71,000,000 Common Shares

Tractebel Energia

suez

Offer Price: R$13.00 per Common Share

Suez Energy South America Participações Ltda., the selling shareholder, and BNDES Participações S.A.—BNDESPAR, or BNDESPAR, are offering to the public in Brazil and, in the case of the selling shareholder, to institutional investors in the United States and to other investors elsewhere a total of 71,000,000 common shares of Tractebel Energia S.A., a *sociedade por ações* (stock corporation) organized under the laws of Brazil. The 16,000,000 shares being offered by BNDESPAR will be offered only in Brazil to Brazilian investors.

This offering was registered with the Comissão de Valores Mobiliários (the Brazilian Securities Commission, which we refer to as CVM). Our common shares are listed on the *Novo Mercado* of the Bolsa de Valores de São Paulo (the São Paulo Stock Exchange, which we refer to as BOVESPA), under the symbol "TBLE3." The ISIN number for our shares is BRTBLEACNOR2. The CVM has not approved or disapproved of these securities or determined if this offering memorandum (or the Portuguese language prospectus used in connection with the offering of our common shares in Brazil) is accurate or complete.

The selling shareholder and BNDESPAR (only in Brazil) have granted the underwriters an option, exercisable by Banco UBS S.A. as the global coordinator, for a period of 30 days following the date of this offering memorandum, to place up to an additional 9,900,000 common shares to cover over-allotments, if any.

	Initial offering price	Underwriting discount	Net proceeds to selling shareholder and BNDESPAR
Per common share	R$ 13.00	R$ 0.26	R$ 12.74
Total	R$923,000,000.00	R$18,460,000.00	R$904,540,000.00

The common shares have not been and will not be registered under the U.S. Securities Act of 1933, as amended, which we refer to as the "Securities Act," or under any U.S. state securities laws. Accordingly, our common shares are being offered only to qualified institutional buyers as defined under Rule 144A under the Securities Act, pursuant to exemptions from registration under the Securities Act and the rules thereunder and outside the United States in accordance with Regulation S under the Securities Act. By purchasing our common shares in the United States, you will be deemed to have represented to us that you are a qualified institutional buyer. For further details about the eligible offerees and a description of the restrictions on transfers of the common shares, see "Notice to investors" on page 139.

Investors residing outside Brazil may purchase the common shares if they comply with the registration requirements of CVM Instruction No. 325, dated January 27, 2000, and Resolution No. 2,689, dated January 26, 2000, of the Brazilian National Monetary Council.

Investing in the common shares involves a high degree of risk. See "Risk factors" beginning on page 12 for a discussion of the factors you should consider before investing in the common shares.

Payment for the common shares will be required to be made in reais to the selling shareholder through the facilities of Companhia Brasileira de Liquidação e Custódia (the Brazilian Settlement and Custodial Company, or CBLC), and the selling shareholder expects to deliver the common shares through the facilities of the CBLC on or about December 13, 2005, which is the fourth business day following the date of this offering memorandum. See "Trading, settlement and clearance."

Global Coordinator and Joint Bookrunner

UBS Investment Bank

Joint Bookrunner

Banco Itaú BBA

Joint Lead Manager

JPMorgan

Co-Managers

Santander Investment Limited

Unibanco Securities Inc.

The date of this offering memorandum is December 7, 2005.

You should rely only on the information contained in this offering memorandum. Neither we, the selling shareholder, the underwriters nor the agents appointed by the underwriters to facilitate the placement of the common shares outside Brazil (which we refer to as the agents) have authorized anyone to provide you with information different from that contained in this offering memorandum. The common shares are being offered, and the offers to buy are being sought, only in jurisdictions where such offers and sales are permitted. The information contained in this offering memorandum is accurate only as of the date of this offering memorandum, regardless of the time of delivery of this offering memorandum or of any sale of the common shares.

This offering memorandum is highly confidential, and we have prepared it for use solely in connection with the proposed offering of the common shares by the selling shareholder. This offering memorandum is personal to the offeree to whom it has been delivered by the agents and does not constitute an offer to any other person or to the public in general to subscribe for or otherwise acquire the common shares. Distribution of this offering memorandum to any person other than the offeree and those persons, if any, retained to advise that offeree with respect thereto is unauthorized, and any disclosure of any of its contents without our prior written consent is prohibited. Each offeree, by accepting delivery of this offering memorandum, agrees to the foregoing and agrees to not make copies of this offering memorandum.

Neither the U.S. Securities and Exchange Commission, which we refer to as the "SEC", any state securities commission nor any other regulatory authority has approved or disapproved these securities nor have any of the foregoing authorities passed upon or endorsed the merits of this offering or the accuracy or adequacy of this offering memorandum. Any representation to the contrary is a criminal offense.

The common shares offered through this offering memorandum are subject to restrictions on transferability and resale, and may not be transferred or resold in the United States except as permitted under the Securities Act and applicable U.S. state securities laws pursuant to registration or exemption from such laws. You should be aware that you may be required to bear the financial risks of this investment for an indefinite period of time. In making an investment decision, you must rely on your own examination of our business and the terms of this offering, including the merits and risks involved.

You must comply with all applicable laws and regulations in force in any jurisdiction in which you purchase, offer or sell the common shares or possess or distribute this offering memorandum and must obtain any consent, approval or permission required for your purchase, offer or sale of the common shares under the laws and regulations in force in any jurisdiction to which you are subject or in which you make such purchases, offers or sales, and neither we, the selling shareholder, the underwriters nor the agents will have any responsibility therefor.

We, the selling shareholder, and the underwriters reserve the right to reject any offer to purchase, in whole or in part, and for any reason, the common shares offered hereby. We, the selling shareholder, and the underwriters reserve the right to sell or place less than all of the common shares offered hereby.

Investors residing outside Brazil, including institutional investors, may purchase or sell the common shares if they comply with the registration requirements of CVM Instruction No. 325, dated January 27, 2000, and Resolution No. 2,689, dated January 26, 2000, of the Brazilian National Monetary Council. See "Trading, settlement and clearance—Investment in the common shares by non-residents of Brazil."

This communication is directed only at persons who: (i) are outside the United Kingdom or (ii) are investment professionals falling within Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2001 (the "Order") or (iii) are persons falling within Article 49(2)(a) to

(d) (“high net worth companies, incorporated associations etc.”) of the Order (all such persons together are being referred to as “relevant persons”). This communication must not be acted on or relied on by persons who are not relevant persons. Any investment or investment activity to which this communication relates is available only to relevant persons and will be engaged in only with relevant persons.

This offering is being made in Brazil by a prospectus in Portuguese with the same date as this offering memorandum. The Brazilian prospectus, which has been filed with the CVM, is in a format different from that of this offering memorandum and contains information not generally included in documents such as this one, including certain forward-looking information. This offering is made in the United States and elsewhere outside Brazil solely on the basis of the information contained in this offering memorandum. You should take this into account when making an investment decision.

Each person receiving this offering memorandum acknowledges that: (1) this offering memorandum does not contain all the information that would be included in a prospectus for this offering were this offering registered under the Securities Act; and (2) our consolidated balance sheets as of December 31, 2004 and December 31, 2003, and the consolidated statements of income, changes in shareholders' equity (company) and changes in financial position for the years ended December 31, 2004, December 31, 2003 and December 31, 2002 and our consolidated balance sheet as of September 30, 2005 and the consolidated statements of income for the nine months ended September 30, 2005 and September 30, 2004, (a) have been prepared for the specific purpose of inclusion in this offering memorandum under the responsibility of our management, (b) have been prepared in accordance with general accounting practices adopted in Brazil, which we refer to as “Brazilian GAAP”, prescribed by Brazilian corporation law No. 6,404 of December 15, 1976, as amended, the accounting regulations promulgated by the Brazilian National Electric Power Agency (*Agência Nacional de Energia Elétrica*), which we refer to as “ANEEL”, the rules and regulations issued periodically by the CVM and the technical releases issued by the Institute of Independent Auditors of Brazil (*Instituto de Auditores Independentes do Brasil*) and that Brazilian GAAP differs in certain significant respects from United States generally accepted accounting principles, which we refer to as “U.S. GAAP”; and (c) are subject to Brazilian auditing standards. See “Management's discussion and analysis of financial condition and results of operations—Discussion of certain principal differences between Brazilian GAAP and U.S. GAAP.”

In connection with this placement, (i) the underwriters may over-allot common shares to their customers including customers of the agents and (ii) Banco UBS S.A., through its affiliate UBS Corretora de Câmbio e Valores Mobiliários S.A. (the “stabilizing manager”) (or any person acting for the stabilizing manager), may effect transactions with a view to supporting the market price of our common shares at a level higher than that which might otherwise prevail for up to 30 days following the date of this offering memorandum. However, there is no obligation on the stabilizing manager (or any agent of the stabilizing manager) to take any action to stabilize such market price. Such stabilizing, if commenced, may be discontinued at any time and must be brought to an end after a limited period. Such stabilizing shall be in compliance with all applicable laws, regulations and rules. See “Plan of distribution.”

ALL DISCUSSIONS OF U.S. FEDERAL TAX CONSIDERATIONS IN THIS OFFERING MEMORANDUM HAVE BEEN WRITTEN TO SUPPORT THE MARKETING OF THE COMMON SHARES. SUCH DISCUSSIONS WERE NOT INTENDED OR WRITTEN TO BE USED, AND CANNOT BE USED BY ANY TAXPAYER, FOR THE PURPOSE OF AVOIDING U.S. FEDERAL TAX PENALTIES. INVESTORS SHOULD CONSULT THEIR OWN TAX ADVISERS IN DETERMINING THE TAX CONSEQUENCES TO THEM OF HOLDING THE COMMON SHARES, INCLUDING THE APPLICATION TO THEIR PARTICULAR SITUATION OF THE U.S. FEDERAL TAX CONSIDERATIONS DISCUSSED IN THIS OFFERING MEMORANDUM, AS WELL AS THE APPLICATION OF STATE, LOCAL, FOREIGN OR OTHER TAX LAWS.

Notice to New Hampshire residents only

Neither the fact that a registration statement or an application for a license has been filed under RSA 421-B with the State of New Hampshire nor the fact that a security is effectively registered or a person is licensed in the State of New Hampshire implies that any document filed under RSA 421-B is true, complete and not misleading. Neither any such fact nor the fact that an exemption or exception is available for a security or a transaction means that the Secretary of State of the State of New Hampshire has passed in any way upon the merits or qualifications of, or recommended or given approval to, any person, security or transaction. It is unlawful to make, or cause to be made, to any prospective purchaser, customer or client any representation inconsistent with the provisions of this paragraph.

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Forward-looking information and statements

This offering memorandum includes forward-looking statements subject to risks and uncertainties, in particular in the sections titled "Summary," "Risk factors," "Management's discussion and analysis of financial condition and results of operations," "The Brazilian power industry" and "Business." These statements are based on current expectations and projections about future events and financial trends that affect or may affect our business. Several factors may adversely affect our estimates and assumptions, including, but not limited to:

- general economic, political, demographic and business conditions in Brazil;
- shortage in hydroelectric resources, operational and technical problems, interruptions in the electrical transmission system or damages to our facilities;
- changes in electricity tariffs;
- changes in governmental regulations in relation to the power industry;
- changes in regulation or implementation of environmental rules;
- interruptions in the services we provide;
- inflation or the appreciation or depreciation of the real;
- early termination or interruption of our concessions by the concession authority;
- our ability to execute our business strategy, including our ability to obtain financing on favorable terms and conditions if and when necessary;
- changes in consumer demand for electricity;
- our ability to obtain new generation projects from our controlling shareholder or from third parties (including the concession authority), in favorable or market conditions;
- changes in tax laws and regulation;
- changes in tariffs and other charges imposed on the energy sector;
- early termination of regulatory subsidies;
- changes in the strategies and plans of our controlling shareholder; and
- other risk factors discussed under "Risk factors."

Words such as "believe," "may," "can," "seek," "estimate," "continue," "anticipate," "intend," "expect" and other similar words are used in this offering memorandum to identify forward-looking statements. These forward-looking statements include information concerning results and projections, strategy, funding plans, competitive position, the electricity sector environment, potential opportunities for growth, the effects of future regulations and the effects of competition. In light of the risks and uncertainties described herein, the forward-looking statements included in this offering memorandum may not prove accurate. Given such limitations, investors should not make any decision to invest in the common shares on the basis of the forward-looking statements contained herein. The forward-looking statements included herein are made only as of the date of this offering memorandum, and we do not undertake any obligation to release publicly any revisions to those forward-looking statements to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events.

Presentation of financial and operating information

We prepare our financial statements based on Brazilian GAAP and the accounting methodologies established by ANEEL. Brazilian GAAP differs in significant respects from generally accepted accounting principles in the United States, or U.S. GAAP. See ''Management's discussion of financial condition and results of operations—Discussion of certain differences between Brazilian GAAP and U.S. GAAP'' for a brief overview of the key differences between Brazilian GAAP and U.S. GAAP as they relate to our company.

The following financial statements are included in this offering memorandum:

- Our consolidated balance sheets as of December 31, 2004 and December 31, 2003, and the consolidated statements of income, changes in shareholders' equity (company) and changes in financial position for the years ended December 31, 2004, December 31, 2003 and December 31, 2002, prepared under the responsibility of our management, which have been audited by Deloitte Touche Tohmatsu Auditores Independentes; and
- Our consolidated balance sheet as of September 30, 2005 and the consolidated statements of income for the nine months ended September 30, 2005 and September 30, 2004, prepared for the specific purpose of inclusion in this offering memorandum, under the responsibility of our management, which have been the subject of a limited review by Deloitte Touche Tohmatsu Auditores Independentes.

Pursuant to applicable rules and regulation, we apply depreciation and amortization rates determined by ANEEL. In this regard, we understand that ANEEL is analyzing possible modifications to such rates, for the purpose of assuring that assets relating to original concessions be totally depreciated within the term of the relevant concession. If these modifications are approved they will significantly increase the depreciation rates of our assets.

The opinion of our auditors on our financial statements included in the offering memorandum includes a disclosure stating that we, based on our internal future cash flow projections, discounted to present value, estimated that certain thermoelectric assets would not be recovered with our future operations. Our management understands that these assets together with the rest of our operational assets will produce positive future cash flows. The potential non-recoverability of these assets relates to reduced usage as compared to our hydroelectric plants as our thermoelectric plants are used primarily to supplement our hydroelectric generation.

COMPANIES WE FULLY CONTROL OR WITH RESPECT TO WHICH WE SHARE CONTROL

We proportionally consolidate our interests in a company that we control together with third parties, namely our 48.75% interest in Itá Energética S.A., or ''Itasa'', for all periods presented, in each case in accordance with Brazilian GAAP. We fully consolidate all companies we control, namely Companhia Energética Meridional—CEM, Lages Bioenergética Ltda. and Tractebel Energia Comercializadora Ltda., for all periods presented.

MARKET INFORMATION

The information contained in this offering memorandum in relation to Brazil and the Brazilian economy are based on data published by the Central Bank, by other public agencies and independent sources of information. The information contained in this offering memorandum concerning the electricity sector and our participation in it has been obtained from established public sources, such as trade associations and government agencies, including the Ministry of Mines and Energy (*Ministério de Minas e Energia*), ANEEL, the Electricity Trading Board (*Câmara de Comercialização de Energia*

Elétrica), and the National System Operator (*Operador Nacional do Sistema Elétrico*), or ONS, among others. We, the selling shareholder and the coordinators disclaim any responsibility for the accuracy or completeness of such information.

GENERAL

In this offering memorandum, references to "we," "us," "our," "the company," or "Tractebel" are to Tractebel Energia S.A. and its consolidated subsidiaries, unless the context otherwise requires. In addition, the term "Brazil" refers to the Federative Republic of Brazil, and the phrase "Brazilian government" refers to the federal government of Brazil. The term "Central Bank" refers to the Central Bank of Brazil. The term "U.S. dollar" and "U.S. dollars" or dollar and dollars and the symbol "US$" refer to the legal currency of the United States. The term *"real"* and *"reais"* and the symbol "R$" refer to the legal currency of Brazil.

This offering memorandum contains translations of various *real* amounts into U.S. dollars at specified rates solely for your convenience. You should not construe these translations as representations by us that the *real* amount actually represents these U.S. dollar amounts or could be converted into U.S. dollars at the rates indicated. Unless otherwise indicated, we have translated the *real* amounts for the year ended December 31, 2004 and for the nine-month periods ended September 30, 2004 and 2005 using a rate of R$2.2222 to US$1.00, the selling rate as of September 30, 2005, as published by the Central Bank. See "Exchange rates."

Certain amounts and percentages included in this offering memorandum have been rounded, and the totals presented in certain tables therefore may not be an arithmetic aggregation of the figures that precede them.

Summary

Set forth below is a summary overview of our business and our financial and operating information as well as of the common shares being offered by the selling shareholder in this offering. This summary does not include all of the information an investor should consider before investing in the common shares. Before investing in the common shares, you should read this offering memorandum in its entirety, including the information contained in the "Risk factors" and "Management's discussion and analysis of financial condition and results of operations" and our consolidated financial statements and related notes. The financial information provided in this offering memorandum includes the consolidated financial information of our company and of our consolidated subsidiaries.

OUR COMPANY

Introduction

As of September 30, 2005, we were Brazil's largest private-sector electricity generation company in terms of both installed capacity and assured energy, based on information provided by ANEEL. As of that date, according to the information provided by ANEEL for 2004, our installed capacity was 5,860 MW, representing 7.5% of the total electricity generating capacity in Brazil, and our assured energy was 3,172 MW. Assured energy is the maximum amount of energy (determined per hydroelectric or thermoelectric power generation facility) that generators are allowed to sell. Our electricity supply capacity, including electricity purchased from third parties under contracts, was 5,968 MW at September 30, 2005.

The table below sets forth certain consolidated financial and operating information for the periods indicated.

	Nine months ended September 30,			Year ended December 31,			
	2005[1][2]	2005[2]	2004[2]	2004[1][2]	2004	2003	2002
	(US$ millions)	(R$ millions)		(US$ millions)	(R$ millions)		
Net sales and services	882.1	1,960.1	1,853.0	1,111.5	2,469.9	1,830.9	1,375.2
EBITDA[3]	487.0	1,082.3	949.8	571.9	1,270.9	928.2	572.3
EBITDA margin[4]		55.2%	51.3%		51.5%	50.7%	41.6%
Net income	315.0	700.0	533.9	348.8	775.2	517.1	(183.5)
Volume of electricity sold (GWh)		22,354.3	22,072.5		29,440.2	24,327.0	25,417.1

(1) Amounts translated into U.S. dollars based on a rate of exchange of R$2.2222 to U.S.$1.00, the selling rate of exchange as of September 30, 2005 reported by the Central Bank.

(2) Unaudited.

(3) We calculate EBITDA by adding back net financial expenses, depreciation and amortization, non-operating results, amortization of goodwill, and income and social contribution taxes to our net income (loss). EBITDA is not a measure recognized under Brazilian GAAP, and it does not represent cash flow for the periods indicated. EBITDA should not be deemed as a substitute for net income or as an indicator of operating performance, cash flow or liquidity. EBITDA does not have a standardized meaning and our definition of EBITDA may not be comparable to the EBITDA utilized by other companies. See "Summary financial and operating information" for a reconciliation of EBITDA and net income (loss).

(4) EBITDA divided by net sales and services.

The Suez Group acquired ownership control of our company through Suez Energy South America Participações Ltda., or SESA, in a privatization auction of the Brazilian electricity industry held on September 15, 1998. In the seven years ended September 30, 2005, we made investments of

approximately R$2.5 billion (not including the price paid in the privatization) to expand and improve our power plants, consolidating our operations in the Brazilian electricity sector and complying with all our investment obligations under our concession contracts. During that same period, our installed capacity increased by 57.6%, from 3,719 MW to 5,860 MW, and our assured energy increased by 48.0%, from 2,143 MW in 1998 to 3,172 MW at September 30, 2005.

Our largest customers are energy distribution companies, that is, companies that deliver electricity to final consumers. Nevertheless, customer portfolio maximization is an important feature of our business strategy, and we are particularly focused on expanding our base of independent consumers, which are companies that qualify to purchase their electricity directly from any suppliers of energy, including generation companies. As of September 30, 2005, we had supply contracts with more than 100 independent consumers located in 12 different Brazilian states. We believe we have one of the highest levels of contracted energy sales with independent consumers, with aggregate sales to independent consumers of approximately 745 MW. At September 30, 2005, our energy was sold to distribution companies under long-term initial contracts (21%), to distribution companies under bilateral contracts (32%), to electricity traders (23%), to independent consumers (21%) and through exports (3%).

Our electricity generation facilities are composed of six hydroelectric plants and seven thermoelectric plants, of which two hydroelectric plants (Itá and Machadinho) are owned by consortia that include other companies and operated by our company. The power plants, their locations and other information concerning their installed capacity, assured energy, and supply capacity are described in the table below:

			Installed capacity		Our	Assured energy	
Facility	Location	Power Generation Units	Total (MW)	Owned by Us (MW)[1]	Supply Capacity (MW)	Total (MW)	Owned by Us (MW)[1]
Hydroelectric plants:							
Salto Santiago	Iguaçu River(PR)	4	1,420	1,420	1,420	723	723
Salto Osório	Iguaçu River(PR)	6	1,078	1,078	1,078	522	522
Passo Fundo	Passo Fundo River(RS)	2	226	226	226	119	119
Itá[2]	Uruguay River(SC/RS)	5	1,450	1,090	1,090	720	513
Machadinho[2]	Uruguay River(SC/RS)	3	1,140	383	383	529	136
Cana Brava	Tocantins River(GO)	3	450	450	450	273	273
Total hydroelectric plants			**5,764**	**4,647**	**4,647**	**2,886**	**2,286**
Thermoelectric plants:							
Jorge Lacerda Complex[3]	Capivari de Baixo(SC)	7	857	857	857	598	598
Charqueadas	Charqueadas(RS)	4	72	72	72	45	45
Alegrete	Alegrete(RS)	2	66	66	66	41	41
William Arjona	Campo Grande(MS)	5	190	190	190	177	177
Lages	Lages(SC)	1	28	28	28	25	25
Purchase of electricity			—	—	108	—	—
Total thermoelectric plants			**1,213**	**1,213**	**1,321**	**886**	**886**
Total			**6,977**	**5,860**	**5,968**	**3,772**	**3,172**

(1) For thermoelectric plants, "available energy" is applied in lieu of assured energy. The term assured energy when used in this offering memorandum includes the available energy of the thermoelectric plants.

(2) For further information on the installed capacity and assured energy of the Itá and Machadinho power plants, see "Business—Power generating facilities."

(3) Jorge Lacerda includes three generation facilities.

New projects

We periodically evaluate opportunities to develop hydroelectric and thermoelectric plants and cogeneration units, such as UHEs Itá and Machadinho, the thermoelectric plant William Arjona and the Lages cogeneration facility. However, larger hydroelectric facilities, such as the UHE Cana Brava plant, are developed by the Suez Group through a separate entity, such as Companhia Energética Meridional—CEM, or CEM, a wholly owned subsidiary, before it is transferred to our company. After initial phase of contracting and financing had been agreed and certain goals achieved in relation to this project, all of the share capital of CEM was transferred to us at a price and valuation determined by an independent financial institution, and we became the owner of CEM and its power plant.

Starting with the UHE Cana Brava project, in conjunction with SESA we adopted a strategy for developing large hydroelectric projects that involve initial project development by SESA or by a separate Brazilian subsidiary of SESA and the subsequent transfer to us, after the project has evolved past the initial stages and is ready to commence construction. Generally, the initial stage consists of bidding for the concession, obtaining regulatory authorizations and negotiating contracts (including power purchase agreements and related financing arrangements), to the beginning of project construction, all of which SESA manages independently of us. After this initial stage, the project is transferred to us, and we become the owner and manager of the project, assuming related liabilities.

As the project is not initially developed by us, we do not incur the risks involved in the development phase of a project. In addition, this project development strategy allows us to capitalize on the know-how and expertise the Suez Group brings to the development of projects of this type and size. The sale and transfer of projects under development is made on an arm's-length basis, and based on an appraisal prepared by an independent financial institution.

Accordingly, as of September 30, 2005, SESA had two projects under development, the Estreito and São Salvador power plants, with construction scheduled to begin in 2006, depending on the results of the new energy auction to be held by MME and ANEEL and scheduled for December 16, 2005.

The São Salvador power plant will be located on the Tocantins river and is expected to have 241 MW of installed capacity. At September 30, 2005, this project had already obtained from IBAMA, the Brazilian Environmental Protection Agency, the necessary preliminary and installation licenses both for the power plant and the transmission line. The Estreito power plant is expected to have 1,087 MW of installed capacity and will also be located on the Tocantins river. The concession rights of the Estreito power plant are owned by a consortium of companies, where SESA currently owns a 30% interest. We expect that these projects will be transferred to us before the construction phase has been initiated.

Strengths

We believe that our competitive strengths include the following:

- ***Strong growth potential.*** We have a record of investment and growth in the Brazilian electricity generation sector, having increased our installed capacity by 57.6% since our privatization in 1998. Additionally, we believe we will be able to leverage our financial resources and management with the know-how of our controlling shareholders in the acquisition and implementation of new projects, to continue expanding existing power generation facilities both by developing new projects and acquiring new facilities without adversely impacting our rate of return.
- ***Solid portfolio of contracted energy.*** A substantial amount of our assured energy is contracted through 2008 at competitive prices and adjusted by the IGP-M, except for contracts executed in the regulated environment, which are adjusted by the IPCA. The high level of contracted energy through 2008 should provide us with a sustained source of cash generation in a period during which there will be a high supply of energy. In later years, when we expect to have substantial volume of energy available for sale, energy demand is expected to increase at a rate that based on projections by the Energy Research Company (*Empresa de Pesquisa Energética—EPE*) will be faster

than the rate of growth in installed capacity. Therefore, we expect to capitalize on potentially higher energy prices expected to exist at that time although the market may evolve differently from our expectations. Additionally, we have 744 MW of assured energy from our operational power plants (Cana Brava, Itá, Machadinho and William Arjona) and expect to have 324 MW of assured energy from the new projects under development by SESA that we anticipate will be transferred to us prior to the beginning of their construction. The assured energy from these projects will be for sale in any of the next three new energy auctions, which are expected to occur until the end of 2007.

- ***First company to supply high volume of electricity to independent consumers.*** We were the first generation company in Brazil to focus on contracting with independent consumers to sell electricity and to develop the loyalty of these consumers. Sales to independent consumers give us more flexibility to negotiate sales terms, including pricing. The expertise we have developed in supplying those consumers has allowed us to maximize the efficiencies of our client portfolio. At September 30, 2005, our customers included over 100 independent consumers, which accounted for aggregate sales of approximately 745 MW, representing 21% of the electricity we sold during the nine months ended September 30, 2005, compared to 15.1% in 2004 and 9.5% in 2003.
- ***Consistent cash generation and sound financial position.*** We have historically achieved strong revenue growth and consistent cash flows, with average annual growth in net revenue for the period from 2002 through 2004 of 34% and of 5.8% for the nine months ended September 30, 2005, compared to the corresponding period in 2004. Our EBITDA margin has improved steadily over the last several years to 55.2% for the nine months ended September 30, 2005, compared to 51.5% for 2004, 50.7% for 2003 and 41.6% for 2002. Investment and capital expenditure requirements remain low, representing 3% of EBITDA in 2004. Those factors combined led us to a strong financial condition and low leverage (ratio of total debt to EBITDA was 1.1 as of September 30, 2005) which is reflected in one of the best ratings in the Brazilian energy sector of "brA +" from Standard & Poor's, and "AA-(bra)" from Fitch Ratings. We believe that our sound financial position gives us the ability to explore new investment opportunities.
- ***Dedicated and experienced management committed to high standards of corporate governance.*** We are disciplined in our investment decisions and consistent in implementing our business plan. Our management team has an average of 20 years of experience in the energy sector having served our company since our privatization in 1998. This management experience and cohesion has enabled us to adapt to changing market and regulatory conditions and to implement innovative solutions which have allowed us to create value for our shareholders since our privatization in 1998. In addition, we are committed to high standards of corporate governance practice, having our common shares listed on the *Novo Mercado* of BOVESPA.
- ***High dividend pay-out.*** Our strong cash flow generation historically has allowed us to make high dividend payments. We distributed 95% of our net income as interest on shareholders' equity and dividends in 2003 and 2004. In addition, we had one of the highest dividend yields among Brazilian generating companies in 2004 (13.0%).
- ***Controlling shareholder with significant experience doing business in Brazil and in the energy sector.*** The Suez group has a long-term commitment to Brazil and has been doing business in the country for the past 50 years, the last eight years of which also were dedicated to the energy sector. Our installed capacity represents approximately 10% of the global installed capacity of the Suez group.

Strategy

Our objective is to continue to be a leading power generation company in Brazil. In this context, we seek to implement the following strategy:

- ***Growth with investment discipline.*** We seek revenue growth by taking advantage of improved prices for our electricity and expanding our generation facilities. We expect that beginning in 2009,

when according to projections by the Energy Research Company (*Empresa de Pesquisa Energética—EPE*) the rate of energy demand increases more rapidly than the growth rate of Brazil's installed capacity, we will be well-positioned to take advantage of potentially increased energy prices as a substantial portion of our assured energy beginning in 2009 will be available to sale. With respect to the growth of our power generation facilities, taking advantage of our sound financial condition and strong revenue generation, we expect to grow by developing new projects and evaluating possible acquisitions. Our controlling shareholder is currently developing two large projects (*i.e.*, Estreito and São Salvador hydroelectric plants) which will, when transferred to us, increase our installed capacity by 567 MW.

- ***Maximization of portfolio efficiency.*** Our trading strategy and focus on expanding our base of independent consumers has allowed us to take advantage of consistently higher average sales prices with prices increasing from R$47.39 per MWh in 2002, compared to R$83.88 per MWh in the nine months ended September 30, 2005. We intend to continue investing in the provision of services to, and in relationships with, these customers by means of targeted initiatives, and by developing a marketing strategy and consumer loyalty program, since contracts with these customers result in multiple benefits to us, particularly flexibility in the terms of the energy contracts and unregulated pricing.
- ***Operating efficiency.*** Operating efficiency is the basis for our strategy to become more competitive and efficient and to continue to create and maximize value for our shareholders. We have historically presented solid operating performance and consistent productivity growth, which we believe allowed us to continue to improve our operating margins over the last years.

Our principal executive offices are located at Rua Antônio Dib Mussi, 366, Florianópolis, Santa Catarina, CEP 88015-110, Brazil, and our telephone number is +55 48 211-7060. Our website is www.tractebelenergia.com.br. Information contained on, or accessible through, our website is not incorporated by reference in, and shall not be considered part of, this offering memorandum.

The offering

Issuer	Tractebel Energia S.A.
Securities offered	The selling shareholder is offering a total of 55,000,000 common shares: ➢ to the public and institutional investors in Brazil in reliance on Regulation S; ➢ to institutions and investors outside the United States and Brazil in reliance on Regulation S; and ➢ to qualified institutional investors in the United States, as defined in Rule 144A, in reliance on Rule 144A. BNDESPAR is offering 16,000,000 common shares only in Brazil to Brazilian investors pursuant to a separate offering document in Portuguese distributed exclusively in Brazil.
Selling shareholder	Suez Energy South America Participações Ltda.
Price	R$13.00 per common share.
Over-allotment option	The selling shareholder and BNDESPAR (only in Brazil) have granted the underwriters an option, exercisable by the global coordinator on behalf of the joint bookrunners for a period of 30 days after the date of this offering memorandum to place up to an additional 9,900,000 common shares to cover over-allotments, if any.
Our capital stock and shares outstanding after the offering	Our capital stock consists of 652,742,192 common shares. Our outstanding capital stock will not change after this offering. See "Description of capital stock."
Tag-along rights	Following the listing of our common shares on the *Novo Mercado* segment of BOVESPA, in the event of the sale of our control, the acquirer must, within 90 days from the purchase of the controlling shares, make a public offer to purchase the common shares held by all our other shareholders, at no less than 100% of the price per share paid for the controlling shares. See "Description of capital stock—Change of control."
Voting rights	Each common share grants the right to one vote at all shareholders' meetings. For further information regarding voting rights, see "Description of capital stock."
Lock-up agreements	We, the selling shareholder, BNDESPAR and Banco Clássico have agreed with the underwriters and their agents, in certain circumstances, not to negotiate any shares issued by us. See "Plan of distribution". These transfer restrictions do not apply to any transfers by the selling shareholder to any of its affiliated companies and to the loan of shares to be made by the selling shareholders to the underwriters and their agents for purposes of stabilization. In addition, under *Novo Mercado* regulations, our controlling shareholder and its directors and executive officers may not sell or offer to sell our common shares or derivatives during the six-month period following the date the common shares begin trading on the *Novo Mercado*. Upon termination of the

	initial six-month period, our controlling shareholder and its directors and executive officers may sell, offer or dispose of up to 40% of their respective holdings during the following six-month period.
Dividends	Brazilian corporation law and our by-laws dated November 9, 2005 require us to pay to our shareholders a minimum mandatory dividend of 30% of our adjusted net income, in the form of dividends and/or interest on shareholders' equity, calculated in accordance with Brazilian corporation law, unless our board of directors determines that such a dividend is incompatible with our financial condition and announces the suspension of the dividend at our shareholders' meeting.
Use of proceeds	We will not receive any of the proceeds from the offering. Since the offering is a secondary offering by the selling shareholder and BNDESPAR (in Brazil), the proceeds from the offering will be received by the selling shareholder or BNDESPAR.
Agents	Placement of our common shares outside Brazil will be made by U.S. broker-dealer affiliates of the underwriters of the Brazilian offering. See "Plan of distribution."
Transfer restrictions	Our common shares have not been registered under the Securities Act and are subject to U.S. restrictions on transfer and resale, as described in "Notice to investors." Delivery of common shares, including by or between residents of jurisdictions outside Brazil, may occur only in Brazil. Please see "Trading, settlement and clearance—Investment in our common shares by non-residents of Brazil."
Trading, settlement and clearance	The underwriters have informed us that payment for the common shares must be made in *reais,* and that they expect the common shares to be delivered via book entry about four business days after the date of this offering memorandum. Trades of the common shares on BOVESPA will be settled through the facilities of the CBLC.
Listing	On November 16, 2005, we executed a listing agreement with BOVESPA in order to list our shares on the *Novo Mercado,* which will be effective on November 16, 2005. At that time, our common shares will be listed on the *Novo Mercado* segment of BOVESPA under the symbol "TBLE3."
Risk factors	An investment in our common shares involves risks. See "Risk factors" for a discussion of some of the factors you should consider before deciding to invest in our common shares.

Summary financial and operating information

The following table presents summary financial information as of and for the years ended December 31, 2004, 2003 and 2002 and as of and for the nine-month periods ended September 30, 2005 and 2004. You should read this information in conjunction with our combined consolidated financial statements and related notes included elsewhere in this offering memorandum, and the information under "Presentation of financial information" and "Management's discussion and analysis of financial condition and results of operations." Our financial statements and the information set forth below were prepared in accordance with Brazilian GAAP, which differs in significant respects from U.S. GAAP.

Although BDO Trevison Auditores Independentes have been our auditors since 2004, the summary consolidated financial information as of and for the years ended December 31, 2004, 2003 and 2002 was derived from our audited consolidated financial statements included elsewhere in this offering memorandum and which were audited by Deloitte Touche Tohmatsu Auditores Independentes specifically for the purpose of inclusion in this offering memorandum. In addition, the summary consolidated financial information as of and for the nine months ended September 30, 2005 and 2004 included in this offering memorandum was derived from our unaudited consolidated financial statements also included elsewhere in this offering memorandum which were prepared specifically for the purpose of inclusion in this offering memorandum and were subject to a limited review by Deloitte Touche Tohmatsu Auditores Independentes. In the opinion of our management, our unaudited consolidated financial statements include all adjustments necessary to reflect a fair presentation of our results and financial condition for such periods. Our results of operations for the nine months ended September 30, 2005 are not necessarily indicative of the results that you should expect for the entire fiscal year ending December 31, 2005 or for any other period. Our consolidated financial statements include the proportional consolidation of our participation in Itá Energética S.A., or Itasa.

The opinion of our auditors on our financial statements included in the offering memorandum includes a disclosure stating that we, based on our internal future cash flow projections, discounted to present value, estimated that certain thermoelectric assets would not be recovered with our future operations. Our management understands that these assets together with the rest of our operational assets will produce positive future cash flows. The potential unrecoverability of these assets relates to reduced usage as compared to our hydroelectric plants as our thermoelectric plants are used primarily to supplement our hydroelectric generation.

This offering memorandum contains translations of various *real* amounts into U.S. dollars at specified rates solely for your convenience. You should not construe these translations as representations by us that the *real* amounts actually represent these U.S. dollar amounts or could be converted into U.S. dollars at the rates indicated. Unless otherwise indicated, we have translated the *real* amounts for the year ended December 31, 2004 and for the nine months ended September 30, 2005 using a rate of R$2.2222 to US$1.00, the selling rate as of September 30, 2005, as published by the Central Bank. See "Exchange rates."

Income Statement Data	Nine months ended September 30,			Year ended December 31,			
	2005[1]	2005[1]	2004[1]	2004[1]	2004	2003	2003
	(US$ millions)	(R$ millions, except per share data)		(US$ millions)	(R$ millions, except per share data)		
Gross operating revenues	986.4	2,192.0	1,985.6	1,197.8	2,661.8	1,952.8	1,437.1
Deductions from operating revenues	(104.4)	(231.9)	(132.6)	(86.4)	(191.9)	(121.9)	(61.9)
Net sales and services	882.1	1,960.1	1,853.0	1,111.5	2,469.9	1,830.9	1,375.2
Costs of electricity and services	(357.1)	(793.6)	(820.0)	(495.9)	(1,101.9)	(879.6)	(866.2)
Gross profit	524.9	1,166.5	1,033.0	615.6	1,368.0	951.3	509.0
Operating expenses	(108.0)	(240.1)	(239.9)	(144.3)	(320.7)	(250.8)	(126.7)
Service income	416.9	926.4	793.1	471.3	1,047.3	700.5	382.3
Income from interests held in other companies	(2.3)	(5.1)	(5.1)	(3.0)	(6.7)	(7.0)	(2.2)
Net expenses	(30.8)	(68.4)	(148.7)	(79.5)	(176.6)	(35.7)	(723.1)
Operating income (loss)	383.8	852.9	639.3	388.8	864.0	657.8	(343.0)
Non-operating income	1.6	3.5	(2.6)	(1.4)	(3.0)	2.7	(2.7)
Income (loss) before taxes	385.4	856.4	636.7	387.5	861.0	660.5	(345.7)
Income and social contribution taxes	(70.4)	(156.4)	(102.8)	(38.6)	(85.8)	(143.4)	162.2
Net income (loss)	315.0	700.0	533.9	348.8	775.2	517.1	(183.5)
Net income (loss) per share (R$)[2]	0.4826	1.0725	0.8179	0.5344	1.1876	0.7923	(0.2812)

(1) Unaudited.

(2) For 2005, presents net income per share while for all other periods presents net income per 1,000 shares. On May 23, 2005, we consummated a reverse stock split whereby our shareholders received one common share for each 1,000 shares previously outstanding.

Balance Sheet Data	Nine months ended September 30, 2005[1]	2005[1]	2004[1]	Year ended December 31, 2004[1]	2004	2003	2002
	(US$ millions)	(R$ millions)		(US$ millions)		(R$ millions)	
Total current assets	462.7	1,028.2	1,119.0	537.0	1,193.4	925.0	1,456.2
Cash and cash equivalents	239.0	531.0	574.2	288.9	642.0	347.0	361.1
Total long-term assets	182.1	404.6	340.1	167.3	371.7	338.5	313.7
Total permanent assets	2,016.5	4,481.1	4,690.2	2,088.0	4,640.0	4,868.8	5,008.5
Total assets	2,661.3	5,913.9	6,149.3	2,792.3	6,205.1	6,132.3	6,778.4
Total current liabilities	289.6	643.5	669.7	555.0	1,233.3	1,054.4	1,122.6
Short-term debt	124.2	275.9	323.8	135.5	301.0	279.7	524.0
Total long-term liabilities	852.0	1,893.4	2,343.9	983.2	2,184.9	2,476.1	2,895.5
Long-term debt	588.7	1,308.2	1,852.8	761.9	1,693.0	2,025.5	2,430.7
Shareholders' equity	1,519.7	3,377.0	3,135.7	1,254.1	2,786.9	2,601.8	2,760.3
Total liabilities and shareholders' equity	2,661.3	5,913.9	6,149.3	2,792.3	6,205.1	6,132.3	6,778.4

(1) Unaudited.

EBITDA[1]	Nine months ended September 30, 2005[2]	2005[2]	2004[2]	Year ended December 31, 2004[2]	2004	2003	2002
	(US$ millions)	(R$ millions)		(US$ millions)		(R$ millions)	
Net income (loss)	315.0	700.0	533.9	348.8	775.2	517.1	(183.5)
Social contribution and income tax	70.4	156.4	102.8	38.6	85.8	143.4	(162.2)
Non-operating income	(1.6)	(3.5)	2.6	1.4	3.0	(2.7)	2.7
Financial income	30.8	68.4	148.7	79.5	176.6	35.7	723.1
Depreciation/amortization	72.5	161.0	161.8	103.6	230.3	234.7	192.2
EBITDA[1]	487.0	1,082.3	949.8	571.9	1,270.9	928.2	572.3

(1) We calculate EBITDA by adding back net financial expenses, depreciation and amortization, non-operating results, amortization of goodwill, and income and social contribution taxes to our net income (loss). EBITDA is not measured recognized under Brazilian GAAP, and it does not represent cash flow for the periods indicated. EBITDA should not be deemed as a substitute for net income or as an indicator of operating performance, cash flow or liquidity. EBITDA does not have standardized meanings and our definition of EBITDA may not be comparable to the EBITDA utilized by other companies.

(2) Unaudited.

Operating Data	Nine months ended September 30,		Year ended December 31,		
	2005	2004	2004	2003	2002
Installed capacity (GW)	5.8	5.8	5.8	5.8	5.8
Assured energy (GW)	3.2	3.2	3.2	3.2	3.1
Energy sold (GWh)	22,354.3	22,072.5	29,440.2	24,327.0	25,417.1
Initial contracts	4,633.1	9,291.7	12,432.8	18,561.0	24,771.9
Bilateral contracts	17,721.2	12,780.8	17,007.4	5,766.0	645.2
Purchased energy (GWh)[(1)]	1,882.3	341.1	359.7	—	193.3

(1) Operating data presented on a consolidated basis, and therefore, amounts of purchased energy between us and our consolidated subsidiaries are not considered.

Risk factors

An investment in our common shares involves a high degree of risk. Potential investors should carefully consider the risks and uncertainties described below and the other information contained in this offering memorandum. The risks described below are not the only ones we face or to which investments in Brazil are subject. Our business, financial position or results of operations may be adverse and materially affected by any of these risks. Additional risks that are not currently known to us, to the selling shareholder or to the underwriters, or which we, the selling shareholder and the underwriters currently consider to be irrelevant, may also affect our business. This offering memorandum also contains estimates and projections that involve risks and uncertainties. Our results may significantly differ from those previously projected as a result of certain factors, including the risks faced by us, as described below and in other sections of this offering memorandum.

RISKS RELATING TO BRAZIL

The Brazilian government and other governmental agencies exercise significant influence over the Brazilian economy. The Brazilian political and economic conditions could adversely affect our business and the price of our common shares.

The Brazilian government frequently intervenes in the Brazilian economy and occasionally makes significant changes in the monetary and credit policy and economic regulation, as well as in other governmental policies. The Brazilian government's actions to influence the economy, control inflation and other policies and regulations have often involved, among other measures, price and salary controls, currency devaluations, exchange controls and limits on imports and the freezing of bank accounts. Our business, financial condition and results of operations, as well as the price of our common shares may be adversely affected by changes in government policies or regulations, whether they are implemented at the federal, state or municipal level, related to public charges and control over the foreign exchange rate, as well as by other factors, such as:

- exchange rates and exchange control policies;
- inflation rates;
- interest rates;
- liquidity of domestic capital and credit markets;
- tax policies;
- price, social and political instability;
- electricity rationing;
- domestic economic growth;
- changes in the tax regime, including charges applicable to specific industry sectors; and
- other political, diplomatic, social and economic developments in or affecting Brazil.

Uncertainty regarding future government policies may contribute to an increase in the volatility of the Brazilian securities markets and securities issued abroad by Brazilian companies. The Brazilian economy grew 4.9% in 2004 and 0.5% and 1.9% in 2003 and 2002, respectively. Due to limited economic growth in recent years, it is uncertain if current economic policies will prevail. We can not predict Brazil's monetary, tax, social security and other policies, nor if such policies will have an adverse impact on the economy and, consequently, on our business and results of operations or the market price of our common shares.

The future development of the Brazilian economy, as well as government policies may adversely affect our business and our results, as well as the market value of our common shares.

Recent allegations of corruption of politicians may generate political and economic instability.

In the past, the performance of the Brazilian economy was impacted by Brazil's political situation. Historically, political crises have affected investor confidence and the public in general and adversely affected the development of the economy. Recently, certain politicians have been accused of allegedly making payment to legislative officers in exchange for political support. As a result, certain legislative officers and ministers resigned their posts or face administrative inquiries. The accusations may weaken the current administration and make difficult Brazil's governability, the economic, social and political reforms scheduled to be implemented and/or generate political and economic instability. We and the selling shareholder cannot predict the consequences of such accusations nor their effects on the economy and our results of operations. This and other political crises may have an adverse impact on the Brazilian economy, our results of operations and the market price of our common shares.

Inflation and efforts by the Brazilian government to curb inflation may contribute significantly to economic uncertainty in Brazil and could harm our business and the market price of our common shares.

Brazil has historically experienced extremely high rates of inflation. In recent years, Brazil's annual rate of inflation was 10.0% in 2000, 10.4% in 2001, 25.3% in 2002, 8.7% in 2003 and 12.4% in 2004, as measured by the General Market Price Index (*Índice Geral de Preços do Mercado*), or IGP-M. Government measures to curb inflation, together with speculation on possible future government measures, have contributed to economic uncertainty in Brazil and heightened the volatility of the Brazilian securities markets. Future measures by the Brazilian government, including increases on interest rates or exchange controls, may adversely impact the Brazilian economy and our business and results of operations or the market price of our common shares. Inflationary pressures may also affect our ability to access the international markets and to anticipate government policies to fight inflation that may damage our business or adversely affect the market price of our common shares.

Volatility in the value of the Brazilian *real* in relation to the U.S. dollar and other currencies may negatively affect our business.

Historically, the Brazilian currency has suffered frequent devaluations. The *real* depreciated by 15.7% and 34.3% against the U.S. dollar in 2001 and 2002, respectively. In 2003 and 2004, the *real* appreciated against the U.S. dollar by 22.3% and 8.8%, respectively. Throughout the periods of currency depreciation, the Brazilian government has implemented certain measures and various economic plans for exchange controls. The depreciation of the *real* also creates inflationary pressures in Brazil that may adversely affect our results and generally restricts access to the international capital markets. It also reduces the U.S. dollar value of our revenues, our distribution of dividends and the U.S. dollar value of the market price of our common shares. On the other hand, appreciation of the *real* in relation to the U.S. dollar may cause the deterioration of the country's accounts, balance of payments, and slower economic growth of exports. The result of the sharp depreciation of the Brazilian *real* in relation to the U.S. dollar has in the past and may in the future generate inflation and governmental measures to counteract the effects of inflation, including increases in interest rates. As of September 2005, we had total consolidated indebtedness denominated in foreign currency of approximately US$238 million. In addition, some costs associated with the acquisition of certain equipment and technology purchases for our generation facilities are pegged to foreign currencies. Consequently, devaluation of the real against the dollar may adversely affect the Brazilian economy

and our results of operations, particularly due to the fact that a portion of our indebtedness is pegged to the U.S. dollar.

Fluctuations in interest rates may have an adverse effect on our business and in the market price of our common shares.

The Central Bank establishes the basic interest rate for the Brazilian financial system by reference to the level of economic growth of the Brazilian economy, the level of inflation and other economic indicators. From February to July 17, 2002, the Central Bank reduced the basic interest rate from 19% to 18%. From October 2002 to February 2003, the Central Bank increased the basic interest rate by 8.5 percentage points, to 26.5% on February 19, 2003. The basic interest rate continued to increase until June 2003 when the Central Bank started to decrease it. Subsequently, in 2004 and in the first nine months of 2005, the basic interest rate began to increase again and, as of the date of this offering memorandum, the basic interest rate was 19.0%.

As of September 30, 2005, a significant portion of our indebtedness was denominated in *reais* and pegged rates in the Brazilian financial market or inflation indexes, such as TJLP and the DI rate. As of September 30, 2005, our total indebtedness was R$1,584.1 million, and R$1,064.2 million of that amount was subject to floating interest rates. Therefore, an increase in the DI interest rates and inflation indices may have an adverse impact on our results, as it would increase the costs of our debt.

The perception of risk in other economies, primarily emerging market economies, may adversely affect the Brazilian economy and our business and the market price of our common shares.

The Brazilian economy, the Brazilian capital markets and securities issued by Brazilian companies have been affected by economic and market conditions in Brazil and other emerging market countries, particularly in Latin America, and by the reactions of investors to these conditions. Events or conditions in other emerging market countries have significantly affected access to capital in the Brazilian economy and resulted in significant outflow of funds and drop in the volume of foreign investments in Brazil. We cannot assure you that future events in emerging market countries, as well as measures adopted by the governments of such countries, will not adversely affect access to domestic or international capital markets. We operate in a sector that requires significant capital expenditures, and limited access to the capital markets may adversely affect our ability to fully develop our investment plan, expand our generating facilities and maintain our market share, which may adversely affect our results of operations and financial position, as well as the market price of our common shares.

RISKS RELATING TO THE BRAZILIAN POWER INDUSTRY

The extensive regulation imposed on the energy sector by the Brazilian government and eventual changes in those regulations may affect our business and results of operations.

Our operations are primarily regulated and supervised by ANEEL and MME. ANEEL, MME and other regulators have historically exercised significant influence over our business, including on the types and terms of our contracts as well as our level of power output. In recent years, the Brazilian government has implemented policies that have had far-reaching impact on the Brazilian power industry and, in particular, the electricity sector. In this regard, the New Electricity Law, which regulates the operations of companies in the power industry, was enacted on March 15, 2004, and

substantially changed the policies then in effect and the rules applicable to the sale of electricity in Brazil, which changes include:

- the creation of a regulated market for the purchase and sale of electricity, on which electricity distribution companies must contract, by means of public auctions conducted and organized by ANEEL and MME, 100% of their demand for electricity;
- the need for power generators to prove that they are capable of supplying required electricity to their consumers; and
- the prohibition of transactions with related parties, including the sale of electricity by power generators to affiliated distribution companies.

Such legislation is subject to regulation by the MME and ANEEL, by way of decrees, resolutions and other regulatory acts, including the prices and conditions of the new energy, conditions and rules for energy activities, and its constitutionality is currently being challenged in the Brazilian Supreme Court. As of the date of this offering memorandum, the Brazilian Supreme Court had not issued a final decision on this matter, and the New Electricity Law remains in effect. If all or a substantial portion of the New Electricity Law is determined to be unconstitutional by the Brazilian Supreme Court, the regulatory scheme introduced by that law may not become effective, thus creating uncertainty as to how and when the Brazilian government will be able to introduce changes to the electricity sector. The impact on our business of the regulatory changes introduced by the New Electricity Law, the above-mentioned legal proceedings and possible future reforms in the power industry are difficult to predict, and could adversely affect our business and results of operations.

Additionally, on November 18, 2004, MME enacted Directive (*Portaria*) No. 303 in which the methodology for the calculation of the generation capacity of the thermoelectric plants was revised, and that new calculation must be observed starting 2008. Our thermoelectric plants had generation capacity of 984.8 MW as of September 30, 2005, and as of 2008, we believe that they will have generation capacity of 852.8 MW, following application of the new methodology proposed by the ANEEL Directive No. 303. We cannot assure you that additional measures with different methodologies, such as those of Directive No. 303, will not be implemented in the future, and accordingly, our generation capacity may be further reduced or otherwise regulated, which may adversely affect our results of operations and the market price of our common shares.

Our main commercial activities, the implementation of our strategy for growth, as well as the ordinary carrying out of our business may be adversely affected by governmental actions such as:

- changes to current legislation applicable to our business;
- changes and/or the termination of the federal and state concession programs;
- creation of more rigid criteria for qualification in future public energy auctions; and
- delay in the revision and implementation of new annual tariffs.

We may not predict future government actions and the impact of such actions on our results of operations. If we are required to conduct our business in a manner substantially different from the one provided for in our business plan, our results of operations and financial results may be adversely affected.

Our growth by means of public auctions for new concessions may be adversely affected by future governmental actions or measures related to concessions for generation facilities.

The government imposes certain restrictions on bidders that participate in auctions for new concessions, including requirements to assess their financial stability, as well as that of their

shareholders. We cannot assure you that we will be able to satisfy all the requirements necessary in order to acquire new concessions or to participate in auctions for new concessions. Concessions for the use of public resources, i.e. water (used in energy generation), may be subject to different levels of political influence. The rules of the auctions for generation plants are subject to federal as well as state legislation. We cannot assure you that future auctions for new generation plants will take place. If such auctions do not occur in the frequency we expect or do not occur at all or on terms that are not attractive to us or our controlling shareholder from an economic standpoint, our current plan for the expansion and diversification of our generation facilities may be adversely affected, and as a result, the market price of our common shares will decrease.

If in the future we increase the sale of energy in the regulated market and distribution companies opt to reduce the electricity they purchase from us, our pricing and sales of energy may be adversely affected.

