



Management's Discussion and Analysis

The Management's Discussion and Analysis highlights the primary factors that impacted the operations and financial results of SaskEnergy Incorporated (SaskEnergy or the Corporation) and its wholly owned subsidiaries for the nine month period ended September 30, 2008. This discussion should be read in conjunction with the consolidated interim financial statements and accompanying notes. For additional information relative to its operations and financial position, refer to the Corporation's Annual Report for the year ended December 31, 2007.

The volume of natural gas distributed is sensitive to variations in the weather, particularly through the prime heating season of November to March. Therefore, the consolidated interim financial results should not be taken as indicative of the performance to be expected for the full year due to the seasonal nature of the natural gas utility business in Saskatchewan.

The following discussion contains certain forward-looking statements that are subject to inherent uncertainties and risks. The significant uncertainties and risks of the Corporation include natural gas price, winter weather, operational, regulatory and counterparty credit risks. Consequently, actual results and events may vary significantly from those included in, contemplated or implied by such statements.

Corporate Profile

SaskEnergy has the legislated franchise for the distribution and transmission of natural gas within Saskatchewan. The distribution system delivers natural gas to over 336,000 residential, farm, commercial and industrial customers over a 66,000 kilometre pipeline distribution system. The transmission system provides transportation and storage services to the distribution utility, producers, marketers and large volume end-use customers within Saskatchewan.

SaskEnergy has seven wholly owned subsidiaries:

- TransGas Limited – owns natural gas transportation and storage facilities;
- Many Islands Pipe Lines (Canada) Limited – transports natural gas to and from other jurisdictions and is regulated by the National Energy Board;
- Bayhurst Gas Limited – owns, produces and sells natural gas from storage-related assets and holds natural gas royalty interests;
- Bayhurst Energy Services Corporation – a wholly owned subsidiary of Bayhurst Gas Limited operates as an energy services company;
- SaskEnergy International Incorporated – holds international equity investments;
- Swan Valley Gas Corporation – owns a natural gas distribution utility in the Swan Valley area of western Manitoba;
- Saskatchewan First Call Corporation – operates an underground infrastructure facility database through which subscribing companies are alerted of the need to perform line locates for landowners or contractors planning to excavate in Saskatchewan;
- SaskEnergy Nova Scotia Holdings Ltd. – holds SaskEnergy's interest in a natural gas distribution utility in Nova Scotia.

Financial and Operating Highlights

| | Three months ended September 30 | | Nine months ended September 30 | |
|--|------------------------------------|------------|-----------------------------------|-----------|
| Financial Highlights | 2008 | 2007 | 2008 | 2007 |
| (\$ millions) | | | | |
| Consolidated Net Income (Loss) before the Impacts of Fair Value | (15) | 7 | 25 | 45 |
| Fair Value Adjustments | (50) | (13) | (16) | 2 |
| Consolidated Net Income | (65) | (6) | 9 | 47 |
| Total Assets | | | 1,475 | 1,345 |
| Long-term Debt | | | 633 | 708 |
| Operating Highlights | | | | |
| Distribution | | | | |
| Volumes Distributed - Petajoules | 19 | 20 | 95 | 92 |
| Winter Weather - Compared to the 30 Year Average | N/A | N/A | 6% Colder | Normal |
| Transmission | | | | |
| Volumes Transported - Petajoules | 59 | 75 | 215 | 244 |
| Peak Day Natural Gas Flows (Winter) - Petajoules | N/A | N/A | 1.50 | 1.49 |
| Date of Peak Flow | N/A | N/A | Jan 28 | Feb 14 |

Financial Results

Effective January 1, 2008, SaskEnergy adopted the new Canadian Institute of Chartered Accountants (CICA) Handbook Section 1535 - Capital Disclosures, Section 3031 - Inventories, Section 3862 - Financial Instruments - Disclosure, and Section 3863 - Financial Instruments - Presentation. These changes in accounting policies are discussed in Note 2 of the attached financial statements.

