for the establishment of funds to finance economic, community and cultural projects, traditional activities and vocational training programs. They also specify community involvement in the construction and environmental follow-up. As well, an understanding in principle was reached with the community of Ekuanitshit in October.
- In line with federal and provincial environmental review procedures, a public hearing on the project was held in the fall. The review bodies issued a positive recommendation on March 5, 2009. Pending the necessary approvals, work will get under way in the second quarter of 2009. Commissioning will take place in stages from 2014 to 2020.



Refitting at Outardes-4 generating station, in the Manicouagan region.

Beauharnois generating station, southwest of Montréal.

Maintaining and upgrading our facilities

In 2008, we devoted $491 million to refurbishment projects designed to ensure the long-term operability of our assets or increase their generating capacity. For this we need detailed knowledge of the condition of each facility, and our employees' expertise plays a critical role in this respect.

We use water to generate 98% of our output.

- Refitting of Outardes-4 generating station (Manicouagan) is nearly complete. The last unit was started up, bringing the additional capacity yielded thus far to 56 MW.
- Rehabilitation proceeded at Beauharnois generating station. This major project will considerably increase annual output.
- In the Mauricie region, phase II of the La Tuque rehabilitation and refitting continued, with the commissioning of a second generating unit. Once completed, the work will add 60 MW to peak capacity.
- Rehabilitation work is ongoing at Rivière-des-Prairies generating station in Montréal.
- In the Manicouagan region, the spherical valves at Manic-5 are undergoing major work to ensure their long-term reliability. This project should be completed by 2011.
- Refurbishment is progressing well at Mercier dam (Outaouais), Melville dam (Mauricie), and Coteau-1, Coteau-3, Île-Juillet-1 and Île-Juillet-2 dams (Montérégie).
- After conducting numerous technical, economic and safety studies, Hydro-Québec decided to extend the service life of Gentilly-2 nuclear generating station, in Bécancour, until 2040. The project will cost an estimated $1.9 billion. Engineering and procurement activities got under way in 2008. The refurbishment itself will begin in 2011, with a view to recommissioning at the end of 2012.

Hydro-Québec Production operates a fleet of 64 generating stations with a total installed capacity of 36.3 GW.

Mercier dam, in the Outaouais region.

At Rivière-des-Prairies generating station, an engineer adjusts one of the components of the multipurpose submersible robot used to determine the condition of embedded parts.

Innovating to improve output

Our collaborative undertakings with our research institute (IREQ) in 2008 were part of a portfolio of about 20 projects worth a total of nearly $19 million.

■ Culminating years of work with IREQ, we launched five tools designed and developed by the institute to optimize operations and efficiency:

- MIDA, a suite of seven diagnostic programs, allows us to accurately gauge the performance of AC generators, rate them on the basis of their degree of wear and consequently better target corrective and preventive maintenance operations.
- A tool for finite element modeling of the mechanical behavior of turbine runners helps reduce the risk of cracking and extends the service life of generating units.
- A software program called Présage is designed to forecast spring runoff, a crucial factor in the fleet's productivity.
- Indicateur is a software tool for assessing the accuracy of runoff forecasting programs.
- RIT is a video inspection robot that detects anomalies in the system used to locate ruptures in the fuel cladding at Gentilly-2 nuclear generating station.

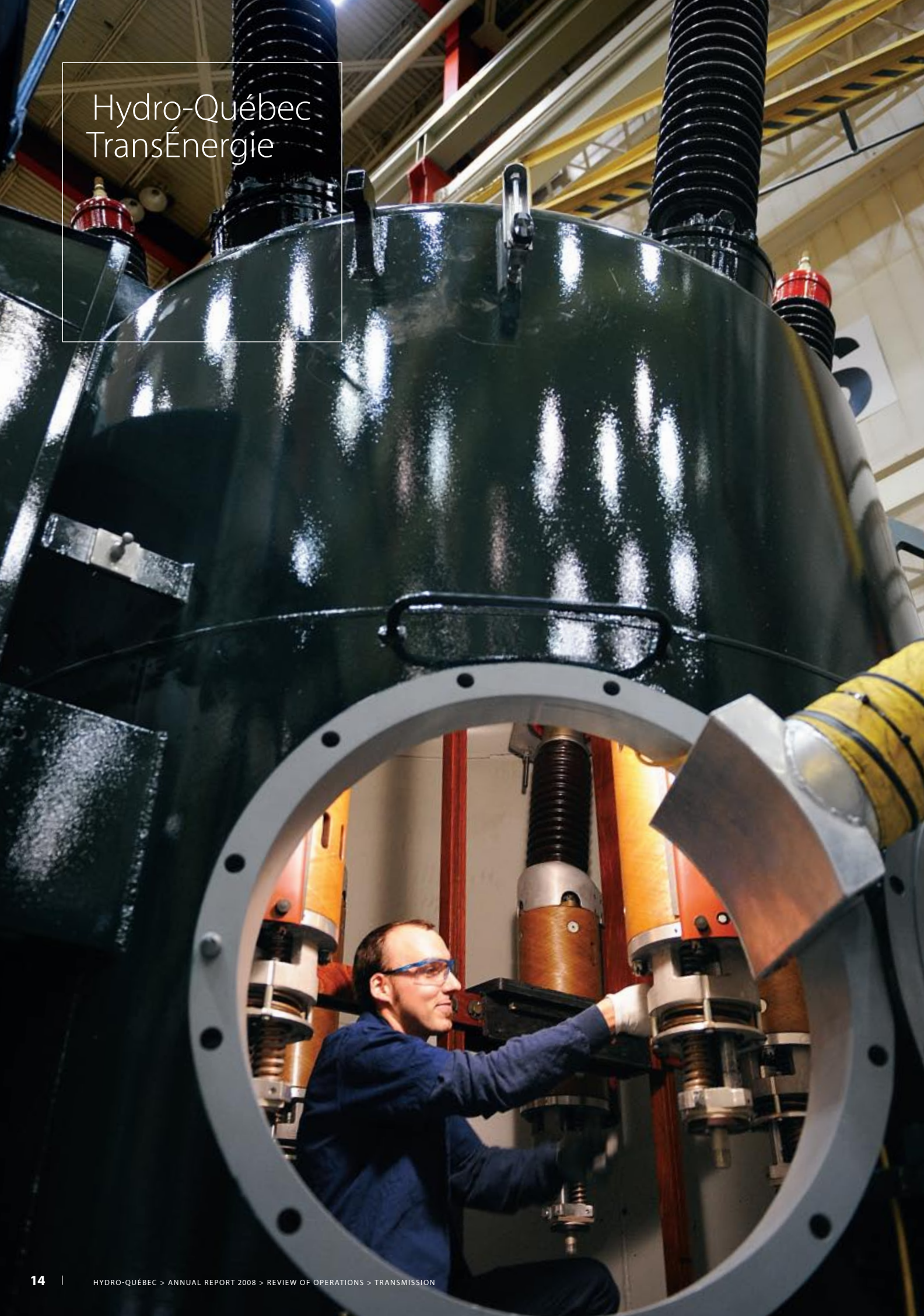
■ With IREQ and industrial partners, we continued to develop various new technologies:

- The GMON (Gamma MONitoring) sensor automatically takes measurements of snow water equivalent and transmits the data in order to improve the accuracy of spring runoff forecasts.
- A multipurpose submersible robot provides an exact picture of the condition of embedded parts (sill, lintel, slots) around gates and stoplogs, with a view to preventing and solving such problems as water leaks and jammed gates or stoplogs. This robot has a 3D scanner designed by Hydro-Québec's research institute, which gives users a 3D view of tasks performed under water.

■ In partnership with the Natural Sciences and Engineering Research Council of Canada and McGill University, we established the NSERC/Hydro-Québec Chair on Precipitation Nowcasting. This chair, to which Hydro-Québec will contribute a total of $750,000 between 2009 and 2013, will enhance our understanding of local precipitation variability and enable us to develop more efficient forecasting tools.

Our investments in technological innovation help optimize our generating assets.

Hydro-Québec TransÉnergie



A Reliable Grid for Powering Our Future

Power system electrician Maxime Larose repairs a circuit breaker in one of the seven equipment overhaul workshops being set up in different parts of Québec. These shops will ensure the long-term operability of our stock of circuit breakers and help us maintain our expertise in this field.

An Evolving System

In 2008, sustained efforts once again went into developing the transmission system in order to meet the dual imperative of integrating new generating facilities and bolstering the capacity of our interconnections with neighboring systems.

In recent years, we have deployed many different means to ensure system reliability and long-term operability. In 2008, for example, we devoted considerable resources to strengthening our facilities and rolling out state-of-the-art technologies. Our excellent record of service continuity is evidence that our efforts are bearing fruit. At the same time, our Direction du contrôle des mouvements d'énergie, which was designated Reliability Coordinator for Québec in 2007, continued to prepare for the 2009 filing of reliability standards that will apply to transmission systems throughout the province.

The ongoing development of the system raises a great many complex challenges. To meet them, we are counting on the know-how of our dedicated workforce and the implementation of best management practices. Preserving our knowledge capital is critical in this context. That is why we have launched various initiatives to maintain and develop our employees' skills.

The commitment and expertise of our employees are reflected in remarkable continuity of service.

Isabelle Courville
President, Hydro-Québec TransÉnergie

OUR MISSION Hydro-Québec TransÉnergie operates the most extensive transmission system in North America. It markets system capacity and manages power flows throughout Québec. In addition, the division's Direction du contrôle des mouvements d'énergie (system control unit) is the designated Reliability Coordinator for Québec.

OUR FACILITIES Our system comprises 33,058 km of lines and 510 substations, as well as interconnections with the systems in Ontario, New Brunswick and the U.S. Northeast. We stringently apply our rates and conditions of service to ensure non-discriminatory access to our system, in compliance with North American regulatory provisions.

2008 IN FIGURES

Revenue	$2.8 billion
Net income	$481 million
Customers (% of revenue)	
Hydro-Québec Distribution (native load transmission service)	89%
North American wholesalers (point-to-point transmission services)	7%
Other	4%
Property, plant and equipment as at December 31 (including work in progress)	$16.3 billion
Investments (property, plant and equipment, and intangible assets)	$1.1 billion

Robin Larouche, power system electrician, working at Dubuc substation to bring Péribonka generating station onto the grid (Saguenay–Lac-Saint-Jean).

Carleton substation (Gaspésie).

A 230-kV line links Carleton wind farm to the grid.

Developing the system

We invested $559 million in developing the system in 2008. Among other projects, we integrated new hydroelectric and wind power facilities, and continued work on the 1,250-MW interconnection with Ontario, which will increase our interchange capacity.

In 2008, our transmission system grew by 50 km.

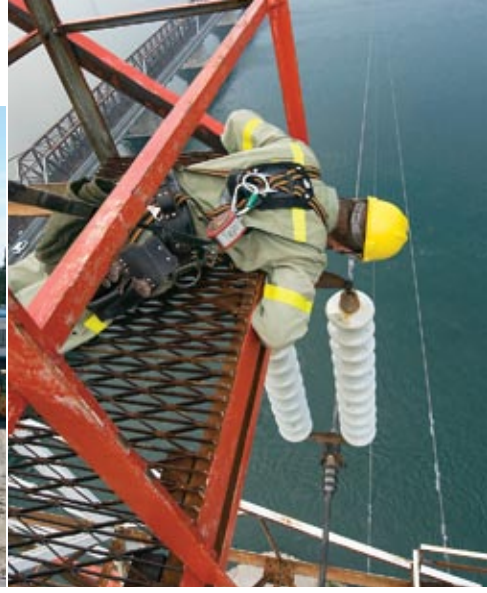
- In Saguenay–Lac-Saint-Jean, we finished work to connect Péribonka generating station to Dubuc, Chicoutimi, Chicoutimi-Nord and Saguenay substations, for a total investment of $171 million, including $14 million in 2008.
- We completed a $108-million project to bring Chute-Allard and Rapides-des-Cœurs generating stations (Haute-Mauricie) onto the grid, thereby allowing their first units to come on stream. The remaining units should be connected in 2009.
- The $20-million, 120/25-kV Wemindji substation (Baie-James) went into operation.
- The 120/25-kV Saint-Lin substation and the 25-km, 120-kV Paquin–Saint-Lin line went into operation—altogether, a $42-million investment (Laurentides).
- In Montréal, we rebuilt two 120-kV underground lines, Beaumont–Dorchester (6 km) and Berri–De Lorimier (2 km), for a total of $22 million.
- The 6-km, 230-kV Sorel–Tracy line (Montérégie) was rebuilt at a cost of $13 million.
- In the Outaouais region, we commissioned an 11-km, 120-kV line to supply ERCO Worldwide at a cost of $12 million.
- We broke ground on the 120/25-kV Mont-Tremblant substation in the Laurentian mountains, and on two 120-kV lines that will run a total of 14 km. The project will cost an estimated $52 million.
- A $30-million project got under way to construct the 120/25-kV Vaudreuil-Soulanges substation and loop the Dorion–Rigaud line in order to bring the substation onto the grid (Montérégie).
- Carleton substation (69/25/12 kV, Gaspésie) was rebuilt and returned to service at a cost of $10 million.
- We carried out several other projects in the Gaspésie and Bas-Saint-Laurent regions in order to integrate the initial 990 MW of wind power:
  - We erected a 230-kV line to connect the 109.5-MW Carleton wind farm, for a total of $33 million.
  - Construction proceeded on the 63-km, 230-kV Rimouski–Les Boules line, scheduled for completion in 2009, at an estimated cost of $73 million.
  - The new 7-km, 230-kV Saint-Ulric–Saint-Léandre line, also due to be commissioned in 2009, is expected to cost $8 million.
  - A project to upgrade the Matapédia regional grid cost $33 million.

Investment in the Transmission System ($M)

	2004	2005	2006	2007	**2008**
System development	165	337	416	349	**559**
Reliability and long-term operability of assets	388	447	524	495	**538**
Total	553	784	940	844	**1,097**

The 230-kV line that will be used for interchanges with Ontario.

Wemindji substation in the Baie-James region.



Inspecting a support structure on the river crossing between Montréal and Saint-Lambert.

■ Construction of the 315/230-kV Outaouais substation, part of the $654-million project to build a 1,250-MW interconnection with Ontario, made good progress and should be completed in 2009. We finished building the 230-kV line to Ontario and secured approval to construct the approximately 115-km, 315-kV Chénier–Outaouais line in an existing right-of-way in order to reinforce the interconnection.

■ In October, the Régie de l'énergie gave the green light to build Anne-Hébert substation (315/25 kV) near the city of Québec, as well as a line connecting it to the grid. The $84-million project is slated for commissioning in 2011.

■ In December, the Régie approved the construction of the facilities required to link Eastmain-1-A and Sarcelle powerhouses to the transmission grid, at a total cost of $191 million.

Reliability and long-term operability

To provide high-quality electrical service throughout the province, we must not only expand the system but also strengthen it and ensure its long-term operability. In 2008, we invested $538 million in refurbishing and upgrading our facilities and integrating state-of-the-art technologies. This investment is meant to achieve three goals: ensure system reliability, see that our facilities remain in compliance with the applicable regulatory provisions and, above all, meet customer expectations. In addition, our Direction du contrôle des mouvements d'énergie, with the approval of the Régie de l'énergie, continued its preparations for the 2009 filing of reliability standards for Québec.

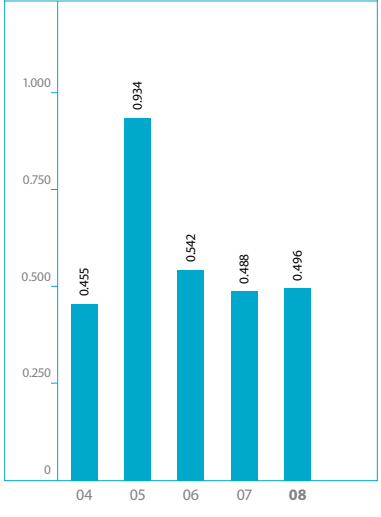
■ The average service interruption duration per customer rose slightly from 0.488 hours in 2007 to 0.496 hours in 2008—a good score relative to our target of 0.600 hours per year.

■ At Lévis substation, near the city of Québec, we commissioned de-icing equipment that will improve system reliability at a cost of $183 million.

■ Also at Lévis substation, we finished refurbishing the second synchronous condenser and will commission it in 2009. The total cost of the two condensers is $33 million.

■ We completed an $18-million overhaul of the 161/25-kV Jonquière substation (Saguenay–Lac-Saint-Jean).

Average Interruption Duration (hours)



During a cold snap in Montréal, a dense cloud of steam fog rises from the St. Lawrence River. Electricity demand reached a new peak on the morning of January 16, 2009.

Valve room at Lévis substation, where alternating current is converted to direct current.

- A $79-million project to refurbish and expand the 315/161/69-kV Hauterive substation made steady progress (Côte-Nord).
- The $54-million refurbishment of Sorel substation (230/120/25 kV) continued and will run until 2010.
- In the northwestern part of Montréal, the 315/25-kV Saraguay substation is being enlarged in a $39-million project due for completion in 2009.
- Also in Montréal, we broke ground on a $17-million project to refurbish and expand the 120/25/12-kV Laurent substation, scheduled for completion in 2011.
- In Abitibi-Témiscamingue, we commenced a $38-million overhaul of the 120/13.8-kV Rapide-2 and Rapide-7 substations that should be finished in 2010.
- In Montérégie, work got under way to boost the transformer capacity of the 120/25-kV Saint-Maxime substation, at an estimated cost of $42 million.
- We concluded the engineering and procurement portion of a $19-million project to rebuild the 120/25-kV Gatineau substation, in the Outaouais region, with a view to a 2009 recommissioning.
- In various regions of Québec, we continued the process of setting up seven circuit breaker overhaul workshops. These shops will enable us to ensure the long-term operability of our stock of circuit breakers and maintain our expertise in this field.
- To help the Direction du contrôle des mouvements d'énergie fulfill its role as Reliability Coordinator for Québec, we mapped the functions defined by the North American Electric Reliability Corporation (NERC) reliability model to our domestic context. These functions (generating and transmission facility operation, load balancing, etc.) are essential to maintaining the reliability of the bulk transmission grid. We determined which reliability standards apply to each function, prepared a register of facilities and entities covered by each standard, and informed these entities of the standards applicable to each function they perform. We also drew up guidelines for determining the sanctions for violations and coordinated the establishment of compliance monitoring/enforcement mechanisms, as prescribed by NERC and the Northeast Power Coordinating Council (NPCC).

The 2008–2009 winter peak load—a record 37,230 MW—occurred on January 16, 2009, at 8 a.m.

Vegetation control in a transmission line right-of-way. These operations enhance service continuity by helping to prevent line damage.

Improving transmission service through innovation

In 2008, we invested $19 million in developing or adapting innovations in order to optimize system performance and ensure long-term operability. We carry out our innovation initiatives in collaboration with the Hydro-Québec research institute and with specialized research centres and firms.

- We are working on a project called IMAGINE that uses automated maintenance and remote monitoring data management to improve system management efficiency. Through digital technologies such as remote monitoring, telemetering and remote uploading and diagnostics, we can better target our maintenance operations and perform some of them remotely. We connected eight substations to a remote maintenance centre in 2008; most of our substations should be similarly linked within the next 10 years.

- We developed an acoustic system for locating winding hot-spots and partial discharges. This system allows us to diagnose energized transformers and confirm signs of anomalies, thus facilitating decision making regarding any repairs needed.

- We developed a model H-frame without crossarms for easier maintenance. We have also developed steel H-frames that will be good replacements for wooden models, especially in hard-to-reach locations or in areas frequented by woodpeckers.

- By 2015, we will be carrying about 4,000 MW of wind power over the transmission system. To integrate wind farm output under optimal conditions, we are conducting extensive modeling and simulation. We have developed an aggregation technique that allows us to simulate an entire wind farm with only a few turbines.

Technological innovation plays a vital role in upholding our leadership in the field of transmission.

- At Péribonka generating station, we tested a method for measuring ground impedance on live power lines. This technique could mean substantial savings over the conventional method, which can only be used on de-energized equipment.

Hydro-Québec Distribution

Powering an Energy-Efficient Future

Cable worker Nadia Lavoie performs maintenance work on an underground distribution line. In recent years, Hydro-Québec cable workers have been testing various ways of reducing their ecological footprint.

Reliable, Efficient Service

In 2008, we continued to invest in maintaining and developing the distribution system, in line with our objective of continuously improving performance.

In addition, we kept up our efforts to maximize the potential of our Customer Information System, the last stage of which was implemented in January 2008. This platform, which replaces 200 customer systems that had reached the end of their useful lives, will make it easier to provide quality services at the lowest possible cost, thanks to better integration of business processes and customer data. At the same time, we introduced new Conditions of Electricity Service to serve all our customers better and streamline customer service.

To meet our commitment to sustainable development and ensure a secure supply of electricity, we rely on a diversified energy portfolio, with an accent on renewable energies, particularly wind power. On the energy efficiency front, we exceeded our objective for the fifth year in a row thanks to our employees' innovative efforts to develop programs adapted to our customers' needs. We are now aiming at savings of 5.8 TWh in 2010 as we move toward our 2015 target, which was raised from 8 TWh to 11 TWh.

We do our utmost to meet the needs of our customers.

André Boulanger
President, Hydro-Québec Distribution

OUR MISSION Hydro-Québec Distribution ensures a secure supply of electricity and delivers high-quality service throughout Québec.

OUR FACILITIES The division operates 110,127 km of lines, a nine-location customer relations centre providing telephone and online services, and five distribution control centres, as well as one hydroelectric generating station and 23 thermal generating stations supplying customers on off-grid systems.

OUR ACTIVITIES To serve the domestic market, Hydro-Québec Distribution relies primarily on the heritage pool of 165 TWh, which it purchases from Hydro-Québec Production at a fixed price of 2.79¢/kWh. To meet demand beyond that volume, it purchases electricity under market conditions. The division ensures that the distribution system operates efficiently and safely at all times. It offers customers products and services tailored to their needs, as well as a wide range of energy efficiency programs.

2008 IN FIGURES

Revenue	$10.6 billion
Net income	$421 million
Customers (% of revenue)	
Residential customers	52%
Commercial and business customers	19%
Large-power customers	29%
Property, plant and equipment as at December 31 (including work in progress)	$8.5 billion
Investments (property, plant and equipment, and intangible assets)	$664 million

CREDIT: CANWEA

Announcement of the awarding of 15 contracts to supply 2,005 MW of wind power. Claude Béchard, Québec Minister of Natural Resources and Wildlife; Jean Charest, Premier of Québec; and Thierry Vandal, President and CEO of Hydro-Québec.

Group Leadership Award of the Canadian Wind Energy Association (CanWEA). Representing CanWEA, Robert Hornung, President, and Joyce McLean, Chair of the Board of Directors, are shown with Éric Chaîné and Mario Boucher of Hydro-Québec.

A flexible portfolio

Hydro-Québec Distribution manages procurement so as to ensure a reliable supply of electricity at the lowest possible cost. Our flexible and diversified energy portfolio gives us the latitude needed to deal with fluctuations in demand. For example, in 2008, we initiated or renewed measures to suspend or defer contracted deliveries that exceeded the requirements of the Québec market.

Managing our supplies with maximum efficiency is an ongoing priority.

- In the fall of 2008, the Régie de l'énergie approved the 2008–2017 Electricity Supply Plan. In it, we present our procurement strategies based on domestic demand forecasts for the next decade. Given the decline in demand, we took the following measures to ensure a balance:
  - In May, the Régie approved the agreements we signed with Hydro-Québec Production to defer a portion of the contract deliveries scheduled for 2008–2011. These deliveries have been carried over to 2012–2020.
  - Following a decision by the Régie in September, we renewed for another year (2009) the suspension of deliveries from TransCanada Energy's Bécancour generating station.
  - We sold 430 GWh of surplus energy on short-term markets.
- In October, the Régie de l'énergie approved 15 contracts resulting from the 2005 call for 2,000 MW of wind power generated in Québec. The wind farms (2,005 MW in total) will come on stream between 2011 and 2015. Under these contracts and upcoming tender calls, Hydro-Québec Distribution's wind power supplies will amount to approximately 3,500 MW by 2015.
- At its 24th annual conference and trade show, the Canadian Wind Energy Association (CanWEA) presented its Group Leadership Award to Hydro-Québec for efforts in developing wind power. As CanWEA noted during the awards ceremony, "the government-owned business corporation demonstrated exemplary integrity, rigor and transparency in its contract awarding process" for its 2,000-MW tender call.
- In November, deliveries began from the Carleton wind farm, the third of the eight wind farms slated to go into operation in the Gaspésie region by the end of 2012 as a result of the 2003 call for 1,000 MW. The wind farms in operation now have a total installed capacity of 319.5 MW.
- In December, Tembec began deliveries of forest biomass power under an 8.1-MW supply contract. Taking into account deliveries from Kruger and Bowater Canadian Forest Products, biomass now accounts for 44 MW of total capacity.
- In February 2008, the Régie de l'énergie approved a 2.9% across-the-board rate adjustment, effective April 1, 2008.

The city of Rivière-du-Loup won top honors in the ENERGY WISE Competition of Excellence for its energy-efficient sports complex, Centre Premier Tech. Shown here are city officials Marc-Émile Dionne and Pierre LeBel and Mayor Michel Morin.

Balcan Plastics is now a member of the Energy Savers' Circle. Guillermo Franco, head of the firm's energy division (right), is shown with André Boulanger, President, Hydro-Québec Distribution.

Hydro-Québec encourages communities to promote the ENERGY WISE Home Diagnostic program with its Go with the Flow campaign. The photo shows Yves Lévesque, Mayor of Trois-Rivières, and Lynda Laquerre of Hydro-Québec.

Energy efficiency: A key component of demand-side management

In 2008, Hydro-Québec Distribution continued its efforts to promote energy efficiency, increasing the number of its programs and stepping up customer awareness activities. Since the division must go to the markets to meet needs exceeding the heritage pool, it seeks to slow the growth of energy consumption in order to reduce supply costs. This strategy benefits all customers and demonstrates our commitment to sustainable development.

Customers in all categories responded favorably to our energy efficiency programs again this year.

Our energy efficiency programs are increasingly popular with customers. In 2008, we surpassed the targets for the fifth consecutive year, achieving savings of 1.1 TWh. Savings since the Energy Efficiency Plan was launched in 2003 now total 3.4 TWh.

■ In June 2008, for the second year in a row, we received two awards from the Canadian government for our efforts to promote ENERGY STAR® certification under the ENERGY WISE programs.

■ We attach great importance to acknowledging the efforts of those business customers and partners who have played a crucial role in helping us achieve our energy efficiency objectives.

□ In the first ENERGY WISE Competition of Excellence, Hydro-Québec gave out roughly 60 awards to customers and partners who achieved exceptional results in energy efficiency. The winners' combined efforts resulted in energy savings of 85 GWh, which is slightly more than the annual residential consumption of the town of Magog.

□ Established in 2005, the Energy Savers' Circle recognizes large-power customers who are particularly proactive in their energy conservation efforts. In 2008, it welcomed 12 new members who took steps to cut their electricity consumption by at least 5% or to save at least 50 GWh per year. The Circle now boasts 27 members.

■ We enlisted the help of local and regional governments to promote our ENERGY WISE Home Diagnostic. Under the Go with the Flow initiative, we make a financial contribution to the community for each household that fills out the questionnaire. The funds must be used for a community project in the area of culture, sports and recreation, environment or community activities. In all, 230 communities have joined the program since it was launched in late 2007. In addition, the campaign promoting the Go with the Flow program received top honors at the 2008 gala of the Association du marketing relationnel, garnering golds in the integrated multimedia and consumer products and services categories.

■ Hydro-Québec introduced the RECYC-FRIGO Environnement™ program for old, energy-guzzling refrigerators and freezers. The program has two objectives: first, to collect 230,000 fridges and freezers by 2010, for total energy savings of roughly 180 GWh, and, second, to recycle 95% of the materials in these appliances and dispose of the hazardous materials (CFCs, mercury, etc.) in accordance with the strictest environmental standards. The program has been extremely successful, with nearly 66,500 appliances collected in 2008, compared with the target of 50,500.

■ For several years, Hydro-Québec has offered rebates and other incentives to customers in all categories to encourage the adoption of energy-efficient products. These initiatives have transformed certain markets, as seen in the significantly increased penetration rate for energy-efficient lighting.

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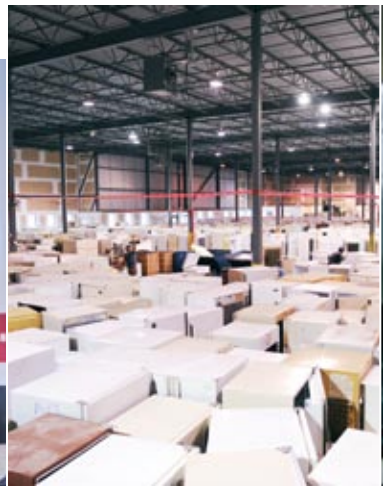
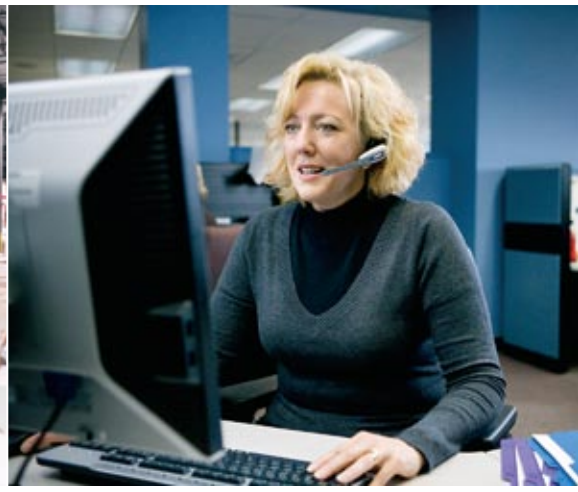
Carminé De Benedictis, Hydro-Québec, and André Caron, Fédération des commissions scolaires du Québec, sign an agreement to encourage energy-saving measures in Québec's public schools.



Under the RECYC-FRIGO Environnement program, energy-guzzling refrigerators and freezers are collected and recycled.



The Customer Information System helps us to manage our customer files more efficiently. Shown here is Diane Turcotte, customer service representative.

■ Hydro-Québec signed an agreement with the Fédération des commissions scolaires du Québec to promote conservation measures in public schools. Under the program, school boards will receive funding for expert assistance in designing and implementing energy efficiency projects.

■ In 2008, under the Empower Programs for Building Optimization and for Industrial Systems, we funded 634 projects resulting in total savings of 191 GWh, as against 606 projects in 2007.

■ In 2008, large-power customers accounted for more than one-third of the savings achieved under our energy efficiency programs, with 144 projects generating annual savings of 430 GWh. To date, 81% of large-power customers have participated in at least one of our programs (76% in 2007).

■ Under our programs for large-power customers, we paid out roughly $1.3 million to IBM Canada for its Bromont plant and $825,000 to SGL Canada for its Lachute plant. The energy savings achieved by the two firms total 20 GWh annually, or the average annual consumption of roughly 1,200 households.

In touch with our customers

In providing services to our customers, we aim for quality at the lowest possible cost.

In 2008, we launched the residential portion of the Customer Information System (CIS), the final stage of our extensive project to integrate management of our customer files.

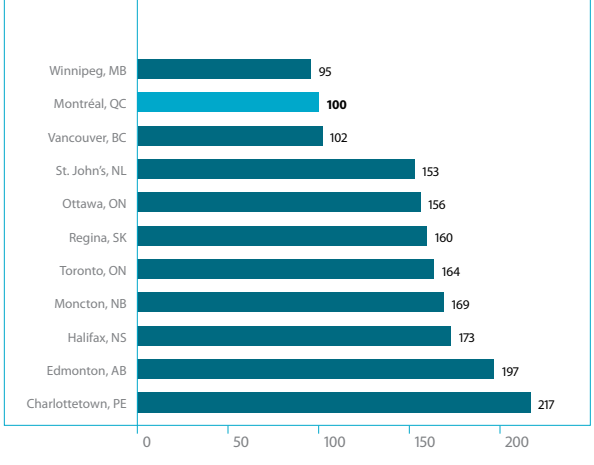
We also implemented an integrated efficiency improvement plan that strikes a balance between quality service, customer satisfaction and evolving practices. Approved by the Régie de l'énergie, the plan will help us achieve recurring annual savings.

RESIDENTIAL CUSTOMERS

■ According to our surveys, the residential customer satisfaction index rose to 7.49 on a scale of 10, compared with 7.45 in 2007. This continued high level of satisfaction despite the disruption resulting from the implementation of the third and final stage in the CIS shows that we paid close attention to our customers' concerns. For example, the new design for Equalized Payments Plan bills was modified in response to customers' comments.

■ To ensure quality service while observing the principles of sustainable development, we continued to expand and promote our self-service options, including automated voice response and Web-based services.

Comparative Index of Electricity Prices at April 1, 2008
Residential Customers[a]



a) Monthly bill (before taxes) for a consumption of 1,000 kWh.

IBM Canada receives funding for energy efficiency projects at its Bromont plant. Bruno Gingras, Hydro-Québec; Peter Bisset, Site Operations Manager, IBM Bromont; Raymond Leduc, General Manager, IBM Bromont; and Daniel Paquin, Hydro-Québec.

Engineers Sébastien Filteau-Gingras and Jean Joly show one of the smart meters tested in the "Time It Right" rate project.

- After the rollout of the CIS, we optimized the processing of change-of-address notifications on the Personal Page of our Web site. In addition, customers can now enter this information through our interactive voice response system, which is accessible 24/7. In 2008, 143,000 out of 1.3 million transactions were carried out using these two services.
- In 2008, over 85,000 customers signed up for online billing, which brought the total number of residential customers not receiving printed bills to roughly 275,000.

■ In a context marked by the high cost of fossil fuels, we received over 8,000 applications for the dual-energy rate (Rate DT) in 2008, a fourfold increase over 2007.

■ Since 2001, we have offered special payment arrangements to low-income customers who are having trouble paying their electricity bills. In 2008, we entered into 21,909 such arrangements, for arrears of $149 million. In addition, Hydro-Québec is working with various organizations to develop practical solutions for these customers.

■ In December, we launched the "Time It Right" rate project in Saint-Jean-sur-Richelieu, Sept-Îles, Val-d'Or and Trois-Rivières. The aim of this two-year pilot project is to determine if time-of-use rates, in which the price charged for electricity varies according to the time of day and season, will encourage customers to switch part of their consumption to off-peak hours. The project required the installation of an advanced mesh network of 2,646 smart meters and displays.

COMMERCIAL AND BUSINESS CUSTOMERS

■ Satisfaction indexes for commercial and business customers remained stable in 2008 at 7.56 and 7.24, versus 7.60 and 7.21 at the end of the previous year.

■ In the spring of 2008, a hydronic ThermElect heating system was installed at Du Rocher high school in Grand-Mère. Designed by the energy technologies laboratory of Hydro-Québec's research institute in collaboration with Steffes Corporation in the U.S., this electrical thermal storage system accumulates heat in ceramic bricks during the night, when power demand is lower, and discharges it during the day to reduce heating costs.

LARGE-POWER CUSTOMERS

Industrial, commercial and institutional customers with a power demand of 5 MW or more consume 40% of the electricity distributed in Québec.

■ In 2008, the satisfaction index for large-power customers rose to 9.20 out of 10, compared with 9.15 in 2007.

■ In September, the city of Salaberry-de-Valleyfield inaugurated its first organic sludge treatment facility using plasma-assisted sludge oxidation (PASO) technology patented by Hydro-Québec and marketed by Québec-based Fabgroups Technologies. Cheaper and more energy-efficient than landfilling, this process uses a rotary kiln equipped with a plasma torch. The very high combustion temperatures reached in the kiln will allow the city to reduce its annual greenhouse gas (GHG) emissions by 2,400 tonnes. In addition, the heat produced by the kiln can be recovered for other uses such as power generation and water heating.

Alain Moreau, a researcher at the energy technologies laboratory of Hydro-Québec's research institute, played a key role in developing the ThermElect hydronic system.

Line workers François Pelletier (left) and Jean Turcotte (right), and line crew chiefs Jean Ouimet and Denis Morin (centre left and centre right), pose in front of a control panel they installed as part of the distribution system automation program.

Bolstering power system reliability

Improving the overall performance of our system is an ongoing priority. In 2008, we integrated new technologies and modified some of our practices to improve service continuity and quality. We also allocated additional resources to maintaining and ensuring the long-term operability of our assets, while working hard to keep up with the increased demand for hookups.

