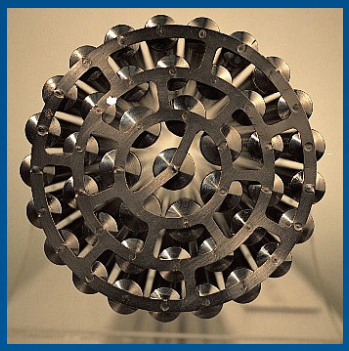
ATOMIC ENERGY OF CANADA LIMITED

2006 ANNUAL REPORT



LEADING THE WAY

UNIQUELY POSITIONED

Atomic Energy of Canada Limited (AECL) is a fully integrated nuclear technology and services company providing services to nuclear utilities worldwide. Our 4,000 employees are dedicated to delivering leading-edge nuclear services, R&D support, design and engineering, construction management, specialized technology, refurbishment, and waste management and decommissioning in support of CANDU® reactor products.

AECL is committed to supporting its Canadian and international customers in all aspects of nuclear power technology management. We provide on-site expertise, closely supported by our nuclear science laboratories, testing capability and engineering facilities. CANDU reactors supply about 15 per cent of Canada's electricity and are an important component of clean-air energy programs on four continents. AECL is a Crown Corporation that was established in 1952 to develop peaceful applications of nuclear energy.

Mandate

AECL will create customer and shareholder value through:

- Managing the Canadian nuclear platform responsibly and cost effectively.
- Leveraging the technology base to deliver nuclear products and services to market.
- Paying dividends from profitable growth.

Vision

- To be the top worldwide nuclear products and services company.
- To protect the health and safety of the public, our employees and the environment.
- To minimize nuclear legacy obligations for future generations.

Values

To achieve our vision, AECL people must be:

- Driven by Customers' Needs.
- Obsessed by Quality, Excellence & Safety.
- Personally Responsible and Accountable.
- Engaged in Open and Honest Communication.
- Empowered to Challenge and Innovate.
- Committed to Learning and Teamwork.
- Motivated by Performance.

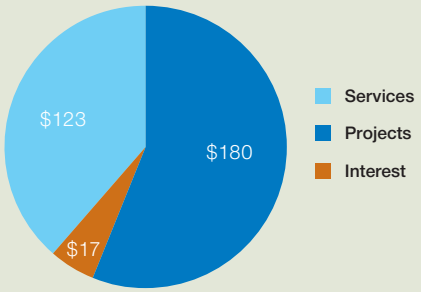
Customer Commitment

Trust, Quality, Innovation, Value ...
AECL's commitment to you.

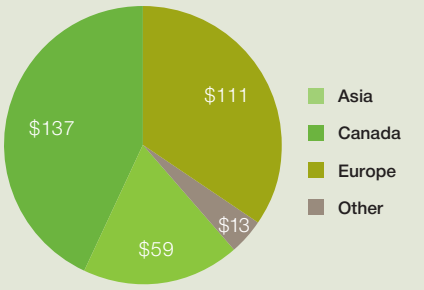
2005–2006 Revenue
($ millions)

Commercial sales are on the rise with double-digit growth expected in 2006–2007, primarily as a result of increased activity in the refurbishment business.

Commercial Operations



By Region



Within the total revenue of $320 million from Commercial Operations, exports were $183 million, contributing positively to a favourable balance of trade for Canada in 2005–2006.

TABLE OF CONTENTS

2005–2006 OPERATING HIGHLIGHTS

At AECL we are dedicated to delivering with excellence. We are well positioned to perform at the highest level and ready to meet the demands of the re-emergence of nuclear energy.

- All health, safety and environmental targets exceeded.
- Secured refurbishment contracts with New Brunswick Power and Bruce Power.
- CANDU Services revenue grew by 18% to $123 million.
- Annual domestic customer satisfaction survey increased 14%, exceeding the target by 4%.
- The CNSC extended the NRU operating licence to July 2006.

- Entered a formal agreement with Babcock & Wilcox Canada, GE Canada, Hitachi Canada, and SNC-Lavalin Nuclear to create Team CANDU. Together, these five world-leading nuclear technology and engineering companies will present a turnkey service and competitive solution for building new nuclear power plants in Ontario.
- Maintained ISO 14001 environmental management accreditation.
- A January 2006 Ipsos-Reid poll showed that 61% of Ontarians support nuclear and 73% support refurbishment, up from 53% and 70% respectively in August 2005.

WORLD CLASS TECHNOLOGY

48 Heavy Water Reactors based on the CANDU design in operation, under construction, or under refurbishment – located on four continents.

AECL OFFICES

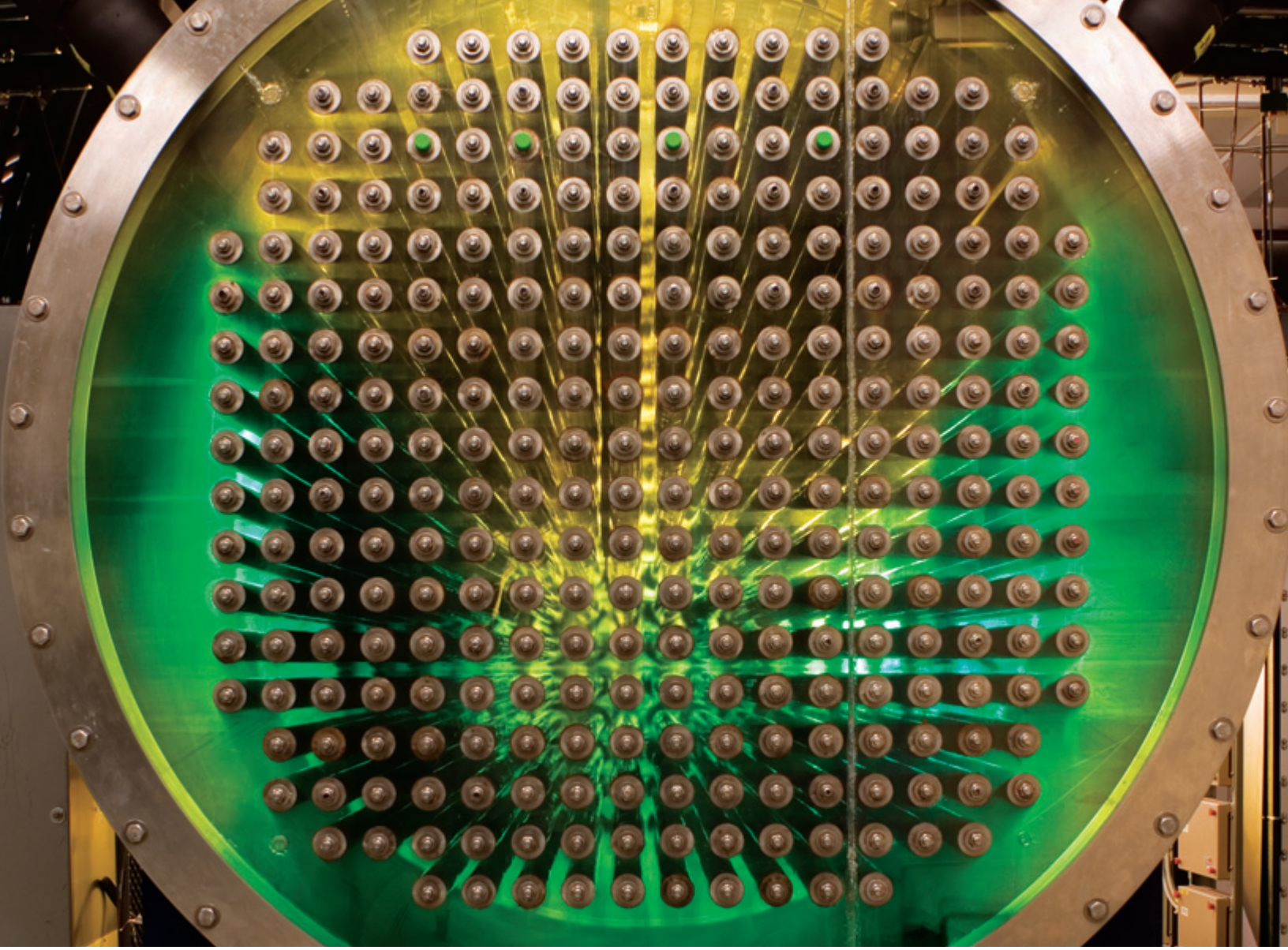
1. Head Office, Mississauga, Canada
2. Whiteshell Laboratories, Canada
3. Montréal, Canada
4. Ottawa, Canada
5. Chalk River Laboratories, Canada
6. Saint John, Canada
7. Gaithersburg, Maryland, U.S.A.
8. Pickering, Canada
9. Seoul, South Korea
10. Beijing, China

CANDU REACTORS

1. Ontario, Canada (18 units)
2. Québec, Canada (1 unit)
3. New Brunswick, Canada (1 unit)
4. Argentina (1 unit)
5. Romania (1 unit, 1 under construction)
6. Pakistan (1 unit)
7. India (13 units, 5 under construction)
8. South Korea (4 units)
9. China (2 units)

REFURBISHMENTS

1. Ontario, Canada
2. Québec, Canada
3. New Brunswick, Canada
4. Argentina
5. South Korea



AECL AT A GLANCE

AECL supports all aspects of the CANDU reactor product life cycle including the design and construction of nuclear reactors and related products, services, life extension and decommissioning and waste management. AECL also manages production and supply of a significant portion of the global medical isotope requirements.

On behalf of the Government of Canada, AECL also fulfills a unique public policy role in maintaining and enhancing Canadian nuclear technology to secure Canada's electricity supply requirements and manage legacy waste obligations.

AECL BUSINESS UNITS

Reactor Sales and Services (Commercial Operations)

CANDU Services	Dedicated to providing cost-effective and high quality services aimed at improving performance of all operating CANDU plants while increasing AECL's market share, revenues and margins.	· Control and information products. · Operational support. · Fuelling machine/fuel handling equipment. · Heavy water. · Non-reactor core equipment. · Plant life management. · Reactor core. · Safety and analysis. · Secondments. · Smart CANDU remote monitoring.
Projects	Focused on supporting AECL's global CANDU customers in optimizing the performance of existing generating assets and the construction of new build plants.	· Inspection and maintenance services. · New build projects. · Reactor refurbishment and retubing.
Technology Commercialization	Responsible for the commercialization of new technology leveraged from AECL's R&D efforts.	· Reactor safety technology. · Waste management services.

Reactor Safety and Research (Technology)

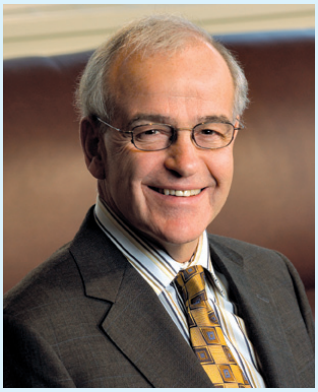
Nuclear Laboratories	R&D activities are carried out at AECL's Chalk River Laboratories. Research initiatives and programs focus on ensuring the safe and effective operation of CANDU reactors; developing new products and services to enhance AECL's business opportunities; and to support Canadian government policy.	· Research reactor (NRU). · Shielded facilities (hot cells). · Nuclear materials production. · Nuclear labs and experimental facilities. · Nuclear safety and analysis. · Shops for radioactive materials. · Isotope Production.
Reactor Development	Leads all activities related to the ACR, including technology and market development. Provide and enhance the safety, licensing, and design technology-basis for CANDU.	· Advanced CANDU Reactor. · CANDU 6. · MAPLE Reactor.

Environmental Management (Liability Management Unit)

Decommissioning and Waste Management	Manages the waste management and decommissioning program, and oversees funding received from the Government of Canada for the program. AECL manages low-level radioactive waste at various locations across Canada on behalf of the Federal Government.	· Decommissioning planning and project management. · Site preparation, fuel handling and high- and low-level decontamination. · Dry used fuel storage system (MACSTOR®). · Modular Above Ground storage (MAGS).

AECL IS A CROWN JEWEL OF TECHNOLOGY IN CANADA

AECL provides high-quality products and services, fulfills a vital public-policy mandate, provides high-quality jobs and makes a disproportionately important contribution to Canada's scientific endeavours and its gross national product.



JEAN-PIERRE SOUBLIÈRE
Acting Chairman of the Board

We live in a world of continuous change, and that means those who stand still soon get left behind. With that in mind, I am pleased to report that AECL has been changed – it has improved its strategies and governance so it can not only keep up, but also be a leader in the nuclear industry. AECL is a crown jewel of technology in Canada, providing high-quality products and services, fulfilling a vital public-policy mandate, providing high-quality jobs and making a disproportionately important contribution to the nation's scientific endeavours and its GNP.

In the past year, the Board of Directors has continued to implement new capabilities in corporate governance, bringing it in line with best practices. AECL has a culture of transparency and accountability. These changes ably position us to meet the most rigorous standards set out for businesses. We are confident that AECL has the administrative tool set and skills to participate in the global renewal of nuclear energy.

Over the past five years, the Board has closely co-operated with management in a strategic vision that has prepared us for that renewal. We continue to evolve our proprietary technology, to address the matter of waste management with the most reliable technology and protocols in the world, to revolutionize our service delivery and to provide value-added products and services to customers. AECL is ready to deliver, and to deliver with excellence.

As Acting Chairman, I have been deeply impressed by the true dedication of the Board of Directors and of all the people at AECL. I am confident that they will continue to provide an astounding ability to change and lead in what is one of Canada's most important and successful advanced technology sectors. I offer them my thanks.

JEAN-PIERRE SOUBLIÈRE
Acting Chairman of the Board

BOARD HIGHLIGHTS

- The Board assessed its own performance against best practices and established an action plan to enhance its effectiveness and demonstrate accountability to the Shareholder.
- New Board members participated in a detailed orientation program and training while continuing education was provided to all other Directors.
- The Minister of Natural Resources confirmed the Nominating Committee's recommendation to reappoint Mr. Robert Van Adel as President and CEO.
- The Board participated in streamlining AECL's financial reporting directed at more timely, transparent and concise information.

OUR COMMITMENT TO CORPORATE GOVERNANCE

AECL will continue its pursuit of the highest levels of transparency and accountability.

The Board of Directors remains on the path to implementing best practices in corporate governance. In 2005–2006, AECL built on steps and actions taken in the previous year by assessing performance against best practices and devised an action plan that will improve its effectiveness and demonstrate accountability to the Shareholder.

From a financial governance perspective, the Board continued working to streamline AECL's financial reporting so that it is more timely, transparent and concise. The Audit Committee, in keeping with best practices, met *in camera* regularly with external and internal auditors and without the presence of management. Further, the committee has measured its performance and reported to the larger board on its effectiveness.

The Science and Technology Committee provided the company with an independent assessment of its research and development, and product development programs, including the Advanced CANDU Reactor (ACR-1000®), to ensure they are aligned with the company's objectives.

With respect to human resources, a Board committee oversaw and advised on all aspects of governance and corporate policies and strategies related to employees, including health and safety. Among other things, it completed a number of governance activities, including ensuring that the Board explicitly takes responsibility for AECL's stewardship, and that it examines its public-policy objectives and legislated mandate. It ensured that the company communicates with the Crown and other stakeholders and completed an annual review of governance. As well, it ensured that the Board assess periodically the position and performance of the CEO.

By these actions, reported in detail in the Management's Discussion and Analysis section of this report, the Board and its committees are ensuring that AECL lives up to its commitments to transparency and accountability.

DELIVERING EXCELLENCE IN EVERYTHING WE DO

AECL is prepared to deliver. After five years of re-inventing this organization, we can say that we are ready, willing and able to perform to the highest standards.

ROBERT G. VAN ADEL
President and
Chief Executive Officer

AECL enjoyed a very good year in 2005–2006. We met or exceeded all key commitments to our Shareholder and have positioned ourselves to seize opportunities for nuclear power growth in Canada and globally. We accelerated our culture change initiatives, dramatically improved customer satisfaction and continue to foster an environment that values safety and performance excellence.

Revenue in our Commercial Operations business grew six per cent on the strength of signing major reactor refurbishment contracts with New Brunswick Power and Bruce Power. In addition, our CANDU Services business continued its strong performance with 18 per cent growth, a sign that AECL is truly a provider of full life cycle support to our customers.

Not only does AECL contribute design and project management of new build nuclear projects and offer critical operations and management support throughout the life cycle of a reactor, we now offer reactor refurbishment capabilities. We expect to take this new life extension business international in 2006–2007 by signing a contract with Korea Hydro & Nuclear Power Co. Ltd. to retube the first Wolsong reactor over the next five years. The addition of refurbishment to our product set complements our CANDU Services business and the new build nuclear business, which is poised for significant growth due to the global nuclear renaissance.

Our CANDU 6 reactor has the best lifetime performance of any competing design. We are completing construction of a reactor in Romania and we continue to receive expressions of interest for CANDU 6 new builds, mainly due to its proven performance and AECL's ability to deliver projects on time, on budget. AECL has been the top global nuclear reactor exporter over the past decade and we have enhanced our project management and design capabilities throughout this period. Our continual excellent performance gives AECL a strong competitive advantage and will allow us to seize the opportunities presented by next generation nuclear technology.

We met our development milestones for the Advanced CANDU Reactor, ACR-1000®, and are positioned to meet market demands for new nuclear using third generation technology and improved

Mathew Handzlik, Mechanical Technician, Sheridan Park. Measuring bore diameter of ACR end shield mock-up.

RAISING THE BAR – 2006–2007 PRIORITIES

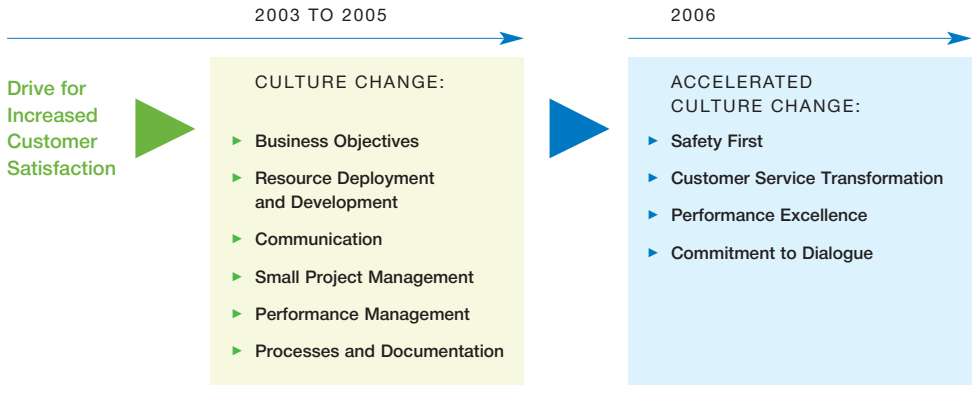
- Achieve sales of $596 million.
- Improve overall health and safety performance.
- Renew Chalk River site operating licence.
- Implement Comprehensive Waste Management and Decommissioning Plan for AECL's nuclear sites.
- Develop ACR to meet customer requirements.
- Ensure the uninterrupted supply of medical isotopes.
- Increase openness with all stakeholders, our Shareholder and the CNSC.

price performance. The ACR-1000 design has benefited from extensive customer input to ensure not only that it meets performance targets, but also is easy to maintain and operate. AECL has focused its efforts on the Ontario market where new sources of energy will be required within the next 10 years, but we also have opportunities in New Brunswick, which has announced its intent to explore new build nuclear, and in the United Kingdom, where CANDU performance and design is recognized as a key nuclear program competitor. The ACR-1000's introduction, coupled with the CANDU 6, offers continued opportunities and promises to deliver double-digit revenue growth.

The core technology expertise, skills and infrastructure supplied by our Nuclear Laboratories Centre of Excellence in Chalk River is an essential component in increasing our Commercial Operations Business, which pays market rates for these services and invests its profits to support day-to-day operations of the Nuclear Laboratories. This structure guarantees transparent flow of funds between the unit and ensures that there is no subsidization of the Commercial Operations by the government-funded laboratories. As a result, Canada operates its nuclear R&D facilities more cost effectively, on a per capita basis, than any other nation.

AECL is committed to developing and maintaining a safety culture that delivers effective quality assurance programs. Our performance excellence culture is integrated into both our commercial project management business and our Chalk River operations. We have increased our investment in the National Research Universal (NRU) reactor operations and have set benchmarked standards based on best in class operators. These investments and continued focus on performance excellence and safety has contributed to improved relations with the Canadian Nuclear Safety Commission (CNSC).

VALUES IN MOTION



Our initial work on culture change began in 2003. At that time we identified six functional root causes to focus on. We have identified four specific areas to accelerate our efforts to achieve "breakthroughs" in culture change: Safety First, Customer Service Transformation, Performance Excellence, and Commitment to Dialogue.
We are excited to report that 83% of our customers surveyed indicated they were satisfied with AECL's performance.

The CANDU industry is vital to Canada's economy and indeed, its future. Its 150 companies provide 30,000 high-quality jobs and generate $6 billion a year. Less tangibly, it contributes to Canada's destiny as a leading intelligence-based economy, giving the world breakthroughs that cannot be duplicated anywhere else.

Ted Chudak, Development Technician, Sheridan Park. Control system upgrade.

During 2005–2006, we extended the operating licence of the NRU to coincide with the renewal of the Chalk River site licence. AECL is now well placed for an overall operating licence extension.

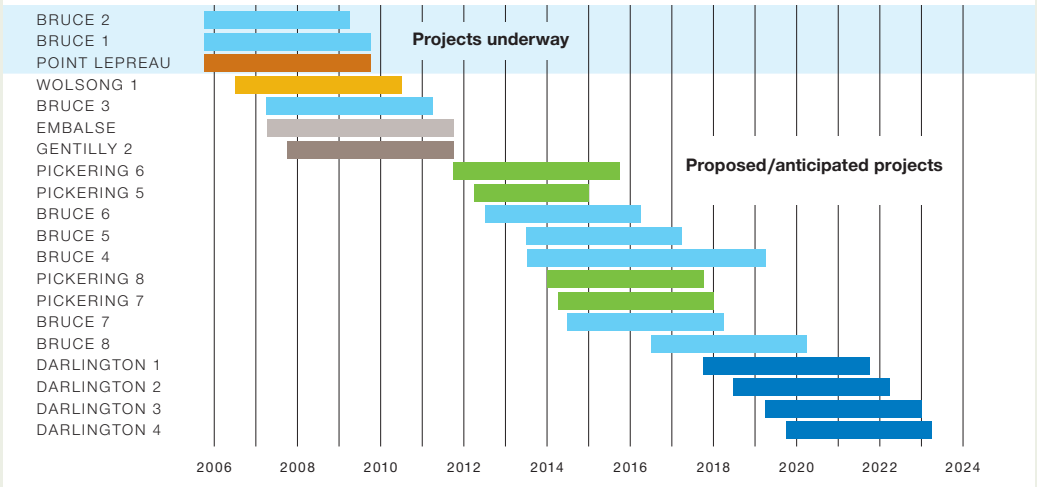
Another key breakthrough was the funding of the legacy waste and decommissioning liability for the Whiteshell and Chalk River laboratories and several prototype reactor sites. During our previous fiscal year, AECL booked a liability to reflect current accounting practices and international best practices for waste management, which is reflected in Government of Canada accounts. The Government has indicated its intention to commit $520 million to fund the first five years of a long-term strategy to deal with the legacy waste and decommissioning liability. AECL has created the Liability Management Unit (LMU), an independent organization, to ensure that these funds are spent in an effective and transparent manner, consistent with the Government's long-term strategy. The LMU will enter into formal internal contracts to ensure clear governance and that the operating arm, the Nuclear Laboratories, delivers its projects with excellence. AECL now has a clear mandate to address the nuclear legacy waste and liability so that future generations will not inherit them.

Resolution through mediation with MDS Inc. and its subsidiary MDS Nordion opened a new era of co-operation. In exchange for ownership of the two MAPLE reactors under construction, and the New Processing Facility at Chalk River, AECL entered into a 40-year agreement to supply MDS Nordion with medical isotopes. AECL will commission the two reactors in 2008 and 2009 and provide funding to complete and operate them. In return, we will receive a share of net revenues from the sale by MDS Nordion of isotopes used worldwide in medical diagnostic and treatment procedures. We are confident that this new agreement will maintain Canada's market leadership in high-technology medicine.

EXECUTING WITH EXCELLENCE

With three life extension projects underway and more anticipated, refurbishment represents about 60% of our business. Each project has a similar economic impact as a new build.

20 YEARS OF ACTIVE AND PLANNED LIFE EXTENSION PROJECTS



In this new nuclear era, we're focusing on delivering what we've learned in recent years. How we execute our strategy will determine how well AECL fares. Yet I'm pleased and confident that we have the strategies, systems, expertise, relationships, and the people we need to deliver.

In late March 2006, AECL joined forces with four of the world's leading nuclear technology and engineering companies to present a turnkey service and competitive solution for building new nuclear plants in Ontario. The four-year, Team CANDU agreement combines AECL's expertise with that of our project partners: GE Canada, SNC-Lavalin Nuclear Inc., Babcock & Wilcox Canada and Hitachi Canada. Having worked together abroad for years, we are now focusing on reactor sales domestically. Team CANDU is proposing to deliver a business model for Ontario that we have successfully deployed in markets around the world over the past decade.

AECL's accomplishments this year were significant, but I am equally proud of the manner in which we achieved them. We exceeded market benchmarks for safety and our days lost due to injury were significantly better than target. In an attempt to foster a workplace that values quality assurance, the number of Non-Conformance Reports increased in response to management encouragement to actively address performance issues. A culture that challenges its performance standards will improve quality assurance processes and drive performance excellence.

Our domestic customer service survey showed that satisfaction levels have improved for the third year in a row with overall customer approval reaching 83 per cent and improvements made in all categories. These leading cultural change indicators bode well for the future as our processes begin to match the world-class skill set of our employees.

Our success in 2005–2006 demonstrates that AECL is prepared to deliver: We met or exceeded key Company milestones and commitments and signed major agreements that will change our direction for years to come; refurbishment contracts complete AECL's product offering, meeting customers' and marketplace needs while our on-schedule ACR development will also fulfil those needs; our Nuclear Laboratories delivers excellence through safety and have established an effective relationship with our regulator; we have forged a long-term partnership with our Shareholder to address legacy waste and decommissioning liability at AECL sites; we entered into a 40 year agreement with MDS Nordion to deliver medical isotopes to the world community; and we have made great strides in establishing a culture which strives for performance excellence in a safe, customer focused manner.

On behalf of the Board of Directors and Senior Management, I wish to thank our employees for their dedication and commitment to this organization and for bringing AECL to a strong position at the dawn of this nuclear renaissance.

The future looks bright and AECL is well positioned to Lead the Way.

The Team CANDU companies have joined forces to deliver a competitive solution for building new nuclear plants in Ontario, Canada.