Effective January 1, 2011, publicly accountable Canadian entities will be required to prepare financial information in accordance with International Financial Reporting Standards (IFRS). IFRS, like current Canadian generally accepted accounting principles (GAAP), are a principle based set of standards. However, there are areas where the accounting treatment differs from Canadian GAAP. SaskEnergy is currently evaluating IFRS to determine which areas of the Corporation's financial reporting will be impacted. In conjunction with evaluating the accounting standards, a review of the information technology and data systems' capability to provide the information required by IFRS will be performed. SaskEnergy is currently engaged in educational activities to expand its knowledge of IFRS. The Corporation has retained a service provider to provide expertise in the implementation of IFRS.

Subsequent to the third quarter, SaskEnergy received approval for changes to the commodity and delivery rates. Effective October 1, 2008 the commodity rate for natural gas increased from \$6.57 per Gigajoule (GJ) to \$8.51 per GJ. Effective November 1, 2008 the delivery rate charged to SaskEnergy customers increased. The Basic Monthly Charge increased \$2.00 per month for residential customers and \$2.55 per month for farm customers, with modest increases for other customer classes. These approved rate increases, when combined, represents an average bill increase of about 22% for residential customers.

Consolidated Net Income

For the first nine months of 2008 consolidated net income was \$9 million, which was \$38 million lower than the \$47 million net income for the same period in 2007. Margins on gas marketing sales were lower in 2008 and there were unfavourable fair value adjustments of \$16 million, compared to favourable fair value adjustments of \$2 million for the same period in 2007.

1. Commodity

(a) Commodity Sales

The commodity rate for natural gas sales to distribution utility customers was \$6.57 per GJ for the period January 1, 2008 to September 30, 2008. In 2007 the commodity rate was \$7.17 per GJ for this period. This resulted in lower average revenue per GJ for the first nine months of 2008 compared to 2007.

The lower average revenue per GJ was partially offset by 6% colder weather in the first nine months of 2008 compared to normal weather during the same period in 2007. The colder weather in 2008 increased the amount of natural gas consumed for space heating purposes by 2.6 Petajoules in 2008 compared to 2007.

(b) Commodity Cost of Gas Sold

The cost of gas sold includes the cost of purchased gas and adjustments that effectively record the change in fair value of natural gas contracts (fair value adjustments) as at September 30. The financial and derivative instruments reported on the Statement of Financial Position are reported at fair value. The change in fair value of financial and derivative instruments from one reporting period to another are reported as fair value adjustments and either increase or decrease net income.

The fair value adjustments unfavourably impacted the financial reporting of the cost of gas sold during the first nine months of 2008 by \$28 million. Therefore, the \$27 million loss on commodity sales for the first nine months of 2008 was primarily due to the fair value adjustments on natural gas contracts. The \$6 million loss on commodity sales during the first nine months of 2007 was primarily due to \$6 million in unfavourable fair value adjustments.

The effect of unfavourable fair value adjustments of \$123 million was the cause of a \$125 million loss on commodity sales in the third quarter of 2008 compared to unfavourable fair value adjustments of \$10 million resulting in a \$12 million loss on commodity sales in the third quarter of 2007.

2. Gas Marketing

In order to maximize the utilization of its assets during off-peak periods, SaskEnergy purchases and sells natural gas in the open market to earn a margin. SaskEnergy also competes to supply natural gas to larger end-use customers in Saskatchewan through non-regulated contract sales.

The Corporation owns underground natural gas storage facilities that are no longer used in commercial storage operations. The natural gas from these facilities is being removed and sold in the open market.

In the first nine months of 2008, the realized margin from the foregoing activity was \$6 million. The margin from gas marketing activities was favourably impacted for financial reporting purposes by the fair value adjustments of \$13 million. This compared to a realized margin of \$31 million and a favourable fair value adjustment of \$9 million for the same period in 2007.

In the three month period ended September 30, 2008, the realized loss from the foregoing activity was \$3 million. The margin from gas marketing activities was favourably impacted for financial reporting purposes by the fair value adjustment of \$74 million. This compared to a realized margin of \$14 million and an unfavourable fair value adjustment of \$3 million for the same period in 2007.

3. Delivery Revenue

Delivery revenue in the first nine months of 2008 was \$123 million, which was \$11 million higher than the same period in 2007. This was a result of higher delivery rates, more customers and increased natural gas consumption in 2008 reflecting the colder weather in 2008 compared to 2007.

For the three month period ended September 30, 2008, delivery revenue of \$24 million was consistent with the same period in 2007.