- The normalized system average interruption duration index was 131 minutes per customer in 2008, which is comparable to 2007.

- We continued the system automation program, aimed at reducing the duration of service interruptions. The program involves installing remote-controlled equipment at strategic points on the system to remotely detect outages and speed up service restoration. In 2008, we installed roughly 600 such units, bringing the total number to over 1,000.

We are continuing to develop the system while ensuring service continuity.

- We completed more than 54,000 new hookups on schedule.

- All affected customers received advance notice of scheduled outages, and the work was carried out on time in 89% of cases. We are relying on new follow-up mechanisms to improve our performance in this area.

- In March 2008, the Régie de l'énergie approved the new Conditions of Electricity Service, which went into effect on April 1, 2008, replacing Bylaw 634. This will enable us to continue providing quality services while meeting requirements for efficiency, fairness and simplicity.

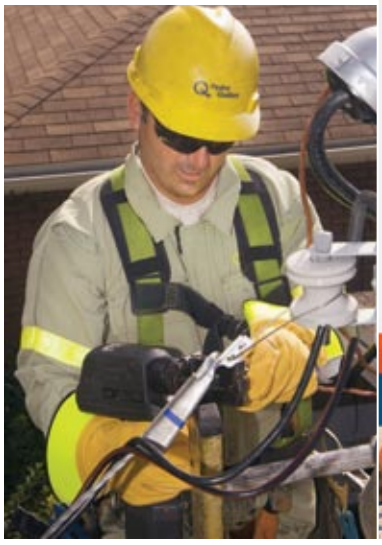
- We broke ground on a thermal generating station in the Northern Village of Kuujjuaq to replace the existing plant, which will not be able to meet demand beyond 2010. The new plant will be equipped with more efficient diesel units that will mean savings of 110,000 to 180,000 litres of fuel per year, and will also help cut GHG emissions by 300 tonnes by 2011 and 490 tonnes by 2030.

- Hydro-Québec Distribution introduced energy efficiency measures at Îles-de-la-Madeleine thermal generating station, resulting in savings of 1.4 GWh in 2008. This will allow us to reduce our annual GHG emissions by 959 tonnes.

- After taking over the Schefferville transmission and distribution system in late 2007, Hydro-Québec Distribution signed a two-year contract in 2008 with Kawawachikamach Energy Services Inc. (KESI) to operate and maintain the system. KESI, which is owned by the Naskapi Nation, will also be responsible for meter reading and some customer service operations. This agreement with a local community is the first of its kind for Hydro-Québec Distribution.

- In 2007, we instituted a program to prevent work-related accidents, the primary objective of which is to remind all employees to think safety while going about their duties. This initiative has had a positive impact, with accident frequency decreasing from 4.64 in 2006 to 3.96 in 2008. The target is a 25% improvement by 2011, compared with 2006.

- In April, ISO 14001 certification was renewed for the third time for all Hydro-Québec Distribution units.



Stéphane Paris, line crew chief, connects a customer's home to the overhead system.

Program to prevent work-related accidents.

The new Hôtel Alt, which is designed according to the principles of "ecotecture," or sustainable architecture, benefited from Hydro-Québec's energy efficiency initiatives. The hotel is in the Quartier DIX30 shopping complex in Brossard.

Improving distribution service and energy efficiency through innovation

Innovation is the key to ensuring the long-term operability of our equipment, enhancing system performance and reliability and improving the energy efficiency of company and customer facilities. In 2008, we invested close to $18.5 million in 51 projects assigned to Hydro-Québec's research institute (IREQ).

- A new partial discharge locator developed by IREQ was patented and installed in 2008.
- As part of a pilot project, we successfully tested a new fault locating process on underground lines. Based on the SimLoc technology developed at IREQ, the process creates very little disturbance for the equipment, making fault location not only quicker but much less damaging to the lines.
- We worked on predictive maintenance tools for overhead and underground lines, including the MILE system (intelligent power line maintenance) developed with IREQ. The technology, which consists of a metering system, a Web interface and fault location and predictive maintenance modules, was installed on five new power distribution lines.
- In cooperation with IREQ, we developed simulation software to estimate building energy and power requirements. Our longer-term objective is to develop an integrated simulation tool for building design, renovation and diagnostics, to increase energy efficiency.
- We continued work on a pilot project to test a new type of three-element water heater that draws less power than conventional models. The results of tests in 75 households confirmed those obtained in the laboratory.
- In partnership with the Natural Sciences and Engineering Research Council of Canada and McGill University, we created the NSERC/Hydro-Québec Chair on the integration of renewable energies and distributed generation into a distribution system. Hydro-Québec will provide a total of $750,000 in funding for this chair from 2009 to 2013.

Hydro-Québec Équipement and SEBJ

Solid Foundations for Powering our Future

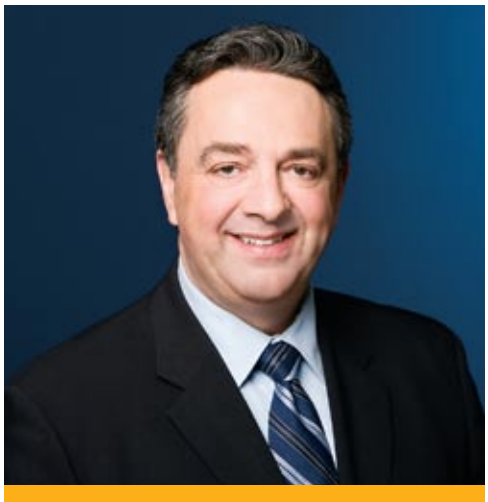
Transfer tunnel that will link the Rupert forebay and tailbay, in the Baie-James region. This key structure in the Rupert diversion will greatly reduce the land area flooded.

Expertise and Innovation: A Winning Combination

In 2008, Hydro-Québec Équipement and Société d'énergie de la Baie James (SEBJ) were in charge of more than a thousand jobsites in Québec. The dedication and know-how of our teams enabled them to keep up a steady pace of work and meet very tight schedules. This performance is all the more remarkable given the formidable challenge of ensuring supplies for the jobsites when there are so many major infrastructure projects under way all over the world.

We reached some important landmarks in our generation projects. In the Saguenay–Lac-Saint-Jean region, the last units at Péribonka generating station went into operation. In the Mauricie, work continued at Chute-Allard and Rapides-des-Cœurs. In the Baie-James region, the Eastmain-1-A/Sarcelle/Rupert jobsite got up to speed, and we achieved a North American first by using asphalt concrete as the watertight core in Nemiscau-1 dam. We plan to apply the same technique in building various dikes and dams in the future Romaine complex, in the Minganie region, which was the subject of a public hearing last fall.

At the same time, we focused considerable energy on extending and reinforcing the transmission grid. Among the many undertakings completed in 2008 were new transmission lines and substations in several regions, including projects designed to integrate the output of wind farms in the Gaspésie region. We also continued work on a host of line and substation refurbishment projects to ensure system reliability and long-term operability.



The secret of our success lies in our expertise, our innovative ability and our record of honoring our commitments.

Réal Laporte
President, Hydro-Québec Équipement
President and Chief Executive Officer,
Société d'énergie de la Baie James

OUR MISSION Hydro-Québec Équipement and Société d'énergie de la Baie James design, engineer and carry out projects for the construction and refurbishment of generating and transmission facilities that meet the needs of their customers, Hydro-Québec Production and Hydro-Québec TransÉnergie, and that are of greatest benefit to the company. They offer high-quality, cost-effective solutions that apply best practices in social and environmental acceptability and that involve the participation of communities and industry.

OUR ACTIVITIES Our services cover all project stages and aspects: geospatial data and mapping, field surveys, study of the biophysical and human environment, engineering, construction, manufacturing quality assurance, and project management up to handover to the operator. We are constantly seeking new ways to maximize facility performance while reducing costs and construction time.

2008 IN FIGURES

Volume of activity	$2.4 billion
Main customers (% of volume)	
Hydro-Québec Production	65%
Hydro-Québec TransÉnergie	34%
Other	1%

The Chicoutimi-Nord–Dubuc line at the point where it crosses the Saguenay.

Construction of Saint-Lin substation (Laurentides).

Abilities that are up to any challenge

Our projects involve large capital outlays and are often highly complex because of logistical, material, technical or climatic constraints. Fortunately, our employees are known for their skill and were able to rise to the many difficult challenges of 2008. Our volume of activity grew to $2,416 million, up 12% over 2007. Here is an overview of the past year's main accomplishments:

- The last two units at the 385-MW Péribonka generating station went into operation in January and March. This $1.4-billion project was completed within budget and three months ahead of schedule. It created 3,077 person-years of employment and $557.4 million in regional spinoffs. The station is connected to the grid by the 7-km, 161-kV Chicoutimi-Nord–Dubuc overhead line, which crosses the Saguenay and was also completed during the year.
- We finished the overhaul of Outardes-4 generating station.
- Construction was completed on the 120/25-kV Wemindji substation (Baie-James).
- At Lévis substation near the city of Québec, refurbishment of the second synchronous condenser, due to return to service in 2009, will allow us to increase the substation's transmission capacity. In addition, our high-voltage line de-icing system—a world first—is now in operation.
- We wound up construction of the 120/25-kV Saint-Lin substation and 120-kV Paquin–Saint-Lin line (Laurentides).
- Refurbishment of Jonquière substation (161/25 kV) was completed (Saguenay–Lac-Saint-Jean).
- We rebuilt two underground lines, Beaumont–Dorchester and Berri–De Lorimier, both 120 kV, in Montréal.
- We erected a 120-kV line to supply ERCO Worldwide (Outaouais).
- In the Richelieu region, we rebuilt the 230-kV Sorel–Tracy line.
- In the Matapédia region, we constructed a 230-kV line and set up the automated operations required to bring the output of Carleton wind farm onto the grid.
- In the Gaspésie region, we rebuilt Carleton substation (69/25/12 kV).

The safety of employees of Hydro-Québec, SEBJ and our partners is of prime importance on our jobsites.

Volume of Activity 2004–2008 ($B)

2004	2005	2006	2007	**2008**
2.0	2.1	2.0	2.2	**2.4**

Sustained momentum in generation projects

- In 2008, we were involved in the construction of five hydroelectric generating stations, two of them for the Eastmain-1-A/Sarcelle/Rupert project. We also carried out nearly 80 refurbishment or refitting projects to increase the capacity of the generating fleet or ensure its long-term operability. Altogether, these projects generated $1,564 million in activity over the course of the year.
- Work at the Eastmain-1-A/Sarcelle/Rupert jobsite was in full swing. This project will add 918 MW in installed capacity to Hydro-Québec's fleet, and 8.7 TWh in annual output.
  - Several structures have already been completed: Lemare, Rupert and Nemiscau-1 dams and a number of dikes, the Rupert spillway (except for the chutes), the transfer tunnel between the Rupert forebay and tailbay, the Lemare, Nemiscau-1, Nemiscau-2 and Ruisseau-Arques instream flow release structures, and the Sakami weir.

The Sarcelle powerhouse jobsite, in the Baie-James region.

Construction of Nemiscau-1 dam. In a North American first, the dam was made watertight with an asphalt concrete core.

- We finished excavating the site of the 768-MW Eastmain-1-A powerhouse, intake and penstocks, and began concreting the powerhouse.
- On the site of the 150-MW Sarcelle powerhouse, construction got under way on the workcamp and excavation commenced. Upcoming stages: cofferdam construction, powerhouse concreting, and installation of the armoring by the turbine manufacturer.

In 2008, the Eastmain-1-A/Sarcelle/Rupert jobsite created 4,023 person-years of employment; Crees and Jamesians made up 16.5% of the workforce. Contracts awarded and expenditures totaled $86 million for the Nord-du-Québec region, $102 million for Abitibi-Témiscamingue and $147 million for Saguenay–Lac-Saint-Jean.

- In the Haute-Mauricie region, the first units at Chute-Allard and Rapides-des-Cœurs were started up. All 12 units planned (138 MW altogether) should be operational by the end of 2009. In 2008, jobs generated by this project represented 493 person-years—with 63% of the workforce coming from the region, in particular the Attikamek community of Wemotaci—while regional spinoffs totaled $38.7 million.

- Hydropower generating stations all across Québec are being worked on. They include Manic-5, Manic-5-PA and Bersimis-2 (Manicouagan); Bryson, Hull-2 and Paugan (Outaouais); Rivière-des-Prairies, Beauharnois and Les Cèdres (near Montréal); La Grande-1, Robert-Bourassa, La Grande-3 and La Grande-4 (Baie-James); and La Tuque (Mauricie). Most of these projects will be completed by 2013.

- Refurbishment continued on several dams—Melville (Mauricie), Mercier (Outaouais) and Barrière (Abitibi-Témiscamingue)—and got under way on Bourque dam (Outaouais).

- We filed the environmental impact statement for the Romaine complex (Minganie) in January. A joint federal-provincial review panel and a fact-finding committee of the Bureau d'audiences publiques sur l'environnement held a hearing on the project in October and December. Provided the necessary approvals are received, work will get under way in the second quarter of 2009.

- Engineering and procurement commenced in preparation for the refurbishment of Gentilly-2 nuclear generating station, in Bécancour. The work will be done in 2011 and 2012. This project, designed to extend the life of the 675-MW plant until 2040, includes refurbishing the reactor and generating unit and replacing the control panel computers. In addition, phase I of the expansion of the solid radioactive waste management facilities was completed in 2008.

- In the region of Nunavik, we launched the construction of a new thermal generating station in the Northern Village of Kuujjuaq to replace the existing plant. We built a road, prepared the building site and carried out the civil engineering work. The $46-million project is scheduled for completion in 2010. Off-grid systems such as the one in Kuujjuaq are operated by Hydro-Québec Distribution.

The Chute-Allard development, in the Mauricie region.

Refurbishment under way at Manic-5 generating station, in Manicouagan.

Building the Rimouski–Les Boules line, in Gaspésie.

A growing number of major transmission projects

Our transmission-related workload grew in 2008, with a volume of activity of $816 million for close to a thousand projects of all types and sizes: extending the grid, increasing capacities within Québec and with Ontario, increasing facility security or long-term operability, etc.

In all, we worked on 1,085 projects—including about a thousand transmission projects—in 2008.

- We broke ground on Mont-Tremblant substation (120/25 kV) and two 120-kV lines slated to start up in 2009 (Laurentides).
- The project to build the 120/25-kV Vaudreuil-Soulanges substation and loop the Dorion–Rigaud line got under way. Commissioning is scheduled for 2009 (Montérégie).
- We carried out the necessary engineering and procurement to rebuild the 120/25-kV Gatineau substation, due to return to service in 2009 (Outaouais).
- Refurbishment and expansion of the 315/161/69-kV Hauterive substation continued, and is on track for completion in 2012 (Côte-Nord).
- Refurbishment of the 230/120/25-kV Sorel substation progressed and will run until 2010 (Montérégie).
- We commenced work to overhaul the 120/13.8-kV Rapide-2 and Rapide-7 substations, with a view to a 2010 startup. We also began the engineering for refurbishment of the synchronous condensers at Abitibi substation (Abitibi-Témiscamingue).
- Refurbishment started at the 120/25-kV Saint-Maxime substation and should be completed in 2010 (Montérégie).
- In Montréal, we launched a project to refurbish and enlarge the 120/25/12-kV Laurent substation, and continued the expansion of the 315/25-kV Saraguay substation. The two projects are scheduled for completion in 2011 and 2009, respectively.
- To supply the Éléonore mining property, we began clearing land prior to construction of a 120-kV line that will be operated temporarily at 69 kV (Baie-James).
- We began building two 230-kV lines—Rimouski–Les Boules and Saint-Ulric–Saint-Léandre—in preparation for bringing wind power onto the grid starting in 2009 (Gaspésie and Bas-Saint-Laurent).
- The project for a 1,250-MW interconnection with Ontario is proceeding on schedule. Outaouais substation (315/230 kV) is 80% complete, while the 230-kV line that runs across the Ottawa River was finished in anticipation of a 2009 commissioning date. In February 2009, we began clearing the ground in preparation for building the 315-kV Chénier–Outaouais line, designed to reinforce the interconnection. The approximately 115-km line is being erected in an existing right-of-way.

Construction of Outaouais substation and the 230-kV line to Ontario.

The Prix Léonard, Energy category, from the Association of Consulting Engineers of Quebec, presented by Richard Lamarche, Alcoa Canada, to Anthony Rattue of SNC-Lavalin and Pierre Geoffrion of Hydro-Québec. Their achievement: Péribonka dam.

Innovating to improve construction

To carry out projects that often involve sizable technical challenges, the teams at Hydro-Québec Équipement and SEBJ bring together their outstanding innovative capability with the best methods and technologies in their areas of specialization.

■ In 2008, we continued to roll out version 5 of CATIA® (Computer Aided Three-Dimensional Interactive Application), which we use to model planned and existing facilities. To further optimize construction project planning, we combined CATIA V5 with DELMIA® (Digital Enterprise Lean Manufacturing Interactive Application). These simulation systems allow us not only to reduce refurbishment time, but also to work in highly congested areas.

■ At the Eastmain-1-A/Sarcelle/Rupert jobsites, we achieved a number of firsts for Québec.

We rely on innovation to optimize our projects.

□ For the watertight core of Nemiscau-1 dam, we opted for asphalt concrete rather than till. This experience familiarized us with a technique we plan to apply in building various structures for the Romaine complex, in the Minganie region, where there is very little till.

□ We decided to use prefabricated components for the structure of Eastmain-1-A powerhouse to speed up the project. These factory-produced components are assembled on site.

□ At Sarcelle powerhouse, we laid the necessary groundwork to install bulb-type units, a technology new to Hydro-Québec. This type of generating unit, essentially a turbine and generator enclosed in a submerged watertight housing, is well suited to the low heads (10 m or so) and heavy flows characteristic of the Sarcelle site.

■ We designed a steel grillage foundation for use in substations. Ideally suited to sandy sites, this foundation stands up well to earthquakes. It has several advantages over concrete foundations: it costs less in some cases, goes into place quickly, lasts longer, is easy to take apart and is highly recyclable. Wemindji substation was built on such a foundation.

■ Using watertight caissons enabled us to refurbish the intake and trashrack guides at Beauharnois without shutting down the generating units and, consequently, without any loss to the operator. This new approach also creates benefits in terms of efficiency, employee safety and respect for the environment.

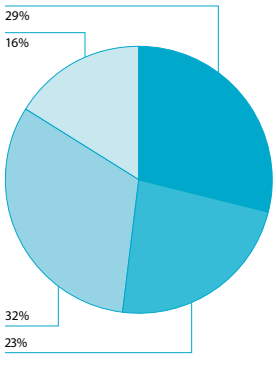
■ At Lévis substation, we commissioned de-icing equipment as part of a project to reinforce 560 km of lines in the 315-kV and 735-kV transmission grids. By pairing two technologies—direct current and static compensation—this equipment can melt ice accumulations up to 50 mm thick on the lines.

■ Normand Bell, Project Manager – Transmission Lines, won the International Council on Large Electric Systems (CIGRE) Technical Committee Award for 2007 in recognition of his outstanding contribution. This distinction attests to Hydro-Québec's power system expertise and innovative capability.

Preparing for the Future with Innovation

R&D technician Marco Lepage makes the final adjustments to a LineScout before sending it out to inspect a transmission line. The LineScout is the first robot of its kind in the world and is the brainchild of researchers at IREQ. Next page: a LineScout at work on a power line.

Breakdown of Innovation Efforts by Hydro-Québec's Research Institute in 2008 (by amount invested)



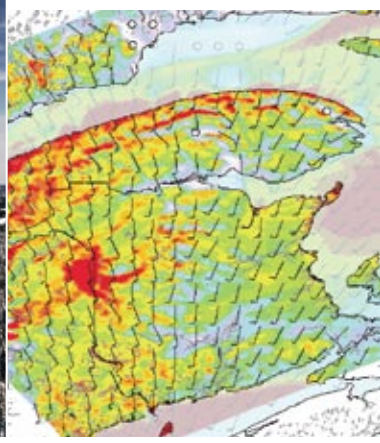
- Generation and construction
- Transmission
- Distribution and customer applications
- Strategic projects

A Strategic Asset

Technological innovation is at the core of Hydro-Québec's commercial and operational strategy. Innovation meets two key requirements: contributing to the company's economic performance and optimizing its facilities based on the objectives of quality, long-term operability and development. To maintain our technological leadership, we count on our employees' expertise in all areas of electricity and related fields, particularly information technologies and telecommunications.

We invest roughly $100 million annually in the activities of our research institute, IREQ. In 2008, IREQ focused on wind power integration, new renewable energies and the long-term operability, reliability and optimization of our facilities, among other areas. Its researchers also continued to develop technologies to facilitate the electrification of ground transportation.

At the same time, we continued to implement an integrated architecture for our telecommunications network and the information systems that form the backbone of our power system.



CREDIT: LM GLASFIBER

The LineScout's movable parts allow it to negotiate a wide variety of obstacles through a series of maneuvers. Here, it prepares to climb over an insulator on a live conductor.

Wind maps generated by our wind forecasting system are used to characterize and forecast wind power output. On the left, the L'Anse-à-Valleau wind farm in the Gaspésie region.

Wind power and new water power technologies

IREQ is at the forefront of research on integrating wind power into major power grids. In 2008, we oversaw a number of innovation projects in this field.

- In cooperation with Environment Canada, we conducted studies to characterize and forecast wind power generation in order to maximize output from this energy source without adversely affecting the reliability of the transmission grid.

- We continued to develop management tools for balancing hydro and wind power, as well as models for simulating the behavior of wind turbines and wind farms connected to the Hydro-Québec grid. For example, we developed an aggregation technique that lets us simulate the behavior of an entire wind farm, including the collector system, based on models consisting of only a few turbines.

- We participated in the activities of the Wind Energy Strategic Network (WESNet), a pan-Canadian network of wind power experts, which seeks innovative solutions to the technical challenges faced by the wind energy industry in Canada.

Other promising avenues for diversifying Québec's energy portfolio are hydrokinetic power, generated by submerged hydraulic turbines in a river or ocean, and salinity gradient power, produced by turbines driven by the pressure that results from the migration of freshwater to saltwater through a semipermeable membrane. In 2008, our teams carried out exploratory analyses on the potential of these renewables to complement large hydro.

Improving energy efficiency

IREQ works hard to improve the energy efficiency of the company's generation, transmission and distribution facilities and also develops energy-saving solutions for its customers.

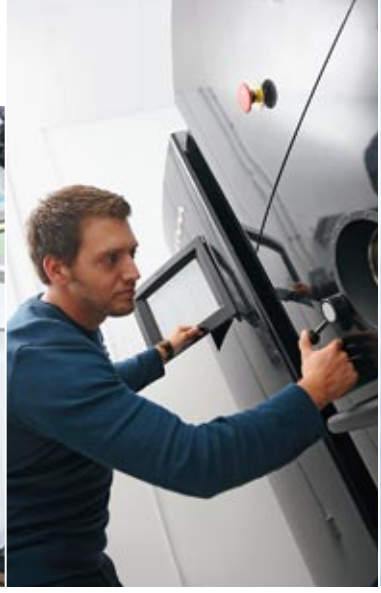
- We participate in the research carried out by the Consortium on Hydraulic Machines, which includes VA TECH HYDRO (Switzerland), Voith Siemens Hydro (United States), Université Laval and Natural Resources Canada. The consortium was established to improve the performance of hydraulic equipment.

- We conducted system tests on a new software tool allowing us to better control the system voltage profile in order to reduce transmission losses. In addition, to improve the system's energy performance, we enhanced the system control centre in various ways to optimize line operation.

- We participated in the CATVAR pilot project (voltage regulation and reactive power control), the objective of which is to reduce energy losses on distribution systems. Our goal was to optimize the CATVAR system before implementing it on a wider scale.

- To help customers reduce their electricity consumption, we also carried out research on such areas as grey water heat recovery. Test results from the laboratory suggest that this technology could generate substantial energy savings.

Technician Denise Lessard-Déziel and researcher Jocelyn Jalbert experiment with a new method for evaluating the condition of the solid insulation in transformers.



Engineer Éric Lavallée adjusts the parameters of the rapid-prototyping machine that IREQ acquired in 2008.

At Lévis substation, a new telecommunications tower stands next to a transmission tower under construction.

Titanium casting manufacturing

In a sector like ours, product development relies heavily on computer-aided design and prototyping. To consolidate the progress it has made in this field, IREQ recently acquired a rapid-prototyping machine. The machine uses an electron beam to fuse metal powders such as titanium, making it possible to create geometrically complex objects in a very short time.

Rapid prototyping enables us to optimize our innovation projects and adds value to our contribution to R&D collaborations with other research centres, universities and the private sector.

A system enhanced by telecommunications

In 2008, we continued to implement an integrated architecture for Hydro-Québec's telecommunications network to ensure the optimal development of our facilities and boost the network's security. We also made strides in expanding the remote management of our facilities.

Our telecommunications network, like our power system, is evolving rapidly. Our communications and data transmission needs are constantly increasing, whether for the integration of new wind power facilities or the management of our growing exports. In 2008, major work (extension, reinforcement and digital conversion) was carried out on our telecommunications infrastructure to improve the efficiency of generating station and substation operations.

- We completed the upgrading of our telecommunications network in the Gaspésie. This network, which serves all the Hydro-Québec facilities in the region, handles the data transmitted to the automatic protection and control systems for wind power integration. The network also transmits data from wind farms to the transmission system's telecontrol centres.

- As part of the Montréal Centre project to relieve congestion on the telecommunications network between Complexe Desjardins and the Jarry Street administrative building, we began the rollout of SONET (Synchronous Optical NETwork) and DWDM (Dense Wavelength Division Multiplexing) systems. The benefits include increased transmission capacity, flexible routing and greater reliability.

- We have also made progress in digitizing the telecommunications network. We upgraded the microwave links between Baie-Comeau and Lévis substations and between Tilly and Le Moyne substations.

Electricity and ground transportation

Hydro-Québec has had an interest in the electrification of ground transportation for nearly 20 years. Our R&D projects in this field involve battery materials, electric drivetrains, and ways for power distribution systems to handle the widespread adoption of electric vehicles.

- In 2008, we continued our work on new battery materials, such as the molten salts used in the manufacture of lithium-ion batteries for electric vehicles. These materials, which are safer for the environment than conventional ones, also have a number of safety and performance benefits. In addition, we signed licence agreements to market these products.

The Indica EV, manufactured by Tata Motors, at the Montréal International Auto Show. This electric vehicle is equipped with a Hydro-Québec TM4 motor. Thierry Vandal, President and CEO of Hydro-Québec, and Claude Béchard, Québec Minister of Natural Resources and Wildlife.

IREQ was awarded the Prix Innovation in the Process category by the Association de la recherche industrielle du Québec for its contributions to research and innovation. The achievement: our Maski robot, which is used to inspect submerged structures.

■ TM4, a subsidiary of Hydro-Québec, was chosen by the Indian automobile manufacturer Tata Motors and its European subsidiary Miljø Innovasjon to supply electric motors, power electronics and vehicle controllers for an all-electric car demonstration program involving one hundred vehicles, to be launched in Norway in 2009–2010.

■ We conducted studies on the potential impact of the electrification of ground transportation on distribution systems. This work included identifying promising R&D avenues to be explored with a view to supporting electrification initiatives.

Progress through partnering

To optimize its innovation efforts, Hydro-Québec is focusing on expanding its world-class network of partners. In 2008, it stepped up its exchanges with universities, government agencies, firms and research institutions in Québec and elsewhere.

■ In 2008, Hydro-Québec contributed $5.1 million to Québec universities for research contracts and 16 research chairs.

■ We continued to participate in the Ouranos consortium on regional climatology and climate change adaptation. Our work included developing a climate change scenario to assess how climate change will impact energy demand in Québec and Hydro-Québec's generating potential by 2050.

■ We continued to collaborate with FPInnovations – Forintek Division (formerly Forintek Canada), Canada's national wood products research institute, on the ÉlectroBois program, a major part of which involves research into new lumber drying technologies. In particular, we worked on heat treatments such as log thawing to facilitate debarking, thermal modification, high-frequency vacuum drying, and drying with high-temperature heat pumps.

In 2008, we signed agreements with a number of partners for various projects:

■ Electric Power Research Institute (EPRI), to compare fault locating technologies used by EPRI and Hydro-Québec.

■ Arch Chemicals, to develop and market a more environmentally friendly wood preservative.

■ Dow Chemical, for the shared funding of a project to develop a technique for checking low-voltage cables.

■ China Electric Power Research Institute (CEPRI), for the adaptation of the Hypersim power system simulator developed by Hydro-Québec's research institute.

■ British Columbia Transmission Corporation, to use the LineScout robot developed by our researchers for inspecting conductors for stream, highway and railroad crossings.

■ ABB, to develop a multi-use version of the multi-band power system stabilizer (MB-PSS). This regulation system, which was developed by our researchers and is used with generators and shunt compensators, significantly improves the dynamic behavior of transmission grids.

■ AREVA, to develop a synchronized phasor measurement unit to monitor the grid under both steady-state and transient conditions.

Powering a Better Future

CREDIT: PHOTOPLEINCIEL

With financial support from the Fondation Hydro-Québec pour l'environnement, the Nature Conservancy of Canada carried out environmental enhancements at the Barachois de Malbaie, a salt marsh in the Gaspésie.

A Responsible Approach

The choices that Hydro-Québec makes express its culture of sustainable development. Our hydropower development projects stand as a prime example of this. They are designed in such a way as to preserve environmental heritage, promote social development and contribute to regional economies. In the same vein, we are investing increasingly in new renewable energies, energy efficiency and technological innovation, thereby playing a key role in the fight against global warming. This responsible approach enables us to provide our customers with a reliable supply of electricity, while adhering to the principles of sustainable development.

In 2008, we defined the measures, targets and indicators to be included in our plan for implementing Québec's *Government Sustainable Development Strategy 2008–2013,* which came into effect on January 1. In line with this strategy, Hydro-Québec will publish its action plan in March 2009.

Atmospheric Emissions from Hydro-Québec's Generation Operations (tonnes)[a]

Type of emission	**2008**	2007
Carbon dioxide (CO_2)	**233,054**	245,832
Sulphur dioxide (SO_2)	**1,154**	1,150
Nitrous oxides (NO_x)	**6,132**	6,205

a) Most of these emissions are from thermal generating stations supplying off-grid systems. According to 2006 data, power generation is responsible for only 0.5% of GHG emissions in Québec, compared with 40.0% for transportation and 33.6% for industry.

We are conducting studies at Baskatong reservoir to determine the impact of our facilities' operations on the biophysical and human environment.

Undergrounding the distribution grid in the historic district of La Prairie, in Montérégie. Archaeological digs have uncovered the remains of a stockade around an old fortified village.

Sound environmental practices

Hydro-Québec's actions in the field hinge on one fundamental principle: protecting the environment. Our infrastructure projects systematically include mitigation measures and environmental follow-up, and the largest ones are preceded by comprehensive impact assessments. In addition, our jobsites are monitored by specialists who ensure compliance with regulatory provisions and with the conditions specified in the project approvals. With respect to our operating and maintenance activities, we promote environmentally responsible practices and the cleanest technologies. Most of our activities are governed by ISO 14001–certified environmental management systems. As a result, Hydro-Québec has an outstanding environmental record.

■ The environmental impact statement (EIS) for the Romaine complex (Minganie) was filed in January 2008. The EIS and its ancillary studies represent more than four years of work by hundreds of engineers, scientists and other contributors, including Innu community members, and cost $145 million. The $6.5-billion project calls for building four generating stations with a total installed capacity of 1,550 MW and annual output of 8 TWh. A public hearing was held in the fall. Hydro-Québec wants to start the work in the second quarter of 2009, once it has obtained the necessary government approvals.

■ On the Eastmain-1-A/Sarcelle/Rupert jobsite (Baie-James), a team of specialists is ensuring that the work fulfills the conditions laid out in the 1,200 ministerial authorizations pertaining to the project, and complies with the applicable laws and regulations. This team is also responsible for seeing that the work does not interfere with the activities of Cree land users.

■ In December 2008, Hydro-Québec TransÉnergie published a brochure summarizing the lessons learned from the environmental follow-up studies on a major line loop project (735-kV Des-Cantons–Hertel line and 735/120-kV Montérégie substation). It is primarily a report on how the company met its objectives in conducting the studies it undertook to carry out after completion of the project. The brochure will also be used to explain the project in non-technical language to different segments of the public, for example at hearings, consultations, presentations and training activities.

■ We produced a video on the environmental follow-up of various hydropower complexes built on two rivers in the Manicouagan region: the Manicouagan and the Rivière aux Outardes. This video describes the measures taken by Hydro-Québec to protect the host environment.

■ Hydro-Québec and McGill University reported on the findings of a major study carried out between 1990 and 2005 to determine whether electric and magnetic fields (EMFs) created by high-voltage lines have a detectable effect on the health and productivity of dairy cows under normal farm conditions. This study, conducted with the Conseil des recherches en pêche et en agroalimentaire du Québec (CORPAQ) and the Medical Research Council of Canada, yielded a substantial body of knowledge on this issue. The results obtained led to the conclusion that the cows' exposure to EMFs does not have a harmful effect either on their productivity or, in all probability, on their health.

■ We continued the ambitious program of archaeological inventories initiated in 2002 in conjunction with the Eastmain-1-A/Sarcelle/Rupert project. About 60 people are actively involved in this program designed to preserve the cultural heritage of the James Bay Crees and study the lives of the peoples who have occupied the land over the last five millennia. With excavations at 45 locations, this is the largest archaeological site in Québec. The objects uncovered include more than 100,000 fragments and several hundred carved stone tools.

Researcher Karim Zaghib shows off an electric bicycle equipped with a lithium-ion battery that uses materials developed at Hydro-Québec's research institute. Zaghib won an award from the International Electric Research Exchange for his outstanding contribution to research.

Environment and corporate affairs staff members Michel Giguère, Julie Sauriol and Maryse Lambert take part in the *allégo* initiative, which encourages employees to opt for public transit, carpooling and active modes of transport.

■ As part of a project to underground the distribution grid in Montérégie, archaeologists have conducted digs to document the history of this region, which was frequented by Aboriginal people for thousands of years. Among the many objects uncovered are an arrowhead at least 4,500 years old and the remains of stakes used in 1687 to build a stockade around a fortified village in what is now the historic district of the town of La Prairie.

■ We awarded a contract to the Normand-Maurice CFER (business and recycling training centre) for the recovery and refurbishment of cell phones. This centre provides training for teens who experienced learning difficulties at school.

■ To increase the energy efficiency of its buildings, Hydro-Québec modernized the lighting fixtures and heating, ventilation and air-conditioning systems of some buildings, thereby achieving recurrent savings of 8.1 GWh. The company also conducted a pilot project that involved adjusting the temperature settings in five administrative buildings. The new settings yielded savings of 1.2 GWh and will be extended to all administrative buildings in 2009. The 9.3 GWh saved through these initiatives corresponds to the consumption of 544 households that heat with electricity.

■ We launched the RECYC-FRIGO Environnement program, targeting the recovery and recycling of 230,000 energy-guzzling refrigerators and freezers by 2010. Participants receive a cheque for $60 in return for each of their old appliances. This program, part of the Energy Efficiency Plan, will generate savings of 180 GWh over three years.

■ In August, Hydro-Québec published the results of a life cycle analysis applied to compact fluorescent lightbulbs. It had commissioned the study from the Interuniversity Research Centre for the Life Cycle of Products, Processes and Services, which is affiliated with the École Polytechnique de Montréal. The results show that, for Québec households that do not heat with oil or gas (84%), compact fluorescents are the best environmental choice from the standpoint of human health, ecosystems, climate change and resource availability. For households that heat with oil or gas (16%), the cross-effects between lighting and heating reduce the advantage of these lightbulbs during the winter heating season.

■ In 2008, we replaced 151 of our light-duty vehicles (40% of those replaced during the year) with more energy-efficient models. The result is a 111,500-litre reduction in annual fuel consumption and a 263-tonne reduction in CO_2 emissions from these vehicles.

■ As part of the annual *Défi Climat* campaign, approximately 900 employees pledged to reduce CO_2 emissions by taking steps such as planting trees, buying ENERGY STAR qualified appliances and shopping for locally grown food.

■ Working with various partners, Hydro-Québec's research institute has developed materials (e.g., graphite, nanotitanates, ionic liquids and lithium iron phosphate) to produce a lithium-ion battery for electric bicycles, scooters and wheelchairs, as well as plug-in hybrid cars and all-electric vehicles.

We use environmentally friendly paper for all our printing and photocopying.

We recycle tonnes of metal every year.