Team CANDU DELIVERING MORE

ROBERT G. VAN ADEL
President and Chief Executive Officer

INDUSTRY DYNAMICS

As the global need for energy continues to grow, many nations are committing to nuclear energy as a key part of their supply strategies. Electricity produced by nuclear can provide reliable, cost-effective and environmentally sound solutions while decreasing reliance on foreign oil and gas, which is increasingly expensive and vulnerable to supply interruptions. According to the World Nuclear Association, countries around the world expect to build about 150 new nuclear energy plants over the next three decades. Here at home, the case for nuclear was clearly made in late 2005, when the Ontario Power Authority (OPA) recommended to the Government of Ontario that nuclear power maintain its place in the proposed mix of energy-supply sources. Nuclear represents about half of the electricity generated in Ontario so to meet the growing need for power, the Province will require more nuclear generating capacity. The OPA's 2005 Power System Planning Study warns that Ontario is at "one of the most challenging points in its

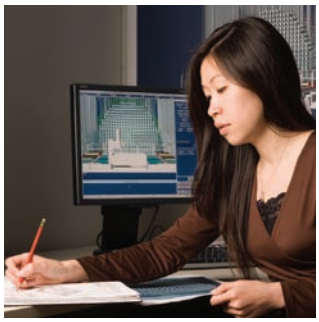
Electricity produced by nuclear can provide reliable, cost-effective and environmentally sound solutions while decreasing reliance on foreign oil and gas, which is increasingly expensive and vulnerable to supply interruptions.

history". While it recognizes that renewable energy and gas-fired sources may replace some coal-generated power, the study says "nuclear plants have less overall environmental impact than natural gas-fired generation and operate at a lower cost for base-load needs".

Through a continuum of technical achievement and solid, ongoing activity building and servicing nuclear reactors, AECL is helping to secure the world's future in energy, medicine, research and a wide array of public-policy activities.

The economics for life extension through refurbishment are also compelling. Refurbishment and life extension represent an exciting growth area for AECL, and demonstrate again the strength and flexibility of CANDU design.

Sylvia Cheong, Simulation Engineer, Sheridan Park, CAD simulation.



A strong, growing nuclear industry to serve these increasing energy needs is more than just the hallmark of a technologically advanced nation. It is a crucial part of Canada's technological future: an expanding industry that provides high-quality, high-tech jobs, with high-value direct and indirect economic activity. Already, Canada's nuclear sector is a $6 billion-a-year industry that employs 30,000 workers in 150 companies throughout the country. AECL is the Canadian industry leader: its CANDU plants are located in seven countries and collectively they avoid about 150 million tonnes of greenhouse gas emissions every year. These plants deliver low-cost energy in a predictable, reliable manner. In addition, AECL produces medical isotopes that are used in 68,000 procedures per day throughout the world.

The economics for life extension through refurbishment are compelling. Refurbishment and life extension represent an exciting growth area for AECL, and demonstrate again the strength and flexibility of CANDU design.

Beyond commercial considerations, AECL participates in a number of public policy initiatives and assignments. Among them is researching new and safer ways for the long-term storage of nuclear waste and leveraging AECL's expertise and Canada's international reputation as a responsible worldwide leader in nuclear affairs. AECL supports Canada's involvement in global nuclear policy discussions at the International Atomic Energy Agency and the Organization for Economic Co-operation and Development. One example is AECL's contribution, under the leadership of Natural Resources Canada, to international efforts in defining and creating the next generation of nuclear reactor, known as Generation IV. It would provide power with unprecedented reliability, economics and safety.

Amy Siegner, Design Engineer (left) and Clayton McGregor, Mechanical Technologist, Sheridan Park. Remote tooling.

Elsewhere, as the price of fossil fuels rises, there will be increasing economic opportunities to develop hydrogen-based activities. Another possibility is to generate steam – powered by nuclear reactors – to help Alberta oil sands operations unlock the oil contained in the bitumen sand.

Through a continuum of technical achievement and solid, ongoing activity building and servicing nuclear reactors, AECL is helping to secure the world's future in energy, medicine, research and a wide array of public-policy activities.

EXPERTISE

Mathew Handzlik, Mechanical Technician (left) and Thomas Zumpe, Mechanical Technician, Sheridan Park. ACR end shield mock-up.

To be a world leader, we have to focus our effectiveness and experience – in our strategic direction, in our responsiveness to customers and stakeholders, in alliances, and in our research and development. R&D doesn't just happen; it is an evolving and committed program supported by a team of the highest quality and skill. AECL is one of Ontario's largest employers of scientists and engineers, with 310 PhDs, 709 Masters, and 1,110 Professional Engineers, and 850 other technical professionals. Our accumulated expertise and ongoing research are enabling AECL to be one of the world's true nuclear industry leaders.

AECL manages one of the most cost-effective national nuclear R&D programs in the developed world. In 2005–2006, thanks to our commercial income, AECL contributed $47 million directly from its commercial operations to support Canada's scientific nuclear capability. This supplements the Government of Canada's contribution of $104 million.

AECL focuses research and development in seven key areas: safety, fuel and fuel cycles, fuel channels, components and systems, heavy water technology, health and environment, and waste management. The Board of Directors' Science and Technology Committee sets policy, monitors strategic direction and provides oversight. It is assisted by an external Research and Development

Advisory Panel comprised of experts and scientists from academia and industry, which advises AECL on strategic needs, overall direction and the effectiveness of our R&D programs.

Renewing our ranks of nuclear scientists is also a vital goal. AECL provides facilities at Chalk River Laboratories for graduate and post-graduate Canadian and international students to receive nuclear technology training. Through their educational institutions and the National Research Council, students have access to the National Research Universal (NRU) reactor and other facilities.

In addition, AECL's summer program allows undergraduate science and engineering students to experience work in a nuclear laboratory. At the secondary school level, AECL supports the Deep River Science Academy, in which students work alongside principal investigators in nuclear research.

Over six decades, AECL has built one of the most extensive nuclear knowledge bases in the world, with current staff continuing the tradition of R&D excellence. A primary example is the groundwork being performed on the Advanced CANDU Reactor, or ACR-1000.

DELIVERING EXCELLENCE

A pioneer in the CANDU retubing process, Bryan Murdoch is leading AECL's Bruce Retube Project – a critical part of client Bruce Power's overall refurbishment of Bruce A, Units 1 and 2, and one of the most important refurbishment projects in CANDU's history. With 35 years in the nuclear industry business, including positions with Ontario Hydro/Ontario Power Generation, Bryan's extensive technical knowledge of fuel channel replacement processes and associated technology is enriched by his high standards for employee safety and quality assurance in all aspects of reactor maintenance. Coupled with a commitment to client satisfaction and his ability to build a strong project management focused organization that emphasizes creative solutions for improving performance, Bryan will ensure the project is done safely, to the highest quality of standards, and on schedule.

Bryan Murdoch, General Manager, Bruce Retube Project

The ACR-1000 represents a new generation of nuclear power plants, designed to meet customer and public expectations by delivering enhanced safety, major improvements in economics, and technology to achieve operational excellence. The ACR development targets are ambitious and highly competitive. They include:

- Enhancing safety by a 10-fold reduction in the (already low) probability of severe accidents.
- Achieving economic improvement through a 25 per cent reduction in lifetime electricity costs.
- Delivering operational excellence through design for a 95 per cent capacity factor – a five per cent improvement on current best-in-class performance.

The ACR-1000 is designed to minimize its environmental footprint. As an emissions-free energy source, it offers advantages for climate change and clean air. Compared to displaced coal plants, each twin-unit ACR-1000 plant will avoid emissions of fourteen million tons of CO_2 per annum, along with large quantities of NO_X, SO_2 and other airborne pollutants.

Qualification testing, including testing for manufacturability and operability, has now started for the specific ACR-1000 design. AECL has completed the definition of the fundamental ACR technology features to achieve these targets.

The ACR-1000's technology is a blend of evolutionary development, building on the successful features of the existing CANDU fleet, and groundbreaking innovations backed up by development and qualification testing. For example, the ACR-1000 maintains the modular, horizontal pressure-tube approach for the reactor core, while adapting fuel channel

Brian McGee, Vice-President, Nuclear Laboratories. New hire breakfast at Chalk River. AECL has hired more than 900 employees in the last ten months.

materials and design features for higher temperature operation, leading to improved thermal efficiency. The fuel design, using low-enriched uranium to increase burn-up, is an innovative adaptation of AECL's CANFLEX fuel bundle, developed to increase operating margins in current CANDU reactors.

The ACR-1000 is designed to be fully modular, with pre-assembly resulting in construction time savings and final plant quality.

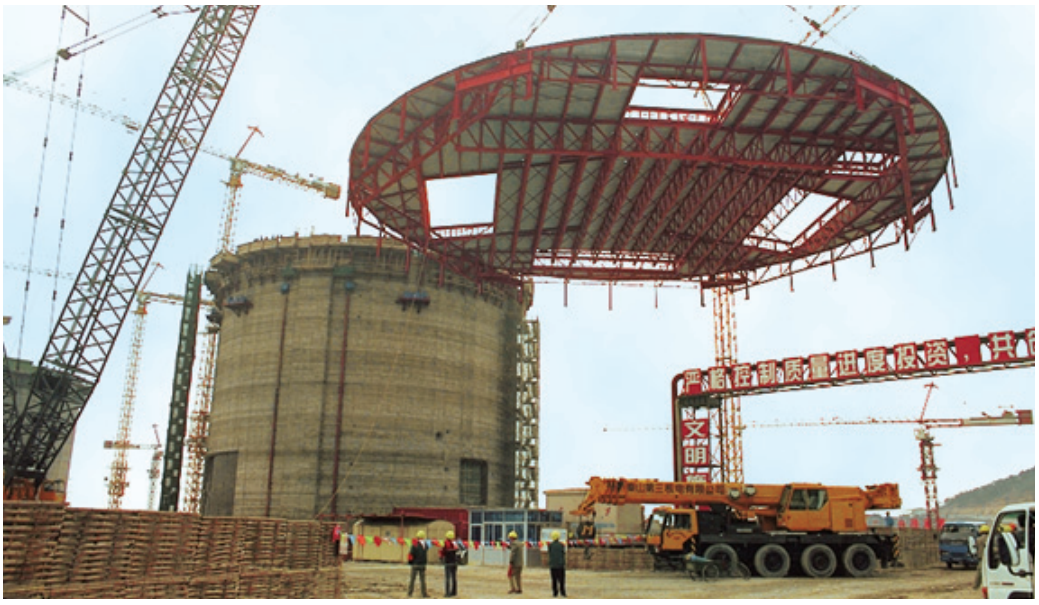
The ACR-1000 design team includes veteran nuclear utility operations and maintenance (O&M) experts, who ensure an emphasis on O&M in the design. This, together with CANDU's unique on-power refuelling capabilities, has resulted in a plant that can be operated for three years between maintenance outages – an unequalled advantage.

The ACR development program builds on AECL's unique breadth of expertise. It forms a central focus of innovation that attracts and develops top engineering and scientific talent. The program will deliver a plant design, ready for project execution, supported by a complete range of technology and delivery capability from fundamental materials R&D conducted at Chalk River Laboratories to the incorporation of project lessons learned via AECL's power plant project management team.

AECL is attracting the right people with the right experience to manage and lead. We are driving with excellence and are well prepared to deliver for today and tomorrow.

Enhancements developed through this comprehensive product development approach can also be applied to AECL's CANDU 6, including services to operating units and new build opportunities. AECL develops its technology as a continuum. Our recent experience in building reactors abroad has given us insight into how we can improve our design and construction for the ACR-1000. In turn, our innovative ACR-1000 design can contribute to the global effort to build the next iteration of reactor under the Generation IV program. For example, the ACR's proposed fuel design can accommodate increased temperature and pressure, thus resulting in higher overall plant efficiency. These refinements and their descendents may contribute to Generation IV specifications. By maintaining a continuum of technology improvement, our reactor designs evolve in manageable steps, and AECL assumes acceptable financial risks with solid commercial returns.

The ACR-1000 is designed to be fully modular, with pre-assembly resulting in construction time savings and final plant quality.



PERFORMANCE EXCELLENCE

Ken Wood, Senior Engineering Technologist, Sheridan Park. Point Lepreau retube mock-up.

This year's strong financial performance is the result of AECL's superior people, products, services and strategies, all of which have positioned the company as a global leader in nuclear technology. At the end of 2005–2006, we had a consolidated revenue backlog of $1.3 billion, approximately seven times the amount for the previous year. We are confident that the nuclear renaissance will find AECL well placed to build on this performance.

For the past 10 years AECL has been continuously building new nuclear reactors and has surpassed all major reactor vendors in completing six reactors on budget and on or ahead of schedule. These new reactors, in Korea, China and Romania have enabled AECL to keep skills sharp and current. We have an experienced pool of talent ready to meet new challenges in the marketplace. We have also developed innovations in sharing capabilities with our overseas construction partners. This year, we announced that we have joined forces with four of the world's leading nuclear technology and engineering companies to create Team CANDU, which will bring our successful international project performance and capabilities to Ontario. Each member of the team, which includes Babcock & Wilcox Canada, GE Canada, Hitachi Canada and SNC-Lavalin Nuclear, brings technical strengths,

expertise and a worldwide track record of delivering projects on time and on budget.

Team CANDU will deliver a business model in Ontario that has proven to be extremely successful abroad during the last decade. With each partner taking a share of project risk to deliver new CANDU plants on a turnkey, fixed-price basis, utility operators are relieved of traditional project risk.

Refurbishment of existing reactors is an excellent way to deliver virtually new generating facilities at low cost and short lead times. The economic value to the owner of CANDU refurbishment projects is remarkable, and AECL is hard at work on several such initiatives. Currently, we have a turnkey, fixed-price contract to refurbish the CANDU 6 reactor at Point Lepreau in New Brunswick. Engineering, procurement and site preparation are underway, laying the groundwork for the planned refurbishment shutdown in April 2008. Meanwhile, we also have a contract in place with Bruce Power to retube Bruce Units 1 and 2 as part of a larger refurbishment program at the Bruce A generating station. We are discussing proposals to refurbish CANDU 6 stations in Canada, South Korea, and Argentina.

POSITIONED TO DELIVER

In a focused effort to serve customers better, AECL is taking steps to enhance its workforce with strategic hires from the utilities sector who have senior operating experience. Bill Pilkington, Director of Technical Delivery for CANDU Services, is one example of the type of leader AECL brought in last year to ensure our service teams start thinking like operators. With close to 30 years of nuclear experience, including positions with Ontario Hydro and NB Power, Bill is helping AECL to better understand and respond to the needs of customers through the delivery of technical solutions that meet operator requirements. Bill's expertise, along with his strength as a motivator, are contributing to AECL's new services culture, which will ensure we become a supplier of choice.

Bill Pilkington, Director of Technical Delivery, CANDU Services

In 2005–2006, we made great strides in continuing to improve our customer service culture. An independent survey of domestic customer satisfaction showed significant improvement in several key areas: the number of respondents who said they were satisfied or more than satisfied with our services rose 47 percentage points in only three years. Our goal is easy to understand: our customers' success is our success and we have made a long-term commitment to support their operations.

For the past 10 years AECL has been continuously building new nuclear reactors and has surpassed all major reactor vendors in completing six reactors on budget and on or ahead of schedule.

CANDU Services, as the original equipment manufacturer (OEM) of the CANDU product line, provides ongoing quality support and services to utilities worldwide. To serve our customers better,

CANDU 6 LIFETIME CAPACITY

The CANDU 6 fleet ranks well ahead of the competition in the international marketplace with an impressive average lifetime capacity factor – the single most important measure of reactor performance – of 86%.

Name of Unit	In-Service Date	Lifetime Capacity Factor	Name of Unit	In-Service Date	Lifetime Capacity Factor
POINT LEPREAU, NEW BRUNSWICK	FEBRUARY 1983	83 PER CENT	WOLSONG 4, SOUTH KOREA	OCTOBER 1999	97 PER CENT
GENTILLY 2, QUEBEC	OCTOBER 1983	79 PER CENT	EMBALSE, ARGENTINA	JANUARY 1984	85 PER CENT
WOLSONG 1, SOUTH KOREA	APRIL 1983	86 PER CENT	CERNAVODA, ROMANIA	DECEMBER 1996	87 PER CENT
WOLSONG 2, SOUTH KOREA	JULY 1997	93 PER CENT	QINSHAN UNIT 1, CHINA	DECEMBER 2002	86 PER CENT
WOLSONG 3, SOUTH KOREA	JULY 1997	94 PER CENT	QINSHAN UNIT 2, CHINA	JULY 2003	89 PER CENT

Lifetime capacity is the percentage of time that a plant operates at its design rating.

we have trained our service teams to think like operators. We also place key personnel at senior levels to drive a services culture and to focus on becoming a supplier of choice. Our CANDU Services business accounted for $123 million in revenues in 2005-2006, an increase of 18 per cent over the previous year. We are committed to proving ourselves to our customers, and in doing so, building real value into their operations.

Noel Harrison, Engineering Physicist (left) and Peter Valliant, Metallurgical Engineering Technician, Chalk River. Assembling fuel string.

AECL's business depends on the wise application of technology from our knowledge base and expertise on new products and refinements for an energy-hungry world. As economies grow, so does the world's need for generating capacity, and that capacity needs to be affordable, reliable and emission-free. To meet such challenges, we are developing the ACR-1000, a 1,200-MW, generation III+ nuclear reactor featuring one of the most advanced designs in the world.

Last year, we met a significant milestone by confirming the fundamentals of the technology behind the ACR-1000. We researched materials behaviour and set parameters that will enable the robust ACR-1000 to meet rigorous operating conditions and customer needs. We co-operated with the CNSC as it established its evaluation criteria for our advanced reactor. The CNSC completed a report in March 2006 outlining issues surrounding ACR-1000 technology and identifying topics they wish to review in the ACR-1000 pre-licensing program. We anticipate that this review by the CNSC will indicate that the ACR-1000 reactor design can be licensed in Canada under the *Nuclear Safety and Control Act*. With the completion of this CNSC report, AECL has moved ahead to start the Basic Engineering program for the ACR-1000.

At the same time, it has been essential to understand customer operating and business requirements for the ACR-1000 to ensure that its design is customer-oriented. The reactor, for example, must be easier to operate and maintain, and thus be more economical than earlier generation CANDUs and our competitors' reactors. To achieve this, we have embedded customer-service experts with first-hand utility operations experience in the design team. These experts work hand-in-glove with the operations experts and leaders who are driving the services business.

ON TIME, ON BUDGET – AECL'S PROJECT TRACK RECORD

In-service date	Plant	Status	
1997	Wolsong Unit 2, S. Korea	On budget	On Schedule
1998	Wolsong Unit 3, S. Korea	On budget	On Schedule
1999	Wolsong Unit 4, S. Korea	On budget	On Schedule
2002	Qinshan Phase III, Unit 1, China (Turnkey contract)	Below budget	6 weeks ahead of schedule
2003	Qinshan Phase III, Unit 2, China (Turnkey contract)	Below budget	4 months ahead of schedule
2007	Cernavoda Unit 2, Romania	On Target	84% complete

SUSTAINABILITY

AECL's commitment to sustainable development starts at the top and is factored into all of its business planning activities.

In today's world of heightened concern over greenhouse gases, the advantages of nuclear are gaining more prominence. Nuclear energy is emission free, causes no acid rain, is dependable, and the technical aspects of nuclear safety are well understood. AECL has been working to strengthen its position as a leader in environmental issues. Last year we maintained our ISO 14001 environmental-management accreditation and undertook initiatives on a number of decommissioning programs that will deal effectively with past legacies. Meanwhile, we laid the groundwork for developing a safety culture throughout the company. We have begun a new era of co-operation and communication with our regulator, the Canadian Nuclear Safety Commission (CNSC). Finally, we engaged the public, building avenues of communication and, it is hoped, new levels of trust and mutual co-operation.

We have adopted three environmental objectives for our products and services: We will minimize our footprint; we will use advanced technology to minimize releases into the environment; and we will examine all aspects associated with fuel designs in future reactors such as the ACR-1000 to ensure they meet stringent environmental requirements for safe storage and disposal after use.

AECL manages nuclear legacies on behalf of the Government of Canada. Last year, in conjunction with our Shareholder, we developed a long-term strategy for dealing with these liabilities. The 70-year action plan will characterize the nature of the legacy wastes at Chalk River and address how to immobilize them in a stable form. The Government of Canada has indicated its intention to commit $520 million over five years to fund the five-year start-up phase of this strategy. This accelerated program to address long-term management of waste and decommissioning of legacy facilities will ensure that the liabilities are dealt with effectively and are not left for future generations. We will apply this protocol not only to Chalk River, but also to ongoing nuclear waste being generated at hospitals and universities across Canada. AECL also has responsibility for decommissioning Whiteshell Laboratories in eastern Manitoba, as well as three prototype reactors located in Quebec and Ontario.

Documents related to the Chalk River portion of the long-term strategy, as well as the five-year implementation plan have been tabled with the CNSC. All of these documents are available to the public. Indeed, we consult with interested parties on our progress, we encourage comments from the public, and where appropriate, incorporate their suggestions into planning.

OPERATIONAL EXPERTISE

With more than 32 years of nuclear operations experience with OPG, Brian McGee, AECL's new VP, Nuclear Laboratories, brings much weight to AECL's ongoing commitment to enhancing R&D excellence, while ensuring adherence to all regulatory requirements at its Chalk River site. Responsible for the safe operation of AECL's licensed nuclear facilities, Brian is focused on continued excellence in health, safety and the environment for the laboratory operations and on ensuring that the organization is prepared to meet all quality assurance and regulatory requirements. Brian continues AECL's enduring drive for R&D excellence to support and advance CANDU technology and to ensure that the organization's expanding decommissioning and waste management activities remain at the leading edge. Brian is also committed to strengthening dialogue with surrounding communities, customers, regulators, and other stakeholders.

Brian McGee, Vice-President, Nuclear Laboratories

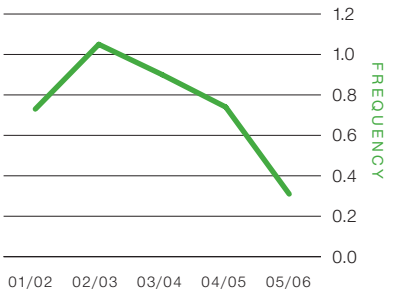
As part of AECL's public policy role we manage the low-level radioactive waste management office (LLRWMO) that addresses historic waste clean-ups throughout the country. In addition, we maintain emergency-response capabilities and expertise and are ready to respond to any incident involving radioactive materials that may happen.

Instilling a safety culture in the company is a serious business, one that not only protects the lives, health and welfare of AECL employees, our customers and their communities, but one that fosters a psychology of excellence. We believe that excellence in safety is conducive to creating a high-performance organization: in operations, in delivery of services and in development of technology.

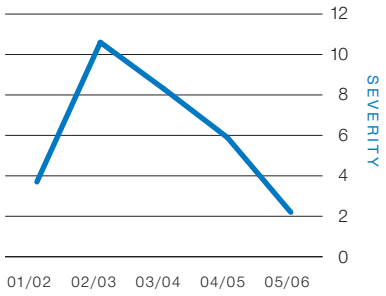
This is not a one-time exercise or a simple program of rules and regulations for avoiding incidents. It is, rather, a mentality that goes to work every day throughout the company: in research and development, in operations, in our laboratories, in decommissioning and in customer service. AECL is focusing on safety leadership through a series of workshops held in 2005–2006 at the managerial level. This year we will extend these safety-consciousness workshops to all workers. AECL strives to be an increasingly transparent organization. To that

AECL's drive toward industry best practices continues to be reflected in the ongoing reduction in the frequency and severity of our lost time injuries. Our FY 2005–2006 frequency and severity rate reduction targets (15% less than average of previous 2 years) were achieved. The launch of a new Safety Culture initiative in early 2005, including awareness training in the areas of human performance and error-free tools, contributed to our continuing performance improvements.

Safety Performance Frequency



Safety Performance Severity



Frequency = Number of Recordable Lost Time Injuries (RLTI) per 200,000 person-hours of exposure.
Severity = Number of work days lost as a result of RLTI per 200,000 person-hours of exposure.

Craig Buchanan, Metallurgical Technician, Chalk River. Optical examination of fuel materials and fuel channel components.

end, we welcomed a suggestion by residents and public-interest groups in Ontario's Renfrew County to create an Environmental Stewardship Council. The panel, which is currently being established, will be comprised of AECL staff, members of public-interest groups and members designated by locally elected councils. It will openly discuss matters of interest in operations at Chalk River, help us to improve environmental performance through community feedback, and provide us with a mechanism for two-way communications.

In an effort to increase understanding of and support for nuclear in neighbouring communities in and around where AECL and its employees are located, we launched a community speakers program last year. Through the program, trained AECL employee volunteers visit organizations and schools to address the benefits, uses and misconceptions of nuclear energy, as well as the important role it will play in ensuring a reliable, safe and affordable energy supply for the future.

AECL identified five priorities in improving and sustaining our regulatory performance and we are making good progress on each. We seek to achieve excellence in meeting regulatory requirements and in continuing to improve our regulator ratings. We seek to improve our ability to identify and act on issues before we are told to. We seek timely and effective resolution of regulatory matters and are pleased to say that we are resolving or undertaking action on all outstanding issues. We seek sustained regulatory performance. Finally, as has been the case in Renfrew County, we seek to develop an attitude of openness with all of our communities, with public stakeholders, the Shareholder and the CNSC.

AECL will continue to foster better communications with the CNSC and to be more thorough and transparent in our reporting. In that regard, the regulator's decision to open an office at Chalk River, a standard practice at major nuclear operations throughout the country, is a welcome one. It will provide AECL with another communications channel, benefiting our relations and our performance.

Furthermore, we want our stakeholders – our Shareholder, customers, communities, governments, employees and advocacy groups to have the information to understand our business. AECL is committed to integrating social, economic and environmental goals into our business planning to create a solid foundation for increasing Shareholder value. Over the past year, we have updated our supporting policies to reflect best practices with respect to governance, disclosure, environmental and social practices.

T. (Nithy) Nitheanandan, Senior Mechanical Research and Development Engineer (left), and Bob O'Connor, Materials Science Technician, Chalk River. Thermite loading of Molten Fuel Moderator Interaction (MFMI).