Effective June 1, 2007 the delivery rate charged to SaskEnergy customers increased for the first time in ten years. As a result, the delivery rate charged to distribution utility customers was 5.7% higher for the period January 1, 2008 to May 31, 2008 as compared to the same period in 2007.

The majority of SaskEnergy's distribution customers consume natural gas for heating purposes and, as a result, the volume of natural gas distributed is sensitive to variations in weather, particularly through the November-to-March prime heating load season. The weather from January 1 to September 30, 2008 was 6% colder than the same period in 2007.

4. Transportation and Storage Revenue

Transportation and storage revenue for the first nine months of 2008 was \$57 million, which was \$5 million lower than the same period in 2007. The number of natural gas wells drilled in Saskatchewan declined in both 2007 and 2008 which contributed to lower volumes of natural gas transported in the first nine months of 2008.

Transportation and storage revenue of \$18 million for the three month period ended September 30, 2008 was \$3 million lower than the same period in 2007 due to lower volumes transported.

5. Other Expenses

Expenses (excluding cost of gas sold) to September 30, 2008 were \$193 million, which was \$5 million higher than the first nine months of 2007. For the three month period ended September 30, 2008 total expenses (excluding cost of gas) were \$60 million or \$4 million higher than the same period in 2007.

Operating and maintenance expenses for the first nine months of 2008 were \$99 million, which was \$6 million higher compared to the first nine months of 2007 primarily due to increased labour costs. For the third quarter ended September 30, 2008 the operating and maintenance expenses of \$32 million were \$4 million higher than the same period in 2007 primarily due to higher labour, contracts and consulting costs.

Interest expense, amortization, payments to municipalities and Saskatchewan taxes to September 30, 2008 and for the three months ended September 30, 2008 were consistent with the same periods in 2007.

Outlook

The Corporation's consolidated net income target for 2008 is \$64 million. Consolidated net income (excluding fair value adjustments) was favourable compared to target for the first nine months of 2008, and SaskEnergy expects net income for 2008 will approximate the target.

Net income expectations include the impact of SaskEnergy's approved average delivery rate increase of 5.8% effective November 1, 2008. The forecast for delivery revenue also assumes normal weather patterns for the remainder of the year. An anticipated decrease of natural gas volumes transported as a result of continued decline in Saskatchewan drilling by producers will reduce transportation revenue.

Results are subject to a number of risks, primarily fluctuations in natural gas prices for purchases of natural gas for the distribution utility customers and variations in winter weather.

SaskEnergy Incorporated
Consolidated Statement of Financial Position
(millions)

| | As at September 30, 2008 <i>(unaudited)</i> (Note 2) | As at December 31, 2007 <i>(audited)</i> |
|---|---|--|
| Assets | | |
| Current assets | | |
| Cash | \$ 16 | \$ 2 |
| Accounts receivable | 52 | 131 |
| Natural gas in storage held for resale | 233 | 149 |
| Inventories of supplies | 11 | 13 |
| Debt retirement funds | - | 3 |
| Fair value of derivative instruments | 41 | 26 |
| | <u>353</u> | <u>324</u> |
| Property, plant and equipment (net) | 1,002 | 978 |
| Natural gas in storage held for resale and operations | 36 | 36 |
| Debt retirement funds | 45 | 40 |
| Investments and other assets | 39 | 33 |
| | <u>\$ 1,475</u> | <u>\$ 1,411</u> |
| Liabilities and Province's Equity | | |
| Current liabilities | | |
| Short-term debt | \$ 242 | \$ 88 |
| Accounts payable | 111 | 144 |
| Dividends payable | 24 | 7 |
| Current portion of long-term debt | 10 | 75 |
| Fair value of derivative instruments | 48 | 18 |
| | <u>435</u> | <u>332</u> |
| Long-term debt | 623 | 633 |
| | <u>1,058</u> | <u>965</u> |
| Province of Saskatchewan's equity | | |
| Retained earnings | 349 | 379 |
| Accumulated other comprehensive loss | (4) | (5) |
| | <u>345</u> | <u>374</u> |
| Equity advances | 72 | 72 |
| | <u>417</u> | <u>446</u> |
| | <u>\$ 1,475</u> | <u>\$ 1,411</u> |

(See accompanying notes)