In the township of Roxton, plant cover and eroded banks along the Rivière Noire were restored with financial support from Hydro-Québec.

■ Hydro-Québec continued its involvement in the *allégo* project, an initiative by Montréal's Agence métropolitaine de transport to encourage the use of modes of transportation other than single-occupancy vehicles for travel between home and work. We provide self-service bicycles for our employees' use and have introduced measures to promote public transit, carpooling and active modes of transport, such as walking and cycling. In 2008, 37% of our employees used single-occupancy vehicles as their chief mode of transport for the daily commute.

■ Using environmentally friendly paper for our printing and photocopying helped save 13,000 trees and 18 million litres of water in 2008. We also reduced the amount of paper we use for photocopying by 87 tonnes.

■ We recycled 1,474 tonnes of paper and cardboard, and 13,123 tonnes of metal in 2008.

■ In the 2008 edition of the *Mérite de l'environnement et du développement durable* contest, Hydro-Québec TransÉnergie's underground lines unit was recognized for its initiative to recycle the structural steel supports from cable ends in transmission substations. When Guy substation was dismantled, 18 steel structures were recovered and sent to the Normand-Maurice CFER to be cleaned, cut, drilled, reassembled and painted. They were then put back into use at Dorchester substation.

■ We recover insulating oil from our facilities. In 2008, we decontaminated and recycled 93% of the contaminated oil for reuse in our transformers. The remainder was reclaimed for other purposes.

Our goal: Healthy communities

With operations throughout the province, Hydro-Québec ensures that its construction projects and facilities are accepted by the host communities and well integrated into their surroundings. In particular, we take steps to preserve the quality of life of people living near our facilities, as well as the landscapes they enjoy. As well, we support many local initiatives of social or environmental interest.

■ In 2008, the Fondation Hydro-Québec pour l'environnement allocated $1.5 million to 20 projects in 12 regions of the province. The Parc Nature de Pointe-aux-Outardes organization, for example, received $49,900 for a project to protect foreshores and shellfish beds in the Manicouagan region.

■ Under our Integrated Enhancement Program, and specifically as part of the 230-kV Rimouski–Les Boules line project, the regional county municipalities of Rimouski-Neigette, La Mitis and Matane, and several of the municipalities they encompass, will receive a total of $697,900 for projects to enhance the biophysical and human environment. This Hydro-Québec program is designed for communities affected by major transmission projects.

■ In cooperation with Tourisme Suroît, the regional county municipality of Beauharnois-Salaberry is currently developing an open-air museum that will explore various themes related to local features, for the enjoyment of bicycle path users. Since Hydro-Québec operates major facilities in the region, the company is taking part in this initiative by supplying information to the museologists in charge of the project and by working with the organization to set up a cyclist rest stop on the topic of hydropower, which is to be inaugurated in spring 2009.

■ To preserve particular landscapes, 14,000 residential customer connections were made to the underground distribution system in 2008, or 30% of the total.

Powering the Québec Economy

Special constable Claudia Ménard accompanies visitors on a tour of Eastmain-1 powerhouse.

Managing Succession and Preserving Expertise Are Key to Our Success

Maintaining a sufficient pool of qualified workers in all our fields of endeavor is a major issue faced by Hydro-Québec in achieving its business objectives. That is why we are counting on our corporate succession plan to help us successfully manage the replacement of a significant portion of our workforce, while safeguarding and developing our know-how. The plan outlines a number of measures for renewing our expertise, including promotional campaigns, recruitment strategies, staffing processes, training activities and knowledge transfer mechanisms.

At the same time, we pay close attention to welcoming new employees and measuring their job satisfaction so we can improve our integration efforts. We also strive to maintain a favorable climate in the workplace, which has prompted us to renew a number of collective agreements well before they expire.

Alain Gervais, a trainer at Hydro-Québec Distribution, with line worker Martin Bizier during a training session.

Intern Rose-Anne Déry (right) works alongside a seasoned employee, Martine Ouellet (left), in preparing an advertising campaign. Rose-Anne is now one of Hydro-Québec's most recent hires.

■ To prevent the potential loss of valuable expertise resulting from the increasing number of retirements, we carried out an analysis of each electricity-related career in 2007 to determine the skills and trades most at risk and the measures required to stem these losses. In 2008, Senior Management paid particular attention to the risks associated with the loss of the company's knowledge base, a concern that is reflected in the 2009 Business Plan.

■ According to our annual employee survey, completed by 14,366 respondents, overall job satisfaction and overall employee motivation were 8.42 and 6.87, respectively, levels similar to those in 2007.

■ According to our annual survey, new hires rated their satisfaction with employee induction and integration procedures at 8.4 out of 10, representing a 0.1 increase over the 2007 level. Of the 1,252 new hires in 2008, 66% were under 35 years of age.

■ Out of the 2,835 permanent employees eligible for retirement in 2008, 896 left the company, compared with 758 out of 2,860 in 2007.

■ Hydro-Québec is a founding partner of the Institute of Electrical Power Engineering. In 2008, we awarded 15 general scholarships and 34 traveling scholarships to 41 IEPE students, for a total contribution of $93,000. In addition, 20 new IEPE graduates joined the company's ranks in 2008; in total, Hydro-Québec has hired 107 graduates since the Institute was created in 2001.

■ We offered internships to 170 students from university graduate and undergraduate programs. We also received 35 college student trainees, mainly in the area of industrial electronics.

■ In 2008, we dedicated 4.0% of the payroll to training programs, and 16,329 employees took part in at least one training activity.

■ In the area of diversity, we continued to prepare an action plan for 2009–2012 to harmonize the profile of our human resources with the labor market, taking into account availability rates established by Québec's Commission des droits de la personne et des droits de la jeunesse for four target groups (women, Aboriginal people, and ethnic and visible minorities, to which people with disabilities will be added in 2009). We will submit our equal access to employment program to the Commission in the spring of 2009.

■ The frequency of work-related accidents remained fairly stable compared with 2007, at 3.29 per 200,000 hours worked.

■ Under its Our Human Resources policy, Hydro-Québec made a commitment to maintain a safe and healthy workplace for its employees. In 2008, a number of activities were undertaken to this end, including intranet info-capsules on workplace health and safety laws and regulations.

■ We renewed seven of the eight collective agreements with our unionized employees several months before their expiry date. These agreements, which cover 91% of Hydro-Québec's unionized employees, now extend to 2013 or 2014.

Employees Hugues Carrière and Dany Tremblay receive an award of excellence from the Commission de la santé et de la sécurité du travail on behalf of Hydro-Québec. The award, in the public agencies category, is for the hand winch they developed for manipulating slings.

Collective agreements were renewed with many of our unions in 2008. Front row: President and Chief Executive Officer Thierry Vandal (second from left) with union presidents Michel Trudeau, Josée Durand, Claude Arsenault and Guy Trudel. Back row: Christian Tamborini, Benoît Bouchard and Richard Perreault.

Encouraging regional spinoffs

Every year, Hydro-Québec invests huge amounts of money in its development projects and day-to-day operations. These investments generate billions of dollars in spinoffs and support thousands of jobs throughout Québec.

Procurement of Goods and Services ($B)[a]

2004	2005	2006	2007	**2008**
2.4	2.4	2.7	2.6	**2.7**

- Procurement of goods and services inside and outside Québec totaled $2,660 million in 2008, compared with $2,586 million the previous year:
  - $1,311 million for the purchase of goods
  - $30 million for rentals
  - $912 million for specialized services and other work
  - $407 million for professional services
- In 2008, goods and services procured from companies in Québec totaled $2,372 million, or 89% of all procurement.
- The number of jobs in Québec supported by our overall procurement of goods and services is estimated at 16,726, including 11,462 direct jobs.
- To guarantee security of supply of goods and services and take advantage of favorable conditions in a context of longer lead times for the delivery of some essential goods, Hydro-Québec relies on proven strategies. For example, we are continuing to diversify our pool of suppliers, while strengthening our links with our most important sources, particularly electrical equipment manufacturers.
- In 2008, our capital spending on various hydroelectric projects generated 4,217 on-site jobs for contractors.[b]

Partnering with local communities

To meet its commitments as a socially responsible organization, Hydro-Québec partners with local communities, socioeconomic organizations and citizens' groups. This approach helps ensure project acceptance and maximizes the economic spinoffs of its activities. Hydro-Québec also contributes to regional development and participates in training the next generation of workers.

- For the Romaine hydropower project, Hydro-Québec and the regional county municipality of Minganie signed a partnering agreement in January 2008 to maximize the local spinoffs of the project. The company also signed agreements with the Innu communities of Nutashkuan (July) and Pakua Shipi and Unamen Shipu (October). Under these agreements, various economic, community and cultural projects will be funded, along with traditional activities and occupational training programs. In addition, the three communities will participate in the construction of facilities and environmental monitoring. Lastly, an understanding in principle on the Romaine project was reached with the Innu community of Ekuanitshit in October.

a) Excluding procurement by Société d'énergie de la Baie James.
b) Including projects carried out by Société d'énergie de la Baie James.

New facility for storing treated wood, in which tanks are used to recover runoff potentially contaminated with wood preservatives.

Hydro-Québec handles the delivery of heavy equipment to all its jobsites, such as the 160-tonne transformer shown here being transported on a long-load dolly.

Regional Spinoffs from Hydro-Québec Procurement ($'000)[a, b]

Administrative region of Québec	Procurement of services[c]	Procurement of goods[d]	**Total**
Abitibi-Témiscamingue (08)	21,250	13,568	34,818
Bas-Saint-Laurent (01)	6,372	4,799	11,171
Capitale-Nationale (03)	121,875	34,377	156,252
Centre-du-Québec (17)	82,219	32,723	114,942
Chaudière-Appalaches (12)	50,999	26,962	77,961
Côte-Nord (09)	41,358	8,598	49,956
Estrie (05)	9,423	17,697	27,120
Gaspésie–Îles-de-la-Madeleine (11)[e]	6,723	563	7,286
Lanaudière (14)	27,051	30,353	57,404
Laurentides (15)	33,768	21,822	55,590
Laval (13)	111,851	36,152	148,003
Mauricie (04)	110,622	47,374	157,996
Montérégie (16)	101,990	237,957	339,947
Montréal (06)	384,124	570,995	955,119
Nord-du-Québec (10)	16,015	6,178	22,193
Outaouais (07)	5,930	18,943	24,873
Saguenay–Lac-Saint-Jean (02)	105,575	25,710	131,285
Total	**1,237,145**	**1,134,771**	**2,371,916**

a) Amount billed by suppliers located in the administrative region.

b) Excluding procurement by Société d'énergie de la Baie James.

c) Specialized services, professional services and other work.

d) Purchases and rentals.

e) In the regional county municipality of Matane and the Gaspésie–Îles-de-la-Madeleine region, contracts awarded under the first Hydro-Québec Distribution call for wind power resulted in spinoffs estimated at $128 million in 2008.

Paul Coonishish, of the Cree Construction and Development Company, at one of the Eastmain-1-A/Sarcelle/Rupert jobsites (Baie-James).

Benoît Vanier and colleagues in one of the hybrid vehicles in Hydro-Québec's fleet. The use of more fuel-efficient cars illustrates the company's commitment to environmentally responsible practices.

Hydro-Québec's Contribution to the Québec Economy

	2008	2007
Dividends declared ($M)	**2,252**	2,095
Capital tax ($M)	**202**	278
Public utilities tax ($M)	**302**	240
Water-power royalties ($M)	**546**	263
Municipal, school and other taxes ($M)	**37**	35
Loan guarantee fees paid to the shareholder ($M)	**167**	169
Percentage of goods and services procured from Québec companies	**89**	94
Direct jobs supported by procurement, including procurement outside Québec (person-years)	**11,462**	13,000
Integrated Enhancement Program grants ($M)[a]	**0.2**	4.5

a) Under the company's Integrated Enhancement Program, communities affected by major transmission projects receive grants equivalent to 1% of the capitalized cost of the facilities.

■ In 2008, the Eastmain-1-A/Sarcelle/Rupert jobsite generated jobs equivalent to 4,023 person-years (including Hydro-Québec personnel); 16.5% of the workforce came from Cree and Jamesian communities. Most of the workers from these communities were employed by Cree businesses that have contracts for land clearing, housekeeping and food services, construction, maintenance, management and other activities.

■ In line with its goal of ensuring transparency and clarity in its communications with all its customers, Hydro-Québec has launched various programs for the cultural communities in the Montréal region, in partnership with organizations that provide orientation and integration services to newcomers. To introduce young people in these communities to careers in electricity and related fields, the company organized visits to its underground distribution training centre, in cooperation with the Association des ingénieurs et scientifiques haïtiano-canadiens and the Quebec Board of Black Educators.

■ Hydro-Québec develops classroom tools to help preschool, elementary and secondary teachers cover subjects such as electricity, sustainable development and energy efficiency. In 2007–2008, roughly 1,500 young people played our *Envirovolt* game, learning about the environmental issues involved in dam or transmission system construction.

International influence

On the world scene, Hydro-Québec is an active participant in the activities and initiatives of organizations such as the International Hydropower Association, World Energy Council, International Council on Large Electric Systems (CIGRE), Centre Jacques Cartier and e8. We also share our expertise with developing nations in international cooperation projects.

The new interpretation centre at Rivière-des-Prairies generating station (Montréal), one of the facilities across the province where Hydro-Québec offers tours to school groups and the general public.

The e8 annual Summit held in La Malbaie, Québec, in 2008 welcomed the heads of the 10 leading electricity companies of the G8 countries.

■ In June, the President and Chief Executive Officer of Hydro-Québec, Thierry Vandal, chaired the e8 annual Summit in La Malbaie, Québec. Under the theme "Climate Change and Technology," the event brought together the heads of the 10 leading electricity companies of the G8 countries. The e8 is an international organization that addresses global electricity issues and actively promotes sustainable development.

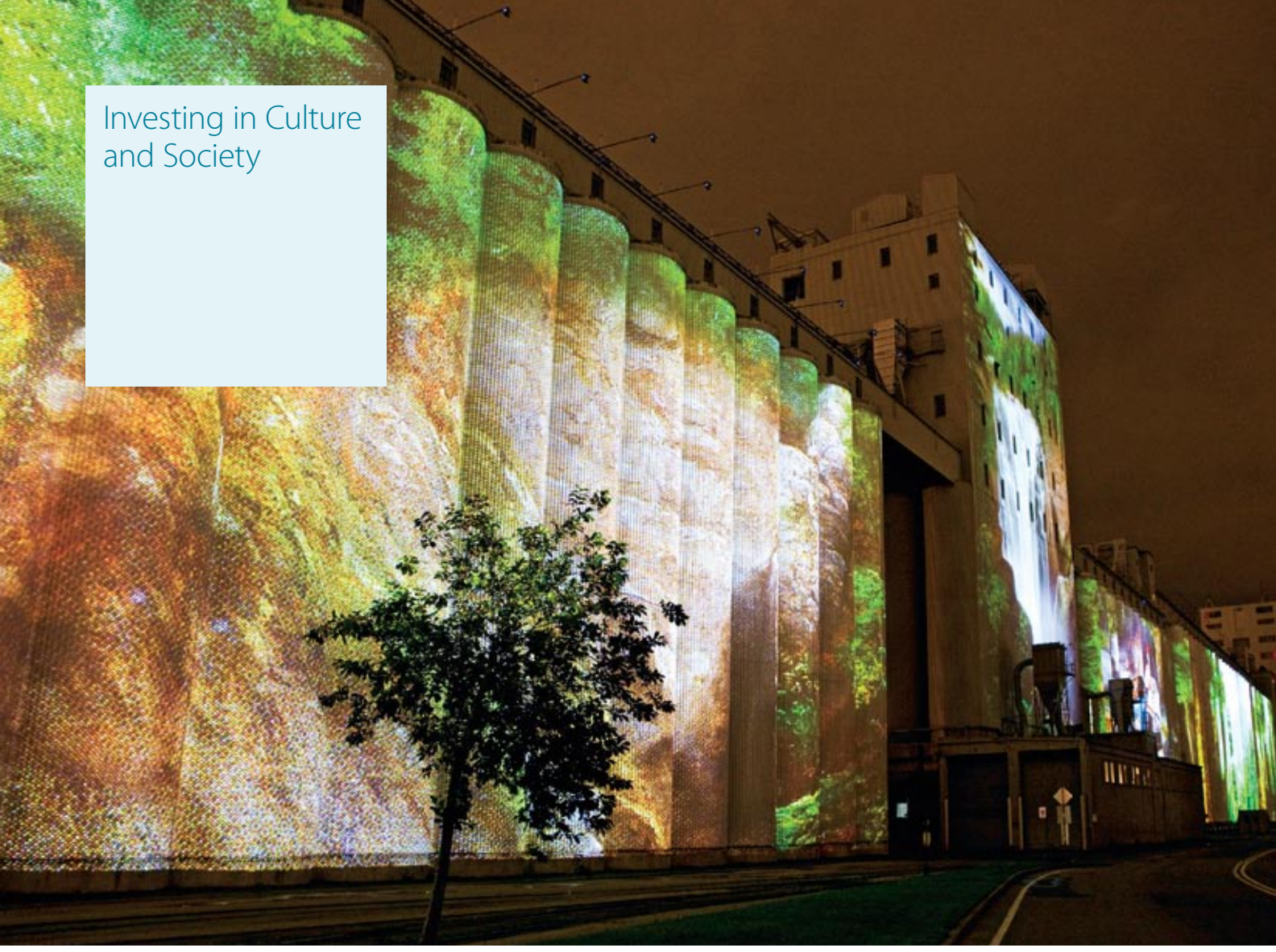
■ In August, Hydro-Québec participated in the 42nd CIGRE Session in Paris. Workshops allowed delegates to exchange views with their counterparts on current technical problems as well as recent progress made in the area of transmission systems. Nearly 4,000 representatives from around the world attended the event.

■ As part of the 21st Entretiens du Centre Jacques Cartier, which took place in Québec from October 3 to 10, 2008, Hydro-Québec organized a very successful one-day workshop on the theme of electricity and climate change, in particular carbon markets and adaptation measures.

■ In 2008, the Fonds Hydro-Québec pour la Francophonie was active chiefly in the following areas:

- Renewal of funding for an assistance program to help Électricité d'Haïti get the power industry in Haiti back on its feet
- Funding of training for foreign students working in the energy field, in cooperation with the Secrétariat international francophone pour l'évaluation environnementale, Université Senghor and the Institut de l'énergie et de l'environnement de la Francophonie (IEPF)
- Funding of Hydro-Québec's participation in *Défis énergétiques et environnementaux: solutions pour un développement durable*, an international conference on environmental and energy issues organized by the IEPF to celebrate its 20th anniversary

Investing in Culture and Society



CREDIT: NICOLAS RUEL

Hydro-Québec joined in the celebrations of the 400th anniversary of the city of Québec by sponsoring *The Image Mill* by Robert Lepage and Ex Machina. In this monumental visual and audio work, 81 grain silos in the port of Québec were transformed into a gigantic video screen. The four movements in the production correspond to the city's four centuries of history: the image shown above is from Waterways, the age of exploration and discovery.

A Strong Social Commitment

A key player in the province's economy, Hydro-Québec is also a responsible corporate citizen, and this is borne out by its contributions to Québec society. In 2008, it gave $25.9 million in donations and sponsorships to all sectors, including culture, health and humanitarian aid, education and youth, social and economic development, sports, and the environment. Continuing its three-decade-long tradition, Hydro-Québec donated $3.5 million to the United Way/Centraide in 2008, while its employees, pensioners and directors contributed $3.2 million.

CREDIT: YVES RENAUD

The Opéra de Montréal production of *Madama Butterfly.*

Orchestre Métropolitain du Grand Montréal, directed by Yannick Nézet-Séguin.

CREDIT: CHUQ

The Centre hospitalier universitaire de Québec houses the largest francophone medical research centre in North America.

Culture

■ Hydro-Québec supports a number of major cultural institutions, including Les Grands Ballets Canadiens de Montréal, Monument-National, Montreal Museum of Fine Arts, Musée de la civilisation (Québec), Montréal Science Centre, Opéra de Montréal, Pointe-à-Callière Foundation, Domaine Forget in the Charlevoix region and the Orford Arts Centre.

■ Hydro-Québec sponsors the Orchestre Métropolitain du Grand Montréal as well as all the symphony orchestras in the province. The company has been a title sponsor of the Orchestre symphonique de Montréal (OSM) since 1999 and, during the 2008–2009 season, provided major funding for programming for the orchestra's 75th anniversary. Hydro-Québec also funded the Montreal International Musical Competition.

■ In 2008, we sponsored a number of theatre companies such as Théâtre Denise-Pelletier, Usine C, Théâtre Prospero, Théâtre du Nouveau Monde and Théâtre La Licorne in Montréal; Théâtre de la Bordée in the city of Québec; Théâtre de Baie-Comeau; and Théâtre La Rubrique and Les Amis de Chiffon puppet theatre in the Saguenay region.

■ We provided funding for a number of cultural events including Les FrancoFolies de Montréal; Journées de la culture; Québec City Summer Festival and Québec Winter Carnival; Festival International des Rythmes du Monde in the Saguenay region: Musiqu'en Nous and L'Outaouais en fête in the Outaouais region; Festi Jazz international de Rimouski; Festival des traditions du monde in Sherbrooke; and the Mondial des Cultures in Drummondville.

Health and humanitarian aid

■ In 2008, Hydro-Québec supported a number of foundations and institutions involved in cancer research or in helping cancer patients, including the Fondation Centre de cancérologie Charles-Bruneau, the Quebec Division of the Canadian Cancer Society, Jewish General Hospital Foundation and its Weekend to End Breast Cancer campaign, McGill University Health Centre, Centre hospitalier de l'Université de Montréal, Institut du cancer de Montréal (Montreal Cancer Institute), Quebec Breast Cancer Foundation, Quebec Cancer Foundation and Leucan.

■ We also supported the foundations of many hospitals including those of the Centre hospitalier universitaire Sainte-Justine, Hôpital du Sacré-Cœur de Montréal, Hôpital Charles LeMoyne (Montérégie), Centre hospitalier universitaire de Sherbrooke, Hôpital de l'Enfant-Jésus and Hôpital du Saint-Sacrement (city of Québec), Centre hospitalier régional de Baie-Comeau, Centre hospitalier régional de Rimouski, Centre hospitalier régional de Trois-Rivières and Hôpital régional de Saint-Jérôme. We supported the Fondation les petits trésors at the Hôpital Rivière-des-Prairies, which is active in the field of children's mental health, and contributed again this year to the fundraising campaign of the Centre hospitalier universitaire de Québec, providing $1.7 million over six years.

■ In addition to the organizations we supported through Centraide, we provided funding for 141 humanitarian organizations, including the YWCA in the city of Québec, Société de Saint-Vincent de Paul, the Québec firefighters' foundation for major burn victims, The Canadian Red Cross Society and the Fondation de la Maison du Père, which helps the homeless.

CREDIT: THE LITERACY FOUNDATION

A child discovers the joy of reading thanks to the Literacy Foundation.

CREDIT: JEAN-BATISTE BENAVENT

Chantal Petitclerc, who has been a spokesperson for the Défi sportif challenge for athletes with disabilities since 1998, is the winner of 21 Paralympic medals and one Olympic medal.

The project to create the promenade Samuel-De Champlain in the city of Québec was sponsored by Hydro-Québec to celebrate the city's 400th anniversary.

Education and youth

■ Financial support from Hydro-Québec has allowed Québec universities to offer scholarships rewarding academic excellence and carry out a wide range of development activities. The company renewed a three-year agreement with Collège des administrateurs de sociétés of Université Laval and also partnered with the Conference of Rectors and Principals of Québec Universities in its *Knowledge Matters* campaign. Hydro-Québec contributed $3.7 million to the education sector in 2008, not including funding for university research contracts and research chairs.

■ We also supported organizations working with troubled youth such as the Fondation Père Sablon, Association sportive et communautaire du Centre-Sud, Intégration Jeunesse du Québec, Québec Youth Foundation, Literacy Foundation, Quebec Breakfast Club and the Fondation des Auberges du cœur.

■ To encourage the next generation of scientists, we supported activities such as the Science Fair organized by the Conseil de développement du loisir scientifique and the ninth edition of *Les filles et les sciences, un duo électrisant !,* an event that encourages girls to get interested in science and technology. We also funded the Engineering Games, the Québec Engineering Competition and the tenth edition of the Québec skills competition known as the Olympiades québécoises de la formation professionnelle et technique.

Socioeconomic development

■ As an extension of its numerous operations, Hydro-Québec partners with socioeconomic and business groups in various sectors. For example, we support a number of chambers of commerce as well as the Association of Consulting Engineers of Quebec, Association québécoise pour la maîtrise de l'énergie, Québec Union of Municipalities, Ordre des ingénieurs du Québec, Fédération Québécoise des Municipalités, Association des constructeurs de routes et grands travaux du Québec, Canadian Hydropower Association, Association de l'industrie électrique du Québec and Sous-Traitance Industrielle Québec.

Sports

■ As a partner of the Quebec Foundation for Athletic Excellence, Hydro-Québec funded 37 grants to outstanding young Hopeful and Elite level athletes.

■ We again supported the Défi sportif challenge for athletes with disabilities (25th edition), as well as the 2008 Quebec National Winter Games and Special Olympics Québec.

■ We funded a new section of the Québec Games called Mes premiers Jeux. It was established to introduce young people to competitive sports and encourage participation in the regional Québec Games.

Environment

■ Hydro-Québec funded various environmental initiatives, including the National Environmental Exhibition and the Conférence internationale de Québec 2008 – Évaluation environnementale et énergie, an international conference on environmental assessment and energy that was organized by the Association québécoise pour l'évaluation d'impacts and the Secrétariat international francophone pour l'évaluation environnementale. In addition, the Fondation Hydro-Québec pour l'environnement supported 20 projects.

■ Other organizations sponsored by Hydro-Québec include the Association québécoise pour l'évaluation d'impacts, Association québécoise de vérification environnementale, Association des biologistes du Québec, Fédération québécoise pour le saumon atlantique, Quebec Environment Foundation and Unisféra International Centre.

Financial Review

Management's Discussion and Analysis

52 Overview

53 Consolidated Results

55 Financial Position

58 Segmented Information

69 Outlook

70 Integrated Enterprise Risk Management

Consolidated Financial Statements

74 Management Report

75 Auditors' Report

76 Consolidated Statements of Operations

76 Consolidated Statements of Retained Earnings

77 Consolidated Balance Sheets

78 Consolidated Statements of Cash Flows

79 Consolidated Statements of Comprehensive Income

80 Notes to Consolidated Financial Statements

103 Five-Year Review

106 Consolidated Results by Quarter

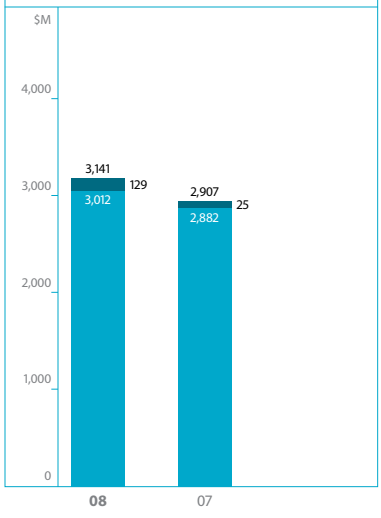
This Management's Discussion and Analysis (MD&A) should be read in conjunction with the Consolidated Financial Statements of Hydro-Québec and the notes thereto. The financial information and tabular amounts presented herein are expressed in Canadian dollars, unless otherwise indicated. The Consolidated Financial Statements take into account certain accounting practices that are specific to regulated enterprises. These practices are detailed in Note 3 to the Consolidated Financial Statements.

Hydro-Québec would like to point out that this MD&A, and especially the Outlook section, contains statements based on estimates and assumptions concerning future results and the course of events. Given the risks and uncertainties inherent in any forward-looking statements, Hydro-Québec's actual future results could differ materially from those anticipated. It should also be noted that certain financial and operating data for previous years have been reclassified to conform to the presentation adopted for the current year. Finally, the information contained herein takes into account any significant event that occurred on or before March 13, 2009.

Management's Discussion and Analysis

Overview

Net Income



Income from continuing operations
Income from discontinued operations

Net income totaled $3,141 million, an increase of $234 million compared to 2007. The increase is due to growth of $380 million in net electricity exports by Hydro-Québec Production, which correspond to electricity sales outside Québec less short-term electricity purchases for exports, and a $126-million non-recurring gain related to the price adjustments provided for in the contract of sale for the interest in HQI Transelec Chile S.A. ("Transelec"), in Chile. Water-power royalties paid by Hydro-Québec Production totaled $552 million, compared to $267 million in 2007. It should be noted that, in 2008, income from continuing operations was the highest in Hydro-Québec's history.

Revenue totaled $12,717 million, an increase of $387 million (3%) from the previous year. Revenue from electricity sales reached $12,364 million, compared to $11,985 million in 2007, an increase of $379 million due to higher electricity sales in Québec ($77 million) and outside Québec ($302 million).

Total expenditure reached $7,260 million, an increase of $324 million from 2007. The difference stems mainly from a $328-million increase in amortization expense for regulatory assets and liabilities arising from variances in Hydro-Québec Distribution's transmission and electricity procurement costs; this expense was recognized in accordance with the conditions established by the Régie de l'énergie. On the other hand, electricity purchases made by this division in excess of the heritage pool decreased by $228 million. Capital tax decreased by $76 million, primarily because of a lower rate of taxation, while water-power royalties levied on Hydro-Québec Production rose by $285 million. It should be noted that in 2007, a transition year, the half-rate rule applied.

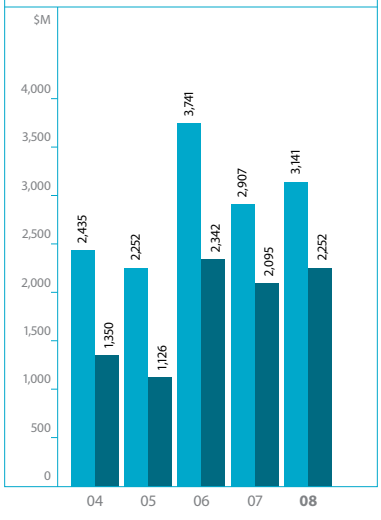
Return on equity totaled 15.4% compared to 15.0% in 2007. This indicator is evidence of our healthy financial performance.

Cash from operations totaled $5.0 billion. Among other things, this cash allowed us to pay the dividends of $2,095 million declared for 2007 and to finance a large part of our investments. The size of our capital program, which reached $4.0 billion in 2008, compared to $3.6 billion in 2007, reflects our continued involvement in major projects in the Generation and Transmission sectors, such as the Eastmain-1-A/Sarcelle/Rupert hydroelectric development and the 1,250-MW interconnection with Ontario.

Dividends declared from 2004 to 2008 totaled $9.2 billion, including $2,252 million for 2008.

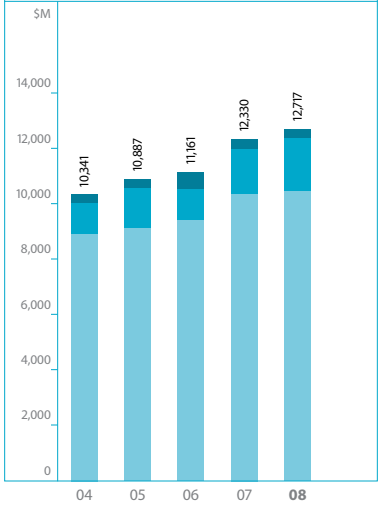
Consolidated Results

Net Income and Dividends Declared



Net income
Dividends declared

Revenue



Electricity sales in Québec
Electricity sales outside Québec
Other revenue

Note: Certain comparative figures have been reclassified to reflect the presentation adopted for 2008.

Net income totaled $3,141 million compared to $2,907 million in 2007. This $234-million increase was due to growth of $380 million in net electricity exports by Hydro-Québec Production and a $126-million gain related to the price adjustments provided for in the contract of sale for the interest in Transelec, in Chile. However, these factors were offset by a $285-million increase in water-power royalties levied on Hydro-Québec Production.

Revenue increased by $387 million to $12,717 million. Revenue from electricity sales rose $379 million to $12,364 million. Sales in Québec accounted for $10,445 million of this amount, or $77 million more than in 2007. In markets outside Québec, revenue from electricity sales totaled $1,919 million, an increase of $302 million. Other revenue totaled $353 million, as against $345 million in 2007. This increase is primarily due to higher revenue from point-to-point transmission services to external customers.

The $77-million increase in revenue from electricity sales in Québec resulted primarily from the April 1, 2007 and 2008, rate adjustments, which were partially offset by the effect of milder temperatures in 2008 and a decrease in demand, particularly in the industrial category.

The $302-million increase in revenue from electricity sales in markets outside Québec is mainly due to Hydro-Québec Production's higher export volume.

Total expenditure amounted to $7,260 million, an increase of $324 million compared to 2007.

Operating expenses were $2,497 million in 2008, down $44 million from $2,541 million in 2007. Indexation and inflation, partially offset by efficiency gains, accounted for a $40-million increase in expenses. The higher volume of activity, related to commissioning Péribonka generating station and some specific work approved by the Régie de l'énergie with regard to distribution system performance, accounted for a $10-million increase. Moreover, restoration of service following weather-related events in 2008 resulted in additional expenditure of $13 million. However, these factors were more than offset by the $125-million decline in pension costs on account of the actuarial effect of higher long-term interest rates on capital markets.

Electricity and fuel purchases totaled $1,406 million in 2008, as against $1,555 million in 2007. The difference is mainly due to a reduction in electricity purchases in excess of the heritage pool by Hydro-Québec Distribution.

Depreciation and amortization expense totaled $2,336 million, an increase of $345 million from 2007, primarily because of a $328-million increase in amortization expense for regulatory assets and liabilities arising from variances in Hydro-Québec Distribution's transmission and electricity procurement costs. This expense was recognized in accordance with the conditions established by the Régie de l'énergie. In fact, amortization of the regulatory asset related to the cost of native load transmission service for 2005 to 2007 totaled $243 million in 2008 compared to $70 million in 2007, an increase of $173 million. Furthermore, amortization of the regulatory liability related to cost variances in electricity purchases in excess of the heritage pool reduced the depreciation and amortization expense by $60 million in 2008, compared to a reduction of $215 million in 2007, accounting for $155 million of the increase. It should be noted that amortization of these two items was taken into account in setting the electricity rates that came into force in April 2008 and 2007.

Taxes were $1,093 million, an increase of $273 million over 2007, basically due to a $285-million increase in water-power royalties levied on Hydro-Québec Production. It should be noted in 2007, a transition year, the half-rate rule applied. Capital tax decreased by $76 million, primarily because of a lower rate of taxation, which decreased from 0.49% to 0.36%.

Regulatory deferrals in 2008 resulted in the recognition of $130 million in regulatory assets and a regulatory liability of $58 million, essentially for revenue variances related to weather conditions and cost variances in electricity purchases in excess of the heritage pool.

With regard to revenue variances related to weather conditions, a $126-million regulatory asset was recognized for differences between Hydro-Québec Distribution's actual transmission and distribution revenue and the revenue forecasts established on the basis of weather normals for rate application purposes. This accounting practice is consistent with the regulatory principle of smoothing for weather conditions approved by the Régie de l'énergie. This asset was recognized as a result of Hydro-Québec Distribution's 2009–2010 rate application, which includes a mechanism for amortizing these differences.

As for cost variances related to electricity purchases in excess of the heritage pool, a $58-million regulatory liability was recorded to take into account the fact that the actual cost of supplying electricity in excess of the heritage pool was lower than the cost forecasted for the purpose of rate-setting by the Régie de l'énergie.

Financial expenses totaled $2,445 million compared to $2,512 million in 2007, a $67-million reduction. The difference is due in part to an increase in the capitalized financial expenses presented as a decrease in financial expenses. The increase in the average value of capital projects under construction, in particular due to continued work at the Eastmain-1-A/Sarcelle/Rupert jobsite, had the effect of increasing capitalized financial expenses. The difference is also due to the effect of converting U.S. dollar–denominated working capital into Canadian dollars, given the depreciation of the Canadian dollar during the last quarter of 2008.

Discontinued operations contributed approximately $129 million to net income, compared to $25 million in 2007. The 2008 income is essentially the result of a $126-million gain related to the price adjustments provided for in the contract of sale for the interest in Transelec, in Chile. These adjustments were made following the ministerial order establishing the value of the regulated trunk transmission asset base of Transelec and the retrospective effect of this revised valuation on Transelec's revenue for the period from March 13, 2004, to June 30, 2006. It should be noted that 2007 income included an $18-million gain on the sale of our interest in DirectLink, in Australia.