We will sell 541 MW of energy in the regulated market commencing in 2008. Beginning in 2009, when our current volumes of energy contracted will begin to be substantially reduced, we may increase the sale of energy in the regulated market. Current legislation permits distribution companies that contract with us in the regulated market to reduce their contracted energy up to a certain point (5%), thereby exposing us to the risk that we may not be able to contract for the sale of energy at a desirable price with other customers. If that happens and we do not succeed in contracting to sell, or are unable to sell surplus capacity at adequate prices and on favorable terms, our business and our results of operations may be adversely affected, which could negatively impact the market price of our common shares.

The impact of a potential lack of electricity and the consequent rationing of electricity may have an adverse effect on our business and results of operations.

Hydroelectricity is the major source of electricity in Brazil, representing in 2004 approximately 78% of Brazil's installed capacity and 92% of the energy generated. In the years prior to 2001, rainfall volumes were substantially lower than the historical averages and the lack of expansion of the installed capacity of SIN (in particular due to legal and regulatory hindrances reflected in the expansion program of the thermoelectric capacity), resulted in a sharp reduction in reservoir levels in the southeastern, mid-western and northeastern regions of Brazil. As a result, on May 15, 2001, the Brazilian government implemented a program to reduce the use of energy, which was known as "Rationing Program." The Rationing Program established indexes for the reduction of energy use by industrial consumers, as well as commercial and residential consumers that varied between 15% and 25% and lasted from June 2001 to February 2002. If Brazil undergoes another period of potential or actual shortage of electricity, the Brazilian government may implement policies and measures that may have a substantial adverse effect on our business, results of operations and financial position, as well as the market price of our common shares.

Changes in environmental laws and regulations may adversely affect the business of companies of the electricity sector, including us.

Companies in the electricity sector, in particular power generation companies, are subject to strict environmental legislation at the federal, state and municipal levels regarding, among other things, air emissions and interventions in protected areas. These companies require licenses and authorizations from governmental agencies to perform their activities. Violation or non-compliance with such laws, regulations, licenses and authorizations may result in administrative sanctions, such as fines, suspension of activities, cancellation of licenses and revocation of authorizations, or, in certain circumstances, criminal sanctions. The Public Prosecutor's Office may start a civil investigation and/or file a public

civil action for compensation for damages to the environment and/or to third parties. The governmental agencies or other authorities may implement stricter rules or seek more restrictive interpretations of the existing ones, which may require expenditure of additional funds in environmental adaptation, including for environmental licenses for facilities and equipment that did not previously require environmental licenses. Governmental agencies or other authorities may also significantly delay the issuance of required licenses and authorizations required to operate in the electricity sector, resulting in delay in schedules for the implementation of projects. Any such action by the governmental agencies may negatively affect the business of the electricity sector and have an adverse effect on our business and results.

We may be subject to substantial costs, including indemnification and penalties for damage to the environment, which may have an adverse effect on our business and on the market price of our shares.

The activities of the energy sector may result in damage to the environment. Under Brazilian law, anyone who directly or indirectly causes damages to the environment may be held responsible for such damages, regardless of whether this person is at fault. In addition, Brazilian law allows for direct responsibility of an entity's executives to make possible the compensation for environmental damages. As a result, our shareholders, officers and directors may be held personally responsible for any damages we may cause to the environment. Payment of substantial indemnification and environmental costs may prevent or cause us to redirect planned investments which may have an adverse affect on our business and operations.

Social pressures designed to limit the expansion of generating facilities may cause electricity generation companies, including us, to delay implementation or interrupt operation of their plants.

Organized social movements that are opposed to the expansion of large hydroelectric facilities may interrupt or cause significant delays in the implementation and/or operation of hydroelectric projects, including by means of claims for collective or individual re-settlement, concession of benefits, compensation or indemnities, among others, in addition to those planned and expected by the companies of the electric sector, including us. Any such action by these social movements may negatively affect the business of the energy sector and have an adverse effect on our business and results.

Reduction in the sales price of electricity resulting from energy auctions promoted by CCEE in the regulated market may have an adverse impact on our results of operations.

On December 7, 2004, the first energy auction was carried out under the New Electricity Law and the electricity of existing energy plants (''so-called old energy'') was auctioned. Supply of energy in the Brazilian market is currently higher than the demand, resulting in a reduction in prevailing energy prices. Because under the New Electricity Law, we own generation assets that were considered ''existing energy assets,'' when participating in the auction of ''old energy,'' we will be competing with state-owned generating companies that generally are able to offer energy that is cheaper than that of private companies. Therefore, the participation of these companies in auctions of old energy may result in a reduction of energy prices. Our participation in these auctions may result in a reduction of our revenues, as we will have to lower our energy sales prices to make possible the sale of energy at the auctions, which may negatively affect our operating and financial results, as well as the market price of our common shares.

Increased competition for independent consumers after the termination of the initial contracts may adversely affect our business and financial condition.

During the transition period to a competitive electricity market from 1998 to 2005, the purchase and sale of electricity between generation and distribution concessionaires of electricity then existing in the market had to be made through initial contracts, at prices and volumes approved by ANEEL. Such initial contracts replaced the then existing system of "supply contracts". The initial contracts were approved by ANEEL in August 1998 for companies located in the south of the country, and in December 1998 for companies located in all other regions. Energy generation and power demand were pre-established for the period between 1999 and 2002. During the transition period, the energy supplied under initial contracts was scheduled to be reduced by 25% every year from 2003 through 2005. Those contracts will expire effective December 31, 2005. Pursuant to the new regulation, the energy originally contracted under the initial contracts may be sold to independent consumers. When the initial contracts expire completely, we expect that competition among power generators and traders to supply energy to independent consumers will increase. Competition may impair our growth or result in difficulties in renewing our existing contracts with independent consumers once they terminate, which could adversely affect our revenues, results of operations and the market price of our common shares.

RISKS RELATING TO OUR BUSINESS

Our concessions and authorizations, pursuant to which we are authorized to generate electricity from our various hydroelectric and thermoelectric, respectively, facilities, are subject to early termination in certain circumstances.

Under our concession contracts with the government (through ANEEL), we are authorized to operate hydroelectric projects from which we produce most of the electricity we sell for a fixed period of years. These concessions may be renewed for an additional period equal to their original term if renewal is requested with at least 36 months advance notice, and provided that the we have complied with all our obligations under the concession contracts. Even if we have fulfilled all our obligations under the concession agreements and requested the renewal of the concession period, renewal of the concession is subject to the discretion of the concession authority. There are no guarantees that our concessions will be renewed by the concession authority. In addition, renewal of a concession would likely be conditioned on the payment by us of new concession fees for the production and trading of electricity. The concession contracts provide for early termination in the following cases: (i) expropriation by the Government by reason of public interest; (ii) forfeiture of the concession (under the terms of the concession contracts); or (iii) non-compliance by us with our obligations provided for in the concession contracts and pursuant to applicable legislation and regulations. We may also declare an early termination of the concession contracts in the event of non-compliance by the government with its obligations but we must first file a lawsuit in that regard.

The indemnity to which we are entitled in the case of early termination of the concession contracts may not be sufficient to compensate us for the full value of our assets. Additionally, if any of the concession contracts is terminated as a result of our non-compliance with our obligations, the effective amount of compensation payable by the Government may be significantly reduced and fines or other penalties may be imposed. Early termination of any of our concession contracts for any reason would have a material adverse effect on our business, results of operations and financial position, as well as on the market price of our shares.

Pursuant to the authorizations for operation of our thermoelectric plants, if we fail to fully comply with the terms of such authorizations, they may be terminated early by the granting authority, which,

individually or in the aggregate, would have a material adverse effect on our business, results of operations and financial position, as well as on the market price of our shares.

We may not be able to fully implement our business strategy.

Our ability to implement our business strategy depends on many factors, including our ability to:

- grow with financial discipline;
- manage our customer portfolio efficiently; and
- maintain operating efficiency.

We cannot assure you that any of these goals will be achieved, in whole or in part. Our strategy is based on our ability to expand our generation facilities on reasonable terms and conditions by means of new projects (by acquisition of existing concessions, including concessions granted to our controlling shareholder, or by winning bids in auctions for new concessions). In addition, we obtain new concessions for which we require financing for the construction of new dams or for the repair or improvement of existing dams. If we are not successful in our bids for new concessions or for the acquisition of existing ones or if the related costs of construction or improvement are not attractive, our financial condition and results of operations may be adversely affected.

ANEEL could penalize us or intervene in our concessions if we fail to comply with the terms of the concession contracts, the authorizations granted by ANEEL or the rules and regulations of the energy sector.

ANEEL may impose penalties and restrictions on us if we fail to comply with our obligations under the concession contracts and authorizations. Depending on the materiality of any such breach, we may be subject to any of the following:

- notices *(advertências);*
- penalties of up to 2% of our revenues in the fiscal year preceding the assessment of respective violation;
- injunctions barring the construction of new facilities and purchase of new equipment;
- restrictions on the operation of existing facilities and equipment;
- temporary suspension from participating in the bidding process for new concessions; and
- forfeiture of our concessions.

ANEEL may, in addition to those penalties described above, intervene in the concessions to ensure adequate operation of our facilities and compliance with applicable laws and regulations.

Any of the foregoing penalties, or the intervention of ANEEL in our concessions, may have a material adverse effect on our business, results of operations and financial condition, as well as on the market price of our common shares.

Construction, expansion and operation of our hydroelectric and thermelectric plants involve significant risks that may reduce revenues, increase expenses or otherwise adversely impact our financial condition.

Construction, expansion and operation of our hydroelectric and thermelectric plants and power generation equipment involve various risks, including:

- the inability to obtain required regulatory permits and approvals;
- the unavailability of equipment;
- the unavailability of distribution and/or transmission centers;
- supply interruptions;
- work stoppage, strikes and other labor disputes;
- social unrest;
- weather and hydrological interferences;
- unforeseen engineering and environmental problems;
- construction and operational delays, or unanticipated cost overruns;
- changes to currently existing regulatory subsidies;
- necessity of high capital expenditures; and
- the unavailability of financing on reasonable terms.

We do not contract insurance to protect against all of these risks. The occurrence of these or other problems may adversely affect our capacity to generate electricity consistent with our projections or obligations to our clients, which may have a material adverse effect on our financial position and results of operations, as well as on the market price of our common shares.

A substantial part of our results of operations depend on favorable hydrologic conditions.

According to data published by the ONS, approximately 92% of the electricity in Brazil is generated by hydroelectric plants. As the SIN operates using an optimized delivery system (meaning that energy is distributed through the national grid from generation facilities based on a formula that takes account of a facility's historical generation capacity based on prevailing hydrological conditions, among other factors), each hydroelectric plant is subject to variations in the amount of energy sold by it if affected by hydrologic conditions prevailing in both the geographic region it operates and other regions of Brazil. The occurrence of unfavorable hydrologic conditions, coupled with the obligation to deliver our assured energy, may result in our having to purchase energy on the short-term energy market, the prices on which tend to be high, which may adversely affect our future financial results, as well as the market price of our common shares.

We are responsible for any losses and damages caused to third parties as a result of failures in the generation of our plants, as well as interruptions or disturbances that may not be attributed to any identified agent of the electric system and the insurance policies contracted may not be sufficient to cover these losses and damages.

We may also be held responsible for (i) losses and damages caused to third parties as a result of failures in the operation of our plants, which can cause interruptions or disturbances in the distribution and/or transmission systems; or (ii) interruptions or disturbances that may not be attributed to any identified agent of the electric system. The indemnities payable in the latter case are

apportioned as follows: 60% to the distribution companies, 20% to the power generators and 20% to the transmission companies. Any such losses could have a material adverse effect on our business, results of operations and financial condition.

We may have to bear significant additional costs associated with our employee pension plan.

Our Defined Benefit Plan (*Plano de Beneficio Denifido (BD)*) represents a risk that cannot be assessed with certainty since its costs are calculated on an actuarial basis. Through September 30, 2005, we have experienced a migration of 94% of our active participants from the BD to our new Defined Contribution Plan (*Plano de Contribuição Denifida*). For the period ending September 30, 2005, our liabilities from retirement benefits were R$267 million, of which R$114 million was related to contracted debts. The total actuarial loss of R$155.3 million (which exceeds the present value of our actuarial obligations in accordance with Brazilian GAAP) will be amortized over an 11-year period, which corresponds to the estimated average remaining employment period for the employees that participate in the plan, using the straight-line method. If we have to record on our financial statements the total actuarial loss, our results of operations may be adversely affected.

Adverse decisions in lawsuits may adversely affect our results of operations.

We are party to several civil, labor, social security and tax lawsuits arising in the regular course of our business. As of September 30, 2005, our potential probable, possible and remote liability from these lawsuits totaled R$237.2 million in aggregate. Of this total, approximately 9.8% relates to tax matters, 13.9% relates to social security matters, 14.4% relates to labor matters and the remaining 61.9% relates to other civil and commercial matters. As of September 30, 2005 we had established provisions in the total amount of R$145.5 million, for potential losses. An adverse decision in any of the lawsuits with possible or remote liability may adversely affect our results of operations.

Adverse judicial decision on the lawsuits filed against the privatization of Gerasul may cause unpredictable results and adversely affect our business and the investors in our common shares.

When Gerasul was privatized in 1998, two public civil actions and three class actions were filed against us, the government, BNDES, ANEEL, Eletrobras, Eletrosul and our controlling shareholder. Such claims challenge the corporate restructure that resulted in the incorporation and privatization of Gerasul (our former corporate name). In 2001, a court decision was entered in favor of one of the public civil actions, holding Eletrosul's spin-off which resulted in the incorporation of Gerasul, and all other acts after such incorporation is invalid. Due to this decision, the court judge extinguished all other claims without analyzing the merits thereof. The parties filed appeals with the relevant appellate court (*Tribunal Regional Federal da 4ª Região*) that reversed the court decision on this public civil action, upholding the validity of all acts related to the privatization of Gerasul. This Tribunal also dismissed the class action suits and held in favor of the privatization of Gerasul. A final decision in relation to these matters may take years since the decision by the appeal tribunal is still subject to appeal to the Brazilian Superior Court and the Brazilian Supreme Court. Although the adverse decision has been reversed we and the other parties to the lawsuit cannot guarantee you that such reversed decision will be upheld by the Brazilian Supreme Court or by the Brazilian Superior Court. It is hard to predict the consequences of an adverse decision with respect to these claims. One possible result could be that the privatization of Gerasul could be declared void. Potential outcomes vary widely and are complex and may involve claims for losses and damages involving the government, BNDES, ANEEL, Eletrobras, Eletrosul, us, our controlling shareholders and third parties, including investors in our common shares.

Because a portion of our assets are dedicated to providing an essential public service, they will not be available for liquidation in the event of bankruptcy, and cannot be subject to attachment to secure a judgment.

A portion of our generation assets is deemed to be dedicated to providing an essential public service. Those assets would not be available for liquidation in the event of bankruptcy or attachment to secure a judgment, and in such cases would, pursuant to the terms of our concession contracts and Brazilian law, revert to the Brazilian government. These restrictions on liquidation and attachment may lower significantly the amounts investors in our common shares would otherwise be entitled to receive in the event of our liquidation and may have an adverse effect on our ability to obtain financing.

The financial agreements, deed of issue of debentures and other instruments that represent our debts have specific covenants, and any default as a result of the non-compliance with these covenants may adversely and materially affect our financial position and our capacity to conduct our business.

We have entered into several agreements relating to financial instruments, some of which require that we comply with certain financial covenants and with other specific obligations. Defaults in these instruments that are not remedied or waived by the respective creditors may cause these creditors to declare the early maturity of such debts, as well as result in the cross default of other financial instruments. Our assets and cash flow may not be sufficient to fully pay for the debt balance of our obligations.

We may need additional capital in the future, which may dilute your ownership interest in our company or which may not be available to us.

We may need to raise additional funds through public or private debt or equity financings. Any additional capital raised through the sale of equity may dilute your percentage ownership interest in our company. Furthermore, any additional financing we may need may not be available on terms favorable to us, or at all.

RISKS RELATING TO OUR SHARES

The relative volatility and lack of liquidity of the Brazilian capital markets may substantially limit the capacity of investors to sell our shares for the desired price and at the desired time.

Any investment in securities, such as our shares, inherently pose risks due to fluctuations in price and, accordingly, investors in our common shares will be subject to the volatility of the capital markets. Investments in the Brazilian capital markets, including investments in our common shares, are subject to economic and political risks, involving, among others:

- changes in the regulatory, tax, economic and political environment that may affect the ability of investors to receive payment, in whole or in part, in respect of their investments; and
- restrictions on foreign investment and on repatriation of capital invested.

Additionally, the possible lack of liquidity of the Brazilian securities market may substantially limit the ability of investors to sell our common shares for the desired price and at the desired time. In particular, prior to the offering, our common shares showed limited liquidity and the offering is part of our strategy and of our controlling shareholder to promote the liquidity of our common shares. However, we cannot assure you whether a liquid and active trading market will develop for our common shares. These factors may unfavorably affect the market value and the liquidity of our shares, which may limit an investor's ability to resell our common shares for the desired price and at the desired time.

The Suez Group, through SESA, our controlling shareholder, may make certain decisions with respect to our business without the participation of all of our shareholders.

SESA, a company controlled by the Suez Group, currently owns approximately 78.3% of our voting capital before the offering and will hold 69.88% of the voting capital after the offering (not taking into account the over-allotment). As a result, SESA has sufficient voting power independently to:

- appoint a majority of the members of our board of directors;
- cast the deciding vote in a change in our control even if the change is not in the best interest of the other shareholders;
- cast the deciding vote in a strategic merger with another company that could bring significant benefits to the companies that participate in the merger;
- limit the opportunity of the other shareholders to receive goodwill for their shares due to a possible capital restructuring, including takeovers, mergers, spin-offs or *incorporação de ações* (merger of shares); and
- influence our dividend policy.

Additionally, the strategy of the Suez Group in Brazil includes the development of new projects, particularly large hydroelectric projects, independently of our company. Therefore, the qualification process for public auctions, the obtaining of concessions and authorizations, the establishment of consortia with other companies, negotiation of construction agreements, acquisition of equipment, and financing of new projects, are carried out by a third party. Although these projects are intended to be subsequently transferred to us after completion of these initial steps, SESA is not contractually obligated to do so. This transfer is made in accordance with the valuation made by an independent institution that evaluates the project and the transfer price is produced by such evaluation. The approval of certain matters, including the implementation of commercial plans and budgets, the issue of shares or securities that represent equity or debt and the approval of certain loan or financing instruments by our Board and our shareholders is ultimately subject to the approval of SESA.

Holders of our common shares may not receive any dividends.

Our by-laws, dated November 9, 2005, require us to pay to our shareholders a minimum mandatory dividend of 30% of our adjusted net income, in the form of dividends and/or interest on shareholders' equity, calculated in accordance with Brazilian corporation law. The distribution of dividends depends, primarily, on our determination of net income. In addition, the distribution of dividends is subject to the favorable decision by our board of directors as provided for in our by-laws and in Brazilian corporation law. Notwithstanding the minimum dividend requirement, our board of directors may elect not to pay any dividends to our shareholders in any particular fiscal year if the board deems such distributions to be inadvisable in light of our financial condition. As a result, an investment in our shares does not ensure the investor will receive dividends.

Substantial sales of our common shares after this offering may cause the market price of our common shares to decrease.

We, our controlling shareholder, BNDESPAR and Banco Clássico S.A. have agreed that, subject to certain exceptions as described in "Plan of distribution," within 180 days of the date of this offering memorandum they will not issue or transfer their common shares issued by us, as applicable. At the end of such period, our common shares held by such shareholders, may be freely traded. Should we decide to issue common shares, or should our controlling shareholder decide to sell additional common

shares, or if the market perceives that our controlling shareholder or we intend to sell additional common shares, the market value of our common shares may decrease significantly.

Changes in Brazilian tax laws may have an adverse impact on the taxes applicable to a sale of our common shares.

According to Law No. 10,833, enacted on December 29, 2003, the disposition by a non-resident of Brazil of assets located in Brazil is subject to taxation in Brazil, regardless of the domicile of the purchaser or whether the sale occurs outside or within Brazil. If the sale of assets is interpreted to include a sale of our common shares, this tax law could result in the imposition of income tax on a sale of our common shares by a non-resident of Brazil to another non-resident of Brazil. Law No. 10,833 does not apply to gains obtained on transactions carried out at a Brazilian stock exchange by investors registered in accordance with Resolution No. 2,689 of the Brazilian National Monetary Counsel, if the investor is not located in a tax haven jurisdiction, as defined in Brazilian tax legislation. See "Taxation—Brazilian tax considerations—Income tax—Gains." Because Law No. 10,833 has been recently enacted and no judicial guidance as to its application yet exists, we are unable to predict whether an interpretation applying such tax laws to sales of our common shares between non-residents could ultimately prevail in the courts of Brazil.

It is expected that non-corporate U.S. shareholders will be ineligible for the favorable U.S. federal income tax treatment that applies to dividend income received from certain corporations.

Dividends received before January 1, 2009 by non-corporate U.S. shareholders on shares of certain foreign corporations will be subject to U.S. federal income tax at lower rates than other types of ordinary income if certain conditions are met. However, because our common shares are not readily tradable on an established securities market in the U.S. and there is no income tax treaty between Brazil and the U.S., we currently do not expect those conditions will be met. As a result, distributions on our common shares paid out of our current or accumulated earnings and profits, as determined under U.S. federal income tax principles, will generally be taxable as ordinary income to U.S. shareholders and will not be entitled to a reduced rate of taxation. See "Taxation—Certain United States federal income tax consequences—Taxation of dividends."

Use of proceeds

Because the offering described in this offering memorandum will be a secondary offering of our common shares by the selling shareholder and BNDESPAR (only in Brazil), we will not receive any proceeds. The selling shareholder and BNDESPAR will receive all net proceeds from the sale of our common shares in this offering.

Exchange rates

Until March 4, 2005, there were two legal foreign exchange markets in Brazil, the commercial rate exchange market, or the Commercial Market, and the floating rate exchange market, or the Floating Market. On January 25, 1999, the Brazilian government announced the unification of the exchange positions of the Brazilian financial institution in the Commercial Market and in the Floating Market, leading to a convergence in the pricing and liquidity of both markets. The Commercial Market was reserved primarily for foreign trade transactions and transactions that generally required prior approval from Brazilian monetary authorities, such as registered investments by foreign persons and related remittances of funds abroad (including the payment of principal of and interest on loans, notes, bonds and other debt instruments dominated in foreign currencies and registered with the Central Bank). The Floating Market rate generally applied to specific transactions for which Central Bank approval was not required. Both the Commercial Market rate and the Floating Market rate were reported by the Central Bank on a daily basis.

On March 4, 2005, the Central Bank issued Resolution no. 3,265, providing for several changes in Brazilian foreign exchange regulation, including: (i) the unification of the foreign exchange markets into a single exchange market; (ii) the easing of several rules for acquisition of foreign currency by Brazilian residents; and (iii) the extension of the term for converting foreign currency derived from Brazilian exports. It is expected that the Central Bank will issue further regulations in relation to foreign exchange transactions, as well as on payments and transfers of Brazilian currency between Brazilian residents and non-residents (such transfers being commonly known as the international transfer of *reais*), including those made through the so-called non-resident accounts (also known as CC5 accounts).

From March 1995 through January 1999, the Central Bank allowed the gradual devaluation of the *real* against the U.S. dollar under an exchange rate policy that established a band within which the *real*/U.S. dollar exchange rate could fluctuate. Responding to pressure on the *real,* on January 13, 1999, the Central Bank widened the foreign exchange rate band. Because the pressure did not ease, on January 15, 1999, the Central Bank abolished the band system and allowed the *real* to float freely.

Since the beginning of 2001, the Brazilian exchange market has been increasingly volatile, and, until early 2003, the value of the *real* declined relative to the U.S. dollar, primarily due to financial and political instability in Brazil and Argentina. In 2004, however, the *real* appreciated in relation to the U.S. dollar 8.8%, and at September 30, 2005, the *real*/U.S. dollar exchange rate was R$2.2222 per U.S.$1.00, which represented an appreciation of the *real* against the U.S. dollar of 16.3% since December 31, 2004. Although the Central Bank has intervened occasionally to control unstable movements in the foreign exchange rates, the exchange market may continue to be volatile as a result of this instability or other factors, and, therefore, the *real* may substantially decline or appreciate in value in relation to the U.S. dollar in the future.

The following tables set forth the selling rate, and, where applicable, the commercial selling rate, expressed in reais per U.S. dollar (R$/U.S.$) for the periods indicated, as reported by the Central Bank.

	***Reais* per US$1.00**		
Year ended December 31,	**Average[(1)]**	**High**	**Low**
2001	2.3522	2.8007	1.9357
2002	2.9309	3.9552	2.2709
2003	3.0715	3.6623	2.8219
2004	2.9257	3.2051	2.6544

Source: Central Bank
(1) The average of the exchange rates during the period.

Exchange rates

Last six months,	*Reais* per US$1.00 Average[1]	High	Low
June 2005	2.4135	2.4891	2.3504
July 2005	2.3735	2.4656	2.3304
August 2005	2.3603	2.4615	2.2767
September 2005	2.2944	2.3623	2.2222
October 2005	2.2564	2.3623	2.2339
November 2005	2.2108	2.2516	2.1633

Source: Central Bank

(1) The average of the exchange rates during the period.

On December 6, the selling rate was R$2.1807 per US$1.00.

Exchange rate fluctuations will affect the U.S. dollar equivalent of the price of our common shares in *reais* on BOVESPA as well as the U.S. dollar equivalent of any distributions we make with respect to our common shares, which will be made in *reais*. Exchange rate fluctuations may also affect our financial condition. See "Risk factors—Risks Relating to Brazil—Volatility in the value of the Brazilian *real* in relation to the U.S. dollar and other currencies may negatively affect our business."

Capitalization

The table below shows our cash, cash equivalents and cash investments; short-term debt; and long-term debt and capitalization at September 30, 2005. This information is derived from our unaudited consolidated financial statements for the nine-month period ended September 30, 2005, prepared in accordance with Brazilian GAAP. You should read this table in conjunction with "Selected financial and operating information," "Management's discussion and analysis of financial condition and results of operations" and our audited consolidated financial statements and the notes thereto included in this offering memorandum.

Solely for the convenience of the reader, *real* amounts as of September 30, 2005, have been translated into U.S. dollars at the exchange rate as reported by the Central Bank on September 30, 2005, of R$2.2222 to US$1.00. The selling rate as reported by the Central Bank on December 6, 2005 was R$2.1807 to US$1.00. The U.S. dollar equivalent information should not be construed to imply that the *real* amounts represent, or could have been or could be converted into, U.S. dollars at such rates or at any other rate.

	At September 30, 2005	
	(R$ millions)	(US$ millions)
Total capitalization[(1)]	$4,961.1	$2,232.5
Total current debt	275.9	124.2
Loans and financing	240.9	108.4
Foreign currency-denominated		
Brazilian Treasury	89.3	40.2
Loans and financing	19.3	8.7
Real-denominated		
Eletrobrás	71.6	32.2
Loans and financing	60.7	27.3
Debentures	35.0	15.8
Total long-term debt	1,308.2	588.7
Loans and financing	963.6	433.6
Foreign currency-denominated		
Brazilian Treasury	288.1	129.6
Loans and financing	131.2	59.0
Real-denominated		
Eletrobrás	193.5	87.1
Loans and financing	350.8	157.9
Debentures	344.6	155.1
Shareholders' equity	3,377.0	1,519.7
Capital stock	2,445.8	1,100.6
Capital reserves	91.7	41.3
Profit reserve	249.5	112.3
Accumulated profits	590.0	265.5

(1) Total capitalization equals the sum of total debt and shareholders' equity.

Dilution

In the U.S. market, dilution is usually presented as the amount by which the offering price paid by the purchasers of the common shares to be sold in this offering will exceed the net book value per common share of our capital stock after the offering. The net book value per common share is equal to the amount of our total assets less total liabilities, divided by the number of common shares outstanding. Because the offering is entirely of secondary shares (common shares already held by our existing shareholders before this offering), the number of shares outstanding does not increase as a result of this offering. In addition, because the net proceeds of this offering will be paid entirely to the selling shareholder, our net book value does not increase as a result of this offering. Our net book value as of September 30, 2005 was R$3,377.0 million or R$5.17 per share. The offering price is R$13.00 per share. This represents an immediate dilution of R$7.83 per share in the value paid per share by new investors purchasing at the offering price relative to the net tangible book value of our company.

Dividends

Our by-laws, dated November 9, 2005, require us to pay to our shareholders a minimum mandatory dividend of 30% of our adjusted net income, in the form of dividends and/or interest on shareholders' equity, calculated in accordance with Brazilian corporation law, unless our board of directors recommends against such distribution due to considerations relating to our financial condition. See "Description of the capital stock—Destination of net income and distribution of dividends" for more information regarding the calculation of the amount available to be distributed to our shareholders. The mandatory minimum distribution may be paid in the form of dividends or interest on shareholders' equity, whose value, net of income tax payable on that amount by the recipient, may be allocated to the mandatory distribution and deducted by us in calculating our income and social contribution tax obligations.

Upon acquiring our common shares, shareholders will have the right to receive dividends declared from the acquisition date onwards. The following table shows the amounts of dividends declared and interest on shareholders' equity for the periods indicated.

	For the Year Ended December 31,[1]				
	2004	2003	2002	2001	2000
	(R$ thousands, except per share data)				
Calculation of mandatory dividends					
Net income (loss) for the fiscal year	775,192	517,154	(183,521)	582,274	162,801
Legal reserve (5%)	(38,760)	(25,857)	—	(29,114)	(8,140)
Base for calculating mandatory dividends	736,432	491,297	—	553,160	154,661
Mandatory dividends (25%)	184,108	122,824	—	138,290	38,665
Proposed dividends/interest on shareholders' equity					
Interest on shareholders' equity (net of income tax)	216,750	198,900	—	68,820	—
Balance of the proposed dividends	482,032	257,297	—	96,300	136,799
Subtotal	698,782	456,197	—	165,120	—
Withholding income tax on shareholders' equity	38,250	35,100	—	11,180	—
Total	737,032	491,297	—	176,300	—
Dividends/interest in shareholders' equity before income tax, per 1,000 shares (in R$1.00)					
Class A preferred	0.920260	0.773822	—	0.345021	0.301852
Class B preferred	0.845321	0.698884	—	0.270083	0.226389
Common shares	1.070525	0.698884	—	0.270083	0.226689

(1) Information is presented per 1,000 shares. On May 23, 2005, we consummated a reverse stock split whereby our shareholders received one common share for each 1,000 shares previously outstanding.

Our board of directors approved the payment of interest on our share capital relating to results for the period from January 1 through May 31, 2005, in aggregate principal amount of R$110 million, corresponding to R$0.199740 per 1,000 class A preferred shares, R$0.168516 per 1,000 class B preferred shares and R$0.168516 for one thousand common shares. Payment for these dividends

became effective on July 8, 2005. On May 23, 2005, we consummated a reverse stock split of our common shares pursuant to which our shareholders received one common share for each 1,000 common shares previously outstanding.

On October 19, 2005, we reported that our board of directors, in a meeting held on that date, approved the following matters: (i) credit of interest on shareholders' equity for the period from June 1 through November 10, 2005, in the aggregate principal amount of R$122 million, corresponding to R$0.186904 per share; (ii) distribution of interim dividends based on our financial statements dated June 30, 2005, in the amount of R$141 million, corresponding to R$0.216012 per share; and (iii) distribution of interim dividends, based on our profit reserve account as of December 31, 2004 (except for legal reserve), in the amount of R$147 million (included in the 2004 column of the table above), corresponding to R$0.225204 per share. Payments for such dividend distributions began on November 10, 2005.

We intend to pay dividends and/or interest on shareholders' equity net of income tax in the amount of approximately 55% of our net income for each fiscal year, and that amount may be adjusted in accordance with Brazilian corporation law. However, our board of directors may change this policy at any time in its sole discretion by a simple majority vote, and we cannot guarantee that we will pay you any dividends or interest on shareholders' equity in the future.

Although we intend to abide by this dividend policy, you should be aware that the declaration of annual dividends, including dividends in excess of the mandatory distribution, requires approval by vote of a majority of the holders of our common shares at a general shareholders' meeting and will depend on many factors. These factors include our results of operations, financial condition, cash requirements, future prospects and other factors deemed relevant by our shareholders.

Dividends received before January 1, 2009 by non-corporate U.S. shareholders on shares of certain foreign corporations are subject to U.S. federal income tax at lower rates than other types of ordinary income if certain conditions are met. However, because our common shares are not traded on an established securities market in the United States and there is no income tax treaty between Brazil and the United States, we currently do not expect that those conditions will be met. As a result, distributions on our common shares paid out of our current or accumulated earnings and profits, as determined under United States federal income tax principles, will generally be taxable as ordinary income to U.S. shareholders and will not be entitled to a reduced rate of taxation. See "Taxation—Certain United States federal income tax consequences—Taxation of dividends."

Selected financial and operating data

The following tables present our selected historical financial and operating information as of and for the years ended December 31, 2004, 2003 and 2002 and as of and for the nine months ended September 30, 2005 and 2004. You should read this information in conjunction with our combined consolidated financial statements and related notes included elsewhere in this offering memorandum, and the information under "Presentation of financial information" and "Management's discussion and analysis of financial condition and results of operations." Our financial statements and the information set forth below were prepared in accordance with Brazilian GAAP, which differs in significant respects from U.S. GAAP.

Although BDO Trevison Auditores Independentes have our auditors since 2004, the selected consolidated financial information as of and for the years ended December 31, 2004, 2003 and 2002 was derived from our audited consolidated financial statements included elsewhere in this offering memorandum which were prepared and audited by Deloitte Touche Tohmatsu Auditores Independentes specifically for the purpose of inclusion in this offering memorandum. In addition, the selected consolidated financial information as of and for the nine months ended September 30, 2005 and 2004 was derived from our unaudited consolidated financial statements also included elsewhere in this offering memorandum which were prepared specifically for the purpose of inclusion in this offering memorandum and were subject to a limited review by Deloitte Touche Tohmatsu Auditores Independentes. In the opinion of our management, our unaudited consolidated financial statements include all adjustments necessary to reflect a fair presentation of our results and financial condition for such periods. Our results of operations for the nine months ended September 30, 2005 are not necessarily indicative of the results that you should expect for the entire fiscal year ending December 31, 2005 or for any other period. Our consolidated financial statements include the proportional consolidation of our participation in Itasa.

The opinion of our auditors on our financial statements included in the offering memorandum includes a disclosure stating that we, based on our internal future cash flow projections, discounted to present value, estimated that certain thermoelectric assets would not be recovered with our future operations. Our management understands that these assets together with the rest of our operational assets will produce positive future cash flows.

This offering memorandum contains translations of various *real* amounts into U.S. dollars at specified rates solely for your convenience. You should not construe these translations as representations by us that the *real* amount actually represent these U.S. dollar amounts or could be converted into U.S. dollars at the rates indicated. Unless otherwise indicated, we have translated the *real* amounts for the year ended December 31, 2004 and for the nine months ended September 30, 2005 using a rate of R$2.2222 to US$1.00, the selling rate as of September 30, 2005, as published by the Central Bank. See "Exchange rates."

Selected financial and operating data

Income Statement Data	Nine months ended September 30,			Year ended December 31,			
	2005[1]	2005[1]	2004[1]	2004[1]	2004	2003	2002
	(US$ millions)	(R$ millions, except per share data)		(US$ millions)	(R$ millions, except per share data)		
Gross operating revenues	986.4	2,192.0	1,985.6	1,197.8	2,661.8	1,952.8	1,437.1
Deductions from operating revenues	(104.4)	(231.9)	(132.6)	(86.4)	(191.9)	(121.9)	(61.9)
Net sales and services	882.1	1,960.1	1,853.0	1,111.5	2,469.9	1,830.9	1,375.2
Costs of electricity and services	(357.1)	(793.6)	(820.0)	(495.9)	(1,101.9)	(879.6)	(866.2)
Gross profit	524.9	1,166.5	1,033.0	615.6	1,368.0	951.3	509.0
Operating expenses	(108.0)	(240.1)	(239.9)	(144.3)	(320.7)	(250.8)	(126.7)
Service income	416.9	926.4	793.1	471.3	1,047.3	700.5	382.3
Income from interests held in other companies	(2.3)	(5.1)	(5.1)	(3.0)	(6.7)	(7.0)	(2.2)
Net expenses	(30.8)	(68.4)	(148.7)	(79.5)	(176.6)	(35.7)	(723.1)
Operating income (loss)	383.8	852.9	639.3	388.8	864.0	657.8	(343.0)
Non-operating income	1.6	3.5	(2.6)	(1.4)	(3.0)	2.7	(2.7)
Income (loss) before taxes	385.4	856.4	636.7	387.5	861.0	660.5	(345.7)
Income and social contribution taxes	(70.4)	(156.4)	(102.8)	(38.6)	(85.8)	(143.4)	162.2
Net income (loss)	315.0	700.0	533.9	348.8	775.2	517.1	(183.5)
Net income (loss) per share (R$)[2]	0.4826	1.0725	0.8179	0.5344	1.1876	0.7923	(0.2812)

(1) Unaudited.

(2) For 2005, presents net income per share while for all other periods presents net income per 1,000 shares. On May 23, 2005, we consummated a reverse stock split whereby our shareholders received one common share for each 1,000 shares previously outstanding.

Balance Sheet Data	Nine months ended September 30,			Year ended December 31,			
	2005[1]	2005[1]	2004[1]	2004[1]	2004	2003	2002
	(US$ millions)	(R$ millions)		(US$ millions)	(R$ millions)		
Total current assets	462.7	1,028.2	1,119.0	537.0	1,193.4	925.0	1,456.2
Cash and banks	239.0	531.0	574.2	288.9	642.0	347.0	361.1
Total long-term assets	182.1	404.6	340.1	167.3	371.7	338.5	313.7
Total permanent assets	2,016.5	4,481.1	4,690.2	2,088.0	4,640.0	4,868.8	5,008.5
Total assets	2,661.3	5,913.9	6,149.3	2,792.3	6,205.1	6,132.3	6,778.4
Total current liabilities	289.6	643.5	669.7	555.0	1,233.3	1,054.4	1,122.6
Short-term debt	124.2	275.9	323.8	135.5	301.0	279.7	524.0
Total long-term liabilities	852.0	1,893.4	2,343.9	983.2	2,184.9	2,476.1	2,895.5
Long-term debt	588.7	1,308.2	1,852.8	761.9	1,693.0	2,025.5	2,430.7
Shareholders' equity	1,519.7	3,377.0	3,135.7	1,254.1	2,786.9	2,601.8	2,760.3
Total liabilities and shareholders' equity	2,661.3	5,913.9	6,149.3	2,792.3	6,205.1	6,132.3	6,778.4

(1) Unaudited.

Selected financial and operating data

EBITDA[1]	Nine months ended September 30,			Year ended December 31,			
	2005[2]	2005[2]	2004[2]	2004[2]	2004	2003	2002
	(US$ millions)	(R$ millions)		(US$ millions)	(R$ millions)		
Net income (loss)	315.0	700.0	533.9	348.8	775.2	517.1	(183.5)
Social contribution and income tax	70.4	156.4	102.8	38.6	85.8	143.4	(162.2)
Non-operating income	(1.6)	(3.5)	2.6	1.4	3.0	(2.7)	2.7
Financial income	30.8	68.4	148.7	79.5	176.6	35.7	723.1
Depreciation/amortization	72.5	161.0	161.8	103.6	230.3	234.7	192.2
EBITDA[1]	487.0	1,082.3	949.8	571.9	1,270.9	928.2	572.3

(1) We calculate EBITDA by adding back net financial expenses, depreciation and amortization, non-operating results, amortization of goodwill, and income and social contribution taxes to our net income (loss). EBITDA is not measured recognized under Brazilian GAAP, and it does not represent cash flow for the periods indicated. EBITDA should not be deemed as a substitute for net income or as an indicator of operating performance, cash flow or liquidity. EBITDA does not have standardized meanings and our definition of EBITDA may not be comparable to the EBITDA utilized by other companies.

(2) Unaudited.

Operating Data	Nine months ended September 30,		Year ended December 31,		
	2005	2004	2004	2003	2002
Installed capacity (GW)	5.8	5.8	5.8	5.8	5.8
Assured energy (GW)	3.2	3.2	3.2	3.2	3.1
Energy sold (GWh)	22,354.3	22,072.5	29,440.2	24,327.0	25,417.1
Initial contracts	4,633.1	9,291.7	12,432.8	18,561.0	24,771.9
Bilateral contracts	17,721.2	12,780.8	17,007.4	5,766.0	645.2
Purchased energy (GWh)[1]	1,882.3	341.1	359.7	—	193.3

(1) Operating data presented on a consolidated basis, and therefore, amounts of purchased energy between us and our consolidated subsidiaries are not considered.

Management's discussion and analysis of financial condition and results of operations

The following discussion and analysis of our financial condition and results of operations should be read together with the audited consolidated balance sheets as of December 31, 2004 and 2003, and the consolidated statements of income, changes in shareholders' equity (company) and changes in financial position for the years ended December 31, 2004, 2003 and 2002 and our unaudited consolidated balance sheet as of September 30, 2005 and the consolidated statements of income for the nine months ended September 30, 2005 and 2004, prepared by our management for the specific purpose of inclusion in this offering memorandum. Our consolidated financial statements contained in this offering memorandum were prepared in accordance with the Brazilian GAAP which differs in significant respects from U.S. GAAP. The financial information regarding our company refers to the consolidated financial information of our company and its subsidiaries.

Introduction

According to data published by ANEEL, as of September 30, 2005, we were the largest private electricity generator of Brazil in terms of installed capacity and assured energy. We hold concessions to use state-owned assets and we are authorized to explore the potential of hydroelectric power and implement and operate thermoelectric plants, and to sell the electricity we produce. We operate an electricity generation complex comprising six hydroelectric plants and seven thermoelectric plants. We own 11 of those plants entirely. The other two we own partially, and they are operated by the consortia in which we participate. As of September 30, 2005, we had installed capacity of 5,860 MW and assured energy of 3,172 MW. Our energy generation capacity including energy contracted through purchase agreements is 5,968 MW. In 2004, we had net revenues of R$2,469.9 million, EBITDA of R$1,270.9 million, and net income of R$775.2 million, of which R$774.8 million was from generation and R$0.4 million from trading activities. For the nine months ended September 30, 2005, we had net revenues of R$1,960.1 million, EBITDA of R$1,082.3 million and net income of R$700.0 million.

We have four subsidiaries, of which we fully own three (CEM, Lages Biogenética, and Tractebel Energia Comercializadora). In addition, we own 48.75% of the voting capital stock of Itá Energética S.A., or Itasa. For the nine months ended September 30, 2005, we generated 21,583 MW of electricity, of which 81.5% was generated by our hydroelectric plants and 18.5% by our thermoelectric plants.

Our results of operations are mainly affected by the following factors: (i) Brazilian economic growth; (ii) availability of hydro resources to generate electricity in Brazil; (iii) adjustments to the energy prices we charge distribution companies, traders, and independent consumers with which we have energy purchase and sale agreements; and (iv) duration and types of supply contracts (*i.e.*, whether with independent consumers, traders or distribution companies, through initial contracts or bilateral contracts).

Overview

Installed capacity and assured energy (hydroelectric plants)

Pursuant to Brazilian regulation, the revenue of hydroelectric power generators arising from the sale of electricity is not calculated by reference to the amount of energy actually generated or its installed capacity, but rather on the assured energy approved for sale for each power plant, which is regulated by the concession authority through the respective concession contracts. The difference between the energy actually generated and the assured energy is adjusted by the Energy Reallocation Mechanism, which we refer to as MRE, whose main purpose is to mitigate hydrological risks, assuring that each participating power plant is compensated up to its assured energy level, regardless of the electricity

actually generated. A plant's actual generation is regulated by the ONS, by reference to energy demand and prevailing hydrological conditions. The price for assured energy generated by power plants is fixed at a rate called ''Energy Optimization Rate (TEO),'' which covers only the operating and maintenance costs of the power plant. The revenue or expense generated by the TEO, corresponding to the surplus or shortage of energy actually generated and a plant's assured energy, is recorded monthly for each power generator. For more information on power generators and MRE compensation, see ''The Brazilian power industry.''

Installed capacity and physical reserve (thermoelectric plants)

As is the case with energy generated by hydroelectric plants, revenues from thermoelectric plants arising from the sale of electricity do not depend on their installed capacity but on the physical generation reserve of each power plant, as regulated by ANEEL. In addition, thermoelectric plants contract energy equivalent to their generation reserve through agreements for the purchase and sale of electricity that are freely negotiated between the generation company and other companies in the sector, except for contracts with distribution companies, since such companies generally acquire energy in auctions held by ANEEL and carried out through CCEE. In practice, the thermoelectric plants can deliver the allocated energy by either generating or purchasing energy in the spot market (CCEE) that varies depending on the generating costs and the spot market price for electricity, and on hydrological conditions. Accordingly, net income from a thermoelectric plant will be based on the difference between the fixed energy price and (i) its generation cost; or (ii) price of electricity on the spot market. If a thermoelectric plant generates energy in excess of its generation reserve because of an ONS ruling, the price of such surplus energy is set at the CCEE's spot price.

On November 18, 2004, the MME enacted Ordinance No. 303, establishing a new methodology to calculate the reserve of thermoelectric plants in order to conform the assured energy of the system (global supply of energy) to a criterion that guarantees that electricity supply does not exceed a deficit risk of 5%. As a result, the maximum volume of electricity we can contract to sell from our thermoelectric plants will be to effectively reduced from 984.8 MW (our current gross contract limit, not taking account of internal consumption of such plants and losses in the transmission system), to 852.8 MW which is the new limit, in gross amount, to be effective as of 2008. We do not currently consider the impact of this reduction on our future results to be material and have taken account of this decrease in our current business projections.

Sale of electricity

We generate revenue from the sale of electricity to distribution companies, traders and independent consumers by means of sales agreements of short, medium and long-term duration. We believe that our long-term agreements provide us stable cash flows and allow us to plan on a long-term basis. Our sales revenue grew by 41.7% from 2002 to 2003, from R$1,209.9 million to R$1,714.5 million and by 37.6% from 2003 to 2004, from R$1,714.5 million to R$2,358.7 million. For the nine months ended September 30, 2004 we had revenue of R$1,775.5 million, compared to R$1,921.8 million as of September 30, 2005. For the nine months ended September 30, 2005, our energy sales revenue derived from the following client categories: 52.3% distribution companies, 23.4% traders, 21.2% independent consumers and 3.1% from exports.

Distribution companies

Our sales to distribution companies increased from 198 GWh in 2002 to 2,642 GWh in 2003, and to 6,951 GWh in 2004, and for the nine-month period ended September 2004 our sales to distribution companies totaled 5,410 GWh, as compared to 7,061 GWh as of September 30, 2005, which represented 31.6% of our total electricity sold.

In 2003, initial contracts with distribution companies accounted for 18,561 GWh or 76.3% of our electricity sales, compared to 12,433 GWh or 44% of our electricity sales in 2004. For the nine months ended September 30, 2004, initial contracts accounted for 9,292 GWh or 42.1% of our electricity sales. For the nine months ended September 30, 2005, initial contracts accounted for 4,633 GWh or 20.7% of our total electricity sales in the period and 39.6% of our electricity sales to distribution companies in the same period. After the end of the initial contracts on December 31, 2005, we will have the possibility to sell all of our energy in the free market.

Traders
We did not have any supply agreements with traders until 2003, when we recorded sales to traders of 807 GWh, increasing to 4,558 GWh in 2004 and representing approximately 15.5% of the total electricity we sold in that year. As of September 30, 2005, our sales to traders amounted to 5,234 GWh, representing approximately 24% of our total sales of electricity.

Independent consumers
In order to stimulate competition in the electricity market, the Brazilian government made modifications to the regulation of the energy industry so that certain consumers may leave the distribution companies' consumer base, and, consequently, not be bound to regulated rates, thus becoming independent consumers, with the right to purchase electricity from other suppliers. In 2003, independent consumers represented 9.5% of our sales of electricity, with sales of approximately 2,317 GWh and gross sales of R$237.6 million. These sales represented approximately 13.9% of our total sales of electricity in 2004. In 2004 we sold approximately 4,448 GWh of electricity (representing 15.1% of our sales) to independent consumers representing gross revenue of R$372.8 million. For the nine months ended September 30, 2005, we had sold to these customers approximately 4,728 GWh of electricity, representing 22% of the total electricity we sold. For the nine months ended September 30, 2005, we had R$343.6 million representing 17.9% in gross revenue from sales to independent consumers. We currently have more than 100 independent consumers, including manufacturing companies from the pulp and paper, fertilizing, industrial gas, petrochemical, automobile and food industries.

2005 market overview
For 2005, we have contracted 6,189 GWh of electricity pursuant to initial contracts with distribution companies, 9,546 GWh through bilateral contracts with distribution companies, 7,219 GWh with traders, 678 GWh through exports and 6,521 GWh with independent consumers, representing a total of 30,153 GWh.

The chart below shows the average remaining term of agreements for purchase and sale of electricity that we have entered into as of September 30, 2005, based on our client categories:

	At September 30, 2005
Initial contracts (distribution companies)	3 months
Bilateral contracts:	
Distribution companies	5.1 years
Traders	4.5 years
Independent consumers	3.0 years

Of the 6,189 GWh that is currently contracted with distribution companies by means of initial contracts under the regulated market, 100% has already been reallocated for periods after December 2005 under the free market.

Changes in the General Market Price Index, or IGP-M have a significant impact on our revenues. In general, all revenue we earn is adjusted by the IGP-M, as our initial contracts and bilateral contracts are adjusted by such index, except for contracts executed in the regulated market auctions that are adjusted by IPCA. Likewise, our costs, including payroll, are adjusted by the National Consumer Price Index, or INPC, which also changes based on inflation and on the same basis as the IGP-M and IPCA.

The Brazilian economy

Since our operations and activities are conducted in Brazil our business is affected by the country's economy. Brazilian economic performance particularly affects demand for electricity, while inflation affects our costs and margins. According to the Brazilian Institute of Geography and Statistics, or IBGE, in 2004 the Brazilian economy grew at the fastest pace in the latest 10 years reaching 5.2% GDP growth compared to 2003. The GDP started to recover in 2003 mostly as a result of increased exports, employment and income rates. Formal employment increased with the creation of approximately 1.9 million jobs and resulted in increased demand for goods and services.

In 2004, inflation of 7.6% as measured by the Amplified Consumer Price Index (*Índice de Preços ao Consumidor Amplo*), or IPCA, estimated by IBGE, decreased as compared to 2003. In 2005, the Central Bank set an inflation goal of 5.1%. In September 2004, interest rates started to increase and by the end of that year, the base interest rate (SELIC) was at 17.75% per year. As of September 30, 2005, SELIC was fixed at 19.50% per year.

In 2005, economic development in Brazil will be influenced by continued growth of the global economy, tax adjustment, exports, and foreign investments. In 2004, such adjustments increased the primary surplus (*superávit primário*) from 4.25% to 4.5% of GDP. These factors together with the appreciation of *real* in relation to foreign currencies caused the public debt to decrease in relation to GDP—from 58.3% in the end of 2003 to 51.8% in December 2004. The Central Bank also decreased the basic interest rates (*juros básicos*). All these factors caused the 12-month cumulative public deficit to represent less than 3.0% of the GDP for the first time since the beginning of Plano Real in 1994.

In 2004, exports and foreign investments caused a significant current account surplus by more than US$10.0 billion (2% of GDP), which enabled the foreign debt to fall in relation to exports multiples, from 3 to less than 2, thus improving slightly the sensitivity to risk in the Brazilian economy.

The table below shows selected economic indicators for the periods presented.

	September 30, 2005[7]	December 31, 2004	2003	2002
Inflation (IGPM)[1]	0.2%	12.4%	8.7%	25.3%
Inflation (INPC)[2]	3.5%	6.1%	10.3%	14.7%
Inflation (IPCA)[3]	4.0%	7.6%	9.3%	12.5%
SELIC rate[4]	19.5%	16.2%	23.3%	19.2%
Our average price increase[5]	14.9%	16.2%	34.9%	14.5%
Actual GDP growth	3.4%	4.9%	0.5%	1.9%
Exchange rate at end of the period—R$/US$[6]	2.2222	2.6544	2.8892	3.5333
Annual average exchange rate—R$/US$[6]	2.4938	2.9171	3.0600	2.9983
Devaluation (appreciation) of real against dollar	(16.28)%	(8.8)%	(22.3)%	34.3%

(1) IGP-M is the market general price index estimated by Fundação Getúlio Vargas.

(2) INPC—National Consumer Price Index.

(3) IPCA is a broad consumer price index estimated by the Brazilian Institute of Geography and Statistics.

(4) Central Bank—actual monthly annualized SELIC rate.

(5) Average price increase in the year in relation to the previous year.

(6) Central Bank—PTAX rate of sales.

(7) Period information, not annualized.

Energy rationing and related regulatory measures

In the years that preceded 2001, the water supply was extremely low because of unusually scarce rainfall and lack of investments in energy generation in Brazil. As a result, the energy supply was low in most of Brazil. These facts had an adverse impact on the Brazilian electricity sector and in the financial condition of distribution companies and power generators, including us. By the end of 2001 and beginning of 2002, the distribution companies and power generators agreed with the Brazilian government to implement a set of measures, collectively known as the "General Agreement on the Electricity Industry", aimed at reestablishing the financial balance of existing agreements and restoring revenues from the levels during the rationing period.

In summary, the General Agreement on the Electricity Industry listed the losses of each participant in the electricity industry, provided for the *recomposição tarifária extraordinária* (RTE) charged from end consumers of electricity in order to adjust the apportionment of losses of such participants during the rationing period, and granted financing secured by RTE to those participants.