2005–2006 PERFORMANCE vs OBJECTIVES

Achieve Services revenue annual growth rate of 10%, and four refurbishment and two new build contracts

Strategies	Year One Measures/Deliverables	Results
Successfully negotiate and execute refurbishment and retubing contracts.	Achieve revenue and cost recoveries of $485 million.	Revenue and cost recoveries increased by $53 million to $431 million. Two major contracts signed late in year will carry forward to the coming fiscal year.
	Achieve Net Income of $11 million (excluding accretion for decommissioning liability).	Exceeded. Net income of $80 million was achieved.
	Achieve cash balance of $46 million.	Exceeded. Year-end balance of $111 million resulted from the project contracts.
	Obtain two reactor retube contracts.	Achieved with the signing of major contracts with New Brunswick Power and Bruce Power, together valued at $1.2 billion.
Achieve a CANDU 6 project replication sale.	90% of 2005–2006 project milestones delivered.	Exceeded. All contractual milestone deliverables for the year were completed for the Cernavoda 2, New Brunswick Power and Bruce Power contracts.
Complete the MMIR Project.	90% of project milestones delivered.	Completed 72% of the MMIR project milestones. On target to achieve in-service date of 2008 for the isotope reactor, MAPLE 1 and related New Processing Facility.
	Canadian Nuclear Safety Commission approval of licence renewal.	Successfully obtained two-year licence renewal.
Strengthen the product and services portfolio by developing and selling value added CANDU products and services to maximize profits.	Obtain services revenue of $117 million.	Services revenue exceeded target expectations by $6 million.
	Achieve 9% revenue growth.	Exceeded with Services revenue growth of 18%.
	Implement Services and Product development program.	Successful product development programs, including CANFLEX LVRF fuel; improved start up automation for CANDU plants; and the Fuel Handling Cable Harness have been completed.
Launch the Advanced CANDU Reactor in Ontario.	Deliver 90% of project milestones.	Exceeded expectations with 100% of Corporate milestones completed and over 90% of the deliverables achieved.
Focus on delivering quality processes to improve customer satisfaction.	Improve Customer Satisfaction by 10%.	Exceeded. The annual domestic survey indicates a 14% increase in customer satisfaction.
	Improve Quality Index by 10%.	93% of the target was achieved reflecting a 5% improvement over last year.
Access capital to invest in growth.	Resources in place to meet business requirements.	Achieved.
Make strategic acquisitions and partnerships to acquire broader capabilities and to secure the supply chain.	Retube and refurbishment projects launched on time with appropriate resources.	Achieved. The Team CANDU initiative was formed and is positioned to address the need for Ontario new builds. Members include General Electric Canada, SNC Lavalin Nuclear, Babcock Wilcox Canada, Hitachi Canada and AECL.
Attract and retain key resources through succession planning, outsourcing, partnerships and acquisitions.	Completion of milestones for project management and commercial awareness training.	Achieved. 200 staff completed project management training and a new commercial awareness program has been launched.

2005–2006 PERFORMANCE vs OBJECTIVES

AECL and nuclear power recognized as leaders in health, safety and the environment

Strategies	Year One Measures/Deliverables	Results
Encourage, communicate and support a safety culture.	Achieve a 5% reduction in amount of radiation exposure.	Achieved a 6% reduction in radiation exposure.
	10% improvement in workdays lost due to accident.	Achieved. The frequency of recordable injuries was reduced by 58%.
	Achieve a 4% training expense to payroll corporate wide.	Achieved.
	Completion of safety and compliance training requirements.	Over 50% of managers have completed the Behavioural Observation program and 84% of NLBU have completed the safety culture workshop, exceeding the year-end target of 60%.
Fulfil environmental policy and regulations.	Achieve a 5% improvement in the Environment Index.	Achieved improvement of 7%.
	Establish environmental objectives for AECL products and services.	Completed.
Continue the uninterrupted supply of isotopes.	Achieve isotope revenue of $37 million.	Isotope revenue finished the year at $35 million.
Achieve NRU License extension.	Achieve National Research Universal (NRU) capacity factor of 80%.	The NRU capacity factor to the end of March was 74%.
	Submit CNSC application and supporting documentation for removal of existing Chalk River Laboratories (CRL) site licence condition.	Achieved. The CNSC extended the operating licence to July 2006 to coincide with the CRL site licence.
Enhance the awareness of and understanding for benefits of nuclear through associations, media and with key stakeholders.	Achieve 50% public acceptance nationally in support of nuclear.	Positive gains in public opinion have been made. An Ipsos-Reid poll completed in January 2006 showed that 61% of Ontarians currently support nuclear energy.
Demonstrate linkage of nuclear technologies in new technology markets.	Demonstrate AECL leadership in nuclear power/ hydrogen synergy.	Provided essential advice to Natural Resources Canada to enable the signing of the International Generation IV Nuclear R&D agreement.

2005–2006 PERFORMANCE vs OBJECTIVES

Achieve measured progress by effectively supporting the CANDU asset life-cycle and nuclear platform obligations

Strategies	Year One Measures/Deliverables	Results
Ensure that the technology base will address Safety, Licensing and Design Basis requirements of the CANDU fleet.	Achieve a 10% improvement in the Research Effectiveness Index over 2004–2005 target.	Exceeded. The Research Effectiveness Index of 89 at the end of the year is better than the 2005–2006-plan target of 82.
	Achieve a 10% improvement in the CANDU Owners Group satisfaction index.	Achieved.
Attract and retain key R&D resources to advance capability.	Achieve 90% of targets.	100% of succession planning targets and 70% of hiring plans were completed.
	Delivery of capability maintenance program training requirements.	Completed.
Focus on Technology development and commercialization to improve customer value.	Achieve ACR and product and services development milestones.	73% of ACR R&D deliverables for 2005–2006 were completed. New product delivery requirements completed.
Demonstrate value and cost effectiveness of NLBU programs and activities.	Achieve a 15% reduction in reportable events.	Executive emphasis on encouraging the reporting of events and improving the reporting culture has resulted in higher than planned reports.
	Complete eight Continuous Business Improvement (CBI) projects with implementation plans.	The CBI programs were evaluated and subsequently two new programs were established: the NRU Operations Improvement program and the Safety Culture Improvement Initiative.
	8% improvement in the platform expenditures to revenue and funding ratio over 2004–2005.	The launch of site, regulatory and safety initiatives along with NRU performance improvement programs resulted in this target being cancelled. The expense to revenue ratio increased to 74% compared to the 2004–2005 year end ratio of 65%.
Structure the management of waste & decommissioning to ensure good governance consistent with available resources.	Achieve 90% of decommissioning plan milestones.	92% of decommissioning and waste management program milestones were achieved.
	Establish the Liability Management Unit (LMU).	The Decommissioning plan and request for funding have been submitted to the Shareholder. The LMU has been established and all key staff positions have been filled.
Reduce AECL Site Liability.	10% improvement in the Liability Reduction Index from the 2004–2005 targets.	Achieved a 17% improvement in the Liability Reduction Index.

2006–2007 OBJECTIVES

2006–2007 MEASUREMENT CRITERIA

People:

- Improve Safety performance for the frequency and severity of accidents by 10%.
- Improve Employee feedback measurement.
- >90% of Resources Plan milestones achieved.

Process:

- Quality index improved by 5%.
- On Time and On Budget delivery >90%.
- Improve environmental index by 5% over the previous three-year average.

Customer:

- Maintain Customer Scorecard results.
- Customer quality ranking of 7 or higher on 90% of completed projects.
- Achievement of customer performance improvement objectives.

Financial:

- Revenue of $596 million.
- Net Cash Outflow of $54 million.
- Profit margin at or better than budget for 90% of projects.

Five Year Objective – **Achieve leadership in our markets through performance excellence and business relationships**

Five Year Strategies

- Successfully negotiate and execute refurbishment and retubing contracts.
- Achieve new build CANDU sales in Ontario and globally.
- Continue the uninterrupted supply of isotopes and develop the business.
- Strengthen the product and services portfolio by developing and selling value added CANDU products and services.
- Focus on delivering quality processes to improve customer satisfaction.
- Broaden capabilities through recruitment, outsourcing and partnerships and strategic acquisitions.

Priority Projects

- Obtaining three additional CANDU 6 refurbishment contracts in the first two years of the plan, and meeting all commercial contract requirements.
- Meeting the requirements for new nuclear plant construction in Ontario, including launching the Generation III + Advanced CANDU Reactor.
- Continuing Isotope production and bringing into operation the new Dedicated Isotope Production Reactors and Processing Facility.
- Continuing the culture change program and improving Employee Dialogue to ensure alignment of employees with Corporate objectives.

Five Year Objective – **Demonstrate Vigilance and Leadership in Health, Safety, the Environment and Operational Excellence**

Five Year Strategies

- Encourage, communicate and lead a safety culture.
- Achieve operational excellence by exceeding environmental policy and regulations.
- Achieve NRU and Chalk River licence extensions.
- Demonstrate value and cost effectiveness of NLBU programs and activities.
- Demonstrate progress and value in the delivery of the Waste Management and Decommissioning Program.
- Work closely with NRCan in assessment of options for the future of NRU.

Priority Projects

- Renewing the Chalk River site operating licence including operation of the NRU research and isotope production reactor.
- Ensuring the uninterrupted supply of isotopes.
- Implementing the Comprehensive Waste Management and Decommissioning Plan for AECL's nuclear sites.
- Work closely with the Government of Canada on the required infrastructure investments in the national nuclear laboratory at Chalk River.

Five Year Objective – **Lead Technology Development and Application to Continuously Improve CANDU Life-cycle Performance**

Five Year Strategies

- Ensure that the technology base will address Safety, Licensing and Design Basis requirements of the CANDU fleet.
- Attract and retain key resources to advance capability.
- Focus on technology development and commercialization to improve customer value.

Priority Projects

- Developing the ACR to meet customer requirements.
- Reinvestment in the nuclear infrastructure including knowledge management.

FINANCIAL HIGHLIGHTS

Building on the recent refurbishment contracts awarded in Canada and recent new build successes in China and Romania, AECL will continue to pursue opportunities for life extension projects and new reactor sales on a global basis with a focus on countries where AECL already has a strong presence.

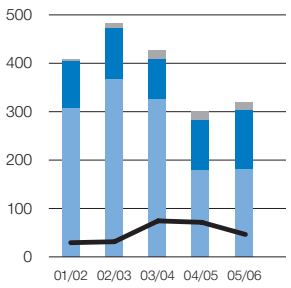
COMMERCIAL OPERATIONS

COMMERCIAL OPERATIONS REVENUE

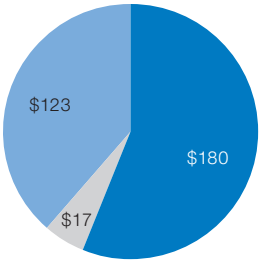
Commercial revenue increased in 2005–2006 while net income relative to sales fell. In the prior year, commercial net income included a one-time cost savings relating to reduced project warranty costs.

Within the total revenue of $320 million from Commercial Operations, exports were $183 million, contributing positively to a favourable balance of trade for Canada in 2005–2006.

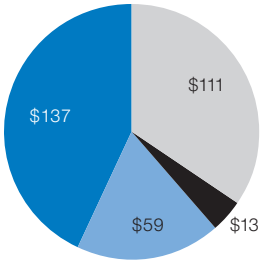
Revenue and Net Income ($ millions)



2005–2006 Revenue ($ millions) **Commercial Operations**



2005–2006 Revenue ($ millions) **By Region**

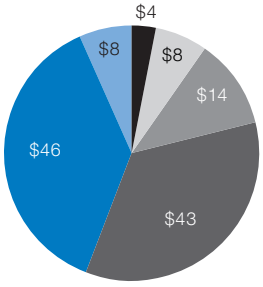


SERVICES

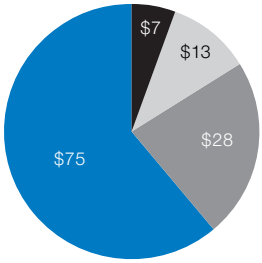
SERVICES REVENUE

The diversity of the Services' revenue base and geographic coverage provides a solid basis for future growth.

2005–2006 Services Revenue ($ millions) **By Product**



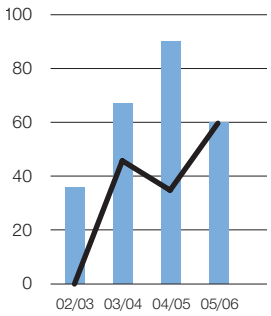
2005–2006 Services Revenue ($ millions) **By Region**



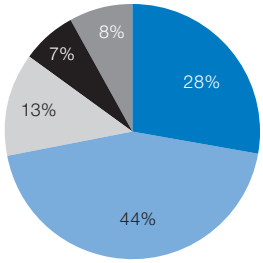
ACR

Investment in ACR product and market development declined in 2005–2006, reflecting the realignment of market strategy. AECL still attained all planned development milestones and secured funding from the Government of Canada equal to expenditures for the year.

ACR Funding and Expenses ($ millions)



ACR Expenses 2005–2006



FINANCIAL SECTION

MANAGEMENT'S DISCUSSION AND ANALYSIS

Forward-Looking Statements

This Management's Discussion and Analysis (MD&A) has been approved by AECL's Audit Committee. It provides comments on the performance of the Corporation for the year ended March 31, 2006 and should be read in conjunction with the consolidated financial statements and accompanying notes included in this Annual Report.

This MD&A contains forward-looking statements with respect to AECL based on assumptions that management considers reasonable at the time of preparation. These forward-looking statements, by their nature, necessarily involve risks and uncertainties that could cause future results to differ materially from current expectations. We caution the reader that the assumptions regarding future events, many of which are beyond the control of AECL, may ultimately prove to be incorrect since they are subject to risks and uncertainties.

Overview

AECL's business activities encompass all aspects of supporting the CANDU reactor product life cycle. This includes the design and construction of nuclear reactors and related products, services, life extension and decommissioning and waste management. In addition, AECL manages production and supply of a significant portion of the global medical isotope requirements.

On behalf of the Government of Canada, AECL also fulfills a unique public policy role in maintaining and enhancing Canadian nuclear technology to secure Canada's electricity supply requirements and manage legacy waste obligations in a safe and effective manner. These activities are partly funded by the Government of Canada and managed at our Nuclear Laboratories Business Unit (NLBU), which include CANDU-related research and development (R&D) facilities at Chalk River, Ontario and Pinawa (Whiteshell), Manitoba.

2005–2006 Highlights

- Revenue from Commercial Operations increased $19 million or 6% in 2005–2006.
- The ongoing new build project at the Cernavoda site is progressing on target with an overall project completion of 84%.
- Consolidated orders-on-hand at the end of 2005–2006 were $1,278 million (2004–2005: $190 million), reflecting two major refurbishment and retubing contracts awarded during 2005–2006.
- AECL invested $60 million in the ACR-1000 program in line with government funding support of $60 million in 2005–2006, consequently enabling the achievement of planned milestones.
- The Technology segment maintained a $39 million investment in support of the safety and performance of the CANDU fleet.
- Overall, AECL's cash position (including cash and cash equivalents, segregated cash and short-term investments) at March 31, 2006 increased to $111 million (2004–2005: $67 million), mainly due to cash generated from operating activities.
- AECL, in resolving a previous contractual dispute, signed a new agreement with MDS Nordion, relating to the long-term supply of isotopes.

Industry Trends and Background

- According to the World Nuclear Association's report on The New Economics of Nuclear Power (2005), global energy demands are forecast to exceed existing supply, consequently requiring new supply generation. In addition, new plants will be required to replace aging facilities facing retirement over the next few decades. The report also suggests that increasing pressures to move to more environmentally friendly electricity production technologies have resulted in several nations re-evaluating nuclear energy as an essential part of their future energy supply mix.
- The public is progressively acknowledging nuclear energy as safe, reliable, affordable and environmentally sustainable. According to an Ipsos-Reid survey (February 2006) conducted on behalf of the

Canadian Nuclear Association, 61% of those surveyed in Ontario support nuclear energy. Also, based on a report published in 2005 by the Nuclear Energy Institute, 70% of Americans favour nuclear energy. International concerns regarding the diversity and security of energy supply, climate change and clean air initiatives and the need for improved economics all indicate a promising future for nuclear power.

- In Canada, it is being increasingly recognized that the need for energy on the scale required cannot be met without increased nuclear power. This could be met by a combination of new builds and refurbishment of existing reactors.
- Utilities are continuing to negotiate contracts that transfer project risk to suppliers. This will promote greater accountability on project performance and facilitate cost efficiencies. This model is consistent with AECL's existing turnkey commitment on major projects.
- Nuclear related licensing requirements continue to drive a higher level of compliance.

Objectives and Strategies

To achieve its vision, AECL is focusing on three key long-term objectives:

1. Achieve leadership in our markets through performance excellence and business relationships

AECL is committed to providing full support and partnering with its suppliers and customers throughout the life cycle of nuclear power technology management. By capitalizing on the synergy provided by our technology capability, AECL provides innovative solutions in maximizing the value to both customers and the Government of Canada. Given its expert knowledge as CANDU developer, designer, builder, and services provider, and its specialized facilities, AECL is uniquely positioned to deliver quality products and services to customers.

To achieve the above objective, AECL will focus on the following strategies:

- Successfully negotiate and execute refurbishment and retubing contracts.
- Achieve new build CANDU sales in Canada and globally.
- Continue the uninterrupted supply of isotopes and develop this business.
- Strengthen the product and services portfolio by developing and selling value added CANDU products and services.
- Focus on delivering quality processes to increase customer satisfaction.
- Broaden capabilities through recruitment, outsourcing partnerships and strategic acquisitions.

2. Demonstrate vigilance and leadership in health, safety, the environment and operational excellence

To achieve its potential as an industry leader, AECL's objective is to position itself as a global leader in environmental and health-related technologies. AECL is committed to managing its nuclear R&D and waste management capabilities and related infrastructure on behalf of the Government of Canada in an effective and efficient manner to meet regulatory, safety, environmental, and technical program requirements. The health and safety of our employees, the communities we conduct business in and the safety of our products are of paramount significance in conducting AECL's business. Strategies are developed and deployed to ensure the operations at all AECL facilities are carried out to meet and exceed the standards required by applicable regulations.

The strategies to achieve this objective are to:

- Encourage, communicate and lead a safety culture.
- Accomplish operational excellence by enhancing environmental performance.
- Achieve licence extensions for the Chalk River Laboratories (CRL) including the National Research Universal (NRU) reactor.
- Demonstrate value and cost effectiveness of the NLBU programs and activities.
- Obtain sustainable funding for the refurbishment of CRL.
- Demonstrate progress and value in the delivery of the Waste Management and Decommissioning program, which has the purpose of reducing and, ultimately, discharging obligations relating to the nuclear legacy liabilities at AECL sites.

3. Lead technology development and application to continuously improve CANDU life cycle performance

AECL ensures that its skills and facilities support the design and licensing basis for domestic and international customers over the life span of all CANDU reactors. This is the type of R&D that is typically performed in national government funded nuclear laboratories in other countries, and not usually by nuclear vendors who focus on commercial and applied development work that leads directly to products and services. AECL is unique in that it fulfills both the national laboratory function and the reactor vendor role. This integrated capability ensures a more effective transfer of technology from the NLBU to commercial products and services. Ongoing investment and leveraging of our R&D and waste management capabilities advances AECL's capability to perform R&D while providing the ability to address public policy requirements.

The strategies to achieve this objective are to:

- Ensure that AECL's technology infrastructure, encompassing nuclear technical knowledge, tools and facilities developed over a period of sixty years will address ongoing safety, licensing and design basis requirements for the entire CANDU fleet.
- Attract and retain key resources to advance capability.
- Focus on technology development and commercialization to improve customer value.

Key Success Factors

Customer Commitment

Commercial success is positively correlated to customer satisfaction. AECL achieves this through delivering on contractual requirements, providing innovative economical products and services and continued customer support. AECL's demonstrated history of successfully delivering CANDU projects on time and on budget reinforces expected performance on existing and future contracts. AECL continues to utilize its R&D capability to deliver high quality economical products and services and provide continued innovative customer support and CANDU expertise.

CUSTOMER SATISFACTION RATING IMPROVED SIGNIFICANTLY IN 2005–2006, THE THIRD CONSECUTIVE YEAR OF IMPROVEMENT

Public Perception of Nuclear Energy

Critical to AECL's long-term success, is recognition by the public of the benefits of nuclear energy. AECL is committed to an open and honest two-way communication that is timely and relevant to the concerns expressed by the Canadian public. We are convinced that through effective communication, the public will increasingly realize that the CANDU nuclear option is one that is truly Canadian, excellent and safe by world standards and that it should be sustained for the benefit of all. AECL's strategies include continued investment in R&D to preserve the excellent performance of the CANDU fleet. This, in turn, is expected to increase the output of economic clean energy to displace coal generation and meet growing demand.

AN IPSOS-REID POLL FOUND THAT 61% OF PEOPLE IN ONTARIO, CANADA SUPPORT NUCLEAR ENERGY

Research and Development (R&D)

AECL's ability to capitalize on development and utilize intellectual property in a timely manner is crucial to its future commercial success. Strong technical competencies provide a firm base to develop and produce new products and services and cost effective solutions to enhance the benefits, quality and value to our customers. The large and growing reservoir of technology that exists within the R&D program can be drawn upon for a wide range of commercial activities. The development of the Advanced CANDU Reactor (ACR-1000), which is expected to substantially reduce capital costs and construction time, is a significant cornerstone of the R&D capability. The ACR-1000 is poised to position AECL as a major competitor in next generation reactor technology. AECL measures its R&D performance based on an index, which is used by the Government of Canada in assessing excellence in science and technology. The index is aligned and weighted based on several factors including: corporate relevance, scientific quality and merit, impact and evidence of results, commercialization, and workplace of choice.

R&D EFFECTIVENESS INDEX IMPROVED TO 89 OUT OF 100, BETTER THAN PLANNED

Project Management Skills

Complementary to the R&D capability are contracts structured to deliver value and timely implementation through effective project management. AECL's Commercial Operations has a strong foundation in managing major projects and ensuring that consistent, effective project management resources, systems and procedures are applied to all such projects. This business segment is the base for project management experience and resources, providing training and procedures in project applications and developing staff with project management skills and commercial acumen. This foundation stems from the completion of highly successful projects in overseas markets over the past few years, which were delivered on time and on budget and from the major refurbishment projects currently underway.

THE LAST 6 MAJOR NEW BUILD PROJECTS HAVE BEEN COMPLETED ON TIME AND ON BUDGET

Capability to Deliver Results

World Class Product

AECL has developed and commercialized a highly efficient world-class technology, the CANDU reactor, which is operational in seven countries around the world. The performance of the CANDU 6 fleet, with its lifetime 86% capacity factor, effectively demonstrates the competitive performance of the reactor, when compared to similar reactors worldwide. At present, nuclear power is supplying close to 15% of Canada's and over 50% of Ontario's electricity needs. The CANDU design has proven to be safe, economic and reliable over the past four decades of operation. An important competitive advantage of the CANDU design is the capability of on-power refuelling, enabling flexible planning of scheduled maintenance. AECL has committed itself to continual improvement to advance and expand its products and processes.

CANDU 6 REACTORS HAVE PERFORMED WITH AN 86% LIFETIME CAPACITY FACTOR

Partnerships

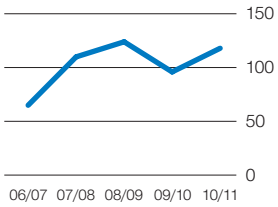
AECL's strength lies in its ability to retain and advance technical knowledge related to nuclear activities and manage both commercial and non-commercial projects. Strategic alliances with both commercial enterprises and research establishments ensure AECL's capability to grow. Agreements with large global companies, notably Team CANDU (announced in March 2006) that is comprised of

SNC-Lavalin Nuclear, General Electric Canada, Hitachi Canada, and Babcock & Wilcox Canada are in place to enable AECL to meet customers' demands and compete in an effective manner. These alliances are essential to mitigating commercial risks associated with project execution and enhancing market and profit potential for AECL, its partners and customers.

Government of Canada Support

Government support, at both the federal and provincial levels, has greatly assisted the development and success of the Canadian nuclear industry to date. In particular, current government funding supports AECL's public policy mandate. The government currently funds $104 million a year, or about 50%, of the ongoing nuclear R&D program. The remainder is funded by commercial business activity performed by the Technology segment of AECL's business and by profits from Commercial Operations. The government also provides funding support for the development of the ACR-1000, which is seen to be important in meeting future energy demand requirements in Canada. The amount of funding for the ACR-1000 varies each year and is approved annually based on market conditions and business economics. Furthermore, the Government of Canada supports CANDU technology at a high level internationally, contributing to international R&D alliances. Government investment and support in and through AECL has been leveraged to develop an entire nuclear industry. Continued support will help safeguard Canada's investment in the industry and will maintain nuclear as a viable energy option. The Government of Canada has indicated its intention to commit $520 million in funding for the decommissioning and waste management program, and a memorandum of understanding is currently being negotiated with Natural Resources Canada (NRCan) that will provide AECL with funding to implement the plan. This will allow AECL to execute its scheduled program activities over the next five years, in accordance with its decommissioning plan.

LMU 5 Year Projected Waste Management and Decommissioning Expenditure ($ millions)

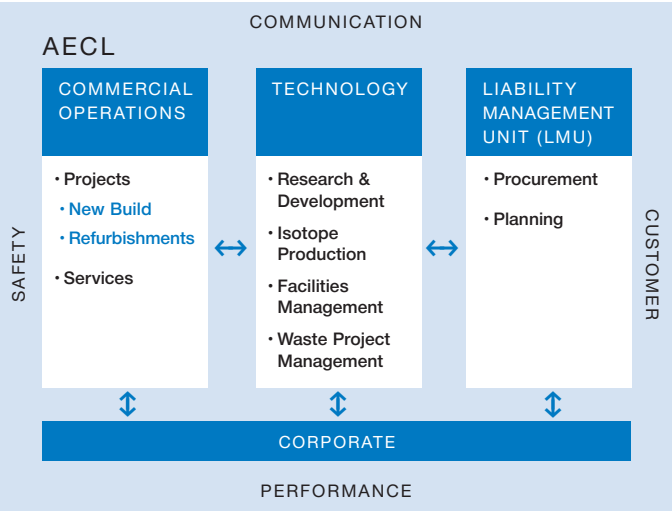


Research and Development (R&D) Infrastructure

AECL maintains a significant R&D infrastructure that supports the existing CANDU fleet and develops new technology. This infrastructure provides AECL with a resource critical to its long-term success and a significant competitive advantage. AECL's R&D infrastructure also contributes to deliver solutions that support the safety and performance of the entire fleet of CANDU reactors, assisting the fleet to exceed international standards and consequently maintaining the credibility of the industry. The key to the long-term assurance of nuclear technology is to maintain an effective R&D infrastructure. Sustained investment in such infrastructure will secure AECL's capability to deliver results in advancing Canada's nuclear option.

Organization

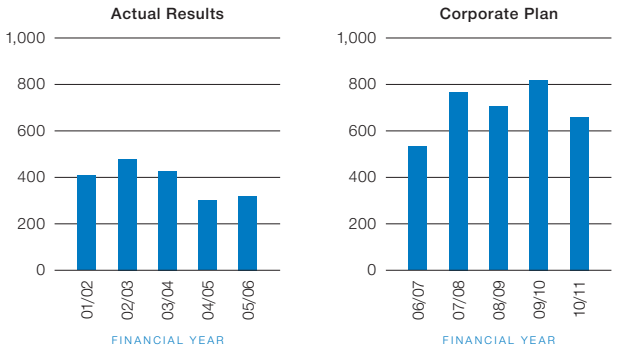
AECL is one of Canada's largest high-tech companies with around 4,000 employees comprising of approximately 3,000 highly skilled engineers, scientists and technical professionals in a wide range of technical disciplines. The optimum use of its human resources is another element essential to the achievement of AECL's corporate objectives. To this end, AECL develops and maintains a working environment that will effectively attract, retain, develop and motivate competent, appropriately skilled employees. Top scientific, engineering and technological talents, as well as broadly experienced managerial and business personnel are essential to its long-term success. In order to effectively carry out its objectives, AECL has reorganized its financial reporting environment into business units under three distinct business segments, each with bottom line or expense target accountability. Furthermore, fundamental programs to achieve changes in AECL's culture have resulted in improved customer satisfaction and AECL's delivery process. In the coming year, the Corporation will accelerate an existing change management program in order to drive excellence throughout the organization and deliver on commitments. We will focus on the four critical areas that will help AECL to achieve breakthrough results: safety, customer satisfaction, performance excellence, employee dialogue and communication.