	2008	2007
OPERATIONS AND DIVIDENDS ($M)		
Revenue	**12,717**	12,330
Operating income	**5,457**	5,394
Income from continuing operations	**3,012**	2,882
Net income	**3,141**	2,907
Dividends declared	**2,252**	2,095
BALANCE SHEETS ($M)		
Total assets	**66,774**	64,866
Property, plant and equipment	**54,987**	53,291
Long-term debt, including current portion and perpetual debt	**36,415**	34,534
Equity	**22,062**	20,892
RATIOS		
Interest coverage	**2.12**	2.13
Return on equity (%)	**15.4**	15.0
Profit margin from continuing operations (%)	**23.7**	23.4
Capitalization (%)	**37.7**	37.5
Self-financing (%)	**44.9**	61.9

Note: Certain comparative figures have been reclassified to reflect the presentation adopted for 2008.

Financial Position

Operating activities

Cash from operating activities totaled $5.0 billion in 2008 compared to $5.2 billion in 2007. These funds were mainly used to finance a large part of our investments and to pay the dividends declared for 2007.

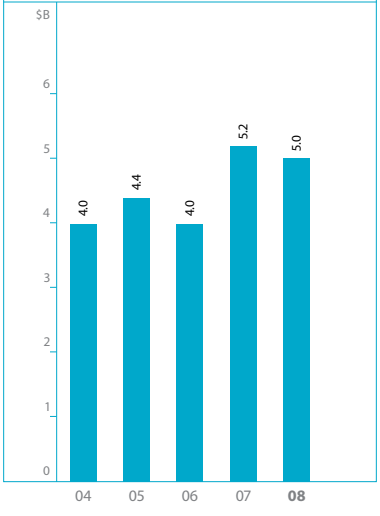
Investing activities

In 2008, Hydro-Québec invested $4.0 billion in property, plant and equipment, intangible assets and the Energy Efficiency Plan (EEP), compared to $3.6 billion in 2007. Of the total, $2.3 billion was invested in development projects and $1.5 billion in maintaining or improving the quality of assets, while $0.2 billion went to the EEP.

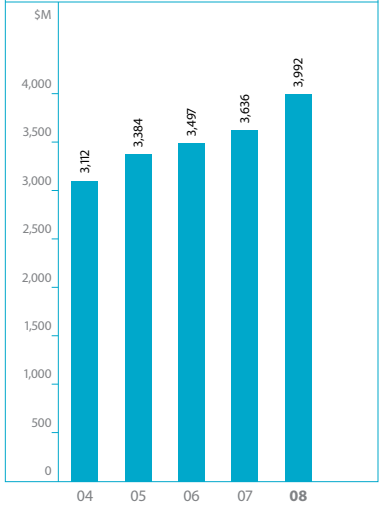
Hydro-Québec Production invested a total of $1,894 million in 2008 compared to $1,807 million in 2007. As expected, a large portion of this amount, $1,403 million, was invested in development projects, such as the Eastmain-1-A/Sarcelle/Rupert, Péribonka (last two generating units commissioned in 2008), Chute-Allard and Rapides-des-Cœurs hydroelectric developments. The amounts allocated to asset maintenance and improvement totaled $491 million. Most of this was earmarked for engineering work and procurement activities related to the refurbishment of Gentilly-2 nuclear generating station and work at La Tuque, Beauharnois and Outardes-4 generating stations.

Hydro-Québec TransÉnergie's capital investments in 2008 totaled $1,097 million, with approximately 50% to increase transmission capacity and integrate the output from new hydroelectric and wind power facilities, including connecting Péribonka, Chute-Allard and Rapides-des-Cœurs generating stations to the grid, along with continuing work to integrate output from wind farms in the Gaspé peninsula and build a 1,250-MW interconnection with Ontario, the components of which will be commissioned in 2009 and 2010. The remainder was devoted to long-term transmission system operability and improving of service quality.

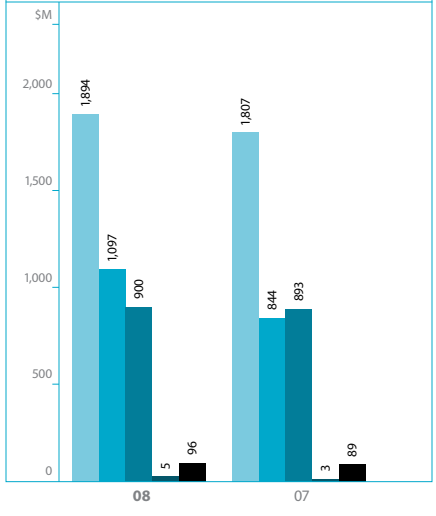
Cash from Operations



Investments in Property, Plant and Equipment, Intangible Assets and the EEP[a]



Investments in Property, Plant and Equipment, Intangible Assets and the EEP[a] by Segment



a) EEP: Energy Efficiency Plan

Note: Certain comparative figures have been reclassified to reflect the presentation adopted for 2008.

Hydro-Québec Distribution invested $664 million in order to handle the growth in the number of subscribers, ensure the long-term operability of the distribution system and enhance service quality. An additional $236 million was allocated to the EEP.

Hydro-Québec Équipement and Société d'énergie de la Baie James carry out engineering, construction and refurbishment projects for Hydro-Québec Production and Hydro-Québec TransÉnergie.

Financing activities

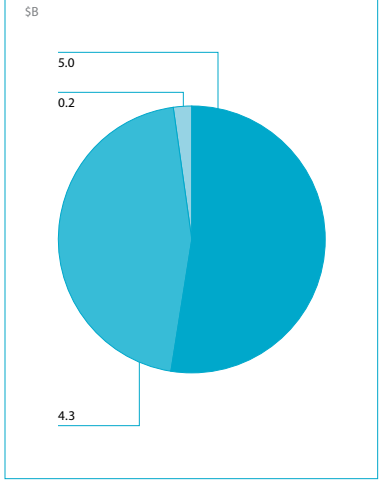
Issuance of long-term debt and cash inflows related to credit risk management totaled $4.3 billion in 2008.

The borrowing program included the reopening, on February 19, April 25, May 16 and September 2, 2008, of a bond issue maturing in February 2045, which raised $2 billion at an average rate of 4.91%, exclusively on the Canadian market.

Hydro-Québec manages its credit risk using a number of methods, including the adoption of credit limits for each counterparty and the implementation of risk mitigation agreements. Changes in the market value of the financial instruments subject to these agreements beyond an agreed level give rise to a cash inflow or outflow. In 2008, net cash inflows of $2.3 billion were recognized in this regard and no counterparty failed to fulfill its obligations.

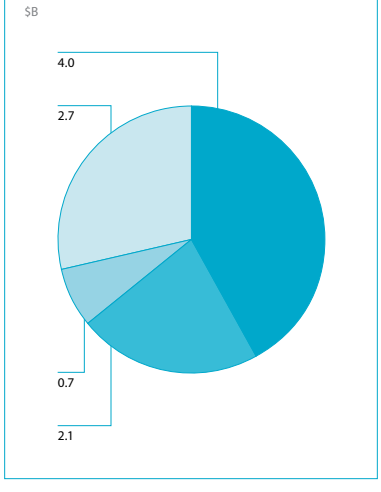
The proceeds from all these activities financed a portion of our investments and were also used to repay certain debts.

Sources of Funds in 2008



- Cash from operations
- Issuance of long-term debt and cash inflows related to credit risk management
- Sale of interest and investments

Uses of Funds in 2008



- Investments in property, plant and equipment, intangible assets and the EEP[a]
- 2007 dividends paid in 2008
- Change in cash, cash equivalents and short-term investments
- Repayment of long-term debt

a) EEP: Energy Efficiency Plan

PREAUTHORIZED CAPITAL RESOURCES

Type of financing	Authorized volume	Market	Outstanding as at December 31, 2008
Credit lines	US$350 million or C$350 million		–
	C$40 million		–
	US$110 million		–
Standby credit[a]	US$2,000 million		–
Commercial paper[a]	US$2,250 million or equivalent in C$	United States or Canada	C$91 million
Medium-term notes[a]	US$3,000 million or equivalent in other currencies	United States	US$440 million
	C$16,000 million or equivalent in US$	Canada	C$10,986 million

a) Guaranteed by the Québec government.

CREDIT RATINGS

	2008		2007	
	Commercial paper	Long-term	Commercial paper	Long-term
U.S. agencies				
Moody's	**P-1**	**Aa2 stable**	P-1	Aa2 stable
Fitch Ratings	**F1+**	**AA- positive**	F1+	AA- stable
Standard & Poor's	**A-1+**	**A+**	A-1+	A+
Canadian agency				
DBRS	**R-1 (middle)**	**A (high) stable**	R-1 (middle)	A (high) stable

Dividends and capitalization rate

Since Hydro-Québec has met all the requisite conditions, dividends totaling $2,252 million were declared for 2008. When these dividends are factored in, the capitalization rate is 37.7%. Dividends declared from 2004 to 2008 total $9.2 billion.

Segmented Information

As in 2007, Hydro-Québec had four operating segments, namely Generation, Transmission, Distribution and Construction, as well as activities grouped under Corporate and Other Activities.

On February 15, 2008, the Régie de l'énergie approved the inclusion of telecommunications assets related to transmission activities in Hydro-Québec TransÉnergie's rate base. These assets, which were transferred from the Groupe de la technologie to Hydro-Québec TransÉnergie, as well as the related investment projects, have therefore been regulated since January 1, 2008. However, management of telecommunications activities remains the responsibility of the Groupe de la technologie. Costs related to these assets were already taken into account in the rate-setting.

Segmented financial information ($M)	Generation	Transmission	Distribution	Construction	Corporate and Other Activities	2008 Hydro-Québec[a]
Revenue	**6,997**	**2,785**	**10,602**	**2,416**	**1,188**	**12,717**
Net income	**2,137**	**481**	**421**	**–**	**90**	**3,141**
Total assets	**30,651**	**17,158**	**12,274**	**360**	**6,734**	**66,774**

Segmented financial information ($M)	Generation	Transmission	Distribution	Construction	Corporate and Other Activities	2007 Hydro-Québec[a]
Revenue	6,752	2,822	10,508	2,150	1,212	12,330
Net income	2,077	396	395	–	27	2,907
Total assets	29,509	16,707	11,833	263	6,814	64,866

a) Includes the intersegment eliminations presented in Note 24 to the consolidated financial statements.

Note: Certain comparative figures have been reclassified to reflect the presentation adopted for 2008.

Segment highlights

The **Generation** segment recorded net income of $2,137 million in 2008 compared to $2,077 million in 2007, for an increase of $60 million. Net electricity exports increased by $380 million, while net revenue from special contracts with large industrial customers in Québec decreased by $86 million, because of additional transmission costs for these contracts in accordance with the conditions established by the Régie de l'énergie. Capital tax decreased by $38 million while water-power royalties rose by $285 million. It should be noted that in 2007, a transition year, the half-rate rule applied.

The **Transmission** segment's net income was $481 million in 2008 compared to $396 million in 2007. This rise is mainly due to an $18-million year-over-year increase in revenue from point-to-point transmission services. In addition, since these services generated $203 million in revenue, whereas the Régie de l'énergie had approved forecasts of $204 million, the division recorded a regulatory asset of $1 million as revenue variances in point-to-point transmission services. It should be noted that in 2007, a $50-million regulatory liability was recorded in this regard, giving rise to a $51-million increase in income in 2008. These items were partially offset by an $11-million decrease in revenue from native load transmission service. In addition, capital tax decreased by $24 million.

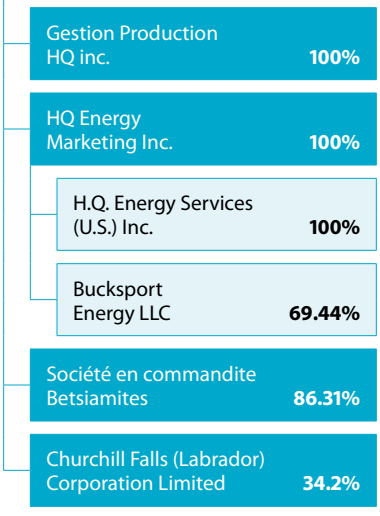
The **Distribution** segment recorded net income of $421 million in 2008 compared to $395 million in 2007. An $85-million increase in revenue from electricity sales and a $222-million reduction in net electricity purchases in excess of the heritage pool and transmission costs, as well as a $13-million decrease in capital tax, were offset by a $343-million increase in amortization expense for regulatory assets and liabilities arising mainly from variances in transmission and electricity procurement costs. The amortization expense was recognized in accordance with the conditions established by the Régie de l'énergie.

An amount of $71 million was recorded as a regulatory deferral in 2008 compared to $21 million in 2007.

The **Construction** segment recorded a volume of activity of $2,416 million compared to $2,150 million in 2007. As in 2007, this high volume stems from construction work on several major projects.

Generation

Hydro-Québec Production



- Hydro-Québec division
- Subsidiary, joint venture or interest held by Hydro-Québec and under the responsibility of Hydro-Québec Production

Under the *Act respecting the Régie de l'énergie,* Hydro-Québec Production is required to provide Hydro-Québec Distribution with up to 165 TWh a year of heritage pool electricity, at an average price of 2.79¢/kWh. The division sells its excess output on deregulated markets in northeastern North America, including Québec, at market prices. It may also compete for contracts under Hydro-Québec Distribution's open tendering process.

The division operates 64 generating stations. Its capital projects serve a twofold objective: to ensure the long-term operability of existing facilities and to continue development of Québec's hydroelectric potential.

Operating results

Hydro-Québec Production recorded net income of $2,137 million in 2008 compared to $2,077 million in 2007, an increase of $60 million. Net electricity exports increased by $380 million while net revenue from special contracts with large industrial customers in Québec decreased by $86 million because of additional transmission costs for these contracts in accordance with the conditions established by the Régie de l'énergie. Capital tax decreased by $38 million while water-power royalties rose by $285 million. It should be noted that in 2007, a transition year, the half-rate rule applied.

Electricity sales in Québec

In 2008, the total volume of electricity sales to Hydro-Québec Distribution was 170.2 TWh, compared to 171.5 TWh in 2007, for a decrease of 1.3 TWh. Revenue generated by these sales decreased by $83 million to $4,839 million. This reduction is mainly due to a drop in electricity sales in excess of the heritage pool following approval by the Régie de l'énergie of Hydro-Québec Production's contracts with Hydro-Québec Distribution to postpone some contractual deliveries (350 MW in baseload power and 250 MW in cycling deliveries) for the period from 2008 to 2011.

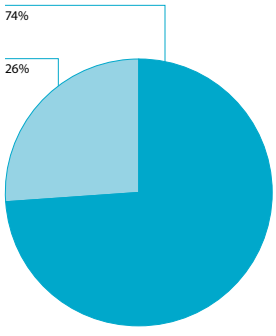
Electricity sales outside Québec

Electricity sales outside Québec generated revenue of $1,897 million for 21.1 TWh in 2008 compared to $1,483 million for 17.5 TWh in 2007. Short-term electricity sales earned $1,677 million for 18.6 TWh compared to $1,258 million for 15.2 TWh in 2007, a $419-million increase that is mainly due to higher sales volumes and favorable market conditions.

Net electricity exports were $1,484 million in 2008 for a net reservoir drawdown of 15.2 TWh compared to $1,104 million for 10.7 TWh in 2007. This represented a unit contribution of 9.8¢/kWh in 2008 against 10.3¢/kWh in 2007.

It should be noted that as at December 31, 2008, energy reserves stood at 116.5 TWh, equivalent to the 2007 level.

Breakdown of 2008 Investments by Hydro-Québec Production



Development
Maintenance and improvement

Operating expenses

Operating expenses totaled $808 million in 2008, a decrease of $32 million from 2007. Indexation, inflation and growth in activity after the commissioning of Mercier and Péribonka generating stations increased expenses, but these factors were more than offset by the reduction in pension costs.

Electricity and fuel purchases

Electricity and fuel purchases totaled $1,277 million in 2008, an increase of $56 million over 2007. This increase is mainly due to a $35-million rise in transmission system reservation expenses, chiefly because of higher sales volumes outside Québec. Short-term purchases for export reached $380 million for 5.2 TWh compared to $373 million for 6.3 TWh in 2007.

Investing activities

Investments in property, plant and equipment and intangible assets affecting cash totaled $1,894 million in 2008. Of this amount, $1,403 million went to development activities, including work on Eastmain-1-A/Sarcelle/Rupert, Chute-Allard and Rapides-des-Cœurs, Péribonka (last two generating units commissioned in 2008) and Romaine (in the government approval phase).

Hydro-Québec Production also invested $491 million in rehabilitating and refitting its facilities. Most of this amount was earmarked for engineering work and procurement activities related to the refurbishment of Gentilly-2 nuclear generating station and work at La Tuque, Beauharnois and Outardes-4 generating stations.

Transmission

Hydro-Québec TransÉnergie

Cedars Rapids Transmission Company, Limited **100%**

- ☐ Hydro-Québec division
- ■ Subsidiary held by Hydro-Québec and under the responsibility of Hydro-Québec TransÉnergie

Hydro-Québec TransÉnergie transmits power at the lowest possible cost while meeting demand growth and customer expectations in terms of power quality. The division ensures the reliability, long-term operability and optimal deployment of the power transmission system in Québec with a view to sustainable development.

The operations of Hydro-Québec TransÉnergie are regulated by the Régie de l'énergie.

Rate cases

For 2008, the revenue authorized by the Régie de l'énergie for transmission rate-setting purposes totaled $2,733 million, including $2,529 million in native load transmission revenue (representing an $11-million decrease from 2007) and $204 million for short- and long-term point-to-point transmission services.

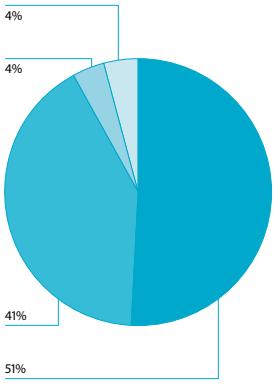
In 2007 the Régie established a new variance account corresponding to the difference between revenue forecasts for point-to-point transmission services recognized by the Régie for rate-setting purposes and actual point-to-point transmission service revenue. This mechanism makes it possible to attribute positive or negative revenue variances to native load customers and long-term point-to-point transmission service customers. In February 2008, the Régie set the conditions governing these variances, which resulted in a one-time $41-million reduction in 2008 of the annual cost of native load transmission service.

In a decision handed down on March 5, 2009, the Régie authorized Hydro-Québec TransÉnergie to modify its transmission rates, effective January 1, 2009. This decision reflects a revenue requirement of $2,824 million for 2009, of which $2,575 million is allocated to native load transmission service and $249 million to short- and long-term point-to-point transmission services.

Operating results

Hydro-Québec TransÉnergie's net income was $481 million in 2008 compared to $396 million in 2007. This $85-million rise is mainly due to an $18-million year-over-year increase in revenue from point-to-point transmission services. In addition, since these services generated $203 million in revenue, whereas the Régie had approved forecasts of $204 million, the division recorded a regulatory asset of $1 million as revenue variances in point-to-point transmission services. It should be noted that in 2007, a $50-million regulatory liability was recorded in this regard, giving rise to a $51-million increase in income in 2008. These items were partially offset by an $11-million decrease in revenue from native load transmission service. In addition, capital tax decreased by $24 million.

Breakdown of 2008 Investments by Hydro-Québec TransÉnergie



- Growth
- Maintenance
- Improvement
- Compliance with requirements

Investing activities

In 2008, Hydro-Québec TransÉnergie invested $1,097 million in property, plant and equipment and intangible assets affecting cash, or $559 million for growth and $538 million for ongoing operations. Ongoing operations involve ensuring the long-term operability of facilities, improving service quality and complying with the legal and regulatory requirements for operating a power transmission system.

The purpose of the growth projects was to increase transmission capacity and bring new hydropower plants and wind farms onto the grid.

The division therefore invested some $249 million in the construction of the 1,250-MW interconnection between Québec and Ontario, which began at the end of 2006 under an agreement between Hydro-Québec TransÉnergie and Hydro One Networks. Most of this amount went into building a 315/230-kV converter station in the Outaouais region. A 315-kV line will also be built between Chénier and Outaouais substations. The facilities are scheduled to be commissioned in 2009 and 2010. The total cost of the project is estimated at $654 million.

Some $21 million was invested during the year to connect Péribonka, Chute-Allard and Rapides-des-Cœurs generating stations. Finally, the division invested $95 million to integrate the output from eight wind farms to be commissioned in the Gaspésie region by 2012 in response to Hydro-Québec Distribution's first tender call for wind power issued in 2003. Connecting these wind farms, which represent a total capacity of 990 MW, will require an investment of some $600 million through 2012.

In 2008, Hydro-Québec TransÉnergie invested $538 million in ongoing operations, including $446 million in replacing equipment and refurbishing facilities. In addition, it invested $43 million in improving service quality, including $10 million to reinforce the transmission system by installing de-icing equipment at Lévis substation. The work was completed in December 2008.

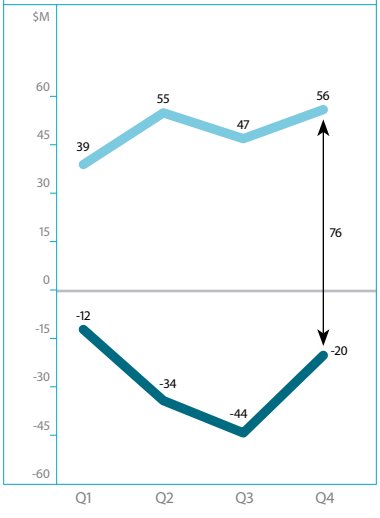
Distribution

Hydro-Québec Distribution

Centre d'innovation sur le transport d'énergie du Québec (CITEQ) inc. **50%**

- Hydro-Québec division
- Interest held by Hydro-Québec and under the responsibility of Hydro-Québec Distribution

Cumulative Effect of Temperatures Compared to Normal



- 2008
- 2007
- Normal temperature

Hydro-Québec Distribution provides electricity to the Québec market and delivers reliable power and quality services to its customers with a view to efficiency and sustainable development. In this context, it also promotes energy-saving measures among its customers.

The division's activities are regulated by the Régie de l'énergie, which has exclusive jurisdiction to set electricity rates.

Rate cases

In February 2008, the Régie approved an across-the-board rate increase of 2.9%, effective April 1, 2008. In March 2009, it approved an across-the-board rate increase of 1.2% for 2009–2010. This will make it possible to absorb certain net costs related to disposal of property, plant and equipment and intangible assets and to recover a portion of the regulatory asset recognized in the revenue variance account for weather conditions. This regulatory practice, accepted by the Régie, reflects the variances between actual transmission and distribution revenue and the revenue forecasts based on weather normals for rate application purposes.

Supplying the Québec market

Hydro-Québec Distribution relies on various sources to supply the Québec market. To meet requirements in excess of the heritage pool (165 TWh) reserved for it by Hydro-Québec Production, the division issues short- and long-term calls for tender. For requirements of less than three months, it may also buy electricity directly in the market, without a call for tender, under an exemption granted by the Régie. For unforeseen needs that cannot be met otherwise, the division relies on a master agreement with Hydro-Québec Production. Since the agreement in effect expired on December 31, 2008, the two divisions signed a new five-year agreement, which has been submitted to the Régie de l'énergie for approval.

In 2008, the Régie de l'énergie approved the Electricity Supply Plan for 2008–2017, which was submitted by Hydro-Québec Distribution in 2007. This plan forecasts the electricity needs of the Québec market, taking into account the energy savings expected from energy efficiency programs and the inclusion of wind power in the division's available resources.

To help Hydro-Québec Distribution balance supply and demand, the Régie also approved the following measures:

- Renewal until the end of 2009 of an agreement signed with TransCanada Energy in 2008 to suspend deliveries of power provided for in the supply contract with this supplier; and
- Postponement until 2012–2020 of contractual deliveries planned for 2008–2011 in the supply contracts with Hydro-Québec Production for electricity in excess of the heritage pool.

The Carleton wind farm made its first deliveries in November 2008. Combined with the supply from the wind farms at L'Anse-à-Valleau and Baie-des-Sables, this brings the division's wind power purchases to approximately 1 TWh per year, for an installed capacity of 319.5 MW.

In October 2008, the Régie approved 15 electricity supply contracts signed by Hydro-Québec Distribution under the second tender call issued in 2005 for the purchase of a block of 2,000 MW of wind power produced in Québec. The first deliveries under these contracts are scheduled for December 2011.

Finally, Hydro-Québec Distribution is continuing its efforts to promote energy efficiency. Given the results of recent years, the annual energy savings target was set at 5.8 TWh by 2010, with an eventual target of 11 TWh by 2015.

Operating results

Hydro-Québec Distribution recorded net income of $421 million in 2008 compared to $395 million in 2007. An $85-million increase in revenue from electricity sales and a $222-million reduction in net electricity purchases in excess of the heritage pool and transmission costs, as well as a $13-million decrease in capital tax, were offset by a $343-million increase in amortization expense for regulatory assets and liabilities arising mainly from variances in transmission and electricity procurement costs. The amortization expense was recognized in accordance with the conditions established by the Régie de l'énergie.

An amount of $71 million was recorded as a regulatory deferral in 2008 compared to $21 million in 2007.

ELECTRICITY SALES IN QUÉBEC BY CATEGORY

		Sales volume			Sales revenue	
	2008	2008–2007 change		**2008**	2008–2007 change	
Customer category	TWh	TWh	%	$M	$M	%
Residential and farm	**60.7**	0.7	1.2	**4,300**	156	3.8
General and institutional	**35.2**	0.5	1.4	**2,687**	85	3.3
Industrial	**69.2**	(3.8)	(5.2)	**3,174**	(162)	(4.9)
Other	**5.2**	–	–	**279**	6	2.2
Total	**170.3**	(2.6)	(1.5)	**10,440**	85	0.8

FACTORS IN THE 2008–2007 CHANGE IN SALES BY CATEGORY

							Volume effects			Price effects	**Total**
	Baseload demand		Temperature		February 29		**Total**	Rate adjust-ments	Other	**Total**	
Customer category	TWh	$M	TWh	$M	TWh	$M	$M	$M	$M	$M	$M
Residential and farm	1.1	75	(0.7)	(56)	0.3	18	**37**	108	11	**119**	**156**
General and institutional	0.7	45	(0.4)	(18)	0.1	10	**37**	68	(20)	**48**	**85**
Industrial	(4.0)	(189)	–	(1)	0.2	9	**(181)**	63	(44)	**19**	**(162)**
Other	0.1	4	–	(1)	–	1	**4**	8	(6)	**2**	**6**
Total	(2.1)	(65)	(1.1)	(76)	0.6	38	**(103)**	247	(59)	**188**	**85**

Electricity sales in Québec

Electricity sales revenue reached $10,440 million, an increase of $85 million over 2007. This increase primarily resulted from the April 1, 2007 and 2008 rate adjustments, which were partially offset by the effect of milder temperatures in 2008 and a decrease in demand.

Sales volume was 170.3 TWh, a decrease of 2.6 TWh from 172.9 TWh in 2007, mainly the result of milder temperatures in 2008 (–1.1 TWh) and a decrease in demand (–2.1 TWh). In this regard, sales volume for the Industrial category declined by 4.0 TWh because of the economic slowdown and mill and plant closures in the pulp and paper and chemical sectors. By contrast, sales in the Residential and farm and General and institutional categories increased by 1.8 TWh primarily because of growth in the number of customer contracts and conversions to electric heating.

Operating expenses

Operating expenses were $1,169 million in 2008 compared to $1,121 million in 2007, an increase of $48 million. Indexation and inflation, partially offset by efficiency gains, resulted in a $17-million increase in expenses. The cost of specific work approved by the Régie de l'énergie, principally with regard to distribution system performance, increased by $6 million. Restoration of service following weather-related events in 2008 resulted in additional expenses of $13 million.

Electricity purchases and cost of transmission

Net electricity purchases in excess of the heritage pool decreased by $170 million from 2007 due to milder temperatures in 2008 than in 2007 and a decrease in baseload demand.

The cost of native load transmission service decreased by $11 million from 2007. Added to this was a one-time $41-million reduction in native load arising from the inclusion in 2008 of the variance account recognized in 2007 for revenue from point-to-point transmission services at Hydro-Québec TransÉnergie. It should be noted that actual point-to-point transmission service revenue in 2007 was higher than the forecasts submitted in the rate application. This reduction brought the total decrease in the cost of native load transmission service to $52 million.

Amortization of regulatory assets and liabilities

In 2008, a net increase of $343 million was recorded in the amortization expense for regulatory assets and liabilities, arising from variances in transmission and electricity procurement costs. In fact, amortization of the regulatory asset related to the cost of native load transmission service for 2005 to 2007 totaled $243 million in 2008 compared to $70 million in 2007, an increase of $173 million. Furthermore, amortization of the regulatory liability related to cost variances in electricity purchases in excess of the heritage pool reduced the depreciation and amortization expense by $60 million in 2008, compared to a reduction of $215 million in 2007, accounting for a $155-million increase.

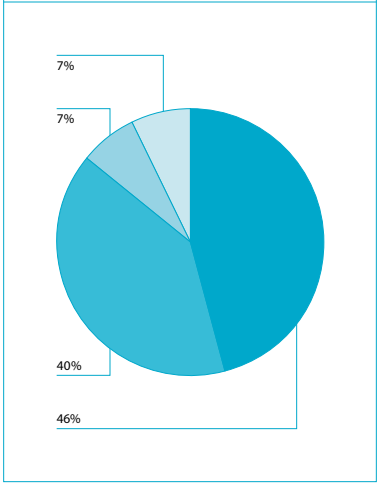
Regulatory deferrals

Regulatory deferrals in 2008 resulted in the recognition of $129 million in regulatory assets and a regulatory liability of $58 million, primarily for revenue variances related to weather conditions and to cost variances in electricity purchases in excess of the heritage pool.

With regard to revenue variances related to weather conditions, a $126-million regulatory asset was recognized for differences between Hydro-Québec Distribution's actual transmission and distribution revenue and the revenue forecasts established on the basis of weather normals for rate application purposes. This accounting practice is consistent with the regulatory principle of smoothing for weather conditions approved by the Régie de l'énergie. This asset was recognized as a result of Hydro-Québec Distribution's 2009–2010 rate application, which includes a mechanism for amortizing these differences.

As for cost variances related to electricity purchases in excess of the heritage pool, a $58-million regulatory liability was recorded to take into account the fact that the actual cost of supplying electricity in excess of the heritage pool was lower than the cost forecasted for the purpose of rate-setting by the Régie de l'énergie.

Breakdown of 2008 Investments by Hydro-Québec Distribution



- Growth
- Maintenance
- Improvement
- Compliance with requirements

Investing activities

Under the category of investments affecting cash, Hydro-Québec Distribution invested $664 million in property, plant and equipment and intangible assets in 2008.

Of this amount, $308 million went toward meeting growth in demand in Québec, including $208 million to hook up new customers. The division also invested $264 million to ensure long-term distribution system operability and $47 million to improve service quality, including $26 million for the system automation program, which will permit remote monitoring of equipment and improvements to the service continuity index.

Hydro-Québec Distribution also invested $236 million in the Energy Efficiency Plan. It should be noted that in 2008, energy efficiency programs yielded savings of approximately 1.1 TWh.

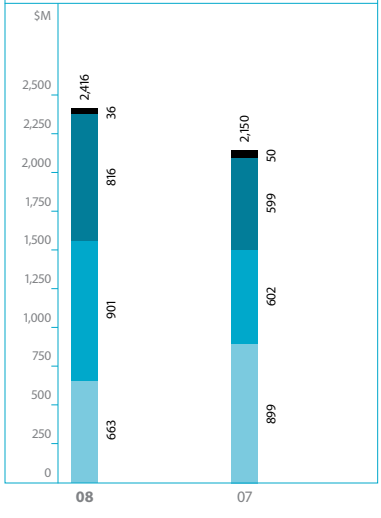
Construction

Hydro-Québec Équipement

Société d'énergie de la Baie James **100%**

- Hydro-Québec division
- Subsidiary held by Hydro-Québec and under the responsibility of Hydro-Québec Équipement

Breakdown of Construction Segment Activities



Hydro-Québec Production
- Hydro-Québec Équipement
- SEBJ

Hydro-Québec TransÉnergie
- Hydro-Québec Équipement and SEBJ

Other
- Hydro-Québec Équipement

Hydro-Québec Équipement carries out engineering, construction and refurbishment projects for power generating facilities throughout Québec, except in the territory governed by the *James Bay and Northern Québec Agreement,* where such work is handled by Société d'énergie de la Baie James (SEBJ). The division is also in charge of power transmission line and substation projects for the company.

As engineering and environmental specialists, Hydro-Québec Équipement and SEBJ also offer Hydro-Québec Production and Hydro-Québec TransÉnergie a variety of services needed for draft-design studies, impact assessments and other undertakings in the context of energy-related projects. These services include technical and scientific surveys, planning, cost estimates, design, architecture, land surveying and quality control.

Volume of activity

Hydro-Québec Équipement and SEBJ carried out activities worth a total of $2,416 million in 2008 compared to $2,150 million in 2007. As in 2007, this high volume can be attributed to several large-scale projects. Work done for Hydro-Québec Production totaled $1,564 million compared to $1,501 million in 2007, while work done for Hydro-Québec TransÉnergie totaled $816 million compared to $599 million in 2007.

Hydro-Québec Équipement

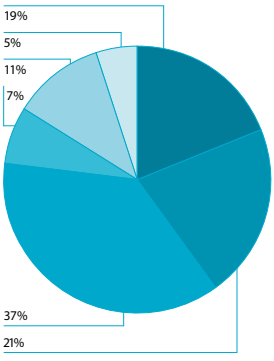
In 2008, Hydro-Québec Équipement carried out activities worth a total of $1,512 million compared to $1,544 million in 2007. This work related to a number of generation and transmission projects, including construction on behalf of Hydro-Québec Production of the Chute-Allard and Rapides-des-Cœurs developments, refurbishment of Gentilly-2 nuclear generating station (engineering work and procurement activities), and work at La Tuque, Beauharnois and Outardes-4 generating stations. The division also continued work for Hydro-Québec TransÉnergie on the 1,250-MW interconnection with Ontario and other projects to increase transmission system capacity.

Société d'énergie de la Baie James

SEBJ's activities, mainly on behalf of Hydro-Québec Production, represented a total of $904 million compared to $606 million in 2007. This increase is due to continuation of the work on the Eastmain-1-A/Sarcelle/Rupert jobsite, which started in January 2007.

Corporate and Other Activities

Breakdown of 2008 Revenue – Groupe des ressources humaines et des services partagés



- Hydro-Québec Production
- Hydro-Québec TransÉnergie
- Hydro-Québec Distribution
- Hydro-Québec Équipement
- Groupe de la technologie
- Other units and external customers

This heading includes corporate activities, the Groupe des ressources humaines et des services partagés, the Groupe de la technologie and the subsidiary Hydro-Québec International.

Results

Corporate and Other Activities recorded net income of $90 million in 2008, compared to $27 million in 2007. This increase is mainly due to a $126-million gain related to the price adjustments provided for in the contract of sale for the interest in Transelec, in Chile. The 2007 figure included an $18-million gain on the sale of the interest in DirectLink, in Australia.

Corporate activities

Corporate activities consist of financial services and corporate affairs. Among other things, the Groupe des affaires corporatives et du secrétariat général coordinates strategic planning. During the year, the Groupe des finances was divided into two departments, the Vice-présidence – Comptabilité et contrôle and the Vice-présidence – Financement, trésorerie et caisse de retraite.

The Vice-présidence – Comptabilité et contrôle is responsible for overseeing accounting (financial, regulatory and management), control and taxation. It also has the task of producing and analyzing the consolidated financial statements. Its other duties include financial planning and risk management.

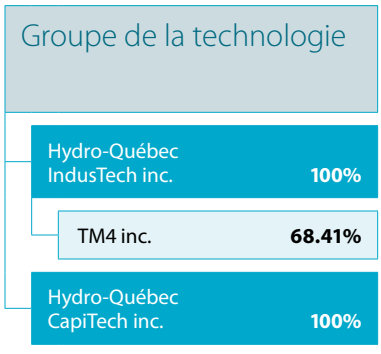
The Vice-présidence – Financement, trésorerie et caisse de retraite is in charge of meeting the company's financing requirements, managing its treasury and maintaining relations with Hydro-Québec bondholders and rating agencies. It also acts as trustee of Hydro-Québec's pension plan.