RTE will remain in effect until the losses incurred by the industry participants are fully recovered, which is expected to occur by 2011. As of December 31, 2004 and September 30, 2005, we recorded free energy receivables amounting to R$22.6 million and R$15.0 million, respectively. According to applicable legislation, the free energy balances are adjusted by the SELIC variation plus interest of 1% per year. Because of uncertainties with respect to the full payment of free energy balances, we have not recorded the adjustment to free energy balances of R$18.7 million that would be due to us through September 30, 2005.

Short term energy—CCEE

As of December 31, 2004, the balance due to us from consumers, concessionaires and permission holders included amounts arising from short-term energy trading of R$26.2 million, net of allowances for doubtful accounts of R$131.6 million (R$46.7 million as of December 31, 2003, net of allowances

for doubtful accounts of R$143.7 million), and payables of R$8.6 million, based on monthly calculations prepared and reported by CCEE. According to applicable regulation, short-term energy transactions that are not settled on the scheduled dates must be negotiated bilaterally between the market agents.

Short-term energy and free energy amounts arising from trading within the MAE during in period from September 1, 2000 to December 31, 2002 was subject to changes based on lawsuits in progress. These lawsuits were filed by certain companies in the industry, located in the southern region of Brazil, to challenge the market rules that were in effect for the period. These companies, which were not subject to rationing, obtained a preliminary order to annul ANEEL Decree No. 288 of May 16, 2002 that provided for clarification to the industry's companies on the treatment and application of certain recording rules of the MAE (the predecessor of CCEE), included in the General Agreement on the Electricity Industry.

These lawsuits involve, among other things, the trading of the Itaipu quota in the Southeast/ Center-West regional market, specially during the 2001 rationing period, when there was a significant difference in short-term energy prices between the two regional markets. The original amount due to us that is under judicial review related to such period was R$143.6 million (sales, net of purchase and system service charges). Of this amount, net receivables of R$24.0 million and R$31.1 million were repaid in installments until December 31, 2004 and September 30, 2005, respectively. In view of the uncertainty of collecting on these receivables arising, we established an allowance for doubtful accounts corresponding to the total amount of receivables from the short-term energy trading that is subject to judicial review, which balance as of December 31, 2004 and September 30, 2005 amounted to R$119.6 million and R$110.5 million, respectively.

As of December 31, 2004 and September 30, 2005, we also had an allowance for doubtful accounts amounting to R$12.0 million, relating to potential default from agent receivables.

Presentation of consolidated financial statements

Introduction

Our consolidated financial statements were prepared and are presented in accordance with Brazilian GAAP. We prepare our consolidated financial statements reflecting the financial results of our controlled subsidiaries. We eliminate investments in subsidiaries, as well as the balance of assets and liabilities and the revenues and expenses relating to transactions between our consolidated companies. The assets and liabilities, revenues and expenses of Itasa are consolidated in proportion to our holding of its capital stock. Since our other subsidiaries are essentially wholly-owned subsidiaries, there was no effect in relation to minority shareholdings on our consolidated financial statements.

Principal accounting practices

Current and long-term assets

Securities are recorded at cost plus income earned to the balance sheet date. Book values are adjusted by the recording of a provision when they exceed their respective average market prices. The allowance for doubtful accounts is associated to receivables arising from transactions carried out within the MAE. Other account receivables are backed by collateral or have not recorded previous losses, so no corresponding provision is established.

Deferred income tax and social contribution (deferred tax credits) are calculated at the rates in effect on the balance sheet date of 25% and 9%, respectively, and are recognized based on tax losses and temporary differences. Segregation between current and long-term assets is made in accordance with our expected recovery of the related receivable.

Inventories are recorded at their weighted average cost of acquisition, which does not exceed their market value. Indexed assets are adjusted to the balance sheet date.

Permanent Assets

Investments in fully and jointly controlled subsidiaries are accounted for by the equity method, and other investments are recognized at their cost of acquisition, not exceeding their market value.

Property, plant and equipment are recorded at acquisition or construction cost. Depreciation is calculated using the straight line method based on the annual rates included in the table attached to ANEEL Resolutions No. 2, dated December 24, 1997, and No. 44, dated March 17, 1999, based on the account balances recorded in the Registration Units (UC) comprising the business ventures, as provided for by DNAEE No. 815 dated November 30, 1994.

Interest and other financial charges and the effects of inflation arising from financing obtained from third parties that are invested in construction in progress are calculated at cost of the respective fixed asset.

Current and long-term liabilities

Future benefits to employees (retirement benefits) are recorded based on actuarial evaluation by the Projected Unit Credit Method, and adjusted monthly according to contractual indexes that are supplemented by amounts projected by actuarial evaluation. The amount of actuarial losses exceeding 10% of the present value of actuarial liabilities is paid annually on a straight line basis for the period corresponding to the average estimated term of employment for the employees that participate in the plan.

Reserves for contingencies are established based on the legal opinion of advisors relating to the possibility of unfavorable decisions in lawsuits.

Loans and financing, debenture funds and related charges are recorded through the balance sheet date, and adjusted by exchange or contractual rates, while other liabilities are recorded at known or estimated amounts, plus related charges and monetary adjustments, when applicable.

Income (loss) for the period

Income and expenses are recorded based on the accrual method of accounting.

Leasing

Our leasing transactions do not have significant amounts and are directly recorded in results based on contract installments.

Results of operations

Gross operating revenue

Our gross operating revenue consists of revenue earned from: (i) the sale of electricity to distributors, traders and independent consumers; (ii) fuel subsidies—CCC/CDE; (iii) provision of other services; (iv) sale of ash; and (v) other revenues. In 2004, approximately 14.0% of our gross operating revenue corresponded to the sale of electricity, of which 74.6% related to electricity supply, and 10.8% related to fuel subsidies—CCC/CDE. The Fossil Fuel Consumption (CCC/CDE) is a financial subsidy administered by Eletrobrás to cover the fuel cost used by thermoelectric power plants. The energy development account (CCC/CDE) was created by the Brazilian government as a substitute for the CCC in the provision of fuel cost subsidies to thermoelectric power plants that use national mineral coal.

Deductions from operating revenue

Deductions from operating revenue consist of the following: (i) taxes levied on operating revenue, such as value-added tax (ICMS), and social contribution taxes (PIS and COFINS), and (ii) revenues from the sale of ash, net of taxes, which funds are transferred to the CCC/CDE fund administrator, Eletrobrás. In 2004, 96.7% of the deductions from operating revenue related to taxes levied on

revenue while the remaining 3.3% to the sale of ash. We pay PIS and COFINS at the rates of 1.65% and 7.60%, respectively. In relation to ICMS, the rate varies by state, as shown in the table below:

State	Rates	Periodicity
Federal District	21.00%	Monthly
Goiás	29.00%	Monthly
Mato Grosso	30.00%	Monthly
Mato Grosso Do Sul	17.00%	Monthly
Minas Gerais	18.00%	Monthly
Paraná	27.00%	Monthly
Rio de Janeiro	25.00%	Monthly
Rio Grande do Sul	17.00%	Monthly
Santa Catarina	25.00%	Monthly
São Paulo	18.00%	Monthly

Cost of electricity and services

The cost of electricity and services consists of the following: (i) cost of electricity production (71.7% of total costs in 2004); (ii) cost of electricity purchased for resale (27.5% of total costs in 2004); and (iii) cost of services provided (0.8% of total costs in 2004). The breakdown of costs of electricity and services is presented in the table below:

Cost	Percentage	Adjustment mechanism
Fuel with CCC/CDE subsidies	32.6%	Mineral coal—the price is negotiated at the annual agreement for the fuel purchase.
Depreciation and amortization	25.4%	Rate established by ANEEL[(1)]
Fuel without subsidy	16.2%	— Gas consumption and transportation—price fixed in U.S. dollars, adjusted annually by the Producer Price Index (PPI) — Distributor margin—price fixed in *reais*, adjusted annually by the IGP-M — Monthly fixed cost to compensate the distribution system investment for five years from 2001—price fixed in *reais*, adjusted annually by the IGP-M — Additional charge—adjusted annually by the change in the *real*—U.S. dollar exchange rate — Mineral Coal—pre negotiated in the annual contract for acquisition of fuel
Personnel costs	8.2%	Collective Agreement—INP-C
Cost of materials and third-parties services	6.6%	IGP-M and INP-C
Financial compensation for hydro resources and public asset usage charges (UBP)	7.6%	IGP-M
Other production costs	3.4%	IGP-M and INP-C

(1) Subject to adjustments by ANEEL.

Operating expenses

Operating expenses comprise the following: (i) sales expenses (representing 41.6% of total operating expenses in 2004), composed principally of expenses related to electricity transmission; and (ii) general and administrative expenses (representing 58.4% of our total operating expenses in 2004), consisting primarily of personnel, third-party supplies, materials expenses and other expenses related to administrative activities. In addition, operating expenses are related to the increase in expenses from electricity grid usage charges, as a result of the increase in electricity available for sale through bilateral contracts while initial contracts, which do not incur transmission expenses, are being terminated.

Financial income (expense)

Financial income mainly originates from investment interest and net monetary variations. In 2004, approximately 70.6% of our financial income derived from financial investment yields, and 5.3% related to monetary variations.

Financial expenses mainly consist of interest and related charges on our debt and amounts due on the ANEEL concession, losses from exchange/interest rate swaps, and provision for financial investment losses. In 2004, 80.5% of our financial expenses related to interest and related charge on our outstanding debt of R$188.1 million, and ANEEL concession expenses of R$13.4 million. Of our financial expenses for 2004, 11.2% related to losses from exchange/interest rate swaps, 7.0% to provision for financial investment losses, and 1.3% to other net financial expenses from exchange income of R$3.2 million due to the appreciation of the real against foreign currencies.

Nine months ended September 30, 2005 compared to nine months ended September 30, 2004

Gross operating revenue

Our gross operating revenue increased 10.4%, from R$1,985.6 million for the nine months ended September 30, 2004 to R$2,192.0 million for the nine months ended September 30, 2005. This revenue increase resulted primarily from the following factors: (i) annual adjustments by IGP-M to most of our energy purchase and sale agreements, which represented an increase of R$207.9 million; (ii) the impact of the termination of 25% of the initial contracts, which meant that energy originally sold pursuant to initial contracts became available to be resold to distribution companies, traders and independent consumers under bilateral contracts at more advantageous prices, in addition to the signing of new bilateral contracts, which together represented an increase of R$73.2 million in our gross operating revenue; (iii) an increase in sales made through CCEE, which represented an increase of R$28.0 million in our gross operating revenue. These results were partially offset by a reduction in export of energy to Argentina and Uruguay in the nine months ended September 30, 2005 compared to the same period in 2004, representing a decrease of R$58.5 million in our gross operating revenue and termination of the contract with CBEE, which resulted in a decrease of R$53.8 million in our gross operating revenue.

Deductions from operating revenue

Our operating revenue deductions increased by 74.9%, from R$132.6 million for the nine months ended September 30, 2004 to R$231.9 million for the nine months ended September 30, 2005. Deductions accounted for 10.6% of gross operating revenue for the nine-month period ended September 30, 2005, as compared to 6.7% for the same period in 2004. This change resulted primarily from: (i) increased taxes payable due to higher gross operating revenue, excluding exports of energy which are not taxable; (ii) higher PIS and COFINS rates, of 3.65% and 9.25%, resulting in an increase of R$44.9 million in deductions from our gross operating revenue; and (iii) increase of the ICMS rate as it started to be levied on energy sale agreements to end consumers, which represented an increase of R$31.9 million in deductions.

Net operating revenue
Our net operating revenue increased 5.8%, from R$1,853.0 million for the nine months ended September 30, 2004 to R$1,960.1 million for the nine months ended September 30, 2005.

Cost of electricity and services
Our sales and services cost decreased by 3.3%, from R$820.0 million for the nine months ended September 30, 2004 to R$793.6 million for the nine months ended September 30, 2005. As a percentage of net revenue, such costs decreased to 40.5% during the nine months ended September 30, 2005, as compared to 44.3% during the nine-month period ended September 30, 2004. This change was mainly due to the following factors:

- a decrease of 47.6% in energy purchased for resale from R$245.9 million for the nine months ended September 30, 2004 to R$128.8 million for the nine months ended September 30, 2005, resulting mainly from the decrease in the purchase of energy on the CCEE (spot market/purchase from other generators) in the amount of R$39.3 million and the decrease in additional costs of energy that arose during the rationing period in 2001 that was amortised during the nine-months ending on September 30, 2004, in the amount of R$43.8 million, and reduction in energy available from CIEN corresponding to R$35.8 million, as a result of the adjustment imposed by ANEEL on electricity generated by the CIEN plant, from 300 MW to 72 MW, in the same period of 2005; and
- an increase of 15.9% in the production cost of electricity operated at thermoelectric plants, from R$567.7 million for the period ended September 30, 2004 to R$658.1 million for the period ended September 30, 2005, mainly due to the increase in the cost of mineral coal in the amount of R$63.6 million as a result of annual price adjustments.

General, administrative and sales expenses
Our general, administrative and sales expenses increased 0.1% from R$239.9 million for the nine months ended September 30, 2004 to R$240.1 million for the nine months ended September 30, 2005. In relation to net operating revenue, such expenses decreased to 12.2% as of September 30, 2005, as compared to 12.9% for the nine months ended September 30, 2004.

Financial income (expense)
Net financial expenses amounted to R$68.4 million in the nine months ended September 30, 2005, representing a decrease of R$80.3 million, or 54.0% over the comparable period of 2004. This result was caused mainly by the following:

- a 16.3% appreciation of the *real* against a basket of foreign currencies that represents the composition of our debt denominated in foreign currencies during the nine months ended September 30, 2005, compared to an appreciation of 1.1% during the nine months ended September 30, 2004, resulting in a net increase of R$146.8 million in our financial income; exchange rate variations resulting from the appreciation of the *real* against the U.S. dollar, which may be a non-recurring item, had a significant impact on the results for the periods ended September 30, 2005 and 2004. Consequently, the results for subsequent periods may not reflect a similar impact;
- financial expenses from hedge and swap transactions increased from R$1.1 million for the nine months ended September 30, 2004 to R$125.7 million for the nine months ended September 30, 2005, as a result of the contracting of exchange swaps to protect a portion of our debt denominated in foreign currency;
- financial expenses related to debt expenses decreased by 21.7%, from R$150.1 million for the nine months ended September 30, 2004 to R$117.5 million for the nine months ended

September 30, 2005 mainly because of early prepayment in May 2005 of our loan due to the Inter-American Development Bank; and

- increase of 20.6% in financial expenses related to concessions from R$9.7 million for the nine months ended September 30, 2004 to R$11.7 million for the nine months ended September 30, 2005.

In addition, due to higher balances of cash on hand, revenue from investments increased 69.9% from R$41.2 million for the nine months ended September 30, 2004 to R$70.0 million as of September 30, 2005.

Non-operating result
Our non-operating result was a non-operating expense for the nine months ended September 30, 2004 of R$2.6 million and a non-operating revenue of R$3.5 million for the nine months ended September 30, 2005 mainly as a result of our sale of Project Jacui to Eletrica Jacui S.A., or Eleja, in July 2005, which resulted in a net gain of R$4.8 million. The extraordinary results related to transactions involving the Jacui Project, including taxation effects, had a significant impact on the results for the nine months ended September 30, 2005 and 2004. As a non-recurring item, the results for subsequent periods may not reflect a similar impact.

Income and social contribution taxes
For the nine months ended September 30, 2005, our expenses for income and social contribution taxes increased by 52.1%, from R$102.8 million as of September 30, 2004 to R$156.4 million. The amount of income and social contribution taxes for the nine months ending September 30, 2004 represented 18.3% of our earnings before taxes compared to 16.1% for the comparable period of 2004. Our effective income tax rate is lower than the 34% corporate tax rate applicable in Brazil primarily because we have recognized income tax over provision for economic losses of the Jacui Project, upon its partial transfer to Eleja in June 2004 and July 2005, by 33.3% in each year. This provision was established in 1997, but we have only recognized the differed tax asset related to the social contribution, pending recognition in relation to income tax. By the partial transfer of the project and realization of part of the provision, there was a positive impact in our results in the nine months ended September 30, 2004 and 2005, in the amounts of R$112.6 million and R$93.6 million, respectively.

Income (loss) for the period
We had income of R$700.0 million for the nine months ended September 30, 2005, 31.1% higher than the R$533.9 million recorded in the comparable period of 2004. The margin over net operating revenue was 35.7% for the nine months ended September 30, 2005, as compared to 28.8% in the comparable period of 2004.

Our income for the nine months ended September 30, 2005 was R$1.0725 per share R$0.8179 per thousand shares in the comparable period of 2004.

EBITDA
The increase in income as well as the reduction in operating costs and expenses discussed above resulted in an EBITDA increase of 14.0% during the nine months ended September 30, 2005, as compared to the comparable period of 2004 to R$1,082.3 million from R$949.8 million for the nine months ended September 30, 2004. Our EBITDA margin was 55.2% for the nine months ended September 30, 2005, compared to 51.3% for the comparable period in 2004.

Year ended December 31, 2004 compared to year ended December 31, 2003

Gross operating revenue
Our gross operating revenue increased by 36.3%, from R$1,952.8 million for the year ended December 31, 2003 to R$2,661.8 million for the year ended December 31, 2004. This increase in gross operating revenue resulted primarily from the following factors: (i) annual IGP-M adjustments, as a general rule, to our energy purchase agreements, representing an increase of R$202.9 million; (ii) the impact of the termination of 25% of the initial contracts which meant that energy originally sold pursuant to initial contracts became available to be resold to distribution companies, traders and independent consumers under bilateral contracts at more advantageous prices, in addition to the signing of new bilateral contracts that accounted for R$350.0 million; (iii) electricity exports to Argentina and Uruguay amounting to R$130.3 million; and (iv) an increase in energy sales to CBEE due to price adjustment, which represented increased revenue of R$20.0 million; partially offset by (a) a decrease in the energy sale transactions within the CCEE, in line with the reduction in the non-allocated energy amounting to R$52.8 million; and (b) an increase in the CCC/CDE fuel subsidy due to the annual adjustment to the mineral coal price that represented an increase of R$59.3 million in our gross operating revenue.

Deductions from operating revenue
Our deductions from operating revenue increased by 57.5%, from R$121.9 million for the year ended December 31, 2003 to R$191.9 million for the year ended December 31, 2004. Deductions represented 6.2% of our gross operating revenue in 2003, as compared to 7.2% in 2004. This increase in deductions in 2004 resulted primarily from: (i) the increased taxes payable due to higher gross operating revenue, not considering energy exports which are not taxable; (ii) increase in the COFINS rate from 3.0% to 7.6% that started to be levied on energy sale agreements from their price adjustment dates, resulting in an increase of R$14.5 million in deductions from our gross operating revenue; and (iii) the increase in the ICMS rate mainly because of new energy sales agreements to consumers that represented an increase of R$29.5 million in deductions.

Net operating revenue
As a result of the foregoing, our net operating revenue increased by 34.9%, from R$1,830.9 million for the year ended December 31, 2003 to R$2,469.9 million for the year ended December 31, 2004.

Cost of electricity and services
Our cost of electricity sales and services increased by 25.3%, from R$879.6 million for the year ended December 31, 2003 to R$1,101.9 million for the year ended December 31, 2004. As a percentage of net revenue, such costs decreased to 44.6% for the year ended December 31, 2004, as compared to 48.0% for the year ended December 31, 2003. This change was mainly due to the following factors:

- cost of electricity purchased for resale increased 20.8%, from R$250.8 million for the year ended December 31, 2003 to R$302.9 million for the year ended December 31, 2004, mainly due to: (a) the acquisition of energy from third parties in order to meet energy exports to Argentina and Uruguay in the amount of R$25.8 million; (b) energy purchased through the CCEE in the amount of R$45.2 million; and (c) reduction in the cost of energy purchased by the PIS/COFINS credit on acquisition of electricity, which represented an increase of R$17.7 million; and
- cost of electricity production increased by 27.2%, from R$621.6 million for the year ended December 31, 2003 to R$790.5 million for the year ended December 31, 2004, mainly due to: (a) an increase in the mineral coal with subsidy of R$52.4 million as a result of annual price adjustments; (b) an increase in the cost of gas of R$6.3 million, and (c) price adjustments and

higher mineral coal consumption without subsidy in the amount of R$53.3 million, to meet electricity exports to Argentina and Uruguay.

General, administrative and sales expenses
The following table sets forth, for the periods indicated, details of general and administrative and sales expenses and the percentage change of each component:

	December 31,		
	2004	2003	Change (%)
	(R$ millions)		
General and administrative expenses:			
Recurring expenses	122.6	107.5	14.0
Recording (reversal) of provision for contingencies, net	64.7	(71.7)	—
Subtotal	187.3	35.8	423.2
Sales expenses:			
Recurring expenses	145.5	71.3	104.1
Recording (reversal) of allowance for doubtful accounts, net	(12.1)	143.7	—
Subtotal	133.4	215.0	(38.0)
Total	320.7	250.8	27.9

Our general, administrative and selling expenses increased by 27.9%, from R$250.8 million for the year ended December 31, 2003 to R$320.7 million for the year ended December 31, 2004, primarily as a result of the following factors:

➢ General and administrative expenses

- Recurring expenses: increase in personnel expenses of 21.4% or R$7.0 million, due primarily to the annual salary adjustment amounting to R$4.4 million, and the payment of profit share, in 2004, relating to 2003 of R$2.6 million.
- Recording (reversal) of provision for contingencies as follows:
  - R$64.7 million, in 2004, relates primarily to the following: (i) recording of a provision for losses on the recovery of the ICMS accumulated credit related to the acquisition of natural gas for the production of electricity in the William Arjona thermoelectric plant due to the fact that the electricity sale is carried out with the deferral of ICMS thus making it impossible to recover all credits; and (ii) recognition of additional provisions for tax, civil and retirement benefit contingencies; and
  - R$71.7 million, in 2003, related to the reversal of provision mainly as a result of the judicial decision in our favor relating to the payment of PIS/COFIS taxes on Itaipu energy transmission, and the favorable settlement of CSSL debt installments without the imposition of any fines and cancellation of interest due on that debt that was in arrears.

➢ Sales expenses

- Recurring expenses: increase resulting from grid usage charges in the amount of R$73.2 million, as a result of the increase in electricity sold through bilateral contracts (which incur such charge) while initial contracts, which do not incur transmission charges, are being terminated;
- Recording (reversal) of allowance for doubtful accounts as follows:
  - R$12.1 million, in 2004, relates to the reversal of the allowance for doubtful accounts, due to the agreement by certain MAE agents, that had previously disagreed with certain amounts

calculated by MAE, of amounts due during the energy rationing period (June 2001 to February 2002); and

- R$143.7 million, in 2003, relates to the allowance for doubtful accounts due to the lawsuit filed by MAE agents challenging certain amounts that were calculated as being due to us during the energy rationing period (June 2001 to February).

Financial income (expense)
Our net financial expense was R$176.6 million for the year ended December 31, 2004, representing an increase of R$140.9 million, or 394.7% compared to 2003, which totaled R$35.7 million. This increase was mainly due to the following factors:

- an 18.2% appreciation of the real against the dollar in 2003, compared to appreciation of 8.1% in 2004, resulting in a decrease of R$167.8 million in financial income;
- an increase in financial expense from exchange and interest rate swap transactions from R$1.7 million for the year ended December 31, 2003 to R$28.1 million in 2004 principally due to expenses resulting from a deficit of R$26.7 million in exchange rate swap transactions entered into in 2004 to hedge a portion of our foreign currency denominated liabilities;
- financial expense from debt interest charges decreased by 17.0%, from R$226.5 million for the year ended December 31, 2003 to R$188.1 million for the year ended December 31, 2004, as a result of the repayment of loans in 2004;
- increase of 30% in financial expense related to concession interest charges, from R$10.3 million for the year ended December 31, 2003 to R$13.4 million for the year ended December 31, 2004; and
- provision for losses in deposits with Banco Santo amounting to R$17.4 million as of December 31, 2004, as a result of the Central Bank intervention in that institution.

In addition, reduced cash balances caused financial investment income to decrease by 18.8%, from R$64.2 million in 2003 to R$52.1 million in 2004.

Non-operating result
Our non-operating result generated income of R$2.7 million for the year ended December 31, 2003 compared to an expense of R$3.0 million as of December 31, 2004. In 2004, we transferred 33.3% of our interest in Jacuí to Electrica Jacuí S.A.—Eleja, for R$29.0 million. The net book value corresponding to the 33.3% that was transferred in the transaction totaled R$27.8 million, resulting in a net gain of R$1.2 million.

In 2004 we also wrote-off obsolete assets related to the Jacuí facility as non-operating expense of R$1.0 million, based on an independent appraisal from specialized companies.

Income and social contribution taxes
Our income and social contribution taxes decreased by 40.1%, from R$143.3 million for the year ended December 31, 2003 to R$85.8 million for the year ended December 31, 2004. The effective income and social contribution tax rate for the year ended December 31, 2004 was 10.0% compared to 21.7% in 2003. This decrease in our effective tax rate was mainly a result of the recording of the losses for income tax purposes generated by the Jacuí facility, which was partially (33.3%) transferred to Eleja, as mentioned above. Such provision was established in 1997 but only the deferred tax credit related to the social contribution was recognized in prior years and, therefore, the amount related to income tax was pending. After the partial transfer of this venture and subsequent realization of a portion of the provision, a credit was recorded in our results of operations for 2004 amounting to R$112.6 million.

Income (loss) for the period
In the year ended 2004, we recorded net income of R$775.2 million, 49.9% higher than the R$517.2 million recorded in 2003. Our net operating margin was 31.4% in 2004, compared to 28.2% in 2003. Our net income per thousand shares for the years ended December 31, 2004 and 2003 were R$1.1876 and R$0.7923, respectively.

EBITDA
The increase recorded in income exceeded the growth in operating costs and expenses discussed above resulting in an increase in our EBITDA of 36.9% or R$342.7 million in 2004, compared to 2003. In 2004, EBITDA totaled R$1,270.9 million, compared to R$928.2 million in 2003. EBITDA margin was 51.5% in 2004, compared to 50.7% in 2003.

Year ended December 31, 2003 compared to year ended December 31, 2002

Gross operating revenue
Our gross operating revenue increased by 35.9%, from R$1,437.1 million for the year ended December 31, 2002 to R$1,952.8 million for 2003. This increase in gross operating revenue resulted primarily from the following factors: (i) the electricity sold under initial contracts and bilateral contracts were adjusted by IGP-M, as a general rule, representing an increase of R$290.9 million; (ii) the electricity originally sold under initial contracts became available to be resold to distribution companies, traders and independent consumers under bilateral contracts at prices more advantageous us, representing an increase of R$80.9 million, (iii) increase in the electricity sale within the MAE, as a result of availability of non-allocated energy, representing an increase of R$106.1 million; and (iv) energy sale within the CBEE as from May 2002, representing an increase of R$34.1 million. These increases in 2003 were partially offset by a non-recurring adjustment to electricity sales prices, representing an increase of R$56.6 million in gross operating revenue in 2002 and by a reduction in sales of electricity in 2003 as compared to 2002, resulting in a decrease of R$59.6 million in gross operating revenue.

Deductions from operating revenue
Our deductions from operating revenue increased by 96.9%, from R$61.9 million for the year ended December 31, 2002 to R$121.9 million for the year ended December 31, 2003. Deductions represented 6.2% of gross operating revenue in 2003, as compared to 4.3% in 2002. This increase in deductions in 2003 was mainly a result of the following: (i) increased taxes payable in 2003 as a result of the increase in gross operating revenue; (ii) 1.0% increase in the PIS rate as from December 2002, representing an increase of R$22.6 million in deductions from gross operating revenue in 2003; and (iii) increase in the ICMS levied on energy sales to consumers arising from new agreements entered into in 2003 that represented an increase of R$10.8 million in deductions from gross operating revenue.

Net operating revenue
As a result of the foregoing, our net operating revenue increased by 33.1%, from R$1,375.3 million for the year ended December 31, 2002 to R$1,830.9 million for the year ended December 31, 2003.

Cost of electricity and services
Our cost of electricity and services increased by 1.5%, from R$866.2 million for the year ended December 31, 2002 to R$879.6 million for the period ended December 31, 2003. As a percentage of net revenue, these costs decreased to 48.0% for the year ended December 31, 2003, as compared to

63.0% for the year ended December 31, 2002. This change was principally due to the following factors:

- electricity purchased for resale increased by 71.5%, from R$146.2 million for the year ended on December 31, 2002 to R$250.8 million for the year ended December 31, 2003 due primarily to the additional cost as result of the effects (exposure in the spot market—MAE) in the rationing period (June 2001 to February 2002) and the increase in transactions carried out in the spot market (MAE) amounting to R$99.0 million.
- cost of electricity decreased 12.9%, from R$713.3 million for the period ended December 31, 2002 to R$621.6 million for the period ended December 31, 2003, mainly due to the reversal of a provision for electricity purchased during the rationing period amounting to R$61.5 million, as a result of the recognition of electricity purchased for resale referred to above.

General, administrative and sales expenses
The following table sets forth, for the periods indicated, details of general, administrative and sales expenses and the percentage change of each component:

	Year ended December 31,		
	2003	2002	Change (%)
	(R$ millions)		
General and administrative expenses:			
Recurring expenses	107.5	96.8	11.1
Recording (reversal) of provision for contingencies, net	(71.7)	0.7	—
Subtotal	35.8	97.5	(63.3)
Sales expenses:			
Recurring expenses	71.3	29.2	144.2
Recording of allowance for doubtful accounts	143.7	—	—
Subtotal	215.0	29.2	636.3
Total	250.8	126.7	97.9

Our general, administrative and sales expenses increased by 97.9%, from R$126.7 million for the year ended December 31, 2002 to R$250.8 million for the year ended December 31, 2003. In relation to net revenue, such expenses increased to 13.7% for the year ended December 31, 2003, as compared to 9.2% for the year ended December 31, 2002. This increase was primarily due to the following factors:

- increased general and administrative expenses due to increases in personnel and third-party service expenses;
- increased selling expenses due to increases in expenses from electrical grid usage charges, from R$20.2 million in 2002 to R$61.7 million in 2003, as a result of the increase in the amount of electricity available for sale through bilateral contracts while initial contracts, which do not incur transmission charges, are being terminated (25% in 2003); and
- the net effect of the reversal of the provision for contingencies and allowance for doubtful accounts recognized in 2003.

Financial income (expense)
Our net financial expenses decreased by 95.1%, from R$723.1 million for the year ended December 31, 2002 to R$35.6 million for 2003. This reduction resulted primarily from the depreciation of the *real* against the dollar by 52.3% in 2002, while in 2003 the real appreciated against the dollar.

Financial expenses related to increases in interest rates increased by 17.1%, from R$193.5 million in 2002 to R$226.5 million in 2003. Financial investment income increased by 175.5%, from R$23.2 million in 2002 to R$64.2 million in 2003 because of our increased cash position. Expenses arising from electricity grid usage charges related to use of public assets increased by 171.1%, from R$3.8 million for the year ended December 31, 2002 to R$10.3 million in 2003, as a result of the start-up of the Cana Brava plant in May 2002, as a result of which these charges ceased to be added to fixed assets and began to be expensed.

Non-operating result
In 2003, we had non-operating net revenue of R$2.7 million, primarily due to the reversal of the provision for losses on assets associated with the Jacuí facility. In 2002, non-operating net expense totaled R$2.7 million mainly related to the write-off of studies and projects considered unfeasible.

Income and social contribution taxes
Income and social contribution taxes in 2003 totaled R$143.3 million, representing 21.7% of income before taxes. Our effective tax rate in 2003 was 21.7% and we recognized income and social contribution taxes on interest on shareholders' equity of R$79.6 million. In 2002, we recorded income tax and social contribution credits amounting to R$162.2 million, corresponding to a loss of 46.9% before taxes. This resulted primarily from the recording of a deferred income tax credit of R$33.4 million on interest on construction in progress, and deferred social contribution credit adjustment of R$13.6 million, due to the increase in the rate of contribution from 8% to 9%.

Income (loss) for the period
Net income in 2003 was R$517.2 million, while income per thousand shares was R$0.7923. In 2002, we recorded a loss of R$183.5 million, corresponding to a loss of R$0.2812 per thousand shares.

EBITDA
As discussed above, the increase recorded in income exceeded the growth in operating costs and expenses resulting in an increase in our EBITDA of 62.2% or R$356.0 million in 2003, compared to 2002. In 2003, EBITDA totaled R$928.2 million, compared to R$572.2 million in 2002. EBITDA margin was 50.7% in 2003, compared to 41.6% in 2002.

Liquidity and capital resources

Our liquidity and capital resources requirements result primarily from:

- liabilities arising from debt service;
- investments to maintain and modernize our power generation plants;
- taxes paid to federal, state and municipal bodies; and
- payment of dividends and other distributions to shareholders.

Our sources for liquidity and capital resources are:

- funds generated by our business activities; and
- financial income from the investment of our cash and available funds.

Our main financing source historically has been funds generated from our business activities. The operating cash flow arising from 2003 and 2004 activities amounted to R$699.7 million and R$857.5 million, respectively. The increase in 2004 was primarily due to the growth in our net income, which totaled R$775.2 million in 2004 compared to R$517.1 million in 2003.

We believe that we have sufficient liquidity and capital resources to cover estimated expenses and debt service needs, capital expenses, and other amounts payable in the following years, although we cannot guarantee that this will be the case.

Investment/Divestment of capital

Main capital expenditures
Our main capital expenditures during the periods under discussion are as follows:

	Nine months ended September 30, 2005	Year ended December 31, 2004	2003	2002
		(R$ millions)		
Power plant maintenance and renovation program	17.3	22.8	23.6	35.1
Precipitor of Unit 6 and rotor of Unit 5 of the Jorge Lacerda B thermoelectric plant	7.2	0.5	—	—
Digital remote measurement and oscilography system	1.6	1.3	0.6	2.3
Lages co-generation unit	3.5	6.4	56.6	4.2
Cana Brava power plant	1.0	1.0	20.0	246.8
System for Jorge Lacerda C thermoelectric plant	1.2	—	—	—
Implementation of UTE William Arjona Units 4 and 5	—	—	—	61.2
Total	31.8	32.0	100.8	349.6

Investments in power plant maintenance and renovation in the amount of R$22.8 million were the most relevant investments in power generation during 2004. In the nine months to September 30, 2005, investments totaled R$31.8 million, principally in our power plant maintenance and renovation program in the precipitor of Unit 6 and of Unit 5 of the Jorge Lacerda B thermoelectric plant.

Our planned investments for the coming two years are as follows:

	2005	2006	2007
	(R$ millions)		
Electricity generation complex (existing)	54	59	61
Implementation of Estreito and São Salvador[(1)]	—	154	246
Total	54	213	307

(1) Amounts corresponding to our equity share in these projects.

In 2006 and 2007, we do not expect to make any material capital investments in our subsidiaries, which are capitalized and paying dividends. Actual investment costs may vary significantly from those mentioned above, based on market valuation, inflation, supply, among other factors.

Divestments
Our main divestment in recent years was the sale of 66% of the Jacuí project. This project comprises assets representing a substantial portion of the plant necessary for implementation of a thermoelectric power plant fueled by mineral coal with power estimated at 350 MW in the State of Rio Grande do Sul. The Jacuí project was included as an asset of Gerasul's when it was privatized in 1998 and acquired by SESA. The Brazilian government through Eletrosul started works to complete the Jacuí project in 1985. Development of this project had been suspended since 1991.

In June 2004, we transferred a 33.3% interest in Jacuí to Elétrica Jacuí S.A. (Eleja) after carrying out a bid process. Eleja is a special purpose company whose parent company holds rights to exploit mineral

coal layers in the Jacuí region. Pursuant to the terms of the transfer agreement, both we and Eleja acquired put and call options, respectively, for the remaining 66.6% interest in the Jacuí project. In July 2005, Eleja exercised its first call option and became the owner of 66.6% of the Jacuí project. In 2006, both we and Eleja will have the right to exercise our respective put and call options, in relation to our remaining interest in the Jacuí project. Pursuant to the transfer agreement, Eleja assumed responsibility to complete the Jacuí project. In 2005, the authorization to implement and explore the UTE Jacuí was transferred from us to Eleja, as approved by ANEEL.

Before the transfer of the Jacuí project to Eleja, we had already written-off certain assets associated to the project that had become obsolete, and, accordingly, were not subject to transfer to Eleja.

Indebtedness

As of September 30, 2005, our total indebtedness was R$1,584.1 million, a decrease of 20.6% compared to the R$1,994.0 million as of December 31, 2004. Short-term indebtedness comprised 17.4% of our total indebtedness, compared to 15.1% in 2004. Of the total gross debt as of September 30, 2005, 33.3% was related to debt in foreign currency, and as of September 30, 2004 we had 55.2% of our gross debt pegged to foreign currency. As of September 30, 2005, 47.5% of our foreign currency debt was hedged against currency variation through financial hedge transactions.

The following table presents a summary on our indebtedness by category as of the periods indicated:

	As of September 30,		As of December 31,		
	2005	2004	2004	2003	2002
			(R$ millions)		
Current liabilities					
Loans and financing:					
Foreign currency:					
National Treasury Secretariat	89.3	111.6	104.6	103.3	78.8
Financial institutions	19.3	60.6	48.8	44.9	62.2
Total foreign currency	108.6	172.2	153.4	148.2	141.0
Local currency:					
Eletrobrás	71.6	64.8	66.4	60.1	54.4
Financial institutions	60.7	55.6	57.9	50.2	311.8
Total local currency	132.3	120.4	124.3	110.3	366.2
Debentures	35.0	31.2	23.3	21.2	16.8
Long-term liabilities					
Loans and financing:					
Foreign currency:					
National Treasury Secretariat	288.1	503.0	414.1	560.1	774.4
Financial institutions	131.2	527.1	491.8	571.2	711.9
Total foreign currency	419.3	1,030.1	905.9	1,131.3	1,486.3
Local currency:					
Eletrobrás	193.5	265.0	247.8	314.2	374.4
Financial institutions	350.8	396.9	385.7	413.9	391.0
Total local currency	544.3	661.9	633.5	728.1	765.4
Debentures	344.6	160.8	153.6	166.1	179.0
Total	1,584.1	2,176.6	1,994.0	2,305.2	2,954.7

For the period ended September 30, 2005, we recorded a debt to EBITDA ratio of 1.1x.

Material finance agreements

The most significant finance agreements entered by us are briefly described below:

- In December 3, 1999, we entered into an Asset Sale and Purchase Agreement with Enersul, pursuant to which we acquired from Enersul certain assets, rights and obligations, including a loan agreement dated September 24, 1998, entered into by Enersul and Deutsche Bank Aktiengesellschaft as part of a financing for the acquisition by Enersul of gas turbines. The loan agreement is subject to adjustment by the LIBOR rate plus a spread of 0.55% per annum. In addition to the Asset Sale and Purchase Agreement, we have entered into a Payment Agreement with Enersul, that regulates our rights and obligations under the Asset Sale and Purchase Agreement referred to above. As of September 30, 2005, the outstanding amount under such loan agreement was R$19.6 million;
- On February 23, 2001, we entered into an Agreement for Transferring Funds in Foreign Currency with ABN Banco AMRO Real S.A., in the total amount of US$14.1 million, equivalent to R$31.3 million, at the rate of exchange effective on September 30, 2005. The principal amount is payable in ten equal semi-annual installments of US$1.4 million, the first and the last installment being due on September 15, 2003 and March 15, 2008, respectively. As collateral, we issued to Banco ABN AMRO Real S.A. a promissory note in the amount of US$16.9 million. As of September 30, 2005, the amount due under this agreement was R$15.7 million;
- On November 29, 1999, we completed a private placement of Floating Rate Notes in the international capital markets amounting to EUR40.0 million, due on November 30, 2007. These Notes accrue interest at EuroLibor, plus a spread of 7% per year, payable every November, the last installment being due on November 30, 2007. As of September 30, 2005, these Notes were held by BNP Paribas Luxembourg and the principal outstanding was R$115.3 million;
- On April 28, 1997, we entered into a Agreement for Debt Acknowledgement and Consolidation with the Brazilian government, in which we acknowledged a debt due of R$201.5 million (equivalent to US$199.2 million on August 1996) related to foreign liabilities arising from short and long-term loan agreements entered into with foreign creditors by our predecessor, Gerasul. We are required to maintain a deposit in Banco do Brasil in an amount sufficient to cover our obligation under this Agreement. As of September 30, 2005, the balance payable under this agreement was R$302.6 million;
- On May 15, 2001, we entered into an Agreement for Debt Acknowledgement and Consolidation with the Brazilian government, Furnas and Banco do Brasil S.A., in which we acknowledged a debt payable to the Brazilian government amounting to R$271.4 million (GBP48.5 million and DEM154.9 million). The principal amount is subject to monetary adjustment and accrues daily interest on the balance payable at variable rates, pursuant to rates published by a foreign creditor agency. As collateral for these liabilities, we pledged deposits held at Banco do Brasil, which are required to be sufficient to cover the amounts payable under this agreement. As of September 30, 2005, the balance payable under this agreement was R$74.8 million;
- On August 1 and September 16, 1991, we entered into finance agreements with Eletrobrás amounting to R$247.7 million and R$127.5 million, respectively. These amounts accrue interest at 10% per year plus a 2% annual administrative fee. As collateral for these liabilities, we (i) pledged to Eletrobrás certain of our account receivables, and (ii) issued to Eletrobrás promissory notes that provide for installment payments. As of September 30, 2005, the balance payable under these agreements was R$124.0 million and R$141.0 million, respectively;
- On December 27, 2001, we entered into a Private Finance Agreement upon Concession of Credit Line with Banco do Brasil, pursuant to which we obtained financing of R$30.0 million at an effective rate of 14% per year. Principal and interest are payable in 102 consecutive monthly

installments, the first and the last ones being due on July 1, 2003 and December 1, 2011, respectively. As collateral for these liabilities, we assigned and transferred to Banco do Brasil a credit amounting to R$8.7 million from the sale of electricity. As of September 30, 2005, the balance payable under this agreement was R$22.3 million;

- On December 23, 2002, we entered into a Finance Agreement upon Concession of Credit Line with BNDES, pursuant to which we obtained financing of R$35.0 million payable in 60 successive monthly installments, the first and the last being due on March 15, 2003 and February 15, 2008, respectively. The principal payable accrues interest at 1% per year above the adjusted average annual rate of daily financing based on the SELIC. As of September 30, 2005, the balance payable under this finance agreement was R$22.2 million; and
- On May 2, 2005, we completed the issuance of 20,000 simple debentures, with nominal value per debenture of R$10,000, totaling R$200.0 million. Such debentures were issued in two series, the first one being due on May 2, 2011, adjusted by IGP-M and interest payable annually at a fixed rate of 9.29% per year on the adjusted nominal value of each debenture. Second series debentures are due on May 2, 2010, and interest is payable every six months, equivalent to 103.9% cumulative DI rate. As of September 30, 2005, the outstanding principal amount of these debentures was R$207.2 million.

In addition to the above-mentioned material finance agreements, as of September 30, 2005, we were party to several guarantee arrangements with total amount of approximately R$144.4 million (including guarantees for obligations of our subsidiaries).

Contractual obligations

For more information our concession contracts, see "The Brazilian power industry—Concessions."

The table below shows the schedule of payments in relation to our contractual obligations, which are primarily financial, as of September 30, 2005.

Year	Financial Agreements	Energy Supply Agreements
	(R$ millions)	
2005	113.2	13.2
2006-2008	678.9	385.0
2009-2011	548.6	—
2012-2014	139.0	—
After 2014	104.4	—

Transactions not recorded on the balance sheet

For the period ended September 30, 2005, we did not have any transaction that was not recorded in our consolidated financial statements, according to Brazilian GAAP.

Information on market risks

The principal market risks that affect our business are listed below:

- ***Interest and index rate risk:*** 67.2% of our indebtedness is subject to variable interest rates such as TJLP, LIBOR and DI. Accordingly, our results of operations are affected by the change in those rates to the extent that a possible increase in such rates would result in increased costs and debt service. For the period ended September 30, 2005, in the event interest rates increased by 1.0%, the additional cost would amount to approximately R$10.6 million; and

- ***Exchange rate risk:*** Our consolidated indebtedness as of September 30, 2005 totaled R$1,584 million, of which 33.3% are amounts payable in foreign currency. In addition, our debt portion in dollars and some of our costs, mainly associated to the purchase of few equipment and technologies of our Power Generating Facility, are in foreign currency. Accordingly, we are directly affected by the market risk arising from exchange rate (dollar). Our group companies carried out hedge transactions to mitigate the risk of exchange rate variation, which covers their cash flow in foreign currency until December 2006, as well as part of their debt service in foreign currency.

Discussion of certain differences between Brazilian GAAP and U.S. GAAP

We prepare our financial statements in accordance with Brazilian GAAP which differs in significant respects from accounting practices generally accepted in the United States, which we refer to as "U.S. GAAP". We set forth below a brief overview of certain key differences between Brazilian GAAP and U.S. GAAP as they affect our financial statements. This brief overview is not complete and is subject to and qualified in its entirety by reference to the pronouncements of the Brazilian and United States accounting professions. Please note that we have made no attempt to identify or quantify the impact of these differences on our financial statements. Potential investors should consult their own professional advisors for an understanding of the differences between Brazilian GAAP and U.S. GAAP, and how those differences might effect the financial information contained herein.

- Under Brazilian GAAP, we capitalize both interest costs and foreign exchange variations on borrowed funds as interest on shareholders' equity used in construction in progress while U.S. GAAP provides that any interest incurred on borrowings be capitalized to the extent borrowings do not exceed construction in progress.
- Under Brazilian GAAP, the acquisition of a controlling stake in another company is accounted for at the carrying amount of the assets and liabilities purchased with the difference between the acquired company's net assets and the purchase price and being accounted for as goodwill and amortized over the concession period of the company acquired, or where it does not pertain to goodwill, is immediately expensed. Brazilian GAAP also allows for the amortization of goodwill based on future profitability projections. Under U.S. GAAP, the assets and liabilities of the acquired company are accounted for at their fair value, and any difference between the fair value of the net assets, including intangible assets, and the purchase price is accounted for as goodwill.
- Brazilian GAAP permits net income per share to be calculated based on the number of shares outstanding at the balance sheet date. Under U.S. GAAP, net income per share is calculated by taking account of share equivalents, and the number of shares is calculated based on a weighted average.
- Under Brazilian GAAP, derivatives are normally recorded at their market value. Under U.S. GAAP, all derivative financial instruments must be accounted for at their fair value at each balance sheet date and classified either as assets or liabilities. Changes in the fair value of derivatives should be recorded in earnings unless the derivative is designated as a part of a hedge transaction and meets the criteria for hedge designation. The ineffective portion of all hedges should be recorded in earnings. Under Brazilian GAAP, there is no such clearly designated set of defined accounting practices to address the valuation of derivative financial instruments, other than for financial institutions.
- Brazilian GAAP allows revaluations (appraisals) to be recorded, net of deferred tax effects, and credited to a reserve account in shareholders' equity and transferred to retained earnings as the related assets are depreciated or disposed of. Brazilian companies may opt to carry property, plant and equipment at cost, monetarily adjusted up or at appraised values. In addition, deferred taxes

must be recognized on revaluation increments. Under U.S. GAAP, revaluations of property, plant and equipment is permitted and is recorded at historical cost less accumulated depreciation.

- Differences exist between Brazilian GAAP and US GAAP in respect of retirement cost. One such difference is the method of accounting for non-funded retirement commitments.
- Under Brazilian corporate law, proposed dividends are provided for in the consolidated financial statements before their approval at the annual shareholders' meeting. Under U.S. GAAP, dividends are not provided for until approved at the annual shareholders' meeting, unless management is authorized to declare statutory dividends.
- Brazilian GAAP does not provide for specific disclosures regarding guarantees and liabilities which generally are recorded only when payment is deemed probable. U.S. GAAP requires certain disclosures to be made by a guarantor regarding guarantee obligations and the recognition by the guarantor of a liability for the fair value of the obligation undertaken.
- Brazilian GAAP generally requires less disclosure in the notes to the financial statements than does U.S. GAAP. In addition, certain income statement line items are presented differently than under U.S. GAAP.

The Brazilian power industry

OVERVIEW

In 2002, the Ministry of Mines and Energy (MME) approved the Ten-Year Expansion Plan under which Brazil's generation capacity is projected to increase to 112.1 GW by 2012, of which 86.8 GW (77.4%) is to be generated by hydroelectric power, 16.8 GW (15.0%) by thermoelectricity, and 8.5 GW (7.6%) is to be imported within the SIN. As of December 31, 2004, the total generation capacity of installed energy within SIN amounted to 82.1 GW, according to the ONS.

Approximately 34.0% of the installed capacity in Brazil is currently generated at plants owned by Eletrobrás, a holding company controlled by the Brazilian government. Through its subsidiaries, Eletrobrás also owns 61.0% of the installed transmission infrastructure in Brazil. Moreover, some Brazilian states control companies involved in the generation, transmission and distribution of electricity. They include CESP, COPEL and CEMIG, among others. In 2003, private companies held 20.0% and 72.0% of the energy generation and distribution markets, respectively, in terms of total capacity, and 21.0% of the transmission market in 2004, in terms of revenue.

Generation capacity

The power industry in Brazil is divided into four geographic regions: southeast, south, north and northeast which are interconnected by high tension transmission lines. Hydroelectric plants generate approximately 92.0% of all electricity generated in Brazil with the remainder being generated by thermoelectric plants using natural gas, diesel, fuel oil, coal, wood, or nuclear fuel. Except for isolated systems in the north region, thermoelectric plants generally are used to supplement energy generated by hydroelectric plants and are brought into service as a less expensive alternative to increasing hydroelectric capacity.

The table below describes the evolution of installed electricity generation capacity in Brazil per hydroelectric, thermoelectric and nuclear generation for the years 1999 through 2004, and an ONS projection through 2008:

	Hydroelectric[1]	Thermoelectric	Nuclear	Total[2]
		(in MW)		
1999	57,724	3,478	657	61,859
2000	59,452	4,251	1,966	65,669
2001	61,044	5,130	1,966	68,140
2002	63,739	8,216	2,007	73,962
2003	66,321	8,993	2,007	77,321
2004	67,873	10,951	2,007	80,603
2005	69,222	19,733	2,007	83,469
Projection				
2006	73,810	11,765	2,007	87,582
2007	74,050	11,765	2,007	87,822
2008	74,050	11,765	2,007	87,822

(1) Includes 50% of Itaipu's total operating capacity.

(2) Data do not include the power of self-generators.

Source: ONS

Electricity consumption in Brazil

Energy consumption in Brazil reached 320,772 GWh in 2004, an increase of 4.5% if compared to 2003, reflecting a GDP growth during the period of 4.9%. In the coming years, electricity consumption is expected to continue to follow the GDP growth.

Expansion program—national electricity plans

As the Interconnected Power System is mainly supplied by hydroelectric generators involving a large geographic area and substantial power interchanges between the different regions of the country, strategic energy expansion programs are necessary to ensure continuity of supply and to monitor and control development. These expansion programs are known as the National Electric Power Plans.

In the past, the *Grupo Coordenador de Planejamento dos Sistemas,* or GCPS, prepared a plan referred to as the Ten-Year Expansion Plan, which established the number, location and generation capacity of power plants that could be build in each region. This responsibility passed to the *Comitê Coordenador do Planejamento de Expansão dos Sistemas Elétricos*, or CCPE and currently is under the responsibility of *Empresa de Pesquisa Energética*, or EPE. The Ten-Year Expansion Plan set out the principal short- and medium-term planning guidelines for the electric power industry. The Plan was first updated in 1989, beginning with the Ten-Year 1990-1999 Expansion Plan, and has been periodically updated. The current version is the Ten-Year 2003-2012 Expansion Plan, or the 2012 Plan. Prior to the enactment of the power industry law in 1989, the Ten-Year Expansion Plan specifically stated which utility would be responsible for building each project contained in the plan. Currently, all hydroelectric generation concessions must be preceded by a public bidding process. As a result, the 2012 Plan in effect only suggests where it would be appropriate to build a generation facility and a public bidding process determines what company will actually build the plant. Furthermore, thermoelectric plants, are not subject to a public bidding process, can be built by an independent power producer.

The 2012 Plan takes into account three different growth scenarios for Brazil from 2003 through 2012: (i) strong, (ii) average and (iii) low. Brazil's GNP is expected to grow, through 2012, 5.5% per year in the strong growth scenario, 4.5% per year in the average growth scenario and, finally, 2.5% per year in the low growth scenario. The estimated increase in total consumption of electric power by concessionaires, which has been adopted as a point of reference for the entire country, is 6.0%, 5.1% and 3.2% per year in the strong, average and low growth scenarios, respectively. Total consumption of electric power is expected to increase to approximately 577.2 KWh.

In addition, the Brazilian government has entered into various other agreements to help meet Brazil's energy needs, such as those relating to the Brazil-Bolivia natural gas pipeline and to the transmission lines between Brazil and Argentina.

Concessions

Companies or consortia that wish to build or operate facilities for generation, transmission or distribution of electricity in Brazil must apply to MME or ANEEL, as representatives of the Brazilian government, for a concession, permission or authorization, as the case may be. There are two types of concessions for power generation: the concession for electricity public services and the concession for use of public assets. Concessions grant rights to generate, transmit or distribute electricity in the relevant concession area for a specified period. This period is usually 35 years for new generation concessions, and 30 years for new transmission or distribution concessions. An existing concession may be renewed at the granting authority's discretion. Even if we have fulfilled all our obligations under the concession agreements and requested the renewal of the concession period, renewal of the concession is subject to the discretion of ANEEL. We cannot assure you that our concessions will be

renewed by the concession authority. In addition, renewal of a concession would likely be conditioned on the payment by us of new concession fees.