SaskEnergy Incorporated
Consolidated Statement of Income and Retained Earnings

(millions)

(unaudited)

| | Three months ended September 30 | | Nine months ended September 30 | |
|--|------------------------------------|------------------|-----------------------------------|------------------|
| | 2008 (Note 2) | 2007 (Note 5) | 2008 (Note 2) | 2007 (Note 5) |
| Revenue | | | | |
| Commodity sales | \$ 29 | \$ 32 | \$ 244 | \$ 271 |
| Gas marketing sales | 292 | 155 | 438 | 380 |
| Delivery | 24 | 24 | 123 | 112 |
| Transportation and storage | 18 | 21 | 57 | 62 |
| Revenue collected for municipalities | 2 | 2 | 17 | 17 |
| Other | 5 | 4 | 13 | 10 |
| | <u>370</u> | <u>238</u> | <u>892</u> | <u>852</u> |
| Expenses | | | | |
| Commodity cost of gas sold | 154 | 44 | 271 | 277 |
| Gas marketing cost of gas sold | 221 | 144 | 419 | 340 |
| Operating and maintenance | 32 | 28 | 99 | 93 |
| Interest | 10 | 10 | 31 | 33 |
| Amortization | 13 | 14 | 40 | 40 |
| Payments to municipalities | 2 | 2 | 17 | 17 |
| Saskatchewan taxes | 3 | 2 | 6 | 5 |
| | <u>435</u> | <u>244</u> | <u>883</u> | <u>805</u> |
| Net income (loss) | (65) | (6) | 9 | 47 |
| Retained earnings, beginning of period | 422 | 364 | 379 | 344 |
| Change in accounting policy (Note 2) | - | - | (2) | - |
| Dividends | <u>(8)</u> | <u>(13)</u> | <u>(37)</u> | <u>(46)</u> |
| Retained earnings, end of period | <u>\$ 349</u> | <u>\$ 345</u> | <u>\$ 349</u> | <u>\$ 345</u> |

(See accompanying notes)

SaskEnergy Incorporated
Consolidated Statement of Comprehensive Income

(millions)
(unaudited)

| | Three months ended September 30 | | Nine months ended September 30 | |
|--|------------------------------------|----------------|-----------------------------------|--------------|
| | 2008 | 2007 | 2008 | 2007 |
| Net income (loss) | <u>\$ (65)</u> | <u>\$ (6)</u> | <u>\$ 9</u> | <u>\$ 47</u> |
| Other comprehensive income (loss): | | | | |
| Gains and losses on derivative instruments designated as hedges for accounting purposes in prior periods transferred to net income in the current period | - | (4) | - | - |
| Gains and losses on derivative instruments designated as cashflow hedges | 1 | - | 1 | - |
| Unrealized gains and losses on translating financial statements of self-sustaining foreign operations | - | (1) | - | (3) |
| | <u>1</u> | <u>(5)</u> | <u>1</u> | <u>(3)</u> |
| Comprehensive income (loss) | <u>\$ (64)</u> | <u>\$ (11)</u> | <u>\$ 10</u> | <u>\$ 44</u> |

SaskEnergy Incorporated
Consolidated Statement of Accumulated Other Comprehensive Loss

(millions)
(unaudited)

| | Three months ended September 30 | | Nine months ended September 30 | |
|---|------------------------------------|---------------|-----------------------------------|---------------|
| | 2008 | 2007 | 2008 | 2007 |
| Accumulated other comprehensive loss, beginning of period | <u>\$ (5)</u> | <u>\$ (1)</u> | <u>\$ (5)</u> | <u>\$ (2)</u> |
| Transitional amounts for gains and losses on derivative instruments designated as hedges for accounting purposes in prior periods | - | - | - | (1) |
| Other comprehensive income (loss) | 1 | (5) | 1 | (3) |
| Accumulated other comprehensive loss, end of period | <u>\$ (4)</u> | <u>\$ (6)</u> | <u>\$ (4)</u> | <u>\$ (6)</u> |

(See accompanying notes)

SaskEnergy Incorporated
Consolidated Statement of Cash Flows

(millions)