Groupe des ressources humaines et des services partagés

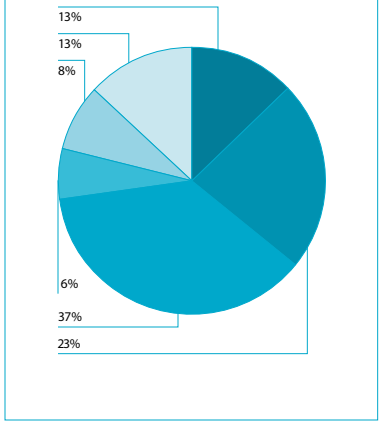
The Groupe des ressources humaines et des services partagés develops strategies, guidelines, frameworks, corporate programs and objectives in matters pertaining to human resources, procurement and services common to the entire company. Its mission includes ensuring that Management benefits from optimum human resources conditions and providing related products and advisory services. The group also provides divisions and corporate units with the support services they need to perform their activities. These services include procurement of goods and services, property management, accounting services, document management, material management and transportation services.

The group's mandate is to provide its customers with quality services tailored to their needs at the lowest possible cost so that they can focus on their core operations.

The group's revenue totaled $509 million in 2008, compared to $499 million in 2007, an increase of 2%.



Breakdown of 2008 Revenue Related to Information Technology and Telecommunications Activities



Groupe de la technologie

The Groupe de la technologie is composed primarily of the Direction principale des télécommunications, the Direction principale de la technologie de l'information, Hydro-Québec's research institute and the subsidiaries Hydro-Québec IndusTech and Hydro-Québec CapiTech. The group's mandate is to ensure the integrated management of technological innovation and the optimal management of telecommunications and information technology infrastructure. With this in mind, it has continued to develop an overall vision for systems governance, architecture and security to build on the convergence of technologies.

■ **Direction principale des télécommunications and Direction principale de la technologie de l'information**

The telecommunications and information technology units enhance the efficiency of divisions and corporate units by offering technology solutions in line with Hydro-Québec's business priorities.

These units recorded revenue of $481 million in 2008 compared to $495 million in 2007.

■ **Research institute**

Hydro-Québec's research institute provides technical assistance to the divisions and carries out technological innovation projects to support their operations and ensure the long-term development of Hydro-Québec. The company allocates approximately $100 million annually to the institute's activities.

■ **Hydro-Québec IndusTech**

The mission of Hydro-Québec IndusTech is to partner with the private sector in industrializing and marketing technologies resulting from Hydro-Québec's research activities. As at December 31, 2008, Hydro-Québec IndusTech held a majority interest in TM4, which develops electric drivetrains. In January 2009, Hydro-Québec IndusTech bought out all the shares of TM4 held by its partner, Groupe Industriel Marcel Dassault.

■ **Hydro-Québec CapiTech**

The venture capital company Hydro-Québec CapiTech invests in businesses that offer energy-related services and technology products.

Investing activities

In 2008, the Groupe de la technologie's investments totaled $74 million, of which $68 million was earmarked for maintaining asset quality and $6 million for meeting growth in demand.

Hydro-Québec International

Hydro-Québec International earned income of $130 million in 2008 as against $35 million in 2007. The 2008 income is primarily the result of a $126-million gain related to the price adjustments provided for in the contract of sale for the interest in Transelec, in Chile. These adjustments were made following the ministerial order establishing the value of the regulated trunk transmission asset base of Transelec and the retrospective effect of this revised valuation on Transelec's revenue for the period from March 13, 2004, to June 30, 2006. It should be noted that 2007 income included an $18-million gain on the sale of the interest in DirectLink, in Australia.

Outlook

In 2009, Hydro-Québec expects to earn net income of $2.7 billion entirely from continuing operations. This projection is $200 million higher than shown in the 2009 outlook of the *Strategic Plan 2006–2010*.

Hydro-Québec plans to invest $5 billion in 2009. Some 60% of this amount will be devoted to development and growth activities as well as to the Energy Efficiency Plan while 40% will be used to finance work to maintain and improve facilities.

Hydro-Québec Production will continue work on major projects to develop the hydroelectric generating fleet. The Eastmain-1-A/Sarcelle/Rupert project will achieve an important milestone, with the Rupert diversion scheduled to go into operation at the end of 2009. The division will start construction on the Romaine complex in the second quarter, subject to the requisite government approvals. It will also finish commissioning Chute-Allard and Rapides-des-Cœurs generating stations. At the same time, the division will continue the engineering work and procurement activities for refurbishing Gentilly-2 nuclear generating station.

Hydro-Québec TransÉnergie will invest a considerable amount in development to accommodate the increased capacity of the hydroelectric fleet and to integrate wind power. It will therefore continue with projects aimed at connecting new hydroelectric and wind power facilities and bringing them onto the grid, in particular Eastmain-1-A and Sarcelle powerhouses and the wind farms built in response to Hydro-Québec Distribution's first call for tender. It will also commission Outaouais substation—one of the components in the new interconnection with Ontario—and Mont-Tremblant substation. The division will also continue to invest in maintenance and improvement activities in order to ensure the reliability and long-term operability of its transmission system and enhance service quality.

Hydro-Québec Distribution will continue to deliver reliable electricity and quality services to its Québec customers. It will pursue its investments to handle the growth of its Québec customer base and to maintain and improve its facilities, including those related to automating the distribution grid. It will also continue to implement the Energy Efficiency Plan, which includes measures for low-income households, to achieve the objective of 11 TWh in energy savings set for 2015. With regard to wind power supply, the division will issue a call for two blocks of 250 MW.

Integrated Enterprise Risk Management

For several years, Hydro-Québec has applied an integrated enterprise risk management process that is now part of its ongoing business practices. This process is supported by various control, communication and assessment mechanisms that enable Hydro-Québec to monitor risk developments on a dynamic basis.

Hydro-Québec's divisions and corporate units are central to the process. As part of their ongoing activities, they manage risks and reassess them, daily in some cases. In concrete terms, each division or corporate unit must determine and assess its main risks and then develop and apply mitigation measures to ensure that residual risks are at a level acceptable to Hydro-Québec. During the annual planning process, this exercise results in a consolidated portfolio of enterprise risks. This portfolio is presented to the Board of Directors with the Strategic Plan or the annual Business Plan, which includes an analysis of the sensitivity of net income to the principal risks. The divisions and corporate units report on their risk management follow-up and activities to the Management Committee, which then acts as a risk management committee to oversee risk management.

ANNUAL INTEGRATED ENTERPRISE RISK MANAGEMENT PROCESS

	January 1 – April 30 1st four-month period	April 30 – August 31 2nd four-month period	August 31 – December 31 3rd four-month period
			Business Plan / **Strategic Plan**
Hydro-Québec Units	Division or group monitoring plans covering main business risks		
	Division or group risk management reports – April review in the form of highlights	Division or group risk management reports – August review in the form of highlights	
		Identification of risks and validation by division/group president	Preparation or revision of division or group business risk portfolios Supporting documents for evaluation
Hydro-Québec Management	**Management Committee and Segment Committees** (in risk management mode)	**Management Committee and Segment Committees** (in risk management mode)	**Management Committee and Segment Committees** (in risk management mode)
	Review of risk management reports included in reviews	Review of risk management reports included in reviews	Review of each division's or group's risk portfolio and discussion
			Management Committee acting as the Risk Management Committee with the President and CEO as CRO
			Review of consolidated enterprise risk portfolio, risk map, quantifiable risks, probability of reaching net income
Board of Directors			**Finance Committee**
			Presentation of consolidated enterprise risk portfolio, risk map, quantifiable risks, probability of reaching net income
			Audit Committee
			President and CEO's report on integrated enterprise business risk management process
			Board of Directors
			Presentation of consolidated enterprise risk portfolio, risk map, quantifiable risks, probability of reaching net income

Financial risks

In the course of its operations, Hydro-Québec carries out transactions that expose it to certain financial risks, such as market, liquidity and credit risk. Rigorous follow-up and the adoption of strategies that include the use of derivative instruments considerably reduce exposure to such risks and their impact on results.

Market risk

Hydro-Québec's results are subject to three types of market risk associated mainly with fluctuations in the Canadian dollar's exchange rate compared to the U.S. dollar as well as fluctuations in interest rates and aluminum prices. Exchange rate fluctuations affect revenue from sales denominated in U.S. dollars as well as the cost of U.S. dollar–denominated debt and swaps. Interest rate fluctuations affect financial expenses, pension costs and the authorized return on equity of regulated divisions. Aluminum price fluctuations have an impact on the net revenue from special contracts with large industrial customers in Québec.

The three types of market risk are subject to active integrated management, in particular through derivative financial products. The purpose of such management is to limit the impact of market risks on Hydro-Québec's short-term results, according to strategies and criteria established based on the company's risk tolerance. Furthermore, Hydro-Québec can count on certain offsetting factors that mitigate its market risk over the medium and long term. For example, it holds debt and swaps denominated in U.S. dollars as a hedge against sales in that currency. The effect of exchange rate fluctuations on sales is thus partially offset by exchange gains or losses on debt in U.S. dollars. There is also an offsetting effect between the impact of a general increase or decrease in interest rates on financial expenses, on the one hand, and the impact of such an increase or decrease on pension costs and the authorized return on equity of regulated divisions, on the other.

Liquidity risk

Liquidity risk is the risk that Hydro-Québec will have difficulty meeting commitments related to its financial liabilities. The present market instability has not had a significant impact on Hydro-Québec's results.

Due to the sharp drop in the markets in 2008, Hydro-Québec expects its pension plan to present a solvency deficiency. However, the Québec government passed Bill 1 to amend the *Supplemental Pension Plans Act* on January 15, 2009. This bill extends the amortization period for consolidated solvency deficiencies of the pension plans covered to 10 years rather than five, and provides for the smoothing of plan assets over a maximum period of five years. Hydro-Québec is currently evaluating the impact of the Bill on its own pension plan and will take the necessary decisions in due course.

Credit risk

Credit risk is the risk that a counterparty may not meet its contractual obligations. Hydro-Québec is exposed to credit risk related to receivables through ongoing energy sales in Québec. These sales are billed at rates that provide for cost recovery according to conditions approved by the Régie de l'énergie. The company is also exposed to credit risk related to cash equivalents, short-term investments and derivative instruments traded with financial institutions and other issuers and, to a lesser extent, with North American energy companies under Hydro-Québec Distribution supply contracts and Hydro-Québec Production energy transactions in markets outside Québec.

Exposure to credit risk is mitigated by the implementation of limits and frameworks for risk concentration and level of exposure by counterparty. To ensure compliance with such limits and frameworks, Hydro-Québec takes a proactive approach based on various controls and monitoring reports. These enable it to react quickly to any event that could have an impact on the financial condition of its counterparties. In addition, the company generally does business with counterparties that have a high credit rating. It also enters into agreements to limit the market value of the main portfolios of derivative instruments.

Operational risk

Generation

One of the principal uncertainties that Hydro-Québec faces is natural runoff. Hydro-Québec Production must ensure that it is able to meet its commitments to supply the annual heritage pool of 165 TWh to Hydro-Québec Distribution and fulfill its contractual obligations. In concrete terms, this means being able to cover a natural runoff deficit of 64 TWh over two consecutive years, and 98 TWh over four consecutive years. To meet this requirement, the division applies a variety of mitigation measures and closely monitors them. In particular, it manages its energy reserves on a multiyear basis and maintains an adequate margin between its generating capacity and its commitments. This allows the division to compensate for runoff shortages, replenish its reserves or take advantage of business opportunities. Hydro-Québec regularly reports to the Régie de l'énergie on Hydro-Québec Production's generating capacity and energy reserves.

Beyond runoff uncertainties and credit risk, Hydro-Québec Production's wholesaling activities are subject to market risk and the risk of unavailability of generation and transmission equipment. Market risk results from fluctuations in electricity and fuel prices, and is mitigated by ongoing monitoring of trends in wholesale markets and the use of hedging derivative instruments. The risk of unavailability of generation and transmission equipment is maintained at a level deemed acceptable through maintenance and upgrade programs.

The risks related to Hydro-Québec Production's marketing activities are quantified in an integrated fashion by a team of specialists that is independent of the group carrying out the transactions. This team sees to the application of controls, presents daily reports to Senior Management and ensures compliance with the limits approved by Management and the Board of Directors.

Transmission

Several factors, such as extreme weather and equipment failure, may cause service interruptions or result in the unavailability of part of the transmission system. The multifaceted strategy adopted by Hydro-Québec TransÉnergie to prevent these problems includes implementing the standards of the North American Electric Reliability Corporation (NERC) and the criteria set by the Northeast Power Coordinating Council (NPCC), as well as measures to maintain and improve transmission facilities and extend their useful life. In 2007 the Régie de l'énergie confirmed the reliability expertise of Hydro-Québec TransÉnergie by designating its Direction du contrôle des mouvements d'énergie (CMÉ), the unit responsible for system control, as Reliability Coordinator for Québec. In this capacity, the CMÉ will file the reliability standards applicable to transmission systems in Québec, as well as a register of entities subject to these standards, with the Régie in 2009.

Over the next few years, Hydro-Québec TransÉnergie must not only ensure adequate transmission capacity to supply Hydro-Québec Distribution and other customers, but also ensure transmission service security and reliability. To do so, the division relies, among other things, on a strategy of ensuring long-term operability of transmission assets and on optimal management of annual peak load.

Distribution

Hydro-Québec Distribution is responsible for supplying electricity to the Québec market. The division's activities are subject to uncertainty related to fluctuations in demand (under normal weather conditions) due to the economic situation, which has an impact on results. When demand is lower than the forecasts made in the rate application, Hydro-Québec Distribution cannot recover from customers all the costs related to power distribution, power transmission through the Hydro-Québec TransÉnergie system and customer service. To counter this risk, the division constantly fine-tunes its method of forecasting short-term demand.

In addition, Hydro-Québec Distribution applies a series of measures to ensure long-term operability of the distribution system, and hence service quality. These measures include compliance with applicable standards for overhead and underground systems, development of a strategy for asset renewal, a maintenance program and vegetation control.

In order to promote better energy use, the division is also pursuing its efforts in the area of energy efficiency.

Construction projects

Strong demand for skilled labor and market-specific inflation may have an impact on Hydro-Québec's project costs. The company has developed strategies to mitigate the impact of economic conditions on procurement and on project completion. Moreover, it applies strict management to contain costs but still meet deadlines, its high standards of quality and security, and the requirements of each project.

Corporate and Other Activities

Environmental protection and conservation are a central concern of Hydro-Québec. Most activities that have a significant impact on the environment are governed by an ISO 14001–certified environmental management system. In addition, every year, the company reviews its management of environmental issues and details them in its Sustainability Report.

Hydro-Québec is also concerned with information security and the risks associated with the misuse of information technologies. It regularly assesses how well its information systems are protected against intrusion and implements the necessary security measures. These measures include the application of an information and communications technologies security program as well as maintaining an antivirus expertise centre, using Internet filtering devices, monitoring systems, managing identities and access, and managing incidents and vulnerabilities.

Finally, Hydro-Québec has a corporate emergency response plan to ensure service continuity and rapid restoration in case of an exceptional event. This plan includes material, technical and organizational means to quickly mobilize staff and effectively coordinate all internal and external responders, including public authorities.

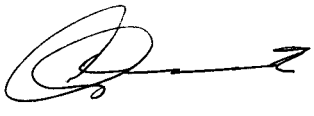
Management Report

Hydro-Québec's consolidated financial statements and all additional information contained in this Annual Report are the responsibility of Management and are approved by the Board of Directors. The consolidated financial statements have been prepared by Management in accordance with Canadian generally accepted accounting principles and take into account the decisions handed down by the Régie de l'énergie with respect to the transmission and distribution of electricity. They include amounts determined based on Management's best estimates and judgment. Financial information presented elsewhere in the Annual Report is consistent with the information provided in the consolidated financial statements.

Management maintains an internal control system which includes communicating Hydro-Québec's code of ethics and a code of conduct to employees, primarily to ensure the proper management of resources and the orderly conduct of business. The objective of this system is to provide reasonable assurance that the financial information is pertinent and reliable and that the assets of Hydro-Québec are adequately recorded and safeguarded. An internal auditing process allows evaluation of the sufficiency and effectiveness 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 is responsible for corporate governance. It assumes its responsibility for the consolidated financial statements principally through its Audit Committee, composed solely of independent directors, who do not hold full-time positions within Hydro-Québec or in one of its subsidiaries. The Audit Committee's mandate is to ensure that the consolidated financial statements present fairly Hydro-Québec's financial position, the results of its operations, its cash flows and its comprehensive income, and to recommend the financial statements to the Board of Directors for approval. The Audit Committee meets regularly with Management, the Internal Auditor and the external auditors to discuss the results of their audits and the resulting findings with respect to the integrity and the quality of Hydro-Québec's financial reporting as well as the effectiveness of its internal control system. The Internal Auditor and the external auditors have full and unrestricted access to the Audit Committee, with or without Management present.

The external auditors are appointed by the Québec government, the sole shareholder of Hydro-Québec. The 2008 and 2007 consolidated financial statements have been audited jointly by the external auditors, KPMG LLP and Ernst & Young LLP.



Michael L. Turcotte
Chairman of the Board

Thierry Vandal
President and Chief Executive Officer

Lise Croteau
Vice President – Accounting and Control

Montréal, Québec
February 6, 2009

Auditors' Report

To the Minister of Finance of Québec:

We have audited the consolidated balance sheets of Hydro-Québec as at December 31, 2008 and 2007, and the consolidated statements of operations, retained earnings, cash flows and comprehensive income for the years 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 audits.

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

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of Hydro-Québec as at December 31, 2008 and 2007, and the results of its operations and its cash flows for the years then ended, in accordance with Canadian generally accepted accounting principles. As required by the *Auditor General Act* (R.S.Q., c. V-5.01), we report that, in our opinion, except for the application of changes in accounting policies described in Note 2 to the consolidated financial statements, these principles have been applied on a basis consistent with that of the preceding year.

KPMG LLP[a]

Ernst & Young LLP[b]

Montréal, Québec
February 6, 2009

a) CA auditor permit No. 6992
b) CA auditor permit No. 13764

Consolidated Financial Statements

Consolidated Statements of Operations

Years ended December 31 In millions of Canadian dollars	Notes	2008	2007
Revenue		**12,717**	12,330
Expenditure			
Operations		**2,497**	2,541
Electricity and fuel purchases		**1,406**	1,555
Depreciation and amortization	4	**2,336**	1,991
Taxes	5	**1,093**	820
Regulatory deferrals	3	**(72)**	29
		7,260	6,936
Operating income		**5,457**	5,394
Financial expenses	6	**2,445**	2,512
Income from continuing operations		**3,012**	2,882
Income from discontinued operations	7	**129**	25
Net income		**3,141**	2,907

Consolidated Statements of Retained Earnings

Years ended December 31 In millions of Canadian dollars	Note	2008	2007
Balance, beginning of year		**15,556**	14,744
Net income		**3,141**	2,907
		18,697	17,651
Dividends declared	18	**2,252**	2,095
Balance, end of year		**16,445**	15,556

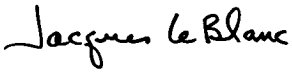
The accompanying notes are an integral part of the consolidated financial statements.

Consolidated Balance Sheets

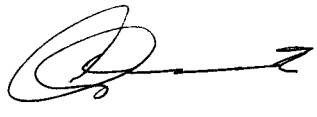
As at December 31 In millions of Canadian dollars	Notes	2008	2007
ASSETS			
Current assets			
Cash and cash equivalents		**370**	54
Short-term investments		**3,545**	3,073
Accounts receivable		**1,961**	1,751
Derivative instruments		**659**	992
Materials, fuel and supplies		**290**	360
		6,825	6,230
Property, plant and equipment	8	**54,987**	53,291
Investments	9	**108**	228
Derivative instruments		**1,428**	1,998
Intangible assets	10	**865**	903
Regulatory assets	3	**1,167**	1,074
Other assets	11	**1,394**	1,142
		66,774	64,866
LIABILITIES			
Current liabilities			
Borrowings		**91**	73
Accounts payable and accrued liabilities		**1,948**	1,877
Dividends payable	18	**2,252**	2,095
Accrued interest		**915**	890
Regulatory liabilities	3	**56**	97
Current portion of long-term debt	12	**770**	1,087
Derivative instruments		**82**	374
		6,114	6,493
Long-term debt	12	**35,290**	33,161
Derivative instruments		**1,887**	2,844
Asset retirement obligations	13	**300**	464
Regulatory liabilities	3	**6**	8
Other long-term liabilities	14	**760**	718
Perpetual debt	15	**355**	286
		44,712	43,974
EQUITY	18		
Share capital		**4,374**	4,374
Retained earnings		**16,445**	15,556
Accumulated other comprehensive income		**1,243**	962
		17,688	16,518
		22,062	20,892
		66,774	64,866
Commitments and contingencies	22		

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

On behalf of the Board of Directors,



Jacques Leblanc
Chair of the Audit Committee



Michael L. Turcotte
Chairman of the Board

Consolidated Statements of Cash Flows

Years ended December 31 In millions of Canadian dollars	Notes	2008	2007
Operating activities			
Net income		**3,141**	2,907
Income from discontinued operations	7	**(129)**	(25)
Income from continuing operations		**3,012**	2,882
Adjustments			
Depreciation and amortization	4	**2,336**	1,991
Amortization of debt premiums, discounts and issue expenses	6	**111**	111
Difference between contributions paid and pension cost		**(305)**	287
Regulatory deferrals	3	**(72)**	29
Other		**82**	50
Change in non-cash working capital items	20	**(149)**	(191)
		5,015	5,159
Investing activities			
Property, plant and equipment and intangible assets		**(3,756)**	(3,464)
Investments		**70**	29
Disposal of investments, net of divested cash and cash equivalents		**154**	51
Costs related to Energy Efficiency Plan		**(236)**	(172)
Net (acquisition) disposal of short-term investments		**(435)**	155
Other		**(7)**	(5)
		(4,210)	(3,406)
Financing activities			
Issuance of long-term debt		**2,027**	2,026
Repayment of long-term debt		**(2,734)**	(993)
Inflows resulting from credit risk management	16	**2,955**	1,374
Outflows resulting from credit risk management	16	**(676)**	(1,855)
Net change in short-term borrowings		**18**	48
Dividends paid		**(2,095)**	(2,342)
Other		**(2)**	(2)
		(507)	(1,744)
Foreign currency effect on cash and cash equivalents		**17**	(14)
Cash flows from continuing operations		**315**	(5)
Cash flows from discontinued operations		**1**	2
Net change in cash and cash equivalents		**316**	(3)
Cash and cash equivalents, beginning of year		**54**	57
Cash and cash equivalents, end of year		**370**	54
Supplementary cash flow information	20		

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

Consolidated Statements of Comprehensive Income

Years ended December 31 In millions of Canadian dollars	**2008**	2007
Net income	**3,141**	2,907
Other comprehensive income		
Change in deferred gains on items designated as cash flow hedges	**389**	693
Reclassification to operations of deferred gains on items designated as cash flow hedges	**(111)**	(207)
	278	486
Other	**3**	5
Comprehensive income	**3,422**	3,398

Notes to Consolidated Financial Statements

Years ended December 31, 2008 and 2007

Amounts in tables are in millions of Canadian dollars, unless otherwise indicated.

Under the provisions of the Hydro-Québec Act, *Hydro-Québec 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. Hydro-Québec is required, in particular, to supply a base volume of up to 165 TWh a year of heritage pool electricity for the Québec market, as set out in the* Act respecting the Régie de l'énergie. *As a government corporation, Hydro-Québec is exempt from paying income taxes.*

Note 1 Significant Accounting Policies

The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles (GAAP) and reflect the decisions of the Régie de l'énergie (the "Régie"). These decisions affect the timing of the recognition of certain transactions in the consolidated operations, resulting in the recognition of regulatory assets and liabilities, which Hydro-Québec considers it is likely to recover or settle subsequently through the rate-setting process.

Regulation

The *Act respecting the Régie de l'énergie* grants the Régie exclusive authority to determine or modify the rates and conditions under which electricity is transmitted and distributed by Hydro-Québec. Hydro-Québec's electricity transmission and distribution activities in Québec are therefore regulated. Under this legislation, rates are set by reasoned decision of three commissioners after public hearings. Moreover, the Act stipulates that rates are determined on a basis that allows for recovery of the cost of service plus a reasonable return on the rate base.

The Régie and Hydro-Québec are both part of the Québec government reporting entity. However, the Régie is an independent, quasi-judicial economic regulatory agency accountable to the National Assembly of Québec through the Minister of Natural Resources and Wildlife.

TRANSMISSION

Hydro-Québec's power transmission rates for 2008 and 2007 were determined in Régie decisions D-2008-027 and D-2007-34, respectively. The authorized return on the rate base was set at 7.84% in 2008 and 7.78% in 2007, assuming a capitalization with 30% equity.

DISTRIBUTION

Hydro-Québec's electricity rates were determined in decisions D-2008-033 and D-2007-22, in which the Régie granted across-the-board rate increases of 2.90% and 1.92%, effective April 1, 2008, and April 1, 2007, respectively. The authorized return on the rate base was set at 7.81% in 2008 and 7.79% in 2007, assuming a capitalization with 35% equity.

Scope of consolidation

The consolidated financial statements include the accounts of Hydro-Québec, its subsidiaries and its joint ventures as well as those of variable interest entities where Hydro-Québec is the primary beneficiary. Interests in joint ventures are accounted for using the proportionate consolidation method.

Use of estimates

The preparation of consolidated financial statements in accordance with GAAP requires that Management make estimates and assumptions that affect the amounts recognized as assets and liabilities, the disclosures regarding contingent assets and liabilities at the date of the consolidated financial statements and the amounts recognized as revenue and expenditure for the years at issue. The estimates relate to revenue, depreciation and amortization expenses, asset retirement obligations and employee future benefits, among other things. Actual results could differ from those estimates.

Revenue

Revenue is recognized when electricity is delivered or services are rendered. Revenue from sales of electricity in Québec is recognized on the basis of cyclical billings and also includes revenue accrued in respect of unbilled electricity deliveries.

Research and development (R&D) costs

R&D costs are charged to operations when incurred, except for capitalizable development costs. Capitalized development costs are amortized on a straight-line basis over a five-year period.

Foreign currency translation

SELF-SUSTAINING FOREIGN OPERATIONS

The financial statements of foreign operations that are self-sustaining in terms of financial and operational management are translated according to the current rate method using the foreign currency as the measuring unit. Under this method, assets and liabilities are translated into Canadian dollars at the exchange rate in effect at the balance sheet date, and revenue and expenditure are translated at the average exchange rates in effect during the period. The exchange gains or losses resulting from the translation of the financial statements of these foreign operations are presented in Accumulated other comprehensive income under Equity on the balance sheet.

INTEGRATED FOREIGN OPERATIONS AND FOREIGN CURRENCY TRANSACTIONS

In the case of foreign operations that are integrated in terms of financial and operational management, as well as foreign currency transactions, accounts stated in foreign currencies are translated according to the temporal method. Under this method, monetary assets and liabilities are translated into Canadian dollars at the exchange rate in effect at the balance sheet date, and non-monetary items are translated at the historical rate. Revenue and expenditure resulting from foreign currency transactions are translated into Canadian dollars at the average exchange rates in effect during the period. The exchange gains or losses resulting from the translation of monetary items are included in the statement of operations, unless they relate to hedging items for future sales in U.S. dollars, in which case they are deferred to other comprehensive income until the year in which such sales are made.

Materials, fuel and supplies

Inventories of materials, fuel and supplies are valued at the lower of cost and net realizable value. Cost is determined by the average cost method.

Property, plant and equipment

Property, plant and equipment are carried at cost, which comprises materials, labor, other costs directly related to construction activities, and financial expenses capitalized during construction. Property, plant and equipment also include draft-design costs for projects whose technical feasibility has been demonstrated, whose profitability has been estimated, and for which Management deems that it will in all likelihood have the necessary resources for completion. The discounted value of retirement obligations related to property, plant and equipment is added to the carrying amount. Moreover, contributions from third parties are applied against the cost of the related property, plant and equipment.

Financial expenses capitalized to property, plant and equipment under construction are determined using the average cost of Hydro-Québec's long-term debt. When the property, plant and equipment under construction relate to regulated transmission and distribution activities, such financial expenses take return on equity into account. The portion that corresponds to return on equity is included in Revenue in the consolidated operations.

Property, plant and equipment are depreciated over their useful life, primarily using the sinking fund method, at a rate of 3%. The depreciation periods for the principal categories of property, plant and equipment are as follows:

Hydraulic generation	40 to 50 years
Thermal generation, including nuclear	15 to 50 years
Transmission substations and lines	30 to 50 years
Distribution substations and lines	25 to 40 years
Corporate and other activities	3 to 50 years

When unregulated property, plant and equipment are retired, the cost of such assets and the cost of their dismantlement, net of accumulated depreciation and salvage value, are charged to operations for the year. When regulated property, plant and equipment are retired, these costs are charged to a separate account and amortized over a maximum period of 10 years, using the sinking fund method, at a rate of 3%.

Maintenance and repair costs are charged to operations when incurred.

Investments

Hydro-Québec is the sole owner of a venture capital company whose mission is to make strategic investments. The investments held by this company are accounted for at fair value in accordance with the rules applicable to investment companies. The fair value is determined according to the quoted market price at the balance sheet date in the case of listed shares, and according to valuation methods recognized by capital markets in the case of unlisted shares.

Investments in companies over which Hydro-Québec can exercise significant influence are accounted for on an equity basis.

Intangible assets

Intangible assets are recorded at cost. This cost includes expenses directly associated with activities to develop or obtain computer software for internal use. Financial expenses are capitalized over the development period.

Intangible assets with an indefinite useful life are not amortized. These assets are tested for impairment annually or more frequently if events indicate a potential impairment loss. The excess of the carrying amount over the fair value is recorded in operations for the period in which the impairment is determined.

Intangible assets with a finite useful life are amortized over their useful life according to the straight-line method over the following periods:

Software and licences	3 to 10 years
Patents	20 years

Impairment of long-lived assets

Hydro-Québec reviews the carrying amount of its property, plant and equipment and its amortizable intangible assets whenever events or changes in circumstances indicate that the expected undiscounted net cash flows could be lower than the carrying amount of the property and assets. An impairment loss corresponding to the amount by which the carrying amount exceeds fair value is recognized, if applicable.

Employee future benefits

Hydro-Québec offers all of its employees a contributory defined-benefit pension plan based on final pay, as well as other post-retirement and post-employment benefits.

The cost of pension benefits and other post-retirement benefits provided in exchange for current service is calculated using the projected benefit method prorated on years of service. It is based on Management's best assumptions of expected return on plan assets, salary escalation, the increase in health care costs, retirement ages of employees and other actuarial factors.

In order to establish its employee future benefit obligations, Hydro-Québec has adopted the following policies:

- Past service costs arising from plan amendments and transitional balances relating to the pension plan and post-retirement benefits as at January 1, 1999, are amortized using the straight-line method over periods not exceeding active employees' average remaining years of service, which totaled 12 years as at January 1, 2008, and January 1, 2007.

- Amortization of actuarial gains or losses is recognized in operations 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 obligations or 10% of the market-related value of the plan assets, whichever is greater. The amortization corresponds to the excess divided by active employees' average remaining years of service.

- 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 and by valuing other asset classes at fair value.

Asset retirement obligations

Hydro-Québec accounts for asset retirement obligations in the period in which these legal obligations are incurred when a reasonable estimate of their fair value can be made. The corresponding costs of asset retirement are added to the carrying amount of the related asset and are amortized over its useful life. In subsequent financial years, any change due to the passage of time is charged to operating expenses for the current year (accretion expense) and the corresponding amount is added to the carrying amount of the liability. Changes resulting from revisions to the timing or the amount of the undiscounted cash flows are recognized as an increase or decrease in the carrying amount of the liability under Asset retirement obligations, and the corresponding offsetting item is accounted for at the carrying amount of the related asset.

The cash flows required to settle asset retirement obligations are estimated on the basis of studies that use various assumptions concerning the methods and timing to be adopted for the retirement. Hydro-Québec periodically reviews the valuation of these cash flows in light of the underlying assumptions and estimates, potential technological advances, and changes in the standards and regulations governing the decommissioning of nuclear generating stations.

Agreements with Aboriginal communities and regional county municipalities

Hydro-Québec has entered into various agreements related to capital projects and intangible assets with Aboriginal communities and regional county municipalities. The commitments under these agreements are recognized in Long-term debt if they fall within the definition of a liability, and the offsetting item is accounted for in Property, plant and equipment or Intangible assets, as the case may be.

Financial instruments

Financial instruments are measured at fair value on initial recognition. Their measurement in subsequent periods and the recognition of any changes in fair value depend on the category in which they are classified.

The following table presents the classification of Hydro-Québec's financial instruments in the various categories:

Category	Financial instruments
Financial assets and liabilities held for trading	Cash and cash equivalents (with initial maturities of three months or less) Derivative instruments
Available-for-sale financial assets	Short-term investments (maturing in more than three months) Investment in bonds (presented in Investments)
Loans and receivables	Accounts receivable Government reimbursement for the 1998 ice storm (presented in Other assets)
Other financial liabilities	Borrowings Accounts payable and accrued liabilities Dividends payable Accrued interest Current portion of long-term debt Long-term debt Perpetual debt

Financial assets and liabilities held for trading are recorded at fair value at the balance sheet date. Gains and losses arising from changes in fair value are recognized in operations for the period during which they occur, except in the case of derivative instruments designated as hedges in a cash flow hedging relationship.

Available-for-sale financial assets are recorded at fair value at the balance sheet date. Changes in fair value are recorded in other comprehensive income until they are realized, at which time they are reclassified to operations. Commodity futures that can be settled net in cash are recorded at the date of settlement if there is a probability of delivery or receipt in accordance with expected needs.

Loans and receivables and other financial liabilities are measured at amortized cost, including debt premiums, discounts and issue expenses.

As part of its integrated enterprise risk management, Hydro-Québec uses various financial instruments to manage its market risk, consisting of currency risk, interest rate risk and risk resulting from fluctuating energy and commodity prices. Hydro-Québec applies cash flow or fair value hedge accounting to the eligible hedging relationships. It formally documents all relationships between hedging instruments and hedged items. This process involves associating all derivative instruments with specific assets and liabilities on the balance sheet, or with probable anticipated transactions. Hydro-Québec also measures the effectiveness of hedging relationships initially and then monthly thereafter.

In the case of a cash flow hedge, the effective portion of changes in the fair value of an instrument designated as a hedge is recognized under other comprehensive income, and the gains and losses related to the ineffective portion are immediately recognized in operations, under the same line item as the hedged item. Amounts included in Accumulated other comprehensive income are reclassified to operations, also under the same component as the hedged item, during the periods in which the change in cash flows attributable to the hedged item affects operations. If a derivative instrument no longer satisfies hedging conditions or is sold or liquidated, or if Hydro-Québec terminates its designation as a hedging item, hedge accounting ceases to be applied on a prospective basis. If the hedged item ceases to exist, the unrealized gains or losses are immediately reclassified to operations.

In the case of a fair value hedge, the derivative instrument is recorded at fair value, and changes in the fair value, including those related to the ineffective portion of the hedge, are recognized in operations in the same line item as the hedged item. Changes in the fair value of the hedged item attributable to the hedged risk are recognized as adjustments to the hedged item's carrying amount and are offset against operations.

In addition, an embedded derivative must be separated from its host contract and recorded at fair value on the balance sheet under certain conditions. Hydro-Québec has opted to apply this accounting treatment to all host contracts issued, acquired or substantially amended on or after January 1, 2003.

Derivative instruments listed on a stock exchange are recognized at closing exchange rates as at the balance sheet date. The fair value of other derivative instruments is based on the spot rates or on the forward rates or prices in effect at market closing at the balance sheet date. In the absence of this information for a given instrument, Management uses the forward rate or price for an equivalent instrument. The valuation techniques used rely on recognized models commonly used by capital market players and make use of market observable data.

Note 2

Changes to Accounting Policies

Recent changes

2008

FINANCIAL INSTRUMENTS

On January 1, 2008, Hydro-Québec adopted two new disclosure and presentation standards of the *Canadian Institute of Chartered Accountants (CICA) Handbook:* Section 3862, "Financial Instruments – Disclosures," and Section 3863, "Financial Instruments – Presentation," which superseded Section 3861, "Financial Instruments – Disclosure and Presentation." These new standards modify disclosure requirements regarding the nature and extent of risks arising from financial instruments as well as how Hydro-Québec manages these risks. The presentation rules remain unchanged. The adoption of these new standards has had no impact on the recognition or measurement of financial instruments. The required information is provided in Note 16, Financial Instruments.