The concession law establishes, among other things, the conditions that the concessionaire must comply with when providing electricity services, the rights of the consumers, and the obligations of the concessionaire and the granting authority. Furthermore, the concessionaire must comply with regulations governing the electricity sector. The main provisions of the concession law are summarized as follows:

- ***Changes in controlling interest.*** The granting authority must approve any direct or indirect change in the concessionaire's controlling interest.
- ***Intervention by the granting authority.*** The granting authority may intervene in the concession, by means of a presidential decree, to ensure the adequate performance of services, as well as the full compliance with applicable contractual and regulatory provisions. Within 30 days after the issuance of the presidential decree, the granting authority's representative is required to commence an administrative proceeding in which the concessionaire may contest intervention. During the administrative proceeding, a person is appointed in the granting authority's decree to carry on the concession. If the administrative proceeding is not completed within 180 days after the decree date, the intervention ceases and the concession is returned to the concessionaire. The concession is also returned to the concessionaire if the granting authority's representative decides not to terminate the concession and the concession term has not yet expired.
- ***Termination of the concession.*** The termination of the concession may be accelerated by means of expropriation and/or forfeiture. Expropriation is the early termination of a concession for reasons related to the public interest that must be expressly declared by law. Forfeiture must be declared by the granting authority after ANEEL or MME has made a final administrative ruling that the concessionaire, among other things:
  - has failed to render adequate service or to comply with applicable law or regulation;
  - no longer has the technical, financial or economic capacity to provide adequate service, or
  - has not complied with penalties assessed by the granting authority.

  The concessionaire may contest any expropriation or forfeiture in the courts. The concessionaire is also entitled to indemnification for its investments in expropriated assets that have not been fully amortized or depreciated, after deduction of any amounts for fines and damages due by the concessionaire.
- ***Expiration.*** When the concession expires, all assets, rights and privileges that are materially related to the rendering of the electricity services revert to the Brazilian government. Following the expiration, the concessionaire is entitled to indemnification for its investments in assets that have not been fully amortized or depreciated as of the expiration.

Penalties applicable to holder of holder of concessions

ANEEL regulation sets forth the application of sanctions and penalties to the electricity agents and classifies the penalties based on the nature and relevance of violation (including warnings, fines, temporary suspension of the right to participate in auctions for new concessions, licenses or authorization and forfeiture). For each violation, the fines may be imposed to 2.0% of the revenue of the concessionaire (net of ICMS), in the 12-month period preceding any assessment notice. Infractions

that may result in fines relate to the concessionaire's failure to request ANEEL's approval for certain actions, including the following:

- execution of agreements between related parties in the cases set forth in regulation;
- sale or assignment of assets related to the provided services, as well as the imposition of any liens (including any type of guarantee, security, pledge or mortgage) on the revenue from energy services; and
- change in control of the holder of the authorization, permission or concession.

In case of agreements entered into between related parties, the agency may impose, at any time, restrictions to its terms and conditions and, in extreme circumstances, determine their termination.

Principal regulatory authorities

Ministry of Mines and Energy (Ministério das Minas e Energia)—MME

After the approval of the New Electricity Law, the Brazilian government, acting primarily through MME, assumed certain duties which were previously under ANEEL's responsibility, especially the granting of concessions and issue of directives governing the bidding processes for concessions related to public services.

National Electricity Agency (Agência Nacional de Energia Elétrica)—ANEEL

The Brazilian power industry is regulated by ANEEL. After the enactment of the New Electricity Law, ANEEL's main responsibility is to regulate and supervise the power industry, in line with the policies to be adopted by MME.

Energy Policy National Council (Conselho Nacional de Política de Enengia)—CNPE

CNPE is presided over by MME, and most of its members are the government's ministers. CNPE was created to optimize the use of Brazil's energy resources and to assure the supply of energy in the country.

National Operator of Electric System (Operador Nacional do Sistema Elétrico)—ONS

ONS is a private non-profit entity, organized by power generators, transmission companies, distribution companies and independent consumers. The New Electricity Law granted the Brazilian government power to appoint officers for ONS Executive Board. ONS basic role is to coordinate and control the generation and transmission operations of the Interconnected System, subject to ANEEL regulation and supervision.

Electricity Trading Board (Câmara de Comercialização de Energia Elétrica)—CCEE

On August 12, 2004, the Brazilian government issued a decree establishing the regulation applicable to CCEE which, on November 10, 2004, succeeded MAE, absorbing all its activities.

One of CCEE's main roles is to hold public auctions in the regulated market. In addition, CCEE is responsible, among other things, for (1) registering all energy trade agreements in the regulated market, the agreements resulting from adjustment contracting and agreements entered into in the free market, and (2) accounting for and settling short-term transactions.

CCEE is organized by generation agents, distribution, trading and independent consumers. Its Board of Directors is composed by four members appointed by these agents and one appointed by MME, who is the Chairman of the Board.

Energy Research Company (Empresa de Pesquisa Energética)—EPE

Created in August 2004, the Energy Research Company, or EPE, is responsible for conducting strategic researches in the electric sector, including those regarding electricity, oil, gas, coal and renewable energy sources. The researches conducted by EPE will be used to subsidize MME.

Power System Monitoring Committee (Comitê de Aprimonamento do Setor de Energia)—CMSE

The New Electricity Law authorized the creation of the Power System Monitoring Committee, or CMSE, which acts under the directions of MME. CMSE is responsible for the monitoring of the system's supply conditions, proposing preventive measures to reestablish the adequate service conditions, which include demand-related actions and the contracting of a supply-side reserve.

New Electricity Law

The New Electricity Law promoted significant changes in the regulation of the electric sector, aiming at (i) encouraging the expansion of the generating capacity; and (ii) assure the supply of electricity in Brazil at low tariffs through competitive public auctions. The key features of the New Electricity Law include:

- the creation of two parallel environments for trading of energy, with (i) a more stable market in terms of energy supply, so as to give additional supply guarantees to the consumer base, called regulated market; and (ii) a market specifically focused on the non-regulated activities, in which the power generators, independent consumers and traders may take part, and which shall permit a certain competition level, *i.e.*, the free market.
- restrictions to certain activities of distribution companies, so as to assure that they concentrate only in its core business, to guarantee more efficient and reliable services to the consumer base;
- existence of an electricity reserve for all energy traded through contracts;
- prohibition of distribution companies to sell energy to independent consumers at non-regulated prices and to develop electricity generation or transmission activities;
- elimination of self-dealing, so as to provide incentives for the distribution companies to buy energy at the lowest prices available, instead of buying it from related parties; and
- validity of the agreements entered into before the effectiveness of the New Electricity Law, so as to provide stability to the transactions carried out before its enactment.

The New Electricity Law also excluded Eletrobrás and its subsidiaries from the National Privatization Plan, a program created by the Brazilian government in 1990 to promote the privatization of state-owned companies.

Dispute as to the constitutionality of the New Electricity Law

The New Electricity Law is currently being challenged on constitutional grounds before the Brazilian Supreme Court. The Brazilian government moved to dismiss the actions arguing that the constitutional challenges were moot because they related to an interim rule that had already been converted into law. However, on August 4, 2004, the Brazilian Supreme Court denied the government's motion and decided to hear the allegations of the actions and rule on their merits. One of the ministers of the Supreme Court has declared that a relevant portion of the New Electricity Law is unconstitutional. Another of the ministers has requested to review the documents related to the proceeding, therefore halting the continuation of the proceeding. A final decision on this matter is subject to majority vote of the 11 Justices, provided that a quorum of at least eight Justices must be present. To date, the Brazilian Supreme Court has not reached a final decision and it is not possible to know when such a

decision may be reached. Therefore, the New Electricity Law is currently in force. Regardless of the Supreme Court's final decision, certain portions of the New Electricity Law relating to the restrictions on distributors performing activities unrelated to the distribution of electricity, including sales of energy by distributors to independent consumers and the elimination of self-dealing, are expected to remain in full force and effect.

Should the New Electricity Law be considered unconstitutional by the Brazilian Supreme Court, the regulatory environment introduced by the New Electricity Law may lose its effectiveness, giving rise to uncertainties about when and how the Brazilian government will introduce new changes in the electric sector.

Trading of electricity

The trading of electricity as an independent activity is set forth in Law No. 9.648/98 and Decree No. 2.655/98, and it is subject to a competitive system, in which several agents may take part, among which are the power generators, acting as public service providers or independent producers, the traders and the energy importers.

As apposed to the function of distribution, energy trading is not classified as a public service and may therefore be subject to negotiated prices governed by market conditions.

Energy traders may be:

- generators selling power to end-users;
- independent traders;
- authorized importers and exporters of energy; and
- independent producers.

Energy trading may be geared toward servicing free consumers or other power generation or distribution companies.

In accordance with the New Electricity Law, under the regulated market, energy purchase and sale agreements must be entered into between each power generator and all concessionaires and permittees of distribution services of SIN, which must provide guarantees to the power generators. The contract between distribution companies and existing power generators provide for the delivery of energy starting the year following the respective public auction and must have a term of at least three and no more than 15 years. As an exception to the rules, by 2006, the public auction process may set forth the beginning of energy delivery to start in up to 5 years. The contracts between distribution companies and new power generators provide for delivery of energy starting in the 3rd or 5th year from the date of the respective public auction and must have a term of at least 15 and no more than 35 years.

Environments for trading of electricity

Under the New Electricity Law, the negotiations involving purchase and sale of electricity shall be conducted in two different market segments: (i) the regulated market, which comprises the purchase by distribution companies in public auctions to serve the consumer base; and (ii) the free market, which comprises the purchase of electricity by non-regulated entities, such as independent consumers and traders.

The energy generated by (i) projects of low generation capacity, located near consumption centers (''Distributed Generation''), (ii) power plants qualified under PROINFA, as defined below, and (iii) Itaipu, are not subject to centralized auction processes for supply in the regulated market. The

electricity generated by Itaipu is traded by Eletrobrás and the volumes which shall be purchased by each distributor are mandatorily determined by ANEEL. The prices for which the energy generated by Itaipu is traded are expressed in U.S. dollars and established in accordance with an agreement entered into between Brazil and Paraguay. Accordingly, prices for Itaipu are subject to variation of the dollar/real exchange rate. Changes in prices of energy generated by Itaipu are, however, subject to the cost recovery mechanism, calculated in the distribution tariffs. In December 2004, the index for transfer of energy supplied by Itaipu was established in an amount equal to US$19.2071/KW.

The acquisition by the distribution companies of energy arising from the Distributed Generation, wind sources, and PCHs should adopt a competitive process of public call, which ensures advertising, transparency and equality of access.

The regulated market

In the regulated market, the distribution companies purchase the energy they expect to sell to their consumer base, by means of auctions regulated by ANEEL and organized by CCEE. The purchases of electricity are made with the power generators, traders and importers of electricity (collectively referred to as "Selling Agents") by means of two types of bilateral contracts: (i) Energy Quantity Agreements (*Contrato de Quantidade de Energia*); and (ii) Energy Capacity Agreements (*Contrato de Disponibilidade de Energia*).

Under an Energy Quantity Agreement, a generator company commits to supply a certain amount of electricity and assumes the risk that electricity supply could be adversely affected by hydrological conditions and low reservoir levels, among other conditions, that could interrupt or reduce the supply of electricity, in which case the generator company will be required to purchase the electricity elsewhere in order to comply with its supply commitments. Under an Energy Capacity Agreement, a power generator commits to make a specified amount of capacity available to the regulated market. In this case, the revenue of the generator is guaranteed and the distributors face the risk of dispatch of these plants, paying the variable costs. However, these costs are passed on by the distributors to consumers. Together, these agreements comprise the energy purchase agreements in the regulated market (*Contratos de Commercialização de Energia no Ambiente Regulado)*, or CCEAR.

Pursuant to the New Electricity Law, the demand estimated by the distribution companies is the main factor taken into consideration to determine the quantity of energy that the system as a whole should contract. In accordance with the new model, the distribution companies must contract 100% of its energy need, instead of the 95% required by the former model. Insufficiency of energy to supply all of a distributor's market is noted in the CCEE accounting process and may result in penalties for distribution companies.

In accordance with the New Electricity Law, distribution companies of energy shall have the right to pass along to its customers the costs related to the energy acquired by means of auctions, as well as any taxes and sectorial charges related to such auctions. In the transfer of energy acquisition costs, certain deviations of volumes for plus or minus are admitted in view of the distribution companies' impossibility to state accurate amounts in advance regarding its demand for electricity for a certain period.

In accordance with the New Electricity Law, in the scope of the regulated market, CCEAR should be entered into between each Selling Agent and all distribution companies and permittees which take part in a certain auction, and they must provide guarantees to the power generators. The contracting between distribution companies and existing power generators may set forth the delivery of energy as from the year following the respective auction and they shall have terms of at least 3 and at most 15 years. The contracting between distribution companies and new power generators may set forth the delivery of energy as from the 3rd or 5th years counted as from the respective auction year and shall

have a term of at least 15 and at most 35 years. The regulation of contracting energy in the regulated market shall also establish the conditions and limits to pass along to end consumers the electricity acquisition cost, as well the sharing of hydrological risks between power generators and purchasers.

Contracted energy reduction
Decree No. 5.163 of March 15, 2004, which regulates electricity trading under the New Electricity Law, allows the distribution companies to reduce the volume of energy contracted by means of CCEAR in the following cases: (i) to compensate for the migration of potentially independent consumers from the regulated market to the free market; (ii) deviations from demand estimates prepared by the distribution companies, after two years of such demand calculation, and in this case the reduction may come up to 4% per year of the amount initially contracted; and (iii) increase in the volumes of energy acquired through agreements entered into before March 17, 2004.

The circumstances in which the reduction in the level of contracted energy may occur shall be duly stipulated in the CCEAR and may be exercised at the distribution company's sole discretion, in the cases set forth above and ANEEL's future regulations.

Mandatory consumption reduction
The New Electricity Law establishes that, in a situation in which the Federal Government orders the mandatory reduction in the consumption of energy in a certain region, all the Energy Quantity Agreements in the regulated market, registered by CCEE, shall have their respective volumes adjusted in the same proportion of the consumption reduction.

The free market

In the free market, electricity is traded between power generators, Independent power producers, traders, energy importers and independent consumers.

Independent consumers are those the demand of which exceeds 3 MW, served in a voltage equal or higher than 69 kV or in any voltage (provided that the supply has started after July 7, 1995), and that, due to this eligibility criterion, may be served by other suppliers, in addition to the local distribution company. Additionally, consumers with contracted demand equal or higher than 500 kW may also be served by other energy suppliers, if said consumers start being supplied by an alternative energy source, such as biomass or PCHs.

A consumer who is qualified to choose its supplier, in this case, a independent consumer, and who has an agreement for an indefinite term with a distribution company, may only terminate this agreement upon notice to the distributor, at least 15 days before the date on which such distribution company shall state its energy needs for the next auction, provided that the supply in the free market shall only be started in the year following such notice.

The potential independent consumer, upon the exercise of the prerogative to become an independent consumer, may only return to the regulated market upon a five year prior notice to the local distribution company, unless the distribution company accepts a shorter term, at its sole discretion.

Elimination of self-dealing

Considering that the purchase of electricity for the consumer base must be made in the regulated market, so-called self-dealing, in which each distribution company was able satisfy up to 30% of its energy needs by means of purchase of energy with related parties, is no longer permitted, except in the context of agreements which were duly approved by ANEEL before the enactment of the New Electricity Law.

Energy purchases under the New Electricity Law

On July 30, 2004, the Brazilian government enacted regulations governing the purchase and sale of energy in the regulated market and free market, as well as the granting of authorizations and concessions for energy generation projects, including rules related to the auction and offer procedures, the format of energy purchase agreements and methods of passing costs to end consumers.

The regulation determines that all agents who purchase electricity should contract the totality of its demand in accordance with the guidelines of the new model. On the other hand, the power generators should provide evidence linking their electricity demand to existing generation facilities or energy purchase agreements. The power generators which do not comply with these requirements shall be subject to penalties for insufficiency of guarantee.

Energy auctions

Pursuant to the New Electricity Law, distribution companies must contract 100% of their expected electricity demand for their respective concession areas. For this purpose, distribution companies should purchase energy in the auctions regulated by ANEEL (as previously mentioned, there are certain situations in which the electricity supply to the distributor does not require regulated auctions, either because it is a compulsory purchase of energy—as in the case Itaipu—or because the contracting by means of public call is authorized—Distributed Generation, wind sources, PCHs, biomass), either for acquisition from already existing or new generation projects.

The energy auctions for new generation projects are required to be held (i) five years before the initial delivery date (the so-called "A-5" auctions); and (ii) three years before the initial delivery date (the so-called "A-3" auctions). There shall also be energy auctions of the already existing generation facilities (i) held one year before the initial delivery date (the so-called "A-1" auctions); and (ii) held in up to four months before the delivery date (the so-called "adjustment auctions").

Each power generator which contracts the sale of energy through an auction shall enter into a CCEAR with each distributor, proportionally to the demand stated in the distributor's purchase intention. The only exception to this rule shall occur in the adjustment auction, in which the agreements entered into between power generators and distribution companies shall be specific, in compliance with the general guidelines established by ANEEL. The terms of the CCEAR for the "A-5" and "A-3" auctions range from 15 to 35 years, and the terms for the CCEAR for the "A-1" auctions range from three to 15 years. Agreements arising from market adjustments shall be limited to a two-year term.

After the end of each auction, the power generators and distribution companies enter into CCEAR establishing the terms, conditions, prices and volumes of contracted energy. The distribution companies provide guarantees to the benefit of the power generators, which may be a bank guarantee, pledge of receivables in an amount equivalent to 100% of the average amount of the last three invoices related to CCEAR and assignment of Bank Deposit Certificates.

The 2004 auction

On December 7, 2004, CCEE held its first auction based on the procedures set forth by the terms of New Electricity Law. The distribution companies and power generators delivered, by December 2, 2004, their estimates of electricity demand for the five subsequent years and the volumes to be acquired to meet their demands related to agreements with beginning of supply in 2005, 2006 and 2007. Based on this information, MME established the total volume of energy to be negotiated in the 2004 auction and the list of power generators taking part in the auction.

The 2005 auctions

In April, 2005, the second auction of existing energy was held in accordance with the terms of the New Electricity Law. A total of 1,325 MW was sold in the auction, corresponding to only 23% of the energy initially scheduled by MME for 2008. Such energy was sold at the average price of R$83.13/MWh.

The energy to be sold with delivery scheduled for 2009 was automatically excluded from the auction, in compliance with the rules established by MME, considering that the price for such energy, during the auction, was below the market expectations, with all power generators withdrawing their bids. As a result, there is existing energy to be contracted for 2009.

In October 2005, the fourth and fifth energy auctions for existing energy were held, with average prices of R$63.00/MWh for delivery between 2006 and 2008 and R95.00/MWh for delivery between 2009 and 2016. The energy volume sold was 102MW for 2006/2008 and 1,166MW for 2009/2016.

The energy contracts executed in relation to the auctions of the regulated market are adjusted by the IPCA.

New energy auction

The first auction of the so-called new energy is scheduled for December 16, 2005. This new energy refers to the electricity produced by new generation ventures or by existing ventures, which do not have a contract for the purchase and sale of energy approved or subject to approval by ANEEL. According to information from the Brazilian government, an installed capacity of approximately 1.8 GW will be offered in the proposed auction.

Limitations on the transfer of costs

Regarding the transfer of electricity-purchasing costs to final consumers, the Decree 5,163 establishes a mechanism, the Annual Reference Value, which limits the amounts of costs that can be passed through to final consumers. Such Annual Reference Value corresponds to the weighted average of the electricity prices in the ''A-5'' and ''A-3'' auctions, calculated for all distribution companies.

The Annual Reference Value creates an incentive for distribution companies to contract for their expected electricity demands in the ''A-5'' auctions, where the prices are expected to be lower than in ''A-3'' auctions. The Annual Reference Value will be applied in the first three years of the power purchase agreements from new power generation projects. After the fourth year, the electricity acquisition costs from these projects will be allowed to be fully passed-through. The decree establishes the following limitations on the ability of distribution companies to pass through costs to consumers:

- No pass-through of costs for electricity purchases that exceed 103% of actual demand;
- Limited pass-through of costs for electricity purchases made in an ''A-3'' auction, if the volume of the acquired electricity exceeds 2% of the demand for electricity purchased in the ''A-5'' auctions;
- Limited pass-through of electricity acquisition costs from new electricity generation projects if the volume contracted under the new contracts related to existing generation facilities is lower than 96% of the volume of electricity provided for in the expiring contract;
- From 2005-2008, electricity purchases from existing facilities in the ''A-l'' auction is limited to 1% of distribution companies' demand. If the acquired electricity in the ''A-1'' auction exceeds 1%, pass-through of costs to final consumers is limited to 70% of the average value of such acquisition costs of electricity generated by existing generation facilities for delivery between 2005 and 2008. The MME will establish the maximum acquisition price for electricity generated by existing projects; and

- If distributors do not comply with the obligation to fully contract their demand, the pass-through of the costs from energy acquired in the short-term market will be the lower of PLD and the Annual Reference Value.

Contracts executed prior to the New Electricity Law

The New Electricity Law provides that the energy agreements entered into by the distribution companies, executed and approved by ANEEL before the enactment of said law, cannot be amended for extension of terms or increases in prices or volumes of electricity already contracted, except for the initial contracts in effect in March 2004, which may be amended by December 2004, being limited to a supply maximum term, *i.e.* December 31, 2005.

During the period from 2003 to 2005, the quantities of energy and power demand of the initial contracts were reduced to an annual rate of 25% of their initial volume. In accordance with the energy sector new regulation, the released energy may be sold in the free market or regulated markets. The purpose of the transition period was to permit the gradual introduction of competition in the sector and protect the market players against exposure to short-term market prices, potentially volatile and with a trend for low prices. During this period, the energy volume contracted by means of initial contracts has been reduced by 25% per year, from 2003, and these agreements shall be in effect until December 31, 2005 at the latest.

Government limitations on agents' participation in the market

In 2000, ANEEL established new limits for the concentration of certain services and activities in the electricity sector. In accordance with such limits, except for the companies participating in the National Privatization Plan (which must comply with these limits when their final corporate restructure is completed), no company in the electricity sector may (i) hold more than 20% of the installed capacity in Brazil, 25% of the installed capacity in the South/Southeast/Center-West regions or 35% of the installed capacity in the North/Northeast regions, except if such percentage corresponds to the installed capacity of only one Power Generator; (ii) hold more than 20% of the Brazilian distribution market, 25% of the distribution market in the South/Southeast/Center-West regions or 35% of the distribution market in the North/Northeast regions, except in the event of an increase in the distribution of energy higher than the national or regional growth rates; or (iii) hold more than 20% of the Brazilian trading market for end consumers, 20% of the Brazilian trading market for users which are non-end consumers or 25% of the sum of the above-mentioned markets.

New regulatory framework

The New Electricity Law provides that concessionaires, permittees and electricity distribution utilities which operate on the SIN shall not develop any of the following activities: (i) of power generation (except for Distributed Generation); (ii) of transmission of energy; (iii) of sale of energy to independent consumers located out of their concession areas; (iv) of participation in other companies, either directly or indirectly, except for funding, investment and management of funds required for the service provision and when set forth in the concession contracts; or (v) unrelated to its corporate purpose, except in cases set forth in law and in the respective concession contracts. Such restrictions do not apply (i) to the supply of energy to isolated electric systems; (ii) to the servicing of its own market, provided that lower than 500 GWh/year; and (iii) to funding, investing in or leading to a distribution company or company of the same economic group, upon prior consent of ANEEL.

Moreover, the concessionaire and other companies authorized for generation or transmission which operates in SIN shall not be affiliates or holding companies of enterprises which develop activities of distribution of electricity in SIN.

The concessionaire, permittees and other companies authorized for distribution, transmission and generation of electricity had to adapt to the rules of said deverticalization by September 2005.

Financial guarantees

Entities participating in the CCEE must provide financial guarantees in order to ensure the proper operation of the electricity market, minimizing the risk of payment default for energy sold in the CCEE.

ANEEL Resolution No. 521/2002 provides that any concessionaire planning to issue a guarantee in favor of a generator must first request ANEEL's authorization. The request must include the amount, the period and other conditions of the transaction. Such guarantees are authorized for the period that corresponds to the construction of the plant, expiring 180 days after commercial operations begin. The guarantees must be linked to the financing of goods and services destined for use by power generators that the concessionaire deals with and belonging to the same guarantor control group of the applicable concessionaire. Resolution No. 521/2002 also provides the methodology to be used by concessionaires to determine the amount of the guarantee.

ANEEL recently approved Resolution No. 150/05, which modifies the calculation methodology. The new criteria take into account the assessment of the last three debit balances for the company in the 24 months preceding the purchase and sale of energy in the CCEE. Atypical periods such as the rationing will not be taken into account during these 24 months. ANEEL has indicated that it is considering rule proposals to provide a definitive characterization of atypical periods.

Remuneration of power generators

Differently from the distribution companies, as a general rule power generators do not have fixed tariffs for their respective concession contracts or mechanisms for their readjustment.

In the scope of the initial contracts, the power generators are remunerated at the tariffs established between them and the respective distribution companies, which are homologated by ANEEL. In the scope of Bilateral Agreements, prices are established between the parties, in general as a result of participation in public auctions.

As to bilateral contracts entered into before the enactment of the New Electricity Law, the prices negotiated between power generators and distribution companies were, in general, influenced by the limit to the transfer of electricity acquisition costs to the tariffs charged by the distribution companies from their end consumers. The transfer of energy acquired by means of supply agreements entered into before the enactment of the New Electricity Law is limited by an administrative benchmark established by ANEEL, the so-called standardizing value.

For the agreements entered into under the effect of the New Electricity Law, the limit to the transfer of costs by the distribution companies is based on the Annual Reference Value, which corresponds to the average prices calculated for the electricity auctions in "A-5" and "A-3", computed for all distribution companies. The Annual Reference Value creates an incentive for the distribution companies to contract their expected energy demands in "A-5" auctions, in which prices are expected to be lower than in the "A-3" auctions, and it shall be applied in the first three years of agreements for purchase of electricity produced by new generation ventures. After the forth year, the acquisition costs of electricity produced by said ventures may be fully passed along to their consumers.

These limits to the transfer by distribution companies of electricity acquisition costs end up restricting the energy prices practiced by the Selling Agents, since they should be similar either to the standardizing value or to Annual Reference Value to be competitive. With the enactment of the New

Electricity Law, the distribution companies may only purchase energy by means of public auctions regulated by ANEEL and, as a rule, operated by CCEE. Such restriction is not applicable to the sale of energy in the free market, in which the trading if performed based on the free negotiation of prices and other terms and conditions.

Certain power generators also count on the MRE for assuring the revenue corresponding to their assured energy. In accordance with the Brazilian regulation, the revenue arising from the sale of electricity by the power generators does not depend directly on the energy effectively generated, but on the assured energy of each power plant, the quantity of which is fixed and determined by the concession authority, and included in the respective Concession Contract. The differences between the energy generated and the assured energy are covered by MRE, the main purpose of which is to mitigate hydrological risks, ensuring that all participant power plants receive according to their level of assured energy, regardless the quantity of electricity effectively generated by them. In other words, MRE relocates the energy, by transferring the surplus of those which generated quantities above their assured energy, to those which generated a quantity of energy insufficient to meet their assured energy. The effective generation amount is determined by ONS, considering the demand for energy, the systemic restrictions and hydrological conditions. The quantity of electricity effectively generated by the power plants, be it larger or smaller than the assured energy, has its price fixed by a tariff called "Optimization Energy Tariff—TEO", which covers only the power plant's operation and maintenance costs. This additional revenue or expense shall be accounted for on a monthly basis for each Power Generator.

Remuneration of thermoelectric power generators

In accordance with Brazilian regulation, revenues arising from the sale of electricity by a thermoelectric plant do not depend on its installed capacity, but on its reserve (*i.e.*, physical guarantee of electricity, thermoelectric plants contract the energy equivalent to its physical guarantee through agreements for the purchase of power that are freely negotiated between the parties. Thermoelectric plants may deliver their contracted power through their own generation or acquisition of power in the spot market (CCEE) and its subsequent transfer, depending on the difference between their generation cost and the energy price in the spot market and, accordingly, such decision depends on the market and hydrological conditions. Thus, net income from thermoelectric plants is related to the difference between the contracted price and (i) their generation cost; or (ii) the energy price in the spot market.

Energy reallocation mechanism—MRE

MRE is a mechanism for spreading hydrological risk among power generators. All hydroelectric power generators with centralized dispatch and thermoelectric power generators benefit from CCC, provided that they have entered into the initial contracts and are members of MRE (starting in January 2006, only hydroelectric generators will be members of MRE). According to this mechanism, each plant owns an amount of energy to be traded proportional to its share of the total value of assured energy in the system. Then the total production of the MRE's member is allocated to each plant according to its share, regardless of its individual production capacity. In summary, the MRE transfers the production surplus from these plants that produce above their assured energy levels to the others that produce below it.

ANEEL defines the assured energy of each hydroelectric power generator based on computational models which use the statistic treatment of the history of energy inflows in the region in questions, river water flows and water levels in the reservoir of each power plant, in a time period of multiple years. Based on this information and considering a risk of 5% of not meeting the demand, the assured energy is calculated and its value may be reviewed every five years by ANEEL or upon the occurrence

of material events, up to the limit of 5% of the amount established in the last review, limiting reductions to 10% of the amount included in the respective agreements entered into with the concession authority.

Allocation of MRE

The MRE allocation is a four-step process that first examines the ability of plants within the same region to meet Assured Energy levels and then moves on to share excess generation between different regions. These steps are detailed below:

- determination if the aggregate net production within the MRE reaches aggregate assured energy levels of the MRE members as a whole;
- determination if a single generator has generated volumes above or below its assured energy volumes, as determined by ONS;
- if an MRE generator produced above its respective assured energy levels, the surplus generation will be allocated to other MRE generators that could not meet their assured energy levels. This allocation of the surplus generation is made, first, between the generators within a region (sub-market), and second, between the different regions, in order to ensure that all MRE members meet their Assured Energy levels. This is referred to as ''Energy Optimization,'' which is distributed in what is called the ''Energy Optimization Market'':
- if, after step 3 above, all MRE members meet their Assured Energy levels and there is still energy remaining, the net regional surplus generation will be allocated among generators in different regions. Energy will be traded at the MAE price prevailing in the region in which the energy was generated. This is referred to as ''Secondary Energy,'' and the ''Secondary Energy Market''; and
- if, after steps 3 and 4 above, all MRE members do not meet their assured energy levels, the energy deficit will be paid by the MRE members based on the PLC.

Secondary energy

The total volume of MRE energy remaining after the allocation for coverage of insufficiency of the power generators which did not produce their respective Assured Energies, is called ''Secondary Energy''. The Secondary Energy is allocated in accordance with the pro-rata participation of the assured energy of each Power Generator in relation to the global assured energy of all MRE members.

Incentives to alternative energy sources

In 2000, the Thermoelectricity Priority Program (''PPT'') was created, with the purpose of diversifying the Brazilian energy matrix and reduce its strong dependence on hydroelectric plants. The benefits granted to thermoelectric plants under PPT include: (1) assured supply of gas for 20 years; (2) assurance that costs related to the acquisition of energy produced by thermoelectric plants shall be transferred to tariffs up to the limit of the standardizing value determined by ANEEL; and (3) assured access to a BNDES special financing program for the electric sector.

PPT faced several hindrances during its implementation, especially regarding the gas price, which is in general pegged to the dollar and, in spite of several regulatory changes, PPT was never fully implemented.

In 2002, PROINFA was established by the Brazilian government to create certain incentives for the development of alternate energy sources, such as wind energy projects, PCHs and biomass projects. In accordance with PROINFA, Eletrobrás shall purchase the electricity generated by alternate sources for a 20-year period and pass them along to the distribution companies. In its initial phase, PROINFA is

limited to a total contracted capacity of 3,300 MW (each source being responsible for one third). The projects intended to be qualified to receive the benefits offered by PROINFA must have their start-up by December 30, 2008.

Regulatory charges

Tariffs for the use of the distribution and transmission systems

ANEEL inspects and regulates the access to transmission and distribution systems. The charges are: (i) TUSD, tariff charged for the use of the distribution network exclusive of each distributor; and (ii) TUST, transmission system use charge, which consists in the basic network and its additional facilities. Additionally, the distribution companies of the South/Southeast Interlinked System pay specific charges for the transmission of electricity generated by Itaipu. Following is a summary of each tariff or charge:

- *TUSD*. TUSD is paid by power generators and independent consumers for the use of the distributor's distribution system to which the power generation company or the independent consumer are connected, and it is readjusted annually, considering the variation of its components. TUSD is composed of two parts, one named TUSD-Charges, calculated in accordance with the electricity use, and the other named TUSD-Service, dimensioned to remunerate the distributor's assets.
- *TUST*. TUST is paid by distribution companies, power generators and independent consumers for the use of the transmission grid, and it is readjusted annually by ANEEL in accordance with (i) inflation; and (ii) annual revenues permitted for transmission concessionaires, including expansion costs, determined by ANEEL. In accordance with the criteria established by ANEEL, the owners of the different portions of the transmission network transferred the coordination of the operation of their facilities to ONS in exchange for the regulated payments of the transmission system users. The network users, including power generators, executed agreements with ONS which entitle them to use the transmission network line in exchange for the payment of disclosed charges. Other portions of the network owned by transmission companies but which are not considered part of the transmission network are made available directly to the interested users that paid a specific compensation to the holders of the respective right.

Itaipu transmission tariffs

Itaipu hydroelectric plant has a transmission grid operated in continuous and alternate current, which is not considered part of the basic network or of the intermediate transmission system. The use of this system is remunerated at a specific charge called Itaipu transmission tariff, paid by companies holding energy quotas produced by Itaipu, in the proportion of their quotas.

Collection for the use of water resources

Pursuant to Law No. 9.648/98, the concessionaire or authorization for development of the hydroelectric potential should pay, as a compensation for the use of water resources, 6% on the amount of the electricity it produced. The payment is due to the States, Federal District and Municipalities, in which territory the usage is located or which have areas flooded by waters from the respective reservoir, and agencies from the Brazilian government direct administration. In 2000, under Law No. 9.984 (which constituted the National Water Agency—ANA), this percentage was changed to 6.75%, and the big electricity power generators started paying the additional 0.75% in July of that year. These amounts have not been collected in full by ANA yet.

ANEEL inspection fee—TFSEE

The Electricity Inspection Fee (TFSEE) was established by Law No. 9.427/96, and regulated by Decree No. 2.410/97. It is an annual fee, differentiated according to the type of service and proportional to

the size of the concession, permission or authorization (including the independent production and the non-utility based power production.

TFSEE comes up to 0.5% of the annual economic benefit earned by the holder of the concession, permit or authorization and should be paid directly to ANEEL, in twelve monthly installments.

Distribution tariffs

The amount of the distribution tariffs is determined by ANEEL, which has power to restate and review tariffs in response to changes in energy purchase costs and market conditions. To restate the distribution tariffs, ANEEL divides the distribution companies' cost between (i) costs not controlled by distribution companies, or the so-called Portion A costs, and (ii) costs controlled by distribution companies, which are named Portion B costs. The tariffs restatement is based on a formula which considers the division of costs between two categories:

Portion A Costs include, among others, the following:

- costs with the purchase of energy for resale, as established in the initial contracts;
- costs with the purchase of Itaipu energy;
- certain tariff charges (regulatory fees);
- costs with the purchase of energy under bilateral contracts which were freely negotiated between the parties; and
- other charges related to connection and transmission and distribution system use.

The transfer of costs with the purchase of energy set forth in supply agreements negotiated before the enactment of New Electricity Law is subject to a ceiling based on the standardizing value established by ANEEL for each energy source (such as hydroelectric, thermoelectric and alternate energy sources). The standardizing value applied to the supply agreements is restated annually so as to reflect cost increases incurred by power generators. Such restatements take into consideration (i) inflation; (ii) costs incurred in convertible currency; and (iii) costs related to fuels (such as supply of natural gas). The incurred costs shall correspond to at least 25% of all costs incurred by power generators.

Portion B comprises cost items which are controlled by the concessionaire (mainly operating costs). Portion B costs are determined by subtracting the Portion A costs from the distributor's revenue.

The concession contracts of each distributor sets forth an annual restatement of tariffs. In general, Portion A costs are fully passed along to consumers. Portion B costs, however, are restated at inflation, in accordance with the General Market Price Index (IGP-M).

distribution companies are also entitled to periodic review every four or five years, depending on the respective Concession Contract. These reviews aim at (i) assuring revenues sufficient to cover operating costs of Portion B and an adequate offset for the essential investments in services within the concession scope of each company, and (ii) determine the X factor, which is based on three components: (a) productivity gains expected from scale-up; (b) evaluations by consumers (verified by ANEEL); and (c) labor costs.

The X factor is used to adjust the proportion of change in IGP-M, which is used in annual adjustments. Thus, after the completion of the periodic review, the application of X factor determines that the distribution companies share their productivity gains with end consumers.

In addition, the electricity distribution concession holders are entitled to the extraordinary review of charges on a case by case basis, so as to assure its financial balance and compensate them for unpredictable costs, including taxes, which can give rise to significant changes in its cost structure.

Global Fund for Reversion of the Electricy Sector Asset Ownership—RGR

In certain circumstances, companies of the electricity industry are indemnified in certain events of revocation or cancellation of the concession. In 1971, the Brazilian government created the Global Fund for Reversion of the Electricy Sector Asset Ownership ("RGR"), designed to provide funds to such indemnification. In February 1999, ANEEL established the collection of a fee, demanding that all distribution companies and certain power generators which operated under public service regime made monthly contributions to RGR, at an annual rate equivalent to 2.5% of all fixed assets of an operating company. However, this contribution shall not exceed 3.0% of the relevant company total operating revenue in any year. In the last years, RGR has been used mainly to finance generation and distribution projects. A RGR is scheduled to exhaust in 2010, and ANEEL should review the charge so that the consumer is benefited with the end of RGR.

The Brazilian government started collecting a remuneration from the Independent Producers for the use of hydrological resources, except for PCHs, similarly to the remuneration collected from the public companies regarding RGR. The Independent Producers should make contributions to UBP Fund, in accordance with the rules of the auction for granting of concessions.

Energy Development Account—CDE

In 2002, the Brazilian government established the Energy Development Account, or CDE, as a successor to the CCC relating to the subsidy for fuel costs incurred by thermoelectric plants operating within the SIN that use domestic mineral coal. CDE is managed by Eletrobrás and ultimately financed by charges paid by electricity consumers. CDE's budget is a fixed amount annually restated in accordance with the IPCA to reflect inflation. The total CDE budget is approximately R$500 million for 2005, which represents approximately 0.6% of the tariffs paid by end-customers.

The CDE subsidy was created to support (i) the development of energy production throughout the country; (ii) the production of energy through alternate fuel sources such as wind, mineral coal and biomass; and (iii) the universal availability of electrical services to all citizens throughout the country. CDE regulation also provides that thermoelectric generation plants can only be added to the CDE account if the CDE account has financial capabilities to support the additional expenses relating to such plant. The CDE subsidy is scheduled to expire in 2027.

An early termination of, or amendment to, the CDE subsidy would require the approval of a new law in Brazil or the enactment into law of a provisional measure promulgated by the Executive Branch, in both cases with due observance of the legislative process.

Pursuant to Brazilian law, a thermoelectric plant that benefits from the CDE subsidy must purchase a minimum amount of domestic coal in order to guarantee a certain level of coal production. Additionally, the thermoelectric plants that use domestic coal contribute to the diversification of the Brazilian energy grid and mitigate the need to import raw materials, thus contributing to the balance of payments.

For the above-mentioned reasons, we believe that early termination of the CDE subsidy for domestic mineral coal is improbable in the medium and long term. If termination does occur, we believe its effect might be mitigated by other factors and initiatives, such as the possibility of importing coal (without the above-mentioned obligation to purchase a minimum amount), which is more efficient and thus could reduce the marginal cost of production (taking into account the cost of transportation to the plant). We believe that this flexibility, under ordinary circumstances of supply and demand, would allow us to substantially reduce the risk that would arise from early termination of the CDE subsidy.

Contribution for research and development

The holders of concessions, permits or authorizations of electricity distribution, generation and transmission utility services should invest, every year, at least 1% of its net operating revenue in the electricity industry. PCHs, solar, wind and biomass energy projects are exempt from such requirement.

Default on the payment of regulatory tariffs and charges

The New Electricity Law establishes that the nonpayment of the RGR contribution, to PROINFA, CDE, CCC, or payments due because of purchase of electricity in the Regulated or Itaipu Market, shall prevent the party in default from receiving charge restatements (except for the extraordinary review) or from receiving funds arising from RGR, CDE or CCC.

Electricity shortage

The small amount of rain in the 2000/2001 rainy season resulted in an unusual drop in the water levels in several reservoirs used by the major hydroelectric power plants in Brazil. Such fact, together with limited investments in generation and transmission projects in the prior years, caused the Brazilian government to impose mandatory restrictions in electricity consumption in 2001. In May 2001, the President of Brazil established the Electricity Crisis Management Chamber, denomination of which subsequently changed to the Electricity Management Chamber—CGSE, with the purpose of proposing and implementing emergency measures to equilibrate supply and demand of electricity and avoid unexpected shortages.

CGSE established special systems for collection of tariffs, use limits and power supply, and other measures, aiming at reducing electricity consumption in the Southeast, Center-West, Northeast and North regions of Brazil.

Due to the improvement in water conditions in Brazil and the successful policy for reduction of electricity consumption, which provided a significant increase in the levels of reservoirs of hydroelectric plants, the Brazilian government announced, in February 2002, the end of the shortage measures.

General agreement for the electric power sector

The General Agreement for the Electric Power Sector was the arrangement made between power generators and distribution companies with the purpose of defining rules for offsetting of financial losses caused by the 2001/2002 electricity shortage. The agreement, entered into in December 2001, establishes a financing of up to R$7.5 billion from Banco Nacional de Desenvolvimento Econômico e Social—BNDES to the Brazilian electricity generation and distribution companies and an extraordinary tariff restatement of 2.9% for rural and residential consumers, except for low-income consumers, and 7.9% for other classes of consumers, as a compensation for losses incurred by such companies.

Environmental aspects

Environmental responsibility

Violations to environmental law may constitute a crime, affecting both managers, who may even be arrested, and our entity. They may also give rise to administrative penalties, such as fines of up to R$50 million (applicable in double or triplicate, in case of recurrence) and temporary or definitive suspension of activities. Such penalties are applicable regardless of the obligation to repair the degradation caused to the environment and third parties.

In the civil and administrative levels, environmental damages imply joint and severally, objective, direct and indirect liability. This means that the obligation to repair the degradation caused may affect all

those directly or indirectly involved, regardless of evidencing the agents' fault. As a result, outsourcing certain of our operations, such as the disposal of waste, does not exempt our liability for possible environmental damages caused by the contractor.

Environmental licensing

The Environment National Policy, the ultimate law of which is the Brazilian Constitution, determines that the regular operation of activities considered effectively or potentially hazardous to the environment, or that in any way cause degradation to the environment, is conditioned to prior obtaining environmental licenses. This procedure is required both for the initial installation and for operation of the venture and for their extensions, and the licenses issued need to be renewed periodically. Environmental licenses relating to activities which environmental effects are considered significant is subject to Previous Study of Environmental Impact and its respective Environmental Impact Report (EIA/RIMA), as well as to the implementation of environmental impact report (funds for implementation and maintenance of conservation units, in the amount of at least 0.5% of the total cost forecast for the venture implementation).

For the ventures with regional environmental impact or performed in areas of public interest or under the Brazilian government's jurisdiction, the licensing jurisdiction is attributed to the Brazilian Institute of the Environment (IBAMA). Except for the cases in which the environmental licensing is subject to IBAMA's jurisdiction, the environment state agencies, such as IAP, in the State of Paraná, FATMA, in the State of Santa Catarina, FEPAM, in the State of Rio Grande do Sul, IMAP, in the State of Mato Grosso do Sul, and Agência Goiana do Meio Ambiente, in the State of Goiás, have jurisdiction to analyze the activities and issue environmental licenses, as well as to impose appropriate restrictions and control measures.

The environmental licensing process comprises, basically, the issue of three licenses: previous license, installation license and operation license. Before the bidding for obtainment of the concession for development of water potential, ANEEL should arrange, by means of EPE, the conduction of the environmental studies required and the obtainment of the respective previous license for the venture. The lack of environmental license, regardless of the activity being causing or not effective damages to the environment, consists in environmental crime, in addition to subjecting the infringing party to administrative penalties, such as fines, which, in the federal level, may come up to R$10 million (applicable in double or triplicate, in case of relapse), and suspension of activities.

Delays or denials, by the licensing environmental bodies, in the issue or renewal of these licenses, as well as our impossibility to meet the requirements established by such environmental bodies during the environmental licensing process, may impair, or event prevent, as the case may be, the installation and operation of our ventures.

For information about the environmental licenses related to installation and operation of our power generating facility, see item ''Environmental Management'' in the ''Business'' section.

Water resources

The Water Resources National Policy determines that the use of water bodies for purposes of intake or discharge of effluents (i) shall be previously authorized by the government, through the granting of right of use; in addition to (ii) giving rise to the collection of amounts for this purpose. In case of our hydroelectric plants located in rivers of state jurisdiction, the authority to issue the granting belongs to the respective water resources state body. In the event the river is under the Brazilian government jurisdiction, this is a responsibility of the National Water Agency (ANA).

The development of the hydroelectric potential by means of our hydroelectric plants is an activity subject to granting and subsequent collection for the water use. The collection for the water use in hydroelectric plants is set forth in law and, currently, together with the financial compensation. In cases of thermoelectric plants, until the date of this offering memorandum, the collection for waster use had not been regulated.

Business

Our Company

Introduction

We are Brazil's largest private-sector electricity generation company in terms of both installed capacity and assured energy, based on information provided by ANEEL, as of September 30, 2005. As of that date, according to the information provided by ANEEL for 2004, our installed capacity was 5,860 MW, representing 7.5% of the total electricity generating capacity in Brazil, and our assured energy was 3,172 MW. Assured energy is the maximum amount of energy (determined per hydroelectric or thermoelectric power generation facility) that generators are allowed to sell. Our electricity supply capacity, including electricity purchased from third parties under contracts, was 5,968 MW at September 30, 2005.

The table below sets forth certain consolidated financial and operating information for the periods indicated.

	Nine months ended September 30,			Year ended December 31,			
	2005[1][2]	2005[2]	2004[2]	2004[1][2]	2004	2003	2002
	(US$ millions)	(R$ millions)		(US$ millions)	(R$ millions)		
Net sales and services	882.1	1,960.1	1,853.0	1,111.5	2,469.9	1,830.9	1,375.2
EBITDA[3]	487.0	1,082.3	949.8	571.9	1,270.9	928.2	572.3
EBITDA margin[4]		55.2%	51.3%		51.5%	50.7%	41.6%
Net income (loss)	315.0	700.0	533.9	348.8	775.2	517.1	(183.5)
Volume of electricity sold (GWh)		22,354.3	22,072.5		29,440.2	24,327.0	25,417.1

(1) Amounts translated into U.S. dollars based on a rate of exchange of R$2.2222 to U.S.$1.00, the selling rate of exchange as of September 30, 2005 reported by the Central Bank.

(2) Unaudited.

(3) We calculate EBITDA by adding back net financial expenses, depreciation and amortization, non-operating results, amortization of goodwill, and income and social contribution taxes to our net income (loss). EBITDA is not a measure recognized under Brazilian GAAP, and it does not represent cash flow for the periods indicated. EBITDA should not be deemed as a substitute for net income or as an indicator of operating performance, cash flow or liquidity. EBITDA does not have a standardized meaning and our definition of EBITDA may not be comparable to the EBITDA utilized by other companies. See "Summary financial and operating information" for a reconciliation of EBITDA and net income (loss).

(4) EBITDA divided by net sales and services.

The Suez Group acquired ownership control of our company through SESA in a privatization auction of the Brazilian electricity industry held on September 15, 1998. In the seven years ended September 30, 2005, we made investments of approximately R$2.5 billion (not including the price paid in the privatization) to expand and improve our power plants, consolidating our operations in the Brazilian electricity sector and complying with all our investment obligations under our concession contracts. During that same period, our installed capacity increased by 57.6%, from 3,719 MW to 5,860 MW, and our assured energy increased by 48.0%, from 2,143 MW in 1998 to 3,172 MW at September 30, 2005.

Our largest customers are energy distribution companies, that is, companies that deliver electricity to final consumers. Nevertheless, customer portfolio maximization is an important feature of our business strategy, and we are particularly focused on expanding our base of independent consumers, which are companies that qualify to purchase their electricity directly from any suppliers of energy, including generation companies. As of September 30, 2005, we had supply contracts with more than 100 independent consumers located in 12 different Brazilian states. We believe we have one of the highest levels of contracted energy sales with independent consumers, with aggregate sales to independent consumers of approximately 745 MW. At September 30, 2005, our energy sold to distribution companies under long-term initial contracts (21%), to distribution companies under bilateral contracts (32%), to electricity traders (23%), to independent consumers (21%) and through exports (3%).

Our electricity generation facilities are composed of six hydroelectric plants and seven thermoelectric plants, of which two hydroelectric plants (Itá and Machadinho) are owned by consortia that include other companies and operated by our company.

New projects

We periodically evaluate opportunities to develop hydroelectric and thermoelectric plants and cogeneration units, such as UHEs Itá and Machadinho, the thermoelectric plant William Arjona and the Lages cogeneration facility. However, larger hydroelectric facilities, such as the UHE Cana Brava plant, are developed by the Suez Group through a separate entity, such as CEM, at that time its wholly owned subsidiary, before it is transferred to our company. After the initial phase of contracting and financing had been agreed and certain goals achieved in relation to this project, all of the share capital of CEM was transferred to us at a price and valuation determined by an independent financial institution, and we became the owner of CEM and its power plant.

Starting with the UHE Cana Brava project, in conjunction with SESA we adopted a strategy for developing large hydroelectric projects that involve initial project development by SESA or by a separate Brazilian subsidiary of SESA and the subsequent transfer to us, after the project has evolved past the initial stages and is ready to commence construction. Generally, the initial stage consists of bidding for the concession, obtaining regulatory authorizations and negotiating contracts (including power purchase agreements and related financing arrangements), to the beginning of project construction, all of which SESA manages independently of us. After this initial stage, the project is transferred to us, and we become the owner and manager of the project, assuming related liabilities.

As the project is not initially developed by us, we do not incur the risks involved in the development phase of a project. In addition, this project development strategy allows us to capitalize on the know-how and expertise the Suez Group brings to the development of projects of this type and size. The sale and transfer of projects under development is made on an arm's-length basis, and based on an appraisal prepared by an independent financial institution.

Accordingly, as of September 30, 2005, SESA had two projects that under development, the Estreito and São Salvador power plants, with construction scheduled to begin in 2006, depending on the results of the new energy auction to be held by MME and ANEEL and scheduled for December 16, 2005.

The São Salvador power plant will be located on the Tocantins River and is expected to have 241 MW of installed capacity. At September 30, 2005, this project had already obtained from IBAMA, the Brazilian Environmental Protection Agency, the necessary preliminary and installation licenses both for the power plant and the transmission line. The Estreito power plant is expected to have 1,087 MW of installed capacity, and will also be located on the Tocantins River. The concession rights of the Estreito power plant are owned by a consortium of companies, with SESA currently owning 30% of the project company. We expect that these projects will be transferred to us before the construction phase has been initiated.

Strengths

We believe that our competitive strengths include the following:

- ***Strong growth potential.*** We have a record of investment and growth in the Brazilian electricity generation sector, having increased our installed capacity by 57.6% since our privatization in 1998. Additionally, we believe we will be able to leverage our financial resources and management with the know-how of our controlling shareholders in the acquisition and implementation of new projects, to continue expanding existing power generation facilities both by developing new projects and acquiring new facilities without adversely impacting our rate of return.
- ***Solid portfolio of contracted energy.*** A substantial amount of our assured energy is contracted through 2008 at competitive prices and adjusted by the IGP-M, except for contracts executed in the regulated environment, which are adjusted by the IPCA. The high level of contracted energy through 2008 should provide us with a sustained source of cash generation in a period during which there will be a high supply of energy. In later years, when we expect to have substantial volume of energy available for sale, energy demand is expected to increase at a rate that based on projections by the Energy Research Company *(Empresa de Pesquisa Energética—EPE)* will be faster than the rate of growth in installed capacity. Therefore, we expect to capitalize on potentially higher energy prices expected to exist at that time although the market may evolve differently from our expectations. Additionally, we have 744 MW of assured energy from our operational power plants (Cana Brava, Itá, Machadinho and William Arjona) and expect to have 324 MW of assured energy from the new projects under development by SESA that we anticipate will be transferred to us prior to the beginning of their construction. The assured energy from these projects will be for sale in any of the next three new energy auctions, which are expected to occur until the end of 2007.
- ***First company to supply high volume of electricity to independent consumers.*** We were the first generation company in Brazil to focus on contracting with independent consumers to sell electricity and to develop the loyalty of these consumers. Sales to independent consumers give us more flexibility to negotiate sales terms, including pricing. The expertise we have developed in supplying those consumers has allowed us to maximize the efficiencies of our client portfolio. At September 30, 2005, our customers included over 100 independent consumers, which accounted for aggregate sales of approximately 745 MW, representing 21% of the electricity we sold during the nine months ended September 30, 2005, compared to 15.1% in 2004 and 9.5% in 2003.
- ***Consistent cash generation and sound financial position.*** We have historically achieved strong revenue growth and consistent cash flows, with average annual growth in net revenue for the period from 2002 through 2004 of 34% and of 5.8% for the nine months ended September 30, 2005, compared to the corresponding period in 2004. Our EBITDA margin has improved steadily over the last several years to 55.2% for the nine months ended September 30, 2005, compared to 51.5% for 2004, 50.7% for 2003 and 41.6% for 2002. Investment and capital expenditure requirements remain low, representing 3% of EBITDA in 2004. Those factors combined led us to a strong financial condition and low leverage (ratio of total debt to EBITDA was 1.1 as of September 30, 2005) which is reflected in one of the best ratings in the Brazilian energy sector of ''brA +'' from Standard & Poor's, and ''AA–(bra)'' from Fitch Ratings. We believe that our sound financial condition gives us the ability to explore new investment opportunities.
- ***Dedicated and experienced management committed to high standards of corporate governance.*** We are disciplined in our investment decisions and consistent in implementing our business plan. Our management team has an average of 20 years of experience in the energy sector having served our company since our privatization in 1998. This management experience and cohesion has enabled us to adapt to changing market and regulatory conditions and to implement innovative solutions which have allowed us to create value to our shareholders since our privatization in 1998.