Financial Review

AECL organizes its business activities and evaluates its financial results through three business segments with the objective of facilitating greater transparency in financial reporting and accountability for program objectives in accordance with good governance. Each segment is charged to achieve its financial goals as established in the Corporate Plan submitted and approved by the Shareholder at the beginning of the fiscal year.

Commercial Operations Revenue ($ millions)



The Commercial Operations segment is responsible for two lines of business: Projects and Services. Projects include new build and refurbishment projects, together with related project management services, equipment procurement and sale of heavy water. The services business includes a full line of engineering and technical products and services that support operating CANDU plants and improve customer productivity and competitiveness. Commercial Operations revenue over the past five years has been significantly impacted by generally lower business activity and the completion of several new build projects. However, the AECL Corporate Plan over the next five years reflects a significant increase in revenue and business activity through refurbishment and retube contracts and new build projects. This is supported by AECL's current orders-on-hand of $1,278 million and energy demand forecasts.

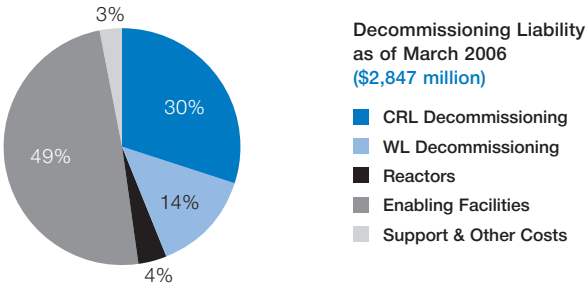
The Technology segment develops new reactor technology and supports the safety, licensing and design basis for the life cycle of the CANDU product set and other Canadian nuclear technology. This business segment also manufactures and sells medical isotopes, constructs isotopes production facilities, and provides waste management and decommissioning services. An important part of Technology's mission is to carry out the Government of Canada's policy mandate in support of Canadian nuclear technology and industry through its technology infrastructure, which includes nuclear laboratories and facilities. AECL fulfils the Government of Canada's policy mandate through:

- Supporting continued and reliable production of 15% of Canada's electricity in a safe and effective manner.
- Supporting and maintaining nuclear energy as a credible alternative source of clean electricity generation.
- Producing medical isotopes for distribution globally.
- Representing Canada internationally with respect to nuclear treaties and scientific matters.

AECL'S CONTRIBUTION TO THE GOVERNMENT OF CANADA'S PUBLIC POLICY

SAFE PRODUCTION OF ELECTRICITY	CLEAN AIR	MEDICAL ISOTOPE PRODUCTION	INTERNATIONAL SCIENTIFIC REPUTATION

The Liability Management Unit (LMU) manages the waste management and decommissioning program, and oversees funding received from the Government of Canada for the program. This liability has arisen from a wide variety of sources, including activities before AECL was incorporated, wastes received from universities, medical facilities, government and industry from across Canada, and R&D in support of Canada's nuclear power program. In addition, the LMU operates the Low-Level Radioactive Waste Management Office (LLRWMO) on a cost-recovery basis for NRCan.



Key Financial Performance Indicators

AECL regularly evaluates its financial performance using key financial indicators such as: revenue and orders-on-hand, level of funding available, net income by business segment and by business unit, consolidated net income, gross margin by project, resource utilization factor, selling, general and administrative (SG&A) expense to revenue and funding ratio, cash generated from operating activities, cash position and working capital.

Summary Of Key Financial Performance Indicators

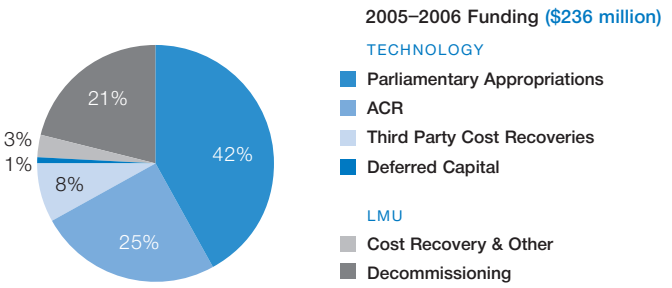
($ millions)	*2005–06*	*2004–05*
Revenue		
Commercial operations	**$ 320**	$ 301
Technology	**87**	55
Total revenue	**$ 407**	$ 356
Orders-on-hand	**$ 1,278**	$ 190
Funding		
Technology	**$ 180**	$ 153
Liability management unit	**56**	47
Total funding	**$ 236**	$ 200
Net income (loss) by business segment		
Commercial operations	**$ 47**	$ 72
Technology	**33**	(106)
Liability management unit	**(75)**	(1,807)
Total net income (loss)	**$ 5**	$ (1,841)
Other		
SG&A expenses to revenue and funding ratio	**18.0%**	18.5%
Cash generated from (used in) operating activities	**$ 56**	$ (50)
Working capital	**(51)**	(4)
Total assets	**$ 1,054**	$ 863

Revenue

Commercial revenues from all business segments increased to $407 million in 2005–2006 from $356 million in 2004–2005 reflecting new refurbishment and retubing contracts, offset by lower revenues on major projects nearing completion. In addition, following the successful resolution of a contractual dispute with MDS Nordion, AECL recognized $33 million of previously deferred revenue. The customer orders-on-hand as of March 31, 2006 totalled $1,278 million (2004–2005: $190 million), reflecting the new refurbishment and retubing projects.

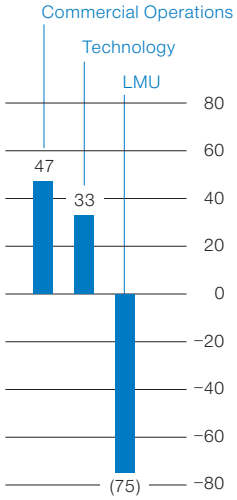
Funding

Funding is comprised of government appropriations, decommissioning funding, cost recoveries, and deferred capital funding. In 2005–2006, AECL received funding for the development of the ACR-1000, R&D, and site operations at CRL. Decommissioning funding arises on



sales of government funded heavy water. Proceeds on these sales are segregated and used for decommissioning activities within the LMU. Cost recoveries represent common development programs under cost-sharing arrangements with domestic CANDU utilities. Total funding increased to $236 million in 2005–2006 (2004–2005: $200 million), mainly as a result of additional support for ACR-1000 development.

2005–2006 Net Income (Loss) ($ millions)



Net Income (Loss) by Business Segment

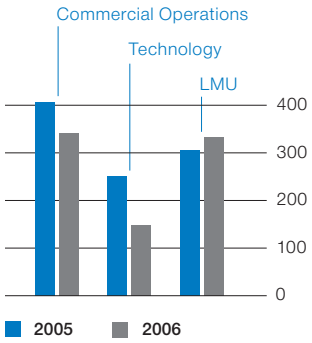
Commercial Operations is managed with revenue growth and profitability as its primary financial goals. Over the past five years, Commercial Operations have contributed net income totalling $256 million, including $47 million in 2005–2006. Technology generated a loss from operations of $28 million during the year which was offset by a one-time gain of $61 million on reversal of previously accrued project losses, and legal provisions for the previous isotope supply agreement with MDS Nordion. Including this gain, the Technology segment is reporting a net income of $33 million in 2005–2006. The Liability Management Unit (LMU) reported a net loss of $75 million, primarily in recognition of current year accretion expenses of the decommissioning liability. The accretion expense represents an increase in the net present value of the decommissioning liability due to the passage of time. With the net loss in LMU, the Corporation reported a net income of $5 million for the year.

Other

The ratio of SG&A expenses to revenue and funding are lower than the previous year, in spite of higher business development requirements and additional costs in support of the execution of new major projects. AECL continues to monitor and maintain an appropriate balance between revenue, funding and SG&A expenses, while sustaining an adequate level of selling and marketing activities to achieve growth.

Successful completion of milestones in major new projects and higher net income have led to $56 million in cash generated from operating activities compared with an outflow of $50 million in 2004–2005.

Assets by Business Segment (Excluding Cash) ($ millions)



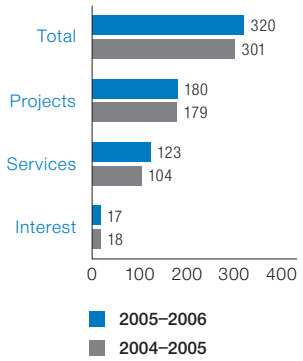
Total assets as at March 31, 2006 amounted to $1,054 million, an increase of $191 million from 2004–2005. Increased project milestone payments and business volumes have led to increases of $44 million in the cash position (including short-term investments) and $60 million in accounts receivables. In addition, as a result of settling the dispute with MDS Nordion, the Corporation acquired $44 million of inventory relating to isotope production, and has invested $47 million to complete construction of the Maple reactors.

Commercial Operations

Commercial Operations are responsible for sales, marketing, customer relations and delivery of AECL's commercial products and services to its CANDU customers. The highlights in 2005–2006 included the award of two major contracts: from New Brunswick Power (NBP) for the refurbishment of the CANDU plant at Point Lepreau and from Bruce Power for retube work on the CANDU reactors at Bruce A units 1 and 2. These projects will generate clean, reliable and affordable base load electricity, which is crucial to the security of Canada's electricity supply. The value of these two contracts to AECL totals approximately $1,170 million. The majority of the financial benefits will be reflected in future years, with

mobilization of resources underway in the current year. Nevertheless, revenue from project start-up in the refurbishment business provided diversity in the revenue base and helped in offsetting the impact of reduced activities in the new build business, reflecting completion or near completion of ongoing projects. The economics of refurbishing CANDU reactors and their environmental benefits are compelling and AECL expects further refurbishment projects in Canada and abroad. Apart from the refurbishment and retube business, our service business experienced important growth in 2005–2006 with increased activities in both Canadian and international markets. Against this background, revenue from Commercial Operations increased to $320 million from $301 million in the previous year.

Commercial Operations Revenue ($ millions)



Notwithstanding the revenue improvement, net income was reduced to $47 million from last year's level of $72 million. In the previous year, the Corporation reduced its expectations for costs related to warranty and other obligations on projects that were successfully completed or near completion, resulting in higher income.

Projects

The key business drivers underlying the Projects business are:

- Executing projects on time and on budget by employing AECL's unique expertise and rigorous quality process;
- Meeting contract specifications and customer requirements;
- Developing strategic partnerships to increase market share; and
- Supporting innovative contractual and financing arrangements.

Revenue from the Projects business unit increased to $180 million (2004–2005: $179 million), reflecting a reduction of activity on projects nearing completion, offset by the impact of the commencement of new refurbishment contracts.

The Projects business has a proven track record in successfully managing major projects over the past decade in China, Korea and Romania. This success was further enhanced in the past year with the award of two refurbishment contracts, which endorses AECL's capability and expertise in the refurbishment business.

Going forward, AECL is pursuing CANDU new build opportunities in China and Romania as well as potential new markets in the U.S. and U.K. In Canada, the potential for new builds is increasing and AECL is well positioned to enter this market with its CANDU 6 or the new ACR-1000 in provinces such as Ontario, Alberta and New Brunswick. In the refurbishment market, the CANDU 6 units in Wolsong (Korea), Gentilly (Québec, Canada) and Embalse (Argentina) are all facing life extension decisions in the near future and AECL is aggressively pursuing these opportunities, in addition to new opportunities with Bruce Power and Ontario Power Generation in Ontario.

Services

The business drivers underlying the Services business are to meet our customer needs in improving their production capacity, increasing operating safety and optimizing reactor performance. Services business strengths include CANDU technical expertise, product development, emergency response, and other unique specialist capabilities.

Revenue from the Services business grew 18% to $123 million, reflecting an increase in the sale of engineering services and commercial products to both domestic and international customers. An expanded portfolio of technology-based products contributed to this growth, specifically the sale of Emergency Core Cooling (ECC) Strainers technology in Europe, improved steam generator tube cleaning technology and the licensing of Low Void Reactivity Fuel (LVRF) in Canada. The ECC Strainers provide flexibility of design, allowing the technology to be custom-fit within existing plant space. Both the LVRF and improvement of steam generator performance are examples of delivering on the Services mandate of improving the performance of operating CANDU plants.

In the past year, the Services business continued to strengthen its market position through gaining and maintaining preferred supplier status with several customers, improving project delivery through implementing a more rigorous project management system and an improved quality assurance process to facilitate effective management and control of project costs. In addition, new markets were entered into, such as those in France and the U.S., with the Strainers product line. Following successful product sales in Europe last year, AECL was awarded four multi-million dollar contracts during the year, thereby increasing sales in Europe as well as extending sales of safety products into nuclear markets in the U.S. In addition, an improved steam generator tube cleaning technology was implemented at Bruce Power, which increases the thermal efficiency of aging reactors and significantly increases their output.

The Services business, in conjunction with the Technology segment is continuing to capitalize on market opportunities for safety and performance technologies, products and services in Europe, the U.S. and Asia. Going forward, Services expects significant growth from refurbishment work over the next few years. We will be increasing our investment to increase our portfolio of products and services with the objective of improving CANDU reactor performance. In addition, we will be developing strategic partnerships to leverage strengths and increase our ability to deliver results.

Technology

The main mandate of the Technology business segment is to provide and enhance the safety, licensing and design, technology-basis for CANDU through R&D and innovation. Activities include managing the nuclear laboratories at Chalk River and Whiteshell, production of isotopes, construction of isotope facilities, and development of ACR and other new technologies. The financial goal of this business segment is to manage with specific bottom line targets within committed funding levels. Funding is derived from federal appropriations and, to a lesser extent, from cost-sharing agreements with Canadian provincial utilities. The Technology segment also performs revenue-generating activities, which contribute to the overall funding of the R&D program. Revenue-generating activities, which comprised of the manufacture and sale of medical isotopes and commercial R&D work, are undertaken for profit.

Technology

($ millions)	***2005–06***	*2004–05*
Revenue	**$ 87**	$ 55
Funding		
Nuclear laboratories	**120**	118
ACR-1000	**60**	35
Total funding	**$ 180**	$ 153
Expenses		
Nuclear laboratories*	**235**	224
ACR-1000	**60**	90
Total expenses	**$ 295**	$ 314
Net income (loss)		
Nuclear laboratories*	**$ (28)**	(51)
Gain on reversal of provisions	**61**	
ACR	**0**	(55)
Net income (loss)	**$ 33**	$ (106)

*Includes isotope supply and related expenditures.

Within the Technology segment, commercial revenue increased to $87 million from $55 million in 2004–2005. The increase reflects settlement of contractual issues with MDS Nordion resulting in a one-time adjustment to isotope revenue. This revenue was previously deferred in the balance sheet as a result of a payment dispute. Excluding this item, revenue is consistent year over year as the volume of isotopes produced in 2005–2006 was comparable with the previous year. The reliability rate for isotopes produced from the NRU reactor remained at a high level of 96% throughout the year while the availability of the reactor was consistent with the previous year.

Total funding in support of Technology activities for 2005–2006 was $180 million compared with $153 million in the previous year. Funding is comprised of appropriations, cost recovery from third parties and deferred capital funding from appropriations received in prior years, which are used to offset related amortization.

Within the total funding, Government of Canada appropriations were $160 million; $60 million for ACR-1000 support, and $100 million for Nuclear Laboratories support, compared with $35 million and $99 million, respectively, in the previous year. Cost recovery from third parties was $18 million compared to $15 million in 2004–2005, representing the CANDU Owners Group (COG) funding support for CANDU safety, licensing and design work. A primary reason for the increase is the ongoing examination of pressure tubes from the Canadian CANDU stations under a five-year agreement signed with the utilities in 2004. Amortization of deferred capital funding declined to $2 million (2004–2005: $4 million), attributable to fully amortizing a significant number of government funded assets during the year.

Technology Funding

($ millions)	***2005–06***	*2004–05*
Funding		
Parliamentary appropriations	**$ 160**	$ 134
Cost recovery from third parties	**18**	15
Amortization of deferred capital funding	**2**	4
Total funding	**$ 180**	$ 153

Basic engineering and development activities for the ACR-1000 continued to progress on target during the year, with reported operating expenditures of $60 million completely offset by government funding. In the previous year a $55 million net expense was reported resulting from a lower level of government funding at $35 million and higher expenditures of $90 million, required to achieve committed business development milestones.

Progress continued on the construction of the isotope production and related facilities for the long-term isotope supply agreement contract with MDS Nordion. These facilities designed solely to produce isotopes are "one-of-a-kind" projects, being the first reactors worldwide to be dedicated for such purposes. Contractual issues were settled through a voluntary mediation process during the year. A new agreement was signed with MDS Nordion, in the latter part of the year, aligning the interests and strengths of AECL and the customer with a view to improve the long-term prospects of the existing isotope supply arrangement.

Under the new agreement, AECL acquired beneficial ownership of the facilities in contrast to an outright sale to MDS Nordion in the previous agreement. As a result, the accrued future project losses and related expenses previously provided for were reversed in the current year. This contributed a net gain of $61 million to the Technology segment's operating results. In exchange for the beneficial ownership of the facilities, AECL made a payment of $25 million, which was capitalized as part of property, plant and equipment in the balance sheet and acquired $44 million in related isotope supply inventory. In addition, future project completion costs and ongoing operating costs are to be incurred by AECL. In return, AECL will receive a share of net revenues from isotopes produced over a 40-year period under the agreement.

CRL currently produces approximately 60% of the world's medical isotopes used in the diagnosis and treatment of life-threatening medical conditions. The isotope production activities provide a significant health benefit and an important contribution to the Canadian and international nuclear medicine business. Medical isotopes, which include Molybdenum-99 and Cobalt-60, among others, are used to treat an estimated 68,000 people daily.

At the NLBU, higher infrastructure expenditures were incurred at the CRL site in 2005–2006. Expenditure related to the NRU Improvement Initiative resulted in a total charge of $7 million for the year. The initiative was launched in June 2005, to ensure improved operations and maintenance in meeting Canadian Nuclear Safety Commission (CNSC) requirements. In addition, a charge of $12 million was recognized for the future disposal of current nuclear waste generated, reflecting the Canadian Institute of Chartered Accountants (CICA) accounting recommendations on asset retirement obligations adopted in the previous year.

As a part of the Enterprise Risk Management process, AECL completed an assessment of the appropriate level of federal support for infrastructure renewal. Management's recommendation will be submitted to NRCan in the year now in progress. If approved, this will provide a more robust financial framework within which to plan and execute infrastructure improvement and compliance programs.

Overall, the Technology segment reported a net income of $33 million in 2005–2006 compared with a net loss of $106 million in the previous year. This reflects lower ACR-1000 net expenses and a net gain attributable to the settlement of contractual disputes with MDS Nordion in respect of the isotope supply activities. This gain largely offset the higher site infrastructure expenditures incurred by NLBU.

The future outlook for the Technology segment is expected to continue in the current direction. Key initiatives include:

- Maintaining and enhancing the safety, design and licensing basis of all CANDU reactors.
- Supporting public policy for nuclear technology.
- Developing pre-commercial CANDU technology.
- Preserving capability and expertise needed to address emerging issues.
- Completing ACR-1000 commercialization.
- Participation in the Generation IV Technologies.

Liability Management Unit (LMU)

The mandate of LMU is to manage AECL's and the Government of Canada's waste management and decommissioning program. The program has a long-term focus of safely addressing nuclear facility liabilities and managing associated waste. Facilities include those acquired from the early years of Canada's nuclear program, prior to the creation of AECL in 1952. Program activities include the stabilization of shutdown facilities, dismantling, decontamination, residual waste storage and disposal. These activities will result in major construction programs associated with enabling facilities and waste storage activities. The program is designed to achieve health, safety and environmental protection objectives in accordance with CNSC regulations. The LMU maintains formal decommissioning plans that guide the execution of the program to address AECL's decommissioning obligations in the future. The short-term plan is based on periodic reviews of the program's priorities, taking into account critical decommissioning and waste management activities based on environmental and other risk factors. The financial objective for LMU is to achieve various planned milestones within the funding level established in the Corporate Plan.

LMU

($ millions)	***2005–06***	*2004–05*
Government and Other Funding	**$ 56**	$ 47
Expenses	**(131)**	(1,854)
Net loss	**$ (75)**	$ (1,807)

Funding for decommissioning and waste management activities for 2005–2006 was derived from the net proceeds received for the lease or sale of government funded heavy water inventory under a funding arrangement with the Government of Canada. That agreement expired on April 1, 2006 and discussions are currently underway with respect to the treatment of funds received through ongoing heavy water business activities. Efforts to obtain funding required in support of the decommissioning and waste management program have resulted in the Government of Canada indicating its intention to commit $520 million in funds. A memorandum of understanding is currently being negotiated with NRCan, that will provide AECL with funding to implement the plan. These funds are required to meet costs associated with scheduled program activities over the next five years.

Progress on activities over the past year included continuation of two major waste management projects with the objective of providing long-term waste management solutions for safe storage of radioactive liquids and used fuel wastes. The LMU has evaluated the design and construction options for the Liquid Waste Transfer and Storage Project and prepared a Technical Scope of Work for tendering retrieval and transport equipment. The LMU has also received internal approval of its safety assessment document and an internal endorsement of its environmental assessment report for the Fuel Packaging and Storage Project. These two major projects are expected to be commissioned for use in late 2008 and 2010, respectively. Other activities included the systematic dismantling of redundant and aging experimental facilities and buildings as well as the ongoing monitoring and surveillance of facilities no longer in operation at CRL, Whiteshell Laboratories (WL) and other sites. Within these activities, approval has been obtained from the CNSC for the removal of the water from the NRX Used Fuel Storage Bays with the project expected to commence in early 2006.

Work supplied on a cost-recovery basis progressed well throughout the year. The Low-Level Radioactive Waste Management Office (LLRWMO) submitted a revised draft Environmental Assessment

Study Report (EASR) to the responsible federal authorities on the Port Hope Project in Ontario. The Port Granby Project, located in the Municipality of Clarington, Ontario, is also progressing well with the completion of a draft EASR expected early in 2006–2007.

Activities undertaken within the LMU resulted in a net loss of $75 million. This reflects expenses of $131 million, including accretion expense of $144 million and $7 million related to the operating cost of the LLRWMO. Partially offsetting this was an adjustment of $20 million to the decommissioning and waste management liability and $56 million funding received during the year. The accretion expense represents an increase in the net present value of the decommissioning liability due to the passage of time.

Consolidated Results

Excluding the loss on decommissioning activities, earnings from core AECL operations were $80 million compared to a loss of $34 million in the previous year. After absorption of the decommissioning activities net loss, AECL reported a net income of $5 million compared with a $1,841 million net loss in the previous year. Last year's losses were caused principally by an increase in the decommissioning liability in recognition of the acceleration in timing of the decommissioning program, additional waste management facility costs, and the adoption of CICA recommendations on asset retirement obligations.

Net Income (Loss)

($ millions)	***2005–06***	*2004–05*
Commercial Operations	**$ 47**	$ 72
Technology	**33**	(106)
Liability Management Unit	**(75)**	(1,807)
Net income (loss)	**$ 5**	$ (1,841)

Comparison with Corporate Plan

Compared with the Corporate Plan, actual earnings from Commercial Operations were lower. This reflected contract effective dates for the two refurbishment and retubing projects occurring later than planned due to slower than anticipated provincial government approvals. Consequently, this caused the shortfall of revenue against plan to be deferred to subsequent years. Nevertheless, project activities were accelerated towards the end of the fiscal year, with good progress being made against contractual milestones. Technology reported a profit this year against a loss in the Corporate Plan, largely as a result of a reduction in ACR-1000 expenses and a significant gain reported for the isotopes related activities reflecting the settlement of contractual issues with MDS Nordion. These gains provided an offset to increased infrastructure and operational costs to meet regulatory requirements at the CRL. The LMU generated a net loss of $75 million attributable to the impact of the change in the decommissioning and waste management liability. The Corporate Plan assumed no such change as the financial impact of the revised decommissioning and waste management plan was uncertain at the time the Corporate Plan was established.

Net Income (Loss)

	2005–2006	
($ millions)	*Actual Results*	*Corporate Plan*
Commercial operations	**$ 47**	$ 52
Technology	**33**	(41)
Liability management unit	**(75)**	–
Net income	**$ 5**	$ 11

Cash Flow and Working Capital

In 2005–2006, AECL generated cash from operating activities of $56 million compared to an outflow of $50 million in the previous year. The significant improvement was principally a result of the receipt of milestone payments from customers on new projects, improved receivables collection from ongoing projects, and sufficient funding of ACR-1000 development. In 2004–2005, lower business activities and a $55 million funding shortfall for the ACR program gave rise to the net cash outflow of $50 million. The Corporation's cash receipts from customers reflects a $170 million increase in advances, which were received on achieving specific milestones for the retubing and refurbishment projects. Partially offsetting these are increases in cash paid to suppliers and employees, which reflect an overall increase in activity within the Corporation and higher staffing levels, required to deliver on major projects and achieve higher services revenue. Within operating activities, funds used for decommissioning and waste management include a $2 million scheduled deposit to the Nuclear Waste Management Organization (NWMO) trust fund, held by AECL on behalf of the NWMO. As at March 31, 2006 the cumulative total for the fund including interest was $17 million, comprised of an initial $10 million deposit in November 2002 and subsequent annual deposits of $2 million on the fund's anniversary date. The funds are deposited to meet the requirements of the *Nuclear Fuel Waste Act* in respect of the long-term management of nuclear fuel waste in Canada, and the deposit amounts are expected to continue at the same level in the future.

Sources and Uses of Cash

($ millions)	***2005–06***	*2004–05*
Cash from (used in) operating activities	**$ 56**	$ (50)
Cash from (used in) investing activities	**(50)**	5
Cash from (used in) financing activities	**43**	(1)
Increase (Decrease)	**49**	(46)
Balance at beginning of year	**61**	107
Balance at end of year	**$ 110**	$ 61
Balance Sheet		
Current assets	**$ 265**	$ 160
Current liabilities	**316**	164
Working capital	**$ (51)**	$ (4)
Current ratio	**0.84**	0.98

Investing activities involved an outlay of $50 million compared to an inflow of $5 million in the previous year, reflecting an increased investment in property, plant and equipment for 2005–2006. Included in the outlay was a $25 million payment to MDS Nordion for acquiring their beneficial ownership of the MAPLE reactors and associated facilities under the new isotope supply agreement. In addition, costs totalling $22 million were incurred and capitalized for these facilities since November 1, 2005, the effective date of the transaction. Excluding these amounts, total funds invested in acquisition of other property, plant and equipment was $9 million (2004–2005: $8 million). In 2005–2006, generally lower cash balances through the first nine months of the year minimized the amount available to invest in short-term investments. The higher cash balances towards the end of the year have been invested in more liquid, shorter-term money market instruments. As such, investing activities involving the purchase and sale of short-term investments are significantly reduced from the prior year.