CAPITAL DISCLOSURES

On January 1, 2008, Hydro-Québec adopted the recommendations of *CICA Handbook* Section 1535, "Capital Disclosures," requiring disclosure of how capital is managed by Management. The required information is provided in Note 19, Capital Management.

INVENTORIES

On January 1, 2008, Hydro-Québec adopted the recommendations of *CICA Handbook* Section 3031, "Inventories," which establishes standards for the measurement of inventories, including determination of their cost. The adoption of these recommendations has not affected net income but required the reclassification of $65 million as Property, plant and equipment on the balance sheet as at December 31, 2008.

2007

FINANCIAL INSTRUMENTS

On January 1, 2007, Hydro-Québec adopted the recommendations of *CICA Handbook* Section 3855, "Financial Instruments – Recognition and Measurement," which states the requirements for the recognition and measurement of financial instruments, and Section 3865, "Hedges," which specifies how hedge accounting is applied and the required disclosures to be made in this context. It also adopted the recommendations of Section 3861 and Section 1530, "Comprehensive Income." This last section establishes standards for the reporting and presentation of comprehensive income, which includes net income and other comprehensive income.

The main impacts of adopting the new accounting policies were as follows as at January 1, 2007: Retained earnings increased by $270 million, Accumulated other comprehensive income increased by $479 million, Long-term debt increased by $551 million, Other long-term liabilities decreased by $2,051 million and the net value of derivative instruments decreased by $701 million.

EQUITY

On January 1, 2007, Hydro-Québec prospectively adopted the recommendations of *CICA Handbook* Section 3251, "Equity," which superseded Section 3250, "Surplus." Section 3251 establishes standards for the presentation of equity and changes in equity as a result of the new requirements in Section 1530. With the adoption of these standards, translation adjustments, which were previously presented separately in Equity, were reclassified to Accumulated other comprehensive income.

ACCOUNTING CHANGES

Hydro-Québec also adopted the recommendations of *CICA Handbook* Section 1506, "Accounting Changes," which prescribes the accounting treatment and disclosure of changes in accounting policies, changes in accounting estimates and corrections of errors. The adoption of these recommendations had no impact on the consolidated financial statements.

Future changes

GOODWILL AND INTANGIBLE ASSETS

In 2008, the CICA issued Section 3064 of the *CICA Handbook*, "Goodwill and Intangible Assets," which superseded Section 3062, "Goodwill and Other Intangible Assets," and Section 3450, "Research and Development Costs." Section 3064 establishes standards for the recognition, measurement, presentation and disclosure of goodwill and intangible assets. It will apply to Hydro-Québec's interim and annual financial statements for periods beginning on or after January 1, 2009. The adoption of these new standards is not expected to have any significant impact on the consolidated financial statements.

REGULATED ACTIVITIES

On January 1, 2009, the temporary exemption provided for in *CICA Handbook* Section 1100, "Generally Accepted Accounting Principles," which allows the recognition and measurement of regulatory assets and liabilities, was withdrawn. Pursuant to a practice allowed by Canadian GAAP, Hydro-Québec will, however, rely on *Statement of Financial Accounting Standard (SFAS)* No. 71, "Accounting for the Effects of Certain Types of Regulation," issued by the U.S. Financial Accounting Standards Board (FASB), to maintain the current accounting treatment for regulatory assets and liabilities. Consequently, the withdrawal of the exemption should not have any impact on the consolidated financial statements.

CREDIT RISK AND FAIR VALUE OF FINANCIAL ASSETS AND FINANCIAL LIABILITIES

On January 20, 2009, the Emerging Issues Committee (EIC) of the CICA released *Abstract of Issue Discussed EIC-173,* "Credit Risk and the Fair Value of Financial Assets and Financial Liabilities." EIC-173 clarifies that an entity's own credit risk and the credit risk of the counterparty should be taken into account in determining the fair value of financial assets and financial liabilities, including derivative instruments. Hydro-Québec is currently assessing the impact of adopting the recommendations in this abstract on the consolidated financial statements.

INTERNATIONAL FINANCIAL REPORTING STANDARDS

On February 13, 2008, the Canadian Accounting Standards Board (AcSB) confirmed that the complete changeover to International Financial Reporting Standards (IFRS) would take effect for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011.

Hydro-Québec is currently examining the issues involved in the changeover from Canadian GAAP to IFRS.

Note 3 — Effects of Rate Regulation on the Consolidated Financial Statements

The following information describes the impact on the consolidated financial statements of accounting methods and practices adopted by Hydro-Québec in accordance with the Régie's decisions with respect to regulated activities.

Regulatory assets and liabilities

COSTS RELATED TO THE ENERGY EFFICIENCY PLAN (EEP)

The costs related to implementation of the EEP, such as specific energy conservation programs, are charged to a separate account and amortized over 10 years on a straight-line basis, except for the costs incurred prior to January 1, 2006, which are amortized over five years. This period begins in the year after the costs were recorded. Financial expenses arising from these costs are capitalized at the rate of return authorized by the Régie on the rate base until such time as they are included in the rate base and amortization begins. This accounting practice relates to Hydro-Québec's power distribution activities and was authorized by the Régie in decisions D-2002-25, D-2002-288, D-2003-93 and D-2006-56. Were these activities not regulated, certain costs not associated with intangible assets as defined in the accounting standards would be recognized in operations for the year in which they were incurred. If none of the costs incurred were related to an intangible asset, net income for 2008 would have been $178 million lower ($129 million in 2007).

NET COSTS RELATED TO RETIREMENT OF PROPERTY, PLANT AND EQUIPMENT AND INTANGIBLE ASSETS

When property, plant and equipment or intangible assets are retired, the cost of such assets and of their dismantlement, net of accumulated amortization and salvage value, are charged to a separate account and amortized over a maximum period of 10 years, using the sinking fund method at a rate of 3%. The Régie authorized this accounting practice in decisions D-2002-95 and D-2003-93, which relate to Hydro-Québec's power transmission and distribution activities, respectively. Were these activities not regulated, the related costs would be recognized in operations for the year, and net income for 2008 would have been $48 million lower ($22 million higher in 2007).

VARIANCES IN REVENUE RELATED TO WEATHER CONDITIONS

Variances between actual transmission and distribution revenue and the revenue forecasts established on the basis of weather normals for purposes of rate cases are recorded in a separate account. Financial expenses arising from the variances charged to this account are capitalized at the rate of return authorized by the Régie on the rate base until such time as they are included in the rate base. This accounting practice was authorized by the Régie in decision D-2006-34, which relates to Hydro-Québec's power distribution activities, and led to a request for an amortization mechanism in the 2009 rate application. Were these activities not regulated, Hydro-Québec's expenditure would have been higher and net income would have been lower by $141 million for 2008 (nil in 2007).

VARIANCES IN ANNUAL COST OF TRANSMISSION SERVICE FOR NATIVE LOAD

Variances resulting from any modification of the annual cost of native load transmission service that has not been taken into account in the setting of electricity rates are recorded in a separate account and amortized according to conditions set by the Régie. Financial expenses arising from these variances are capitalized at the rate of return authorized by the Régie on the rate base until such time as they are included in the rate base and amortization begins. This accounting practice relates to Hydro-Québec's power distribution activities and was authorized by the Régie in decisions D-2003-93, D-2006-34, D-2007-12 and D-2008-024. Were these activities not regulated, Hydro-Québec's expenditure would have been lower and net income would have been higher by $240 million for 2008 ($11 million in 2007).

COSTS INCURRED UNTIL THE RESCISSION OF DUAL-ENERGY RATE BT

The costs incurred until the rescission of dual-energy Rate BT were charged to a separate account and have been amortized on a straight-line basis over five years since the rescission date of April 1, 2006. These costs mainly include the deficit resulting from the variance between the supply cost recognized by the Régie and energy prices in effect, multiplied by the quantity of electricity delivered to customers at Rate BT between January 1, 2004, and March 31, 2006. Financial expenses arising from these costs were capitalized at the rate of return authorized by the Régie on the rate base until March 31, 2006. This accounting practice was authorized by the Régie in decisions D-2004-47, D-2004-170 and D-2006-34, which relate to Hydro-Québec's power distribution activities. Were these activities not regulated, the costs would have been recognized in operations for the year in which they were incurred, and net income for 2008 would have been $29 million higher ($30 million in 2007).

COSTS RELATED TO THE DE-ICING SYSTEM AT LÉVIS SUBSTATION

Certain costs related to the Lévis substation de-icing system, a project designed in the wake of the 1998 ice storm to secure the transmission lines supplying the greater Québec area, were charged to a separate account. These costs have been depreciated using the sinking fund method at a rate of 3%, starting from the date of commissioning of the de-icing system, over a period corresponding to the average remaining useful life of the assets enhanced by the project. Financial expenses arising from these costs were capitalized at the rate of return authorized by the Régie on the rate base until such time as they were included in the rate base and amortization began. The Régie authorized this accounting practice in decision D-2004-175, which relates to Hydro-Québec's power transmission activities. Were these activities not regulated, the costs would have been recognized in operations for the year in which they were incurred, and net income for 2008 would have been $5 million higher ($6 million lower in 2007).

COST VARIANCES RELATED TO ELECTRICITY PURCHASES IN EXCESS OF THE HERITAGE POOL

Volume and price variances recognized for a given year between the actual costs of electricity purchases in excess of the heritage pool and the costs forecasted in the rate cases and accepted by the Régie for rate-setting purposes are recorded in a separate account and amortized according to conditions set by the Régie. Financial expenses arising from these variances are capitalized at the rate of return authorized by the Régie on the rate base until such time as amortization begins. This accounting practice was authorized by the Régie in decisions D-2005-34, D-2005-132, D-2006-34, D-2007-12 and D-2008-024, which relate to Hydro-Québec's power distribution activities. Were these activities not regulated, the actual costs would be recognized in operations for the year in which they are incurred, and net income for 2008 would have been $2 million lower ($177 million in 2007).

VARIANCES IN REVENUE FROM POINT-TO-POINT TRANSMISSION SERVICES

Variances recognized for a given year between actual revenue from point-to-point transmission services and revenue forecasted in the rate cases and accepted by the Régie for rate-setting purposes are recorded in a separate account and amortized according to conditions set by the Régie. Financial expenses arising from these variances are capitalized at the rate of return authorized by the Régie on the rate base until such time as amortization begins. This accounting practice was authorized by the Régie in decisions D-2007-08 and D-2008-019, which relate to Hydro-Québec's power transmission activities. Were these activities not regulated, Hydro-Québec's expenditure would have been higher and net income would have been lower by $41 million for 2008 ($50 million higher in 2007).

REGULATORY ASSETS

	Expected years of amortization	2008	2007
Costs related to EEP	2009–2018	**559**	381
Net costs related to retirement of property, plant and equipment and intangible assets	2009[a]	**267**	219
Variances in revenue related to weather conditions[b]	2009–2014	**141**	–
Variances in annual cost of transmission service for native load[b]	2009	**104**	344
Costs incurred until rescission of dual-energy Rate BT	2009–2011	**66**	95
Costs related to de-icing system at Lévis substation	2009–2047	**13**	18
Other	2009–2028	**17**	17
		1,167	1,074

REGULATORY LIABILITIES

	Expected years of amortization	2008	2007
Cost variances related to electricity purchases in excess of heritage pool[b]	2009–2010	**(53)**	(55)
Variances in revenue from point-to-point transmission services[b]	2009	**(9)**	(50)
		(62)	(105)
Current portion		**(56)**	(97)
		(6)	(8)

a) Except certain asset retirements.

b) The change in the variance accounts, net of an amortization expense of $141 million (amortization credit of $145 million in 2007) and capitalized financial expenses of $13 million ($1 million in 2007), corresponds to the Regulatory deferrals presented in the Consolidated Statements of Operations, namely, a decrease in expenditure of $72 million (increase of $29 million in 2007).

RISKS AND UNCERTAINTIES

The risks and uncertainties related to the above regulatory assets and liabilities are subject to periodic monitoring and assessment. Once Hydro-Québec considers that it is no longer likely that the net carrying amount of a regulatory asset or liability will be taken into account in setting future rates, this amount is recognized in operations for the year in which the conclusion is reached.

Other regulatory practices

Under Régie decisions D-2002-95 and D-2003-93, the compensation granted by the Québec government for the 1998 ice storm was applied against the cost of newly constructed property, plant and equipment; it is amortized over the remaining life of the retired assets, with the exception of the portion equivalent to the unamortized cost of these assets, which is amortized over 10 years. The sinking fund method, at a rate of 3%, is used in both cases. Were these activities not regulated, the compensation would be amortized over the useful life of the newly constructed property, plant and equipment.

In decisions D-2002-95 and D-2004-47, the Régie prescribed capitalizing financial expenses to property, plant and equipment under construction and intangible assets under development according to the authorized rates of return on the rate bases. These rates, which are set using methods approved by the Régie, take into account a component associated with the cost of the debt and a component associated with the return on equity. Were these activities not regulated, financial expenses would be capitalized using the average cost of Hydro-Québec's long-term debt.

Under Régie decisions D-2002-95 and D-2003-93, the cost of dismantling assets that were retired and replaced, net of the salvage value, is added to the cost of the newly constructed assets. Were these activities not regulated, these costs would be charged to operations.

Under Régie decisions D-2006-76 and D-2006-76R, contributions received for relocation or modification projects relating to certain transmission grid assets are charged to a separate account and applied against property, plant and equipment. These contributions are amortized over the average useful life of assets for each project, using the sinking fund method, at a rate of 3%. Were these activities not regulated, the contributions would be amortized over the useful life of each fixed asset concerned.

In decision D-2007-134 issued in December 2007, the Régie approved an agreement whereby energy deliveries provided for in a power purchase contract with an independent power producer were suspended for 2008. In decision D-2008-114 issued on September 10, 2008, the Régie authorized the renewal of the agreement until the end of 2009. As at December 31, 2008, a $57-million commitment ($52 million as at December 31, 2007) was recorded on the balance sheet but had no impact on operating results.

Note 4 Depreciation and Amortization

	2008	2007
Property, plant and equipment[a]	**1,819**	1,857
Intangible assets	**122**	104
Regulatory assets and liabilities	**286**	(7)
Deferred charges	**10**	11
Write-offs	**99**	26
	2,336	1,991

a) Revision of the useful life of property, plant and equipment resulted in a $71-million decrease in the depreciation and amortization expense for 2008 ($13-million increase in 2007). In fiscal 2009, Hydro-Québec will revise the useful life of some property, plant, and equipment used for hydraulic generation, which could have a major impact on the depreciation and amortization expense.

Note 5 Taxes

	2008	2007
Water-power royalties	**552**	267[a]
Public utilities tax	**302**	240
Capital tax	**202**	278
Municipal, school and other taxes	**37**	35
	1,093	820

a) The payment of water-power royalties results from the fact that Hydro-Québec is subject to the *Watercourses Act*. For this transition year, the half-rate rule applied.

Note 6 Financial Expenses

	2008	2007
Interest		
Interest on debt securities	**2,585**	2,584
Amortization of debt premiums, discounts and issue expenses	**111**	111
	2,696	2,695
Net exchange (gain) loss	**(25)**	18
Loan guarantee fees	**167**	169
	142	187
Less		
Capitalized financial expenses	**306**	283
Net investment income[a]	**87**	87
	393	370
	2,445	2,512

a) As at December 31, 2008, the weighted average interest rate on short-term investments was 2.33% (4.20% as at December 31, 2007).

Note 7 Discontinued Operations

In 2008, Hydro-Québec recognized a gain of $121 million, net of $26 million in related income taxes, for the price adjustment provided for in the contract for the sale of its interest in HQI Transelec Chile S.A. (Transelec). This adjustment was made following the ministerial order issued on January 15, 2008, establishing the value of the regulated trunk transmission asset base of Transelec. The retrospective effect of this revised valuation on Transelec's revenue for the period from March 13, 2004, to June 30, 2006, resulted in an additional $5-million adjustment of the selling price, net of $1 million in related income taxes.

On February 28, 2007, Hydro-Québec completed the sale of its interest in HQI Australia Pty Ltd (DirectLink), through its wholly owned subsidiary Hydro-Québec International, for a cash consideration of $52 million, which gave rise to a gain of $18 million.

For purposes of segmented information, the results of foreign holdings are classified under Corporate and Other Activities.

Note 8 Property, Plant and Equipment

	In service	Accumulated depreciation	Under construction	2008 Total
Generation				
Hydraulic	33,829	8,832	3,458	**28,455**
Thermal, including nuclear	2,573	1,999	248	**822**
Other	750	332	25	**443**
	37,152	11,163	3,731	**29,720**
Transmission				
Substations and lines	21,393	6,932	931	**15,392**
Other	1,980	1,150	108	**938**
	23,373	8,082	1,039	**16,330**
Distribution				
Substations and lines	11,850	4,550	234	**7,534**
Other	1,863	1,019	101	**945**
	13,713	5,569	335	**8,479**
Construction	28	14	1	**15**
Corporate and Other Activities	1,023	642	62	**443**
	75,289	25,470	5,168	**54,987**

	In service	Accumulated depreciation	Under construction	2007 Total
Generation				
Hydraulic	32,235	8,256	3,344	27,323
Thermal, including nuclear	2,715	1,933	158	940
Other	725	314	23	434
	35,675	10,503	3,525	28,697
Transmission				
Substations and lines	20,842	6,532	669	14,979
Other	1,916	1,085	87	918
	22,758	7,617	756	15,897
Distribution				
Substations and lines	11,434	4,270	191	7,355
Other	1,801	1,016	123	908
	13,235	5,286	314	8,263
Construction	31	14	2	19
Corporate and Other Activities	992	638	61	415
	72,691	24,058	4,658	53,291

Note 9 Investments

	2008	2007
At equity		
Churchill Falls (Labrador) Corporation Limited	**87**	77
CITEQ inc.	**(5)**	(5)
	82	72
At fair value		
Churchill Falls (Labrador) Corporation Limited		
Bonds	**–**	55
Venture capital[a]	**19**	40
	19	95
Other	**7**	61
	108	228

a) The gross unrealized gains and losses on investments held by the venture capital company amounted to $6 million and $13 million, respectively, as at December 31, 2008 ($12 million and $13 million as at December 31, 2007). Net realized and unrealized losses in 2008 totaled $1 million and $6 million, respectively (realized and unrealized gains of $12 million and $2 million in 2007).

Note 10 Intangible Assets

	2008			2007		
	Cost[a]	Accumulated amortization	Net carrying amount	Cost[a]	Accumulated amortization	Net carrying amount
Subject to amortization						
Software and licences	1,260	744	**516**	1,322	763	559
Patents	10	4	**6**	9	4	5
	1,270	748	**522**	1,331	767	564
Not subject to amortization						
Servitudes			**343**			339
			865			903

a) The intangible assets commissioned during the year totaled $481 million as at December 31, 2008 ($87 million as at December 31, 2007).

Note 11 Other Assets

	Note	2008	2007
Accrued benefit asset	21	**1,133**	828
Deferred charges		**111**	153
Government reimbursement for the 1998 ice storm[a]		**90**	107
Nuclear fuel waste management trust fund[b]		**50**	44
Goodwill[c]		**10**	10
		1,394	1,142

a) Payable in quarterly installments of $6 million until January 15, 2014, and a final installment of $1 million on April 15, 2014. These installments include interest at the annual rate of 7.2%. The fair value of this financial asset was $97 million as at December 31, 2008 ($110 million as at December 31, 2007).

b) On November 15, 2002, the *Nuclear Fuel Waste Act* came into force. Under this Act, nuclear energy corporations in Canada were required to set up a waste management organization whose role would be to propose a long-term approach for managing spent nuclear fuel to the Government of Canada. Nuclear energy corporations were also required to set up a trust fund to finance the costs of long-term nuclear fuel waste management. In November 2005, the Nuclear Waste Management Organization (NWMO) filed its report with the Government of Canada and recommended an approach which was adopted in June 2007.

In October 2007, the members of the NWMO ratified an agreement that sets forth a formula for financing the costs of long-term nuclear fuel waste management. This formula will be used to determine each member's share for the next five years and will become effective only after approval by the Government of Canada. Each member's share will be determined according to the number of spent nuclear fuel bundles it had generated as at June 30, 2006. It will also take into account the date on which each member plans to send the spent nuclear fuel bundles to the future national repository.

c) For purposes of segmented information, goodwill is classified under Generation.

Note 12 Long-Term Debt

The following table presents the debt, at amortized cost, including the current portion of long-term debt, broken down by currency at the time of issue. Swaps related to the debt were taken into account in determining the percentages of debt by currency at the time of repayment.

	2008				2007			
			At time of issue	At time of repayment			At time of issue	At time of repayment
	In Canadian dollars and other currencies	At closing exchange rates as at the balance sheet date	%	%	In Canadian dollars and other currencies	At closing exchange rates as at the balance sheet date	%	%
Hydro-Québec's debt								
Canadian dollars	25,482	**25,482**	**71**	**95**	24,829	24,829	72	96
U.S. dollars	8,076	**9,888**	**28**	**5**[a]	8,135	8,012	24	4[a]
Other currencies								
Euros	59	**101**	**–**		671	968	3	
Yen	2,506	**34**	**–**		2,508	22	–	
Pounds sterling	238	**425**	**1**		237	465	1	
Swiss francs	–	**–**	**–**		100	87	–	
		35,930				34,383		
Plus								
Adjustment for fair-value hedged risk		**98**				(163)		
Subsidiaries' debt								
U.S. dollars	26	**32**	**–**	**–**	29	28	–	–
		36,060	**100**	**100**		34,248	100	100
Less								
Current portion		**770**				1,087		
		35,290				33,161		

a) Of this amount, 99.4% was used to hedge sales in U.S. dollars as at December 31, 2008 (99.3% as at December 31, 2007).

Interest rates

The following table shows Hydro-Québec's interest rates, which take into account stated interest rates on borrowings, debt premiums, discounts and issue expenses, and the effect of debt-related swaps:

%				2008	2007
Maturity	Canadian dollars	U.S. dollars	Other currencies	Weighted average	Weighted average
1 to 5 years	7.93	7.51	8.55	**7.71**	8.14
6 to 10 years	3.31	7.07	9.90	**7.58**	9.58
11 to 15 years	10.45	8.97	–	**9.96**	9.99
16 to 20 years	7.30	8.28	–	**8.27**	8.50
21 to 25 years	5.70	9.35	–	**8.10**	8.40
26 to 30 years	5.99	–	–	**5.99**	5.99
31 to 35 years	5.17	–	–	**5.17**	5.17
36 to 40 years	4.93	–	–	**4.93**	4.88
41 to 45 years	6.44	–	–	**6.44**	6.44
46 to 50 years	–	–	–	**–**	–
51 to 55 years	6.62	–	–	**6.62**	6.62
Weighted average	6.31	8.65	9.79	**6.93**	7.32

The variable-rate portion of Hydro-Québec's debt amounted to 10.1%, or 11.0% including perpetual debt, as at December 31, 2008 (6.8%, or 7.8% including perpetual debt, as at December 31, 2007).

Note 12 Long-Term Debt (continued)

Fair value

As at December 31, 2008, the fair value of Hydro-Québec's long-term debt, including the current portion, amounted to $47,072 million ($44,753 million as at December 31, 2007). Including debt-related swaps, total indebtedness stood at $47,856 million ($46,044 million as at December 31, 2007).

Fair value is obtained by discounting future cash flows, based on forward interest rates derived from interest rates at close of business on the balance sheet date for similar instruments available on capital markets. Changes in fair value reflect sensitivity to capital market interest rates. However, Management's primary intention is to hold these debt securities until maturity.

Standby credit

Hydro-Québec has undrawn standby credit facilities of US$2,000 million, composed of two tranches, one of US$360 million and the other of US$1,640 million, which will expire in 2012 and 2013, respectively. Any borrowings will bear interest at a rate based on the London Interbank Offered Rate (LIBOR). A US$750-million swing loan at the U.S. base rate is included in the US$2,000-million credit facility.

Note 13 Asset Retirement Obligations

Liabilities arising from asset retirement obligations relate to the cost of dismantling Gentilly-2 nuclear generating station at the end of its useful life, the removal of spent nuclear fuel resulting from its operation, and the dismantling of fuel tanks and of certain thermal generating stations.

In 2008, the Board of Directors approved the project to refurbish Gentilly-2 nuclear generating station, which will extend its useful life by 28 years. Therefore, the main assumptions for calculating the obligation related to the dismantling of Gentilly-2 generating station at the end of its useful life had to be revised, resulting primarily in a 28-year deferral of the expected timing for the settlement of the obligation.

Hydro-Québec has also identified asset retirement obligations relating to thermal generating stations and power transmission substations and lines for which no liability has been recognized since it expects to use these assets for an undetermined period. These relate to property, plant and equipment for which Hydro-Québec does not have sufficient information to accurately establish a schedule for the obligations. A liability resulting from these asset retirement obligations will be recognized in the period in which there is sufficient information to establish such a schedule.

The aggregate carrying amount of the asset retirement obligations is as follows:

	Dismantling of nuclear generating station	Removal of spent nuclear fuel	Dismantling of other assets	**2008** Total
Balance, beginning of year	306	141	17	**464**
Liabilities incurred	–	2	–	**2**
Accretion expense	15	13	1	**29**
Liabilities settled	–	(1)	(2)	**(3)**
Revision of estimated cash flows and expected timing of payments	(192)[a]	–	–	**(192)**
Balance, end of year	129	155	16	**300**

	Dismantling of nuclear generating station	Removal of spent nuclear fuel	Dismantling of other assets	2007 Total
Balance, beginning of year	288	127	16	431
Liabilities incurred	–	3	–	3
Accretion expense	18	12	1	31
Liabilities settled	–	(1)	(2)	(3)
Revision of estimated cash flows and expected timing of payments	–	–	2	2
Balance, end of year	306	141	17	464

a) The decrease in the obligation is mainly due to the deferral of the dismantling of Gentilly-2 generating station, since Hydro-Québec now has an additional 28 years to provide for its obligation.

The carrying amount of the asset retirement obligations is based on the following key assumptions:

	Dismantling of nuclear generating station	Removal of spent nuclear fuel	Dismantling of other assets
Estimated cash flows (in constant dollars) required to settle the obligations[a]			
As at December 31, 2008	761	598	17
As at December 31, 2007	795	598	18
Expected timing of payment of the cash flows required to settle the obligations			
As at December 31, 2008	Between 2040 and 2071	Between 2009 and 2159	Between 2009 and 2031
As at December 31, 2007	Between 2011 and 2057	Between 2008 and 2159	Between 2008 and 2031
Credit quality–adjusted, risk-free rate at which the estimated cash flows have been discounted (%)			
Initial recognition of obligations	6.4	6.4	6.4
Subsequent recognition of obligations	5.5 and 5.2	5.5	5.7

a) Inflation rates varying between 1.8% and 3.6% were used to determine the asset retirement obligations.

Note 14 Other Long-Term Liabilities

	Note	2008	2007
Accrued benefit liability	21	**663**	601
Accounts payable		**97**	117
		760	718

Note 15 Perpetual Debt

Perpetual notes in the amount of $355 million (US$289 million) as at December 31, 2008, and $286 million (US$289 million) as at December 31, 2007, bear interest at a rate determined semiannually based on LIBOR, plus 0.0625%. They are redeemable at Hydro-Québec's option. No portion was redeemed in 2008 and 2007. Various derivative instruments recorded at fair value are used to mitigate currency risk associated with this debt.

As at December 31, 2008 and 2007, the rates applicable to the perpetual notes were 3.6% and 5.2%, respectively. As at December 31, 2008, the fair value of the perpetual notes was $246 million ($290 million as at December 31, 2007). Fair value is obtained by discounting future cash flows, based on forward interest rates derived from interest rates at close of business on the balance sheet date for similar instruments available on capital markets.

Note 16 Financial Instruments

As part of its operations, Hydro-Québec carries out transactions that expose it to financial risks such as market, liquidity and credit risks. Exposure to such risks and the impact on operating results are significantly reduced through careful monitoring and implementing strategies that include the use of derivative instruments.

Market risk

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate as a result of changes in market prices. Hydro-Québec is exposed to three main types of market risk: currency risk, interest rate risk and risk associated with the price of aluminum. Active integrated management of these three factors aims to limit their impact on operating results so that the mitigated risk is at an acceptable level.

Management of long-term risk

MANAGEMENT OF RISK ASSOCIATED WITH SALES IN U.S. DOLLARS

Currency risk – Hydro-Québec uses currency swaps and a portion of U.S. dollar–denominated debt to manage currency risk associated with probable U.S.-dollar sales, designating them as cash flow hedges. The impact of these hedging transactions on operating results is recorded in Revenue. Hydro-Québec regularly assesses the probability of realizing future sales denominated in U.S. dollars.

MANAGEMENT OF RISK ASSOCIATED WITH LONG-TERM DEBT

Currency risk and interest rate risk – Hydro-Québec uses currency swaps to manage the currency risk associated with long-term debt and interest rate swaps to modify long-term exposure to interest rate risk. When designated as hedging items, these derivative instruments are recognized as cash flow hedges or fair value hedges, depending on the risk hedged. The impact on operating results of foreign currency hedging transactions and those associated with long-term debt interest rates is recorded in Financial expenses.

The following table shows the notional amounts of swaps used to manage risk associated with U.S.-dollar sales and long-term debt, expressed in Canadian dollars and other currencies:

Maturity	1 to 5 years	6 to 10 years	11 to 15 years	16 to 20 years	More than 20 years	**2008**[a] Total	2007[a] Total
Swaps							
Canadian dollars	(384)	(194)	(2,465)	(2,337)	(2,637)	**(8,017)**	(6,413)
U.S. dollars	(347)	(12)	2,030	1,950	2,039	**5,660**	5,418
Other currencies							
Yen	1,500	1,000	–	–	–	**2,500**	2,500
Euros	–	61	–	–	–	**61**	673
Pounds sterling	40	200	–	–	–	**240**	240
Swiss francs	–	–	–	–	–	**–**	97

a) Figures in parentheses represent amounts to be paid.

The following table shows the fair value of swaps used to manage risk associated with U.S.-dollar sales and long-term debt, expressed in Canadian dollars:

	2008	2007
Instruments designated as cash flow hedges for U.S.-dollar sales[a]	**452**	894
Instruments designated as cash flow hedges for debt	**(36)**	(2,451)
Instruments designated as fair value hedges for debt	**104**	(274)
	520	(1,831)
Instruments not designated as hedges[b]	**(695)**	1,548
	(175)	(283)

a) A portion of the long-term debt, with a nominal amount of US$1,437 million as at December 31, 2008 (US$1,504 million as at December 31, 2007), was also designated as a cash flow hedge for U.S.-dollar sales.

b) Transactions carried out as part of Hydro-Québec's risk management, including ($852 million) in 2008 in consideration of amounts received or disbursed with respect to credit risk mitigation agreements ($1,435 million in 2007).

Management of short-term risk

Currency risk – Hydro-Québec uses options and forward contracts to manage its foreign currency risk exposure over the short term. When designated as hedging items, these derivative instruments are recognized as cash flow hedges. The impact of currency risk hedging transactions on operating results is recorded in the line item corresponding to the hedged item, namely Revenue or Electricity and fuel purchases. The nominal amount of the open positions as at December 31, 2008, was US$258 million, with US$52 million in purchase contracts and US$310 million in sales contracts (US$563 million as at December 31, 2007, that is, US$107 million in purchase contracts and US$670 million in sales contracts).

Interest rate risk – Hydro-Québec uses options, interest rate swaps and forward rate agreements to manage short-term interest rate risk. When designated as hedging items, these derivative instruments are recognized as cash flow hedges. The impact on operating results of transactions to hedge short-term interest rate risk is recorded in Financial expenses.

Market risk – Hydro-Québec uses mainly options, swaps and commodity futures to manage risk resulting from fluctuations in energy and aluminum prices. When these derivative instruments are designated as hedging items, they are recognized as cash flow hedges. The impact on operating results of transactions to hedge the risk of variability in energy and aluminum prices is recorded in the line item corresponding to the hedged item, namely Revenue. Hydro-Québec regularly assesses the probability of realizing these transactions. To hedge exposure to variability in energy and aluminum prices, Hydro-Québec has traded derivative instruments for which open positions as at December 31, 2008, totaled 152,625 tonnes of aluminum (227,525 tonnes as at December 31, 2007) and in electricity swaps for which open positions as at December 31, 2008, were 3.5 TWh (8.0 TWh as at December 31, 2007).

The fair value of derivative instruments used to manage short-term financial risk, depending on whether or not they are designated as hedges, is presented in the following table:

	2008	2007
Instruments designated as cash flow hedges	**285**	66
Instruments not designated as hedges	**8**	(11)
	293	55

Effect of hedges

EFFECT OF HEDGES ON OPERATING RESULTS

EFFECT OF CASH FLOW HEDGES

As at December 31, 2008, the net loss related to the ineffectiveness of cash flow hedges recognized in operations totaled $15 million (net gain of $9 million as at December 31, 2007).

As at December 31, 2008, Hydro-Québec estimated at $401 million the amount of net gains presented in Accumulated other comprehensive income that would be reclassified to operations in the next 12 months ($222 million as at December 31, 2007).

In 2008, Hydro-Québec did not reclassify any amount from Accumulated other comprehensive income to operations (net gain of $10 million reclassified in 2007) as a result of the discontinuance of cash flow hedges.

As at December 31, 2008, the maximum period over which Hydro-Québec hedged its exposure to the variability of future cash flows for anticipated transactions was 22 years (23 years as at December 31, 2007).

EFFECT OF FAIR VALUE HEDGES

As at December 31, 2008, the net loss related to the ineffectiveness of fair value hedges recognized in operations totaled $25 million (net gain of $3 million as at December 31, 2007).

EFFECT OF REVALUATION OF DERIVATIVE INSTRUMENTS NOT DESIGNATED AS HEDGES

As at December 31, 2008, the net gain recognized in operations as a result of the revaluation, at fair value, of derivative instruments not subject to hedge accounting totaled $143 million ($32 million as at December 31, 2007). These instruments are essentially related to risk management transactions.

SENSITIVITY ANALYSES

Integrated management of risk associated with variability in foreign exchange rates, interest rates and aluminum prices aims to limit the impact of such risk on operating results. Most of the derivative instruments traded are designated as cash flow hedges or fair value hedges and therefore reduce the volatility in operating results, except for the ineffective portion of the hedges, which is insignificant.

Derivative instruments which are not designated as hedges, but which nonetheless serve to hedge at-risk opposite positions, also reduce the volatility in operating results. The sensitivity of operating results is thus limited to net exposure to unhedged risks.

As at December 31, 2008, had the exchange rate (C$/US$) been 5% higher or lower, net income would have been $17 million higher or $7 million lower, respectively, taking into account the impact of hedged sales, while other comprehensive income would have been $100 million higher or $104 million lower, respectively.

For the year ended December 31, 2008, had interest rates been 50 basis points higher or lower, net income would have been $2 million lower or higher, respectively, while other comprehensive income would have been $3 million higher or $4 million lower, respectively.

For the year ended December 31, 2008, had the price of aluminum been 5% higher or lower, net income would have been $3 million higher or lower, respectively, taking into account the impact of hedged sales, and other comprehensive income would have been $15 million lower or higher, respectively.

Liquidity risk

Liquidity risk is the risk that Hydro-Québec will have difficulty meeting commitments related to its financial liabilities.

Hydro-Québec's exposure is reduced by a large volume of cash from operations, a diversified portfolio of highly liquid or readily convertible instruments traded with high-quality counterparties, preauthorized capital resources, the quality of Hydro-Québec's signature on financial markets, diversified capital resources and its management of the proportions of variable-rate debt and debt repayable in foreign currency.

In addition, as at December 31, 2008, $34,881 million in long-term debt, perpetual debt and borrowings was guaranteed by the Québec government ($33,402 million as at December 31, 2007).

Maturities of financial liabilities are presented in the following table. The amounts reported are contractual undiscounted cash flows, representing payments of principal and interest for financial liabilities as at December 31, 2008.