In addition, we are committed to high standards of corporate governance practice, having our common shares listed on the *Novo Mercado* of BOVESPA.

- ***High dividend pay-out.*** Our strong cash flow generation historically has allowed us to make high dividend payments. We distributed 95% of our net income as interest on shareholders' equity and dividends in 2003 and 2004. In addition, we had one of the highest dividend yields among the Brazilian generating companies in 2004 (13.0%), annualized).
- ***Controlling shareholder with significant experience doing business in Brazil and in the energy sector.*** The Suez group has a long-term commitment to Brazil and has been doing business in the country for the past 50 years, the last eight years of which also were dedicated to the energy sector. Our installed capacity represents approximately 10% of the global installed capacity of the Suez group.

Strategy

Our objective is to continue to be a leading power generation company in Brazil. In this context, we seek to implement the following strategy:

- ***Growth with investment discipline.*** We seek revenue growth by taking advantage of improved prices for our electricity and expanding our generation facilities. We expect that beginning in 2009, when according to projections by the Energy Research Company (*Empresa de Pesquisa Energética*) the rate of energy demand increases more rapidly than the growth rate of Brazil's installed capacity, we will be well-positioned to take advantage of potentially increased energy prices as a substantial portion of our assured energy beginning in 2009 will be available to sale. With respect to the growth of our power generation facilities, taking advantage of our sound financial condition and strong revenue generation, we expect to grow by developing new projects and evaluating possible acquisitions. Our controlling shareholder is currently developing two large projects (*i.e.*, Estreito and São Salvador hydroelectric plants) which will, when transferred to us, increase our installed capacity by 567 MW.
- ***Maximization of portfolio efficiency.*** Our trading strategy and focus on expanding our base of independent consumers has allowed us to take advantage of consistently higher average sales prices with prices increasing from R$47.39 per MWh in 2002, compared to R$83.88 per MWh in the nine months ended September 30, 2005. We intend to continue investing in the provision of services to, and in relationships with, these customers by means of targeted initiatives, and by developing a marketing strategy and consumer loyalty program, since contracts with these customers result in multiple benefits to us, particularly flexibility in the terms of the energy contracts and unregulated pricing.
- ***Operating efficiency.*** Operating efficiency is the basis for our strategy to become more competitive and efficient and to continue to create and maximize value for our shareholders. We have historically presented solid operating performance and consistent productivity growth, which we believe allowed us to continue to improve our operating margins over the last years.

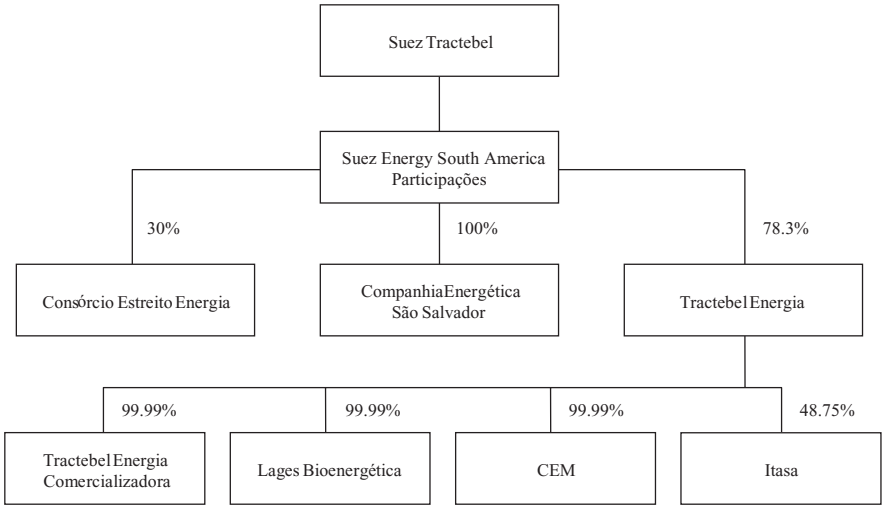
History

On December 23, 1997, the Brazilian government commenced the privatization of the power industry which to that date had been controlled by Eletrobrás. As part of this privatization, certain assets owned by Eletrosul were contributed to Gerasul. Gerasul was at that time controlled by Eletroger, a company that resulted from the partial spin-off of Eletrobrás. In April 1988, Eletroger was merged into its subsidiary Gerasul. In an auction held on September 15, 1998, on the Rio de Janeiro Stock Exchange, SESA, a company incorporated in Brazil by Suez Tractebel Société Anonyme, with principal

offices in Brussels, Belgium, acquired control of Gerasul by acquiring, for a purchase price of R$945.7 million, 227,095,639,468 Gerasul common shares, representing 50.01% of Gerasul's voting capital.

In February 2002, Gerasul adopted the trademark of its controlling company and changed its corporate name to Tractebel Energia S.A. Through September 2005, the Company had invested approximately R$2.5 billion in the expansion and improvement of our power plants. During this period our installed capacity increased by 57.6%, from 3,719 MW to 5,860 MW, representing an increase of 48.0% in our assured energy during the period, from 2,143 MW to 3,172 MW.

As of September 30, 2005, we were controlled by SESA, which held 78.31% of our total capital stock. The chart below shows our corporate structure as of September 30, 2005:



Subsidiaries

Tractebel Energia Comercializadora

Tractebel Energia Comercializadora was incorporated in October 2000, and its corporate purpose is the trading of electricity in the free market, including the purchase, sale, import and export of electricity, as well as the intermediation of any of these operations. Beginning in September 2004, Tractebel Energia Comercializadora expanded its operations and by the end of the year it had sold 632 MW of electricity. As of September 30, 2005, Tractebel Energia Comercializadora had agreements to sell electricity with 28 customers, representing approximately 280 MW of sale of electricity per month. As of September 30, 2005, we owned 99.9% of Tractebel Energia Comercializadora's voting capital stock.

Lages Bioenergética

As of September 30, 2005, we owned 99.9% of Lages Bioenergética's capital stock. In 2002, Lages Bioenergética was authorized by ANEEL to operate as an independent producer upon the implementation of the Lages co-generation unit, located in the Municipality of Lages, State of Santa Catarina. For further information regarding the Lages co-generation unit, see ''—Thermoelectric generation—plants in operation.''

Companhia Energética Meridional—CEM

CEM holds a concession to generate electricity at UHE Cana Brava, located on the Tocantins river, between the Municipalites of Minaçu and Cavalcante, in the State of Goiás. For further information on Cana Brava, see ''—Hydroelectric Generation—Plants in operation.'' As of September 30, 2005, we owned 99.9% of CEM's capital stock.

Itá Energética S.A.—Itasa

Itasa was incorporated for the sole purpose of implementing the construction and development of the Itá hydroelectric plant in partnership with members of a consortium of companies, based on a concession granted by the Brazilian government. Itasa does not have a single controlling shareholder, and its control is governed by a shareholders' agreement among its shareholders, namely, Tractebel Energia (48.75%), Companhia Siderúrgica Nacional—CSN (48.75%) and Companhia de Cimento Itambé (2.50%). For further information on the Itá hydroelectric plant, including its assured energy, see ''Hydroelectric Generation—Plants in Operation.''.

Power generating facilities

As of September 30, 2005, we had a total installed generation capacity of 5,860 MW, generated through six hydroelectric plants and seven thermoelectric plants (11 of these plants were wholly owned by us or our subsidiaries, and two of the hydroelectric plants were owned through consortia formed with other companies). In each case, we are responsible for the maintenance and operation of these power plants.

We are currently (and have been for some years) the largest private electricity generation company in Brazil based on our assured energy and the generating capacity of our facilities. In December 2004, our installed capacity, including the direct and/or indirect ownership of Itá, Machadinho, and Cana Brava hydroelectric plants and the Lages co-generation unit, reached 5,860 MW, representing an increase of approximately 57.6% compared to our installed capacity at our privatization in September 1998.

Based on information provided by ONS, our power generating facilities have among the best performance in the Brazilian electricity sector, with low rates of forced unavailability (period of time a power plant is taken out of service for maintenance). We believe that this performance is the result of our investments in planned preventive maintenance and reactivation of power plants.

The table below summarizes the information on our power generating facility as of September 30, 2005:

Facility	Location	Power Generation Units	Installed capacity Total (MW)	Installed capacity Owned by Us (MW)[1]	Our Supply Capacity (MW)	Assured energy Total (MW)	Assured energy Owned by Us (MW)[1]
Hydroelectric plants:							
Salto Santiago	Iguaçu River (PR)	4	1,420	1,420	1,420	723	723
Salto Osório	Iguaçu River (PR)	6	1,078	1,078	1,078	522	522
Passo Fundo	Passo Fundo River (RS)	2	226	226	226	119	119
Itá[2]	Uruguay River (SC/RS)	5	1,450	1,090	1,090	720	513
Machadinho[2]	Uruguay River (SC/RS)	3	1,140	383	383	529	136
Cana Brava	Tocantins River (GO)	3	450	450	450	273	273
Total hydroelectric plants			**5,764**	**4,647**	**4,647**	**2,886**	**2,286**
Thermoelectric plants:							
Jorge Lacerda Complex[3]	Capivari de Baixo (SC)	7	857	857	857	598	598
Charqueadas	Charqueadas (RS)	4	72	72	72	45	45
Alegrete	Alegrete (RS)	2	66	66	66	41	41
William Arjona	Campo Grande (MS)	5	190	190	190	177	177
Lages	Lages (SC)	1	28	28	28	25	25
Purchase of electricity			—	—	108	—	—
Total thermoelectric plants			**1,213**	**1,213**	**1,321**	**886**	**886**
Total			**6,977**	**5,860**	**5,968**	**3,772**	**3,172**

(1) For thermoelectric plants, "available energy" is applied in lieu of assured energy. The term assured energy when used in this offering memorandum includes the available energy of the thermoelectric plants.

(2) For further information on the installed capacity and assured energy of the Itá and Machadinho power plants, see "Business—Power Generating Facilities".

(3) Jorge Lacerda includes three generation facilities.

Hydroelectric generation—plants in operation

Passo Fundo hydroelectric power plant. As of September 30, 2005, Passo Fundo hydroelectric plant was wholly-owned by us and had installed capacity of 226 MW, assured energy of 119 MW with two generation units of 113 MW each. This hydroelectric plant, which started operating in 1973, is located in the north of the state of Rio Grande do Sul, in the municipality of Entre Rios do Sul.

Itá hydroelectric plant. As of September 30, 2005, the Itá hydroelectric plant was owned by the Itá Consortium and had installed capacity of 1,450 MW and assured energy of 720 MW, with five generation units of 290 MW each. This hydroelectric plant, which started operating in 2000, is located in the Uruguay River, on the border of the municipalities of Itá (in the state of Santa Catarina) and Aratiba (in the state of Rio Grande do Sul).

The Itá hydroelectric plant is the first hydroelectric venture on the Brazilian portion of the Uruguay River and represents an investment of approximately US$1.1 billion. Itá was built by a consortium between us (39.5%) and Itasa (60.5%) and its operation and maintenance is carried out by us. Itasa is under joint control by us and Companhia Siderúrgica Nacional—CSN, each with an interest of 48.75% on Itasa's capital stock. The remaining 2.5% owned by Cimento Itambé S.A.

The total assured energy of the Itá hydroelectric plant is 741 MW. Starting in 2003, the capacity of 720 MW was reviewed—in conformity with ANEEL Resolution No. 232/99 and pursuant to the Consortium Development Agreement between us and Itasa—and its assured energy was reduced to 668 MW. Accordingly, Itasa is entitled to receive 60.5%, that is, 404.1 MW of the energy generated at Itá. We are entitled to the remaining 39.5%, that is, 263.9 MW, plus (i) 52 MW, corresponding to the difference between the total assured energy of the power plant as built (720 MW) and the assured energy under the Consortium Development Agreement (668 MW), and (ii) 197.0 MW, corresponding to our interest in Itasa (48.75%), totaling 513 MW.

Itasa sells the electricity it generates to us, CSN, and Itambé, by means of an Energy Purchase Agreement entered into in 2001 that expires in 2030.

Machadinho hydroelectric plant. As of September 30, 2005, the Machadinho hydroelectric plant had an installed capacity of 1,140 MW and assured energy of 529 MW, with three generation units of 380 MW each. Machadinho hydroelectric plant which started operating in 2002 is located on the Pelotas River, on the border of the states of Rio Grande do Sul and Santa Catarina, between the municipalities of Maximiliano de Almeida and Piratuba.

The Machadinho hydroelectric plant was built by a consortium of companies, as shown below:

Consortium members	Interest (%)
Tractebel	16.94
Alcoa Alumínio S.A.	22.61
Camargo Corrêa Cimentos S.A.	4.63
Companhia Brasileira de Alumínio	24.17
Cimento Rio Branco S.A.	4.93
Valesul Alumínio S.A.	7.28
Local Electricity Office	2.40
CELESC	12.15
CEEE	4.86

The total assured energy of the Machadinho hydroelectric plant is 529 MW. However, pursuant to the Consortium Development Agreement, the plant's assured energy was reduced to 473 MW. The consortium members are entitled to 83.6%, that is 392.87 MW, of the plant's assured energy, which corresponds to their ownership interest in the Machadinho hydroelectric plant. We are entitled to the remaining 16.94%, that is, 80.3 MW, plus 56 MW, corresponding to the difference between the total assured energy of the power plant (529 MW) and the assured energy under the Consortium Development Agreement (473 MW), totaling 136.13 MW.

The total installed capacity of the Machadinho Plant is 1,140 MW. However, pursuant to the Consortium Development Agreement, the plant's installed capacity was reduced to 912 MW. The consortium members are entitled to 83.06%, that is, 757.5 MW, which corresponds to their interest in the available power of the Machadinho hydroelectric plant. We are entitled to the remaining 16.94%, that is, 154.5 MW, plus 228 MW, corresponding to the difference between the total capacity of the plant as built (1,140 MW) and the power determined under the Consortium Development Agreement (912 MW), totaling 382.4928 MW.

Salto Osório hydroelectric plant. As of September 30, 2005, the Salto Osório hydroelectric plant was wholly-owned by us. It had installed capacity of 1,078 MW and assured energy of 522 MW, with four generation units of 180 MW each and two generation units with 175 MW each. The Salto Osório hydroelectric plant, which started operating in 1975, is located in the "principal bed" of the Iguaçu River, in the state of Paraná, in the municipality of Quedas do Iguaçu.

Salto Santiago hydroelectric plant. As of September 30, 2005, the Salto Santiago hydroelectric plant was wholly-owned by us. It had installed capacity of 1,420 MW and assured energy of 723 MW, with four generation units of 355 MW each. The Salto Santiago hydroelectric plant, which started operating in 1980, is located in the "principal bed" of the Iguaçu River, in the state of Paraná, in the municipality of Saudade do Iguaçu. The Salto Santiago hydroelectric plant has the ability to install two additional generation units.

Cana Brava hydroelectric plant. As of September 30, 2005, the Cana Brava hydroelectric plant had installed capacity of 450 MW and assured energy of 273.5 MW, with three generation units of 150 MW each. The Cana Brava hydroelectric plant, which started operating in 2002, is located on the Tocantins River, state of Goiás, between the municipalities of Minaçu, Cavalcante and Colinas do Sul. The concession for operation of the Cana Brava hydroelectric plant is held by our subsidiary, CEM. We obtained a credit facility from the Inter-American Development Bank and other institutions to finance the Cana Brava hydroelectric plant that we prepaid in May 2005. The Inter-American Development Bank has recently informed us that, notwithstanding prepayment of the credit facility, it is currently undertaking social and environmental audits, specifically with respect to the relocation of population that lived in the vicinity of the Cana Brava reservoir.

Thermoelectric generation—plants in operation

Jorge Lacerda thermoelectric complex. The Jorge Lacerda thermoelectric complex, which is wholly owned by us, has the largest coal-powered plant in Latin America, located in the municipality of Capivari de Baixo, state of Santa Catarina. As of September 30, 2005, it had installed capacity of 857 MW. The Jorge Lacerda thermoelectric complex consists of three thermoelectric plants (Jorge Lacerda A, Jorge Lacerda B, and Jorge Lacerda C) and seven generation units, and it is fueled with mineral coal produced in the state of Santa Catarina. The Jorge Lacerda A began operations in 1965. Jorge Lacerda B and C began operations in 1980 and 1996, respectively. Output from Jorge Lacerda A, B, and C thermoelectric plants is intended primarily to supply energy to the southern and eastern coast of the state of Santa Catarina.

William Arjona thermoelectric plant. The William Arjona thermoelectric plant is wholly-owned by us. It is located in the municipality of Campo Grande, State of Mato Grosso do Sul, and, as of September 30, 2005, it had installed capacity of 190 MW. The William Arjona thermoelectric plant is composed of five turbo generators that use natural gas or diesel fuel. The William Arjona thermoelectric plant is the first power plant in Brazil to use gas from the Brazil-Bolivia Gas Pipeline. The William Arjona thermoelectric plant began operations in 1999. Its production helps meet increased energy demand during peak hours, thus preventing outages in the state of Mato Grosso do Sul.

Alegrete thermoelectric plant. The Alegrete thermoelectric plant, which is wholly owned by us, is located at the right margin of the Ibirapuitã River, by the city of Alegrete, in the state of Rio Grande do Sul. It is gasoline powered, and composed of two generation units with combined installed capacity of 66 MW as of September 30, 2005. This power plant started operations in 1968.

Charqueadas thermoelectric plant. The Charqueadas thermoelectric plant, which is wholly owned by us, began operating in 1962. It is located in the municipality of Charqueadas, state of Rio Grande do Sul, near the city of Porto Alegre, a major electricity consumption center. The Charqueadas

thermoelectric plant is powered by mineral coal, and composed of four generation units with a total installed capacity of 72 MW.

Lages co-generation unit. Lages was built by our subsidiary, Lages Bioenergética. The Lages co-generation unit is a cogeneration power plant which is powered by biomass. As of September 30, 2005, the Lages co-generation unit had an installed capacity of 28 MW and supply capacity of 25t/h of steam. The Lages co-generation unit was designed to use the region's wood waste and byproducts as fuel and thus was eligible for the World Bank's Clean Development Mechanism (CDM) project, developed within the Kyoto Protocol. For further information, see "—Environmental Management—Clean Development Mechanism (CDM) Project—Lages Co-generation unit". The steam power generated at the Lages Co-generation unit is supplied to wood manufacturing companies located in the surrounding area and a portion is sold to CELESC and the remainder to independent consumers.

Our market

As of September 30, 2005, we had installed capacity of 5,860 MW, of which 79.3% was generated by our hydroelectric plants and 20.7% was generated by our thermoelectric plants. In 2004, we generated a total of 30,721 GWh of electricity, representing a 13.0% increase over the volume generated in 2003 while our hydroelectric plants had an increase in total energy production of 11.0% if compared to 2003. Our thermoelectric plants' production in 2004 was 23.0% higher than in 2003.

For the period ended September 30, 2005, our total production of electricity was 21,583 GWh, approximately 1.7% lower than the volume produced in the same period of 2004. Such decrease was a result of the low levels of the reservoirs of the south region of the country. Our hydroelectric plants had total production in the period ended September 30, 2005 of 17,597 GWh, 1.6% lower than the production in the same period of 2004 while our thermoelectric plants had a total energy production in the same period of 3,987 GWh, 2.0% lower than that of the comparable period of 2004.

We operate in the south, southeast, and central-west of Brazil. In 2004, the total energy consumption in these markets was approximately 34,485 MW, representing approximately 79% of the country's total consumption that reached 43,729 MW during the period. In September, the total consumption of these markets was approximately 35,633 MW, 79% of the consumption of SIN for such period, reaching 45,118 MW. In 2004, our production represented approximately 8% of all energy required by SIN and 48.5% of the consumption of the states in the southern region. The production as of September 30, 2005 was 3,293 MW, representing 7.3% of the consumption on SIN and 45.6% of the consumptions of the states in the southern region.

Commercial strategy

Our commercial strategy relies on two basic milestones, that is, commercial risk management and the expansion and diversification of our consumer base. We have an energy committee which, together with our CEO manages our pricing process, monitors the trading of the energy we generate and manages our energy reserves.

Additionally, our commercial strategy comprises: (i) selling our generated energy available; (ii) maintaining a critical energy reserve (energy not committed to contracts in order to cover for any of our future needs, with this energy being sold if necessary); (iii) establishing a minimum price for our energy, depending on the level of purchase and the pricing mix in the market per type of energy; (iv) driving the sales of energy available to sub-markets of the south and southeast of Brazil; (v) increasing sales to independent consumers; and (vi) reaching annual sales energy to independent consumers of 1,200 MW by 2010.

The critical reserve is the volume of our guaranteed generation capacity that is not contracted for sale to cover our exposure to CCEE (spot market). This amount is contracted if this exposure does not materialize. The value of the critical reserve for each year is obtained through a process of simulation that is based on the NEWAVE model. Within the maximum critical reserve limit (which guarantees that we are not exposed to the spot market, in the event of a worse case hydrological scenario that has occurred in the past) the contracted level is increased from zero until the negative revenue obtained is equivalent to 25% of consolidated EBITDA projected in relation to the year under consideration. The complementary reserve to this contract level is defined as a critical reserve.

Our trading process is composed of three phases: pre-sales, sales, and post-sales. In the first phase, we establish the energy price, as well as our critical reserve and the energy balance. The sales process itself starts soon afterwards with (i) the preparation of trading proposals to independent consumers; (ii) participation in bids in the free market and in the regulated market intended for independent consumers and distribution companies, respectively; (iii) exploration of sales in the short term; (iv) credit analysis; and (v) negotiation and execution of agreements. After the sale is made, we put in practice our post-sales policy which aims to maintain customer satisfaction and high quality customer service.

Our commercial area has two principal offices (located in Florianópolis and São Paulo), staffed with 19 people, of whom 14 are in the commercial team and five in the marketing team. We believe that we are a market leader in operations in the commercial sector.

Customers and sale of energy

Consumer profile

Our consumer base is composed of distribution companies, energy traders, and independent consumers. The table below shows our category of consumer base and the corresponding percentage of energy purchased during the periods indicated:

	As of September 30,		As of December 31,			Contracted	
	2005	2004	2004	2003	2002	2006	2005
				(%)			
Distribution companies (initial agreements)	21	42	42	76	97	—	20
Distribution companies (bilateral agreements)	32	25	24	11	1	48	32
Traders	23	14	16	3	—	24	24
Independent consumers	21	14	15	10	2	28	22
Exports	3	5	3	—	—	—	2

Our independent consumers include companies operating in the following sectors: paper and pulp, fertilizers, industrial gas, petrochemical, automobiles and food. We believe that we are not dependent on any single industrial consumer for the maintenance of our activities and operating revenues. The table below shows the distribution of independent consumers served by us by industry, as of September 30, 2005:

Industry	Agreements with independent consumers (%)
Paper and pulp	30.7
Petrochemical	17.9
Industrial gas	13.8
Cement	11.1
Chemical	9.2
Automobiles	8.4
Mining	3.2
Steel/Mechanical	3.2
Food	1.5
Others	1.0

As of September 30, 2005, our independent consumers included Fosféntil, International Paper Group, Norske Skog, Pisa, Braskem and White Martins.

Volume of energy sold (purchasing profile)

Initial contracts are electricity supply agreements with tariffs and quantities approved by ANEEL, entered into between power generators (including us) and distribution companies that were operating in the market at the time of the privatization of the power sector. The main purpose of these initial contracts was to ensure that distribution companies had access to a stable supply of electricity with tariffs that would guarantee a fixed rate of return to the power generators during the transition period, that is, after the privatization of the energy sector.

The volume of electricity purchased by means of initial contracts has been reduced by 25% every year since 2003, and, pursuant to the New Electricity Law, each initial contract may only remain in force through December 31, 2005. In 2002, 2003, and 2004, the energy we traded by means of the initial contracts corresponded to 24,772 GWh, 18,561 GWh, and 12,433 GWh, respectively, representing approximately 97.5%, 76.3%, and 42.2% of the total electricity traded by us in such periods. By means of the initial contracts, we supply electricity to the following concessionaires: AES Sul, CEEE, CELESC, Enersul, Furnas, and RGE. At September 30, 2005, the energy we traded by means of the initial contracts corresponded to 4,633 GWh, representing approximately 20.7% of the total electricity we traded during the period.

Even with the gradual 25% reduction in the initial contracts, the volume of energy sold by us in 2004 was 29,440 GWh, representing a 21% increase in relation to the 24,327 GWh sold in 2003. This increase arises from the trading of free energy directly with other electricity sector participants such as distribution companies, traders and independent consumers. In the period ended September 30, 2005, the volume of energy we sold was 22,354 GWh, representing a 1.3% increase compared to the 22,072 GWh sold during the comparable period of 2004.

The volume of electricity traded to distribution companies, by means of bilateral contracts, increased from 198 GWh in 2002 to 2,642 GWh in 2003 and to 6,931 GWh in 2004. By means of the bilateral contracts, we supply energy to the following concessionaires: CPFL Paulista, CPFL Piratininga, RGE, Light, and CELESC. The volume of energy we contracted directly with distribution companies increased from 5,410 GWh at September 30, 2004 to 7,061 GWh at September 30, 2005. In 2002, we did not have supply agreements with energy traders, but in 2003 the volume traded with traders was 807 GWh, and 4,558 GWh in 2004, which represented approximately 15.5% of the total electricity we traded during the period.

The table below shows our purchasing profile from 2002 to 2011 by type of consumer and volume of energy sold or contracted for sale:

	Volume of Energy Sold						
	2005	2006	2007	2008	2009	2010	2011
				(MW)			
Own funds[1]	3,284	3,170	3,170	3,279	3,279	3,279	3,279
Purchases from Third Parties	149	390	200	200	200	200	—
Total Availability	3,433	3,560	3,370	3,479	3,479	3,479	3,279
Supply Agreements	3,410	3,474	3,213	3,208	2,863	2,724	1,783
Balance of available energy	23	86	157	271	616	755	1,496
(R$/MWh)[2]	85	90	96	—	—	—	—

(1) Includes the reduction of 100 MW provided in MME Ordinance 303 and, in relation to the contract with CIEN, it includes 72 MW in 2008 and 2007 and 281 MW as from 2008.

(2) Related to energy effectively generated.

Sales revenue

The table below shows the variation of sales revenue per type of customer for the periods indicated.

	Nine months ended September 30,				Years ended December 31,					
	2005		2004		2004		2003		2002	
	(R$ millions)	(%)	(R$ millions)	(%)	(R$ millions)	(%)	(R$ millions)	(%)	(R$ millions)	(%)
Distribution companies (initial contracts)	340.9	17.7	619.2	34.9	839.8	35.6	1,087.8	63.4	1,164.5	96.2
Distribution companies (Bilateral Contracts)	801.4	41.7	520.9	29.3	693.4	29.4	220.9	12.9	8.0	0.7
Traders	311.9	16.2	221.8	12.5	312.4	13.3	105.3	6.1	28.8	2.4
Independent consumers	343.6	17.9	276.4	15.6	372.8	15.8	237.6	13.9	47.6	3.9
CCEE (former MAE)	35.8	1.9	7.8	0.4	10.1	0.4	62.9	3.7	(39.0)	(3.2)
Exports	88.2	4.6	129.4	7.3	130.3	5.5	—	—	—	—

In December 2004 and April 2005, we entered into CCEARs with distribution companies in connection with the energy auctions held by CCEE. The total volume of electricity we sold was 160 MW. The independent consumers' share in our gross revenue was 3.3% in 2002, 12.2% in 2003, and reached approximately 14% in 2004, when we sold approximately 4,448 GWh of electricity to these consumers. As of September 30, 2005, we served over 100 independent consumers in the states of São Paulo, Goiás, Paraná, Rio de Janeiro, Rio Grande do Sul, Bahia, Maranhão, Mato Grosso do Sul, Mato Grosso, Minas Gerais, Santa Catarina, and the Federal District. During this period we sold 4,728 MW of energy to independent consumers.

Customer loyalty program

For the coming years, we intend to increase our participation in the industrial consumer segment. Accordingly, we have implemented a Customer Loyalty Program which enables the adjustment of the electricity to be purchased to the production process of each consumer, by entering into agreements customized to address the needs of each consumer. Additionally, we provide audit services of energy needs of selected customers, the purpose of which is to ensure the efficient use of electricity.

Additionally, in 2004 we started a number of activities within this "Customer Loyalty Program", with the purpose of getting to know our customers and their needs. Throughout the year, we conduct surveys of independent consumers that we used as a basis for preparing our action plans, which enabled us to significantly improve our customer service process.

Competition

The Brazilian energy sector is characterized by the participation of state-owned companies, especially in electricity generation. As of December 31, 2004, according to ONS, SIN total capacity of generation of installed energy was 82.1 GW, of which 34% was operated by Eletrobrás, and 20% involved operations by private companies (including us). As of September 30, 2005, according to ANEEL data from 2004, we had installed capacity of 5,859 MW, corresponding to 7.5% of the total output of the Brazilian electricity market. According to ANEEL, we are the largest private generation company in the Brazilian energy sector.

Credit, default and collection policy

We adopt a series of actions and policies aimed at preventing consumer defaults. As of September 30, 2005, we had R$3.5 million of defaulted receivables that we were negotiating with different clients. As of September 30, 2005, we had past due amounts of R$14.0 million, arising from the settlement of electricity purchase and sales transactions within CCEE, that were held on December 30, 2004. These receivables are the subject of bilateral negotiations, but in view of the uncertainty of these amounts, as of September 30, 2005, the receivables were written off as an allowance for doubtful accounts.

As of September 30, 2005, we had also recognized a provision for doubtful accounts of R$110.5 million as a result of the uncertainty of collection of amounts arising from transactions carried out within CCEE from September 2000 to September 2002, which were subject to legal actions filed by the respective debtors.

Concessions and authorizations

We operate our hydroelectric plants by means of concessions that were awarded by the concession authority following our participation in public auctions. These concessions grant us the right to generate energy for a determined period of time, generally for a term of 35 years that may be extended by the concession authority in its discretion. Each concession contract requires that we pay the government a concession fee, determined separately for each concession contract. This fee is generally paid in installments throughout the term of the concession contracts. As of the date of this offering memorandum, all of our concession fees for the use of our hydroelectric plants had been paid, except with respect to UHE Cana Brava, which had an outstanding present value balance due as of September 30, 2005 of R$174.9 million. We operate our thermoelectric plants by means of authorizations granted by ANEEL.

Concessions

All of our concession contracts have similar provisions. Pursuant to such contracts our main obligations are to:

- comply with environmental and water resources legislation, meet requirements established in existing licenses, obtain other licenses as required by law, and be liable for any consequences in connection with any noncompliance with such laws, regulations, or licenses;
- manage power plant reservoirs and respective protected areas;

- maintain the water or power reserve as required by public utilities, and respect the maximum and minimum limits required for downstream users;
- maintain and carry out regular inspection and monitoring program, in addition to emergency measures and security assessments of the power plant structures, install dam control tools wherever adequate, and ensure that analyses and interpretations of collected data are updated and made available for ANEEL inspection;
- inform ANEEL about any transfer of shares which may arise from a change in our control, as well as any proposed corporate restructuring;
- not transfer, under any circumstances, any of the concession-related assets, except upon express consent by ANEEL;
- be liable for the adequate operation and maintenance of flood gates connected to the power plants, in order to ensure minimum flow levels;
- control the levels of all banks and islands on the reservoirs, and ensure the several uses of such banks, islands, and reservoirs by licensing third parties, which should be informed to ANEEL; any gains arising from such licenses should be invested back in the maintenance of reservoirs or as instructed by ANEEL;
- inform ANEEL about any agreements between us and any of our related parties;
- comply with all tax, labor and social security regulations, and pay any related taxes, including any fees for use of water and other fees pursuant to the concession contracts; and
- invest 1.0% of our annual operating revenue in research and development in the energy industry, in conformity with a plan which should be submitted to ANEEL. Our failure to achieve the plan goals, we will be subject to a fine which should not exceed the amount of the estimated investments.

Failure by us to comply with any of such obligations may cause the early termination of the concession contracts by the concession authority. In such case, we would be entitled to indemnification less any possible penalties imposed by the concession authority.

As of September 30, 2005, we had the following concessions to use state-owned assets for generation of electricity:

	Holder of Concession or Authorization	Effective Date	Maturity Date
Salto Santiago hydroelectric plant	Tractebel Energia	09-28-1998	09-28-2028
Salto Osório hydroelectric plant	Tractebel Energia	09-28-1998	09-28-2028
Passo Fund hydroelectric plant	Tractebel Energia	09-28-1998	09-28-2028
Ita hydroelectric plant	Tractebel Energia/Itasa	12-28-1995	10-16-2030
Machadinho hydroelectric plant	Tractebel Energia/Others	07-15-1997	07-15-2032
Cana Brava hydroelectric plant	CEM	08-27-1998	08-27-2033

Concession contract for Passo Fundo, Salto Osório, and Salto Santiago
On September 28, 1998, Gerasul (the former name of Tractebel Energia) entered into Concession Contract No. 192/98 with the Federal Government, acting through ANEEL, with the purpose of regulating the concession to use state-owned assets for the production and trading of electricity, in the capacity of independent producer, by means of Passo Fundo hydroelectric plant (RS), Salto Osório thermoelectric plant (PR), and Salto Santiago hydroelectric plant (PR). The agreement has a term of 30 years and it is renewable upon our request, at the discretion of ANEEL.

The amounts due by us to the Brazilian government for the use of state-owned assets for the production and trading of electricity by means of Passo Fundo, Salto Osório, and Salto Santiago hydroelectric plants were fully paid on October 15, 2003.

Concession contract for Itá
On December 28, 1995, the Brazilian government, acting through DNAEE (succeeded by ANEEL), and the companies member of the Itá Consortium, entered into the Concession Contract No. 003/95 for electricity generation, which was amended July 31, 2000 by means of the First Amendment to the Concession Contract No. 003/95 for Electricity Generation (concession contracts No. 003/95).

The Concession Contract No. 003/95 will be in force through October 16, 2030, and it is renewable, at ANEEL discretion, upon a prior 36 months request from the members of the Itá Consortium. As of September 30, 2005, the amount due by us to the Brazilian government for the use of state-owned assets for the production and trading of electricity by means of the Itá hydroelectric plant had already been paid. For further information on the Itá Consortium, see ''Generation of Hydroelectricity—Power Plants in Operation—Itá Hydroelectric Plant''.

Concession contract of Machadinho hydroelectric plant
On July 15, 1997, the Brazilian government, by means of ANEEL, entered into the concession contracts No. 009/97 with the member companies of the Machadinho Consortium, with the purpose of sharing the use of the concession and the conditions of use of the hydroelectric power of Machadinho hydroelectric plant for purposes of electricity production. The concession has a 35 year term, renewable upon requirement of the consortium companies and approval by ANEEL.

The electricity generated in the Machadinho hydroelectric plant is shared among the consortium companies, and the we are entitled to a share of 16.9%, equivalent to approximately 80.1 MW. Nevertheless, upon express prior authorization of the concession authority, the consortium companies may carry out assignments among each other of the respective shares of the power and energy generated.

Pursuant to Concession Contract No. 009/97, we have a preference right in the purchase of the excess assured energy offered by other consortium companies. For further information on the Machadinho Consortium, see ''—Generation of Hydroelectricity—Power Plants in Operation—Machadinho Hydroelectric Plant''.

Concession contract for Cana Brava hydroelectric plant
On August 7, 1998, CEM, our subsidiary, entered into the Concession Contract No. 185/98 with the Brazilian government, by means of ANEEL, with the purpose of regulating the use of the hydroelectric power of Cana Brava hydroelectric plant and the related transmission system, for the purpose of producing electricity. The concession has a 35 term, renewable upon requirement of CEM and approval by ANEEL.

Amounts due by CEM to the Brazilian government for concessions to use the state-owned assets for the production and trading of electricity through the Cana Brava hydroelectric plant are paid in monthly installments equivalent to 1/12 of the respective annual payment amounts due under the concession, adjusted based on the annual variation of the IGP-M. As of September 30, 2005, the balance of this obligation was R$174.9 million, of which R$1.5 million was recorded in our current liabilities and R$173.4 million in the long-term liabilities.

Renewal of the concession periods
Even if we have fulfilled all our obligations under the concession agreements referred to above and requested the renewal of the concession period pursuant to the terms of such contracts, renewal of the

concession is subject to the discretion of ANEEL. We cannot assure you that our concessions will be renewed by the concession authority. In addition, renewal of a concession would likely be conditioned on the payment by us of new concession fees.

Authorizations

In accordance with the regulation in force in the electricity sector, companies must obtain authorizations granted by ANEEL for the regular operation of thermoelectric plants. As of September 30, 2005, we had the following authorizations in connection with the operation of our thermoelectric plants:

Authorizations	Holder of Concession or Authorization	Date we obtained the authorization	Date of end of authorization
Jorge Lacerda Thermoelectric complex	Tractebel Energia	09-25-1998	09-28-2028
Charqueadas Thermoelectric plant	Tractebel Energia	09-25-1998	09-28-2028
Alegrete Thermoelectric plant	Tractebel Energia	09-25-1998	09-28-2028
William Arjona Thermoelectric plant	Tractebel Energia	06-02-2000	04-28-2029
Lages Co-generation unit	Lages Bioenergética	10-30-2002	10-30-2032

Other Services

In addition to selling electricity to distribution companies, traders, and independent consumers, we provide services to monitor the quality of the energy produced, the operation and maintenance of production equipment, cogeneration, steam generation, change of voltage level in network connection equipment, and trading of excess energy. As of September 30, 2005, these activities represented 0.5% of our gross revenue and 1.0% of our EBITDA.

Suppliers

The table below shows our accounts payable with suppliers in the years ended December 31, 2002, 2003, and 2004, and in the nine months ended September 30, 2004, and 2005:

	September 30,		December 31,		
	2005	2004	2004	2003	2002
			(R$ millions)		
Materials and services	54.2	47.8	52.9	34.4	55.4
Electricity	16.8	34.4	26.9	22.3	93.8
Fossil fuel (coal and natural gas)	39.0	53.5	37.5	31.8	32.8
Total	110.0	135.7	117.3	88.5	182.0

Purchased electricity

A portion of the electricity that we sell is purchased mainly from our subsidiaries Itasa and CEM, and, in a lower volume from CIEN. As of September 30, 2005, these companies had shares of approximately 29.4%, 56.3%, and 10.4%, respectively, in Tractebel Energia's total energy purchases.

Fossil Fuel

As of September 30, 2005, we used mineral coal, natural gas, fuel oil and diesel fuel to produce electricity at our thermoelectric plants. Our major supplier of mineral coal is the Consórcio Catarinense do Carvão Energético, from which we had total purchases of 82.1% of our coal needs as of September 30, 2005.

In addition to mineral coal, the plants of the Jorge Lacerda thermoelectric complex and the Charqueadas thermoelectric plant use gasoline and diesel fuel that we purchase from Petrobrás

Distribuidora S.A. and Agricopel Comércio de Derivados de Petróleo Ltda. As of September 30, 2005, expenses incurred by us to purchase gasoline and diesel fuel used at the Jorge Lacerda thermoelectric complex and the Charqueadas thermoelectric plant represented approximately 1.2% of our total purchases.

We purchase the natural gas used at the William Arjona thermoelectric plant mainly from MSGás. As of September 30, 2005, our purchases of natural gas corresponded approximately to 16.7% of our total purchases of fuels.

Construction of hydroelectric and thermoelectric plants

We enter into agreements with third parties for the provision of engineering services, purchase of equipment and construction of hydroelectric and thermoelectric plants and transmission lines (''EPC Agreements''). These agreements are for a fixed price, and generally provide that the developer or contractor is responsible for:

(i) developing the project, in conformity with legal requirements and applicable environmental legislation; (ii) supplying the equipment for operation of the power plant or transmission line; (iii) concluding the primary and secondary civil engineering work; (iv) concluding the construction and assembly of the equipment; (v) transporting all materials and equipment; (vi) ensuring quality; (vii) commissioning, included the ongoing reliability test (ORT) of 30 days; (viii) starting commercial operation; (ix) supplying an operation and maintenance manual; (x) supplying replacement parts; and (xi) providing training services to staff and correcting possible defects.

The schedule for concluding the construction work, the price we pay, the manner of payment, guarantees, and penalties for delays in the conclusion of construction work, among others, are negotiated between us and the contracted company upon execution of each EPC Agreement.

With respect to large hydroelectric projects developed by our controlling shareholder (Estreito and São Salvador hydroelectric plants, for example), the EPC Agreements are initially negotiated and entered into by SESA and subsequently transferred to us. Accordingly, when the project is transferred to us by our controlling shareholder, the EPC Agreement is already in effect and we adhere to its terms.

As of September 30, 2005, we did not have any construction work being performed under the EPC Agreements, since the latest constructions of our power plants were concluded in 2002 (the fifth Generating Unit of the William Arjona thermoelectric plant) and 2003 (Lages Co-generation unit).

Patents, trademarks and licenses

We do not have any patents registered on our behalf with INPI, the Brazilian National Institute of Intellectual Property. As of September 30, 2005, Suez Tractebel S.A., indirect controlling shareholder of our company, was the holder of the trademark ''Tractebel'', duly registered with INPI.

Property, plant and equipment

Our major asset is our Power Generating Facilities. As of September 30, 2005, the consolidated book value of our Power Generating Facilities, net of depreciation, was R$4,389.5 million. For further information, see item ''Power Generating Facility'' in this ''Business'' section.

Some of the basic furniture and facilities we use to comply with our obligations pursuant to the concession contracts may not be transferred, assigned, encumbered or sold to any of our creditors without the prior approval of ANEEL. Pursuant to applicable legislation, the assets used for providing energy generation services are deemed as reversible, that is, at the end of the concession term or upon its early termination these assets must return to the concession authority.

Environmental management

We have an Environmental Management plan for our hydroelectric and thermoelectric plants. We also sponsor research designed to develop methodologies that minimize the environmental and social impact of our operating activities, by controlling the emission and disposal of waste, preserving natural resources, recovering damaged areas or ecosystems, and providing benefits to populations dwelling in the areas impacted by our power plants. Environmental education is a permanent feature of our projects. We also take part in the hydrographic basin committees in our areas of operation.

With respect to our thermoelectric plants, we engage in many activities to monitor the air and water quality, as well as technical procedures for control over emission, such as the retention of suspended particles system, by means of electrostatic precipitators, control over sulphur in fuels to prevent the formation of carbon dioxide, the reuse of waste (100% of light ashes from coal burnt in our thermoelectric plants are used in the cement production), and deposit of heavy ashes in landfills, mining areas, or deposits of waste from the processing of coal, in order to assist in the environmental recovery of these areas.

With respect to the production of hydroelectricity, we have a number of environmental programs, which include, among other initiatives, monitoring the quality of surface and sub-surface waters, fish fauna (monitoring and research), control over macrophytes, marginal slopes, climatology, recovery and formation of the ciliary band, and the environmental and equity surveillance of the surroundings of artificial reservoirs.

Environmental licensing

As of September 30, 2005, we were in good standing in relation to the environmental licensing required by the proper state and federal bodies that are responsible for inspecting the activities performed within our Power Generating Facilities, whether those related to the generation of hydroelectric or thermoelectricity.

Quality and environmental management systems

In November 2004, the Itá, Salto Osório, Salto Santiago, and Passo Fundo hydroelectric plants, as well as the Jorge Lacerda thermoelectric complex, were granted the NBR-ISSO 9001 (quality) and 14001 (environment) certifications, awarded by the Bureau Veritas Quality International—BVQI. Other power plants (Machadinho and Cana Brava hydroelectric plants, Charqueadas, Alegrete, William Arjona thermoelectric plants and Lages Cogeneration unit) are under an implementation process, aiming at being eligible for such certification in the second half of 2006.

Hydroelectric plants

In our hydroelectric plants, we focus on the use and preservation of reservoirs. The quality of the water in reservoirs and the preservation of the area surrounding each lake are ensured by means of permanent assessments, with environmental monitoring carried out by trained professionals and by means of agreements with inspection agencies.

As of September 30, 2005, all of our hydroelectric plants had environmental programs related to the quality of water/limnology, fish fauna, climatology, environmental and equity monitoring, plans to use water, islands, and surrounding reservoirs, among others, in addition to research and development projects.

Thermoelectric plants

In our thermoelectric plants, we focus on the quality of air and water, and on the use of ashes from the coal burnt, adopting over ten permanent monitoring items. In order to prevent water pollution, our thermoelectric plants have (i) treatment systems for liquid waste which operate in closed systems, thus

preventing the release of waste into rivers in the region in which they are located; and (ii) fuel storage areas with retention basins in case of any leakage accidents.

We carry out ongoing environmental monitoring, checking the quality of water and air. The outcome of such monitoring is forwarded to environmental agencies responsible for the licensing and inspection of power plants and other local agencies and entities (city halls, city councils, and others).

Clean Development Mechanism (CDM) Project—Lages co-generation unit

Lages Co-generation unit, which started operations in December 2003, was the first power plant in Santa Catarina powered by biomass. Due to its use of wood wastes (renewable energy) of the region as fuel, the operation system of the unit was deemed eligible by the World Bank as a Clean Development Mechanism (CDM) Project—MDL, pursuant to the Kyoto Protocol, by means of which carbon credits will be generated for future trading and negotiations by us.

In view of the carbon credits to be generated by the Clean Development Mechanism (CDM) Project of the Lages Co-generation unit, we are negotiating the sale of a portion of these carbon credits with the World Bank by means of the Prototype Carbon Fund.

Insurance

We have insurance policies covering various operating and other risks, including property damage and business interruption. The coverage limit under these policies is US$150.0 million per incident. Additionally, we have insurance policies to cover civil liability for damages against third parties up to the limit of US$50.0 million. This type of insurance covers legal liabilities arising from bodily injury or property damage caused by our operations, the industrial electricity generation or the operation and maintenance of flood gates. Additionally, we have insurance policies to cover civil liability of our directors and officers with coverage of US$5.0 million. We have insurance policies covering our whole vehicle fleet.

We also have operational risk policies, in force up to August 1, 2006, covering pecuniary damages, in the total amount of US$3,515.2 million, and lost profits of US$98.5 million.

Employees and human resources policy

Labor force

Our current labor force is composed of 894 employees, with average length of service of 14.6 years and average age of 39.9 years. Our total payroll amounted to R$6.3 million for the month of September 30, 2005. The table below shows our employee numbers for the periods indicated, segregated between administrative and operational roles:

	As of September 30,	As of December 31,		
	2005	2004	2003	2002
Administrative	120	119	119	114
Operational (power plants)	402	388	382	394
Total number of employees	894	849	844	859

Health and safety

We have occupational risk prevention programs that require the preparation of technical reports on working conditions in our Power Generating Facility. These technical appraisal reports informs us on risks associated to the work in our power plants and the exposure time, intensity and/or concentration of risks to which the employees are exposed, as well as the need to use individual or collective protection equipment.

In accordance with Brazilian legislation, employees on leave due to occupational accidents are entitled to job tenure of 12 months. On September 30, 2005, we had 1 employee on leave due to occupational accidents.

Profit sharing

In the 2005 fiscal year, on April 13, 2005, the amount of R$7.25 million was distributed to our employees as profit sharing for 2004. The related amount distributed was proportional to the compensation received by each employee and took into account the results of their individual performance evaluation.

Private pension plan

We offer to all our employees a private pension plan through PREVIG—Sociedade de Previdência Complementar, a closed private pension entity solely sponsored by us. Benefit plans managed by PREVIG are defined benefit plan and defined contribution plan.

Our defined benefit plan is covered by contributions made by our active participants and us. The defined benefit plan covers 6% of our employees with retirement scheduled for the coming nine years. Under this plan, our contribution is two times higher than the amount contributed by the plan participant. Additionally, we contribute 1.78% of our total payroll in order to amortize the reserves related to the past length of time recognized, reassessed on an actuarial basis, whose commitment ends in December 2023. During 2004 and for the period from January through September 2005, our aggregate contributions to this pension plan amounted to R$5.9 million and R$2.5 million, respectively. On October 5, 2004, we terminated participation in the defined benefit plan.

On October 5, 2004, we entered into an Adhesion Contract with PREVIG, and began offering a defined contribution plan to our employees, and commenced migration of our employees from our prior benefit plan. The effective registration of our employees in the defined contribution plan commenced in January 2005, and the migration process ended July 31, 2005. As of September 30, 2005, 843 participants were registered under this plan.

Under the defined contribution plan, in which 94% of our employees take part, the cost of the plan is formed by basic contributions made by the participant and the sponsor. Our basic contribution corresponds to the same amount of the basic contribution made by our employees. Additionally, as an incentive to migration, we have agreed to make a special contribution that will be paid to the participant who contributes to the plan for at least ten (10) years to the plan, calculated with the purpose of increasing the mathematical reserves of participants. Our contributions to these plans amounted to R$2.0 million in the period from January through September 2005.

We are also responsible for the payment of 100% of the administrative expenses of PREVIG, which is limited to 15% of its total revenues. For the period from January to September 2005, these expenses totaled R$1.8 million.

Prior to the establishment of PREVIG, our benefit plan was managed by Fundação Eletrosul de Previdência e Assistência Social—ELOS, sponsored by us and another company, which were not jointly liable. In October 2002, the Supplementary Social Security Secretariat approved the termination of the adhesion contract with ELOS and the overall transfer of the management of the benefit plan to PREVIG. In spite of the termination of the adhesion contract, the benefit plan comprising the participants who started enjoying the benefits through December 23, 1997, *i.e.*, Eletrosul's spin-off date, as well as the participants who opted for the proportional benefit deferred to that date, remains under our responsibility, at the Fundação ELOS, by force of legal actions.

While this situation remains, we will be responsible for costing 57% of ELOS administrative expenses also limited to 15% of the total respective social security revenues, and the amount we were liable for the period ended September 30, 2005 was R$1.5 million.

For the period ended September 30, 2005, our liabilities attributable to post-employment benefits amounted to R$267 million, of which R$114 million is related to contracted debts. The amount of our actuarial losses of R$155.3 million (which exceeds the present value of our actuarial obligation) is not recorded on our financial statements as per the accounting rules provided for in CVM Deliberation no. 371. Such losses shall be amortized using the straight-line method over a period of approximately 11 years (which such period corresponds to the estimated average remaining employment period for the employees that participate in the plan).

As per the instructions provided for by CVM Deliberation no. 371, the gains and losses related to reductions and anticipated liquidations of a defined benefit plan have to be recognized when such event occurs. Our independent actuaries are in process of preparing new actuarial valuations, taking into account the impacts related to the migration between the plans. Our management does not expect the occurrence of relevant effects in our financial statements as a result of this new valuation. Resulting gains and losses will be accounted for in the next fiscal quarter.

Collective bargaining agreement

We are party to a collective bargaining agreement with a number of unions representing its employees, whereby our employees are entitled to certain vested rights. This Agreement is valid for a two (2) year period, except for the economic clauses which are in force for one (1) year starting on November 1, 2004. We never had our activities halted due to any strikes.

Energy purchase agreement with CIEN

On May 5, 1998, Gerasul and CIEN entered into an agreement to purchase 300MW of "guaranteed" power (Eletrobrás, Furnas and Eletrosul acted as intervening parties). The agreement has a 20 year term, counted as from June 21, 2000, and its purpose is the purchase of 300 MW of "guaranteed" power with associated energy by us, which CIEN will make available through the energy interconnection system built and operated by CIEN in order to interconnect Brazil and Argentina. The "guaranteed" power and associated energy subject to this agreement must be from Argentina, under the responsibility of CIEN. This agreement is not registered with CCEE as an ordinary energy purchase agreement, but rather as if it was one of our thermoelectric plants in Brazil.

In March 2005, CMSE recommended ANEEL to carry out some tests to evidence the availability of the generated electricity and the physical guarantee for purposes of energy interconnections operated by CIEN to interconnect Brazil and Argentina. Based on the outcome of these tests, MME Ruling No. 153/05 on March 30, 2005, and ANEEL Resolution No. 155/05, of March 31, 2005, were enacted reducing the amount of the physical guarantee originally attributed to CIEN for performance of the agreement, from 300 MW to approximately 72 MW. In view of the manner that the agreement is registered with CCEE, this reduction would subject us to penalties set forth by proper legislation, due to insufficient physical reserve, in addition to the exposure to the CCEE short-term market. That has led us to enter into another agreement to purchase the corresponding electricity from another player.

Accordingly, we understand that this event characterized CIEN's failure to comply with the agreement, and thus CIEN should pay us the fines and refunds provided for in the agreement. Therefore, based on contractual provisions setting forth that the amounts stated in the invoices issued by CIEN must be netted from all amounts due by CIEN to us as fines and refunds (which CIEN has failed to do with respect to any of the invoices issued under this agreement since the reduction of its physical guarantee),

we have not made any payments in connection of said invoices, since we understands that these invoices are inadequate.

On November 12, 2001, CIEN filed a lawsuit against us, by means of an injunction seeking the revision of certain contractual prices linked to foreign exchange variation, in addition to the termination of the agreement. The request for advance protection was rejected. For further information on this lawsuit see item "Judicial and Administrative Matters" in this section.

We and CIEN have been discussing alternatives to settle all outstanding matters in connection with the agreement.