(unaudited)

| | Three months ended September 30 | | Nine months ended September 30 | |
|--|------------------------------------|-------------|-----------------------------------|--------------|
| | 2008 (Note 2) | 2007 | 2008 (Note 2) | 2007 |
| Operating Activities | | | | |
| Net income (loss) | \$ (65) | \$ (6) | \$ 9 | \$ 47 |
| Add (deduct) items not requiring an outlay of cash | | | | |
| Amortization | 13 | 14 | 40 | 40 |
| Change in fair value of derivative instruments | 49 | 16 | 15 | (3) |
| Debt retirement fund earnings | - | - | (1) | (1) |
| Equity earnings | - | (2) | (1) | (2) |
| Other | - | (3) | (2) | (1) |
| | <u>(3)</u> | <u>19</u> | <u>60</u> | <u>80</u> |
| Net change in non-cash working capital related to operations | <u>(37)</u> | <u>7</u> | <u>(36)</u> | <u>9</u> |
| Cash provided by (used in) operating activities | <u>(40)</u> | <u>26</u> | <u>24</u> | <u>89</u> |
| Investing Activities | | | | |
| Additions to property, plant and equipment | (34) | (28) | (80) | (54) |
| Additions to investments and other assets | (2) | (2) | (4) | (3) |
| Customer capital contributions received | 6 | 6 | 16 | 21 |
| Increase in natural gas in storage - non-current | - | (9) | - | (4) |
| | <u>(30)</u> | <u>(33)</u> | <u>(68)</u> | <u>(40)</u> |
| Financing Activities | | | | |
| Decrease in bank indebtedness | - | - | - | (2) |
| Increase (decrease) in short-term debt | 88 | (12) | 154 | (29) |
| Debt retirement fund investments | (2) | (1) | (4) | (4) |
| Debt retirement fund redemptions | - | - | 3 | - |
| Proceeds from long-term debt | - | 40 | - | 76 |
| Repayments of long-term debt (net) | - | - | (75) | (44) |
| Dividends paid | - | (21) | (20) | (46) |
| | <u>86</u> | <u>6</u> | <u>58</u> | <u>(49)</u> |
| Cash provided by (used in) financing activities | <u>86</u> | <u>6</u> | <u>58</u> | <u>(49)</u> |
| Increase (decrease) in cash during period | 16 | (1) | 14 | - |
| Cash position, beginning of period | - | 1 | 2 | - |
| Cash position, end of period | <u>\$ 16</u> | <u>\$ -</u> | <u>\$ 16</u> | <u>\$ -</u> |
| Supplemental cash flow information | | | | |
| Interest paid | <u>\$ 9</u> | <u>\$ 7</u> | <u>\$ 34</u> | <u>\$ 33</u> |

(See accompanying notes)

SaskEnergy Incorporated
Notes to the Consolidated Financial Statements
September 30, 2008
Unaudited

1. Accounting Policies

SaskEnergy Incorporated (SaskEnergy or the Corporation) prepares its consolidated interim financial statements in accordance with Canadian generally accepted accounting principles except that the disclosures do not conform in all respects to the requirements for annual financial statements. The consolidated interim financial statements follow the same accounting policies and methods of computation as the consolidated financial statements for the year ended December 31, 2007 except as noted in the Changes in Accounting Policies Note 2.

These consolidated interim financial statements, which are unaudited, should be read in conjunction with the consolidated financial statements for the year ended December 31, 2007 and have been prepared from the records of the Corporation. The preparation of financial statements in accordance with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amount of assets, liabilities, revenue and expenses. Actual amounts could differ from these estimates.

The consolidated interim financial statements should not be taken as indicative of the performance to be expected for the full year due to the seasonal nature of the natural gas utility business in Saskatchewan.

2. Changes in Accounting Policies

Effective January 1, 2008, SaskEnergy adopted the Canadian Institute of Chartered Accountants (CICA) Handbook Section 1535 – Capital Disclosures in accordance with the transition provisions of the section. This section requires disclosure of information related to the objectives, policies and processes for managing capital, and particularly whether the Corporation has complied with externally imposed capital requirements. As this standard only addresses disclosure requirements, there is no impact on the Corporation's operating results. The new required disclosure is provided in Note 3.