Maturity	Borrowings[a]	Accounts payable and accrued liabilities	Dividends payable	Long-term debt	Derivative instruments[b]
2009	92	1,527	2,252	3,228	148
2010	–	51	–	3,134	1,067
2011	–	20	–	4,903	124
2012[c]	–	16	–	3,356	53
2013	–	2	–	3,270	115
1 to 5 years	92	1,616	2,252	17,891	1,507
6 to 10 years	–	–	–	11,160	270
11 to 15 years	–	–	–	17,056	198
16 to 20 years[c]	–	–	–	8,287	177
21 to 25 years	–	–	–	8,275	172
26 to 30 years	–	–	–	8,406	–
31 to 35 years	–	–	–	6,693	–
36 to 40 years	–	–	–	6,875	–
41 to 45 years	–	–	–	1,657	–
46 to 50 years	–	–	–	1,479	–
51 to 55 years	–	–	–	825	–
56 years and over	–	–	–	1,425	–
Total	**92**	**1,616**	**2,252**	**90,029**	**2,324**
Net carrying amount	91[d]	1,616[d, e]	2,252	36,060[f]	1,969

a) As at December 31, 2008, the weighted average interest rate on short-term borrowings was 2.59% (4.38% as at December 31, 2007).

b) Agreements entered into with certain counterparties to limit the market value of these financial instruments could result in cash inflows or outflows at dates different from the initially scheduled maturity dates.

c) Certain debts carry sinking fund requirements.

d) Because of their short-term maturities, the carrying amount of these financial liabilities approximates their fair value.

e) Of this amount, $1,527 million is recorded in Accounts payable and accrued liabilities and $89 million in Other long-term liabilities.

f) Including the current portion.

Contractual maturities of perpetual debt result in biennial interest flows. Perpetual notes in the amount of $355 million (US$289 million) bear interest at a rate determined semiannually based on LIBOR, plus 0.0625%. As at December 31, 2008, the applicable rate was 3.6%.

Credit risk

Credit risk is the risk that one party to a financial asset will fail to meet its obligations.

Hydro-Québec is exposed to credit risk related to cash equivalents, short-term investments and derivative instruments traded with financial institutions. It is also exposed to credit risk related to accounts receivable arising primarily from its day-to-day energy sales in and outside Québec. It should be noted that sales in Québec are billed at rates that allow for recovery of costs based on conditions approved by the Régie. Credit risk is limited to the carrying amount presented under assets on the balance sheet, which approximates fair value.

CASH EQUIVALENTS, SHORT-TERM INVESTMENTS AND DERIVATIVE INSTRUMENTS

In order to reduce its credit risk exposure, Hydro-Québec deals with Canadian and international issuers and financial institutions with high credit ratings. In addition, it applies policies to limit risk concentration as well as various monitoring programs and sets credit limits for each counterparty. Through prior agreements, it can also limit the market value of the main derivative instrument portfolios. Any variation in market value beyond the agreed-upon limit results in an inflow or outflow of cash. As at December 31, 2008, substantially all counterparties with whom Hydro-Québec dealt had a rating over A- and none of them had defaulted on their obligations to Hydro-Québec.

CUSTOMERS – ENERGY SALES (RECORDED IN ACCOUNTS RECEIVABLE)

Exposure to credit risk from energy sales is limited due to Hydro-Québec's large and diverse customer base. Management is of the opinion that Hydro-Québec is not exposed to a major credit risk. Moreover, Hydro-Québec holds as collateral customer deposits of $39 million ($30 million as at December 31, 2007), of which $9 million is recorded in Accounts payable and accrued liabilities and $30 million is in Other long-term liabilities.

The value of accounts receivable, by age and net of the related bad debt provision, is presented in the following table.

	2008
Under 30 days[a]	**1,481**
30 to 60 days	**62**
61 to 90 days	**30**
Over 90 days	**140**
	1,713

a) Including unbilled electricity deliveries.

In 2008, the bad debt provision increased by $57 million to $201 million as at December 31 ($144 million as at December 31, 2007). The provision is based on account age and customer standing.

Note 17 Interests in Joint Ventures

The proportionate share of the joint venture items included in the consolidated financial statements is presented in the following table. These joint ventures consist of the interests managed by Groupe de la technologie and Hydro-Québec Production.

	2008	2007
Operations		
Revenue	**26**	21
Expenditure and financial expenses	**30**	26
Income from discontinued operations	**–**	1
Net loss	**(4)**	(4)
Balance sheets		
Current assets	**9**	13
Long-term assets	**35**	29
Current liabilities	**9**	14
Long-term liabilities	**35**	30
Net liabilities	**–**	(2)
Cash flows		
Operating activities	**–**	(4)
Investing activities	**(2)**	(2)
Financing activities	**(3)**	(1)
Discontinued operations	**–**	(3)
Net change in cash and cash equivalents	**(5)**	(10)

Note 18 Equity

Share capital

The authorized share capital consists of 50,000,000 shares with a par value of $100 each, of which 43,741,090 shares were issued and paid-up as at December 31, 2008 and 2007.

Retained earnings

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

However, in respect of a given financial year, no dividend may be declared in an amount that would have the effect of reducing the capitalization rate to less than 25% at the end of the year. The Québec government declares the dividends for a given year within 30 days after Hydro-Québec has sent it the financial data related to the distributable surplus. Upon expiry of the prescribed period, all or a portion of the distributable surplus that has not been subject to a dividend declaration may no longer be distributed to the shareholder as a dividend.

For 2008, the Québec government declared dividends of $2,252 million ($2,095 million in 2007).

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

ACCUMULATED OTHER COMPREHENSIVE INCOME

			2008
	Cash flow hedges	Other	Total
Balance, beginning of year	965	(3)	**962**
Change for the year	278	3	**281**
Balance, end of year	1,243	–	**1,243**

			2007
	Cash flow hedges	Other	Total
Balance, beginning of year	479	(8)	471
Change for the year	486	5	491
Balance, end of year	965	(3)	962

Note 19 Capital Management

Hydro-Québec manages its capital in such a way as to meet its shareholder's expectations, safeguard its funds at all times and sustain its growth. It fosters a management environment allowing it to enhance the long-term value of its assets and equity, ensure its financial sustainability, preserve its financing capability and safeguard its funds and securities.

In addition to equity, capital includes long-term debt, perpetual debt, short-term borrowings and derivative instruments.

Hydro-Québec uses its capitalization rate to monitor its capital structure. It aims to maintain capitalization at no less than 25%.

CAPITALIZATION

	2008	2007
Equity	**22,062**	20,892
Long-term debt, including current portion	**36,060**	34,248
Perpetual debt	**355**	286
Short-term borrowings	**91**	73
Derivative instruments	**(118)**	228
Total	**58,450**	55,727
Capitalization rate (%)[a]	**37.7**	37.5

a) Equity divided by the sum of equity, long-term debt, perpetual debt, short-term borrowings, current portion of long-term debt and derivative instrument liabilities, less derivative instrument assets.

In 2008, Hydro-Québec's capital management objectives were unchanged from those in 2007.

Note 20 Supplementary Cash Flow Information

	2008	2007
Change in non-cash working capital items		
Accounts receivable	**(175)**	(172)
Materials, fuel and supplies	**6**	5
Accounts payable and accrued liabilities	**–**	23
Accrued interest	**20**	(47)
	(149)	(191)
Investing activities not affecting cash		
(Decrease) increase in property, plant and equipment and intangible assets	**(92)**	90
Interest paid	**2,093**	2,131

Note 21 Employee Future Benefits

Hydro-Québec's pension plan (the "Pension Plan") is a funded plan that ensures pension benefits based on the number of years of service and an average of the best five years of earnings. These benefits are indexed annually based on a rate which is the greater of the inflation rate, up to a maximum of 2%, and the inflation rate less 3%.

Hydro-Québec also offers other post-retirement and post-employment benefits. Post-retirement benefits are provided by group life, medical and hospitalization plans, which are contributory plans with contributions adjusted annually. Post-employment benefits are under non-contributory salary insurance plans, which pay short- and long-term disability benefits. Most of these plans are not funded, with the exception of the long-term disability salary insurance plan, which is fully funded, and the supplementary group life insurance plan, which is partially funded.

Hydro-Québec's employee benefit plans are defined-benefit plans. The accrued benefit obligations of these plans, valued by independent actuaries, and assets, at fair value, are valued as at December 31 of each year. The most recent actuarial valuation for funding purposes of the Pension Plan was as at December 31, 2007, and the next valuation must be performed no later than December 31, 2010.

The following table presents information concerning Hydro-Québec's employee future benefit plans:

	Pension Plan		Other plans	
	2008	2007	**2008**	2007
Accrued benefit obligations				
Balance, beginning of year	**12,607**	12,720	**929**	850
Current service cost	**285**	336	**42**	38
Employee contributions	**84**	66	**–**	–
Benefit payments and refunds	**(510)**	(460)	**(51)**	(49)
Interest on obligations	**712**	659	**51**	46
Actuarial (gains) losses	**(3,138)**	(714)	**(198)**	44
Amendments to the Pension Plan	**168**	–	**–**	–
Balance, end of year	**10,208**	12,607	**773**	929
Plan assets at fair value				
Balance, beginning of year	**12,926**	12,811	**58**	56
Actual return on plan assets	**(2,434)**	538	**2**	2
Employee contributions	**84**	66	**–**	–
Current contributions by Hydro-Québec	**291**	5	**11**	11
Special contribution by Hydro-Québec	**149**	–	**–**	–
Benefit payments and refunds	**(510)**	(460)	**(11)**	(12)
Administrative fees	**(31)**	(34)	**–**	–
Balance, end of year	**10,475**	12,926	**60**	57
Surplus (deficit), end of year	**267**	319	**(713)**	(872)
Unamortized past service costs	**335**	217	**–**	–
Unamortized net actuarial loss (gain)	**1,292**	1,205	**(17)**	190
Unamortized transitional (asset) obligation	**(761)**	(913)	**67**	81
Accrued benefit asset (liability)	**1,133**	828	**(663)**	(601)

In 2008, some amendments were made to the Pension Plan following agreements reached between Hydro-Québec and its unions. These amendments, which came into force on January 1, 2009, concern temporary and permanent provisions. The main temporary provisions concern retirement without pension reduction and the bridging benefit, whereas the main permanent provisions apply to the cost of optional pension forms and the broadening of the definition of the surviving spouse upon a retiree's death. Amendments to the funding rules of the Pension Plan were also adopted under these agreements. As a result, the rates for employee and employer contributions have been 6.0% and 6.9%, respectively, since January 1, 2009. These rates will be increased annually by 0.5% and 0.9% until they reach up to 7.5% and 10.5% of the eligible base earnings in 2013.

Additional disclosures with respect to plan assets

At year end, assets of the plans at fair value consisted of:

	Pension Plan		Other plans	
%	**2008**	2007	**2008**	2007
Bonds	**54**	39	**91**	95
Equities	**32**	46	**–**	–
Real-estate investments	**10**	6	**–**	–
Short-term investments	**4**	9	**–**	–
Other	**–**	–	**9**	5
	100	100	**100**	100

Assets of the plans include the following securities issued by Hydro-Québec and the Québec government:

	Pension Plan		Other plans	
	2008	2007	**2008**	2007
Bonds	**1,359**	1,266	**56**	55

Cash payments

Cash payments made by Hydro-Québec for employee benefit plans consist of the contributions paid to the funded plans and the benefits paid to employees and pensioners under unfunded plans. The cash payment details are as follows:

	2008	2007
Contributions by Hydro-Québec		
Pension Plan	**440**	5
Other funded plans	**11**	11
Benefit payments		
Unfunded plans	**41**	38
Cash payments	**492**	54

In compliance with the actuarial valuation for funding purposes as at December 31, 2007, Hydro-Québec made a current contribution of $291 million in 2008, including an additional contribution of $208 million, to cover the current service cost, and a special contribution of $149 million to cover the unfunded actuarial liability.

In 2007, Hydro-Québec took a contribution holiday as of February 16, namely the filing date of the actuarial valuation with the Régie des rentes du Québec. Earlier in 2007, Hydro-Québec had made a contribution of $5 million to the Pension Plan.

ELEMENTS OF ACCRUED BENEFIT COST RECOGNIZED FOR THE YEAR

	Pension Plan		Other plans	
	2008	2007	**2008**	2007
Current service cost[a]	**285**	336	**42**	38
Administrative fees[b]	**31**	34	**–**	–
Interest on obligations	**712**	659	**51**	46
Actual return on plan assets	**2,434**	(538)	**(2)**	(2)
Actuarial (gains) losses	**(3,138)**	(714)	**(198)**	44
Amendments to the Pension Plan	**168**	–	**–**	–
Cost (credit) before adjustments required to recognize the long-term nature of employee future benefits	**492**	(223)	**(107)**	126
Difference between actual and expected return on assets	**(3,237)**	(201)	**–**	–
Difference between actuarial (gains) losses on accrued benefit obligations and actuarial losses recognized	**3,150**	829	**207**	(34)
Difference between amendments to the Pension Plan and amortization of past service cost	**(118)**	39	**–**	–
Amortization of transitional (asset) obligation	**(152)**	(152)	**14**	14
	(357)	515	**221**	(20)
Cost recognized for the year	**135**	292	**114**	106

a) For the long-term disability salary insurance plan, the current service cost corresponds to the cost of new disability cases for the year.

b) Administrative fees billed to the Pension Plan by Hydro-Québec amounted to $12 million for 2008 ($13 million for 2007).

Significant actuarial assumptions

The following actuarial assumptions, used to determine the accrued benefit obligations and cost of the plans, result from a weighted average:

	Pension Plan		Other plans	
%	**2008**	2007	**2008**	2007
Accrued benefit obligations				
Rate at end of year				
Discount rate	**7.49**	5.53	**7.49**	5.53
Salary escalation rate[a]	**2.86**	3.26	**–**	–
Accrued benefit cost recognized				
Rate at end of prior year				
Discount rate	**5.53**	5.20	**5.53**	5.20
Expected long-term rate of return on plan assets	**6.25**	6.25	**3.81**	4.23
Salary escalation rate[a]	**3.26**	3.38	**–**	–

a) This rate takes salary increases into account as well as promotion opportunities while in service.

As at December 31, 2008, health care costs were based on an annual growth rate of 7.5% for 2009. Thereafter, based on the assumption used, this rate will gradually decrease until it ultimately reaches 4.6% in 2017. A change of 1% in this annual growth rate would have had the following impact for 2008:

	1% increase	1% decrease
Impact on current service cost and interest cost on accrued benefit obligations for the year	6	(5)
Impact on accrued benefit obligations at end of year	40	(33)

Note 22

Commitments and Contingencies

Electricity purchases

On May 12, 1969, Hydro-Québec signed a contract with Churchill Falls (Labrador) Corporation Limited [CF(L)Co] whereby Hydro-Québec undertook to purchase substantially all the output from Churchill Falls generating station, which has a rated capacity of 5,428 MW. Expiring in 2016, this contract will be automatically renewed for a further 25 years under agreed-upon terms and conditions. On June 18, 1999, Hydro-Québec and CF(L)Co 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.

As at December 31, 2008, Hydro-Québec was committed under 115 contracts to purchase electricity from other power producers, for an installed capacity of about 5,792 MW. It expects to purchase approximately 22 TWh of energy annually over the terms of these contracts, which extend through 2045. The majority of these contracts include renewal clauses.

Hydro-Québec expects to make the following minimum payments on all its electricity purchase contracts over the next five years:

2009	690
2010	1,098
2011	1,158
2012	1,376
2013	1,596

Guarantees

Hydro-Québec grants guarantees to third parties for indemnification purposes in connection with its energy-related transactions on markets outside Québec. These guarantees are issued under long-term agreements and agreements governing its involvement in organized markets. These markets require that each participant provide guarantees enabling it to meet its obligations in the event of a default of payment by another participant. Hydro-Québec also grants guarantees as part of its international operations and in the field of electrotechnology.

As at December 31, 2008, the potential maximum amount Hydro-Québec could have had to pay under letters of credit or guarantees provided as security totaled $405 million. Of this amount, $326 million was related to energy purchases. Guarantees amounting to $140 million will expire between 2009 and 2019, while others totaling $265 million do not have maturity dates.

Hydro-Québec provided guarantees to the purchasers of its interests with respect to contingent tax liabilities and certain other customary representations. These guarantees, for which no liability was recognized, will be in effect until the applicable limitation periods expire.

In accordance with the terms and conditions of certain debt securities issued outside Canada, Hydro-Québec has undertaken to increase the amount of interest paid to non-residents in the event of changes to Canadian tax legislation governing the taxation of non-residents' income. Hydro-Québec cannot estimate the maximum amount it might have to pay under such circumstances. Should an amount become payable, Hydro-Québec has the option of redeeming most of the securities in question. As at December 31, 2008, the amortized cost of these debts was $4,769 million.

Under the contract signed on May 12, 1969, with CF(L)Co, Hydro-Québec could be required to provide additional funding if CF(L)Co were unable to pay its expenses and service its debt. The maximum amount that Hydro-Québec could be required to pay cannot be reasonably evaluated, however, since it is not stated in the contract and since the amount payable would depend on the outcome of future events whose nature and probability cannot be determined. To date, Hydro-Québec has not had to pay any amount under this contract.

Investments

Hydro-Québec expects to invest approximately $4.7 billion in property, plant and equipment and intangible assets in 2009.

Litigation

In the normal course of its development and operating activities, Hydro-Québec is sometimes party to claims and legal proceedings. Management is of the opinion that adequate provisions have been made for any disbursements that could result from these legal actions. Consequently, it does not foresee any adverse effect of such contingent liabilities on Hydro-Québec's consolidated operating results or financial position.

Note 23 Related Party Transactions

Hydro-Québec enters into various business transactions, including sales of electricity, with the Québec government and its agencies, as well as with other government corporations in the normal course of business. These business transactions are measured at the exchange amount.

The main transactions and balances owing to related parties or owed by them are as follows:

	2008	2007
Québec government		
Accounts receivable	**5**	7
Accounts payable	**26**	45
Capital tax	**202**	278
Public utilities tax	**302**	240
Water-power royalties	**546**	263
Guarantee fees	**167**	169
Significantly influenced investees		
Accounts payable	**9**	14
Electricity purchases	**98**	106

Note 24 Segmented Information

Hydro-Québec carries on its activities in the four reportable business segments defined below. The non-reportable business segments and other activities are grouped together under Corporate and Other Activities for reporting purposes.

Generation: Hydro-Québec Production operates and develops Hydro-Québec's generating facilities. This division also sells electricity on external markets and engages in energy trading. Hydro-Québec Production provides Hydro-Québec Distribution with a base volume of up to 165 TWh of heritage pool electricity annually at an average price of 2.79¢/kWh. In excess of this volume, it can participate in Hydro-Québec Distribution's calls for tender in a context of free market competition.

Transmission: Hydro-Québec TransÉnergie operates and develops Hydro-Québec's power transmission system in Québec and manages power flows on the transmission system.

Distribution: Hydro-Québec Distribution operates and develops Hydro-Québec's distribution system and is responsible for sales and services to Québec customers. It also promotes energy efficiency and ensures the security of the supply of electricity to the Québec market.

Construction: Hydro-Québec Équipement carries out engineering, refurbishment and construction work related to hydroelectric development projects throughout Québec, except on the territory governed by the *James Bay and Northern Québec Agreement,* where Société d'énergie de la Baie James assumes this responsibility. Hydro-Québec Équipement also builds power transmission lines and substations throughout the province.

Corporate and Other Activities: The corporate units support the divisions in the achievement of their business objectives. They include Groupe de la technologie, Groupe des affaires corporatives et du secrétariat général, Groupe des ressources humaines et des services partagés, Vice-présidence à la comptabilité et au contrôle and Vice-présidence au financement, à la trésorerie et à la caisse de retraite. The Centre de services partagés brings together internal services including goods and services procurement, real estate management, and material and transportation service management.

The amounts presented for each segment are based on the financial information used to prepare the consolidated financial statements. The accounting policies used to calculate these amounts are as described in Notes 1 and 3.

Intersegment transactions related to electricity sales are recorded based on the supply and transmission rates provided for by the *Act respecting the Régie de l'énergie*. The Act sets a commodity rate for an annual base volume of up to 165 TWh of heritage pool electricity for the Québec market.

Other intersegment products and services are measured at full cost.

Hydro-Québec derives the bulk of its revenue in Québec, and substantially all its property, plant and equipment is located in the province. In 2008, revenue from outside Québec amounted to $2,099 million, with $1,776 million coming from the U.S. ($1,780 million and $1,483 million, respectively, in 2007).

Note 24 Segmented Information (continued)

OPERATIONS AND ASSETS BY SEGMENT

	Generation	Transmission	Distribution	Construction	Corporate and Other Activities	Intersegment eliminations and adjustments	2008 Total
Revenue							
External customers	2,066	52	10,540	–	32	27[a]	**12,717**
Intersegment	4,931	2,733	62	2,416	1,156	(11,298)	**–**
Depreciation and amortization	777	611	828	5	127	(12)	**2,336**
Financial expenses	1,101	817	486	–	41	–	**2,445**
Income from continuing operations	2,137	481	421	–	(39)	12	**3,012**
Net income	2,137	481	421	–	90	12	**3,141**
Total assets	30,651	17,158	12,274	360	6,734	(403)	**66,774**
Investing activities							
Increase (decrease) in property, plant and equipment and intangible assets							
Affecting cash	1,894	1,097	664	5	96	–	**3,756**
Not affecting cash	(113)	17	4	–	–	–	**(92)**

	Generation	Transmission	Distribution	Construction	Corporate and Other Activities	Intersegment eliminations and adjustments	2007 Total
Revenue							
External customers	1,649	37	10,452	–	49	143[a]	12,330
Intersegment	5,103	2,785	56	2,150	1,163	(11,257)	–
Depreciation and amortization	837	636	446	7	77	(12)	1,991
Financial expenses	1,180	817	484	–	31	–	2,512
Income from continuing operations	2,077	396	395	–	2	12	2,882
Net income	2,077	396	395	–	27	12	2,907
Total assets	29,509	16,707	11,833	263	6,814	(260)	64,866
Investing activities							
Increase in property, plant and equipment and intangible assets							
Affecting cash	1,807	844	721	3	89	–	3,464
Not affecting cash	41	14	35	–	–	–	90

a) Resales of excess supply by Hydro-Québec Distribution on outside markets are presented as offsets of electricity purchases rather than in Revenue.

Note 25 Comparative Information

Some of the prior year's data have been reclassified to conform to the presentation adopted in the current year.

Five-Year Review

Consolidated Financial Information

$M	**2008**	2007	2006	2005	2004
OPERATIONS					
Revenue	**12,717**	12,330	11,161	10,887	10,341
Expenditure					
Operations	**2,497**	2,541	2,389	2,245	2,154
Electricity and fuel purchases	**1,406**	1,555	1,315	1,496	1,464
Depreciation and amortization	**2,336**	1,991	2,007	2,023	1,862
Taxes	**1,093**	820	534	597	610
Regulatory deferrals	**(72)**	29	(93)	(11)	–
	7,260	6,936	6,152	6,350	6,090
Operating income	**5,457**	5,394	5,009	4,537	4,251
Financial expenses	**2,445**	2,512	2,212	2,186	2,083
Income from continuing operations	**3,012**	2,882	2,797	2,351	2,168
Income (loss) from discontinued operations	**129**	25	944	(99)	267
Net income	**3,141**	2,907	3,741	2,252	2,435
DIVIDENDS DECLARED	**2,252**	2,095	2,342	1,126	1,350
BALANCE SHEET SUMMARY					
Total assets	**66,774**	64,866	63,254	60,431	58,072
Long-term debt, including current portion and perpetual debt	**36,415**	34,534	34,427	33,007	33,401
Equity	**22,062**	20,892	18,840	17,376	16,220
INVESTMENTS FOR CONTINUING OPERATIONS AFFECTING CASH					
Property, plant and equipment and intangible assets	**3,756**	3,464	3,348	3,293	3,071
Costs related to Energy Efficiency Plan	**236**	172	149	91	41
Total investments	**3,992**	3,636	3,497	3,384	3,112
FINANCIAL RATIOS					
Interest coverage[a]	**2.12**	2.13	2.06	2.00	1.79
Return on equity (%)[b]	**15.4**	15.0	20.6	13.3	15.4
Profit margin from continuing operations (%)[c]	**23.7**	23.4	25.1	21.6	21.0
Capitalization (%)[d]	**37.7**	37.5	36.1	34.1	32.7
Self-financing (%)[e]	**44.9**	61.9	69.9	51.2	65.9

a) Sum of operating income and net investment income divided by gross interest expense.

b) Net income divided by average equity less average accumulated other comprehensive income.

c) Net income from continuing operations divided by revenue.

d) Equity divided by the sum of equity, long-term debt, perpetual debt, short-term borrowings, current portion of long-term debt and derivative instrument liabilities, less derivative instrument assets.

e) Cash flows from operating activities less dividends paid, divided by the sum of cash flows from investing activities—excluding net (acquisition) disposal of short-term investments—and repayment of long-term debt.

Note: Throughout the Five-Year Review and the Consolidated Results by Quarter, certain comparative figures have been reclassified to reflect the presentation adopted in the current year.

Operating Statistics

	2008	2007	2006	2005	2004
GWh					
Electricity sales					
In Québec, by category					
Residential and farm	**60,747**	60,046	56,722	57,269	58,002
General and institutional	**35,228**	34,751	32,440	33,463	33,137
Industrial	**69,144**	73,005	73,297	73,447	69,722
Other	**5,278**	5,353	4,878	4,998	5,026
	170,397	173,155	167,337	169,177	165,887
Outside Québec					
Canada/U.S. (long-term)	**2,516**	2,384	2,384	2,068	1,930
Canada/U.S. (short-term)	**18,783**	17,240	12,074	13,274	12,462
	21,299	19,624	14,458	15,342	14,392
Total electricity sales	**191,696**	192,779	181,795	184,519	180,279
$M					
Revenue from electricity sales					
In Québec, by category					
Residential and farm	**4,300**	4,144	3,775	3,690	3,690
General and institutional	**2,687**	2,602	2,356	2,284	2,234
Industrial	**3,174**	3,336	3,022	2,892	2,751
Other	**284**	286	249	255	247
	10,445	10,368	9,402	9,121	8,922
Outside Québec					
Canada/U.S. (long-term)	**220**	225	198	174	179
Canada/U.S. (short-term)	**1,699**	1,392	951	1,290	905
	1,919	1,617	1,149	1,464	1,084
Total revenue from electricity sales	**12,364**	11,985	10,551	10,585	10,006
As at December 31					
Number of customer accounts					
In Québec, by category					
Residential and farm	**3,603,330**	3,554,443	3,501,709	3,450,455	3,399,776
General and institutional	**296,504**	299,524	295,618	283,616	282,748
Industrial	**10,111**	11,565	12,032	12,796	13,117
Other	**3,499**	3,440	5,767	5,643	5,634
Total customer accounts	**3,913,444**	3,868,972	3,815,126	3,752,510	3,701,275
kWh/customer account					
Average annual consumption					
In Québec, by category					
Residential and farm	**16,974**	17,019	16,318	16,720	17,203
General and institutional	**118,209**	116,782	112,010	118,168	117,352
Industrial	**6,379,775**	6,187,651	5,904,382	5,668,738	5,262,038
Other	**1,521,257**	1,162,811	855,039	886,406	878,211

	2008	2007	2006	2005	2004
MW					
Installed capacity[a]					
Hydroelectric	**34,118**	33,305	32,973	32,299	31,622
Nuclear	**675**	675	675	675	675
Thermal	**1,634**	1,665	1,665	1,595	1,593
Wind	**2**	2	2	2	2
Total installed capacity	**36,429**	35,647	35,315	34,571	33,892
GWh					
Total energy requirements[b]	**211,228**	209,818	199,447	200,179	193,025
MW					
Peak power demand in Québec[c]	**37,230**	35,352	36,251	33,636	34,956
km					
Lines (overhead and underground)					
Transmission	**33,058**	33,008	32,826	32,544	32,487
Distribution[d]	**110,127**	109,618	108,883	108,344	107,423
	143,185	142,626	141,709	140,888	139,910

a) Hydro-Québec also has access to almost all the output from Churchill Falls generating station (5,428 MW) and purchases all the output from eight privately owned wind farms with a total installed capacity of 530 MW. In addition, 1,277 MW are available under agreements with other independent suppliers.

b) Total energy requirements consist of kilowatthours delivered within Québec and to neighboring systems.

c) Total power demand at the annual domestic peak for the winter beginning in December, including interruptible power. The 2008–2009 winter peak for Québec occurred at 8:00 a.m. on January 16, 2009.

d) These figures include off-grid systems but exclude private systems, lines under construction and 44-kV lines (transmission).

Other Information

	2008	2007	2006	2005	2004
%					
Rate increases					
Average increase from January 1 to December 31	**2.7**	2.8	4.3	1.3	4.1
Inflation rate	**2.3**	2.2	2.0	2.2	1.8
Number of employees[a]					
Permanent as at December 31	**19,297**	19,459	19,116	19,009	18,835
Temporary (year's average)	**4,048**	3,910	3,799	3,577	3,567
Women (%)	**30.9**	31.3	30.6	29.8	29.4

a) Excludes employees of subsidiaries and joint ventures.

Consolidated Results by Quarter

$M	1st quarter	2nd quarter	3rd quarter	4th quarter	2008 12-month period
				(unaudited)	(audited)
Revenue	3,771	2,960	2,814	3,172	**12,717**
Expenditure					
Operations	614	629	601	653	**2,497**
Electricity and fuel purchases	337	329	364	376	**1,406**
Depreciation and amortization	575	577	525	659	**2,336**
Taxes	298	230	239	326	**1,093**
Regulatory deferrals	(1)	(116)	–	45	**(72)**
	1,823	1,649	1,729	2,059	**7,260**
Operating income	1,948	1,311	1,085	1,113	**5,457**
Financial expenses	615	595	598	637	**2,445**
Income from continuing operations	1,333	716	487	476	**3,012**
Income from discontinued operations	117	5	4	3	**129**
Net income	1,450	721	491	479	**3,141**

$M	1st quarter	2nd quarter	3rd quarter	4th quarter	2007 12-month period
				(unaudited)	(audited)
Revenue	3,732	2,828	2,554	3,216	12,330
Expenditure					
Operations	606	616	597	722	2,541
Electricity and fuel purchases	422	337	441	355	1,555
Depreciation and amortization	482	477	472	560	1,991
Taxes	208	188	200	224	820
Regulatory deferrals	(14)	(14)	(15)	72	29
	1,704	1,604	1,695	1,933	6,936
Operating income	2,028	1,224	859	1,283	5,394
Financial expenses	618	589	642	663	2,512
Income from continuing operations	1,410	635	217	620	2,882
Income from discontinued operations	21	–	–	4	25
Net income	1,431	635	217	624	2,907

Corporate Management

Thierry Vandal
President and Chief Executive Officer

Marie-José Nadeau
Executive Vice President,
Corporate Affairs and Secretary General

Maurice Charlebois
Executive Vice President,
Human Resources and Shared Services

Élie Saheb
Executive Vice President,
Technology

Jean-Hugues Lafleur
Vice President,
Financing, Treasury and Pension Fund

Lise Croteau
Vice President,
Accounting and Control

Board of Directors

Michael L. Turcotte
Chairman of the Board,
Hydro-Québec
Appointment: November 17, 2005
Term: November 17, 2009
Status: Independent director

Mr. Turcotte holds a Bachelor of Arts degree from the University of Montréal and a Master's degree from Laval University School of Business. He enjoyed a lengthy career with the Royal Bank of Canada where he held various senior positions. Since retirement from the Bank, Mr. Turcotte has acted as a corporate director. He was Chairman of the Board of Management of the Canada Customs and Revenue Agency from 1999 to 2004.

Thierry Vandal
President and Chief Executive Officer,
Hydro-Québec
Appointment: April 6, 2005
Term: October 3, 2012
Status: Non-independent director

With a Bachelor of Engineering from the École Polytechnique de Montréal and an MBA from HEC Montréal, Thierry Vandal has worked in the energy sector for more than 25 years. In particular, he participated in the operations, marketing and strategic planning aspects of the petroleum, petrochemical and natural gas industries before joining Hydro-Québec in 1996. Mr. Vandal is Chairman of the Board of The Conference Board of Canada and Collège Notre-Dame and is a director of HEC Montréal and McGill University.

Previous page, from left to right: Michael L. Turcotte, Chairman of the Board, Louis Lagassé, Thierry Vandal, President and Chief Executive Officer, Suzanne Gouin, Marie-Anne Tawil, Bernard Gaudreault and Jacques Leblanc. Below: Carl Cassista, Nathalie Le Prohon, Normand Bergeron, Deputy Minister of Natural Resources and Wildlife, Marie-France Poulin, Emmanuel Triassi, Gilles Vaillancourt, Anik Brochu, Gaston Blackburn. Absent: Michel Plessis-Bélair.

Normand Bergeron

Deputy Minister of Natural Resources and Wildlife, Gouvernement du Québec

Appointment: May 2, 2005 (indefinite term)

Status: Non-independent director

Normand Bergeron has a Bachelor's degree in Sociology from the Université de Montréal and studied at the Master's level at the École nationale d'administration publique. Mr. Bergeron joined the Québec public service in 1975 and has held many executive positions, particularly in the energy sector. He served as Director General of the Agence de l'efficacité énergétique (1998–2000), Vice-Chairman of the Régie de l'énergie (2002–2005) and Associate Deputy Minister for Energy and Climate Change (2000–2002) before his appointment as Deputy Minister of Natural Resources and Wildlife.

Gaston Blackburn

President, G. Blackburn Inc.

Appointment: September 10, 2003

Term: February 11, 2012

Status: Independent director

A merchant and businessman, Gaston Blackburn was elected MNA for Roberval in 1988. He was successively Parliamentary Secretary to the Premier, Minister for the Environment, Minister of Recreation, Fish and Game and Minister for Transport, responsible for highway maintenance. He has served on the boards of companies in various sectors, including the food industry and natural resources.

Anik Brochu
Lawyer,
Cain Lamarre Casgrain Wells, LLP/Barristers & Solicitors
Appointment: September 13, 2006
Term: September 13, 2010
Status: Independent director

A graduate of the University of Ottawa in Law and member of the Barreau du Québec, Anik Brochu was General Manager of the Chambre de commerce de Val-d'Or from 1997 to 2008 before she joined the law firm Cain Lamarre Casgrain Wells. She sits on the boards of the Université du Québec en Abitibi-Témiscamingue and of the Association de l'exploration minière du Québec. She is also a member of various committees involved in the field of socio-economic development.

Carl Cassista
President, Axion Technologies Ltd.
Appointment: September 26, 2007
Term: September 26, 2011
Status: Independent director

A graduate of Université Laval and member of the Ordre des ingénieurs du Québec, Carl Cassista has worked in electrical engineering and in R&D, mainly for the Axion Technologies group. He joined that company in 1982 and has served there as President since 1994.

Bernard Gaudreault
Corporate Director
Appointment: December 5, 2001
Term: September 26, 2010
Status: Independent director

With a diploma in commerce from the Noranda Business School, Bernard Gaudreault has more than 30 years' experience in corporate management in real estate and the food industry. He is Chairman of the Board of the municipal housing bureau in Rouyn-Noranda.

Suzanne Gouin
President and Chief Executive Officer,
TV5 Québec Canada
Appointment: September 26, 2007
Term: September 26, 2011
Status: Independent director

Suzanne Gouin has a Bachelor's degree in Political Science from Concordia University, where she also took graduate courses in media studies. She completed an MBA at the University of Western Ontario and has certification from the Institute of Corporate Directors. She has held several management positions in media companies and joined TV5 Québec Canada in 2002. Ms. Gouin sits on the boards of various not-for-profit organizations.

Louis Lagassé
Chairman of the Board, Lagassé Group
Appointment: September 10, 2003
Term: February 11, 2012
Status: Independent director

Louis Lagassé is a member of the Chambre des notaires du Québec. He completed a law degree at the Université de Montréal, an MBA at the University of Western Ontario and a German language diploma at the University of Salzburg in Austria. Mr. Lagassé heads an industrial group that is active on the Canadian and European markets, and he serves on the boards of several telecommunications companies as well as various not-for-profit organizations.

Jacques Leblanc
President, Gestion Jacques Leblanc inc.
Appointment: April 7, 2004
Term: September 26, 2010
Status: Independent director

A graduate of Université Laval in administration, Jacques Leblanc is a chartered accountant and a Fellow of the Ordre des comptables agréés du Québec. He was a partner in the firm of Leblanc Bourque Arsenault for 25 years.

Nathalie Le Prohon
Corporate Director
Appointment: September 26, 2007
Term: September 26, 2011
Status: Independent director

Nathalie Le Prohon has a Bachelor of Commerce from McGill University and an MBA from Concordia University. She has held numerous executive positions in high-technology companies, including President of Nokia Canada. Ms. Le Prohon is a member of the board of Bentall and serves on the audit committee of National Defence. She also sits on the boards of various not-for-profit organizations.