Contracts with suppliers

Contract for sale and purchase of energy with subsidiaries

We entered into a contract, dated January 15, 2001, relating to our purchase of 61 MW of electricity from Itasa. This contract is subject to specific regulations by ANEEL and must comply with prevailing market rules. The price per MW of electricity we pay is adjusted annually by the fluctuation in the rate of exchange of the *real* against the U.S. dollar and by the rate of inflation in the United States. This contract will expire October 16, 2030.

We also entered into a separate contract with Itasa also dated January 15, 2001, relating to our purchase of 167 MW of electricity. This contract also is subject to specific regulations by ANEEL and is required to comply with prevailing market rules. The price per MW of electricity we pay under this contract is adjusted annually by the IGP-M.

We are also party to a contract dated as of January 5, 2001 (amended March 6, 2001 and August 9, 2002), and expiring in 2015, entered into with respect to annual purchases from UHE Cana Brava of 1,125,616 MWh, 2,189,036 MWh and 2,395,903 MWh, starting October 2002, November 2002 and December 2002, respectively. The price we pay per MW of electricity pursuant to the terms of this contract is adjusted annually by the IGP-M. This contract expires in 2015.

Contract entered into with the purpose of regulating the monthly sale of 26 MW of energy produced by us to our subsidiary Lages Bioenergética, valid as from April 1, 2004 until March 31, 2017.

Purchase of natural gas

We purchase natural gas pursuant to contract with Gás do Mato Grosso do Sul—MSGÁS, dated as of November 10, 2000, expiring five years from May 2001, date of inauguration of operations at the Thermoelectric Plant William Arjona. We have already commenced negotiations for the renewal of the agreement.

Maintenance of the generation units of UHE Salto Osório

Four-year contract entered into with GE Hydro Inepar do Brasil S.A. for the maintenance of six generation units at UHE Salto Osório, dated as of December 19, 2003.

Transmission contracts

In accordance with Law 9,648/98 and Decree 2,655/98 which provide that contracts for the transmission of energy cannot to be contracted together with contracts for the sale of electricity, we entered into a transmission contract with Eletrosul—Centrais Elétricas S.A., dated as of August 20, 1998. This contract is valid as from September 1, 1998 and until the termination of our concession contracts or liquidation of Eletrosul, whichever is earlier.

Contracts for the use of transmission and distribution systems

W entered into contracts with ONS, transmission companies and Empresa Energética do Mato Grosso do Sul S.A.—Enersul pursuant to which we assumed 75% of transmission costs associated with the sale of electricity, with the remaining 25% being for the account of the distribution companies. This contract is valid until the liquidation of the transmission companies or the distribution companies, whichever is earlier.

Judicial and administrative matters

We are a party to a number of civil, tax, social security and labor claims, as well as to certain administrative proceedings. As of September 30, 2005, our provisions to cover judicial and administrative matters amounted to approximately R$145.5 million, of which R$14.2 million related to tax claims, R$20.3 million to social security claims, R$20.9 million to labor claims, and R$90.1 million to civil claims. We believe that these provisions are sufficient to cover any possible losses arising therefrom.

We are also party to other lawsuits. Based on the opinion of our legal consultants, such lawsuits do not represent a probable risk of loss and, therefore, have not been accounted for in our financial statements. The amounts of these lawsuits are shown below.

	As of September 30, 2005		
	Possible Risk	Remote Risk	Total
	(R$ millions)		
Labor	8.9	11.5	20.4
Civil	26.1	24.1	50.2
Tax	17.5	3.5	21.0
	52.5	39.1	91.6

Tax

As of September 30, 2005, we and our subsidiaries had a total tax liability of R$34.4 million.

Our material tax liabilities are related to the writ of mandamus (*mandado de segurança*) filed by us against the Federal Tax Supervisor of the city of Florianopolis in relation to the interpretation of SRF Instruction no. 468/2004 that changed the concept of determined price (*preço determinado*), as provided for in Law 10.833/03. We understand that such Instruction no. 468/2004 could not have amended, as we and our counsels believe it did, legal principles previously established by law and by the decree 1,598/1977.

As a result, we are paying PIS and COFINS taxes applicable over revenues from contracts executed prior to October 31, 2003, with a term over one year and that provide for predetermined prices, based on the previous legislation. We are depositing the balance in a judicial escrow account.

Many of our customers are industrial clients that operate in several states throughout Brazil and purchase our energy to be used in their production process. In the past, we made interstate sales to such costumers and we did not pay the related ICMS tax. Due to recent decisions by the Brazilian Supreme Court in similar cases, we started to pay the ICMS tax in such interstate transactions. We are not paying ICMS tax in connection with one of our clients in the State of Rio Grande do Sul since we have a pending administrative tax proceeding in that state. This client, located in the State of Rio Grande do Sul, has assumed the liabilities related to such proceeding by contract with us. In other states of Brazil, and in relation to the period prior to 2003, there is no judicial or administrative claim or proceeding in this regard.

Social security

As of September 30, 2005, our total social security liabilities and the total social security liabilities of our subsidiaries were estimated at R$20.3 million. As of September 30, 2005, the provision recognized to cover such liabilities amounted to R$20.3 million.

Social security claims and tax assessment notices of higher amounts are related to:

- Assessment related to the premium for occupational accident insurance for costing of special retirement benefit. This lawsuit is pending decision on the administrative challenge filed by us against INSS, the National Social Security Institution; and
- Collection notice on social security contribution on indemnity installments. At the administrative level, we were found partially acquitted. We filed a lawsuit and we were successful in trial court. An appeal filed by INSS is currently pending a court decision.

In the opinion of our legal advisors, the risk of an unfavorable decision in the administrative level is probable, and as of September 30, 2005, our provision to cover possible related losses amounted to R$20.3 million.

Civil and environmental

We and/our subsidiaries are party to 1,004 civil and environmental claims with probable, possible and remote risks of loss, which, as of September 30, 2005, represented liabilities estimated at R$100.0 million. Among the lawsuits filed against us, the following are the most significant:

Lawsuits against the privatization process

When Gerasul was privatized in 1998, two public civil actions and three class actions were filed against us, the Brazilian government, BNDES, ANEEL, Eletrobras, Eletrosul and our controlling shareholder. Such claims challenge the corporate restructuring that resulted in the incorporation and privatization of Gerasul (our predecessor). In 2001, a court decision was entered in favor of one of the public civil actions, holding Eletrosul's spin-off which resulted in the incorporation of Gerasul, and all other acts after such incorporation to be invalid. Due to this decision, the court extinguished all other claims without analyzing the merits. The parties filed appeals with the relevant appellate court (*Tribunal Regional Federal da 4ª Região*) that reversed the court decision on this public civil action, upholding the validity of all acts related to the privatization of Gerasul. This Tribunal also dismissed the class action suits and held in favor of the privatization of Gerasul. A final decision in relation to these matters may take years since the decision by the appeal tribunal is still subject to appeal to the Brazilian Superior Court and the Brazilian Supreme Court. Although the adverse decision has been reversed we and the other parties to the lawsuit cannot guarantee you that such reversed decision will be upheld by the Brazilian Supreme Court or by the Brazilian Superior Court. It is hard to predict the consequences of an adverse decision with respect to these claims. One possible result could be that the privatization of Gerasul could be declared void. Potential outcomes vary widely and are complex and may involve claims for losses and damages involving the government, BNDES, ANEEL, Eletrobras, Eletrosul, us, our controlling shareholders and third parties, including investors in our common shares.

Potential outcomes vary widely and are complex and may involve claims for losses and damages involving the government, BNDES, ANEEL, Eletrobras, Eletrosul, us, our controlling shareholders and third parties, including investors in our common shares.

Environmental Lawsuit

A public civil action was filed in October 2004 by the Federal Public Office of Santa Catarina, which is in progress before the Federal Courts, seeking remedy for environmental damages caused by pollution emanating from the Jorge Lacerda Complex, including pain and suffering and pecuniary

damages to citizens victims of pollution and to the Fund for Defense of Diffuse Rights, as well as any environmental remedy required. The action is pending an environmental audit to be conducted by experts appointed by the judge. We believe that the pollution levels emanating from the Jorge Lacerda Complex are within the limits permitted by federal and state environmental rules and, therefore, we believe this is a groundless lawsuit. As it involves diffuse interests that are difficult to assess, we are not able to assess the amount involved in this lawsuit. In view of the remote chance of an unfavorable outcome and the impossibility of assessing the amount involved, we have not recognized any related provision.

Lawsuit for contract rescission
CIEN filed suit against us before the courts of Florianópolis, state of Santa Catarina, arguing the rescission and price adjustment of the agreement entered into with us. As of September 30, 2005, the amount of this claim was R$10.6 million.

As of September 30, 2005, we recognized provisions for civil and environmental lawsuits with probable risk of loss in the amount of R$44.6 million.

Labor
At the judicial level, as of September 30, 2005, there are approximately 511 labor claims in progress, of which 96 are in pre-hearing trial and have not yet been judged on trial court, 239 are pending decision on any appeals filed, and 176 are already in the enforcement phase, due to the final decision condemning us. Out of the total labor claims filed against us, 33.1% are related to the period prior to the privatization process and were under our responsibility, in accordance with Eletrosul spin-off criteria and subsequent privatization of Gerasul.

Of the 511 labor claims currently pending, 260 are claims filed by former employees, two by unions, and 249 by outsourced employees. Major claims in individual actions relate to recognition of labor relationship, overtime pay, subsidiary responsibility, adjustments of retirement payments and adjustments of the pension plans. Major claims in union actions relate to payments for salary adjustments as a result of the implementation of new economic plans by the Brazilian government and penalty fees in relation to the delay on payments. In both union claims the court has entered judgment in our favor but a final decision on this matter is still pending.

As of September 30, 2005, our potential labor liabilities amounted to R$41.3 million. Of this total amount, R$20.9 million are related to claims where the loss is probable, R$8.9 million are related to possible losses and R$11.5 million are related to claims where the risk of loss is remote. As per the analysis of our legal consultants, there are no individual labor lawsuits in excess of R$1.0 million. As of September 30, 2005, the related provision amounts for these judicial actions is R$20.9 million, representing the total estimated amount to cover losses arising from labor claims which are considered a ‘‘probable’’ loss. Of this amount, R$17.8 million are currently in a judicial escrow account.

Currently there is an investigative procedure against us that has been filed by the Federal Public Office on July 1, 2005 (*Ministério Público do Trabalho da 12 Região*) related to a labor claim filed by employees of a company that has an outsource agreement with us. According to our legal consultants such procedure does not represent any liability to us.

Management

Under our by-laws and the Brazilian corporation law, we are managed by our board of directors (*Conselho de Administração*) that consists of seven members and by our board of executive officers (*Diretoria*) which constitutes our senior management, consisting of six members.

There is no family relationship between any of the managers or between any manager and us or any manager and our controlling shareholder. There is no contract or material obligation between our management and us.

In addition to our board of directors and our board of executive officers, we have a fiscal board and a strategic committee. Our fiscal board is not permanent and is composed of up to five members. Our strategic committee consists of up to seven members (that may be shareholders), elected by our board of directors. The principal responsibility of our strategic committee is to give advice to our board of directors and board of executive officers principal on matters that are submitted for its consideration.

Board of directors

Our board of directors is responsible for establishing our long-term strategies and setting our general business policies and guidelines. Our board of directors is composed of seven members, who are elected by our shareholders at our annual shareholders' meeting. One of the members of our board of directors is elected by our employees in accordance with the rules for the privatization of Gerasul (*Edital de Privatização da Gerasul*), PND-0001/98/Gerasul.

The members of our board of directors are elected for a one year term, reelection being permitted. Our bylaws provide that if a board position becomes vacant, a substitute member shall be appointed by the other board members and he/she shall remain in his/her position until the next shareholders' meeting.

The members of our board of directors meet every three months, or as may be necessary under special circumstances, as called by the president of the board or by at least one-third of its members. The responsibilities of our board of directors include, among others, setting our general business policies and guidelines, electing the members of our board of executive officers, establishing their responsibilities and supervising our management.

The current members of our board of directors were elected on our annual shareholders' meeting dated as of April 12, 2004, with term of office expiring April 4, 2007. Their names, titles, dates of appointment and term of office are presented in the following table:

Director	Title	Election Date	Term of office
Maurício Stolle Bähr	Chairman of the Board	4/12/2004	4/12/2007
Jan Franciscus Maria Flachet	Vice Chairman	4/12/2004	4/12/2007
Manoel Arlindo Zaroni Torres	Director	4/12/2004	4/12/2007
Victor Frank de Paula Rosa Paranhos	Director	4/12/2004	4/12/2007
Dirk Beeuwsaert	Director	4/12/2004	4/12/2007
Nicolas Alain Marie Tissot	Director	4/12/2004	4/12/2007
Luiz Antônio Barbosa	Director	4/12/2004	4/12/2007

The term of office of our board members will be changed to one year in our annual shareholders' meeting to be held in April 2006 in order to conform the provisions of our bylaws to the requirements of the *Novo Mercado* Regulations.

Executive officers

On September 30, 2005, our board of executive officers was composed of six members. The members of our board of executive officers are elected by our board of directors for a term of three years, reelection being permitted.

Our chief executive officer, or any two executive officers acting jointly, may call meetings of our management. The meetings of our executive officers must take place at least once every month and a special meeting may be called whenever the company business so requires. No prior call notice is required if all board members are present at the meeting.

The executive officers are responsible for the day-to-day management of our business and implementing the resolutions of our board of directors.

The composition of our board of executive officers, as from September 30, 2005, is presented in the following table:

Officer	Title	Election Date	Term of office
Manoel Arlindo Zaroni Torres	CEO	4/30/2004	4/30/2007
Marco Antonio Amaral Sureck....	Planning and Controlling Officer	4/30/2004	4/30/2007
José Carlos Cauduro Minuzzo	Energy Production Officer	4/30/2004	4/30/2007
Marc Jacques Zelie Verstraete	Financial and Investor Relations Officer	4/30/2004	4/30/2007
Miroel Makiolke Wolowski.....	Trading and Business Officer and Project Implementation Officer	4/30/2004	4/30/2007
Luciano Flávio Andriani	Administrative Officer	4/30/2004	4/30/2007

Fiscal board

According to the Brazilian corporation law, the fiscal board is an independent management body from the company and external auditors. The fiscal board is not a permanent body and it can be composed by 3 to 5 members. Its main responsibilities are to opine on our financial statements and review our management's actions. The Brazilian corporation law requires that the fiscal board members shall receive remuneration not lower than 10% of the average remuneration of the board of directors, not including benefits, entertainment allowances and profit sharing.

Individuals who are members of other management bodies of the company and employees or employees of a subsidiary or the same group, or a spouse or relative of our administrators may not be elected to the fiscal board.

Our fiscal board is composed by three members, one of them elected by our minority shareholders. The meetings of our fiscal board take place every three month to analyze and approve annual and quarterly financial statements. Our fiscal board was in force as of September 30, 2005. The composition of fiscal board as from such date is presented in the following table:

Member	Title	Election Date	Term of Office
Newton de Lima Azevedo Junior	President	4/7/2005	4/7/2006
Carla Carvalho de Carvalho.....	Secretary	4/7/2005	4/7/2006
Manoel Eduardo Lima Lopes.....	Board Member	4/7/2005	4/7/2006
Manoel Eduardo Bouzan de Almeida	Deputy	4/7/2005	4/7/2006
Flávio Marques Lisboa Campos.....	Deputy	4/7/2005	4/7/2006
Ailton Pinto Siqueira	Deputy	4/7/2005	4/7/2006

Strategic committee

Our strategic committee is composed of seven members (who may be shareholders), resident or non residents of Brazil. The members of our strategic committee are elected by our board of directors. Our strategic committee is a consulting body and its responsibilities are to opine and advise the board of directors in such matters that are submitted to its opinion. The members of our strategic committee are elected for an indefinite period of time and its functioning is oriented by our internal regulation policies. The composition of our strategic committee as from September 30, 2005, is presented in the following table:

Member	Election Date
Nicolas Alain Marie Tissot	5/28/2004
Manoel Colcombet	1/18/2001
Maurício Stolle Bähr	6/25/1999
Jan Franciscus Maria Flachet	4/25/2003
Victor Frank de Paula Rosa Paranhos	6/25/1999
Dirk Beeuwsaert	3/15/2001
Manoel Arlindo Zaroni Torres	4/12/2004

Biographic information of our management

Below are the biographic information of the current members of our board of directors, fiscal board and board of executive officers.

Board of directors

Maurício Stolle Bähr. Mr. Maurício Stolle Bähr is a mechanical engineer graduated from Universidade Gama Filho, Rio de Janeiro, and a system analyst graduated from Pontifícia Universidade Católica do Rio de Janeiro. He holds master's degrees in Business Administration (MBA) from Universidade Federal do Rio de Janeiro and in Corporate Finance from Berkeley University (USA). He was the financial director of Serra da Mesa Energia S.A. in 1997, the financial director of Nacional Energética S.A. between 1994 and 1997, and also a member of the Board of Directors of Iven S.A. from 1996 to 1997. He is currently the chairman of our board of directors, the CEO of Suez Energy Brasil, a director of SESA, and the general representative of the Suez Group in Brazil.

Jan Franciscus Maria Flachet. Mr. Jan Franciscus Maria Flachet is an electro-mechanical engineer. He graduated from the Catholic University of Louvain, holds a master's degree in Business Administration from Instituto de Administração e Gestão da UCL, and attended the CEDEP, General Management Program associated to INSEAD in Fontainebleau. He developed a number of activities in the operation and development areas of the Tractebel group companies, having started his career in 1979 at Unerg as the head of the Operations department in Brabant. From 1990 to 1996, Mr. Flachet worked for Electrabel as the general electricity distribution manager for the Flemish municipalities surrounding Brussels. In 1996, he took office as the general manager of Litoral Gas in Argentina, and in 1999 he started to act as the senior vice-president of Distribution and Trading Operations at SESA. In 2001, he took office as the executive vice-president of Business Development in South America. He is currently the Vice-Chairman of our board of directors and regional manager of the Tractebel group in South America.

Manoel Arlindo Zaroni Torres. Mr. Manoel Arlindo Zaroni Torres is an electrician engineer graduated from Escola Federal de Engenharia de Itajubá. He attended the CEDEP, General Management Program associated with INSEAD in Fontainebleau. He was the head of the Transmission Division of Ivaiporã in Furnas, being in charge of the Production Department in the state of Paraná

and, subsequently, the South Production Superintendent. From 1992 on he worked as the Superintendent of Furnas System Operations, being in charge of activities related to the trading of energy. He was the Furnas representative at GCOI—Coordinating Group for Interconnected Operations, at the Joint Commission for Itaipu Power Plant Operation, and at COESE, the Committee for Operations of the Eletrobrás System Companies, as the coordinator of the Operation Subcommittee. He is currently our CEO and a member of our board of directors.

Victor Frank de Paula Rosa Paranhos. Mr. Victor Frank de Paula Rosa Paranhos is a mechanical engineer graduated from Universidade Católica de Petrópolis, and also holds bachelor's degrees in Economics from Instituto Metodista Bennett, and in Actuary Sciences from Sociedade Universitária Augusto Motta—SUAM. He was a resident engineer at Sociedade Técnica de Engenharia e Representação—STER, a director at Corretora de Títulos e Valores Mobiliários Paulo Williansems, the managing director of Montreal Bank's pension fund area, of Banco Nacional, and President of Nacional Energética S.A. (responsible for the construction of Serra da Mesa hydroelectric plant). He acted as the CEO of CEM, the company responsible for the construction of the Cana Brava hydroelectric plant through June 2002. He is currently a member of our board of directors.

Dirk Beeuwsaert. Mr. Dirk Beeuwsaert is a mechanical and electrician engineer graduated from University of Gent. He attended the CEDEP, Management Program, in Fontainebleau, France. He was a member of the Executive Board of Tractebel Societè Anonyme, a member of the Strategic Committee of Electrabel Societè Anonyme, a member of the Board of Directors and President of Tractebel Inc., a member of the Board of Directors of Tractebel North America, a director of Thai Cogeneration Co., Nong Khae Cogeneration Co., and of Samutprakarn Cogeneration Co. He took part, as a member, in the Board of Vlerick Management School Leuven-Gent, the Council of Advisors of University of Gent, and the Board of the Faculty of Applied Sciences. He is currently the President of Suez Energy International and a member of our board of directors.

Nicolas Alain Marie Tissot. Mr. Nicolas Alain Marie Tissot is an economist graduated from the High Commercial School. Between 1995 and 1999 he worked as an auditor and senior advisor for the Ministry of Economy, Finance and Industry of France. He joined the Suez Group in June 1999, and between June 2000 and August 2003 Mr. Tissot managed the business control department. In September 2003 he started to act as the Financial Director of Tractebel Electricity & Gás International. He is currently also a member of our board of directors.

Luiz Antônio Barbosa. Mr. Luiz Antônio Barbosa is a power plant maintenance technician and a member of our board of directors, elected by its employees. He was a director of Eletrosul Employees Association, a delegate of the Eletrosul Professionals Association, and has been the Financial Director of the Electricians' Trade Union of the Southern Region of the State of Santa Catarina (SINTRESC) since 1993.

Executive officers

Manoel Arlindo Zaroni Torres. Mr. Torres is currently our CEO. For the biographical information of Mr. Manoel Arlindo Zaroni Torres, see item ''Board of Directors'' in this ''Management'' section.

Marco Antonio Amaral Sureck. Mr. Marco Antonio Amaral Sureck is an electric engineer graduated from Universidade Federal do Paraná, holds a master's degree in Production Engineering from Universidade Federal de SC—UFSC and is an expert in Electric Systems Expansion and Operation Planning from University of Waterloo—Canada. He worked for Eletrosul from 1982 to 1997, acting as Energy Planning Engineer and was manager of the Energy Planning Division and of the Generation, Transmission, and Telecommunications Planning Department. At Gerasul he worked from 1998 to 2002 as manager of the Energy Operation and Trading Planning area. He took part in bidding processes (Itá and Machadinho hydroelectric plants, and interconnection with Argentina), in the

restructuring of the electricity sector, in the Expansion Planning Coordinating Group (GCPS), and was a representative of the MAE (Wholesale Energy Market) Technical Committee in the establishment of market rules. He is currently our Planning and Control Officer.

José Carlos Cauduro Minuzzo. Mr. José Carlos Cauduro Minuzzo is a mechanical engineer graduated from Pontifícia Universidade Católica of Rio Grande do Sul. He started his professional career at Eletrosul in 1976, having worked in the Thermoelectricity Generation area in the Jorge Lacerda Thermoelectricity Complex. He was an intern at the steam turbine plant of Ansaldo e Skoda in 1984 and at the Nei Parsons plant in 1987. He took part in the maintenance group of the Instituto Brasileiro de Petróleo—IBP from 1981 to 1987, and in the thermoelectric plant maintenance group of GCOI from 1986 to 1998, acting as the group coordinator from 1994 to 1998. He managed the Engineering and thermoelectric plant Maintenance Division through 1997 and, subsequently, the Thermoelectricity Generation Department through June 1999. He is currently our Energy Production Officer.

Marc Jacques Zelie Verstraete. Mr. Marc Jacques Zelie Verstraete is graduated in Economics and Applied Economics from the Catholic University of Louvain, and a commercial engineer graduated from Catholic University of Louvain. He holds a master's degree in Business Management from International University of America. He was a financial advisor at ING Bank—Belgium and a senior financial advisor at Suez Tractebel Sociètè Anonyme (Belgium). He is currently our Financial and Investor Relations Officer.

Miroel Makiolke Wolowski. Mr. Miroel Makiolke Wolowski is an electric engineer graduated from Universidade Federal de Santa Catarina—UFSC and a business administrator from Escola de Administração de Santa Catarina—ESAG. He is post-graduate in Public Administration from ESAG. He was a project engineer at Ericsson do Brasil and production manager at Intelbrás. At Eletrosul he acted as an engineer, working in the acquisition of power plants and large equipment area, including preparing the public notices related to Jacuí and Corumbá thermoelectric plants.

At Gerasul he worked at the business development area through December 2000. He is currently our Trading and Business Director and Project Implementation Director.

Luciano Flávio Andriani. Mr. Luciano Flávio Andriani is a business administrator graduated from Universidade Federal de Santa Catarina—UFSC and is a post-graduate in International Development and Cooperation Management from Universidade Moderna de Lisboa. At Eletrosul, he was an Organization and Methods Analyst, manager of the Equity, Documentation, Transportation and Services Department, and Human Resources Manager. Mr. Andriani was subsequently the Human Resources and Information Technology manager of Gerasul. He is currently our Administrative Officer.

Fiscal board

Newton de Lima Azevedo Júnior. Mr. Newton de Lima Azevedo Júnior is a civil engineer graduated from Escola Politécnica of Universidade de São Paulo in 1972. He worked for Themag Engenharia from 1972 to 1991, acting as the General Director of the Itaipu Project from 1978 to 1991. Between 1992 and 1999, he was the CEO of Estudos Técnicos e Projetos ETEP Ltda and a director at ABCE, the Brazilian Association of Engineering Advisors. From 1999 to 2002 Mr. Azevedo was the CEO of Lyonnaise dês Eaux do Brasil. Between 2001 and 2003 he was the CEO of Águas do Amazonas (the private water and sewage concessionaire of the city of Manaus). He is currently the CEO of Degrémont Brasil, Vice-President of Degrémont América do Sul and Vice-President of ABDIB, being in charge of the sanitation area. He is an incumbent member of our fiscal board.

Carla Carvalho de Carvalho. Mrs. Carla Carvalho de Carvalho holds a bachelor's degree in Law from the Universidade Federal Fluminense—UFF and is a post-graduate in Tax Law from Universidade Estácio de Sá. She holds an Executive MBA from COPPEAD-UFRJ and is post-graduate in Civil Law from Escola Superior de Advocacia, associated to the OAB, the Brazilian Bar Association—Rio de Janeiro Section. She worked for Banco Nacional from April 1991 to May 1995 as a Senior Lawyer. Between May 1995 and April 1996, she worked at Banco Boavista as a Tax Manager. In 1997 she was a Legal Advisor for Serra da Mesa Energia S.A., where she remained through February 1998. In February 1998 she took office as the Legal Coordinator of Suez Energy Brasil, where she is now working. She is an incumbent member of our fiscal board.

Manoel Eduardo Lima Lopes. Mr. Manoel Eduardo Lima Lopes holds bachelor's degrees in Accounting and Law from Universidade do Estado do Rio de Janeiro. He worked at Banco do Estado do Rio de Janeiro S.A.—BANERJ from 1979 to 1981, acting as a General Auditor, and from 1981 to 1990 as a Control Superintendent. Between 1990 and 1996, Mr. Lopes acted as an advisor for Banco Clássico, having been appointed Director for the 1996-1998 period. In 1998 he took office of the Control Management of IRB—Brasil Resseguros S.A., where he remained through 2001. He is currently a Director at Banco Clássico and a retired employee of Banco do Estado do Rio de Janeiro S.A.—BANERJ. He is an incumbent member of our fiscal board.

The company's address of the members of the Board of Directors, Executive Board, Fiscal Board and Strategic Committee is the address of our executive office.

Executive compensation

In accordance with Brazilian corporate Law, our shareholders are responsible for determining the aggregate compensation to be paid to the members of the board of directors, fiscal board, and the executive board, the board of directors will determine the compensation levels for each member of the board of directors, fiscal board, and executive board based on the total previously fixed amount.

For the year ended December 31, 2004, the overall compensation paid to the members of our board of directors and executive board was R$8.0 million, including social security contribution, severance pay fund, health insurance, private pension plan, health care, and housing.

For 2005, our shareholders' meeting held on April 7, 2005 determined the overall annual compensation payable to the members of our board of directors and executive board at R$8.8 million, including social security contribution, severance pay fund, health insurance, private pension plan, health care, and housing.

As of September 30, 2005, there were no agreements of any nature or other significant obligations between us and members of the executive board and the board of directors, who held, at said date, any direct or indirect interest over 1% in our capital stock.

As of September 30, 2005, we did not have stock option plans for members of our management.

Principal and selling shareholder

Principal Shareholders

The table below shows information related to our principal shareholders as of September 30, 2005. Percentages included in the table are based on the 652,742,192 common shares outstanding before and after the offering:

	Common shares before Offering		Common shares after Offering[1]	
Shareholder	**Shares**	**%**	**Shares**	**%**
Suez Energy South America Participações Ltda.	511,130,462	78.31	456,130,462	69.88
Banco Clássico	65,268,744	10.00	65,268,744	10.00
BNDES Participações S.A.-BNDESPAR	36,666,193	5.62	20,666,193	3.17
Brazilian government	12,425,102	1.90	12,425,102	1.90
Banco Nordeste do Brasil S.A.	2,457,918	0.38	2,457,918	0.38
National Development Fund (FND)	2,362,827	0.36	2,362,827	0.36
Board members as a group	606	—	606	—
Others	22,430,340	3.43	93,430,340	14.31
Total	652,742,192	100.00	652,742,192	100.00

(1) Assumes that the agents do not exercise the over-allotment option to purchase up to an additional 9,900,000 common shares.

We present below a description of shareholders holding over 5% of our common shares:

SESA

The selling shareholder in this offering is Suez Energy South America Participações Ltda, or SESA, our controlling shareholder. SESA is a Suez Group company, through which the Suez Group carries out investments in Brazil in the power industry. The Suez Group provides the following public services, sometimes operating as a partner to the public administration other times individually: (i) electricity, (ii) gas, (iii) energy, (iv) water, and (v) garbage management. In South America, the Suez Group operates in Peru, Chile, Argentina, and Brazil.

The history of the Suez Group in Brazil goes back 50 years, with a project to restructure the water services in Rio de Janeiro. It currently controls our company which is the largest private electricity generation company in the country, with approximately 7.5% of the country's power generating facility. Including water and garbage services provided, in Brazil the Suez Group employs approximately 14,000 employees and partners, generating revenues of approximately €1.0 billion. In Brazil, in addition to controlling our company, SESA holds 100% interest in Companhia Energética São Salvador and 30% in the Estreito Energia Consortium.

Banco Clássico

Banco Clássico S.A. has operated in the Brazilian market for 15 years. Its operations are focused on financing and investing in the power industry, with a significant participation in the capital stock of our company and Petrobrás. On August 31, 2005, Banco Clássico had a net worth of R$1.5 billion.

BNDESPAR

BNDES Participações S.A.—BNDESPAR is a wholly owned subsidiary of BNDES, Bank for Economic and Social Development, one of the largest development banks in Latin America, with a budget of R$60.8 billion for 2005.

BNDESPAR was incorporated by BNDES to participate in the Brazilian capital markets, by purchasing interests in companies deemed strategic for the development of the country.

BNDESPAR is offering 16,000,000 common shares only in Brazil to Brazilian investors pursuant to a separate offering document in Portuguese distributed exclusively in Brazil.

Shareholders' Agreements

As of September 30, 2005, there were no agreements entered into between our shareholders filed with us.

Related-party transactions

Suez Tractebel

On May 2, 2002, we entered into a consulting service agreement with Suez Tractebel, our indirect controlling company, with executive offices in Brussels, Belgium, for consulting services on specific matters. The agreement will be in effect for 36 months, and its renewal is conditioned on approval of our minority shareholders, every 12 months, at a general shareholders' meeting called for such purpose. The validity of this agreement was conditioned on ANEEL's approval, issued on April 23, 2003 by means of Notice No. 526/2003-SFF/ANEEL. The fees for services rendered are limited to the annual non-cumulative amount of €1.5 million, and services performed and respective fees paid are reported to our fiscal board. The first renewal, approved by our minority shareholders, took place at the special shareholders' meeting held on April 12, 2004. Said agreement was not renewed at the special shareholders' meeting held on April 7, 2005. In the year ended December 31, 2004, we paid R$5.3 million to Suez Tractebel in respect of this agreement.

Itasa

We and other Itasa shareholders are intervening parties in agreements entered into by and between Itasa and its lenders, linked to the construction of the Itá hydroelectric plant. Itasa's and our shareholders pledged the total amount of their shareholding in Itasa to secure this agreement. As of September 30, 2005, the debt due by Itasa totaled R$284.3 million. As collateral for obligations arising from the aforementioned agreements, Itasa granted the following (a) pledge of rights arising from the concession for exploitation of the Itá hydroelectric plant; and (b) pledge of credit rights arising from energy purchase agreements entered into with its shareholders.

Companhia Energética Meridional—CEM

We are party to the Agreement for Subscription and Payment of Debentures not Convertible into Shares No. 98.2.654.3.1 and in the Loan Agreement through Line of Credit No. 98.2.654.3.3, entered into between CEM and BNDES, dated May 19, 1999 and April 5, 2000, with the former being amended May 25, 1999. Under the terms of such contracts entered into with BNDES, we assumed the following obligations: (i) ensure the acceleration of payment in the following cases: (a) termination of concession due to a reason attributable to CEM, to the intervening parties or its subsidiaries, affiliates or controlling companies; and (b) execution of an agreement with the concession authority by CEM, any intervening parties or any of its subsidiaries, affiliates or controlling companies, with the purpose of terminating the concession; and (ii) assigning to BNDES any amounts arising from the indemnity received in view of the termination of the concession of the Cana Brava hydroelectric plant by the concession authority.

This loan agreement is intended to provide funds for construction of the Cana Brava hydroelectric plant. An amortization of the principal amount is over 117 monthly installments, with the first installment on July 15, 2003 and the last one on April 15, 2013, at the rate of 4.0% per year above the Brazilian long-term interest rate, the so-called TJLP, publicized by the Central Bank, to be made in quarterly installments starting at the agreement execution date through July 15, 2003, and in monthly installments starting July 15, 2003 inclusive, together with the principal amortization installments. As of September 30, 2005, the amounts outstanding under this loan agreement were R$110.2 million.

The purpose of the Agreement for Subscription and Payment of Debentures Not Convertible into Shares is to fund the construction of UHE Cana Brava. This agreement provides for the payment of the principal amount on April 1, 2013 and interest to be paid semi-annually, as from October 1, 2003

until April 1, 2003 at the rate of 4% over TJLP. As of September 30, 2005, the amounts outstanding under this loan agreement were R$99.1 million.

In guarantee for CEM's obligations under these loan agreements, the following was granted in favor of BNDES: (i) assignment, by CEM, of credit rights (receivables) arising from Cana Brava hydroelectric plant, including credit rights related to the generation and trading of electricity from Cana Brava hydroelectric plant, (ii) assignment, by CEM, of its rights to receive any and all amounts which, effectively or potentially, are or will become payable and pending payment, by the concession authority to CEM, pursuant to its Concession Contract, and (iii) pledge, by us, of our total shares held at CEM.

Additionally, we are the purchaser of all the electricity generated by Cana Brava hydroelectric plant, pursuant to the Second Amendment and Consolidation to the Energy Purchase Base Agreement entered into on August 2, 2002 between us and CEM. In order to ensure its obligations under this agreement, we obtained a letter of guarantee with Banco Bradesco S.A., in the maximum amount of R$74.9 million, with CEM as the beneficiary, and said bank guarantee was assigned and transferred to BNDES.

Lages Bioenergética

We are the intervening guarantor in the Credit Line Agreement entered into between Lages Bioenergética and Banco Regional de Desenvolvimento do Extremo Sul—BRDE, dated as of July 25, 2003, and we have pledged our interest held in the capital stock of Lages Bioenergética in guarantee of the settlement of Lages' obligations thereunder. As of September 30, 2005, said debt totaled R$45.9 million. In order to ensure the payment of obligations arising from said agreement, Lages Bioenergética assigned its receivables arising from the trading of electricity from Lages Co-generation unit, in addition to granting, by means of a chattel mortgage, the assets purchase with funds from said loan.

Description of capital stock

The following is a summary of certain significant provisions of our by-laws, the Brazilian corporation law and the rules and regulations of the CVM. This description does not purport to be complete and is qualified by reference to our by-laws, the Brazilian corporation law and the rules and regulations of the CVM. In Brazil, by-laws (estatuto social) are the principal governing document of a corporation (sociedade por ações). As long as we are listed in Novo Mercado, we may not issue preferred shares. Accordingly, this section does not discuss the Brazilian statutory rights conferred upon holders of preferred shares. In order to de-list from the Novo Mercado, a company is required to conduct a public offering for the purchase of our common shares. See "—De-listing from the Novo Mercado."

General

We are a publicly-held corporation, incorporated under the laws of Brazil and registered with the Brazilian Securities Commission, or CVM, as from May 28, 1998, under No. 017329. Our headquarters is located in the State of Santa Catarina, city of Florianopilis, Brazil.

Share capital

As of September 30, 2005, our capital stock (totally subscribed and paid for) was R$2,445,766,091.90, represented by 652,742,192 outstanding common shares, all nominal and without par value. Our by-laws authorize our board of directors to increase our capital stock to a maximum of R$5,000,000,000.00, irrespective of any amendment to our by-laws. Any capital increase in excess of this authorized limit is subject to approval by our shareholders. According to the *Novo Mercado* regulations we may not issue preferred shares or beneficiary parts (*partes beneficiárias*).

Corporate purpose

Our corporate purpose is to:

- carry out studies, projects, construction and operation of electricity generating power plants, or perform trading in relation to these activities;
- take part in researches of interest to the energy sector, in connection with the electricity generation and distribution, as well as studies for utilization of reservoirs for multiple purposes;
- contribute to the development of technical staff needed for the electricity and training of qualified workers, by means of specialized courses;
- take part in entities intended for the operational coordination of interconnected power systems;
- take part in international, national or regional technical, scientific and business associations or organizations, of interest to the electricity sector;
- contribute for the preservation of the environment upon carrying out our activities;
- contribute to programs related to the development and incentives to the Brazilian industry of materials and equipment for the electricity and for its technical regulation, standardization and quality control; and
- participate in other businesses and enterprises that carry out operations similar to our own, as shareholders, quotaholders or partners, in Brazil or abroad.

Rights of common shares

Our share capital is composed of one class of common shares. Each of our common shares entitles its holder to one vote in resolutions at our annual and special shareholders meetings. Holders of our common shares are entitled to dividends, or other distributions made to shareholders. In addition, holders of our common shares are not required to subscribe future capital increases. The investors who acquire shares in this offering will be entitled to receive dividends which were declared after the acquisition of their shares. According to the *Novo Mercado* regulation, our common shares have tag-along rights, which enable their holders to, upon the sale of a controlling in interest in us, receive 100% of the price paid per common share of the controlling block.

Rights of the shareholders

According to the Brazilian corporation law, neither a company's by-laws nor actions taken at a shareholders meeting may deprive a shareholder of certain specific rights, including the following:

- the right to participate in the distribution of profits;
- the right to participate, in the proportion of the holder's share of our capital stock, in the distribution of any remaining assets in the event of the liquidation of our company;
- preemptive rights in the event of subscription of shares, convertible debentures or subscription warrants, except in certain specific circumstances under Brazilian law;
- the right to inspect, in accordance with the Brazilian corporation law, the company's business and management; and
- the right to withdraw from the corporation, in the cases provided for in the Brazilian corporation law, including (i) merger or consolidation (*fusão ou incorporação*); (ii) spin-off; and (ii) changes in rights and preferences of preferred shares.

Share grouping

On April 7, 2005, our shareholders' meeting approved the grouping of all of our shares, in the ratio of 1,000 shares for 1 share of the same type and class, and of 5 shares for 1 ADR. The share grouping was approved with the purpose to standardize the quotation unit for the shares in the international and domestic markets and did not have any impact on the total amount of the capital stock.

Conversion of the preferred shares into common shares

In the shareholders' meeting for the holders of class A and B preferred shares, held on August 17, 2005 and June 27, 2005, respectively, the holders of class A and B preferred shares approved the conversion of their preferred shares into common shares, in the ratio of 1:1. As a result, our capital stock is now composed solely by 652,742,192 common shares.

The purpose for the conversion of the preferred shares into common shares was to, among other things, (i) equalize the rights of the shares; (ii) adapt our corporate structure to higher corporate governance standards; and (iii) to provide liquidity to our shares.

No preferred shareholder has exercised its withdrawal rights due to such conversion of preferred shares into common shares.

Stock options

Until the date of this Offering memorandum, we have no stock option plans in effect.

Shareholders' meetings

At shareholders meetings, our shareholders are authorized to take any action relating to our corporate purpose and to pass such resolutions as they deem necessary. It is the sole responsibility of our shareholders, at the annual shareholders meeting, to analyze, discuss and approve our financial statements and to determine the allocation of the net income and the distribution of dividends relating to the immediately preceding fiscal year. The election of directors and members of the fiscal board *(Conselho Fiscal)* typically takes place at the annual shareholders' meeting, although under Brazilian law it may also occur on certain occasions at a special shareholders' meeting. A shareholders' meeting may be held concurrently with the annual shareholders' meeting.

The following actions, among others, shall be taken solely at shareholders' meetings:

- amendment of our by-laws;
- approval of any transformation of corporate type;
- issuance of debentures (except for common debentures, not convertible into shares, and without *in rem* guarantees which can be issued if approved by our board of directors);
- acceptance or rejection of the valuation of in-kind contributions offered by a shareholder in consideration for common shares;
- de-listing from CVM as a publicly held corporation;
- suspension of the rights of a shareholder who has violated the Brazilian corporation law or our bylaws;
- our merger or spin-off;
- delisting from *Novo Mercado*, as well as appointment of a financial institution responsible for our valuation, in the event that a tender offer for our common shares is carried out in connection with the de-listing of our shares, or de-listing from the *Novo Mercado;*
- approval of any dissolution or liquidation, the appointment and dismissal of the respective liquidator and the official review of the reports prepared by him or her; and
- authorization to petition for bankruptcy or request the judicial or extra-judicial rescheduling of our debts.

Quorum

As a general rule, Brazilian corporation law provides that a quorum for purposes of a shareholders' meeting consists of shareholders representing no less than 25% of a company's issued and outstanding capital on the first call and, if that quorum is not reached, any percentage on the second call. A quorum for purposes of amending our by-laws consists of shareholders representing at least two-thirds of our issued and outstanding capital on the first call and any percentage on the second call.

A shareholder may be represented in a shareholders meeting by an attorney-in-fact appointed no more than one year as from the date of the relevant shareholders meeting. The attorney-in-fact must be a shareholder, manager of the company, lawyer or a financial institution.

As a general rule, the affirmative vote of shareholders representing at least the majority of our issued and outstanding common shares is required to ratify any proposed action, with abstentions not taken

into account. However, the affirmative vote of shareholders representing at least 50% of our issued and outstanding voting capital is required to:

- change our corporate purpose;
- approve the creation of preferred shares;
- reduce the mandatory dividend;
- our consolidation or merger with another company;
- spin-off;
- approve our participation in a group of companies (as defined in the Brazilian corporation law);
- cancel any liquidation; and
- approve our dissolution.

Who may call a shareholders meeting

In addition to our board of directors, shareholders' meetings may also be called by:

- any shareholder, if our directors fail to call a shareholders' meeting within 60 days after the date they were required to do so under the applicable laws and our by-laws;
- shareholders owning at least five percent of our capital stock, if our directors fail to call a meeting within eight days after receipt of a request to call the meeting by shareholders, indicating the proposed agenda;
- shareholders holding at least five percent of our capital stock, if our directors fail to call a meeting within eight days after receipt of a request to call the meeting to convene the fiscal board;
- our fiscal board, if one is in place, if the board of directors delays calling an annual shareholders meeting for more than one month. The fiscal board may also call a special shareholders meeting at any time, if it believes that there are important or urgent matters to be addressed; and
- the president of our board of directors in two days as from BOVESPA determines that the quotations for our securities be issued separately from securities of other companies or if trading in our securities are suspended from *Novo Mercado* due to the non-compliance of our obligations under the *Novo Mercado* regulation. This shareholders' meeting will be called in order to replace all the members of the board of directors.

Conditions of admission to a shareholders' meeting

In order to attend a shareholders meeting, our shareholders must prove their ownership of common shares by presenting proof of deposit, issued by the financial institution responsible for the bookkeeping of our shares, issued no later than 72 hours prior to the shareholders meeting and by presenting his/her identity card. A shareholder may be represented at a shareholders meeting by proxy, as long as the proxy is appointed less than one year before the meeting. A proxy must be a shareholder, officer of our company, a lawyer or a financial institution. Investment funds must be represented by its manager.

Board of directors

Election of directors

Our by-laws require that our board of directors consist of a minimum of five and a maximum of seven directors. Our board members are elected by our shareholders in the annual shareholders' meeting for a period of one year, reelection being permitted. Pursuant to the Brazilian corporation law each

member of our board of directors has to own at least one share of our company. In addition, pursuant to the Brazilian corporation law the number of board members may only be superior to seven if separate deliberations are requested, as provided for in article 141, paragraph 4° of the Brazilian corporation law and if election of our board of directors is conducted through cumulative voting. Pursuant to the Brazilian corporation law, should this occur, shareholders bound by voting agreements representing more than 50% of our common shares would be entitled to select the same number of directors elected by our other shareholders plus one, regardless of the number of directors specified in our by-laws. The Brazilian corporation law permits the cumulative voting upon request of holders of at least 10% of our voting capital. Each share is granted as many votes as there are places to the board and the shareholder has the option to distribute his votes into one or many candidates.

CVM Ruling No. 282/98 allows for cumulative voting for directors at the request of less than 10% of the shareholders of the relevant corporation depending on the total amount of the capital stock.

If there is no request for cumulative voting, directors are elected by a majority of our issued and outstanding common shares present in person or represented by proxy at a shareholders' meeting, except that any shareholders that, individually or collectively, hold at least 15% of our common shares have the right to select one director and his or her alternate. If cumulative voting is requested, each shareholder may vote in one or more board members, and each common share will entitle its holder to one vote in the relevant shareholders' meeting, and such shareholders may distribute votes may between the members as they want.

Destination of net income and distribution of dividends

Below is a summary of the provisions of the Brazilian corporation law in respect to profit retention, reserves and the rules for distribution and payment of dividends and interest on shareholders' equity.

Calculation for the payment of mandatory dividends

At each annual shareholders' meeting, our board of directors is required to propose how our earnings for the preceding fiscal year are to be allocated. For purposes of the Brazilian corporation law, a company's income after federal income tax for a given fiscal year, net of any accumulated losses from prior fiscal years and amounts allocated to employees' and management's profit sharing, represents its ''net income'' for that fiscal year.

The Brazilian corporation law generally requires that the by-laws of each corporation specify a minimum percentage of the amounts available for distribution by such corporation that must be distributed to shareholders as dividends for each fiscal year. The mandatory distribution is based on a percentage of adjusted net income and cannot be lower as from the last amendment to our by-laws, dated November 9, 2005, our mandatory divided became 30% and can be, reduced by amounts allocated to the legal reserve and contingencies reserve, if any, and increased by any reversions from contingencies reserve. The mandatory dividend may be restricted to the ''realized'' portion of our net income. Calculation of our net income and allocation of reserves for the preceding fiscal year is calculated under Brazilian GAAP and adjusted under the Brazilian corporation law. In addition, the Board of Directors may recommend to the shareholders the approval of distribution of dividends from other sources that according to the law are available for distribution.

The Brazilian corporation law permits the suspension of the mandatory distribution of dividends in any fiscal year in which the management reports to the shareholders' meeting that the distribution would be inadvisable due to the company's financial condition. The suspension is subject to approval at the shareholders' meeting and review by members of the corporation's fiscal board, if it is in place at the time. In the case of publicly-held corporations, the board of directors must file a justification for such suspension with the CVM. If the mandatory dividend is not paid and funds are available, those

funds must be attributed to a special reserve account. If not absorbed by subsequent losses, those funds must be paid out as dividends as soon as the financial condition of the company permits.

Payment of dividends

We are required by the Brazilian corporation law and by our by-laws to hold an annual shareholders' meetings no later than April 30 of each year, at which time the allocation of the results of the fiscal year and the distribution of an annual dividend are reviewed. The payment of annual dividends is based on our non-consolidated, audited financial statements prepared for the immediately preceding fiscal year.

Any holder of record of common shares at the time that a dividend is declared is entitled to receive dividends. Under the Brazilian corporation law, the annual dividend must be paid to shareholders within 60 days of its declaration, except when another date for payment, which must be a date prior to the closing of the fiscal year in which the dividend was declared, is set by the shareholders. Our bylaws do not provide that unclaimed dividends will accrue interest or be adjusted on account of inflation.

Our shareholders have a three-year period from the date the dividend or interest on shareholders' equity is made available to them to claim dividends or interest on shareholders' equity with respect to their common shares, after which the aggregate amount of any unclaimed dividends or interest on shareholders' equity legally reverts to us.

As a general rule, our shareholders not residents in Brazil must register themselves with the Central Bank in order to be able to remit abroad dividends, earnings from sale of their shares or other amounts related to their shares.

Any payment of dividends or distributions in currency will be made in *reais*. According to current Brazilian legislation, dividends paid to shareholders not resident in Brazil are not subject to withholding income tax.

Our board of directors may declare intermediate dividends based on the accrued profits or the profits allocated to our profit reserve accounts in our annual or semi-annual financial statements. In addition, our board of directors may declare dividends according to the net profit based on our semi-annual or quarterly balance sheet. Such interim dividends cannot exceed the amount of our capital reserves. The payment of interim dividends may be deducted from the amount of mandatory distributions relating to the net profit earned in the year in which the interim dividends were paid.

Interest on shareholders' equity

Since January 1, 1996, Brazilian companies have been authorized to pay interest on shareholders' equity to holders of equity securities, and to treat those payments as a deductible expense for purposes of calculating corporate income tax and, since 1998, also for purposes of the social contribution tax. Payment of such interest may be made at the discretion of our board of directors. The amount of the distribution is limited to the greater of: (i) 50% of net income (after the deduction of the provisions for social contribution on net profits but before taking into account the provision for income tax and the interest on shareholders' equity) for the period in respect of which the payment is made; and (ii) 50% of the sum of accrued profits and profit reserves as of the beginning of the year in respect of which the payment is made. Interest on shareholders' equity is limited to the daily (*pro rata die*) variation of the long-term interest rate—TJLP (*taxa de juros a longo prazo*). Our bylaws permit the payment of interest on shareholders' equity as an alternative for dividend distributions. The amount distributed to our shareholders as interest on shareholders' equity, net of any income tax, may be included as part of the mandatory dividend distribution.

Any payment of interest on shareholders' equity to the holders of our shares, whether or not they are Brazilian residents, is subject to a withholding tax at the rate of 15%. A 25% withholding tax rate is applied if the holder is a resident of a tax haven (*i.e.*, a country that does not charge income tax, or that charges income tax at a maximum applicable rate lower than 20% or where the local legislation imposes restrictions on the disclosure of the shareholding composition or title to the investment).

In accordance with applicable law, we are required to pay to shareholders an amount sufficient to ensure that the net amount they receive in respect of interest on shareholders' equity, after payment of any applicable withholding tax, plus the amount of declared dividends is at least equivalent to the mandatory dividend amount. When we pay interest on shareholders' equity and such payment is not accounted for as a portion of the mandatory dividends distribution, withholding income tax will be applicable. All payment of dividends made as of this date were accounted for as part of the mandatory dividend payments.

Dividend policy

We intend to pay dividends and interest on shareholders' equity as provided for in our bylaws and in the Brazilian corporation law. Our board of directors may approve the payment of dividends or interest on shareholders' equity, based on our semi-annual or quarterly financial statements. The payment of annual dividends, including dividends in excess of the mandatory dividends requires the approval of the holders of the majority of our common shares. The amount of any distribution will depend on many issues, including results of operations, financial condition, cash needs, projections and perspectives, and other issues considered relevant by our board of directors. As part of our tax planning, we may continue in the future to pay interest on shareholders' equity if such practice is found appropriate by us.

Payments to our shareholders for the years of 2004, 2003, 2002, 2001 and 2000 are shown below.

	For the year ended December 31,[1]				
	2004	2003	2002	2001	2000
	(R$ thousands, except per share data)				
Calculation of mandatory dividends					
Net income (loss) for the fiscal year	775,192	517,154	(183,521)	582,274	162,801
Legal reserve (5%)	(38,760)	(25,857)	—	(29,114)	(8,140)
Base for calculation of the mandatory dividends	736,432	491,297	—	553,160	154,661
Mandatory dividends	184,108	122,824	—	138,290	38,665
Proposed dividends/Interest in shareholders' equity					
Interest on Shareholders' Equity (net of withholding income tax)	216,750	198,900	—	68,820	—
Balance of the proposed dividends	482,032	257,297	—	96,300	136,799
Subtotal	698,782	456,197	—	165,120	—
Withholding income tax on shareholders' equity	38,250	35,100	—	11,180	—
Total	737,032	491,297	—	176,300	—
Dividends/interest in shareholders' equity before withholding income tax, by group of 1000 shares (R$):					
Class A preferred	0.920260	0.773822	—	0.345021	0.301852
Class B preferred	0.845321	0.698884	—	0.270083	0.226389
Common shares	1.070525	0.698884	—	0.270083	0.226689

(1) Information is presented per 1,000 shares. On May 23, 2005, we consummated a reverse stock split whereby our shareholders received one common share for each 1,000 shares previously outstanding.

Our board of directors approved the payment of interest on our share capital relating to results for the period from January 1 through May 31, 2005, in aggregate principal amount of R$110 million, corresponding to R$0.199740 per 1,000 class A preferred shares, R$0.168516 per 1,000 class B preferred shares and R$0.168516 for one thousand common shares. Payment for these dividends became effective on July 8, 2005. On May 23, 2005, we consummated a reverse stock split of our common shares pursuant to which our shareholders received one common share for each 1,000 common shares previously outstanding.

On October 19, 2005, we reported that our board of directors, in a meeting held on that date, approved the following matters: (i) credit of interest on shareholders' equity for the period from June 1 through November 10, 2005, in the aggregate principal amount of R$122 million, corresponding to R$0.186904 per share; (ii) distribution of interim dividends based on our financial statements dated June 30, 2005, in the amount of R$141 million, corresponding to R$0.216012 per share; and (iii) distribution of interim dividends, based on our profit reserve account as of December 31, 2004 (except for legal reserve), in the amount of R$147 million (included in the 2004 column of the table above), corresponding to R$0.225204 per share. Payments for such dividend distributions began on November 10, 2005.