Effective January 1, 2008, SaskEnergy adopted the CICA Handbook Section 3862 – Financial Instruments – Disclosures and Section 3863 – Financial Instruments – Presentation in accordance with the transition provisions of the sections. These sections replace the existing CICA Handbook Section 3861 – Financial Instruments – Presentation and Disclosure. The new disclosure standards increase the disclosures related to financial instruments, and the nature, extent and management of the Corporation's risks arising from financial instruments. As these standards only address disclosure and presentation requirements, there is no impact on the Corporation's operating results. The new required disclosure is provided in Note 4.

Effective January 1, 2008, SaskEnergy adopted the CICA Handbook Section 3031 – Inventories. The new recommendations establish standards for the determination of the cost of inventories and the subsequent recognition as expense, including any write-down to net realizable value and reversals of previous write-downs for increases to net realizable value. Also, guidance is provided related to reclassification of inventory items as property, plant and equipment. The standard requires retrospective application with no restatement of prior year results.

2. Changes in Accounting Policies (continued)

Upon the adoption of the new standard, SaskEnergy began using the weighted average cost method for valuing all natural gas inventories. The impact of applying this change in accounting policy effective January 1, 2008 was as follows:

| | January 1, 2008 |
|--|----------------------------|
| | (millions) |
| Natural gas in storage held for resale | \$ (5) |
| Total assets | \$ (5) |
| Accounts payable | \$ (3) |
| Retained earnings | (2) |
| Total liabilities and equity | \$ (5) |

3. Capital Disclosure

The Corporation's objective when managing its capital is to maintain financial stability through the effective management of liquidity and capital structure. Ensuring financial stability is critical to providing safe reliable service to Saskatchewan residents, businesses and industries.

SaskEnergy funds its capital requirements through internally generated funds and debt. As a Crown corporation, SaskEnergy receives its capital funding primarily from the Saskatchewan Ministry of Finance. SaskEnergy also has a \$30 million line of credit with the Toronto-Dominion Bank. By legislation, SaskEnergy cannot have more than \$1,300 million of debt outstanding at any time. In addition to this limit on total debt outstanding, by Order-in-Council, SaskEnergy may have \$400 million of short-term loans outstanding at any time. SaskEnergy can only issue debt upon approval by the Lieutenant Governor in Council.

SaskEnergy's capital consists of short-term debt having a term to maturity of one year or less, long-term debt having a term to maturity greater than one year and equity, primarily in the form of retained earnings.

3. Capital Disclosure (continued)

The Corporation monitors capital on the basis of the debt ratio. The current long-term per cent debt ratio target is 65%, which is consistent with the prior period. The per cent debt ratio is calculated as net debt divided by end of period capitalization as follows:

| | September 30, 2008 | December 31, 2007 |
|-----------------------|-----------------------|----------------------|
| | (millions) | |
| Gross long-term debt | \$ 633 | \$ 708 |
| Short-term debt | 242 | 88 |
| Debt retirement funds | (45) | (43) |
| Cash | (16) | (2) |
| Total net debt | <u>\$ 814</u> | <u>\$ 751</u> |
| Equity advances | 72 | 72 |
| Retained earnings | 349 | 379 |
| Total capital | <u>\$ 1,235</u> | <u>\$ 1,202</u> |
| Debt ratio | <u>65.9%</u> | <u>62.5%</u> |

SaskEnergy complied with all externally imposed requirements on its capital for the nine months ended September 30, 2008.

4. Financial Instruments and Risk Management

a. Financial instruments

The fair value of the Corporation's financial instruments is listed below:

| | September 30, 2008 | | December 31, 2007 | |
|--------------------------|--------------------|---------------|--------------------|---------------|
| | Carrying Amount | Fair Value | Carrying Amount | Fair Value |
| | (millions) | | | |
| Other liabilities | | | | |
| Long-term debt | \$ 633 | \$ 680 | \$ 708 | \$ 798 |
| Held-for-trading | | | | |
| Debt retirement funds | 45 | 45 | 43 | 43 |

The fair value of the above instruments was based on the following:

- i. Long-term debt – The present value of future cash flows discounted at the market rate of interest for the equivalent Province of Saskatchewan debt instruments.
- ii. Debt retirement funds – The market value of the investments held in the debt retirement fund as determined by Saskatchewan's Ministry of Finance as at September 30 and December 31.