Financing activities generated proceeds of $43 million, principally accounted for by a $44 million long-term payable related to the purchase of isotope supply related inventory from MDS Nordion. Other financing activities include the repayment of $1 million for a long-term payable to the Government of Canada, consequently reducing the liability to $3 million as at March 31, 2006.

Overall, AECL's year-end closing cash position, including segregated cash, was increased to $110 million from the previous year's level of $61 million. Including short-term investments, the total cash position increased to $111 million compared to $67 million in the previous year. This level of cash reserve, together with the large commercial project milestone payments expected in the near-term is satisfactory for the needs of ongoing operations over the 2006–2007 fiscal year. However, to upgrade and refurbish the Chalk River infrastructure, additional cash outlays will be necessary and may require interim financing. Looking ahead, significant funding requirements have been identified to carry out the revised decommissioning and waste management plan.

Balance Sheet

The following table summarizes the changes in AECL's assets, liabilities and shareholder's deficit as at March 31, 2006 and March 31, 2005.

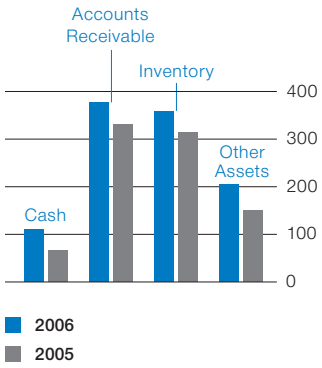
Balance Sheet

($ millions)	*2005–06*	*2004–05*
Assets		
Current assets	**$ 265**	$ 160
Long-term assets	**789**	703
Total assets	**$ 1,054**	$ 863
Liabilities and Shareholder's Deficit		
Liabilities		
Current liabilities	**$ 316**	$ 164
Long-term liabilities	**2,990**	2,930
Total liabilities	**$ 3,306**	$ 3,094
Shareholder's Deficit		
Shareholder's deficit	**$ (2,252)**	$ (2,231)
Total liabilities and shareholder's deficit	**$ 1,054**	$ 863

Assets

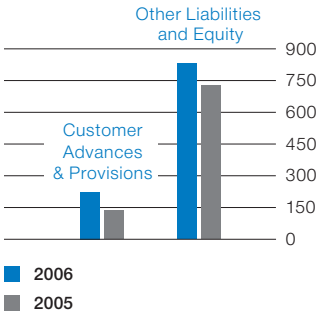
The Corporation's total consolidated assets were $1,054 million as at March 31, 2006 compared to $863 million as at March 31, 2005. Under current assets the major increases are in the overall cash balance and receivables with an increase of $49 million and $60 million respectively, reflecting increased business activities attributable to the new orders-on-hand. Long-term assets increased approximately $86 million over the previous year reflecting a new addition of isotope supply inventory in the balance sheet, and an increase in property, plant and equipment, partially offset by a reduction in long-term receivables. The isotope supply inventory amounted to $44 million as at March 31, 2006, representing the inventory purchased from MDS Nordion as part of the new isotopes supply agreement. The inventory amount of $44 million has a corresponding amount set up as a long-term liability to reflect the delayed payment term, which will commence in 2008. Property, plant and equipment as at March 31, 2006 totalled $188 million compared to $135 million as at March 31, 2005. A substantial portion of this increase is comprised of the net addition of $57 million largely related to the capitalization of the isotopes production and other related facilities. Long-term receivables decreased $13 million to $241 million from the previous year as scheduled heavy water lease payments were collected.

Assets ($ millions)



Liabilities and Shareholder's Deficit

Liabilities and Shareholder's Deficit ($ millions)



Current liabilities were $316 million as at March 31, 2006, an increase of $152 million over the previous year. The current portion of customer advances and provisions increased $170 million to $219 million, compared to $49 million as at March 31, 2005. The increase is mainly attributable to customer deposits and advance payments received during the year offset by the removal of provisions related to the settlement of contractual issues with MDS Nordion. Deferred decommissioning funding was reduced to $3 million from $26 million reflecting the requirement of the Corporation to utilize segregated funds comprised of proceeds from government funded heavy water sales to fund decommissioning and waste management activities.

Long-term liabilities increased $60 million to $2,990 million. The decommissioning and waste management provision increased $97 million to $2,847 million compared to $2,750 million in the previous year mainly representing accretion of the provision, net of adjustments to estimates and expenses incurred during the year. The spending levels at the beginning of the decommissioning cycle are lower than in later years when enabling facilities are constructed and waste is disposed. Consequently, the current period accretion, which is calculated using the interest rate of 5.25% and applied to the liability, is greater than current spending. As a result, the liability increases and a loss results. The long-term portion of customer advances and provisions were reduced by $81 million to $4 million as a result of a portion of these balances moving to current liabilities as they become due in 2006–2007, reflecting accelerated operational commitments in the coming year. Long-term payables increased $43 million primarily reflecting a deferred obligation associated with isotope supply inventory acquired from MDS Nordion.

Shareholder's deficit increased $21 million to $2,252 million compared to $2,231 million in the previous year. As part of this increase, contributed capital relating to government funded heavy water activities, which was utilized for decommissioning and waste management activities declined by $26 million from the previous year to $267 million. This increase was offset by $5 million as a result of the net income in 2005–2006.

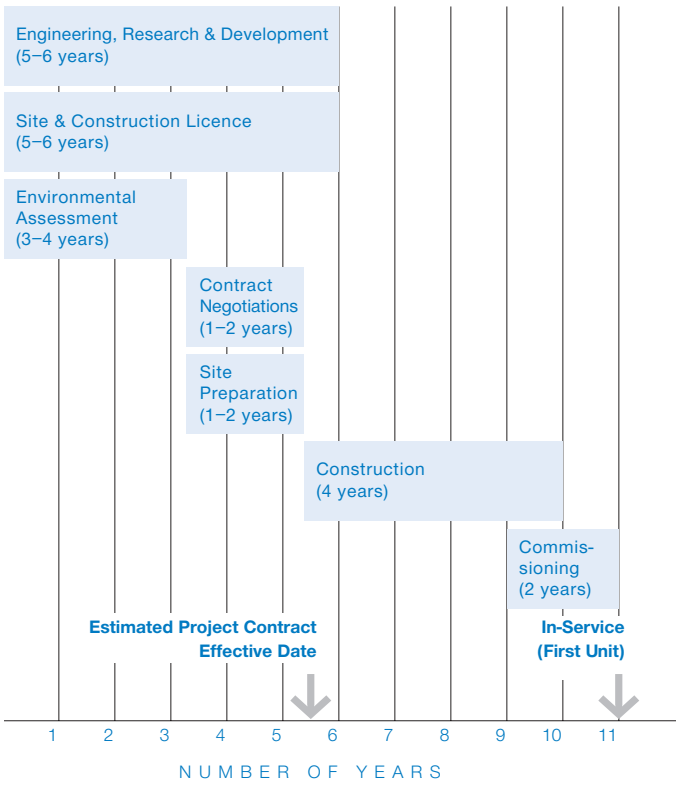
Outlook

Increasing public recognition of the safety, environmental and economic benefits of nuclear energy has left the nuclear industry well positioned to take on a greater role in the future energy mix around the world. In Canada, the growing need for sustainable base-load power cannot be met without increased use of nuclear power. In particular, the Ontario electricity sector is at one of the most challenging points in its history as a result of a possible shortfall in supply capacity later in the next ten years, which is expected to widen over time. The recent release by the Ontario Power Authority of its recommendation concerning the electricity supply mix in Ontario clearly reflects the seriousness of this challenge. The recommendation calls for significant investment over the next 20 years as part of an overall strategy to maintain nuclear generation supply at 50% of Ontario's electricity needs. Refurbishing existing units, rebuilding on existing sites and undertaking new build plants can all contribute to achieving this strategy.

Given the positive industry and market fundamentals, we anticipate significant growth in our Commercial Operations over the next few years. In addition to increased activities of the life extension projects currently underway with Bruce Power and NB Power, we anticipate securing refurbishment and retube projects with existing customers in Canada, Korea and Argentina.

Commercialization of the ACR-1000 is an important element of AECL's growth strategy in support of new build projects. The ACR-1000 product is expected to increase our competitive advantage, helping to capture new market share and opening opportunities for future growth. AECL continues to be focused on the Ontario

Projected ACR-1000 Deployment Schedule (Estimate)



market, where success in selling an ACR-1000 solution will set up the international market potential. AECL's 5–year Corporate Plan assumes the sale of a new build reactor in Ontario by the end of the 5th year. In Alberta, AECL will continue to pursue the development of CANDU technology as an option to generate low cost and non-carbon based steam, which is required in extracting bitumen from oil sands. The CANDU 6 has been confirmed as a technically and economically viable option for steam generation to help meet the growing energy needs in the oil sands region of Alberta. The ACR-1000 could also be utilized in certain larger oil sands developments after its successful deployment in Ontario. In addition, possible opportunities lie ahead for the addition of a second reactor to New Brunswick Power's Point Lepreau plant. AECL is also actively pursuing opportunities for new reactor sales on a global basis with a focus on countries where AECL has a strong existing presence.

New build opportunities in Ontario and Canada bring with them both regulatory and business challenges. A new ACR-1000 unit (see table on page 40) is expected to be deliverable in 11 years. However, as engineering work is completed and practical project experience is gained, the time taken to bring subsequent ACR-1000 units in-service is expected to significantly improve.

For service work, we expect to maintain the double-digit growth we achieved in 2005–2006 by building on the growth in refurbishment projects and by leveraging our R&D capability to provide innovative and integrated solutions based on customer requirements.

Reflecting these opportunities, revenues from Commercial Operations in 2006–2007 are expected to increase 66% from $320 million in 2005–2006. By the end of the Corporate Plan period revenues are projected to increase to $660 million up 106% from 2005–2006, with a peak of $819 million in 2009-2010. The associated net income is expected to increase to $61 million with a peak of $125 million in 2009–2010 from $47 million in 2005–2006.

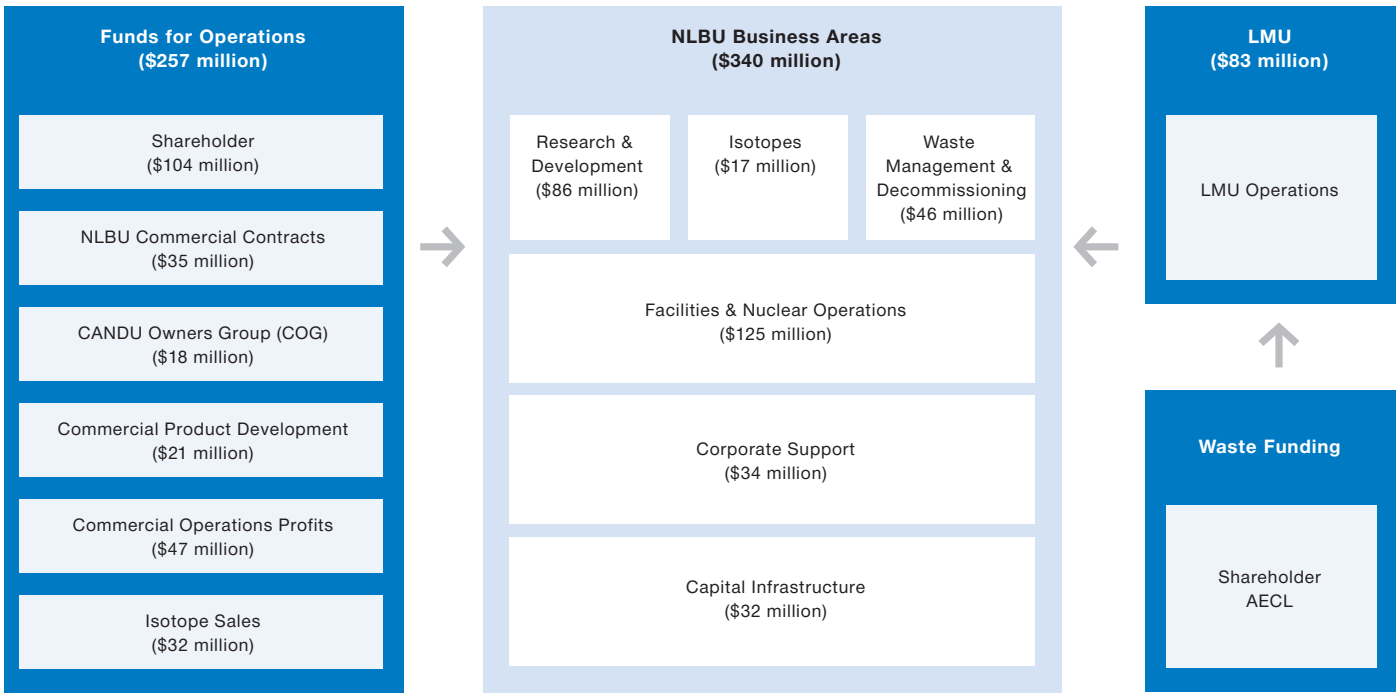
2006–2007 Corporate Plan – Commercial Operations

($ millions)	*2006–07*	*2007–08*	*2008–09*	*2009–10*	*2010–11*
Revenue	$ 532	$ 768	$ 705	$ 819	$ 660
Net income	$ 56	$ 122	$ 103	$ 125	$ 61

The current opportunities provide a solid basis for continued growth and profitability for Commercial Operations. To realize the benefits we must stay close to our customers so we can understand and anticipate their needs. In addition, we need to continually improve quality, to execute projects on budget and on schedule and to deliver maximum value to our customers. AECL committed to accelerate its culture change program with initiatives in the coming year focusing on health and safety, meeting customer needs and continued performance improvement.

In the Technology business segment, AECL will continue to invest in R&D in order to deliver solutions that support the licensing and operational performance of the entire fleet of CANDU reactors. The operating and capital infrastructure costs of NLBU for 2006–2007 (before decommissioning expense) is estimated at $257 million (see table below) against the current available government funding of $104 million. The remaining funding of $153 million comes from commercial work within the Technology segment, the sale of isotopes,

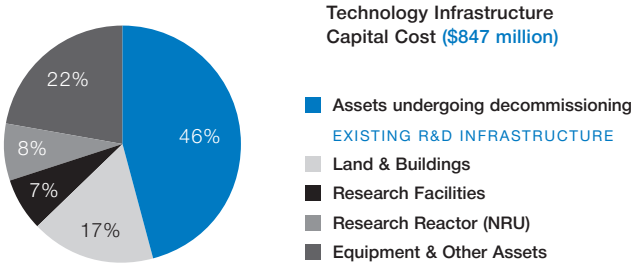
NLBU 2006–2007 Operating and Capital Infrastructure Costs and Sources of Funds



third party funding for research and profits generated by Commercial Operations. The proportion of funding from Commercial Operations has increased over the past ten years to meet cost increases, while Government of Canada funding has decreased in real terms. In addition, $83 million is projected to be required for waste management and decommissioning services. The source of this funding comes largely from the Shareholder and is managed through LMU.

The cost increases facing the NLBU have been driven by more stringent CNSC licensing requirements and also by the increasing infrastructure support required at Chalk River to meet these requirements. Increasing requirements, including those for security and for the operation of aging nuclear facility infrastructure will continue to increase pressure on Technology's capability. Rising energy costs, grants in lieu of taxes to municipalities, and increased charges from the CNSC for site and nuclear facility licensing, are examples of escalating expenditures that AECL incurs. These costs are not discretionary, but are necessary to meet AECL's commitment as a leader in health, safety and the environment and will not vary with the level of commercial activity. The financing requirements for the Technology segment are a matter that is subject to continued review.

The capitalized cost of the technology infrastructure totals $847 million. A significant portion (approximately $390 million) of NLBU's infrastructure is undergoing decommissioning. The remaining infrastructure (approximately $457 million) is critical and essential to AECL's business and is to be maintained at a level that meets CNSC and other regulatory requirements. Both groups of assets



require funding to allow the safe and effective utilization and management of facilities.

For the LMU, the plan for 2006–2007 assumes funding of $65 million to meet immediate health safety, security and environmental (HSSE) requirements associated with the decommissioning and waste management program. In addition, $7 million is planned for Low-Level Radioactive Waste Management Office activities and $11 million is allocated for new waste arising. Including these two activities, the total expenditures for LMU in 2006–2007 is estimated to be $83 million. The Government of Canada has expressed its intent to provide funding over the next five years for the decommissioning and waste management program, and a memorandum of understanding relating to this is currently being negotiated with NRCan.

Controlling costs remain an important objective for all business segments with an emphasis to achieving greater cost effectiveness through productivity and process improvements, while focusing on meeting customer and program deliverables.

The Corporation's 2006–2007 cash flows from operating activities are expected to increase at a rate consistent with net income growth and are projected to fund a large portion of our anticipated funding requirements, including planned capital investment related to isotopes production and related facilities.

Management of Risks and Uncertainties

AECL manages risk through a formal risk identification and assessment process. This involves three levels of risk review: the Risk Evaluation Committee of the Board of Directors ensures satisfactory governance reviews of proposed commitments that present the highest level exposures; intermediate level exposures are reviewed by business unit heads and senior corporate staff; and commitments deemed to have a lower level of risk are reviewed by senior staff in operations and corporate services. In addition, the Audit Committee of the Board plays an important role in overseeing how management identifies, assesses and addresses the risks it faces. The Audit Committee reviews and assesses risk in respect of the financial performance of the Corporation. The Chief Executive Officer (CEO) is accountable to the Board of Directors for all risk taking activities and risk management programs. The executives that support the CEO include the Chief Financial Officer, the Corporate Risk Review Panel, the Chief Regulatory Officer, the Chief Engineer and the Chief Risk Assessment Officer, who is responsible for administering the Corporation's risk management process.

Risk Management Process

In the upcoming year, AECL will continue to implement enhancements to the existing risk management process in order to establish a more integrated and cross-functional approach to managing and monitoring risk throughout AECL. A multifaceted review of risks and opportunities in the context of annual planning to achieve strategic business and operations objectives will facilitate better understanding of options available and their potential consequences. Management will be better positioned to align priorities and resources with AECL's appetite and tolerance for risk. This approach will provide greater transparency in decision-making, support governance responsibilities and is expected to strengthen accountability, enhance stewardship and improve corporate performance.

Industry

The primary business risk relates to the industry in which AECL operates. This is characterized by very long decision cycles for new

major projects. Furthermore, demand levels for AECL's products and services are affected by factors such as technology development, worldwide economic trends, public acceptance, government policy initiatives and levels of commitment to new nuclear electricity generation capacity. To moderate such risks, AECL is establishing new strategic business alliances, growing its full service capability, pursuing the refurbishment business, commercializing newly developed technologies, and carefully managing the portfolio of existing product lines. AECL has programs in place to retain and build core competence to support AECL's corporate objective and business opportunities.

Technology

In the new build project business, our continued success is dependent on technological advances. As AECL continues to invest in supporting the CANDU design, a significant commitment is required to complete developing the ACR-1000, which will be well placed to address the market needs relative to both nuclear vendors and competing technologies. Achieving the ACR-1000 commercialization plan requires that the product meet functionality, cost and performance parameters as well as licensing requirements. Timing, continued support of partners including the government and customer participation, licensing preparation and business/financing model and delivery structure will all be critical in achieving the successful launch of the ACR-1000. AECL manages the risk by closely monitoring progress towards achieving ACR-1000's key performance parameters and by carefully managing available resources in accordance with market conditions.

Licensing

AECL designs and builds nuclear reactors requiring a high level of safety, reliability and sustainability. Therefore, AECL operates and conducts business in a highly regulated environment. The preparation, construction, operation and decommissioning of nuclear related facilities are subject to CNSC licensing requirements. The licensing process for the construction of nuclear facilities is comprised of three separate licence applications: site preparation, construction and operation. A site preparation licence is issued based on satisfying the CNSC that the project is feasible to design, construct and operate on the proposed site. Consequently, the site preparation licence application requires completion of an Environmental Assessment (EA). The EA process requires harmonization and coordination of activities at a federal and provincial (territorial if applicable) level, as many of the requirements at each level overlap. Assessments include consideration of factors that impact health, the socio-economic environment, and physical and cultural heritage. A construction licence would require that the proposed facility conforms to regulatory requirements and provides for safe operation over the facility's life. The operation licence requires that established facility programs are appropriate to ensure safe and secure operation of the facility. The timeframe for the granting of a licence would vary based on the type of licence and individual circumstances. During the EA and at each significant licensing phase of the project, the public is consulted prior to the CNSC granting a licence.

In addition, the issuance of a licence would require compliance with applicable regulations issued under the *Nuclear Safety and Control Act* (NSCA) and other legislation including the:

- *Nuclear Liability Act;*
- *Nuclear Fuel Waste Act;*
- *Canadian Environmental Assessment Act;*
- *Canadian Environmental Protection Act;*
- *Fisheries Act;*
- *Species at Risk Act;*
- *Migratory Bird Conservation Act;* and
- *Canada Water Act.*

The stringent licensing requirements described above contribute to the safe and secure operation of nuclear facilities in Canada. However, it also contributes to an increased project timeframe and associated compliance and administrative costs. AECL mitigates this risk through extensive monitoring of all licensing activities on an ongoing basis. In addition, AECL has in place well established environmental and quality management systems. In the case of ACR-1000, AECL is proactive in moving the licensing and environmental reviews in Canada, in parallel with the development and pre-project programs. In addition, AECL has positive interaction with key stakeholders and potential partners and is actively seeking input into the ACR-1000 design from these stakeholders.

CRL Site Licensing

In 2005–2006, the operating licences for the MAPLE reactors and the New Processing Facility (NPF) were successfully renewed for a 2-year period. In 2006–2007, the operating licence for the CRL site must be renewed. AECL has applied for a 63-month licence period, longer than recent licence renewals for the site, but generally consistent with licence periods granted to other major licensees. The CNSC has noted AECL's improved performance against regulatory requirements in some areas, and this will support our application for a longer licence period. Performance improvements must be sustained to reduce the risk of CNSC regulatory action. This is a challenge at the CRL site where buildings and facilities are aging, and will require significant investment in infrastructure. This issue is fundamentally linked to the discussion of a long-term funding strategy with the Government of Canada in the coming year.

Health, Safety, Security & Environment (HSSE)

AECL is committed to the effective management of all HSSE risks that are inherent in the operation of its major Canadian sites. AECL implemented several formal compliance programs that specifically address the deployment of due diligence processes and associated resources necessary to comply with all applicable laws and

regulations. AECL's established environmental policy emphasizes compliance to all applicable environmental legislation and other relevant regulations; this is supported through the efforts of the Chief Environmental Officer and the Environmental Committee, which has established objectives for further improving the Corporation's environmental performance in its site operations as well as the delivery of quality products and services in keeping with AECL's focus on environmental stewardship. In addition, the Chief Regulatory Officer (CRO) has worked closely with the AECL executive and management team to ensure that the Corporation complies with the current regulatory framework. This is being done by carefully managing the regulatory interface and through the development of a licensing strategy that provides overall coordination of licensing activities related to nuclear facilities and site operations, including decommissioning and waste management. Ultimately, this change will enhance AECL's ability to bring quality products to market in a timely and efficient manner, exceeding customer and stakeholder expectations.

AECL research laboratories operate major facilities such as reactors, experimental loops, shielded facilities and waste management plants. These are used both to conduct research and support commercial activities including the isotope business. Facilities are subject to applicable laws and regulations regarding safety and environmental matters including the management of hazardous wastes and materials. There are business risks associated with the availability of facilities for production, and the availability of funding for facilities maintenance and upgrades, which consequently pose a risk to AECL's reputation. AECL seeks to manage the safety and environmental risks through its Safety Management System, which includes numerous program controls, such as stringent safety reviews and audits. These controls provide assurance of compliance to all applicable laws and regulations, and where shortfalls are identified, appropriate corrective action plans are put in place. Fitness of AECL's facilities is also ensured by a prudent program of equipment and facility maintenance such as investment in the NRU safety upgrades. AECL has in place an extensive insurance program to mitigate losses that may arise from certain types of liability and property risks associated with operations at the laboratories.

Quality Assurance and Quality Management

Attention to safety and quality reduces the risk of eroding the confidence of regulators and customers. Maintaining and enhancing customer and regulatory confidence continues to be the main objective of the organization. AECL has implemented a strong corporate oversight function to ensure compliance with the widely accepted national and international technical Quality Assurance standards (such as CSA, IAEA and US standards), company-wide requirements, and the *Nuclear Safety and Control Act* and its regulations. Leading the quality organization is the Chief Quality Officer who reports directly to the CEO, thereby ensuring the independence of corporate quality. Numerous oversight activities have been conducted at all AECL Business Units. AECL is continually improving its Quality Management System through steady and progressive implementation of Business Process Management, implementing process improvement initiatives and frequent Program Reviews. Continual improvements have led to the maintenance of ISO 9001:2000 Quality Management System Global Certifications at all AECL sites and achieving ISO 14001 Environmental Management System Certification at the Chalk River site. AECL quality management system goes through an extensive internal auditing program and also receives a number of external audits from its customers and regulatory bodies. Progress in quality improvements is being monitored on a quarterly basis through a Quality Index. Focus on customer satisfaction, health and safety and excellence in performance is invigorating the organization and directing the culture toward adopting best practices to achieve business excellence. AECL continues to align its management system with the National Quality Institute's Progressive Excellence Program (currently progressing to Level 2 certification).

Project Management

There are considerable risks in managing AECL's major projects. These include managing a complex supply chain and ensuring that procurement, delivery and installation meet quality, schedule and price requirements, in addition to contract performance risk, legal claims and changes in political conditions. We seek to manage these risks by stringent project cost and schedule control, rigorous legal review of contracts, ongoing monitoring and evaluation, including regular review of project forecast to completion and delivery of quality products and services. Maintaining comprehensive insurance coverage for various aspects of a given project and developing effective relationships with clients, project partners, subcontractors and suppliers are important elements in the project management process. Obtaining sovereign and third party guarantees have been part of our risk management strategy to reduce the adverse impact of changes in political conditions. Despite these risks, AECL has delivered all major CANDU projects it has managed in the past decade on time and on budget.

Foreign Operations

As AECL operates globally with sales and project offices in multiple jurisdictions, it is subject to risks and other factors associated with doing business outside Canada. Foreign operations involve inherent financial risks that include taxes, currency controls and fluctuations, tariffs, import and other related restrictions and regulations. AECL mitigates the risk through specific contractual requirements and obtains government rulings to reduce the financial impact of such risks, when possible. Sales and purchases are made mainly in Canadian dollars. In addition, where large foreign currency purchase commitments exist, forward contracts reduce exposure. AECL is also subject to credit risks, but these are minimal as its customer base is primarily large corporations and government related entities, which offer sovereign guarantees in their support.