In addition, on November 14, 2005 our board of directors approved the indicative minimum dividend distribution policy pursuant to which we will pay approximately 55% of our adjusted net income for each year, and that amount may be adjusted in accordance with Brazilian law.

Reserve accounts

According to the Brazilian corporation law, the amount to be distributed as dividends is the amount corresponding to our net income, minus any portions that should be accounted for as legal reserve and contingency reserve.

- ***Legal reserve.*** Pursuant to the Brazilian corporation law, we are required to maintain a legal reserve to which we must allocate five percent of our net profits for each fiscal year, until the aggregate amount of the reserve equals 20% of our capital stock. Nonetheless, we are not required to make allocations to the legal reserve in fiscal years in which the legal reserve, when added to our other existing capital reserves, exceeds 30% of our capital stock. Any net loss may be offset with amounts in the legal reserve. The amount of profits allocated to establishing the legal reserve must be approved by our shareholders at an annual shareholders' meeting. The legal reserve account is not available for the payment of dividends. On December 31, 2004, our legal reserve had a balance of R$102.25 million, corresponding to 4.2% of our capital stock.
- ***Unrealized profits reserve.*** Under the Brazilian corporation law, the amount by which the mandatory distribution exceeds the "realized" net income in a given fiscal year may be allocated to the unrealized profits reserve. The Brazilian corporation law defines "realized" net profits as the amount by which net profits exceed the sum of (1) net positive results, if any, from the equity method of accounting for earnings and losses of subsidiaries and certain affiliates; and (2) the profits, gains or returns that will be received by the company after the end of the subsequent fiscal year related to transactions already undertaken by us. Profits recorded in the unrealized profits reserve, if realized and not absorbed by losses in subsequent fiscal years, must be added to the first dividend distribution following the realization. On December 31, 2004, the balance of our unrealized profits reserve was zero.
- ***Contingency reserve.*** Pursuant to the Brazilian corporation law, a portion of our net profits may be allocated to a contingency reserve to offset the anticipated losses that are deemed probable in future fiscal years. Any amount so allocated in a previous fiscal year either must be reversed in the fiscal year in which the loss was anticipated, if the loss does not occur as projected, or must be cancelled and written-off if the anticipated loss actually occurs. On December 31, 2004, our contingency reserve had a balance of zero.
- ***Retained profits reserve.*** Under the Brazilian corporation law, our shareholders may, upon the proposal of our management, decide to allocate the portion of net profits foreseen in a capital budget previously approved at a shareholders meeting to the retained profits reserve. The reserve may remain valid for five fiscal years, and must indicate all sources of funds and capital investments, whether fixed or current, which must be reviewed annually by our shareholders for it to remain valid for more than one fiscal year. On December 31, 2004, the balance of our retained profits reserve was R$147.2 million.

Rights of withdrawal and redemption

Withdrawal rights

Any of our shareholders who disagree with certain decisions made in a shareholders' meeting have the right to withdraw from our company and receive reimbursement for the value of their shares. Pursuant

to the Brazilian corporation law, the right of withdrawal may be exercised under the following circumstances:

- a reduction of our mandatory dividend;
- a change of our corporate purpose;
- our merger with another company or our consolidation with another company; or
- participation in a group of companies, as defined in the Brazilian corporation law.
- The Brazilian corporation law further provides that our spin-off will entitle withdrawal rights to our shareholders in the case of:
- change in our corporate purpose;
- reduction of our mandatory dividends; or
- participation in a group of companies, as defined in the Brazilian corporation law.

In the event of our merger with another company where we are not the surviving entity or our consolidation with another company, or our participation in a group of companies, our shareholders do not have the right of withdrawal if their shares (a) are liquid, defined as part of the BOVESPA index or some other traded stock exchange index (as defined by the CVM); and (b) are widely held, such that the controlling shareholder or companies it controls hold less than 50% of our shares. Currently our shares are not part of any BOVESPA index.

The Brazilian corporation law further provides that the spin-off of our assets or liabilities will give rise to the right of withdrawal if it results in: (i) a change of our corporate purpose, except when the equity spun-off becomes part of a company whose core business is identical to ours; (ii) a reduction of the mandatory dividend to be paid to shareholders; or (iii) our participation in a group of companies, as defined in the Brazilian corporation law.

Our shareholders will have the right of withdrawal if we are part of a merger, consolidation or spin-off, and the resulting company does not obtain registration as a publicly-held company or fails to list its new shares in the secondary market within 120 days from the date of the shareholders' meeting approving the transaction.

The right of withdrawal expires 30 days after publication of the minutes of the relevant shareholders' meeting. Additionally, we are entitled to reconsider any decision giving rise to withdrawal rights within 10 days after the expiration of those rights if the redemption of shares of dissenting shareholders would jeopardize our financial stability.

As a general rule, if shareholders exercise withdrawal rights, they are entitled to receive the net book value of their shares, based on the last balance sheet approved by the shareholders. If the resolution giving rise to the rights is made later than 60 days after the date of the last approved balance sheet, the shareholder may demand that his or her shares be valued according to a new balance sheet dated no less than 60 days before the resolution date. In this case, we must immediately pay 80% of the equity value of the shares, according to the most recent balance sheet approved by our shareholders, and the balance must be paid within 120 days after the date of the resolution of the shareholders meeting.

Pursuant to the Brazilian corporation law, our common shares may be redeemed if our shareholders vote to do so at a special shareholders meeting. A lottery shall determine which shares will be redeemed.

Registration of our shares

Our shares are held in book-entry form with Banco Itaú S.A. The transfer of shares requires a written order of the disposing shareholder or a judicial order or authorization.

Preemptive rights

Except as described below, our shareholders have a general preemptive right to subscribe for shares in any capital increase according to the proportion of their interest in us, including the issuance of convertible debentures and rights to acquire our shares or subscription warrants. In accordance with Brazilian law, a period of at least 30 days from the publication of notice of the capital increase is granted for the exercise of preemptive rights. However, in accordance with the Brazilian corporation law and our by-laws, our board of directors may exclude preemptive rights or reduce the period for their exercise with respect to the issuance of new shares, debentures convertible into our shares and warrants up to the limit of our authorized share capital, if the distribution of those shares occurs through a stock exchange, a public offering or an exchange of shares in a public offering with the purpose of acquiring another company. Currently, our bylaws do not have any provisions in this regard.

Restrictions on certain transactions by controlling shareholders, directors, executive officers and members of our fiscal board

Our controlling shareholders, directors, executive officers and members of our fiscal board (insiders for purposes of Brazilian law) may not trade with our securities or derivatives, in the following circumstances:

- prior to the public disclosure of any material act or fact related to our business;
- during the period preceding an established plan to merge with another company, consolidate, spin-off part or all of our assets or reorganize;
- during the 15-day period before the disclosure of our quarterly and annual financial statements; or
- with respect to our direct or indirect controlling shareholders, directors and officers, in the event of the acquisition or sale of our shares by us or our controlled or associated companies or another company under common control, or if an option or power of attorney has been granted for the same purpose.

Arbitration

Any disputes or controversies brought against us that relate to the listing rules of the *Novo Mercado,* our by-laws, the Brazilian corporation law, the rules published by the CMN, the Central Bank and the BOVESPA regulations, the shareholders' agreements filed in our headquarters and other rules applicable to the Brazilian capital markets in general, must be submitted to arbitration conducted before the Market Arbitration Chamber established by the BOVESPA, in accordance with its own rules. Under Market Arbitration Chamber's rules (Chapter 12), the parties may agree to choose another chamber in which to settle their disputes or controversies. Any shareholder that becomes the owner of shares representing 5% or more of our capital stock shall abide to the Market Arbitration Chamber's rules in 30 days as from the date such participation is obtained, except when such holding is acquired in a public offering or in the open market.

De-listing as a publicly held corporation (Becoming a private company)

We may become a private company only if we or our controlling shareholder(s) conduct(s) a public tender offer to acquire all of our outstanding shares, subject to the following conditions:

- the price offered must not be less than the economic value of our shares calculated in accordance with a methodology established by the CVM; and
- shareholders holding more than two-thirds of our outstanding share capital must have expressly agreed to our decision to become a private company or accepted the offer; *provided that* for such purposes, outstanding share capital refers only to those shares for which holders have expressly agreed to our decision to become a private company or participated in the public tender offer.

According to the regulations of the *Novo Mercado* and our by-laws, the minimum price for the public tender offer to acquire the outstanding shares for the purposes of de-listing must correspond to the economic value of those shares as determined in a valuation report, prepared by a specialized and independent company of recognized experience, which will be chosen at a shareholders' meeting from a list of institutions presented by our board of directors, by an absolute majority of the votes of the outstanding shares of the shareholders present at the meeting, excluding blank votes. All of the expenses and costs incurred in connection with the preparation of the valuation report must be paid by the controlling shareholder.

According to the Brazilian corporation law, we may only de-list as a publicly held corporation if we or our controlling shareholder make a tender offer for the acquisition of all shares traded in the market, for a fair price, at least equal to the valuation of our company according to one or more of the following criteria: book value, net worth at market value, discounted cash flow, comparison of market multiples, quotation of our shares in the market or any other criteria accepted by CVM. Shareholders holding at least 10% of our outstanding shares may require our management to review the price offered for the shares, in which case our board of directors is required to call an special shareholders' meeting to determine whether to perform another valuation using the same or a different valuation method. This request must be made within 15 days from the disclosure of the price to be paid for the shares in the public offering. The shareholders who make such request, as well as those who vote in its favor, must reimburse us for any costs involved in preparing the new valuation, if the new valuation price is not higher than the original valuation price. Otherwise, we assume the costs of the new valuation. If the new valuation price is higher than the original valuation price, the public offering must be made at the higher price.

De-listing from the *Novo Mercado*

Novo Mercado regulations permit us to de-list our shares from the *Novo Mercado* of BOVESPA at any time, provided that shareholders representing the majority of our voting capital stock approve the action and that we give at least 30 days written notice to the BOVESPA. The resolution must specify if the delisting will occur because the securities will only be traded other than on the *Novo Mercado,* or because we are delisting from the BOVESPA generally. Withdrawal from *Novo Mercado* will not affect our condition as a publicly held corporation.

If we de-list from the *Novo Mercado,* in order for our shares to be tradable outside the *Novo Mercado,* our controlling shareholder must conduct a public offering for the acquisition of our outstanding shares within a period of 90 days, at a price per share equivalent to the economic value of those shares as determined in a valuation report prepared by a specialized and independent company of recognized experience, which will be chosen at a shareholders' meeting from a list of institutions presented by our board of directors, by an absolute majority of the votes of our outstanding shares of

the shareholders present at the meeting, excluding blank votes. All the expenses and costs incurred in connection with the preparation of the valuation report must be paid by the controlling shareholder.

If our de-listing from the *Novo Mercado* occurs as a result of our decision to become a private company, our controlling shareholders must follow the procedure applicable from delisting as a publicly held corporation.

If we de-list from the *Novo Mercado* as a result of a corporate reorganization, in which the surviving company is not listed in the *Novo Mercado,* our controlling shareholders must, within 120 days from the date of the shareholders' meeting that approved the reorganization, conduct a public offering for the acquisition of the outstanding shares at the economic value of those shares.

In the event of a transfer of control over us within 12 months from our de-listing from the *Novo Mercado,* the selling controlling shareholder and the acquirer must offer to acquire the remaining shares for the same price and terms offered to the selling controlling shareholder, adjusted for inflation.

If our shares are de-listed from the *Novo Mercado,* we will not be permitted to have shares listed on the *Novo Mercado* for a period of two years from the de-listing date, unless there is a change in control in our company after the de-listing.

Change of control

According to the *Novo Mercado* regulation, if the controlling interest in our company is disposed of, either directly or indirectly, through a single or successive transactions, the same terms and conditions of the purchase must be extended by the acquirer in an offer to buy all of the shares of our other shareholders within 90 days from the date of acquiring the controlling shares, so as to assure equal treatment among all of our shareholders.

The same tender offer must also be made in the following situations:

- if there is a significant assignment of rights to purchase our shares and other instruments or rights related to securities convertible into our shares, which may result in the change of our control;
- if our controlling shareholder is a legal entity, the control of such legal entity is transferred; and
- If any of our existing shareholders acquire control of us through a private contract with our controlling shareholders involving any quantity of shares. In this case, the acquiring shareholder must make a tender offer on the terms and conditions offered to the selling shareholder and pay to any shareholders from which he acquired shares through a stock exchange, during the six months prior to the date of the sale of control, an amount equal to the difference between the price paid to the selling controlling shareholder and the value paid at the stock exchange for our shares during that period, duly adjusted to account for inflation until the date of actual payment.

The acquiring shareholder, if necessary, shall take the necessary measures to reestablish, in the sixth month subsequent to the acquisition, the 25% minimum free float requirement.

Purchases of our own shares by our company

Our by-laws authorize our board of directors to approve the acquisition of our own shares. The decision to acquire our shares, maintain the acquired shares in treasury or cancel treasury shares may not, among other things:

- result in a reduction of our share capital;
- require the use of resources exceeding our retained earnings and reserves recorded in our most recent financial statements;
- create, directly or indirectly, any artificial demand, supply or share price condition, or constitute an unfair practice as a result of any action or omission;
- involve any unfair practice (*prática não equitativa*);
- be used to purchase shares held by our controlling shareholder;
- be used to purchase shares that have not been paid up for; or
- be taken if there is a public offering of our shares going on.

Our treasury stock may not exceed 10% of our outstanding shares, including the shares held by our subsidiaries and associated companies. Any purchase of our own shares must be made through the stock exchanges. We may also buy our own shares if we cease to be a publicly-held company, by means of a public offering, in the terms set forth by CVM.

Moreover, we may acquire or issue put or call options related to our shares.

Disclosure of information

We are subject to the reporting requirements established by Brazilian corporation law and the CVM.

Periodic and occasional publication of information

Pursuant to the applicable legislation, we must provide certain information to the CVM and BOVESPA on a periodic basis, including annual information, quarterly information and the quarterly reports by our management and independent auditors, published calls for annual shareholders' meetings and minutes of shareholders meetings, as well as shareholders' agreements.

Disclosure of trading by insiders

Brazilian securities regulations and the *Novo Mercado* rules require our controlling shareholder, management, directors, executive officers and, members of our fiscal board, as well as any other technical or consultative body, to disclose to us when requested, for release to the CVM and to the BOVESPA, the number and type of shares (including derivative securities) held by them or by persons related to them, that are listed and issued by us, our subsidiaries and companies under our control. Such persons are also required to disclose any changes in their ownership. Information regarding the acquisition of any shares (price, amount and date of acquisition) must be provided to the CVM and to the BOVESPA within a period of 10 days from the end of the month in which the securities were traded.

Disclosure of material developments

Under Brazilian securities regulations, we must disclose any material development related to our business to the CVM and BOVESPA. We are also required to publish a notice of those material developments. A development is deemed material if it has a material impact on the price of our securities, the decision of investors to trade in our securities or the decision of investors to exercise any

rights as holders of any of our securities. Under special circumstances, we may submit to the CVM a request for confidential treatment of certain material developments.

Trading in stock exchanges

Our shares will be traded in the *Novo Mercado* segment of BOVESPA, which is a not-for-profit entity owned by its broker members. Trading in BOVESPA is carried out by its broker members. BOVESPA and CVM have the power to suspend the trading of shares of a corporation under certain circumstances.

Settlement of trades in BOVESPA takes place after three business days. Settlement and delivery of the shares are made through an independent facility, which is CBLC. CBLC is the guarantor of the transactions carried out in BOVESPA (for this purpose it makes multilateral compensations for financial obligations and transfer of securities). According to CBLC regulation, liquidation is carried out through the Central Bank System for Transfer of Reserves (*Sistema de Transferência de Reservas do Banco Central*). The transfer of securities is carried out through the CBLC system. Delivery and payments are final and may not be revoked.

Taxation

The following summary contains a description of certain Brazilian and U.S. federal income tax consequences of the acquisition, ownership and disposition of common shares, but it does not purport to be a comprehensive description of all the tax considerations that may be relevant to a decision to purchase common shares. The summary is based upon the tax laws of Brazil and regulations thereunder and on the tax laws of the United States and regulations thereunder as in effect on the date hereof, which are subject to change. **Prospective purchasers of common shares should consult their own tax advisors as to the tax consequences of the acquisition, ownership and disposition of common shares.**

Although there is at present no income tax treaty between Brazil and the United States, the tax authorities of the two countries have had discussions that may culminate in such a treaty. No assurance can be given, however, as to whether or when a treaty will enter into force or how it will affect the United States Holders (as defined below) of common shares. Prospective holders of common shares should consult their own tax advisors as to the tax consequences of the acquisition, ownership and disposition of common shares in their particular circumstances.

BRAZILIAN TAX CONSIDERATIONS

The following discussion summarizes the principal Brazilian tax consequences of the acquisition, ownership and disposition of common shares by a holder that is not domiciled in Brazil for purposes of Brazilian taxation (a "Non-Resident Holder"). It is based on Brazilian law as currently in effect. Any change in that law may change the consequences described below.

The following discussion summarizes the principal tax consequences applicable under Brazilian law to a Non-Resident Holder of common shares in general and, therefore, does not specifically address all of the Brazilian tax considerations applicable to any particular Non-Resident Holder. Each Non-Resident Holder should consult its own tax adviser concerning the Brazilian tax consequences of an investment in common shares. The tax consequences described below do not take into account tax treaties entered into by Brazil and other countries. Nevertheless, please note that Brazil has not entered into any tax treaty with the United States.

Income tax

Dividends

Dividends paid by a Brazilian corporation, such as our company, including stock dividends and other dividends paid to a non-resident holder of common shares, are currently not subject to withholding income tax in Brazil, as far as such amounts are related to profits generated after January 1, 1996.

Interest on net equity

Law No. 9,249, dated December 26, 1995, as amended, permits a Brazilian corporation, such as our company, to make distributions to shareholders of interest on net equity. These distributions may be paid in cash. For tax purposes, this interest is limited to the daily pro rata variation of the TJLP, as determined by the Central Bank from time to time, and may not exceed the greater of:

- 50% of net income (after the deduction of the provisions for social contribution on net profits but before taking into account the provision for income tax and the interest on shareholders' equity) for the period in respect of which the payment is made; and
- 50% of the sum of retained profits and profit reserves as of the date of the beginning of the period in respect of which the payment is made.

Payment of interest to a Non-Resident Holder is subject to withholding income tax at the rate of 15%, or 25% if the Non-Resident Holder is domiciled in a tax haven—that is, a country or location that does not impose income tax or where the income tax rate is lower than 20% or where the local legislation imposes restrictions on disclosing the shareholding composition or the ownership of the investment (''Tax Haven Residents''). These payments may be included, at their net value, as part of any mandatory dividend. To the extent payment of interest on net equity is so included, the corporation is required to distribute to shareholders an additional amount to ensure that the net amount received by them, after payment of the applicable withholding income tax, plus the amount of declared dividends is at least equal to the mandatory dividend.

Gains

According to Law No. 10,833/03, the disposition of assets located in Brazil, such as our common shares, by a Non-Resident Holder, whether to other Non-Resident Holders or to Brazilian holders, may be subject to capital gain in Brazil.

Gains realized as a result of a disposition transaction are the positive difference between the amount in *reais* realized on the sale or exchange of a security and its acquisition cost measured in *reais* (without correction for inflation).

For purposes of taxation of gains earned in Brazil, by a Non-Resident Holder on disposition of the common shares, two situations should be considered:

- gains earned by Resolution 2,689 investors, other than tax haven residents, which are not subject to income tax (unless the sale takes place outside a Brazilian stock exchange, in which case the gains are subject to a 15% income tax); and
- gains earned by Non-Resident Holders who invest in Brazil through any means other than under Resolution No. 2,689 (''Non-Registered Investors'') and any Tax Haven Residents, whether or not they are Resolution 2,689 investors.

In this last situation, gains derived from the sale of our common shares (i) on a Brazilian stock exchange are subject to income tax at a rate of 15% (a withholding income tax of 0.005% shall be levied, to be offset against the tax due on eventual capital gain; (ii) outside a Brazilian stock exchange are subject to income tax at a rate of 15%, except Tax Haven Residents, which are subject to income tax at a rate of 25%, according to Law No. 10,883, enacted on December 29, 2003.

In the case of redemption of securities or capital reduction by a Brazilian corporation, such as our company, the positive difference between the amount effectively received by the non-resident and the acquisition cost of the securities redeemed in *reais* is treated as capital gain derived from sale or exchange of shares not carried out on a Brazilian stock exchange market and is therefore subject to income tax at the rate of 15%, or 25%, as the case may be.

Tax on foreign exchange and financial transactions (''IOF Tax'')

Foreign exchange transactions

Brazilian law imposes a Tax on Foreign Exchange Transactions, or IOF/Exchange Tax, on the conversion of *reais* into foreign currency and on the conversion of foreign currency into *reais*. Although the current applicable rate for almost all foreign currency exchange transactions is zero, the Ministry of Finance is permitted to increase the rate at any time up to 25%. However, any increase in rates may only apply to future transactions.

Tax on transactions involving bonds and securities

Brazilian law imposes a Tax on Transactions Involving Bonds and Securities, or IOF/Bonds Tax, due on transactions involving bonds and securities, including those carried out on a Brazilian stock exchange. The rate of IOF applicable to transactions involving stocks is currently zero, although the Minister of Finance is permitted to increase such rate at any time up to 1.5% per day, but only in respect of future transactions.

Temporary contribution on financial transactions (''CPMF Tax'')

As a general rule, transactions carried out in Brazil that result in the transfer of *reais* from an account maintained with a Brazilian financial institution are subject to the CPMF tax at the rate of 0.38% Each Non-Resident Holder should note that because our common shares will be acquired in a ''non-organized over-the-counter transaction,'' CPMF tax of the purchase price may be withheld by the custodian or other party closing the foreign exchange transaction from the amounts deposited by such investor when such amounts are transferred to the CBLC. Any amount withheld would have the effect of reducing the amount of common shares purchased by the investor. Therefore, each such investor should consult its own legal and financial advisors with respect to the applicability of CPMF tax to its purchase as well as other tax consequences of such investment. The CPMF will be in effect until December 31, 2007. However, it may be extended.

Currently, the funds transferred for the acquisition of shares on BOVESPA and the remittance abroad of the proceeds earned from the disposition of stocks in Brazil by means of a currency exchange transaction are exempted from the CPMF tax.

When applicable, the CPMF tax must be withheld from the amounts transferred from such account and must be collected in favor of the Brazilian government by the financial institution that carries out the relevant financial transaction.

Other Brazilian taxes

There are no Brazilian inheritance, gift or succession taxes applicable to the ownership, transfer or disposition of stocks, except for gift and inheritance taxes imposed by some Brazilian states on gifts or bequests by individuals or entities not domiciled or residing in Brazil to individuals or entities domiciled or residing within such states. There are no Brazilian stamp, issue, registration, or similar taxes or duties payable by holders of shares.

CERTAIN UNITED STATES FEDERAL INCOME TAX CONSEQUENCES

To ensure compliance with Internal Revenue Service Circular 230, you are hereby notified that any discussion of tax matters set forth in this offering memorandum was written in connection with the promotion or marketing of the transactions or matters addressed herein and was not intended or written to be used, and cannot be used by any prospective investor, for the purpose of avoiding tax-related penalties under federal, state or local tax law. Each prospective investor should seek advice based on its particular circumstances from an independent tax advisor.

The following summary describes certain United States federal income tax consequences of the ownership of our common shares as of the date hereof. Except where noted, this discussion deals only with United States Holders (as defined below) that hold our common shares as capital assets for United States federal income tax purposes (generally, property held for investment). This summary does not represent a detailed description of the United States federal income tax consequences

applicable to you if you are subject to special treatment under the United States federal income tax laws, including if you are:

- a dealer in securities or currencies;
- a financial institution;
- a regulated investment company;
- a real estate investment trust;
- an insurance company;
- a tax-exempt organization;
- a person holding our common shares as part of a hedging, integrated or conversion transaction, a constructive sale or a straddle;
- a trader in securities that has elected the mark-to-market method of accounting for your securities;
- a person liable for alternative minimum tax;
- a person who owns 10% or more of our voting stock;
- a partnership or other pass-through entity for United States federal income tax purposes; or
- a person whose "functional currency" is not the United States dollar.

The discussion below is based upon the provisions of the Internal Revenue Code of 1986, as amended (the "Code"), and regulations, rulings and judicial decisions thereunder as of the date hereof, and such authorities may be replaced, revoked or modified so as to result in United States federal income tax consequences different from those discussed below. In addition, this discussion does not address the effects of any state, local or non-United States tax laws. **If you are considering the purchase, ownership or disposition of our common shares, you should consult your own tax advisors concerning the United States federal income tax consequences to you in light of your particular situation as well as any consequences arising under the laws of any other taxing jurisdiction.**

As used herein, "United States Holder" means a holder of our common shares that is for United States federal income tax purposes:

- an individual citizen or resident of the United States;
- a corporation (or other entity treated as a corporation for United States federal income tax purposes) created or organized in or under the laws of the United States, any state thereof or the District of Columbia;
- an estate the income of which is subject to United States federal income taxation regardless of its source; or
- a trust if it (1) is subject to the primary supervision of a court within the United States and one or more United States persons have the authority to control all substantial decisions of the trust or (2) has a valid election in effect under applicable United States Treasury regulations to be treated as a United States person.

If a partnership (or other entity treated as a partnership for United States federal income tax purposes) holds our common shares, the tax treatment of a partner will generally depend on the status of the partner and the activities of the partnership. If you are a partner of a partnership holding our common shares, you should consult your tax advisors.

Taxation of dividends

Distributions on our common shares (including amounts withheld to reflect Brazilian withholding taxes, as described above under "Brazilian Tax Considerations") will be taxable as dividends to the extent paid out of our current or accumulated earnings and profits, as determined under United States federal income tax principles. Such income (including withheld taxes) will be includable in your gross income as ordinary income on the day actually or constructively received by you. Such dividends will not be eligible for the dividends received deduction allowed to corporations. Under current law, dividends received before January 1, 2009 by non-corporate United States holders on shares of certain foreign corporations will be subject to United States federal income tax at lower rates than other types of ordinary income if certain conditions are met. However, because our common shares are not readily tradable on an established securities market in the United States and there is no income tax treaty between Brazil and the United States, we currently do not expect that those conditions will be met. Thus, we do not expect that dividends we pay will be entitled to such reduced rates.

The amount of any dividend paid in *reais* will equal the United States dollar value of the *reais* received calculated by reference to the exchange rate in effect on the date the dividend is actually or constructively received by you, regardless of whether the *reais* are converted into United States dollars. If the *reais* received as a dividend are not converted into United States dollars on the date of receipt, you will have a tax basis in the *reais* equal to their United States dollar value on the date of receipt. Any gain or loss realized on a subsequent conversion or other disposition of the *reais* will be treated as United States source ordinary income or loss.

Subject to certain conditions and limitations, Brazilian withholding taxes on dividends may be treated as foreign taxes eligible for credit against your United States federal income tax liability. For purposes of calculating the foreign tax credit, dividends paid on our common shares will be treated as income from sources outside the United States and will generally constitute passive income. Further, in certain circumstances, if you:

- have held our common shares for less than a specified minimum period during which you are not protected from risk of loss, or
- are obligated to make payments related to the dividends,

you will not be allowed a foreign tax credit for foreign taxes imposed on dividends paid on our common shares. The rules governing the foreign tax credit are complex. You are urged to consult your tax advisors regarding the availability of the foreign tax credit under your particular circumstances.

To the extent that the amount of any distribution exceeds our current and accumulated earnings and profits for a taxable year, as determined under United States federal income tax principles, the distribution will first be treated as a tax-free return of capital, causing a reduction in the adjusted basis of our common shares (thereby increasing the amount of gain, or decreasing the amount of loss, to be recognized by you on a subsequent disposition of our common shares), and the balance in excess of adjusted basis will be taxed as capital gain recognized on a sale or exchange (as discussed below under "—Taxation of capital gains"). Such distributions in excess of our current and accumulated earnings and profits would generally not give rise to foreign source income and you would generally not be able to use the foreign tax credit arising from any Brazilian withholding tax imposed on such distributions unless such credit can be applied (subject to applicable limitations) against United States federal income tax due on other foreign source income in the appropriate category for foreign tax credit purposes. However, we do not expect to keep earnings and profits in accordance with United States federal income tax principles. Therefore, you should expect that a distribution will generally be treated as a dividend (as discussed above).

Passive foreign investment company

We do not believe that we are, for United States federal income tax purposes, a passive foreign investment company, (a ''PFIC''), and we expect to operate in such a manner so as not to become a PFIC in the future. If, however, we are or become a PFIC, you could be subject to additional United States federal income taxes on gain recognized with respect to our common shares and on certain distributions on our common shares, plus an interest charge on certain taxes treated as having been deferred under the PFIC rules.

Taxation of capital gains

For United States federal income tax purposes, you will recognize taxable gain or loss on any sale, exchange or redemption of our common shares in an amount equal to the difference between the amount realized for the common shares and your tax basis in the common shares. Such gain or loss will generally be capital gain or loss. Capital gains of non-corporate shareholders derived with respect to capital assets held for more than one year are eligible for reduced rates of taxation. The deductibility of capital losses is subject to limitations. Any gain or loss recognized by you will generally be treated as United States source gain or loss. Consequently, you may not be able to use the foreign tax credit arising from any Brazilian tax imposed on the disposition of our common shares unless such credit can be applied (subject to applicable limitations) against tax due on other income treated as derived from foreign sources.

Other Brazilian taxes

You should note that any Brazilian IOF/Exchange Tax, IOF/Bonds Tax or CPMF Tax (as discussed above under ''Brazilian Tax Considerations'') may not be treated as a creditable foreign tax for United States federal income tax purposes, although you may be entitled to deduct such taxes, subject to applicable limitations under the Code. You should consult your tax advisors regarding the United States federal income tax consequences of these taxes.

Information reporting and backup withholding

In general, information reporting will apply to dividends in respect of our common shares and the proceeds from the sale, exchange or redemption of our common shares that are paid to you within the United States (and in certain cases, outside the United States), unless you establish that you are an exempt recipient such as a corporation. A backup withholding tax may apply to such payments if you fail to provide a taxpayer identification number or certification of other exempt status or fail to report in full dividend and interest income.

Any amounts withheld under the backup withholding rules will be allowed as a credit or a refund against your United States federal income tax liability provided the required information is timely furnished to the Internal Revenue Service.

Each holder should consult such holder's own tax advisor concerning the overall tax consequences to it, including the consequences under laws other than U.S. federal income tax laws, of an investment in common shares.

Plan of distribution

General

Under an underwriting agreement dated December 7, 2005, Banco UBS S.A., Banco Itaú BBA S.A. and Banco J.P. Morgan S.A. have severally agreed to place the number of common shares listed opposite their names below.

Underwriter	Common Shares	Percentage
Banco UBS	28,400,000	40%
Banco Itaú BBA	28,400,000	40%
Banco J.P. Morgan S.A.	14,200,000	20%
Total	71,000,000	100%

Banco UBS S.A. will act as sole global coordinator, and UBS Securities LLC, Itaú Securities Inc. and J.P. Morgan Securities Inc. will act as agents for Banco UBS S.A., Banco Itaú BBA S.A. and Banco J.P. Morgan S.A., respectively, for common shares offered to investors outside Brazil. UBS Limited will act as sub-agent of UBS Securities LLC for common shares offered to investors outside Brazil, Canada and the United States. In addition, Banco Santander Brasil S.A. and Unibanco—União de Bancos Brasileiros S.A. will act as co-managers in connection with the placement facilitation of the common shares in this offering. All placement facilitations of common shares in the United States will be made by U.S. registered broker-dealers.

The underwriting agreement provides that the obligation of the underwriters to place the common shares is subject to, among other conditions, the delivery of certain legal opinions by our and their legal counsel and comfort letters from our auditors. The underwriting agreement also provides that, if any of the common shares are not placed, the underwriters are obligated to purchase them on a firm commitment basis on the settlement date, subject to certain conditions and exceptions. The common shares will initially be offered by the underwriters and the agents at the price indicated on the cover page of this offering memorandum. After the initial offering of the common shares, the offering price and other selling terms may from time to time be varied by the underwriters. We and the selling shareholder have also entered into a placement facilitation and agency agreement with the agents relating to the offering of our common shares outside Brazil.

We and the selling shareholder have also been advised by the agents that they propose to facilitate the placement of the common shares initially to persons in the United States whom the agents reasonably believe to be "qualified institutional buyers"; and to non-U.S. persons in transactions meeting the requirements of Regulation S under the Securities Act.

The common shares have not been registered under the Securities Act and will be subject to significant resale restrictions. See "Notice to investors."

The selling shareholder and BNDESPAR have granted to the underwriters an option exercisable by Banco UBS S.A., as sole global coordinator, within 30 days after the date of the final offering memorandum relating to this offering to place up to an aggregate of 9,900,000 additional common shares to cover over-allotments, if any. The option, if exercised, will be at the price per common share indicated on the cover page of this offering memorandum.

The following table shows the per share offering price, the underwriting commission and other commissions to be paid by the selling shareholder and BNDESPAR to the underwriters and net proceeds to the selling shareholder. This information is presented assuming either no exercise or exercise in full of the over-allotment option. Since this offering is a secondary offering by the selling

shareholder and BNDESPAR, we will not receive any proceeds from the sale of our common shares and such proceeds will be received solely by the selling shareholder and BNDESPAR.

	Per share	Without over-allotment option	Total with over-allotment option
	(R$)	(R$ millions)	
Offering price	13.00	923,000,000.00	1,051,700,000.00
Underwriting commissions	0.26	18,460,000.00	21,034,000.00
Net proceeds	12.74	904,540,000.00	1,030,666,000.00

The expenses of this offering, exclusive of the underwriting commission, are estimated to be approximately R$3.5 million.

The price at which the common shares will be offered is based in part on the demand encountered at various price levels in the course of the bookbuilding process.

Pursuant to the underwriting agreement and the placement facilitation and agency agreement, we will indemnify the underwriters and the agents against certain liabilities, including liabilities under the Securities Act, and, pursuant to the placement facilitation and agency agreement, will contribute to payments the underwriters and the agents may be required to make in respect thereof.

Our common shares have been approved for listing on the *Novo Mercado* segment of BOVESPA under the symbol "TBLE3".

Price stabilization

In connection with this offering, Banco UBS S.A. on behalf of the underwriters, for a period of up to 30 days after the date of this offering memorandum and, through UBS Corretora de Câmbio e Valores Mobiliários S.A., may engage in transactions that stabilize, maintain or otherwise affect the price of the common shares. In addition, the underwriters' representative may over-allot in connection with the offering, creating a syndicate short position. The underwriters' representative may bid for, and purchase, common shares in the open market to cover syndicate short positions or stabilize the price of the common shares. Any of these activities may stabilize or maintain the market price of the common shares above independent market levels or may retard a decline in the market price of the common shares. Neither the stabilizing manager nor any other underwriter is required to engage in these activities and may end any of these activities at any time. Reports on stabilization activity are required to be furnished to the CVM.

Shares eligible for future sale

We, the selling shareholder, BNDESPAR and Banco Clássico have agreed with the underwriters and their agents, for a period of 180 days following the date of the final offering memorandum, not to issue, offer, sell, or, contract to sell, or otherwise dispose of any, or grant any rights or file a registration statement under the Securities Act or Brazilian laws with respect to any common shares. Additionally, we and the selling shareholder have agreed with the underwriters and the agents, for a period of 180 days, not to enter into any swap or other arrangement that transfers to another, in whole or in part, any of the economic consequences of ownership of common shares or any securities convertible into or exercisable or exchangeable for common shares or any such securities, or warrants or other rights to purchase our common shares, whether any such transaction is to be settled by delivery of common shares or such other securities, in cash or otherwise, and not to publicly announce

an intention to effect any transaction specified in this paragraph. We call such actions, other than issuance, "transfer."

Under these agreements, transfers of these securities could be made under the following circumstances, among others:

- with the prior written consent of UBS Securities LLC;
- by a shareholder of any common shares, subsequently acquired in the open market;
- lending by our controlling shareholder pursuant to certain transaction documents relating to this offering;
- if the shareholder is a corporation, to any subsidiary or other affiliate of the shareholder, so long as the recipient thereof agrees in writing with the agents to be bound by the terms of the lock-up;
- in the case of Banco Clássico, it will be able to sell shares outside a stock exchange, subject to the restrictions set forth in the following paragraph; or
- in the case of BNDES, the selling restrictions do not apply to managed securities portfolios that belong to third parties and/or are deposited in funds managed by the BNDES System, that is, the group of companies composed by BNDES itself, BNDESPAR and by the Special Agency of Industrial Financing (FINAME).

In any of the last three cases, it will be a condition of the transfer that the transferee agrees that it is receiving and holding the transferred securities subject to the provisions of the lock-up agreement and that the transferee will not transfer the securities except in accordance with the lock-up agreement for the remainder of its term.

Novo Mercado regulations

In addition, under *Novo Mercado* regulations, our controlling shareholder and our directors and executive officers may not sell or offer to sell our common shares or derivatives during the six-month period following the date the common shares begin trading on the *Novo Mercado*. Upon the termination of the initial six-month period, our controlling shareholder and our directors and executive officers may sell, offer or dispose of up to 40% of their respective holdings during the following six-month period.

We cannot predict the effect, if any, that future sales of the common shares, or the availability of such common shares for future sale, will have on the market price of the common shares prevailing from time to time or on our ability to raise capital in the future. Sales of substantial amounts of common shares in the public market, or the perception that such sales could occur, could adversely affect the prevailing market price of the common shares and our ability to sell shares in the future at a time and at a price that we deem appropriate.

Other relationships

As of the date of this offer, Banco UBS S.A. or any of its affiliates did not have any commercial relations with us or our affiliates but in the future they may provide us with services and products, including commercial, banking, investment banking, brokerage, financing, financial advisory and other services for which they will expect to receive customary fees The other underwriters, agents, the co-managers and/or their affiliates have from time to time in the past provided, and may in the future provide, commercial banking, investment banking, brokerage, financing, financial advisory and other services to us and our affiliates, for which they have received or expect to receive customary fees.

Banco Itaú BBA S.A., Banco JP Morgan S.A. and Banco Santander Brasil S.A. (and/or their affiliates) currently provide or in the future may provide to us or our affiliates, among other products and services, credit lines, loans, financing, financing related to BNDES resources, derivative market transactions, foreign exchange transactions, certificate of deposit, investment banking services and custodian services. In addition Banco Santander Brasil S.A. participated as coordinator of our debenture issuance in May of 2005. We have commercial relations with Unibanco—União de Bancos Brasileiros S.A. in the normal course of our business. In addition, Unibanco—União de Bancos Brasileiros S.A. also participated as coordinator of our debenture issuance in May of 2005.

Notice to investors

Because of the following restrictions, investors are advised to consult legal counsel prior to making any offer, resale, pledge or transfer of our common shares.

Our common shares have not been registered under the Securities Act and may not be offered or sold within the United States or to, or for the account or benefit of, U.S. persons (as defined in Regulation S under the Securities Act) except:

- in compliance with the registration requirements of the Securities Act and all applicable securities laws of the states of the United States; or
- in accordance with an applicable exemption from, or in a transaction not subject to, the registration requirements of the Securities Act and any applicable securities laws of the states of the United States.

Accordingly, our common shares are being offered and sold only:

- in the United States to "qualified institutional buyers," as defined in Rule 144A under the Securities Act, pursuant to Rule 144A; or
- outside the United States in offshore transactions in reliance on Regulation S under the Securities Act.

Each purchaser of our common shares who is a U.S. person within the meaning of Regulation S, including any purchaser who is a U.S. person acquiring our shares outside the United States, will be deemed to have made the following acknowledgments, representations and agreements with us, the underwriters and the agents:

- the offering and sale of the common shares have not been registered under the Securities Act and are intended to be exempt from registration under the Securities Act;
- the purchaser is a qualified institutional buyer, as such term is defined in Rule 144A under the Securities Act (or, if it is acquiring the common shares as a fiduciary or agent for one or more investor accounts, each such account is a qualified institutional buyer);
- the purchaser acknowledges that the underwriters and the agents may rely on the exemption from the registration requirements of the Securities Act provided by Rule 144A;
- the purchaser is acquiring our shares for its own account (or, if it is acquiring the common shares as a fiduciary or agent for one or more investor accounts, the purchaser has the full power and authority to make the representations, warranties and agreements herein on behalf of each such account) and is not acquiring the common shares with a view to any distribution of the common shares within the meaning of the Securities Act;
- the purchaser understands and agrees that our common shares may not be reoffered, resold, pledged or otherwise transferred, except:
  - to a person whom the purchaser reasonably believes is a qualified institutional buyer in a transaction meeting the requirements of Rule 144A;
  - outside the United States in a transaction meeting the requirements of Regulation S; or
  - pursuant to another available exemption from the registration requirements of the Securities Act; and
  - in each case, in accordance with all applicable securities laws of the states of the United States.

- except with respect to transactions over the São Paulo Stock Exchange that meet the requirements of Regulation S, the purchaser (1) will not transfer our common shares to any person or entity unless that person or entity could itself truthfully make each of the acknowledgments, representations and agreements set forth in this section and (2) will provide notice of the transfer restrictions applicable to our common shares to any subsequent transferees;
- the purchaser has sufficient knowledge and experience in financial and business matters so as to be capable of independently evaluating the merits and risks of an investment in our common shares, and the purchaser is able to bear the economic risk of the investment. The purchaser has made its own investment decision regarding the common shares based on its own knowledge; and
- the purchaser acknowledges that we, the underwriters, the agents and others will rely upon the truth and accuracy of the foregoing acknowledgments, representations and agreements.

Selling restrictions

European Economic Area

With respect to each Member State of the European Economic Area which has implemented Prospectus Directive 2003/71/EC, including any applicable implementing measures, from and including the date on which the Prospectus Directive is implemented in that Member State, the offering of our common shares in this offering is only being made:

(a) to legal entities which are authorized or regulated to operate in the financial markets or, if not so authorized or regulated, whose corporate purpose is solely to invest in securities;

(b) to any legal entity which has two or more of (1) an average of at least 250 employees during the last financial year; (2) a total balance sheet of more than €43,000,000 and (3) an annual net turnover of more than €50,000,000, as shown in its last annual or consolidated accounts; or

(c) in any other circumstances which do not require the publication by the Issuer of a prospectus pursuant to Article 3 of the Prospectus Directive.

United Kingdom

Our common shares may not be offered or sold and will not be offered or sold to any persons in the United Kingdom other than to person whose ordinary activities involve them in acquiring, holding, managing or disposing of investments (as principal or as agent) for the purposes of their businesses and in compliance with all applicable provisions of the FSMA with respect to anything done in relation to shares of our common shares in, from or otherwise involving the United Kingdom. In addition, any invitation or inducement to engage in investment activity (within the meaning of Section 21 of the FSMA) in connection with the issue or sale of our common shares may only be communicated in circumstances in which Section 21(1) of the FSMA does not apply to the Company. Without limitation to the other restrictions referred to herein, this offering circular is directed only at (1) persons outside the United Kingdom, (2) persons having professional experience in matters relating to investments who fall within the definition of ''investment professionals'' in Article 19(5) of the Financial Services and Markets act 2000 (Financial Promotion) Order 2005; or (3) high net worth bodies corporate, unincorporated associations and partnerships and trustees of high value trusts as described in Article 49(2) of the Financial Services and Markets act 2000 (Financial Promotion) Order 2005. Without limitation to the other restrictions referred to herein, any investment or investment activity to which this offering circular relates is available only to, and will be engaged in only with, such persons, and persons within the United Kingdom who receive this communication (other than persons who fall within (2) or (3) above) should not rely or act upon this communication.

Switzerland

Our common shares may be offered in Switzerland only on the basis of a non-public offering. This prospectus does not constitute an issuance prospectus according to articles 652a or 1156 of the Swiss Federal Code of Obligations or a listing prospectus according to article 32 of the Listing Rules of the Swiss exchange. Our common shares may not be offered or distributed on a professional basis in or from Switzerland and neither this prospectus nor any other offering material relating to our common shares may be publicly issued in connection with any such offer or distribution. The shares have not been and will not be approved by any Swiss regulatory authority. In particular, the shares are not and will not be registered with or supervised by the Swiss Federal Banking Commission, and investors may not claim protection under the Swiss Investment Fund Act.

Trading, settlement and clearance

General

On November 16, 2005, we executed a listing agreement with BOVESPA in order to join the *Novo Mercado,* which will be effective on November 16, 2005. Our shares are listed for trading on the *Novo Mercado* segment of BOVESPA under the symbol "TBLE3." BOVESPA is the only trading market for our common shares. The standard trading lot for our common shares on BOVESPA is 1 share.

We agreed to comply with heightened corporate governance and disclosure requirements established by BOVESPA in order to qualify as a company admitted to the *Novo Mercado*.

To become a company within *Novo Mercado,* we agreed, among other things, to:

- issue voting shares only;
- ensure, in three years from the date of execution of the *Novo Mercado* Agreement, that shares representing 25% of our total capital are effectively available for trading;
- during that three-year period, ensure that shares representing 21.69% of our total capital stock are effectively available for trading;
- adopt offering procedures that favor widespread ownership of shares whenever making a public offering;
- comply with minimum quarterly disclosure standards and improvements in quarterly financial statements, including quarterly consolidated financial statements and limited audit revision;
- follow stricter disclosure policies with respect to transactions made by controlling shareholders, directors and officers involving securities issued by us;
- disclose any existing shareholders' agreements and stock option plans;
- make a schedule of corporate events available to the shareholders;
- disclose and periodically update a listing of any related party transactions;
- ensure that the same conditions provided to controlling shareholders in the transfer of our control are extended to all shareholders (*i.e.*, tag-along rights);
- establish a one-year term of office for the entire board of directors;
- make the annual balance sheet available according to U.S. GAAP or International Financial Reporting Standards;
- accept the BOVESPA arbitration panel for conflict resolution between investors, management and *Novo Mercado* companies; and
- if the we ever decide to delist from *Novo Mercado,* conduct a tender offer based on economic valuation criteria.

Trading on the Brazilian Stock Exchanges

Our shares will trade on BOVESPA, which is a not-for-profit entity owned by its member brokerage firms. Trading on BOVESPA is limited to member brokerage firms and a limited number of authorized non-members.

The CVM and BOVESPA have discretionary authority to suspend trading in shares of a particular issuer under certain circumstances. Trading in securities listed on BOVESPA, including the *Novo Mercado* and Levels 1 and 2 of Differentiated Corporate Governance, may be effected off the exchanges in the unorganized over-the-counter market in certain circumstances.

The shares of all companies listed on BOVESPA, including *Novo Mercado* and Level 1 and Level 2 companies, are traded together.

Settlement of transactions occurs three business days after the trade date. Delivery of and payment for shares is made through the facilities of separate clearing houses for each exchange, which maintain accounts for member brokerage firms. The seller is ordinarily required to deliver the shares to the clearing house on the third business day following the trade date. The clearing house for BOVESPA is the CBLC.

In order to reduce volatility, BOVESPA has adopted a ''circuit breaker'' system pursuant to which trading sessions may be suspended for a period of 30 minutes or one hour whenever specified indices of BOVESPA fall below the limits of 10% and 15%, respectively, in relation to the index levels for the previous trading session.

Although the Brazilian equity market is Latin America's largest in terms of market capitalization, it is smaller and less liquid than the major U.S. and European securities markets. Moreover, BOVESPA is less liquid than the New York Stock Exchange and other major exchanges in the world. BOVESPA had a market capitalization of US$473 billion as of September 30, 2005 and an average monthly trading volume of approximately US$520 billion from January though September 2005. In comparison, the New York Stock Exchange had a market capitalization of US$13.2 trillion as of September 30, 2005 and an average monthly trading volume of approximately US$55 trillion from January through September 2005. Although any of the outstanding shares of a listed company may trade on a Brazilian stock exchange, in most cases fewer than half of the listed shares are actually available for trading by the public, the remainder being held by small groups of controlling persons, governmental entities or one principal shareholder.

Trading on Brazilian stock exchanges by non-residents of Brazil is subject to registration procedures. See ''—Investment in our common shares by non-residents of Brazil.''

Regulation of Brazilian securities markets

The Brazilian securities markets are principally governed by Law No. 6,385, dated December 7, 1976, and the Brazilian corporation law, each as amended and supplemented, and by regulations issued by the CVM, which has authority over stock exchanges and the securities markets generally; the National Monetary Council; and the Central Bank, which has, among other powers, licensing authority over brokerage firms and regulates foreign investment and foreign exchange transactions.

These laws and regulations, among others, provide for licensing and oversight of brokerage firms, governance of the Brazilian stock exchanges, disclosure requirements applicable to issuers of traded securities, restrictions on price manipulation and protection of minority shareholders. They also provide for restrictions on insider trading. However, the Brazilian securities markets are not as highly regulated and supervised as the U.S. securities markets or securities markets in some other jurisdictions. Accordingly, any trades or transfers of our equity securities by our officers and directors, our controlling shareholders or any of the officers and directors of our controlling shareholders must comply with the regulations issued by the CVM, in particular Instruction No. 358. See ''Description of capital stock—Disclosure requirements.''

Under the Brazilian corporation law, a corporation is either publicly held (*companhia aberta*), or closely held (*companhia fechada*). All publicly held companies are registered with the CVM and are subject to reporting requirements.

We have the option to ask that trading in securities on BOVESPA be suspended in anticipation of a material announcement. Trading may also be suspended the initiative of BOVESPA or the CVM, based on or due to, among other reasons, a belief that a company has provided inadequate information regarding a material event or has provided inadequate responses to inquiries by the CVM or BOVESPA.

The Brazilian over-the-counter market consists of direct trades between individuals in which a financial institution registered with the CVM serves as intermediary. No special application, other than registration with the CVM, is necessary for securities of a publicly held company to be traded in this market. The CVM requires that it be given notice of all trades carried out in the Brazilian over-the-counter market by the respective intermediaries.

Investment in our common shares by non-residents of Brazil

Investors residing outside Brazil, including institutional investors, are authorized to purchase equity instruments, including the common shares, on BOVESPA provided that they comply with the registration requirements set forth in Resolution No. 2,689 of the National Monetary Council, which we refer to as Resolution 2,689, and CVM Instruction No. 325.

With certain limited exceptions, under Resolution 2,689 investors are permitted to carry out any type of transaction in the Brazilian financial capital market involving a security traded on a stock exchange, futures exchange or organized over-the-counter market. Investments and remittances outside Brazil of gains, dividends, profits or other payments under our common shares are made through the new unified exchange rate market. See ''Exchange Rates.''

In order to become a Resolution 2,689 investor, an investor residing outside Brazil must:

- appoint a representative in Brazil with powers to take actions relating to the investment;
- appoint an authorized custodian in Brazil for the investments, which must be a financial institution duly authorized by the Central Bank and CVM; and
- through its representative, register itself as a foreign investor with the CVM and the investment with the Central Bank.

Securities and other financial assets held by foreign investors pursuant to Resolution 2,689 must be registered or maintained in deposit accounts or in the custody of an entity duly licensed by the Central Bank or the CVM. In addition, securities trading by foreign investors is generally restricted to transactions involving securities listed on the Brazilian stock exchanges or traded in organized over-the-counter markets licensed by the CVM.

CPMF tax

The offering of our shares constitutes a ''non-organized over-the-counter transaction'' under Brazilian law. Each investor who is not a resident of Brazil should note that because our shares will be acquired in a ''non-organized over-the-counter transaction,'' CPMF tax in the amount of 0.38% of the purchase price may be withheld by the custodian or other party closing the foreign exchange transaction from the amounts deposited by such investor when such amounts are transferred to the CBLC. Any amounts withheld would have the effect of reducing the amount of our common shares purchased by the investor. Therefore, each such investor should consult its own legal and financial advisors with respect to the applicability of CPMF tax to its purchase as well as other tax consequences of such investment.

Please refer to ''Taxation'' in this offering memorandum for a more detailed description of the tax consequences to an investor residing outside Brazil of investing in our common shares in Brazil.

Legal matters

The validity of our common shares under Brazilian law will be passed upon by Mattos Filho, Veiga Filho, Marrey Jr. e Quiroga Advogados, Brazilian counsel to our company and by Pinheiro Neto Advogados, Brazilian counsel to the underwriters. We have been represented as to U.S. legal matters by Simpson Thacher & Bartlett LLP. The underwriters have been represented as to U.S. legal matters by Clifford Chance US LLP.

Experts

The consolidated financial statements for the years ended December 31, 2004, 2003 and 2002, including the notes thereto, included herein have been audited by Deloitte Touche Tohmatsu Auditores Independentes, as stated in their report appearing herein.

The unaudited financial statements for the nine-month periods ended September 30, 2005 and 2004 included herein, have been reviewed by Deloitte Touche Tohmatsu Auditores Independentes which reported that they have applied limited procedures in accordance with professional standards adopted in Brazil for the review of such information. However, they did not audit and do not express an opinion on that interim financial information. Accordingly, the degree of reliance on their reports on such information should be restricted in light of the limited nature of the review procedures applied.

Enforcement of judgments and service of process

We are incorporated under the laws of Brazil. All of our directors and officers reside outside the United States. Substantially all of our assets are located in Brazil. As a result, it may not be possible (or it may be difficult) for you to effect service of process upon us or these other persons within the United States or to enforce judgments obtained in United States courts against us or them, including those predicated upon the civil liability provisions of the federal securities laws of the United States.

In addition, any claims under the *Novo Mercado* rules must be submitted to arbitration conducted in accordance with the rules of the Market Arbitration Chamber of BOVESPA. See "Description of capital stock—Arbitration."