4. Financial Instruments and Risk Management (continued)

b. Natural gas derivative instruments

The fair value of natural gas derivative instruments held-for-trading is calculated daily and is based on quoted market prices. For physical natural gas contracts notional values are an approximation of future net cash flows based on contract price multiplied by contract quantity. For other derivative financial instruments, the notional value is the difference between the contract price and the market price. SaskEnergy has sufficient borrowing capacity to fund these contractual obligations. Where contract prices are referenced to an index price that has not yet been fixed, the market price at September 30, 2008 has been used to estimate the contract price. At September 30, 2008, all derivative assets and liabilities held-for-trading are recorded on the statement of financial position at fair value.

As at September 30, 2008, natural gas derivative instruments held-for-trading had the following fair values, notional values and maturities:

| | <u>2008</u> | <u>2009</u> | <u>2010</u> | <u>2011</u> | <u>2012</u> | <u>Total</u> |
|--|-------------|-------------|-------------|-------------|-------------|--------------|
| | (millions) | | | | | |
| Physical natural gas contracts | | | | | | |
| Fair value | \$ 4 | \$ 6 | \$ - | \$ - | \$ - | \$ 10 |
| Notional value | (73) | (119) | 10 | 4 | 1 | (177) |
| Natural gas price swaps | | | | | | |
| Fair value | (11) | (2) | 6 | (1) | - | (8) |
| Notional value | (11) | (2) | 6 | (1) | - | (8) |
| Natural gas price options | | | | | | |
| Fair value | (3) | (6) | - | - | - | (9) |
| Notional value | (4) | (4) | - | - | - | (8) |
| Total | | | | | | |
| Fair value | \$ (10) | \$ (2) | \$ 6 | \$ (1) | \$ - | \$ (7) |
| Notional value | \$ (88) | \$ (125) | \$ 16 | \$ 3 | \$ 1 | \$ (193) |
| Fair value - increase (decrease) | | | | | | |
| Notional value - estimated net cash inflow (outflow) | | | | | | |

c. Changes in fair value

The fair value of derivative instruments is presented on the consolidated statement of financial position as follows:

| | <u>September 30,</u> <u>2008</u> | <u>December 31,</u> <u>2007</u> |
|---|-------------------------------------|------------------------------------|
| | (millions) | |
| Fair value of derivative instrument assets | \$ 41 | \$ 26 |
| Fair value of derivative instrument liabilities | (48) | (18) |
| Total fair value | <u>\$ (7)</u> | <u>\$ 8</u> |

4. Financial Instruments and Risk Management (continued)

The fair value of other financial instruments, including cash, accounts receivable, bank indebtedness, short-term debt, accounts payable and dividends payable approximate their carrying values due to the short-term nature of the instruments.

The change in fair value of financial and derivative instruments is recorded in net income within the relevant revenue or expense category. For the period ended September 30 the impact on net income, increase (decrease) in net income, of these unrealized gains and losses was as follows:

| | Three months ended | | Nine months ended | |
|-----------------------------------|--------------------|---------|-------------------|------|
| | 2008 | 2007 | 2008 | 2007 |
| | (millions) | | (millions) | |
| Derivative instruments | | | | |
| Commodity sales | \$ - | \$ - | \$ - | \$ - |
| Gas marketing sales | 104 | 1 | 15 | 22 |
| Commodity cost of gas sold | (123) | (10) | (28) | (6) |
| Gas marketing cost of gas sold | (30) | (4) | (2) | (13) |
| | (49) | (13) | (15) | 3 |
| Financial instruments | | | | |
| Interest expense | (1) | - | (1) | (1) |
| Increase (decrease) in net income | \$ (50) | \$ (13) | \$ (16) | \$ 2 |

d. Risk management

The Corporation uses various derivative financial instruments to manage the risks associated with its operating exposures to fluctuations in foreign currency exchange rates, interest rates and the price of natural gas. A Corporate Derivatives Policy and specific risk management strategies establish the guidelines within such derivative financial instruments may be used.

i. Natural gas price risk

The Corporation may manage the risk associated with the purchase and sale price of natural gas. The purchase or sale price of natural gas may be fixed within the contract, or referenced to a floating index price. When the price is referenced to a floating index price, natural gas derivative instruments may be used to fix the settlement amount. The types of natural gas derivative instruments SaskEnergy uses for price risk management include natural gas price swaps, options, swaptions and futures contracts. An increase of \$1.00 per Gigajoule in natural gas prices would increase net income by \$10 million, while a decrease of \$1.00 per Gigajoule would decrease net income by \$10 million.