Public Perception

Public perception is a risk that impacts AECL's nuclear related activities. In Canada, public consultations are a mandatory part of the Environmental Assessment process. Nuclear related Environmental Assessments are generally initiated through CNSC licensing requirements. AECL mitigates this risk through proactive public information programs to inform the public on safety measures and risks associated with nuclear activities. In addition, AECL is committed to maintaining an honest two-way communication dialogue with the public, the customer, the regulators and the community in which AECL conducts business and with all government levels.

Human Resources

Achievement of strategic business objectives and the long-term assurance of the safety, licensing and design basis for CANDU technology requires that AECL attract, retain and develop adequate levels of staff with the requisite skills and technical depth. The challenge lies in the changing demographics of scientific and technical staff industry-wide, resulting in a need to infuse fresh talent as well as to develop and train them, in order to achieve an appropriate balance in the experience and versatility of the workforce. AECL will focus investment in the development of staff in the right technical areas. In support of that goal, AECL has put in place an active hiring program to address loss of staff through demographics-based attrition, as well as a robust succession planning process. It will also ensure that its staff resources are optimally deployed to the key commercial and technology development activities.

AECL is acting to improve employee engagement and has launched a change management initiative to ensure all staff are given the appropriate tools required to adapt to the current competitive business environment. Training in customer satisfaction, leadership and internal communications have been deployed company-wide to ensure employees are informed and fully engaged in a customer focused culture. Ongoing implementation of programs in quality, knowledge management, career and succession planning and continuous process improvement is a management focus to ensure that the Corporation is geared to meet a business environment which is both challenging and robust.

Internal Control

The Corporation's internal auditors review, monitor and assess inherent operational risks and the effectiveness of internal controls. The independent auditors review the effectiveness of internal controls to the extent they consider necessary in the course of their audit of the Corporation's financial statements. Both the internal and independent auditors report directly to the Audit Committee on findings from their audits. AECL has established processes in place to facilitate the communication of illegal or unethical acts by employees in a confidential manner through a Chief Privacy Officer, who will investigate such matters. In addition, AECL's Board of Directors have established a Code of Ethics and Business Conduct policy required to be signed and adhered to by all employees.

Off-Balance Sheet Arrangements

In the normal course of business, AECL enters into the following off-balance sheet arrangements:

- Bank guarantees and standby letters of credit used in connection with performance guarantees on major contracts. The guarantees generally relate to project and product performance, and advance payments. The aggregate amount of AECL's potential exposure under these guarantees is estimated to be $76 million on current commercial projects as at March 2006. In addition, AECL also guarantees that certain projects will be completed within a specified time and if the Corporation does not fulfill the obligations, it will assume responsibility for liquidated damages. Management's best estimate of the total maximum potential exposure of liquidated damages under the terms of contracts is approximately $105 million. Historically, AECL has not made any payment on performance guarantees or on any liquidated damages. Management does not expect these guarantees to have a material impact on the consolidated financial statements of the Corporation.
- Indemnification arrangements are part of the standard contractual terms to counterparties in transactions such as service agreements, sale and purchase contracts. These indemnification agreements may require us to compensate the counterparties for costs incurred as a result of certain events. The nature of these indemnification agreements prevents us from making a reasonable estimate of the likely maximum amount to be paid out by us. Management does not expect these arrangements to have a material current or future effect on the results of the consolidated financial statements of the Corporation.
- Foreign currency forward contracts are for the sole purpose of limiting exposure to exchange rate fluctuations relating to contractual terms and ongoing business operations. AECL formally documents all relationships between the hedge instrument and hedged items, as well as its risk management objective and strategies for undertaking various hedge transactions. Gains and losses resulting from foreign exchange contracts are recognized in earnings in the period in which the transactions are settled. As at March 31, 2006, AECL has the following 31 outstanding foreign currency forward contracts: 24 contracts to buy US dollars and pay Canadian dollars in the amount of $24.7 million (average exchange rate of C$1.16 / US$1), and 7 contracts to buy Euros and pay Canadian dollars in the amount of C$3.7 million (average exchange rate of C$1.41 / Euro 1).

Accounting Recommendations Adopted in 2005–2006

On April 1, 2005, the Corporation adopted the Canadian Institute of Chartered Accountants' ("CICA") accounting guideline AcG-15, Consolidation of Variable Interest Entities. AcG-15 requires the Corporation to identify and evaluate entities in which it has an interest, to determine whether it is the primary beneficiary of such entities. As a primary beneficiary of an entity, the Corporation will consolidate the financial statements of the entity. The Corporation has evaluated its various business arrangements and has identified no arrangements that meet the definition of a variable interest entity and has concluded that AcG-15 has no impact on these financial statements.

Future Accounting Policy Changes

The Corporation will adopt three new CICA accounting standards: Section 1530, Comprehensive Income; Section 3855, Financial Instruments – Recognition and Measurement; and Section 3865, Hedges. These standards will be incorporated on April 1, 2007.

Comprehensive Income

A new category, accumulated other comprehensive income, will be added to the shareholder's deficit on the consolidated balance sheet. Major components for this category will include unrealized gains and losses on financial assets. These amounts will be recorded in the statement of other comprehensive income until the criteria for recognition in the consolidated statement of operations are met.

Financial Instruments – Recognition and Measurement

Financial assets will be classified based on their term to maturity, trade or sale characteristics. Liabilities will be classified based on whether they are held for trading or other purposes. Financial assets and liabilities for trading will be measured at fair value with gains and losses recognized in net income. In general, AECL holds financial instruments to maturity, as such, financial assets and liabilities will be measured at amortized cost. Financial instruments measured at fair value with unrealized gains and losses are recognized in other comprehensive income.

Hedges

The change in fair value of the hedged item to the extent that the hedging relationship is effective (criteria established by the CICA accounting standard), is offset by changes in the fair value of the derivative. The carrying value of a hedged item is adjusted by gains or losses attributable to the hedged risk and recognized in net income. In a cash flow hedging relationship, the effective portion of the change in the fair value of the hedging derivative will be recognized in other comprehensive income. The ineffective portion will be recognized in net income. The amounts recognized in accumulated other comprehensive income will be reclassified to net income when net income is affected by the variability in cash flows of the hedged item. In hedging a foreign currency net investment in a self-sustaining foreign operation, foreign exchange gains and losses on the hedging instruments will be recognized in other comprehensive income.

Critical Accounting Estimates and Policies

AECL's critical accounting policies are those considered to be the most important in determining its financial condition and results, and which require significant subjective judgement by management. A summary of the Corporation's significant accounting policies, including the critical ones discussed below, is set out in the notes to the consolidated financial statements.

Revenue Recognition

AECL generates a significant portion of its revenue from long-term contracts. Revenue from long-term contracts is recognized using the percentage of completion method, where revenue, earnings and work-in-progress are recorded as related costs are incurred on the basis of percentage costs incurred to date, relative to the estimated total contract costs. The nature of this accounting method is such that refinements of the estimating process for changing conditions and new developments are continuous. Accordingly, revisions in cost and earnings estimates throughout the duration of a contract term are reflected in the period in which the need for revision becomes known. Additionally, losses on long-term contracts are recognized in the period when they are identified and are based upon the anticipated excess of contract costs over the related contract revenues. Any such losses are recorded as a component of cost of sales. Revenue from services sales are recorded when services are rendered and goods are shipped. Revenue from heavy water shipments is recognized when the shipment is accepted in the manner and timing that is in accordance with the related contract.

Asset Impairment

AECL reviews its long-lived assets, which include property, plant and equipment for impairment whenever circumstances indicate that the carrying amount of the asset may not be recoverable. Determination of recoverability is based on an estimate of undiscounted future cash flows, and measurement of an impairment loss is based on the fair value of the assets. Estimated undiscounted future cash flows reflect management's best estimates and changes in those estimates could materially affect the carrying amount of the long-lived assets. AECL concluded that no impairment charge was required for its long-lived assets for 2005–2006.

Heavy Water Inventory

Heavy water inventory is valued at the lower of cost or net realizable value. It is recorded as a long-term asset since the lead time required in relation to future reactor sales exceeds one year.

At the end of March 2006, the inventory includes 1,003 megagrams provided to the Sudbury Neutrino Observatory Institute, at no cost, for research and experimental purposes, the majority of which is scheduled for return in 2007–2008.

Parliamentary Appropriations

Parliamentary appropriations that are not in the nature of contributed capital are recorded as funding in the year for which they are appropriated, except as follows:

- Appropriations restricted by legislation and related to expenses of future periods are deferred and recognized as funding in the period in which the related expenses are incurred. No appropriations restricted by legislation or related to expenses of future periods were received in 2005–2006.
- Appropriations used for the purchase of property, plant and equipment are deferred and amortized on the same basis as the related asset. The balance of deferred capital funding as at March 2006 amounted to $37 million compared with $39 million in the previous year.

Commencing in 1996–1997, and pursuant to a 10-year arrangement with Treasury Board for funding decommissioning activities, AECL retains the net proceeds from the sale or lease of government funded heavy water inventory. The net proceeds are transferred from contributed capital to deferred decommissioning funding and are then recorded as funding in the consolidated statement of operations as related expenditures are made. The funding arrangement expired on April 1, 2006.

Decommissioning and Waste Management

AECL's obligation for decommissioning and waste costs is recorded as a long-term liability. The liability is recorded based on the discounted value (using present value technique) of the estimated future decommissioning and waste management costs to the extent that they can be reasonably estimated. The provision is reviewed annually to reflect actual expenditures incurred and changes in management's estimate of the future costs and timing thereof.

MANAGEMENT'S RESPONSIBILITY

The consolidated financial statements, all other information presented in this Annual Report and the financial reporting process are the responsibility of management. These statements have been prepared in accordance with Canadian generally accepted accounting principles and include estimates based on the experience and judgement of management.

Where alternate accounting methods exist, management has chosen those it deems most appropriate in the circumstances. The Corporation and its subsidiaries maintain books of account, financial and management control, and information systems, together with management practices designed to provide reasonable assurance that reliable and accurate financial information is available on a timely basis, that assets are safeguarded and controlled, that resources are managed economically and efficiently in the attainment of corporate objectives, and that operations are carried out effectively. These systems and practices are also designed to provide reasonable assurance that transactions are in accordance with Part X of the *Financial Administration Act* (FAA) and its regulations, as well as the *Canada Business Corporations Act*, the articles, and the by-laws and policies of the Corporation and its subsidiaries. The Corporation has met all reporting requirements established by the FAA, including submission of a Corporate Plan, an operating budget, a capital budget and this Annual Report.

The Corporation's internal auditor has the responsibility of assessing the management systems and practices of the Corporation and its subsidiaries. AECL's independent auditors conduct an audit of the consolidated financial statements of the Corporation and report on their audit to the Minister of Natural Resources.

The Board of Directors is responsible for ensuring that management fulfills its responsibility. To accomplish this, the Board has established five committees: Audit, Human Resources and Governance, Nominating, Science and Technology, and Risk Evaluation.

The Audit Committee, composed of independent directors, has a mandate for overseeing the independent auditors, directing the internal audit function and assessing the adequacy of AECL's business systems, practices and financial reporting. The Audit Committee meets with management, the internal auditor and independent auditors on a regular basis to discuss significant issues and findings, in accordance with their mandate.

The independent auditors and internal auditor have unrestricted access to the Audit Committee, with or without management's presence. The Audit Committee reviews the consolidated financial statements and the Management's Discussion and Analysis (MD&A) report with both management and the independent auditors before they are approved by the Board of Directors and submitted to the Minister of Natural Resources. The Chair of the Audit Committee signs the audited financial statements.

ROBERT G. VAN ADEL
President and Chief Executive Officer

MICHAEL ROBINS
Chief Financial Officer

AUDITORS' REPORT

To the Minister of Natural Resources

We have audited the consolidated balance sheet of Atomic Energy of Canada Limited as at March 31, 2006 and the consolidated statements of operations, contributed capital, deficit and cash flow for the year then ended. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Corporation as at March 31, 2006 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles. As required by the *Financial Administration Act*, we report that, in our opinion, these principles have been applied on a basis consistent with that of the preceding year.

Further, in our opinion, the transactions of the Corporation and of its wholly-owned subsidiaries that have come to our notice during our audit of the consolidated financial statements have, in all significant respects, been in accordance with Part X of the Financial Administration Act and regulations, the Canada Business Corporations Act, and the articles and by-laws of the Corporation and its wholly-owned subsidiaries.

NANCY Y. CHENG, FCA
Assistant Auditor General
for the Auditor General of Canada

ERNST & YOUNG LLP
Chartered Accountants

Ottawa, Canada
May 5, 2006

CONSOLIDATED BALANCE SHEET

As at March 31

(thousands of dollars)	***2006***	*2005*
Assets		
Current		
Cash and cash equivalents (Note 3)	**$ 107,335**	$ 35,275
Segregated cash (Note 14)	**2,640**	25,851
Short-term investments (Note 3)	**1,352**	6,302
Accounts receivable (Note 17)	**120,719**	60,325
Current portion of long-term receivables (Note 5)	**16,232**	17,229
Current portion of inventory (Note 4)	**16,494**	14,961
	264,772	159,943
Long-term receivables (Note 5)	**241,205**	253,764
Trust fund (Note 6)	**17,347**	15,004
Inventory (Note 4)	**44,178**	–
Heavy water inventory (Note 7)	**299,101**	299,503
Property, plant and equipment (Note 8)	**187,858**	134,961
	$ 1,054,461	$ 863,175
Liabilities		
Current		
Accounts payable and accrued liabilities	**$ 93,508**	$ 87,864
Current portion of customer advances and provisions	**218,773**	49,071
Deferred decommissioning funding (Notes 11 and 14)	**2,640**	25,851
Current portion of long-term payables (Note 9)	**1,000**	1,000
	315,921	163,786
Decommissioning and waste management provision (Note 11)	**2,846,756**	2,750,000
Customer advances and provisions	**4,467**	85,898
Deferred capital funding (Note 8)	**36,880**	39,264
Employee future benefits (Note 13)	**55,756**	52,748
Long-term payables (Note 9)	**45,829**	2,500
	3,305,609	3,094,196
Commitments and contingencies (Note 16)		
Shareholder's deficit		
Capital stock		
Authorized – 75,000 common shares		
Issued – 54,000 common shares	**15,000**	15,000
Contributed capital (Note 14)	**504,446**	530,064
Deficit	**(2,770,594)**	(2,776,085)
	(2,251,148)	(2,231,021)
	$ 1,054,461	$ 863,175

The accompanying notes are an integral part of these consolidated financial statements

Approved on behalf of the Board:

BARBARA TRENHOLM
Director

ROBERT G. VAN ADEL
Director

CONSOLIDATED STATEMENT OF OPERATIONS

For the year ended March 31

(thousands of dollars)	***2006***	*2005*
Commercial operations		
Revenue		
Nuclear products and services	**$ 302,809**	$ 282,979
Interest on long-term receivables (Note 5)	**15,158**	16,274
Interest on investments and other (Note 3)	**1,909**	2,061
	319,876	301,314
Expenses		
Cost of sales and operating expenses	**273,011**	229,046
Interest on long-term payables (Note 9)	**81**	96
	273,092	229,142
Commercial operations net income	**46,784**	72,172
Technology		
Revenue		
Services	**87,307**	55,238
	87,307	55,238
Funding		
Parliamentary appropriations (Note 12)	**160,349**	133,838
Cost recovery from third parties	**17,348**	15,255
Amortization of deferred capital funding	**2,384**	3,530
	180,081	152,623
Gain on reversal of provisions (Note 10)	**60,852**	–
Expenses		
Cost of sales and operating expenses	**294,247**	314,332
Interest on long-term payables (Note 9)	**150**	–
Technology net income (loss)	**33,843**	(106,471)
Liability management unit		
Funding		
Parliamentary appropriations	**–**	29,000
Cost recovery from third parties and other	**6,959**	9,551
Decommissioning funding	**48,829**	8,049
	55,788	46,600
Expenses		
Revision in estimate and timing of expenditures (Note 11)	**1,210**	1,792,331
Accretion and other expenses	**129,714**	60,827
Liability management unit net loss	**(75,136)**	(1,806,558)
Net income (loss)	**$ 5,491**	$ (1,840,857)

Amortization disclosure (Note 8)

The accompanying notes are an integral part of these consolidated financial statements

CONSOLIDATED STATEMENT OF CONTRIBUTED CAPITAL

For the year ended March 31

(thousands of dollars)	***2006***	*2005*
Balance at beginning of the year	**$ 530,064**	$ 557,729
Transfer to deferred decommissioning funding (Note 14)	**(25,618)**	(27,665)
Balance at end of the year	**$ 504,446**	$ 530,064

CONSOLIDATED STATEMENT OF DEFICIT

For the year ended March 31

(thousands of dollars)	***2006***	*2005*
Balance at beginning of the year	**$(2,776,085)**	$ (935,228)
Net income (loss)	**5,491**	(1,840,857)
Balance at end of the year	**$(2,770,594)**	$(2,776,085)

The accompanying notes are an integral part of these consolidated financial statements

CONSOLIDATED CASH FLOW STATEMENT

For the year ended March 31

(thousands of dollars)	***2006***	*2005*
Operating activities		
Cash receipts from customers	**$ 552,973**	$ 332,701
Cash receipts from parliamentary appropriations	**160,349**	162,838
Cash paid to suppliers and employees	**(608,574)**	(488,567)
Funds used for decommissioning activities	**(50,926)**	(58,665)
Interest on investments received (net)	**1,820**	1,965
Cash from (used in) operating activities	**55,642**	(49,728)
Investing activities		
Purchase of short-term investments	**(1,352)**	(39,418)
Sales and maturities of short-term investments	**6,302**	50,994
Proceeds on disposal of property, plant and equipment	**704**	948
Acquisition of property, plant and equipment	**(55,625)**	(7,954)
Cash (used in) from investing activities	**(49,971)**	4,570
Financing activities		
Proceeds from long-term payable	**44,178**	–
Repayment of long-term payable	**(1,000)**	(1,000)
Cash from (used in) financing activities	**43,178**	(1,000)
Cash, cash equivalents and segregated cash:		
Increase (decrease)	**48,849**	(46,158)
Balance at beginning of the year	**61,126**	107,284
Balance at end of the year	**$ 109,975**	$ 61,126
Interest and bank charges paid during the year	**$ 144**	$ 143

As at March 31 (thousands of dollars)	***2006***	*2005*
Cash, cash equivalents and segregated cash are comprised of:		
Cash	**$ (1,503)**	$ 3,075
Short-term money market instruments	**108,838**	32,200
Segregated cash	**2,640**	25,851
	$ 109,975	$ 61,126

The accompanying notes are an integral part of these consolidated financial statements

1. The Corporation

Atomic Energy of Canada Limited (collectively "AECL" or the "Corporation") was incorporated in 1952 under the provisions of the *Canada Corporations Act* (and continued in 1977 under the provisions of the *Canada Business Corporations Act*), pursuant to the authority and powers of the Minister of Natural Resources under the *Nuclear Energy Act*.

The Corporation is a Schedule III Part I Crown Corporation under the *Financial Administration Act* (FAA) and an agent of Her Majesty the Queen in right of Canada. The Corporation is exempt from income taxes in Canada.

AECL conducts its business through three business segments: Commercial Operations, Technology, and the Liability Management Unit. These segments represent strategic business units established by senior management to facilitate the achievement of the Corporation's long-term objectives, to aid in resource allocation decisions and to assess operational and financial performance.

2. Significant Accounting Policies

The Corporation's financial statements are prepared in accordance with Canadian generally accepted accounting principles. The significant accounting policies are:

a) Basis of Presentation

These consolidated financial statements include the accounts of the Corporation's wholly-owned subsidiaries, AECL Technologies Inc., incorporated in the state of Delaware, U.S.A. in 1988, and AECL Technologies B.V., incorporated in the Netherlands in 1995. All significant inter-company transactions have been eliminated.

b) Use of Estimates

The Corporation's financial statements include estimates and assumptions made by management that affect the amounts reported in the financial statements and accompanying notes. Estimates are based on management's best knowledge of current information. However, actual results may differ significantly from current estimates.

The more significant areas requiring the use of estimates are heavy water inventory, costs of future decommissioning and waste management, future contract costs, revenue, derivatives, commercial and other provisions, employee future benefits and amortization of property, plant and equipment. The Corporation reviews these estimates annually.

c) Cash, Cash Equivalents and Short-Term Investments

Investments with maturities of 90 days or less from the date of purchase are presented as cash equivalents. Short-term investments have original maturities greater than 90 days but less than one year. Cash equivalents and short-term investments are carried at the lower of cost or market.

d) Trust Fund

Long-term investments in the Trust Fund established pursuant to the Nuclear Fuel Waste Act are carried at the lower of cost or market.

e) Foreign Currency Translation

Transactions denominated in a foreign currency are translated into Canadian dollars at the exchange rate in effect at the date of the transaction. Monetary assets and liabilities outstanding at the balance sheet date are adjusted to reflect the exchange rate in effect at that date. Exchange gains and losses arising from the translation of foreign currencies are included in income.

f) Derivative Financial Instruments

The Corporation enters into foreign exchange forward contracts to manage its exposure to changes in exchange rates arising from contractual terms and ongoing business operations. The Corporation's policy is not to utilize derivative financial instruments for trading or speculative purposes.

The Corporation formally documents all relationships between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions. This process includes linking all derivatives to specific assets and liabilities on the balance sheet or to specific firm commitments or forecasted transactions. The Corporation also formally assesses, both at the hedge's inception and on an ongoing basis, whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items.

For foreign exchange forward contracts used to hedge anticipated foreign currency sales, the portion of the forward premium or discount on the contract relating to the period prior to consummation of the sale is recognized as an adjustment of the revenues when the sale is recorded; and the portion of the premium or discount that relates to the resulting account receivable is amortized as an adjustment of interest expense over the remaining term of the contract.

Realized and unrealized gains or losses associated with derivative instruments, which have been terminated or cease to be effective prior to maturity, continue to be deferred under other current, or non-current, assets or liabilities on the balance sheet and recognized in income in the period in which the underlying hedged transaction is recognized. Subsequent changes in the fair value of the derivative are recognized in earnings.

In the event a forecast transaction is no longer probable of occurring, any deferred realized or unrealized gain or loss on such a derivative instrument is recognized in income. Subsequent changes in the fair value of the derivative are recognized in earnings.

g) Inventory

Heavy water is valued at the lower of cost or net realizable value. Supplies and reactor fuel are valued at the lower of cost or net replacement cost.

h) Property, Plant and Equipment

Property, plant and equipment are recorded at cost less amortization. Construction in progress, once ready for use, is transferred to the appropriate category and amortized. Asset retirement costs are included as part of the related asset costs. Amortization is provided on a straight-line basis over the estimated useful life of the asset, and on a usage basis for certain machinery and equipment used in commercial projects, as follows:

Land improvements	*10 to 20 years*
Buildings and reactors	*20 to 40 years*
Machinery and equipment	*3 to 20 years*

i) Impairment of Long-Lived Assets

AECL reviews long-lived assets to be held and used whenever events or changes in circumstances indicate that the carrying amount of such assets may not be fully recoverable. Determination of recoverability is based on an estimate of undiscounted future cash flows resulting from the use of the assets and its eventual disposition.

Measurement of an impairment loss for long-lived assets is based on the fair value of the assets. The fair value is estimated using accepted valuation methodologies such as discounted future net cash flows, earnings multiples or prices for similar assets, whichever is most appropriate under the circumstances.

j) Customer Advances

To properly match revenues with costs, certain contracts may have revenue recognized in excess of billings (unbilled revenues), and other contracts may have billings in excess of revenue recognized (customer advance payments). Revenues collected in advance under service contracts are recorded as a liability and recognized in accordance with the contract.

k) Decommissioning and Waste Management Provision

AECL provides for its legal obligation to decommission nuclear facilities and to manage nuclear waste in order to satisfy regulatory requirements. The obligation is recognized in the period incurred when a reasonable estimate of fair value can be determined. As the provision is recorded based on a discounted value of the projected future cash flows, it is increased annually to reflect the passage of time by removing one year's discount. The accretion is charged to expense in the Consolidated Statement of Operations.

The provision is reduced by actual expenditures incurred. The cost estimate is subject to periodic review and any material changes in the estimated amount or timing of the underlying future cash flows are recorded as an adjustment to the provision. Upon settlement of the liability, a gain or loss will be recorded. The provision includes future construction costs associated with certain enabling facilities, such as disposal facilities for nuclear waste.

Decommissioning costs of new assets are added to the carrying amount and amortized over the related assets' useful life.

l) Revenue Recognition

Long-Term Contracts and Service Contracts

Revenue is derived from sales of the Corporation's services and products to clients. Revenue under certain long-term contracts, many of which provide for periodic payments, are recognized under the percentage-of-completion method using the ratio of cost incurred to total estimated cost as the measure of performance. When adjustments in contract value or estimated costs are determined, any changes from the prior estimates are generally reflected in earnings in the current period. Anticipated losses on contracts are charged to earnings when identified and determined to be probable. Revenue under cost-reimbursement contracts are recorded as costs are incurred and include an estimate of fees earned. Revenue under all other contracts are recognized when services are performed.

Supply of Product

Revenue is recognized based on shipments of product to customers, supported by evidence of invoicing and shipping documents. In the case of isotope supplies, revenue is recognized based on customer contract.

Interest Revenue

Interest entitlement under a long-term receivable is recorded as deferred revenue and released to revenue over the term of the related agreement.

m) Research and Development

Research and development (R&D) costs include: salaries, wages and other related costs of personnel engaged in R&D activities, the cost of materials and services consumed in R&D activities, amortization of equipment and facilities to the extent that they are used for R&D activities, overhead costs related to R&D activities, and other costs related to R&D activities such as amortization of patents and licences. Research expenses are expensed as incurred.

Development charges are expensed unless they meet the following criteria for capitalization: the product or process is clearly defined and the attributable costs are identifiable, technical feasibility of the product or process has been established, management intends to produce and either market or use the product or process, a market for the product or process is clearly defined or its usefulness to the enterprise has been established, and adequate resources exist, or are expected to be available, to complete the project. No costs have been capitalized in 2005–2006.