Michel Plessis-Bélair
Vice-Chairman, Power Corporation of Canada
Appointment: April 7, 2004
Term: September 26, 2011
Status: Independent director

Michel Plessis-Bélair holds a Bachelor of Arts from the Université de Montréal, a business and accounting degree from HEC Montréal and an MBA from Columbia University in New York. In 1986, he joined Power Corporation of Canada. From 1986 to 2006, he successively served as Senior Vice-President, Finance and Administration, as Executive Vice-President and Chief Financial Officer and as Vice-Chairman and Chief Financial Officer. Currently, he is Vice-Chairman and a director of Power Corporation and several of its subsidiaries. Mr. Plessis-Bélair also sits on the boards of various not-for-profit organizations.

Marie-France Poulin
Executive Vice President,
Camada Group Inc.
Appointment: April 7, 2004
Term: September 26, 2011
Status: Independent director

Marie-France Poulin has a Bachelor of Business Administration with an option in Marketing from Université Laval, as well as certification from the Collège des administrateurs de sociétés. She has held several executive positions, including that of Vice President, Sales and Marketing, of MAAX. Ms. Poulin sits on the boards of various not-for-profit organizations.

Marie-Anne Tawil
President and Chief Executive Officer,
Les Investissements Iron Hill Inc.
Appointment: December 7, 2005
Term: December 7, 2010
Status: Independent director

With a Licentiate in Civil Law and a Bachelor of Common Law from the University of Ottawa and an MBA from Concordia University, Marie-Anne Tawil has earned certification from the Institute of Corporate Directors and is a member of the Barreau du Québec. She has practised law with two major law firms in Montréal, was Legal Counsel and Secretary of Quebecor and has held management positions in various other companies. Ms. Tawil is Chairman of the SAAQ (Société d'assurance automobile du Québec).

Emmanuel Triassi
President, Groupe T.E.Q. Inc.
Appointment: September 26, 2007
Term: September 26, 2011
Status: Independent director

A member of the Ordre des ingénieurs du Québec, Emmanuel Triassi holds a Bachelor's degree from McGill University and a Master's degree in Building Engineering from Concordia University. He is the founding president of a general contracting company specializing in construction project management.

Gilles Vaillancourt
Mayor, Ville de Laval
Appointment: September 26, 2007
Term: September 26, 2011
Status: Independent director

Following studies in pharmacology and business management, Gilles Vaillancourt launched his career in business. At the same time, he became involved in municipal affairs. He was elected Mayor of Laval in 1989 and serves in this capacity on the boards of various representational organizations at the local, regional, provincial and national levels. Mr. Vaillancourt also sits on the boards of various not-for-profit organizations.

Activity Report of the Board of Directors and Board Committees

Hydro-Québec's head office, in Montréal.

Board of Directors

Hydro-Québec's Board of Directors is made up of 16 members, including the Chairman of the Board and the President and Chief Executive Officer. The directors' diverse professional backgrounds are a definite asset for the seven Board committees: Executive, Governance and Ethics, Audit, Human Resources, Finance, Environment and Public Affairs, and Pension Plan Financial Management. The Board is chaired by Michael Turcotte.

Mandate: The Board administers the company's business efficiently, in accordance with the *Hydro-Québec Act*, the *Companies Act* and the applicable regulations. Its principal functions include reviewing and approving the Strategic Plan and the annual Business Plan, setting the company's annual performance targets, reviewing financial results on a monthly basis, and performing the cyclical review of integrated enterprise risk management. It also approves the appointment of executives other than the President and Chief Executive Officer and the policies governing compensation and working conditions for Hydro-Québec's employees and executives. In addition, it approves the company's major capital projects in generation, transmission and distribution as well as matters submitted to the Régie de l'énergie.

Activities: The Board met 11 times in 2008, while its committees held 32 meetings in all. The Board reviewed Hydro-Québec's *Follow-up to the Strategic Plan 2006–2010* and participated in work sessions to develop the *Strategic Plan 2009–2013*, which will be filed with the government of Québec by August 1, 2009. As part of this activity, presentations were made to the directors on the business and economic context in which the company operates; the challenges it faces in generation, transmission and distribution; and the principal risks with which it has to contend. The Board also considered the follow-up report on the induction and training program for its members, examined the expertise and experience profiles established for the selection of new directors and reviewed the mandates of its committees. Moreover, it approved Hydro-Québec's updated policies. It also assessed its own functioning and updated the bylaw setting out the functions and powers of the Chairman and Vice-Chairman of the Board, as well as the senior executives and other members of Management.

The Board's many decisions in 2008 included its authorization to continue the draft design of the Romaine hydropower complex and to sign the necessary agreements with three of the Innu communities concerned. It approved the refurbishing of Gentilly-2 nuclear generating station, construction of Anne-Hébert substation (315/25 kV) and upgrading of the transmission system. It also greenlighted the refurbishment of the synchronous condensers at Abitibi substation, the modernization of Manic-1 generating station and a revision of the total budget allocated to construction and to the financing of agreements in connection with the Chute-Allard and Rapides-des-Cœurs project and phase II of the La Tuque refurbishment.

The Board's recurring deliberations dealt with the quarterly and annual objectives and financial results of the company and certain wholly owned subsidiaries, as well as with the financial management of the pension plan. It reviewed the progress of the company's capital projects and examined the risk management process and consolidated enterprise risk portfolio. It gave its prior approval to matters submitted to the Régie de l'énergie as well as to the annual internal audit plan and the external auditors' plan and fees in connection with the audit of the financial statements of the company and of the pension plan. Finally, the Board closely monitored the work of its committees.

Directors visiting jobsites. Left, in foreground, Bernard Gaudreault. Right, Marie-Anne Tawil, Thierry Vandal and Marie-France Poulin.

Director Attendance at Meetings of the Board of Directors and Board Committees in 2008

		Number of Meetings							
		11		7	7	7	4	3	4
Directors	Notes	**Board**	**A**[1]	**B**	**C**	**D**	**E**	**F**	**G**
Michael L. Turcotte A B C D E F G		11		7	7	7	4	3	4
Thierry Vandal A E F G	2	11		6	7	7	4	0	3
Normand Bergeron		9							
Gaston Blackburn F		10						3	
Anik Brochu F		10						3	
Carl Cassista D	3	11				5			
Bernard Gaudreault C		11			7				
Suzanne Gouin F		9						3	
Louis Lagassé A D E G	3	8				2	2		3
Jacques Leblanc B C	4	11		7	7		1		
Nathalie Le Prohon A D	5	10				5			
Michel Plessis-Bélair A B E G		8		5			4		3
Marie-France Poulin B D		11		7		6			
Marie-Anne Tawil B D		10		7		6			
Emmanuel Triassi C		10			6				
Gilles Vaillancourt G		9							3

	Number of Meetings							
	7		5	5	5	2	2	2
Outgoing Director	**Board**	**A**	**B**	**C**	**D**	**E**	**F**	**G**
Hélène F. Fortin C E (Resignation: September 5, 2008)	7			5		2		

Board Committees

A Executive
B Governance and Ethics
C Audit
D Human Resources
E Finance
F Environment and Public Affairs
G Pension Plan Financial Management

1) The Executive Committee meets when necessary. It did not hold any meetings in 2008.
2) Thierry Vandal attends meetings of the Governance and Ethics, Audit and Human Resources committees as a guest.
3) Carl Cassista was appointed to the Human Resources Committee as a replacement for Louis Lagassé on May 16, 2008.
4) Jacques Leblanc replaced Louis Lagassé at the Finance Committee meeting of November 12, 2008.
5) Nathalie Le Prohon was appointed to the Human Resources Committee on March 14, 2008.

Executive (A)

Mandate: The Executive Committee is vested with all of the powers of the Board of Directors, except those powers that are expressly reserved for the Board by law and under the company's bylaws. The Executive Committee, which meets only in emergencies, did not hold any meetings in 2008. It is chaired by Michael Turcotte.

Governance and Ethics (B)

Mandate: The role of the Governance and Ethics Committee is to develop the rules of governance and codes of ethics applicable to directors, senior executives appointed by the company and employees of Hydro-Québec and its wholly owned subsidiaries; the expertise and experience profiles used in appointing Board members; the criteria for assessing the performance of directors and the Board; the induction and training program for directors; and the measures for evaluating the company's efficiency and performance. This committee also makes recommendations to the Board regarding the company's policies and Strategic Plan and the composition and mandate of the Board committees. It is chaired by Michael Turcotte.

Activities: In 2008, the Governance and Ethics Committee met seven times. Closely observing the governance measures for state-owned enterprises as incorporated into the *Hydro-Québec Act*, it assessed the performance of the Board of Directors and reviewed the mandates of the Board committees and the expertise and experience profiles of the Board members. In addition, it made recommendations regarding appointments to Board committees.

Summary of the assessment of Board performance: In accordance with the *Hydro-Québec Act*, in 2008 the Governance and Ethics Committee assessed the performance of the Board of Directors. The directors completed a questionnaire based on the assessment criteria approved by the Board, to whom the results were submitted. Thereafter, an action plan was developed in light of the comments received, and all recommendations in the action plan were implemented. Thus, at each meeting of the Board, the President and Chief Executive Officer informs the directors of changes in the business and economic context in which Hydro-Québec operates, thereby allowing them to gauge the various challenges faced by the company against the objectives set out in the Strategic Plan. The President and Chief Executive Officer also reports on the principal risks faced by the company.

Audit Committee (C)

Mandate: The Audit Committee's role is to make recommendations to the Board of Directors on the approval of the financial statements of Hydro-Québec and of its pension plan. It ensures that the financial statements accurately reflect the financial positions and changes therein, and that internal controls are adequate and effective. It is also responsible for issuing an opinion prior to the Board's approval of the annual internal audit plan, supervising internal audit activities, ensuring that the company has a plan to optimize the use of its resources and monitoring this plan. The Audit Committee also makes recommendations to the Board on the external auditors' fees and meets periodically with the external auditors. In addition, it examines the integrated enterprise risk management process. It can also act as the audit committee of any of the company's wholly owned subsidiaries. The Audit Committee is composed solely of independent directors who have the necessary expertise for the performance of its mandate. It is chaired by Jacques Leblanc.

Activities: The Audit Committee held seven meetings in 2008. As part of its recurring deliberations, the committee ensured the independence of the external auditors. It also examined internal and external audit results and internal audit reports on control and optimization of the company's operations and resources as well as management of the related risks. It examined the quarterly and annual financial statements of Hydro-Québec and the annual financial statements of its pension plan, of Hydro-Québec International and of Société d'énergie de la Baie James. The committee also monitored progress in Hydro-Québec's migration to the International Financial Reporting Standards and received the report on the project to attest to the effectiveness of internal controls related to financial information. Moreover, it examined the company's 2009 internal audit plan and recommended its approval by the Board. The plan addresses the effectiveness, efficiency and profitability of operations; the reliability, integrity and availability of financial and operational information; the protection of assets; and compliance with the laws, regulations and other rules that govern the company. It specifically targets the optimization of the company's resources and the tracking of performance indicators.

Human Resources (D)

Mandate: The Human Resources Committee is responsible for establishing human resources policies as well as standards and rate scales applicable to the compensation of senior executives and employees of the company and its wholly owned subsidiaries. It is also responsible for developing the expertise and experience profile to be used in selecting the President and Chief Executive Officer and for proposing a candidate for that position to the Board of Directors, which will then make a recommendation to the government of Québec. In addition, it develops and suggests criteria for assessing the performance of the President and Chief Executive Officer and makes recommendations to the Board regarding his compensation. It also participates in selecting the senior executives of the company and its subsidiaries and in developing a succession plan. The committee is chaired by Marie-France Poulin.

Activities: In 2008, the Human Resources Committee held seven meetings, including a joint meeting with the Finance Committee to examine Hydro-Québec's Business Plan, objectives and corporate risk management. It evaluated whether or not the company had met its annual performance objectives, examined the overall compensation of its employees, executives and President and Chief Executive Officer and of the employees and senior executives of its wholly owned subsidiaries and recommended that the Board approve the negotiation mandate that led to the renewal of seven collective agreements. It also proposed to the Board, for approval by the government, the updating of the bylaws governing Hydro-Québec's pension plan. In addition, it closely monitored the succession plan for Senior Management. Finally, it examined the *Report of Activities of the Corporate Ombudsman 2007* and analyzed the results of the 2008 employee survey on job satisfaction and employee motivation.

Finance (E)

Mandate: The role of the Finance Committee is to advise the Board on Hydro-Québec's directions, policies, strategies and overall objectives related to financing, borrowing, insurance, banking, risk management, and any other subject concerning the company's finances. In addition, every year, it examines the company's consolidated portfolio of internal and external risks. The committee is chaired by Michel Plessis-Bélair.

Activities: In 2008, the committee held four meetings, including a joint meeting with the Human Resources Committee for the purpose of analyzing the company's Business Plan, objectives and corporate risk management. It also examined various annual programs (borrowing, guarantee, financial risk management, swap and sinking fund) before recommending their approval by the Board, and it reviewed financial tracking reports on capital projects worth more than $50 million.

Environment and Public Affairs (F)

Mandate: The role of the Environment and Public Affairs Committee is to provide opinions and make recommendations to the Board of Directors on environmental management and compliance; integration of sustainable development principles; environmental incident reports and related claims, opinions, investigations and legal proceedings; public health and safety; community relations; the company's social responsibility and its contribution to the community; and its public image. The committee is chaired by Gaston Blackburn.

Activities: The Environment and Public Affairs Committee met three times in 2008. It examined environmental issues and considered requests for donations and sponsorships. It studied the summary of environmental management assessments carried out by the President and Chief Executive Officer as well as the annual report on environmental compliance and legislation, the *Sustainability Report 2007* and the *Annual Report 2007* of the Fondation Hydro-Québec pour l'environnement. It also examined the 2007 regional profile of Hydro-Québec's activities and prepared a report on contributions to university research chairs in 2007. In addition, the committee reviewed the annual activity reports of the liaison committees established by the company with groups representing Québec agricultural producers and municipalities.

Pension Plan Financial Management (G)

Mandate: The role of the Pension Plan Financial Management Committee is to advise the Board on the directions, policies, strategies and overall objectives established by Hydro-Québec for its pension plan: the Pension Plan Funding Policy, the Pension Fund Investment Management Policy, actuarial valuations of the plan, choice of the benchmark portfolio, the plan's financial situation and plan expenses. It also expresses its opinion on any other aspect of pension fund management. The committee is chaired by Louis Lagassé.

Activities: In 2008, the committee met four times. It recommended that the Board approve the annual pension fund management and pension plan administration budgets, updating of the Pension Fund Investment Management Policy, the actuarial valuation for purposes of pension plan funding and solvency, and the reappointment of the actuary for the next annual valuation. It also examined the process for analyzing, approving and managing the company's real estate investments and reviewed the performance of the pension plan portfolio and specialized portfolio managers. Finally, it closely monitored the pension plan's position and made recommendations to the Board on employer contributions to the pension fund.

Corporate Governance

Guide Mathieu Ouellet welcomes a visitor.

Hydro-Québec's Board of Directors complies with the requirements of corporate governance legislation applicable to state-owned enterprises. It also follows the guidelines of the Canadian Securities Administrators applicable to state-owned enterprises, even though it is not legally bound to do so because Hydro-Québec is not publicly traded.

Independence

A total of 14 of the 16 directors of Hydro-Québec, including the Chairman of the Board, are independent directors, that is, they have no direct or indirect relationships or interests, for example of a financial, commercial, professional or philanthropic nature, which are likely to interfere with the quality of their decisions as regards the interests of the company. The two Board members who are not independent are Thierry Vandal, the company's President and Chief Executive Officer, and Normand Bergeron, Deputy Minister of Natural Resources and Wildlife.

The Québec government appoints the members of the Board based on the expertise and experience profiles established by the company. Directors are appointed for a term of up to four years and the Chairman for a term of up to five years; they may be reappointed twice, successively or not.

The Board is responsible for compliance with the rules set out in the *Code of Ethics and Rules of Professional Conduct for Directors, Executives and Controllers of Hydro-Québec*, which are based on the *Regulation respecting the ethics and professional conduct of public office holders*.

Compensation and other benefits paid to directors

Compensation for all independent directors, except the Chairman, is set out in Order in Council No. 610-2006. Compensation consists of a basic annual retainer of $16,646, plus a meeting fee of $780 for each Board or committee meeting. A yearly supplement of $5,202 is paid to the chairs of Board committees. Pursuant to Order in Council No. 1099-2005, the Chairman of the Board receives annual compensation of $125,000. Board members are also entitled to reimbursement of travel expenses incurred in the performance of their duties.

Director induction and training program

When Board members are first appointed, they receive training on their roles and responsibilities as well as the nature and business context of Hydro-Québec's principal activities. Board members are also informed about the company's legal and regulatory context, with particular emphasis on the governance of a government-owned utility. They are given documents designed to help them perform their functions. Board committee members also receive documents regarding the mandate of their committee and the matters it handles. The director induction and training program also includes presentations on major issues and projects, as well as tours of the company's facilities. In 2008, Board members visited the telecommunications control centre, IREQ (Hydro-Québec's research institute), the Robert-Bourassa and La Grande-1 hydroelectric developments and the Eastmain-1-A/Sarcelle/Rupert construction site. External training programs are also available to complement directors' knowledge.

Deintegration

In 1997, Hydro-Québec implemented an organizational structure that allows some units to work independently from each other while remaining part of the same company. This is the principle of deintegration, or unbundling.

The operations of these units are subject to set rules of conduct and ethics. The Distributor's electricity procurement process is governed by the *Code of Ethics on Conducting Calls for Tenders*, which was approved by the Board of Directors and the Régie de l'énergie. The code ensures that calls for tenders are conducted fairly for all electricity suppliers. The Régie follows up annually on its application. Moreover, the Régie de l'énergie approved the *Code de conduite du Distributeur* (Distributor Code of Conduct) in March 2006. This code applies to transactions between

Mérite du français 2008, catégorie Langue du travail – Administration, from the Office québécois de la langue française. Johanne Charland, Hélène Michon, Michelle Dyke and Hélène Pelletier, from the Direction principale de l'environnement et des affaires corporatives.

At the head office, guide Geneviève Lafortune explains the environmental issues related to power generation in North America.

the Distributor and the Generator for procurement not subject to the tendering process. It also governs dealings between the Distributor and its affiliates, with the aim of preventing affiliates' business operations from being financed, in whole or in part, by electricity service customers. The Distributor provides details on the application of the code in its annual report to the Régie. The code is available for consultation, in French only, on the company's Web site.

Hydro-Québec TransÉnergie is subject to the *Transmission Provider Code of Conduct* approved by the Régie in 2004. This code governs relations between the Transmission Provider and Hydro-Québec affiliates, and its purpose is to prevent any form of preferential treatment or cross-subsidization. The information that must be made public pursuant to the *Transmission Provider Code of Conduct* is published on the OASIS (Open Access Same-Time Information System) Web site at **www.transenergie.com/oasis/hqt/en/entree.htmlx**. The OASIS Web site includes information on staff transfers and on violations of the code deemed likely to confer a business advantage on certain clients of the transmission service. It is possible to consult this information by simply registering as a guest on the OASIS Web site.

The *Reliability Coordinator Code of Conduct*, which was approved by the Régie de l'énergie in December 2007 after Hydro-Québec TransÉnergie's Direction du contrôle des mouvements d'énergie (System Control) was designated as Reliability Coordinator for Québec, came into force in January 2008. Its purpose is to ensure that the reliability of the transmission system remains a top priority and to prohibit any form of preferential treatment in favor of other branches of the Transmission Provider, its affiliates or other system users.

Internal control system

The company's Management maintains an internal control system that meets the demanding requirements of the internationally recognized framework developed by the Committee of Sponsoring Organizations (COSO) of the Treadway Commission. This includes communicating Hydro-Québec's code of ethics and code of conduct to employees, primarily to ensure the proper management of resources and the orderly conduct of business. The objective of this system is to provide reasonable assurance that financial information is relevant and reliable and that Hydro-Québec's assets are appropriately recorded and safeguarded. The system includes an enterprise risk management process. The internal audit helps to determine whether the internal control system is sufficient and effective and to assess the company's policies and procedures. It includes a performance audit to ensure the efficiency, effectiveness and cost-effectiveness of operations. The internal auditor and the external auditors have full and unrestricted access to the Audit Committee, without Management present.

Directors' Compensation and Benefits in 2008

	Base compensation[a, b]	Meeting fees[b]	Benefits[c]
Michael L. Turcotte[d]	$125,000	–	$59
Thierry Vandal[e]	–	–	–
Normand Bergeron[e]	–	–	$3,193
Gaston Blackburn	$12,714	$10,635	$3,193
Anik Brochu	$16,791	$9,870	$64
Carl Cassista	$16,635	$11,715	$4,014
Hélène F. Fortin	$11,989	$10,860	$2,853
Bernard Gaudreault	$16,791	$13,890	$3,193
Suzanne Gouin	$16,635	$8,940	$64
Louis Lagassé	$22,038	$11,528	$3,193
Jacques Leblanc	$22,038	$20,175	$3,193
Nathalie Le Prohon	$16,635	$10,935	$64
Michel Plessis-Bélair	$22,038	$15,323	$64
Marie-France Poulin	$22,038	$18,608	$64
Marie-Anne Tawil	$16,791	$17,453	$4,014
Emmanuel Triassi	$16,635	$12,090	$4,014
Gilles Vaillancourt	$16,635	$9,000	$3,193

a) Pursuant to Orders in Council Nos. 1099-2005 and 610-2006.
b) Includes indexing from April 1, 2007.
c) Insurance premiums paid by Hydro-Québec.
d) Michael Turcotte also receives a car allowance of $15,120.
e) Thierry Vandal, President and Chief Executive Officer, and Normand Bergeron, Deputy Minister of Natural Resources and Wildlife, may not receive compensation as members of Hydro-Québec's Board of Directors.

Policy on the independence of external auditors

Hydro-Québec has introduced various mechanisms to enable the Audit Committee to ensure that external auditors remain independent:

- A process whereby any assignment to be given to external auditors is analyzed first to prevent any interference with their independence; external auditors are not authorized to provide services that fall within the prohibited category
- Rules requiring prior approval of all requisitions for services sent to the external auditors
- Reports to the Audit Committee on the fees billed by the external auditors

External auditors' fees

KPMG LLP and Ernst & Young LLP are the joint auditors for Hydro-Québec for 2008. Professional fees billed by the external auditors in 2008 for services other than auditing and certification amounted to 3.8% of the total $5.0 million in fees billed.

Access to documents and protection of personal information

Hydro-Québec carefully protects the personal information of its customers, suppliers and employees and respects the public's right of access to information. It takes all the necessary measures to comply with the *Act respecting Access to documents held by public bodies and the Protection of personal information*, or the "Access Act."

In 2008, models of the personal information files collected by Hydro-Québec were updated and published on the company's Web site. The register recording the release of personal information was also updated.

To facilitate access to information, Hydro-Québec publishes many documents on its Web site at **www.hydroquebec.com/publications/en** in accordance with the *Regulation respecting the distribution of information and the protection of personal information*. Moreover, it provides explanations regarding access to documents and the protection of personal information at **www.hydroquebec.com/publications/en/others/acces_information.html**, including an explanation of the procedure for requesting access to a document.

In 2008, Hydro-Québec received 253 requests for access to information under the Access Act, all of which were processed within the prescribed time limit. Applicants either were looking for documents (such as corporate reports and contracts) or wanted to know what personal information the company held about them. Of these requests, 132 were granted in full, 83 were granted in part and 38 were denied. Request denials were due mainly to security issues, to opposition by a third party to the disclosure of information belonging to it, or to the commercial nature of the documents requested.

Ethics

Hydro-Québec attaches great importance to ethics in all aspects of its activities. The concept of ethics has been included in official company guidelines since 1988, with the aim of setting high standards of judgment and behavior in professional activities.

As a government-owned utility, Hydro-Québec must demonstrate exemplary probity, and it can do so only with the consistent support of its employees. Loyalty, integrity, respect, discretion and fairness are fundamental values reflecting Hydro-Québec's social commitment to its customers and the community. Ethical standards and rules resulting from these values are set out in the *Code of Ethics and Rules of Professional Conduct for Directors, Executives and Controllers of Hydro-Québec* (see page 120 of this Annual Report) and in the *Code of Conduct* for employees. This document, which is available at **www.hydroquebec.com/profile/**, has a twofold purpose: facilitate an understanding of the ethical principles set out in the policy Our Management and approved by the Board of Directors, and help all employees perform their duties in keeping with Hydro-Québec's values.

Language guidelines

In 2008, Hydro-Québec continued its efforts to maintain the quality of the French used within the company. Various proficiency courses (grammar, business correspondence and specialized writing) were offered to employees, six terminology bulletins were published on the intranet and a telecommunications vocabulary was developed. In addition, various promotional and awareness activities were organized to highlight Francofête, a celebration of French language and culture. Moreover, Hydro-Québec's standing committee on language met twice during the year.

Sustainable development

Published concurrently with this Annual Report, the *Sustainability Report 2008* discusses the company's main sustainable development initiatives, the progress made in this area and the company's sustainable energy choices. The report is based on the *Global Reporting Initiative Guidelines*. It is published at **www.hydroquebec.com/sustainable-development**, where additional information is provided on the company's performance in sustainable development.

Compensation and Other Benefits Paid to the Company's Five Most Highly Compensated Officers in 2008

				Automobile		Life insurance and health insurance premiums paid by Hydro-Québec[b]
	Base compensation	Variable compensation	Perquisites used[a]	Description of benefit	Operating cost	
Vandal, Thierry President and Chief Executive Officer	$417,321	$122,211	$12,778	Executive vehicle	$1,744	$4,342
	Pension Plan and Supplementary Benefits Program					
	Basic Hydro-Québec Pension Plan (HQPP) - Usual contribution under the plan - Pension calculated in accordance with usual plan provisions **Supplementary Benefits Program** - Same terms as for senior executives (see below) *plus* - Pension calculated on the basis of average salary for the best three years (less pension payable under the HQPP) - Credit of 3.5% per contribution year (less pension credit under the HQPP) - Recognition of two years for each year of participation - Recognition of 100% of the maximum bonus as eligible salary (less portion of bonus recognized under the HQPP) - Pension limited to 70% of the average base salary and variable compensation for the best three years					
Boulanger, André President, Hydro-Québec Distribution	$361,075	$105,740	$4,953	Car allowance or vehicle, plus parking	$17,995	$5,696
Cacchione, Richard President, Hydro-Québec Production	$360,851	$101,837	$5,000		$11,462	$5,024
Courville, Isabelle President, Hydro-Québec TransÉnergie	$349,423	$84,728	$5,000		$16,500	–
Saheb, Élie Executive Vice President, Technology	$344,443	$96,664	$2,790		$5,474	$21,234
	Pension Plan and Supplementary Benefits Program					
	Basic Hydro-Québec Pension Plan (HQPP) - Usual contribution under the plan - Pension calculated on the basis of average salary for the best five years - Credit of 2.25% per contribution year - Recognition of 66.67% of the maximum bonus as salary for purposes of the HQPP **Supplementary Benefits Program** - Contribution assumed by Hydro-Québec - Additional benefits to offset the tax limits under the HQPP (lifting of ceiling on the permitted maximum amount) - Payment of benefits according to the same terms as those applicable under the HQPP					

a) Health assessment, financial and succession planning, sports clubs, professional memberships.

b) Applicable to officers who participate in the plans.

Compensation and Other Benefits Paid to the Only Officer Compensated by One of the Company's Wholly Owned Subsidiaries in 2008

	Base compensation	Variable compensation	Perquisites used[a]	Employee benefits
Girouard, Yves General Manager, Cedars Rapids Transmission Company, Limited	$114,408	$15,194	$2,000	Hydro-Québec Pension Plan and group insurance plans

a) Financial and succession planning, sports clubs, public transit passes.

Code of Ethics and Rules of Professional Conduct

for Directors, Executives and Controllers of Hydro-Québec

Part I – Interpretation and application

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

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

b) **"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 in Schedule D;

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

d) **"Board"** means the Board of Directors of the Company;

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) **"controller"** means the controller of the Company and the controllers of divisions or groups or units reporting to the President and Chief Executive Officer of the Company;

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

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 Company or a non-profit association or group that has no financial link with the Company or is not incompatible with the objects of the Company;

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

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

l) **"subsidiary"** means a legal person or company controlled directly or indirectly by the Company;

m) **"Regulation"** means the *Regulation respecting the ethics and professional conduct of public office holders* (Order-in-Council 824-98 of June 17, 1998 (1998) 130 G.O. II., 3474, pursuant to sections 3.01 and 3.02 of the *Act respecting the Ministère du Conseil exécutif,* R.S.Q., c. M-30), as amended from time to time;

n) **"Company"** means Hydro-Québec.

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, the President and Chief Executive Officer, other executives of the Company and its controllers.

The directors and the President and Chief Executive Officer are also subject to the Regulation.

Part II – Ethical principles and general rules of professional conduct

3. The director, executive or controller is appointed to contribute to the achievement of the Company's mission 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 Company by law and the good administration of the property it owns as mandatary of the State.

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

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

- a vision of the Company 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 Company as a government-owned business company, which include customer satisfaction, a "business first" approach, respect for employees, quality improvement, respect for the environment, partnership with local communities and safeguarding the future; and
- the principles set out in the basic policies of the Company, 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, executive or controller is required, in the performance of his duties, to respect the ethical principles and rules of professional conduct provided by law, the Regulation as applicable, and those defined in this Code. In case of discrepancy, the more stringent rules and principles apply.

When in doubt, act according to the spirit of these principles and rules.

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

4. The director, executive or controller shall not merge the assets of the Company with his own; he may not use the assets of the Company 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, executive or controller has ceased to hold his position.

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

5.1 The director, executive or controller 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, executive or controller shall make decisions without regard for any partisan political considerations.

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

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

6.2 The director, executive or controller 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, executive or controller may not, in the performance of his duties, deal with a person who has ceased to be a director, executive or controller of the Company 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 Company is a party and about which he has information not available to the public.

7.2 After ceasing his duties, no director, executive or controller may disclose confidential information he has obtained or give anyone advice based on information not available to the public concerning the Company 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 Company is a party and about which he has information not available to the public.

8. The director, executive or controller 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 The director, executive or controller who intends to be a candidate for elective 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 Conseil exécutif.

Part III – Duties and obligations of directors, executives and controllers with respect to conflicts of interest

Prevention of conflicts of interest

9. The director, executive or controller 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 Company 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 Company, 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 Company.

   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, executive or controller of the Company who serves as director, executive or controller 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 this director, executive or controller works full-time for the enterprise and the profit-sharing program is closely linked with the individual performance of the director, executive or controller 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, executive or controller who:

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

   b) has a direct or indirect interest in an enterprise that is a party to a contract with the Company or a subsidiary or is a director, executive, controller 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 any information of any kind to any employee, controller, executive or director of the Company 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.

12.1 A director who is a member of the Audit Committee of the Board of Directors may not have an interest in the Company or a subsidiary. In particular, he may not accept from the Company or a subsidiary fees with respect to consulting, consulting services or any other similar service.

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 or controller 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; or

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

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

15. The director, executive or controller 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 Company, 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, executive or controller.

17. The director, executive or controller shall notify the Chairman of the Board in writing of the rights he may invoke against the Company, 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, executive or controller 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 B and containing the following information:

a) the name of any enterprise in which the director, executive or controller 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, executive or controller.

A director, executive or controller 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, executive or controller 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 Company, who keeps them at the disposal of the members of the Board and the Ethics and Corporate Governance Committee.

Moreover, the Secretary of the Company 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, executive or controller in a conflict of interest;

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

c) to owning interests through a blind trust whose beneficiary cannot know its makeup;

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, executive or controller operates;

f) to a directors' liability insurance agreement; or

g) to the owning of shares issued or guaranteed by the Company, 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, executive or controller shall submit to the Chairman of the Board and the Secretary of the Company the attestation appearing in Schedule C.

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

Part IV – Remuneration

20.2 The director, executive or controller, 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 Company.

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

20.4 A director, executive or controller 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, executive or controller 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, executive or controller 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, executive or controller is not covered by sections 20.4 to 20.6.

20.8 For the application of sections 20.4 to 20.6, "public sector" means the bodies, institutions and companies referred to in the Regulation in Schedule A.

The period covered by the severance allowance or payment referred to in 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 salary in his prior 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 Company appointed by the Government.

The Chairman of the Board is the competent authority with respect to all directors of wholly owned subsidiaries, executives or controllers of the Company.

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

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, executive or controller 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, executive or controller 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 to directors, executives or controllers 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, executive or controller who is accused of violations of ethics or the rules of professional conduct.

24. The Secretary of the Company 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, executives and controllers 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, executive or controller 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, executive or controller 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 or this Code has been violated, the competent authority may impose either of the following penalties:

a) for an executive or a controller, 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 Conseil exécutif. 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 Conseil exécutif 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, executive or controller shall render an account and restore to the Company 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.

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

Generating and Transmission Facilities

as at December 31, 2008

Generation Installed capacity in MW

Hydroelectric generating stations
34,118 MW

The installed capacity of a hydroelectric generating station is equivalent to that of its generating units operating in winter conditions (water temperature 5°C).

Robert-Bourassa	5,616
La Grande-4	2,779
La Grande-3	2,417
La Grande-2-A	2,106
Beauharnois	1,903
Manic-5	1,596
La Grande-1	1,436
Manic-3	1,244
Bersimis-1	1,178
Manic-2	1,123
Manic-5-PA	1,064
Outardes-3	1,026
Sainte-Marguerite-3	884
Laforge-1	878
Bersimis-2	869
Outardes-4	763
Carillon	753
Toulnustouc	526
Outardes-2	523
Eastmain-1	507
Brisay	469
Péribonka	405
Laforge-2	319
Trenche	302
La Tuque	294
Beaumont	270
Rocher-de-Grand-Mère	230
Rapide-Blanc	204
Paugan	204
Shawinigan-2	200
Shawinigan-3	194
Manic-1	184
Rapides-des-Îles	176
Chelsea	152
La Gabelle	131
Première-Chute	131
Les Cèdres	122
Rapides-Farmer	104
Rapides-des-Quinze	103
Other (20 generating stations rated less than 100 MW)	733

Nuclear generating station
675 MW

Gentilly-2	675

Thermal generating stations
1,634 MW

Tracy (steam)	660
Bécancour, La Citière and Cadillac (gas turbine)	852
Other (23 diesel plants)	122

Wind farm
2 MW

Saint-Ulric (3 wind turbines)	2

Hydroelectric generating stations under construction
1,012 MW

Chute-Allard and Rapides-des-Cœurs (8 remaining units)	94
Eastmain-1-A and Sarcelle	918

Installed capacity of Hydro Québec's generating fleet
36,429 MW

Hydroelectric (59)	**34,118**
Nuclear (1)	**675**
Thermal (27)	**1,634**
Wind (1)	**2**

Other sources of supply
7,235 MW

Churchill Falls generating station [Churchill Falls (Labrador) Corporation Limited][a]	**5,428**
Eight privately owned wind farms[b]	**530**
Agreements with other independent power producers[c]	**1,277**

a) Hydro-Québec has access to almost all the output.
b) Hydro-Québec purchases all the output.
c) Hydro-Québec has access to this output.

Transmission

Voltage	Lines (km)	Substations (number)
765 and 735 kV	11,422	38
450 kV dc	1,218	2
315 kV	5,127	63
230 kV	3,048	50
161 kV	2,013	40
120 kV	6,624	214
69 kV or less	3,606	103
Total	**33,058**	**510**

Major Facilities

Other Information

To contact us

HYDRO-QUÉBEC
75 René-Lévesque Blvd. West
20th floor
Montréal, Québec H2Z 1A4
CANADA
Telephone: 514 289-2211

INVESTOR RELATIONS
75 René-Lévesque Blvd. West
6th floor
Montréal, Québec H2Z 1A4
CANADA
Telephone: 514 289-2518
E-mail: rel.inv@hydro.qc.ca

Units of measure

¢/kWh	cents ($0.01) per kilowatthour
$M	millions of dollars
$B	billions of dollars
kV	kilovolt (one thousand volts)
kW	kilowatt (one thousand watts)
MW	megawatt (one million watts)
GW	gigawatt (one million kilowatts)
kWh	kilowatthour (one thousand watthours)
MWh	megawatthour (one million watthours)
GWh	gigawatthour (one million kilowatthours)
TWh	terawatthour (one billion kilowatthours)
km	kilometre

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

Annual Report 2008 (this document)

Sustainability Report 2008

Financial Profile 2008–2009

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