ii. Foreign currency exchange and interest rate risk

The Corporation uses derivative financial instruments to manage the interest rate risk on anticipated borrowing requirements and the foreign currency exchange rate on foreign currency denominated transactions. For the purpose of managing interest rate risk, the Corporation may use forward rate agreements, options and interest rate swaps to achieve an annual average interest rate target. For the purpose of managing the exchange rate risk on transactions denominated in foreign currency, SaskEnergy may use currency forwards and currency options.

4. Financial Instruments and Risk Management (continued)

iii. Liquidity risk

Liquidity risk is the risk that the Corporation is unable to meet its financial obligations as they become due. For the following financial obligations, the Corporation has credit facilities available to refinance maturities in excess of anticipated operating cash flows. The following summarizes the contractual maturities of the Corporation's financial obligations as at September 30, 2008:

| | <u>6 months or less</u> | <u>7-12 months</u> | <u>1-2 years</u> (millions) | <u>3-5 years</u> | <u>More than 5 years</u> |
|----------------------------------|-----------------------------|------------------------|--------------------------------|------------------|------------------------------|
| Short-term debt | \$ 242 | \$ - | \$ - | \$ - | \$ - |
| Accounts payable | 111 | - | - | - | - |
| Dividend payable | 24 | - | - | - | - |
| Derivative instruments | 114 | 74 | - | - | - |
| Long-term debt | 19 | 46 | 125 | 137 | 722 |
| Debt retirement fund investments | 3 | 3 | 5 | 13 | 40 |
| | <u>\$ 513</u> | <u>\$ 123</u> | <u>\$ 130</u> | <u>\$ 150</u> | <u>\$ 762</u> |

iv. Credit risk

The Corporation extends credit to its customers in the normal course of business and is at risk of loss in the event of non-performance by counterparties on certain of the financial instruments described above. To reduce its credit risk, SaskEnergy has established policies and procedures to monitor and limit the amount of credit extended to its customers and counterparties.

The carrying amount of financial assets represents the maximum credit exposure as follows:

| | <u>September 30, 2008</u> | <u>December 31, 2007</u> |
|--|-------------------------------|------------------------------|
| | (millions) | |
| Cash | \$ 16 | \$ 2 |
| Accounts receivable | 52 | 131 |
| Debt retirement funds | 45 | 43 |
| Fair value of derivative instrument assets | 41 | 26 |
| Investments and other assets | 39 | 33 |
| Maximum credit exposure | <u>\$ 193</u> | <u>\$ 235</u> |

4. Financial Instruments and Risk Management (continued)

The following reflects an aging summary of the Corporation's accounts receivable:

| | September 30, 2008 | December 31, 2007 |
|---------------------------------|-----------------------|----------------------|
| | (millions) | |
| Current | \$ 53 | \$ 127 |
| 30 - 59 days | (2) | 4 |
| 60 - 89 days | 1 | 1 |
| Greater than 90 days | 1 | - |
| | <u>53</u> | <u>132</u> |
| Allowance for doubtful accounts | (1) | (1) |
| Accounts receivable | <u>\$ 52</u> | <u>\$ 131</u> |

Provisions for credit losses are maintained and regularly reviewed by the Corporation. Credit losses are estimated based on an aging of customer accounts. Amounts are written off once reasonable collection efforts have been exhausted. Details of the allowance are as follows:

| | September 30, 2008 | December 31, 2007 |
|--|-----------------------|----------------------|
| | (millions) | |
| Allowance for doubtful accounts, beginning of period | \$ 1 | \$ 2 |
| Provision | 1 | 1 |
| Recoveries | 1 | 2 |
| Write-offs | (2) | (4) |
| Allowance for doubtful accounts, end of period | <u>\$ 1</u> | <u>\$ 1</u> |

Derivative credit risk arises from the possibility that a counterparty to a contract fails to perform according to the terms and conditions of that contract. Derivative credit risk is minimized by dealing with large, credit-worthy counterparties in accordance with established credit approval policies.

5. Comparative Figures

Certain of the prior period's figures have been reclassified to conform to the current period's presentation.