R&D costs incurred to discharge long-term waste management and decommissioning obligations for which specific provisions have already been made are charged to the related liability.

n) Parliamentary Appropriations

Parliamentary appropriations that are not in the nature of contributed capital are recorded as funding in the year for which they are appropriated, except as follows. Appropriations restricted by legislation and related to expenses of future periods are deferred and recognized as funding in the period in which the related expenses are incurred. Appropriations used for the purchase of property, plant and equipment are deferred as deferred capital funding and amortized on the same basis as the related asset. From 1997 to 2006, and pursuant to the 10-year arrangement for funding decommissioning activities, the Corporation retained cash proceeds from the sale or lease of certain heavy water. The cash proceeds were transferred from contributed capital to deferred decommissioning funding and were then recorded as funding in the consolidated statement of operations as related expenditures were incurred.

o) Cost Recovery from Third Parties

The Corporation and the Canadian nuclear utilities (Ontario Power Generation, New Brunswick Power, Hydro-Québec and Bruce Power L.P.) have a common interest in the safe, efficient and economical use of power utilizing CANDU technology. Research programs aligned with these objectives are undertaken by the Corporation and cost-shared with the utilities. In addition, AECL operates the Low-Level Radioactive Waste Management Office (LLRWMO) on a cost-recovery arrangement with Natural Resources Canada. Funding under these arrangements is recorded as cost recovery from third parties and is recognized as the related expenses are incurred.

p) Pension Plan

Employees of the Corporation participate in the Public Service Pension Plan (PSPP) administered by the Government of Canada. Although the PSPP is a defined benefit plan, the Corporation is not required under present legislation to make contributions with respect to actuarial deficiencies of the Plan, and therefore, contributions to the Plan are limited to those made by the employees and the Corporation on account of current service. These contributions represent the total pension obligations of the Corporation and are charged to income on a current basis.

q) Other Employee Future Benefits

The Corporation provides certain termination benefits for current employees pursuant to collective agreements and conditions of employment. Other benefits include workers' compensation claims for which the Corporation reimburses Human Resources and Social Development Canada in accordance with the Government Employee's Compensation Act for current payments billed by the provincial compensation boards.

The Corporation accrues the cost of these employee future benefits over the periods in which the employees earn the benefits. The cost of employee future benefits earned by employees is actuarially determined using the unit credit actuarial cost method prorated on length of service and management's best estimate of salary escalation, retirement ages of employees and expected employee turnover.

New Accounting Recommendations

On April 1, 2005 the Corporation adopted the Canadian Institute of Chartered Accountants' ("CICA") accounting guideline AcG-15, Consolidation of Variable Interest Entities ("AcG-15"). AcG-15 requires the Corporation to identify entities in which it has an interest, determine whether it is the primary beneficiary of such entities and if it is the primary beneficiary, to consolidate the entity in the financial statements of the Corporation. A variable interest entity ("VIE") is an entity in which the equity invested is not sufficient to permit that entity to finance its activities without external support, or, the equity investors lack voting control, an obligation to absorb future losses, or the right to receive future returns. The primary beneficiary of a VIE is the enterprise that will absorb a majority of the VIE's expected losses, receive a majority of its expected returns, or both. The Corporation has evaluated its various business arrangements and has identified no arrangements that meet the definitions of a VIE and has concluded that AcG-15 has no impact on these financial statements.

Future Accounting Policy Changes

The CICA has issued three new accounting standards that the Corporation will adopt effective April 1, 2007: Section 1530, Comprehensive Income; Section 3855, Financial Instruments – Recognition and Measurement; and Section 3865, Hedges. These standards will be effective for AECL on April 1, 2007. The impact of implementing these new standards on the Corporation's Consolidated Financial Statements has not been determined. The following provides further information on each of the new accounting standards as they related to AECL.

Comprehensive Income

As a result of adopting these standards, a new category, accumulated other comprehensive income, will be added to shareholder's equity on the consolidated balance sheets. Major components for this category will include unrealized gains and losses on financial assets classified as available-for-sale, unrealized foreign currency translation amounts, net of hedging, and changes in the fair value of the effective portion of cash flow hedging instruments. These amounts will be recorded in the consolidated statement of other comprehensive income until the criteria for recognition in the consolidated statement of operations are met.

Financial Instruments – Recognition and Measurement

Under the new standard, for accounting purposes, financial assets will be classified as one of the following: held-to-maturity, loans and receivables, held-for-trading or available-for-sale, and financial liabilities will be classified as held-for-trading or other than held-for-trading. Financial assets and liabilities held-for-trading will be measured at fair value with gains and losses recognized in net income. Financial assets held-to-maturity, loans and receivables and financial liabilities other than those held-for-trading, will be measured at amortized cost. Available-for-sale instruments will be measured at fair value with unrealized gains and losses recognized in other comprehensive income. The standard also permits designation of any financial instrument as held-for-trading upon initial recognition. All derivatives, including embedded derivatives that must be separately accounted for, generally must be classified as held-for-trading and recorded at fair value in the consolidated balance sheet.

Hedges

This new standard specifies the criteria under which hedge accounting can be applied and how hedge accounting is to be executed for each of the permitted hedging strategies: fair value hedges, cash flow hedges and hedges of a foreign currency exposure of a net investment in a self-sustaining foreign operation. In a fair value hedging relationship, the carrying value of the hedged item is adjusted by gains or losses attributable to the hedged risk and recognized in net income. This change in fair value of the hedged item, to the extent that the hedging relationship is effective, is offset by changes in the fair value of the derivative. In a cash flow hedging relationship, the effective portion of the change in the fair value of the hedging derivative will be recognized in other comprehensive income. The ineffective portion will be recognized in net income. The amounts recognized in accumulated other comprehensive income will be reclassified to net income in the periods in which net income is affected by the variability in the cash flows of the hedged item. In hedging a foreign currency exposure of a net investment in a self-sustaining foreign operation, foreign exchange gains and losses on the hedging instruments will be recognized in other comprehensive income.

3. Cash, Cash Equivalents, Segregated Cash and Short-term Investments

Bank deposits are maintained at levels required to meet daily operating needs. Any surplus deposits are invested in the short-term money market. The investing strategy is based on a conservative risk assessment. All instruments are rated as R1 Low or higher by the Dominion Bond Rating Service and as A1 Global by Standard and Poor's. These investments are comprised of bank certificates of deposit, high-grade commercial and government agency paper, and government Treasury bills. The weighted average yield on the short-term investments held as at March 31, 2006 is 3.8% (2005 – 2.6%).

4. Inventory

(thousands of dollars)	***2006***	*2005*
Reactor fuel	**$ 9,500**	$ 8,205
Spare parts and store supplies	**6,994**	6,756
Current portion of inventory	**16,494**	14,961
Inventory – Dedicated isotope inventory (Note 10)	**44,178**	–
	$ 60,672	$ 14,961

5. Long-term Receivables

(thousands of dollars)	***2006***	*2005*
Contract receivables from customers in respect of the financing of products and services, maturing through 2019 at fixed repayment amounts	**$ 257,437**	$270,993
Current portion	**(16,232)**	(17,229)
	$ 241,205	$253,764

Repayment amounts required over subsequent years are as follows:

(thousands of dollars)	
2007	**$ 16,232**
2008	**16,045**
2009	**16,983**
2010	**17,977**
2011	**19,028**
Subsequent to 2011	**171,172**
	$ 257,437

6. Trust Fund

The *Nuclear Fuel Waste Act* required the Canadian nuclear utilities to form a waste management organization, the Nuclear Waste Management Organization (NWMO), to provide recommendations to the Government of Canada on the long-term management of nuclear fuel waste and to implement the approach selected. The legislation also requires that each nuclear fuel waste owner establish a trust fund to finance implementation of the approach. Each individual trust fund is held in order to meet the requirements of the Act and only NWMO may withdraw moneys from it in accordance with the provisions of the Act. As required by the Act, AECL's initial deposit to its Trust Fund was $10 million on November 25, 2002. Subsequent annual deposits of $2 million have been made as required, and will continue until the obligation ceases or the amount is modified by the Government of Canada once certain requirements stipulated in the Act are met by NWMO.

The Trust Fund, managed by AECL, invests in fixed income instruments, with various maturities. The fund has been recorded as a long-term

asset. Interest earned from the fund offsets accretion expense related to the decommissioning and waste management provision. These instruments comprise government bonds, high-grade corporate bonds, government agency paper, government Treasury bills and bank certificates of deposit. Quoted market values of the instruments are estimated at $17.3 million as at March 31, 2006 (2005 – $15 million) with a weighted average yield of 3.8% (2005 – 3.1%). Interest earned on trust assets accrues to the Trust Fund.

7. Heavy Water Inventory

Heavy water inventory includes 1,003 megagrams provided to the Sudbury Neutrino Observatory Institute at no cost, the majority of which is scheduled for return in 2007–2008. AECL retains the right to recall this inventory if required to meet operational needs. Heavy water inventory is recorded as a long-term asset since the lead-time required in relation to future reactor sales exceeds one year. A provision has been made for the detritiation and upgrading of certain heavy water inventory.

8. Property, Plant and Equipment

	2006		2005	
(thousands of dollars	**Cost**	**Accumulated Amortization**	Cost	Accumulated Amortization
Commercial operations				
Construction in progress	**$ 1,098**	**$ –**	$ –	$ –
Land and land improvements	**999**	**253**	999	250
Buildings	**18,698**	**12,470**	19,447	12,792
Machinery and equipment	**26,193**	**19,806**	25,825	17,743
	46,988	**32,529**	46,271	30,785
Technology				
Construction in progress	**79,422**	**–**	24,038	–
Land and land improvements	**42,986**	**22,569**	42,978	21,142
Buildings	**200,206**	**157,255**	200,505	155,939
Reactors and equipment	**270,033**	**239,424**	265,673	236,638
	592,647	**419,248**	533,194	413,719
	$639,635	**$ 451,777**	$579,465	$444,504
Net book value		**$ 187,858**		$ 134,961

Amortization of property, plant and equipment for the year ended March 31, 2006 amounted to $11.5 million (2005 – $12.0 million). Amortization of deferred capital funding was $2.4 million (2005 – $3.5 million).

9. Long-term Payables

(thousands of dollars)	**2006**	2005
Loans from Government of Canada		
Maturing September 2008 bearing interest at 2.67% to 3.36%	**$ 2,500**	$ 3,500
Long-term payable (Note 10)		
Maturing September 2012, repayments begin October 2008. Amount is net of discount of $8.9 million at 4.08%	**44,329**	–
	46,829	3,500
Less current portion	**(1,000)**	(1,000)
	$ 45,829	$ 2,500

Required payments over subsequent years are as follows (Note 10):

(thousands of dollars)	
2007	**$ 1,000**
2008	**1,000**
2009	**7,160**
2010	**13,319**
2011	**13,319**
Subsequent to 2011	**19,979**
	$ 55,777

10. Isotope Supply Agreement

During the year, AECL entered into a new agreement with MDS Nordion with respect to a long-term arrangement for the supply of isotopes. Under the agreement, AECL acquired beneficial ownership of the MAPLE reactors and New Processing Facility (NPF) currently under-construction at Chalk River, Ontario. AECL paid $25 million in consideration for acquiring these facilities and has assumed responsibility for remaining construction and commissioning activities. In addition, AECL acquired $53 million in isotopes production related

inventory with a deferred payment obligation in 48 monthly installments of $1.1 million, commencing on October 2008. The value of this inventory and the related deferred obligation were recorded at the present value of these future payments (Notes 4 and 9).

The amortization of the discount of the long-term payable of $0.2 million was expensed on the Consolidated Statement of Operations, and added to the outstanding principal balance of the related payable. Required payments are disclosed at the undiscounted amount (Note 9).

This new agreement resolved prior disputes with MDS Nordion with respect to completion of the facilities and related activities. Consequently, AECL reversed certain accruals for project losses and other provisions totalling $61 million for the year.

11. Decommissioning and Waste Management Provision

AECL has an obligation to decommission its nuclear facilities and other assets in order to satisfy Canadian Nuclear Safety Commission (CNSC) and other applicable regulations. These facilities include prototype reactors, heavy water plants, nuclear research and development, waste management and other facilities. Due to the variety of facilities, the decommissioning process may differ in each case. In some situations decommissioning activities are carried out in stages with intervals of several decades between them to allow radioactivity to decay before moving on to the next stage. These activities include surveillance and monitoring, decontamination, demolition and the management of the associated waste. A significant portion of the obligation relates to liabilities that were incurred prior to the creation of AECL in 1952.

In 2005, AECL completed a review of its decommissioning plan, the significant assumptions that underlie the estimate and the calculation of the nuclear facility decommissioning and waste management provision. The amended decommissioning plan adopted international standards with respect to prompt decommissioning practices. This involves addressing the waste early in the decommissioning cycle, and optimizing the safe storage period to avoid deferring unnecessarily activities associated with physical demolition, waste processing and ultimate disposal. The amended plan projected undiscounted expenditures of $6,800 million (in current dollars) over a period of 70 years.

The estimated future decommissioning and site remediation costs require that judgements be made about the regulatory environment, health and safety considerations, the desired end-state, technology to be employed and, in some cases, research and development activities that extend well into the future. Significant assumptions determine the valuation, such as timing of major decommissioning and remediation project expenditures, regulation requirements, volumes of waste, market based premium, interest rate estimates, inflation factors, and the impact of technological advances. Another important assumption is that the liability reflects the affordable funding level necessary to achieve health, safety and environmental protection objectives that are in accordance with CNSC regulations. Changes to these assumptions, as well as changes to the timing of the programs or the technology employed, or changes in the standards and regulations governing the decommissioning of nuclear facilities, could result in material changes to the Decommissioning and Waste Management provision.

The decommissioning plan follows a hierarchy of activities to achieve: a controlled and controllable state for all redundant nuclear facilities that removes short-term risks; a sustainable, stable, safe state of the facilities under surveillance; and cost-optimized completion of actions to achieve a final end state that is an accepted completion of the decommissioning process as required by the regulator. The discount and inflation rates used to calculate the present value of the provision, at the time the plan was implemented, were 5.25% and 1.7% respectively. In accordance with the requirements of CICA section 3110, an increase in estimates resulting from new liabilities or increases in the spending profile are discounted using a current rate of 4.3%. The table below details transactions incurred in fiscal 2006:

Decommissioning and Waste Management Provision reconciliation

(thousands of dollars)	***2006***	*2005*
Opening balance	**$ 2,750,000**	$ 945,100
Liabilities settled	**(48,829)**	(37,049)
Accretion expense	**144,375**	49,618
Revision in estimate and timing of expenditures	**1,210**	1,792,331
Closing balance	**$ 2,846,756**	$ 2,750,000

The funding of actual expenditures of $48.8 million (2005 – $37.0 million) is described in Notes 12 and 14.

12. Parliamentary Appropriations

The use of government funding by AECL's Technology Division was as follows:

(thousands of dollars)	***2006***	*2005*
Research and related infrastructure	**$ 105,249**	$ 103,738
Year 2000 reduction in appropriation	**(4,900)**	(4,900)
Advanced CANDU reactor development	**60,000**	35,000
	160,349	133,838
Program Integrity – Decommissioning activities	**–**	29,000
	$ 160,349	$ 162,838

Government funding in 2005–2006 included ongoing support for nuclear research programs, less the final part of a five-year reduction in appropriation on account of $24.5 million received in prior years to

assist in defrayment of the Year 2000 computer costs, and funding for the development of the Advanced CANDU reactor (ACR) program. In the previous year, the Corporation received funding of $29 million for activities under the government's Program Integrity initiative for health and safety upgrades, including the safe long-term management of nuclear materials or waste. Appropriations are recognized in the Technology segment and not used to fund Commercial operations.

13. Employee Future Benefits

a) Pension Plan

The Corporation's employee pension benefits are covered through the Public Service Pension Plan (PSPP). Payments are made to three accounts: Public Service Superannuation Account (PSSA), Public Service Pension Fund account (PSPF), and the Retirement Compensation Arrangement account (RCA). Total contributions made on account of current service are as follows:

(thousands of dollars)	***2006***	*2005*
Payments by employees	**$ 14,545**	$ 13,651
Payments by employer	**$ 32,891**	$ 31,041

The Corporation's rate of contribution to the PSPF account is a 2.14 multiple of the employee contributions (2005 – 2.14). The contribution to the RCA account for calendar year 2006 is a multiple of 7.2 of the employee contributions (calendar year 2005 – 8.9). The multiple is subject to change based on revaluation by the PSPP administration.

b) Other Employee Future Benefits

The Corporation provides certain termination and other benefits as described in note 2 (q). The accrued benefit obligation is not funded as funding is provided when benefits are paid. Accordingly, there are no plan assets and the plan deficit is equal to the accrued benefit obligation.

(thousands of dollars)	***2006***	*2005*
Accrued benefit obligation, beginning of year	**$ 73,353**	$ 69,635
Current service cost	**3,548**	3,311
Interest on accrued benefit obligation	**3,893**	4,018
Benefits paid	**(4,650)**	(5,295)
Actuarial (gains) losses	**(1,992)**	1,684
Accrued benefit obligation, end of year	**74,152**	73,353
Unamortized net actuarial losses	**(11,885)**	(14,534)
Accrued benefit liability	**62,267**	58,819
Current portion, accrued benefit liability	**(6,511)**	(6,071)
Net accrued benefit liability	**$ 55,756**	$ 52,748
Net benefit plan cost		
Current service cost	**$ 3,548**	$ 3,311
Interest cost	**3,893**	4,018
Amortization of actuarial losses	**658**	593
Annual benefit plan expense	**$ 8,099**	$ 7,922

Cumulative actuarial gains or losses in excess of 10% of the obligation are amortized over the remaining average service period of active employees. The average remaining service period of the active employees covered by the other employee future benefits plan is 11 years (2005 – 11 years). The measurement date of the accrued benefit obligation is March 31, 2006, and the latest actuarial valuation of these benefits was performed in March 2006. The next valuation will be performed in March 2007.

The significant actuarial assumptions adopted in measuring the Corporation's accrued benefit obligation are:

- a discount rate of 5.25% (2005 – 5.25%)
- a rate of compensation increase of 5% (2005 – 5%)

14. Contributed Capital and Deferred Decommissioning Funding

Included in contributed capital is approximately $267 million (2005 – $291 million) related to parliamentary appropriations received for the production of heavy water inventory. Up to and including 1995–1996, the Corporation was required to repay the Government of Canada, by way of a dividend, the cash proceeds from the sale of government-funded heavy water. From 1997 to 2006 a Decision by the Treasury Board directed the Corporation to hold the proceeds from the sale or lease of government-funded heavy water in a segregated fund for use in decommissioning activities for the 10-year period following the Decision. As government-funded heavy water was sold or leased, the cash proceeds were transferred from contributed capital to deferred decommissioning funding, which was used to fund ongoing decommissioning activities.

Subsequent to 2005–2006, the prior arrangement will apply whereby cash proceeds, including interest and principal on long-term receivables from heavy water sales, would be repayable to the Government of Canada and decommissioning activities would be funded through parliamentary appropriations. Accordingly, the Corporation expects that the Government of Canada will continue to finance this obligation. (Note 19)

15. Related Party Transactions

In addition to the transactions disclosed in Notes 9, 12,13 and 14, the Corporation had the following transactions with the Government of Canada:

(thousands of dollars)	***2006***	*2005*
Repayment of loans		
Principal	**$ 1,000**	$ 1,000
Interest	**81**	96
	$ 1,081	$ 1,096

In the normal course of business, the Corporation also enters into various transactions with the Government of Canada, its agencies and other Crown Corporations. These transactions are recorded at the exchange amount.

16. Commitments and Contingencies

a) Commitments

The Corporation has entered into non-cancellable operating leases expiring on various dates for the rental of office space. The leases contain an escalation clause providing for additional rent. Minimum future lease payments under these operating leases are as follows:

(thousands of dollars)	
2007	$ 6,638
2008	6,802
2009	6,176
2010	2,106
2011	822
Subsequent to 2011	6,503
	$ 29,047

b) Performance Guarantees & Liquidated Damages

It is industry practice to use letters of credit, surety bonds and other performance guarantees on major contracts. Such guarantees may include guarantees that a project will be completed or that a project or particular equipment will achieve defined performance criteria.

AECL also guarantees that certain projects will be completed within a specified time and may bear responsibility for liquidated damages should obligations not be met.

The aggregate amount of the Corporation's potential exposure under the performance guarantees is estimated to be $76 million on current commercial projects as at March 2006 (2005 – $102 million). In addition to performance guarantees, liquidated damages as of March 2006 are estimated to be $105 million (2005 – $nil). Management does not expect these guarantees to have a material impact on the consolidated financial statements of the Corporation.

c) Other

In the normal course of operations, AECL has become involved in various claims and legal proceedings. While the final outcome with respect to claims and legal proceedings pending at March 31, 2006 cannot be predicted with certainty, it is the opinion of management that their resolution will not have a material adverse effect on AECL's financial position or results of operations.

17. Financial Instruments and Financial Risk Management

a) Foreign Currency Exchange

The Corporation enters into foreign exchange forward contracts to reduce the risk associated with the purchase and sale of goods in foreign currencies. There are thirty-one (2005 – one) forward contracts with a notional value of $28 million (2005 – $0.9 million) and fair value equivalent to book value as at March 31, 2006.

b) Credit Risk

The Corporation is exposed to credit risk in the collection of its accounts receivable. Three customers (2005 – three), each representing greater than 10 per cent of the total accounts receivable, comprise an aggregate 77% (2005 – 67%) of total accounts receivable. No significant amounts are due in foreign currency.

c) Interest Rate Risk

The Corporation is exposed to interest rate risk through its asset retirement obligations. Changes in the discount rate are based on a credit adjusted risk-free rate that is sensitive to interest rate fluctuations.

d) Regulatory Risk

The nature of the business environment the Corporation operates in is highly regulated. Changes in political environment or government policy may have an adverse impact on the Corporation's financial position.

e) Fair Value

Fair value represents management's estimates of the market value at a given point in time. The carrying value of all financial assets and liabilities approximate fair value as at March 31, 2006 and 2005 with the exception of Long-term receivables. The fair value of Long-term receivables is $256.2 million (2005 – $266.7 million).

18. Segmented Information

The Corporation has three reportable operating segments; Commercial Operations, Technology, and Liability Management Unit. The accounting policies of the segments are the same as those described in Note 2. These segments represent strategic business units established by senior management to facilitate the achievement of the Corporation's long-term objectives, to aid in resource allocation decisions and to assess operational performance. AECL monitors and evaluates each division's performance based on net operating income, defined as revenue less operating expenses. Revenues generated and expenses incurred on transactions between segments approximate fair value and are eliminated on consolidation. AECL does not own capital assets that reside in countries outside Canada.

Commercial Operations

This segment is largely responsible for two lines of business: Projects and Services. Projects include new build projects and refurbishment projects together with related project management services, equipment procurement and deliveries and the sale of heavy water. Services

include a full line of engineering and technical services that supports operating CANDU plants and improves customer productivity and competitiveness.

Technology

This segment develops new reactor technology and supports the safety, licensing and design for the life cycle of the CANDU product set and other Canadian nuclear technology. Business activities include engineering and development of the Advanced CANDU Reactor, manufacture and sale of medical isotopes, operations of nuclear facilities and carrying out the Government of Canada's policy mandate in support of nuclear technology and the nuclear industry.

This business segment is closely linked to Commercial Operations and the Liability Management Unit (LMU), supporting commercial project delivery activity, new product development and execution of the decommissioning and waste management program.

Liability Management Unit

The segment operates as a procurement and planning office with a mandate to manage the decommissioning and waste management program in a cost effective manner and to oversee funding received from the Government of Canada for the program. Included with LMU assets is an amount related to parliamentary appropriations received for the production of heavy water inventory as described in Note 14.

	*Commercial Operations**		*Technology*		*Liability Management Unit*		*Consolidated*	
(millions of dollars)	***2006***	*2005*	***2006***	*2005*	***2006***	*2005*	***2006***	*2005*
Operating revenue								
Total operating revenue	**$ 329.7**	$ 312.6	**$ 158.9**	$ 77.4	**$ 3.8**	$ –	**$ 492.4**	$ 390.0
Inter-segment revenue	**(9.8)**	(11.3)	**(71.6)**	(22.2)	**(3.8)**	_	**(85.2)**	(33.5)
External operating revenue**	**319.9**	301.3	**87.3**	55.2	**–**	–	**407.2**	356.5
Funding and cost recovery	**_**	_	**180.1**	152.6	**55.8**	46.6	**235.9**	199.2
Operating income (loss)***	**46.8**	72.2	**33.8**	(106.5)	**(75.1)**	(1,806.6)	**5.5**	(1,840.9)
Amortization of property, plant and equipment	**1.9**	1.9	**7.2**	6.6			**9.1**	8.5
Accretion expense					**144.4**	49.6	**144.4**	49.6
Segmented Assets	**407.0**	341.1	**249.5**	147.2	**289.3**	333.3	**945.8**	821.6
Cash and short term investments							**108.7**	41.6
Total Assets****							**1,054.5**	863.2
Segmented Liabilities	**261.9**	85.4	**135.6**	177.8	**2,852.3**	2,778.3	**3,249.8**	3,041.5
Employee future benefits							**55.8**	52.7
Total Liabilities							**$3,305.6**	$3,094.2

	2006	*2005*
Revenues by geographic segment		
Canada	**$ 224.6**	$ 129.4
Europe	**110.7**	127.0
Asia	**58.9**	91.5
Other	**13.0**	8.6
Total revenue	**$ 407.2**	$ 356.5

** Commercial Operations had one customer (2005 – two) that contributed 24% of AECL's revenue (2005 – 45%).*
*** Commercial Operations includes $15.2 million of interest revenue (2005 – $16.3 million) related to long-term receivables.*
**** The 2006 amount includes a $60.9 million gain on reversal of accrued project losses and provisions (Note 10).*
***** Includes capital expenditures for Commercial Operations of $2 million (2004 – $1 million) and Technology of $54 million (2004 – $7 million).*

19. Subsequent Events

As of April 1, 2006, the 1997 decision of the Treasury Board allowing AECL to retain a portion of the cash proceeds on sale of government-funded heavy water sales as deferred decommissioning funding had not been renewed. Decommissioning activities are now expected to be funded through parliamentary appropriations. The Corporation is currently in discussions with the Government of Canada regarding the use of cash proceeds from heavy water sales. These discussions may impact $256 million of long-term receivables, $160 million of heavy water inventory, and $267 million of contributed capital.

20. Comparative Figures

Certain of the 2005 comparative amounts have been reclassified from financial statements previously presented to conform to the 2006 financial statement presentation.

BOARD OF DIRECTORS

JEAN-PIERRE SOUBLIÈRE

Appointed October 20, 2005, Acting Chair of the Board, AECL, Mississauga, Ontario

President, Anderson Soublière Inc., Ottawa, Ontario

Formerly President of SHL Systemhouse Canada and International, and President and COO of Alis Technologies. Directorships include: the University of Ottawa, United Way of Canada (Past Chair), Provance Technologies Inc. (Chair), the Harmony Foundation (Chair). Appointed October 1998. Committees: Audit; Science & Technology; Human Resources & Governance; Risk Evaluation.

ROBERT G. VAN ADEL

President & CEO, AECL, Mississauga, Ontario

Formerly an Executive Vice-President at Export Development Canada and the President of AGRA Engineering Inc. Directorships include: Canadian Nuclear Association, Nuclear Energy Institute (USA), Canada China Business Council, Energy Council of Canada, Junior Achievement of Central Ontario. Mr. Van Adel was appointed President & CEO of AECL in February 2001. Committees: Risk Evaluation; Science & Technology.

MARCEL AUBUT, Q.C.

Lawyer, senior partner, Heenan Blaikie, law firm, Quebec

Previously President, Chairman & CEO of the Quebec Nordiques (Quebec City's franchise in the National Hockey League) and Governor of the NHL; Founder of Aubut Chabot (Quebec City law firm); Chairman of the Québec Metro High Tech Park; President and CEO of Trans-America Productions Ltd. Current directorships include: Olybro inc; Æterna Zentaris Inc.; Boralex Power Income Fund; Triton Electronik Inc.; Faculty of Law, Laval University; Canadian Olympic Committee (Board of Directors and Executive Committee); Canada's Sports Hall of Fame, Mont Tremblant Resort, Fondation Nordiques. Member (1986) and Officer (1993) of the Order of Canada, Official Medal of the Quebec National Assembly (1981), Queen's Counsel (1986), and inducted into Canada's Sports Hall of Fame in 1999. Appointed January 2001. Committees: Human Resources & Governance; Nominating.

DOUGLAS THOMPSON

Lawyer, Hatter, Thompson, Shumka & McDonagh, Victoria, B.C.

Member of the Law Society of B.C. and the Canadian Bar Association. Former Directorships include: British Columbia Hydro and Power Authority, the Power Exchange Corporation (Powerex), the University of Victoria, and the Victoria Bar Association. Appointed September 2002. Committees: Chair – Risk Evaluation; Vice Chair – Science & Technology.

BARBARA TRENHOLM

Professor, Faculty of Business Administration, University of New Brunswick, Fredericton, N.B.

Fellow Chartered Accountant. Other directorships include: Plazacorp Retail Properties Ltd. Formerly a member of the Canadian Institute of Chartered Accountant's board of directors, co-chair of the University of New Brunswick's Pension Board of Trustees, president of the New Brunswick Institute of Chartered Accountants, and acting dean of UNB's Faculty of Business Administration. Appointed June 2002. Committee: Chair – Audit.

STELLA THOMPSON

Governance Consultant and Director, Principal and Co-Founder of Governance West Inc., Calgary, Alberta

Current directorships include: Alberta's Electricity Balancing Pool, Calgary Airport Authority, Canada Foundation for Innovation, Genome Alberta (Vice Chair), and Talisman Energy Inc. Formerly a Vice-President at Petro-Canada. Appointed September 2002. Committees: Chair – Human Resources & Governance; Audit; Nominating.

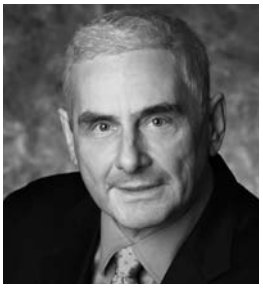
ROBERT J. HARDING F.C.A.

Chairman Brookfield Asset Management Inc.

Fellow Chartered Accountant (F.C.A.), Awarded the Queen's Golden Jubilee Medal for community service and an honorary Doctor of Laws Degree from University of Waterloo. Current directorships include Brookfield Asset Management, BPO Properties Limited, Norbord Inc, and Fraser Papers Inc. He is also Chair of the board of governors of University of Waterloo, Vice Chair of United Way of Greater Toronto Board of Trustees and a Trustee of the Toronto Hospital for Sick Children. Appointed May 2005. Committees: Vice Chair – Audit; Risk Evaluation.

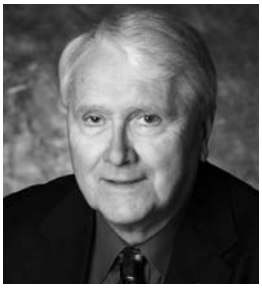
PETER P. DHILLON
President & CEO, Richberry Group of Companies, Richmond, B.C.

Directorships include: Vice Chairman, Ocean Spray Cranberries, Inc., Chairman of the Audit Committee for the Vancouver Organizing Committee for 2010 Winter Olympics and Vice Chairman of the Agricultural Lands Commission. Formerly Vice Chairman for B.C. Ferries and Director, Canada Customs and Revenue Agency. Appointed November 2002. Committee: Science & Technology.



CLAUDE LAJEUNESSE
President, Concordia University, Montreal, Quebec

Formerly President of Ryerson University, Toronto, and President & CEO of the Association of Universities and Colleges of Canada (AUCC). Member of the Board of TD Meloche Monnex. Appointed March 2005. Committees: Vice-Chair – Risk Evaluation; Science & Technology.



JAMES (JASPER) MCKEE
Professor Emeritus, University of Manitoba, Winnipeg, Manitoba

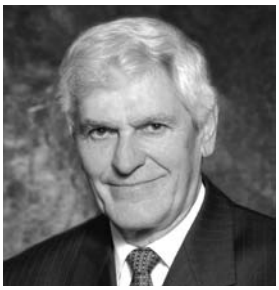
Formerly Professor of Physics at the University of Manitoba and Director of its Accelerator Centre. Fellow of the Institute of Physics (UK) and past President of the Canadian Association of Physicists, past membership of the National Advisory Board on Science and Technology. Directorships include: President Canadian Club of Winnipeg, Westminster Housing Society, elected member of the European Academy of Sciences. Also the Editor of *Physics in Canada*. Appointed December 1995. Committees: Chair – Science & Technology; Human Resources & Governance.

MARNIE PAIKIN
Director, Hamilton, Ontario

Commissioner of the Ontario Human Rights Commission 1996 to 2005. Recipient of Ontario's "Outstanding Woman Award" and the Human Relations Award of the Canadian Council of Christians and Jews. Former director of Westcoast Energy Inc. and Union Gas Ltd. Inducted into the Hamilton Gallery of Distinction and a Member of the Order of Canada. Appointed July 1985. Committees: Chair – Nominating; Vice Chair – Human Resources & Governance; Risk Evaluation.

J. RAYMOND FRENETTE
Retired September 23, 2005, Chair of the Board, AECL, Mississauga, Ontario

Previously Chairman New Brunswick Power Corporation and former Premier of New Brunswick. Elected to the New Brunswick Legislative Assembly in 1974, he was Minister of Health and Community Services, Government House Leader, Deputy Premier and President of the Executive Council. Previous Directorships include Service New Brunswick and the Canadian Millennium Scholarship Fund.



PIERRE FORTIER
Resigned August 19, 2005, Company Administrator and Consultant, Montreal, Quebec

Formerly Vice-President, Corporate Affairs of SNC Inc. and President of Canatom Inc. Served for seven years on Canada's Advisory Council on Science & Technology. Served as President of Societe financiere des Caisses Desjardins. During nine years as an elected Member of the Quebec National Assembly he was Minister of Privatization and Associate Minister of Finance responsible for financial institutions. Directorships include Univalor Inc. and Fondation de Polytechnique where he serves as President.

TERRY VINCENT MCCANN, Q.C.
Retired May 6, 2005, Retired Lawyer, Pembroke, Ontario

Former Mayor of the City of Pembroke. Previous directorships included Saint Francis Xavier University, deHavilland Aircraft Company of Canada, Pembroke Police Commission (Chairman), Pembroke Hydro Commission, and many Pembroke area commercial and charitable organizations. Terry has an Executive MBA from Queen's University and is a recipient of a 125th Confederation Commemorative Medal.

OFFICERS

ROBERT G. VAN ADEL
President and Chief Executive Officer

RICHARD COTÉ
Vice-President, Finance

PAUL FEHRENBACH
Vice-President, Special Advisor

DENNIS GALANGE
Vice-President, Ontario Strategy

ALLAN HAWRYLUK
Vice-President, Corporate Affairs, General Counsel & Corporate Secretary

KEN HEDGES
Vice-President, Dedicated Isotopes Facility

MICHAEL INGRAM
Vice-President, CANDU Services

BRIAN MCGEE
Vice-President, Nuclear Laboratories

BETH MEDHURST
Vice-President, Human Resources

KEN PETRUNIK
Senior Vice-President & Chief Operating Officer

MICHAEL ROBINS
Senior Vice-President, Chief Financial Officer

MICHAEL TAYLOR
Vice-President, Special Projects

PATRICK TIGHE
Vice-President, Marketing & Business Development

DAVID F. TORGERSON
Senior Vice-President & Chief Technology Officer

CORPORATE GOVERNANCE

At AECL, corporate governance continues to reflect the best practices for Crown corporations and publicly traded companies. AECL firmly believes from its research that leading Canadian companies are also pacesetters in the area of corporate governance. In 1998, AECL established *Corporate Governance Guidelines* based upon the recommendations of the Treasury Board of Canada in its publication entitled, *Corporate Governance in Crown Corporations and Other Public Enterprises* and also based upon AECL's research of other leading companies. Since that time, AECL has continued to improve its governance structure through the work and leadership of the committees of the Board including the Audit, Human Resources and Governance, Risk Evaluation, Science and Technology and Nominating Committees. In the fiscal year 2005, AECL actively participated in the Treasury Board review of Crown Corporations. Many of AECL's views, including the introduction of its corporate policy on "Disclosure of Wrongdoings" (the whistleblower policy), were reflected by the Treasury Board Report, *Review of the Governance Framework for Canada's Crown Corporations* in February, 2005.

In 2005, AECL introduced the requirement for all directors and employees to sign a declaration confirming no conflict of interest as part of meeting their responsibilities pursuant to the corporation's *Code of Ethics and Business Conduct Policy*. From the signed declarations, there were no breaches of the aforementioned policy.

The Board recognizes that effective corporate governance is important to identify and manage potential risks and opportunities and ensure transparent accountability to the Government, Parliament and Canadians. Overall, the Board is satisfied that its corporate governance structure met and exceeded the recommendations made by the Auditor General of Canada respecting corporate governance for Crown corporations assessed annually through detailed surveys.

The Board

The Board of Directors of AECL is comprised of thirteen members, including AECL's President and Chief Executive Officer. At the present time, there are two vacancies. Directors are appointed by the Minister of Natural Resources with approval by the Governor-in-Council for a term of three years and are eligible for re-appointment upon the expiration of their terms. The Board oversees the strategic direction for the organization as well as its financial management and corporate systems. With the exception of the President and CEO, all Board members are independent of management. The Chairs of each of the five committees are also independent of management. It is the practice of the Board members to meet *in camera* at all regular Board meetings.

In 2005, AECL's Board of Directors assessed its own performance against best practices. To further continuous improvement, the Board established an action plan of items to enhance its effectiveness and demonstrate accountability to the shareholder. In addition, key activities included:

- Participation by new Board members in a detailed orientation program and training.
- Continuing education programs for Board members sponsored by the Privy Council Office.
- Recommendation by the Board, supported by the Nominating Committee (composed of independent directors and two prominent outside independent members) to reappoint the current President and CEO, Mr. Robert Van Adel to an additional five-year term which was subsequently confirmed following a Parliamentary review process undertaken by the Standing Committee on Industry, Natural Resources, Science and Technology.
- Developed a more streamlined performance and financial reporting system aligned to AECL's goals and objectives and strategic plan.

Board Remuneration

Directors are each paid a base annual retainer of $7,200.00 and a *per diem* of $555.00, as set by the Governor in Council pursuant to the *Financial Administration Act*. Currently, the Acting Chair receives the base annual retainer of $7,200.00 and a *per diem* of $555.00 for Board related work. The retainer for each of the Chairs of the Committees is $9,200.00 (a marginal increase of $2,000.00 over the base retainer) and a *per diem* of $555.00 for Board related work. For the fiscal year, the average remuneration for each director amounted to approximately $20,000.00 for Board and Committee meetings and other Board related work. Directors are also reimbursed for all reasonable out-of-pocket expenses, including travel, accommodation and meals while on company business. These expenses averaged $10,863.92 for each director over the fiscal period.

In 2005–2006, the Board met 6 times for a total of 11 days and additionally held 8 teleconferences (for a total of 19 meetings) while the Committees met for a total of 29 meetings. For Board and Committee meetings, the attendance was at 86% and 89%, respectively. The table on page 65 sets forth the record of attendance for Board and Committee meetings for each of the independent directors for the fiscal year commencing April 1, 2005 and ending March 31, 2006.

Nominating Committee

MR. ALEX TAYLOR

DR. HUGH WYNNE-EDWARDS

AECL's Nominating Committee was established in 2004 and is made up of three independent directors and two prominent outside independent members. The mandate of this Committee is to identify candidates for the position of Chair of the Board, President and Chief Executive Officer and members of the Board, as and when appropriate. From time to time, this Committee obtains recommendations from an independent third party for potential candidates. In 2005, the Nominating Committee completed the following initiatives after an extensive review process:

- Searched for prospective members by matching an individual's skill sets to a competency profile developed by the Human Resources and Governance Committee.
- Reviewed and assessed the Board members' skill sets in order to ascertain if any gaps were present.
- Identified and recommended a short list of qualified candidates to the Minister of Natural Resources.
- Recommended to the Minister the appointment of the Acting Chair.

Audit Committee

The Audit Committee is composed of three independent directors with the Chair of the Board an *ex officio* member of the Committee. The Committee advises the Board on the financial management of AECL as well as assists the Board in overseeing the internal control systems, financial and audit processes. All members of the Committee have extensive financial background and experience. During the past year, the Committee assisted the Board in AECL's transition to new external auditors.

Table of Directors' Attendance at Meetings of the Board, and at Board Committees, 2005–2006

Director	*Audit (6 meetings)*	*Science & Technology (3 meetings)*	*Human Resources & Governance (6 meetings)*	*Risk Evaluation (8 meetings)*	*Nominating (6 meetings)*	*Board of Directors (19 meetings)*
J.P. Soublière[1]	5/6	2/2	2/2	3/3	N/A	17/19
R. Van Adel	N/A	3/3	N/A	4/8	N/A	17/19
M. Aubut	N/A	N/A	6/6	N/A	4/6	17/19
P. Dhillon	N/A	1/3	N/A	N/A	N/A	9/19
R. Harding	5/5	N/A	N/A	0/1	N/A	12/17
C. Lajeunesse	N/A	2/3	N/A	3/4	N/A	16/19
J. McKee	N/A	3/3	6/6	N/A	N/A	17/19
M. Paikin	N/A	N/A	4/6	6/8	6/6	15/19
D. Thompson	N/A	3/3	N/A	8/8	N/A	19/19
S. Thompson	6/6	N/A	6/6	N/A	6/6	17/19
B. Trenholm	6/6	N/A	N/A	7/7	N/A	19/19
R. Frenette[2]	4/4	N/A	4/4	5/5	N/A	8/8
P. Fortier[3]	N/A	N/A	N/A	5/5	N/A	6/6
T. McCann[4]	1/1	N/A	N/A	N/A	N/A	2/2
Outside Eminent Persons – Nominating Committee						
H. Wynne-Edwards					6/6	
A. Taylor					6/6	

1 Jean-Pierre Soublière was appointed Acting Chair on October 20, 2005
2 Raymond Frenette retired on September 23, 2005
3 Pierre Fortier resigned on August 19, 2005
4 Terry McCann retired on May 6, 2005

In keeping with best practices, the Committee regularly met on the following basis:

- Regular meetings with only the members of the Committee.
- Regular meetings with senior management.
- *In camera* with external auditors without the presence of management.
- *In camera* with Internal Audit.

In 2005, the Committee assessed its own performance and reported to the Board on its initiatives with regard to the Committee's mandate. In an ongoing effort to ensure the policies of AECL were aligned with its strategic plan and to maintain transparency of its operations, the Audit Committee reviewed AECL's legal and ethical compliance programs, in particular, AECL's *Code of Ethics and Business Conduct*. As part of AECL's commitment to corporate governance, the Chair of the Audit Committee reviews, on an ongoing basis, the detailed travel expenses of the Chair of the Board and the President and CEO.

Science and Technology Committee

This Committee is made up of four independent members with assistance from an Advisory Panel of highly qualified independent research advisors. This Committee provides the Board and AECL with an independent review and assessment of the corporation's research and development programs and product development programs, including the Advanced CANDU Reactor (ACR), to ensure they are responsive to the objectives of the corporation, reflect market requirements, and provide value for money. In addition, this Committee reviews programs directed at protection of the environment as well as reviews policies to ensure AECL's intellectual property is protected. Overall, this Committee is responsible for setting policy, monitoring and providing oversight in the areas of AECL's science, technology and environmental programs. This Committee also provides an interface with the regulator, the Canadian Nuclear Safety Commission, and a technical interface with the shareholder, the Government of Canada. In 2005, this Committee, with the assistance of the Research and Development Advisory Panel, assessed and provided independent advice to the Board through the Committee validating AECL's research and development activities.

Human Resources and Governance Committee

This Committee is composed of four independent members of the Board and is responsible for overseeing and advising the Board on all aspects of corporate governance, corporate policies and strategies related to human resources including health and safety, succession planning, compensation, training and recruitment.

In 2005, this Committee defined the responsibilities for the Chair of the Board. The Committee also reviewed the updated succession plan prepared by senior management for key positions within the organization. The Committee reviewed its corporate governance practices and made recommendations to the Board in relation to its *Corporate Governance Guidelines* established the previous year. Areas of governance included the updating of Board practices and procedures relating to the frequency, length and content of materials and information provided to the Board. Other highlights included ongoing training programs for the Board and programs for development of management.

Risk Evaluation Committee

This Committee, made up of four independent members, evaluates, on behalf of the Board, risk areas associated with significant contracts, proposals and other business ventures. In 2005, the Committee evaluated the risks associated with key projects including Pt. Lepreau, Bruce Power and the MMIR agreement. The MMIR agreement with MDS Nordion is a long-term agreement for the supply of isotopes.

Summary

This past year both the Board and management have continued to improve the corporate governance practices to ensure the organization operates to the highest standards, which has become a way of life within the corporation. The initiatives undertaken by the Board and the Committees during the fiscal year reflect transparency and accountability and sound governance. The ongoing commitment to corporate governance ensures that AECL operates to the highest ethical standards while at the same time delivering value to our shareholder, customers and to all Canadians.

FIVE-YEAR CONSOLIDATED FINANCIAL SUMMARY

Unaudited

(millions of dollars)	***2006***	*2005**	*2004**	*2003**	*2002**
Commercial Operations					
Revenue	**$ 303**	$ 283	$ 407	$ 473	$ 404
Interest revenue	**17**	18	20	9	4
Net income	**$ 47**	$ 72	$ 74	$ 33	$ 34
Technology					
Revenue	**$ 87**	$ 55	$ 60	$ 89	$ 88
Funding	**180**	153	173	128	157
Gains	**61**	–	–	–	–
Net income (loss)	**$ 34**	$ (106)	$ (40)	$ (44)	$ 21
Liability Management Unit					
Funding	**$ 56**	$ 47	$ 50	$ 48	$ 30
Net loss	**$ (75)**	$ (1,807)	$ (68)	$ (40)	$ (28)
Financial position					
Cash, cash equivalents, segregated cash and short term investments	**$ 111**	$ 67	$ 125	$ 159	$ 157
Heavy water inventory	**299**	300	300	427	563
Capital expenditures	**56**	8	14	22	23
Property, plant and equipment	**188**	135	127	128	117
Decommissioning and waste management provision	**2,847**	2,750	945	915	901
Long-term payables (excludes current portion)	**$ 46**	$ 3	$ 4	$ 5	$ 6
Other					
Export revenues	**$ 183**	$ 225	$ 358	$ 361	$ 257
Number of full-time employees	**3,604**	3,221	3,214	3,334	3,456

**Certain of these amounts have been reclassified to conform to the 2006 Financial Statement presentation.*

GLOSSARY OF TERMS

Base Load: The minimum continuous load or demand required over a given period of time at a steady rate. Variations in load due to temperature, production, etc., are in addition to base load.

Base Load Capacity: Generating capacity that tends to operate continuously and steadily, due primarily to its low unit operating costs. Base load output is generally not adjusted to follow demand fluctuation.

CANDU: Canada deuterium uranium reactor, moderated and cooled by heavy water.

Capacity: The maximum volume of power that can be produced or delivered under specified conditions by a generator or system, measured on an instantaneous basis. Typically expressed in megawatts.

Core: The central part of a nuclear reactor containing the fuel elements and any moderator.

Decommissioning: The permanent removal of a facility from active service. In the case of a nuclear plant this includes safely closing, and possibly dismantling (or otherwise disposing of) the existing facilities at the end of their service life.

Energy: In an electrical system, a quantity of electric power, typically expressed as kilowatt-hours (kWh), megawatt-hours (MWh), or gigawatt-hours (GWh). Differs from electric *capacity*, which is measured in kilowatts or megawatts.

Fossil fuel: A fuel based on carbon presumed to be originally from living matter, eg coal, oil, gas. Burned with oxygen to yield energy.

Fuel bundle: The package of natural uranium fuel elements for insertion into a CANDU reactor. The uranium is contained in zirconium alloy tubes or elements and the elements are held together by welding them to zirconium alloy plates. Each bundle is a half a metre long and weighs about 20 kg.

Greenhouse Gas Emissions: Discharge into the atmosphere of gases – primarily carbon dioxide, methane and nitrous oxide – believed to contribute to global warming. Main sources include fossil fuel generating plants, transportation vehicles and industrial production.

Heavy water: Water containing an elevated concentration of molecules with deuterium ("heavy hydrogen") atoms.

Isotope: An atomic form of an element having a particular number of neutrons. Different isotopes of an element have the same number of protons but different numbers of neutrons and hence different atomic mass, eg. U-235, U-238. Some isotopes are unstable and decay (qv) to form isotopes of other elements.

MACSTOR: MACSTOR (Modular Air-Cooled STORage) units were developed by AECL as safe, highly-efficient, above-ground modules for storing used fuel from CANDU and other types of reactors.

Megawatt (MW): Unit of electricity equal to one million watts or one thousand kilowatts. Typically used to measure the power production capacity of a generating station or the maximum demand of an electricity consumer.

NRU: The 200-megawatt National Research Universal research reactor at Chalk River Laboratories. It started up in 1957 and currently produces about 60% of the world's supply of molybdenum-99, a critical isotope used for medical diagnostic purposes.

Nuclear reactor: A device in which a nuclear fission chain reaction occurs under controlled conditions so that the heat yield can be harnessed or the neutron beams utilized. All commercial reactors are thermal reactors, using a moderator to slow down the neutrons.

Radiation: The emission and propagation of energy by means of electromagnetic waves or particles. (cf ionising radiation)

Radioactivity: The spontaneous decay of an unstable atomic nucleus, giving rise to the emission of radiation.

Refurbishment: Large-scale replacement of a CANDU reactor's primary components. Refurbishment of a CANDU reactor can extend its life cycle by 25–30 years.

Regulator: An entity with the legislative authority to develop, impose and enforce regulations in a given industry or industries.

Spent fuel: Fuel assemblies removed from a reactor after several years use.

Sustainable Development: Economic development that meets the needs of the present without compromising the ability of future generations to meet their own needs.

AECL OFFICES

CANADA

AECL
2251 Speakman Drive
Mississauga, Ontario
Canada L5K 1B2

AECL
Chalk River Laboratories
Chalk River, Ontario
Canada K0J 1J0

AECL
Whiteshell Laboratories
Pinawa, Manitoba
Canada R0E 1L0

AECL
Place de Ville, Tower B
112 Kent Street,
Suite 501
Ottawa, Ontario
Canada K1A 0S4

AECL
1000, rue de la
Gauchetière ouest
14e étage, Suite 1440
Montréal, (Québec)
Canada H3B 4W5

AECL
1400 Bayly Street,
Units 20-22
Pickering, Ontario
Canada L1W 3R2

AECL
Low Level Radioactive
Waste Management
1900 City Park Drive,
Suite 200
Gloucester, Ontario
Canada K1J 1A3

AECL
Point Lepreau
Refurbishment Office
430 Bayside Drive
Saint John, New Brunswick
Canada E2J 1A8

U.S.A.

AECL Technologies
481 North Frederick Ave,
Suite 405, Gaithersburg,
Maryland 20877 USA

SOUTH KOREA

4th Floor, IL Won Building
1000-1 Daechi-dong,
Kangnam-Ku
Seoul, 135-280
South Korea

CHINA

Suite 2912, North Tower
Beijing Kerry Centre
1 Guang Hua Road
Chao Yang District
Beijing 100020,
People's Republic of China

Inquiries
Public Requests for
Information/Media Inquiries
Phone: 905-823-9040 ext. 7539
Toll free: 1-866-886-2325

Marketing Services
Email: info@aecl.ca

Visit Our Website
www.aecl.ca

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annuel sera fournie sur demande.

Photos:

Front cover, 2nd photo from left: Amy Siegner and Clayton McGregor, Sheridan Park.

Front cover, 3rd photo: Laura Hansen, Chalk River.

Page 1, top photo: Stuart Parrott, Mechanical R&D Engineer, Whiteshell.

Page 1, bottom photo: Daniel Kuchar, Mechanical Engineer (left) and Dave Gunn, Fuel Channel Design Engineer, Sheridan Park.

Page 3: Craig Buchanan, Metallurgical Technician (left) and James Valliant, Hot Cell Technician, Chalk River. Hot cell manipulators, post irradiation examination.

Page 3, middle: John Rabiasz, Senior Technologist (left) and Taifoor Ali, Mechanical Technician, Sheridan Park Fuelling machine.

Page 15: Construction of Qinshan Unit 2, China.

Page 19: Awad Beekhoo, Senior Engineering Development Technologist, Sheridan Park. ACR-1000 flow visualization test rig of a reactor fuel channel.

Page 23: Laura Hansen, university student with Environmental Technologies, and Adam Miller, Environmental Technician, Chalk River. Riverbed core sampling.

Back cover, left to right: Yvan Lachance, Systems Analyst, Chalk River; Tracey Kemp, Chalk River; Mark Carney, Sheridan Park.

Canada

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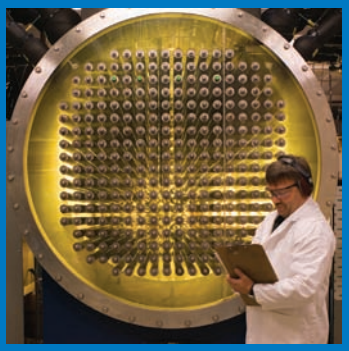
AECL LEADING THE WAY




CANDU Nuclear = Power

51% of Ontario's electricity (16% of Canada's) comes from CANDU nuclear power.

CANDU Nuclear = Clean Air

CANDU nuclear is an energy source that does not produce harmful greenhouse gas emissions.

CANDU Nuclear = Safe

CANDU nuclear is the most regulated industry in Canada for safety, health and environment.

CANDU Nuclear = Minimal Waste

CANDU nuclear accounts for all of its wastes – small volume in confined space.

CANDU Nuclear = Economic Benefits

The Canadian nuclear industry employs more than 30,000 workers and generates $6 billion per year.

CANDU Nuclear = Health

Canada supplies 2/3 of the world's reactor-produced radioisotopes used in over 12 million diagnostic tests each year.

AECL

ATOMIC ENERGY OF CANADA LIMITED
2251 SPEAKMAN DRIVE
MISSISSAUGA, ONTARIO
CANADA L5K 1B2
TEL: 905.823.9060
FAX: 905.823.7565

WWW.AECL.CA