We have been advised by our Brazilian counsel, Mattos Filho, Veiga Filho, Marrey Jr., that a judgment of a United States court for civil liabilities predicated upon the federal securities laws of the United States may be enforced in Brazil, subject to certain requirements described below. Such counsel has advised that a judgment against us, the directors and officers or certain advisors named herein obtained in the United States would be enforceable in Brazil upon confirmation of that judgment by the *Superior Tribunal de Justiça* (STJ). That confirmation will only be available if the U.S. judgment:

- fulfills all formalities required for its enforceability under the laws of the United States;
- is issued by a court of competent jurisdiction after proper service of process is made in accordance with Brazilian law or after sufficient evidence of our absence has been given, as requested under the laws of the United States;
- is not subject to appeal;
- is for payment of a liquidated amount;
- is authenticated by a Brazilian diplomatic office in the United States and is accompanied by a sworn translation into Portuguese; and
- is not against Brazilian national sovereignty or public policy or equitable principles (as set forth in Brazilian law).

We have been further advised by Mattos Filho, Veiga Filho, Marrey Jr. that (1) original actions may be brought in connection with this offering memorandum predicated solely on the federal securities laws of the United States in Brazilian courts and that, subject to applicable law, Brazilian courts may enforce liabilities in such actions against us or the directors and officers and certain advisors named herein; and (2) our assets and equipment that are considered essential for the rendering of public services under governmental concessions (*bens vinculados à concessão* or *bens reversíveis*) are entitled to immunity and cannot be attached prior to any entry of judgment or in aid of execution upon a judgment.

In addition, a plaintiff (whether Brazilian or non-Brazilian) that resides outside Brazil during the course of litigation in Brazil must provide a bond to guarantee court costs and legal fees if the plaintiff owns no real property in Brazil that could secure payment. This bond must have a value sufficient to satisfy the payment of court fees and defendant attorney's fees, as determined by the Brazilian judge, except in the case of the enforcement of foreign judgments that have been duly confirmed by the *Superior Tribunal de Justiça* (STJ). Notwithstanding the foregoing, we cannot assure you that confirmation of any judgment will be obtained, or that the process described above can be conducted in a timely manner.

Glossary of terms

ANEEL: Brazilian Electric Power Agency *(Agência Nacional de Energia Elétrica)*.

Gigawatt (GW): One billion watts.

Gigawatt hour (GWh): One gigawatt of power supplied or demanded for one hour, or one billion watt hours.

High voltage: A class of nominal system voltages equal to or greater than 100,000 volts (100 kVs) and less than 230,000 volts (230 kVs).

Kilovolt (kV): One thousand volts.

Kilowatt (kW): One thousand watts.

Kilowatt hour (kWh): One kilowatt of power supplied or demanded for one hour, or one thousand watt hours.

Megawatt (MW): One million watts.

Megawatt hour (MWh): One megawatt of power supplied or demanded for one hour, or one million watt hours.

MME: Ministry of Mines and Energy *(Ministério de Minas e Energia)*.

National Interconnected System, or SIN: System comprising the basic network and other transmission facilities that interconnect the generation and distribution units in the Brazilian systems: south, southeast, center-west, and northeast.

Small hydroelectric power plant or PCHs: Power plants with capacity from 1 MW to 30 MW.

UHE: A generating unit that uses water power to drive the electric generator.

Volt: The basic unit of electric force analogous to water pressure in pounds per square inch.

Watt: The basic unit of electrical power.

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Independent auditors' report

To the Board of Directors and Shareholders of
Tractebel Energia S.A.
Florianópolis—SC

1. We have audited the accompanying consolidated balance sheets of Tractebel Energia S.A. as of December 31, 2004 and December 31, 2003, and the consolidated statements of income, changes in shareholders' equity (Company) and changes in financial position for the years ended December 31, 2004, December 31, 2003 and December 31, 2002, all expressed in Brazilian reais, prepared under the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

2. Our audits were conducted in accordance with generally accepted auditing standards in Brazil and comprised: (a) planning of the work taking into consideration the significance of the balances, the volume of transactions and the accounting and internal control systems of the Company and subsidiaries; (b) checking, on a test basis, the evidence and records that support the amounts and accounting information disclosed; and (c) evaluation of the most relevant accounting practices followed by the Company and subsidiaries, as well as the presentation of the financial statements taken as a whole.

3. In our opinion, the financial statements referred to in paragraph 1 present fairly, in all material respects, the consolidated financial position of Tractebel Energia S.A. as of December 31, 2004 and December 31, 2003, and the consolidated results of its operations, the changes in its shareholders' equity (Company) and the consolidated changes in its financial position for the years ended on December 31, 2004, December 31, 2003 and December 31, 2002, in conformity with the accounting practices adopted in Brazil.

4. The Company, based on its internal future cash flow projections, discounted to present value, estimated that certain assets would not be recovered with its future operations. The Company's management understands that these assets together with the rest of Company's operational assets will produce positive future cash flows.

DELOITTE TOUCHE TOHMATSU
Auditores Independentes
CRC—SP 011609/O-S-SC

Celso de Almeida Moraes
Contador
CRC—SP 124669/O-S-SC

January 31, 2005

Consolidated balance sheets as of December 31

	2004	2003
	(In thousands of Brazilian reais)	
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	7,710	6,357
Securities	651,704	340,688
(–) Provision for investment losses	(17,427)	—
Funds restricted for payment of obligations	—	27,203
Consumers, concessionaires and holder of permissions	412,272	398,625
(–) Provision for doubtful debtors	(131,625)	(143,720)
Advances to suppliers	8,849	33,226
Credits from fuel consumption account—CCC/CDE	35,538	23,766
Disposals, services in progress and expenditures to reimburse	8,050	10,229
Taxes and social contributions recoverable	107,684	22,061
(–) Provision for losses in recovery of ICMS credit	(32,977)	—
Deferred taxes	98,173	122,329
Warehouse/maintained in stock	13,610	13,426
Prepaid expenses	5,800	52,528
Other	26,053	18,331
	1,193,414	925,049
LONG-TERM ASSETS		
Concessionaires and holders of permission	14,920	23,246
Miscellaneous receivables	16,572	—
Securities	35,550	—
Advances to suppliers	—	2,357
Taxes and social contributions recoverable	8,684	30,381
Pledges and restricted deposits	53,536	63,293
Deposits in court	26,050	23,195
Disposal of assets and rights	29,303	—
Deferred taxes	186,643	191,847
Prepaid expenses	—	3,668
Other	483	483
	371,741	338,470
PERMANENT ASSETS		
Investments	50,365	56,861
Property, plant and equipment	4,536,430	4,748,995
Deferred	53,202	62,934
	4,639,997	4,868,790
TOTAL ASSETS	6,205,152	6,132,309

The accompanying notes are an integral part of these statements.

Consolidated balance sheets as of December 31

	2004	2003
	(In thousands of Brazilian reais)	
LIABILITIES		
CURRENT LIABILITIES		
Suppliers	117,286	88,508
Dividends and interest on shareholders' equity	553,045	441,203
Loans and financing	265,410	245,306
Interest and charges on loans and financing	12,302	13,191
Debentures	18,599	15,814
Charges on debentures	4,761	5,423
Current taxes and social contributions	74,897	15,913
Taxes and social contributions on installments	979	1,307
Customer advances	—	19,094
Estimated obligations	36,540	83,878
Provision for contingencies	731	13,010
Post-employment benefits	51,619	43,722
Deferred taxes	39,616	48,603
Derivatives	28,002	—
Other	29,470	19,437
	1,233,257	1,054,409
LONG-TERM LIABILITIES		
Loans and financing	1,539,409	1,859,455
Debentures	153,619	166,100
Taxes and social contributions on installments	7,016	7,738
Estimated obligations	17,333	23,002
Provisions for contingencies	108,637	83,889
Concessions payable	160,417	131,232
Post-employment benefits	198,508	200,379
Other	—	4,309
	2,184,939	2,476,104
SHAREHOLDERS' EQUITY		
Share capital	2,445,766	2,445,766
Capital reserves	91,695	91,695
Surplus reserves	249,495	64,335
	2,786,956	2,601,796
TOTAL LIABILITIES	6,205,152	6,132,309

The accompanying notes are an integral part of these statements.

Consolidated statements of income

For the years ended on December 31

	2004	2003	2002
	(In thousands of Brazilian reais)		
GROSS OPERATING REVENUE			
Provision of electric energy	372,743	237,612	47,613
Supply of electric energy	1,986,055	1,476,912	1,162,351
Fuel subvention—CCC/CDE	286,194	226,856	216,294
Services rendered	4,687	4,210	3,784
Sales of ash	10,393	6,746	4,382
Other income	1,738	443	2,747
	2,661,810	1,952,779	1,437,171
DEDUCTIONS FROM OPERATING REVENUE			
Social tax and contributions	(185,550)	(116,586)	(57,702)
Sales of ash, net of taxes—CCC/CDE	(6,329)	(5,257)	(3,630)
Transfer of energy revenue in advance	—	—	(564)
	(191,879)	(121,843)	(61,896)
NET INCOME FROM SALES AND SERVICES	2,469,931	1,830,936	1,375,275
COSTS OF ELECTRIC ENERGY AND SERVICES			
Electric energy purchased for resale	(302,956)	(250,858)	(146,211)
Production cost of electric energy	(790,329)	(621,460)	(713,215)
Cost of services rendered	(8,561)	(7,267)	(6,783)
	(1,101,846)	(879,585)	(866,209)
GROSS PROFIT	1,368,085	951,351	509,066
OPERATING EXPENSES			
Selling expenses	(133,412)	(215,002)	(29,164)
General and administrative expenses	(187,301)	(35,834)	(97,537)
	(320,713)	(250,836)	(126,701)
SERVICE INCOME	1,047,372	700,515	382,365
Income from interests held in other companies			
Equity in the earnings of subsidiary companies	—	(254)	—
Amortization of goodwill	(6,746)	(6,746)	(2,288)
	(6,746)	(7,000)	(2,288)

	2004	2003	2002
	(In thousands of Brazilian reais)		
Financial Income/(Expenses)			
Income from investments	52,106	64,208	23,286
Charges on debts	(188,150)	(226,536)	(193,537)
Charges on ANEEL concessions	(13,431)	(10,297)	(3,807)
Provision for investment losses	(17,427)	—	—
Losses with exchange rate swap/interest	(28,157)	—	—
Net monetary variations	29,626	170,653	(529,579)
Other	(11,123)	(33,721)	(19,468)
	(176,556)	(35,693)	(723,105)
OPERATING INCOME (LOSS)	864,070	657,822	(343,028)
NON OPERATING INCOME (LOSS)	(3,035)	2,682	(2,745)
INCOME (LOSS) BEFORE TAXES	861,035	660,504	(345,773)
Social contribution	(53,215)	(39,708)	43,512
Income tax	(32,628)	(103,642)	118,740
NET INCOME (LOSS) FOR THE YEAR	775,192	517,154	(183,521)
NET INCOME (LOSS) PER THOUSAND SHARES	1.1876	0.7923	(0.2812)

The accompanying notes are an integral part of these statements.

Consolidated statements of shareholders' equity

For the years ended on December 31

	Share capital	Capital reserves	Surplus reserve	Retained earnings	Total
			(in thousands of Brazilian reais)		
DECEMBER 31, 2001	2,445,766	91,695	406,359	—	2,943,820
Net loss in the year				(183,521)	(183,521)
Compensation of the loss	—	—	(183,521)	183,521	—
DECEMBER 31, 2002	2,445,766	91,695	222,838	—	2,760,299
Interim dividends	—	—	(184,360)	—	(184,360)
Net income in the year	—	—	—	517,154	517,154
Management's proposed appropriation of net income:					
—statutory reserve	—	—	25,857	(25,857)	—
—dividends/interest on shareholders' equity PNA—R$0.827595, PNB—R$0.752657 and ON—R$0.752657, all per thousand shares	—	—	—	(491,297)	(491,297)
DECEMBER 31, 2003	2,445,766	91,695	64,335	—	2,601,796
Net income in the year	—	—	—	775,192	775,192
Management's proposed appropriation of net income:					
—statutory reserve	—	—	38,760	(38,760)	—
—retained earnings reserve	—	—	146,400	(146,400)	—
—dividends/interest on shareholders' equity PNA—R$0.978858, PNB—R$0.903920 and ON—R$0.903920, all per thousand shares	—	—	—	(590,032)	(590,032)
DECEMBER 31, 2004	2,445,766	91,695	249,495	—	2,786,956

The accompanying notes are an integral part of these statements.

Consolidated statements of changes in financial position

For the years ended on December 31

	2004	2003	2002
	(In thousands of Brazilian reais)		
SOURCES OF FUNDS			
From operations			
Net income for the year	775,192	517,154	(183,521)
Expenses (revenues) that do not affect the net working capital			
Depreciation and amortization	223,487	227,637	189,877
Long-term interest	11,485	30,016	(18,473)
Long-term monetary variation	(32,618)	(161,212)	473,355
Equity in the earnings of subsidiary companies	—	254	—
Amortization of goodwill	6,746	6,746	2,288
Long-term provision (reversal), net	74,214	(45,420)	5,452
Deferred income tax and social contribution	25,844	131,719	(181,605)
Partial reimbursement of free energy cost — MAE	—	397	22,076
Income (loss) in the sale of property, plant and equipment	3,168	(2,284)	2,748
	1,087,518	705,007	312,197
From third parties			
Incoming funds from long-term financing	13,771	49,163	165,581
Energy purchase financing	—	4,646	—
Customer advances	—	5,718	—
PIS/COFINS credit on depreciation and amortization	2,060	1,496	—
Sales of assets and rights	29,190	—	—
Transfer of long-term assets to current assets	63,333	66,452	153,796
Other	—	264	72
	108,354	127,739	319,449
TOTAL SOURCES	1,195,872	832,746	631,646

	2004	2003	2002
	(In thousands of Brazilian reais)		
USES OF FUNDS			
Long-term assets	110,867	222,774	16,283
Investments	250	—	16
Acquisition of property, plant and equipment and investment in deferred charges	38,053	86,442	193,739
Short-term charges and inflation effects allocated to property, plant and equipment	—	904	26,628
PIS/COFINS credit on noncurrent financial expenses	—	1,690	—
Interim dividends	—	184,360	—
Proposed dividends	590,032	491,297	—
Transfer of noncurrent liabilities to current liabilities	367,153	308,277	274,341
TOTAL USES	1,106,355	1,295,744	511,007
INCREASE (DECREASE) IN NET WORKING CAPITAL	89,517	(462,998)	120,639
CHANGES TO NET WORKING CAPITAL			
Current assets			
End of period	1,193,414	925,049	1,456,228
Beginning of period	925,049	1,456,228	1,087,157
	268,365	(531,179)	369,071
Current liabilities			
End of period	1,233,257	1,054,409	1,122,590
Beginning of period	1,054,409	1,122,590	874,158
	178,848	(68,181)	248,432
	89,517	(462,998)	120,639

The accompanying notes are an integral part of these statements.

Explanatory notes to consolidated financial statements

As of December 31 2004, 2003 and 2002

NOTE 1—BUSINESS OF THE COMPANY

The Company is an independent producer utility concessionaire with its head office in the city of Florianopolis—SC, and its activity is the generation and sale of electric energy. It is regulated by the National Agency of Electric Energy—ANEEL, linked to the Ministry of Mines and Energy.

Its installed capacity, including the indirect ownership of Hydroelectric Power Plants (UHEs) of Itá and Cana Brava and Cogeneration Unit of Lages, is of 5,859 MW, of which 79.30% in hydroelectric plants and 20.70% in thermoelectric plants, composed of the following generation plants in operation: UHE Salto Osório (PR), UHE Salto Santiago (PR), UHE Passo Fundo (RS), UHE Itá (RS/SC), UHE Machadinho (SC/RS), UHE Cana Brava (GO), UTE Charqueadas (RS), UTE Alegrete (RS), UTE William Arjona (MS), Themoelectric Complex Jorge Lacerda (SC) and Cogeneration Unit of Lages (SC).

The Company's capacity to provide electric energy, including the long-term purchase agreements entered into with the subsidiary Itá Energética S.A.—ITASA and with Companhia de Interconexão Energética—CIEN, totals 6,202 MW.

The concessions and authorizations held by the Company and its subsidiaries are listed under Note 8-d.

The Company's controlling interest is owned by Tractebel EGI South America Ltda., a company organized in Brazil and controlled by Suez-Tractebel Sociètè Anonyme, with its head office in Brussels, Belgium, a member of Suez Group, headquartered in France.

The Company is the parent company of Companhia Energética Meridional—CEM and holds 99.99% of its share capital, CEM holds the concession to Cana Brava Hydroelectric Power Plant located on the Tocantins River, State of Goiás. The Company also shares with Companhia Siderúrgica Nacional—CSN, the controlling interest in Itá Energética S.A.—ITASA, in which it owns 48.75% of voting shares. ITASA is a SPC—Special Purpose Company organized to build and exploit, via joint-venture, by means of consortium, the hydroelectric power plant of Itá, located on the Uruguay River, on the border of the States of Santa Catarina and Rio Grande do Sul. It also holds 99.99% the share capital of Lages Bioenergética Ltda., which has the authorization to exploit the cogeneration unit of Lages, in the Municipality of Lages (SC). The main characteristics of subsidiaries and their businesses are described under Note 7-b.

NOTE 2—PRESENTATION OF FINANCIAL STATEMENTS

All figures (texts and tables) presented in the financial statements and Explanatory Notes are expressed in thousands of Brazilian reais, except when indicated otherwise.

The financial statements are in accordance with accounting principles and practices adopted in Brazil. The main accounting practices adopted by the Company to prepare the financial statements are described below:

Recognition of inflation effects

Only the effects of monetary variations on assets and liabilities indexed as a result of legal and contractual provisions are reflected. In compliance with Law No. 9.249, of 12.26.1995, as of January 1996 the adjustment for inflation ended. Therefore, amounts corresponding to property, plant and equipment and shareholders' equity are adjusted only through 12.31.1995.

General Evaluation Criteria

a) Current and long-term assets

Securities are recorded at cost, with corresponding accrued interest earned until the balance sheet date. Book values are adjusted by creating a provision whenever they exceed average market prices;

the provision for doubtful debtors is associated with credits resulting from transactions made in the Wholesale Electric Energy Market—MAE. Other accounts receivable have guarantees or no record of losses, and therefore no provision is needed (see Note 4);

deferred income tax and social contribution (deferred tax credits) are determined at the rates of 25% and 9%, respectively, in force on the date of the balance sheet, and are recognized based on tax losses and timing differences. The separation between current and long-term assets is in agreement with the expectation of realization of amounts that give origin to such assets;

warehouse/materials in stock are recorded at their average weighted purchase cost, which does not exceed the market value;

indexed assets are adjusted up to the date of the balance sheet;

b) Permanent assets

Investments in subsidiaries and joint subsidiaries are assessed by the equity method of accounting and other investments are recognized at their acquisition cost, which does not exceed the market value;

property, plant and equipment are recorded at the acquisition or construction cost. Depreciation is determined on a the straight-line basis, based on annual rates shown on the table attached to ANEEL Resolution No. 002, of 12.24.1997, and No. 044, of 03.17.1999, based on the book balances recorded at the Registration Units—UC that form the business ventures, as set forth by DNAEE Ordinance No. 815, of 11.30.1994. Average annual depreciation rates determined by the Company and its subsidiaries, in compliance with the above regulations, are shown under Note 8-a;

interest and other financial charges and effects of inflation resulting from financing obtained from third-parties, actually used in property, plant and equipment under construction, are calculated as cost of the corresponding asset;

up to 12.31.1998 interest on shareholders' equity linked to construction work in progress were capitalized, in compliance with the specific laws of the electric industry. As of January 01, 1999, such procedure was discontinued by the Company and starting on January 01. 2002, it was no longer used by Brazil's electric industry due to the change of ANEEL standards regulating the subject;

c) Current and long-term liabilities

Future benefits to employees (post-employment benefits) are recorded based on actuarial evaluation by the Projected Unit Credit Method and adjusted monthly according to contractual indexes for agreed to obligations and complemented by amounts projected by actuarial evaluation (see Note 16);

loans and financing and resulting interest and charges, allocated until the balance sheet date, are adjusted by exchange rates or contractual indexes (see Note 11) and other obligations are recorded at amounts known or determinable, plus corresponding charges and monetary variation incurred, when applicable;

d) Income (Loss) for the period

Income and expenses are recorded in accordance with the accrual basis of accounting;

e) Leasing

Leasing transactions existing in the Company do not have relevant amounts and are recognized directly in income, based on payments provided for in the agreement (see Note 21).

Consolidated financial statements

Investor's investments in the capital of investees are removed, as well as assets and liabilities balances and income and expenses resulting from transactions among consolidated companies.

Components of assets and liabilities and income and expenses of ITASA are consolidated in the proportion of Company's interest in its share capital, due to the shared control (see Note 7-b).

Due to the high proportion of interest of the holding company in the other subsidiaries (see Note 7-b), there was no effect of the minority shareholders' interest in the consolidated financial statements.

NOTE 3—SECURITIES

	2004	2003
Current		
Certificate of Deposit—CDB	440,035	290,285
Treasury Bonds—LFT	167,666	28,425
Negative adjustments in swap transactions	(13,698)	—
Committed transactions	33,925	21,978
Central Bank Notes—NBC—E	23,776	—
	651,704	340,688
Provision for investment losses	(17,427)	—
	634,277	340,688
Noncurrent		
Certificate of Deposit—CDB	35,550	—
	35,550	—

Securities are recorded at cost plus corresponding accrued interest earned until 12.31.2004, whose amounts do not exceed average market prices, and may be negotiated regardless of their maturities, without prejudice to earnings.

The Company has Certificates of Deposit and Brazilian Treasury Bonds in an Exclusive Investment Fund, both indexed to the CDI, and swap transactions carried out in the over-the-counter market recorded and settled at Cetip, in which the Fund has assets in exchange rates and liabilities in CDI.

Investments of the Exclusive Investment Fund are consolidated in the financial statements and separated according to the nature of their assets.

As a result of the intervention by the Central Bank of Brazil in Banco Santos S.A. on 11.12.2004, which created uncertainties about the possibility of withdrawing investments in Certificates of Deposit

that the Company and its Subsidiary Companhia Energética Meridional—CEM have with such financial institution, the management of the Company and of CEM decided to make provisions equivalent to the balances of such investments, in the amounts of R$11,896 and R$5,531, respectively.

NOTE 4—CONSUMERS, CONCESSIONAIRES AND HOLDERS OF PERMISSIONS

	2004				2003
		Overdue			
	To fall due	For 90 days or less	For more than 90 days	Total	Total
Current					
Free consumers	32,458	1,641	1,187	35,286	22,068
Concessionaires	170,250	—	—	170,250	163,044
Sellers	38,262	1,152	1,110	40,524	14,243
Exports	—	—	740	740	—
Transactions within MAE	151,522	—	13,950	165,472	199,270
	392,492	2,793	16,987	412,272	398,625
(–) Provision for Doubtful Debtors	(119,596)	—	(12,029)	(131,625)	(143,720)
	272,896	2,793	4,958	280,647	254,905
Long-term					
Transactions within MAE	14,920	—	—	14,920	23,246
	14,920	—	—	14,920	23,246

The invoices of electric energy provided to customers classified as "Free consumers" are due on the 15th of the month following the energy provision.

The energy supply invoices issued to concessionaires are divided in three equal payments, due on the 15th and 25th day of the month following the supply and on the 5th day of the second following month.

The amount of R$13,950 overdue for more than 90 days refers to a debit of a defaulting agent in the 1st settlement of the Wholesale Electric Energy Market—MAE, carried out on 12.30.2002. Such amount is subject to bilateral negotiations. Nevertheless, due to the uncertainties of receiving such debt, the Company's Management decided to create a provision for doubtful debtors in the amount of R$12,029, regardless of actions that may be taken in this case.

In September of 2003, the Company made a provision in the amount of R$143,720 due to the uncertainties regarding the realization of credits resulting from transactions made within MAE in the period from September 2000 through September 2002, whose debtor agents filed lawsuits because they disagreed with the interpretation adopted by such body in connection with ANEEL Order N. 288, of 05.16.2002. In the second semester of 2004, certain authors of those lawsuits agreed to settle the amount due which resulted in a reversal of R$24,124 for the Company.

NOTE 5—DEFERRED TAX CREDITS

	2004				2003
Credit type	Tax basis	Income tax	Social contribution	Total	Total
Provision for losses UTE Jacuí	606,171	—	54,555	54,555	87,458
Remuneration of Construction Work in Progress—RIC	249,105	33,433	—	33,433	33,433
Post-employment benefits	150,929	37,732	13,584	51,316	46,405
Provision for doubtful debtors	131,625	32,906	11,846	44,752	48,866
Provision for contingencies	111,307	27,827	10,017	37,844	31,517
Provision for accelerated depreciation UTE William Arjona	35,214	8,803	3,169	11,972	7,245
Provision for losses with ICMS credits	32,977	8,244	2,968	11,212	54
Provision for extensive maintenance	30,709	7,678	2,764	10,442	8,007
Employees profit-sharing program	6,500	1,625	585	2,210	2,961
Provision for management bonus	4,000	1,000	360	1,360	1,190
Provision for purchase of electric energy	1,467	367	132	499	21,329
Provision for attorneys' fees	606	151	55	206	198
Provision for financial investment losses	17,427	4,357	1,569	5,926	—
Other provisions	—	—	—	—	5
Tax loss	18,002	4,501	—	4,501	5,793
Negative basis for social contribution	162,086	—	14,588	14,588	19,715
		168,624	116,192	284,816	314,176
Classification of deferred tax credits:					
Current		73,073	25,100	98,173	122,329
Noncurrent		95,551	91,092	186,643	191,847
		168,624	116,192	284,816	314,176

The realization of deferred tax credits resulting from timing differences will be made upon payment of provisions made or, when applicable, upon realization of losses recorded in the provision. With regard to deferred tax credits resulting from tax losses and negative basis for social contribution, realization will be made by offsetting their basis, limited to 30% of taxable income in following years.

As mentioned in Note 8-e, in June 2004 the Company transferred 33.33% of the Jacuí business venture to the company Elétrica Jacuí S.A.—ELEJA and, in May 2004, it wrote-off the equipment which had become unusable or obsolete related to the project. As a result, there was a reversal of part of the provision for economic losses, in the amount of R$365,581. The realization of the balance of provision for economic losses of UTE Jacuí is based on the assumption of the conclusion of the project. In such situation, the provision will be realized in the proportion to the business venture depreciation, after it begins to operate. The amount of deferred tax credits, already recognized for accounting purposes, refers to the Contribution on Net Income and was recorded in 1997. The Company's management is waiting for some pending issues of the project to be solved in order to recognize the deferred Income Tax on such provision, in the amount of R$151,543, when the total deferred tax credits will be complemented, observing the limit of ten years for its recovery.

Technical feasibility studies examined by the Audit Committee and approved by the management bodies of the Company and its subsidiaries ITASA and CEM indicate that deferred tax credits existing

on 12.31.2004 will be totally recovered by future taxable income. Such technical studies are in accordance with CVM Instruction No. 371, of 06.27.2002.

The timeframe for realization of such assets and their recovery by generating future taxable income have been estimated as follows:

Type of asset	2005	2006	2007	2008	2009	Next 2 years	Next 3 years	After 2014	Total
Provision for losses—UTE Jacuí	—	—	—	—	2,250	4,910	7,365	40,030	54,555
Remuneration of Construction Work in Progress—RIC	3,343	3,343	3,343	3,343	3,344	6,687	10,030	—	33,433
Other timing differences	33,532	11,749	6,376	20,423	19,605	85,195	859	—	177,739
Tax loss	1,050	1,093	1,589	769	—	—	—	—	4,501
Negative basis for social contribution	11,174	2,523	568	323	—	—	—	—	14,588
Deferred tax credits, recorded	49,099	18,708	11,876	24,858	25,199	96,792	18,254	40,030	284,816
Deferred tax credits—Jacuí	—	—	—	—	7,440	16,235	24,352	103,516	151,543
Deferred tax credits—RIC	—	—	—	—	—	—	—	28,843	28,843
	49,099	18,708	11,876	24,858	32,639	113,027	42,606	172,389	465,202

The realization of RIC is carried out in the proportion of the depreciation of corresponding assets, whose term currently exceeds 10 years, which results in deferred tax credits not recognized, in the amount of R$28,843 (R$32,244 on 12.31.2003), in compliance with CVM Instruction N. 371/02.

NOTE 6—RECONCILIATION OF TAXES, IN INCOME

	2004		2003		2002	
	Social contribution	Income tax	Social contribution	Income tax	Social contribution	Income tax
Income before taxes	**861,035**	**861,035**	**660,504**	**660,504**	**(345,773)**	**(345,773)**
Permanent differences						
Additions						
Equity in the earnings of subsidiary companies	—	—	254	254	—	—
Amortization of goodwill	—	6,746	—	6,746	—	2,288
Bonus and 13th month pay of directors	—	1,273	—	1,688	—	1,068
Donations with fiscal incentive	521	521	585	585	—	—
Non-deductible donations	858	858	674	674	445	445
Other nondeductible expenses	921	952	1,050	1,094	609	623
Exclusions						
Provision for losses UTE Jacuí	—	(365,581)	—	(6,101)	—	—
Remuneration of Construction works in Progress—RIC	—	(98,492)	—	(13,461)	—	(147,266)
Interest on shareholders' equity	(255,000)	(255,000)	(234,000)	(234,000)	—	—
Adjustment of subsidiary taxed by presumed profit	(3,433)	(4,424)	—	—	—	—
Tax basis on income	604,902	147,888	429,067	417,983	(344,719)	(488,615)
Rates	9%	25%	9%	25%	9%	25%
Social contribution and income tax	(54,441)	(36,973)	(38,616)	(104,496)	31,025	122,154
Tax incentives	—	879	—	651	(11)	(339)
Additional 10% on income up to R$20 per month	—	94	—	59	—	24
Adjustment of negative basis of CSLL before 1992	—	—	(1,074)	—	—	—
Adjustment of the deferred social contribution rate	—	—	—	—	13,614	—
Recognition of deferred tax credits from previous periods	1,166	3,203	—	—	(1,116)	(3,099)
Other	60	169	(18)	144	—	—
Social contribution on income and income tax	(53,215)	(32,628)	(39,708)	(103,642)	43,512	118,740
Composition of taxes:						
Current	(20,201)	(45,269)	(49,498)	(141,309)	(5,748)	(13,428)
Deferred	(33,014)	12,641	9,790	37,667	49,260	132,168
	(53,215)	(32,628)	(39,708)	(103,642)	43,512	118,740

NOTE 7—INVESTMENTS

a) Composition

	2004	2003
Permanent interests valued by the equity method of accounting		
Itá Energética S.A.—ITASA Goodwill	12,587	14,875
Companhia Energética Meridional—CEM Goodwill	35,662	40,120
	48,249	54,995
Permanent interests valued by acquisition cost		
Electric Energy Sales Chamber Interest quota	3	3
	48,252	54,998
Assets and rights for future use and meant for disposal	1,742	1,742
Other investments	371	121
	50,365	**56,861**

b) Permanent interests

b.1—Itá Energética S.A.—ITASA (joint subsidiary)

The shares representing the share capital of ITASA are held by Tractebel Energia, Companhia Siderúrgica Nacional—CSN and Companhia de Cimento Itambé, in the proportion of 48.75%, 48.75% and 2.50%, respectively.

ITASA's purpose is to exploit the Hydroelectric Power Plant Itá in joint venture, by means of consortium, upon concession granted by the Federal Government through the National Agency of Electric Energy—ANEEL. The business venture is located on the Uruguay River, on the border of the States of Santa Catarina and Rio Grande do Sul, between the Municipalities of Itá (SC) and Aratiba (RS) and has an installed capacity of 1,450 MW resulting from 5 generation units of 290 MW, and the last unit started to operate in March 2001.

Pursuant to the Consortium Agreement, ITASA is entitled to 60.5% of 668 MW average, which corresponds to the Ensured Energy of UHE Itá.

The information relating to the interest in the joint subsidiary is shown below:

	2004	2003
Amount of common shares of share capital	520,219,172	520,219,172
Amount of common shares owned by Tractebel Energia	253,606,840	253,606,840
Interest %	48.75	48.75
Share Capital	426,300	426,300
Shareholders' Equity	520,516	510,136
Income for the year	13,613	15,079

The economic basis for the goodwill in the investment acquisition is the expectation of future income and it is being amortized over 10 years.

The determination of the goodwill is based on cash flows calculated by an expert financial institution, according to assumptions applicable to the context of the investee, projected for the concession period, and one renewal of the concession.

The valuation considered the debt/equity ratio of 50/50 to implement the Itá project, using discount rates of 11.0% for third-party capital and 11.5% for equity capital.

The goodwill amortized in the year amounted to R$2,288 (R$2,289 in 2003, and R$2,288 in 2002).

The main account groups under assets, liabilities and shareholders' equity of the joint subsidiary are shown below, and they have been consolidated in proportion to Company's investment in the share capital of the subsidiary:

	2004	2003
ASSETS		
Current Assets	54,885	150,252
Long-term assets	13,942	7,813
Permanent assets	1,105,752	1,147,189
	1,174,579	1,305,254
LIABILITIES		
Current Liabilities	108,855	192,856
Long-term Liabilities	545,208	602,262
Shareholders' Equity	520,516	510,136
	1,174,579	1,305,254

	2004	2003	2002
INCOME			
Gross operating income	**322,630**	**363,003**	**201,020**
Deductions from operating income	**(28,546)**	**(16,872)**	**(7,248)**
NET SALES INCOME	294,084	346,131	193,772
ELECTRIC ENERGY COSTS			
Electric energy purchased for resale	(93,870)	(112,325)	(1,900)
Electric energy production cost	(52,862)	(46,996)	(46,445)
	(146,732)	(159,321)	(48,345)
GROSS PROFIT	147,352	186,810	145,427
OPERATING EXPENSES			
Selling expenses	(22,469)	(18,792)	(15,411)
General and administrative expenses	(19,309)	(21,606)	(18,946)
	(41,778)	(40,398)	(34,357)
SERVICE INCOME	105,574	146,412	111,070
NET FINANCIAL EXPENSES	(98,440)	(123,119)	(136,475)
OPERATING INCOME (LOSS)	7,134	23,293	(25,405)
NON OPERATING INCOME (LOSS)	(1)	233	7
INCOME (LOSS) BEFORE TAXES	7,133	23,526	(25,398)
Income and social contribution taxes	6,480	(8,447)	(6)
NET INCOME (LOSS) FOR THE YEAR	13,613	15,079	(25,404)

b.2—Companhia Energética Meridional—CEM (subsidiary)

CEM holds the concession of Cana Brava Hydroelectric Power Plant, located on the Tocantins River, in the north of the State of Goiás, with an installed capacity of 450 MW and 273.4 MW average of assured energy. The concession to build and exploit the business venture is valid for 35 years, as from 08.27.1998.

The information relating to the interest in the subsidiary is shown below:

	2004			2003
	Common shares	Preferred shares	Total	Total
Amount of shares of share capital	79,063,566	146,107,126	225,170,692	225,170,692
Amount of shares owned by Tractebel Energia	79,063,562	146,107,126	225,170,688	225,170,688
Interest %	99.99	100.00	99.99	99.99
Share capital	78,748	145,474	224,222	224,222
Shareholders' equity	—	—	348,563	227,000
Income for the year	—	—	68,785	94,638

The economic basis for the goodwill in the acquisition of controlling interest is the expectation of future income and it is being amortized during 10 years, starting in January 2003.

The determination of the goodwill is based on cash flow calculated by an expert financial institution, according to assumptions applicable to the context of the investee, projected for 35 years, the concession period of the plant, adjusted to present value at a discount rate of 14% p.a.

The valuation considered a debt/equity ration of 70/30 for the plant construction. Part of the goodwill is associated with the subscription bonuses purchased in the transaction, which have been used to make investments during the pre-operating stage of the investee.

The goodwill amortized in the year amounted to R$ $4,458 (R$4,457 in 2003).

b.3—Delta Energética S. A. (subsidiary)

The Company owns 9,999 of the 10,000 shares that compose the share capital of Delta. This subsidiary was formed on 10.31.2001, under the name Delta Participações S.A. and on 04.26.2004 its company name was changed to Delta Energética S.A.. To this date, the subsidiary has not been in operation.

b.4—Tractebel Energia Comercializadora Ltda. (subsidiary)

The share capital, on 12.31.2004, amounts to R$1,000, represented by 1,000,000 capital shares, of which the Company owns 999,999.

The information relating to the interest in the subsidiary is shown below:

	2004	2003
Shares that compose the share capital	1,000,000	26,000
Shares owned by Tractebel Energia	999,999	25,999
Interest %	99.99	99.99
Share capital	1,000	26
Shareholders' equity	1,423	10
Income for the year	439	—

b.5—Lages Bioenergética Ltda. (subsidiary)

Company formed on 06.26.2002, authorized by the National Agency of Electric Energy—ANEEL on 10.30.2002 to be an Independent Producer, upon implementation of the thermoelectric generation center of Lages, located in the municipality of Lages, State of Santa Catarina, with a steam turbogenerator of 28 MW, using wood waste as fuel. The cogeneration unit has a restricted interest transmission system, composed of a substation with transformer of 31,250 kVA—13.8/138 kV and a transmission line of 138 kV, in a simple circuit, approximately 5 km long. The authorization to

implement and exploit the business venture is valid for 30 years, starting on 10.30.2002. The construction work started in January 2003 and were scheduled to be completed by April 2004, however, the schedule advanced and the work was completed on 12.16.2003. The National Agency of Electric Energy—ANEEL, by means of Order N.

990, of 12.19.2003, authorized the beginning of the commercial operations of the generation center as of 12.23.2003,

The information relating to the interest in the subsidiary is shown below:

	2004	2003
Shares that compose the share capital	30,529,984	30,529,984
Shares owned by Tractebel Energia	30,529,983	30,529,983
Interest %	99.99	99.99
Share capital	30,530	30,530
Shareholders' equity	37,067	30,530
Income for the year	6,537	—

NOTE 8—PROPERTY, PLANT AND EQUIPMENT

a) Composition

	2004				2003
	Average depreciation rate	Adjusted cost	Accumulated amortization depreciation	Net amount	Net amount
Property, plant and equipment in operation					
Intangible assets					
Right to exploit UHE Cana Brava	3.2	88,664	(6,950)	81,714	84,560
Tangible assets					
Hydroeletric generation					
UHE Salto Santiago	2.5	638,767	(459,991)	178,776	194,146
UHE Salto Osório	2.8	288,901	(224,268)	64,633	72,455
UHE Passo Fundo	2.5	123,257	(86,858)	36,399	39,063
UHE Itá (consortium)	2.3	1,779,329	(178,581)	1,600,748	1,641,381
UHE Machadinho (consortium)	2.4	178,888	(11,468)	167,420	171,017
UHE Cana Brava	2.5	869,322	(50,702)	818,620	838,288
		3,878,464	(1,011,868)	2,866,596	2,956,350
Thermoeletric Generation					
Jorge Lacerda Complex	4.3	2,453,365	(1,097,029)	1,356,336	1,426,305
UTE Charqueadas	4.4	55,006	(47,007)	7,999	9,179
UTE Alegrete	4.1	8,101	(7,169)	932	879
UTE William Arjona	4.3	139,900	(27,370)	112,530	132,145
Lages Cogeneration Unit	4.3	57,843	(2,324)	55,519	—
		2,714,215	(1,180,899)	1,533,316	1,568,508
Communication system	6.1	1,102	(433)	669	788
General equipment and other	10.0	31,388	(17,101)	14,287	14,791
		6,713,833	(2,217,251)	4,496,582	4,624,997
Property, plant and equipment under construction					
Hydroeletric generation					
UHE Itá (late costs)		5,471	—	5,471	5,987
UHE Machadinho (late costs)		—	—	—	1,090
UHE Cana Brava		1,602	—	1,602	2,132
UHE S, Santiago (addition work)		17,394	—	17,394	238
Other		194	—	194	1,473
		24,661	—	24,661	10,920
Thermoeletric Generation					
UTE Jacuí		52,320	—	52,320	83,314
UTE J. Lacerda (addition work)		7,680	—	7,680	20,720
UTE Charqueadas (addition work)		421	—	421	636
Lages Cogeneration Unit		9,646	—	9,646	61,052
Other		15	—	15	199
		70,082	—	70,082	165,921
General equipment and other		1,794	—	1,794	3,846

	2004			2003
	Average depreciation rate	Adjusted cost	Accumulated amortization depreciation	Net amount	Net amount
		96,537	—	96,537	180,687
Total property, plant and equipment		6,810,370	(2,217,251)	4,593,119	4,805,684
Special obligations		(56,689)	—	(56,689)	(56,689)
		6,753,681	(2,217,251)	4,536,430	4,748,995

b) Change to property, plant and equipment

	In operation	Under construction	Total
Balance on 12.31.2001	3,774,452	984,275	4,758,727
Acquisitions	—	203,589	203,589
Financial charges on debts, net	—	150,680	150,680
Transfers	1,200,735	(1,200,735)	—
Depreciation	(181,082)	—	(181,082)
Write-offs	(2,713)	—	(2,713)
Balance on 12.31.2002	4,791,392	137,809	4,929,201
Acquisitions	—	92,450	92,450
Financial charges on debts, net	—	856	856
Financial charges and adjustments of obligations linked to construction	—	336	336
Transfers	55,033	(55,033)	—
Depreciation	(219,462)	—	(219,462)
Reversal of Remun, of Construction Work in Progress—RIC—UTE Jacuí	—	6,100	6,100
Write-offs	(1,966)	(1,831)	(3,797)
Balance on 12.31.2003	4,624,997	180,687	4,805,684
Acquisitions	—	38,016	38,016
Financial charges on debts, net	—	(48)	(48)
Financial charges and adjustments of obligations linked to construction	—	(3,116)	(3,116)
Transfers	87,516	(87,516)	—
Depreciation	(215,716)	—	(215,716)
Write-offs	(215)	(31,486)	(31,701)
	4,496,582	96,537	4,593,119
Special obligations	(56,689)	—	(56,689)
Balance on 12.31.2004	4,439,893	96,537	4,536,430

c) Special obligations

Special obligations refer to liabilities linked to the electric energy utility and represent amounts invested in the business ventures under concession, with Federal Government funds and funds from donations not conditioned to any return for the benefit of the donor. The settlement of such obligations will

happen at the end of the corresponding concessions, established by the Granting Authority. These obligations are composed as follows:

	2004	2003
Donations and subventions meant for investments	48,062	48,062
Reversal and amortization	2,230	2,230
Interest of Federal Government	3,758	3,758
Other	2,639	2,639
	56,689	56,689

d) Concessions and authorizations by the regulating authority

The Company and its subsidiaries hold the following concessions and authorizations to exploit electric energy:

	Holder of concession or authorization	Installed capacity MW	Date of concession/ authorization	End date
I—Concessions				
UHE Salto Santiago	Holding Company	1,420	09.28.1998	09.28.2028
UHE Salto Osório	Holding Company	1,078	09.28.1998	09.28.2028
UHE Passo Fundo	Holding Company	226	09.28.1998	09.28.2028
UHE Itá	Holding Co./ ITASA	1,450	12.28.1995	10.16.2030
UHE Machadinho	Holding Company	1,140	07.15.1997	07.15.2032
UHE Cana Brava	CEM	450	08.27.1998	08.27.2033
II—Authorizations				
Complexo Jorge Lacerda	Holding Company	857	09.25.1998	09.28.2028
UTE Charqueadas	Holding Company	72	09.25.1998	09.28.2028
UTE Alegrete	Holding Company	66	09.25.1998	09.28.2028
UTE William Arjona	Holding Company	190	06.02.2000	04.28.2029
UTE Jacuí	Holding Company	350	02.07.2002	02.07.2032
UTE Lages	Lages Bioenergética	28	10.30.2002	10.30.2032

The concession relating to UHE Itá is shared with the joint subsidiary Itá Energética S.A.—ITASA (see Note 7-b.1).

The concession of UHE Machadinho is shared with other concessionaires that compose the Machadinho Consortium, of which the Company is the leader and holds an interest of 16.94%.

e) Jacuí Thermoelectric Power Plant

On 12.03.1999 the Company, in compliance with the requirements under the Privatization Notice, communicated to the National Agency of Electric Energy—ANEEL its intent to complete the work of UTE Jacuí, and was authorized by such regulating agency to implement the project.

Since then, the Company has been using all efforts to make the business venture feasible. Nevertheless, several factors relating to regulation, entering into agreements regarding the electric energy to be generated, contracting an EPC, among others, posed serious difficulties to the business feasibility which counts exclusively on the Company, which resulted in the consideration of alternative solutions.

Therefore, in June 2004 the Company, within the context of a strategic joint venture, transferred 33.33% of the business venture to Elétrica Jacuí S.A.—ELEJA, for R$29,000, pursuant to the

Agreement of Transfer of Interest in Business Venture entered into by the parties. ELEJA is a Special Purpose Company (SPC) organized by Riomaggiore Mineração Ltda. for the special purpose of completing the project. The transfer included rights, licenses, authorizations, projects, studies, drawings, blueprints and documents, books and tax enrollments, in addition to assets, land, equipment, civil engineering works and other facilities, that compose a substantial part of the assets needed and/or adequate for the implementation of the business venture located in the Municipality of Charqueadas, State of Rio Grande do Sul.

In May 2004, the Company had written-off assets linked to the Jacuí project that would become unusable or obsolete, based on an opinion report issued by specialized companies. The written-off assets were given to the Center of Automation and Computer Technology—CTAI, an agency linked to SENAI/SC and will be used for training in its professional skill building courses.

The amounts associated with the written-off assets, as a result of the above mentioned facts, are the following:

	Obsolescence	Disposal	Total
Gross cost	77,258	402,036	479,294
RIC	(13,650)	(71,241)	(84,891)
Subtotal	63,608	330,795	394,403
Reversal of provision	(62,541)	(303,040)	(365,581)
Net book value	1,067	27,755	28,822

f) Restricted assets

Pursuant to Articles 63 and 64 of Decree 41.019, of February 26, 1957, assets and facilities used in the production, transmission, distribution, including sale of electric energy, are restricted to such services, and may not be removed, disposed of, assigned or given as mortgage guarantee without the previous and express consent of the Regulating Authority, Resolution 20/99 of ANEEL regulates the removal of restrictions on assets of Electric Power Utility concessions, granting previous authorization for the removal of restrictions on assets unserviceable to the concession, when meant for disposal, and further sets forth that the proceed of disposals be deposited in a blocked bank account and that such funds be invested in the concession.

g) Assets of the federal government used by the company

The Company exercises possession and operates the Alegrete Thermoelectric Power Plant, composed of two generation units with a total capacity of 66 MW and a residential village with 15 houses, located in the Municipality of Alegrete, RS, owned by the Federal Government and granted under special use.

NOTE 9—UNITS 4 AND 5 OF UTE WILLIAM ARJONA

Generation units 4 and 5 of the thermoelectric plant of William Arjona, with a total power of 70 MW, use natural gas to generate electric energy and have been implemented with the specific purpose of meeting the needs of Brazilian Trader of Emergency Energy—CBEE, governed by the Electric Energy Supply Agreement executed on 01.10.2002, effective until 12.31.2004.

The Company's management was studying the possibility of ceasing the operation of such generation units at the end of the agreement with CBEE. In line with this possibility, the Company amortized the economic value of such assets in the period they were used, reaching a residual value of R$68,485 on 12.31.2004, compatible with the estimated disposal value, in the event such hypothesis was confirmed.

Within such context, the amount of R$13,906 is being recognized in the income of this year, totaling R$35,214 when added to amortization relating to 2002 and 2003. Such amounts were considered as "timing differences" for tax purposes.

On October 26, 2004 the Management of the Company communicated to the Advisory Department of the Ministry of Mines and Energy that, after the end of the agreement with CBEE, the generation units under reference will be maintained and will remain available for centralized operation, according to the standards and procedures of the National Electric System Operator—ONS, as from January 1st. 2005, on the same conditions as units 1, 2 and 3.

Therefore, the depreciation process will continue with no effects on future income, since the accelerated amortization carried out during the agreement with CBEE will be reverted simultaneously with the depreciation.

NOTE 10—SUPPLIERS

	2004	2003
Electric energy	26,909	22,246
Fossil fuels	37,445	31,843
Materials and services	52,932	34,419
	117,286	88,508

NOTE 11—LOANS AND FINANCING

The main information on loans and financing in domestic and foreign currency are as follows:

a) Composition:

	2004			2003		
	Principal, interest and charges			Principal, interest and charges		
	Current	Long-term	Total	Current	Long-term	Total
Foreign Currency						
National Treasury Office	104,561	414,074	518,635	103,309	560,165	663,474
Financial Institutions	48,857	491,788	540,645	44,958	571,211	616,169
	153,418	905,862	1,059,280	148,267	1,131,376	1,279,643
Domestic Currency						
ELETROBRÁS	66,406	247,802	314,208	60,111	314,208	374,319
Financial Institutions	57,888	385,745	443,633	50,119	413,871	463,990
	124,294	633,547	757,841	110,230	728,079	838,309
	277,712	1,539,409	1,817,121	258,497	1,859,455	2,117,952

b) Changes to loans and financing

	Current	Long-term
Balance on 12.31.2001	140,038	1,732,690
Incoming funds	520,000	165,581
Transfers	211,003	(211,003)
Charges generated	213,686	3,880
Monetary variation generated	34,158	580,999
Interest on escrow	—	(20,451)
Amortization	(611,620)	—
Balance on 12.31.2002	507,265	2,251,696
Incoming funds	—	49,163
Transfers	239,980	(239,980)
Charges generated	199,328	7,345
Monetary variation generated	(21,134)	(207,404)
Interest on escrow	—	(1,365)
Amortization	(666,942)	—
Balance on 12.31.2003	258,497	1,859,455
Incoming funds	—	13,771
Transfers	275,964	(275,964)
Charges generated	173,497	5,498
Monetary variation generated	(8,737)	(53,191)
Interest on escrow	—	(10,160)
Amortization	(421,509)	—
Balance on 12.31.2004	277,712	1,539,409

c) Composition by type of foreign currency and domestic indexes:

	2004			2003		
	Currency thousand	Reais	%	Currency thousand	Reais	%
Foreign Currency						
US dollar—USD	295,767	785,082	43.20	316,681	914,953	43.20
Pound Sterling—GBP	11,474	58,814	3.24	16,306	84,506	3.99
Euro—EUR	59,507	215,384	11.85	76,750	280,184	13.23
		1,059,280	58.29		1,279,643	60.42
Domestic Currency						
IVRRJR (based on UFIR)	—	314,208	17.29		374,319	17.67
URTJLP	—	391,523	21.55	—	402,364	19.00
Not indexed	—	52,110	2.87	—	61,626	2.91
		757,841	41.71		838,309	39.58
		1,817,121	100.00		2,117,952	100.00

d) Variation of foreign currencies and indexes:

	%		
Currency—index	2004	2003	2002
US dollar—USD	(8.13)	(18.23)	52.27
Pound Sterling—GBP	(1.09)	(8.98)	68.77
Euro—EUR	(0.85)	(1.37)	79.35
ICF (based on IGP-DI)	—	1.98	29.95
URTJLP	3.66	12.82	3.71

e) Maturity of long-term loans, financing and charges

	2004	2003
2005	—	270,620
2006	289,044	294,020
2007	370,297	375,457
2008	156,534	160,106
2009	145,224	147,736
2010	139,052	141,402
From 2011—2024	439,258	470,114
	1,539,409	**1,859,455**

f) Loans and financing are subject to interest and charges at fixed and floating rates, distributed as follows:

Domestic market

Fixed rates from 11.90% to 12.00% p.a. (2003, 11.90% to 12.00% p.a. and in 2002, 6.00% to 12.00% p.a.)

Floating rates: 12.00% to 18.18% p.a. (2003, 13.25% to 18.49% p.a. and in 2002, 14.00% to 26.00% p.a.)

International market

Fixed rates from 6.00% to 10.43% p.a. (2003, 6.00% to 8.49% p.a. and in 2002, 3.00% to 8.49% p.a.)

Floating rates from 2.77% to 9.29% p.a. (2003, 1.73% to 9.95% p.a. and in 2002, 2.22% to 9.99% p.a.)

NOTE 12—DEBENTURES

a) Companhia Energética Meridional—CEM

A Subscription and Payment of Debentures Agreement was entered into by and between the Subsidiary and the National Bank of Economic and Social Development—BNDES on May 19, 1999, and from May to December of 1999, 7,773 debentures were subscribed and paid-in, whose balance adjusted up to 12.31.2004, amounts to R$98,107, R$10,008 under current liabilities and R$88,099 under long-term liabilities (up to 12.31.2003, R$101,536, R$9,146 under current liabilities and R$92,390 under noncurrent liabilities).

Interest on debentures is based on TJLP plus 4% p.a.; interest is paid every six months, from 10.01.1999 until 04.01.2013.

The amount corresponding to TJLP that exceeds 6% p.a. will be capitalized, and will become part of the principal of debentures.

The amortization of debentures' principal started on 10.01.2003 with final maturity on 04.01.2013, and occurs every six months based on an increasing amortization schedule that varies from 3.0625%, for the first amortization, to 7.5737% for the last installment, due on 04.01.2013;

b) Itá Energética S.A.—ITASA

On March 7, 2001, the joint subsidiary issued two series of 8,400 nonconvertible debentures each, publicly issued, in the total amount of R$168,000, paid in on March 23, 2001. The adjusted balance on 12.31.2004, amounts to R$78,872, R$13,352 under current liabilities and R$65,520 under long-term liabilities (up to 12.31.2003, R$85,801, R$12,091 under current liabilities and R$73,710 under long-term liabilities).

Interest on debentures is paid annually; on the 1st series as from December 1, 2001 and on the 2nd series as from June 1, 2002 and are determined as set forth below:

1st series: from 12.01.2001 to 12.01.2003—IGP-M + 11.2% p.a.
from 12.02.2003 to 12.01.2013—IGP-M + 9.4% p.a.
2nd series: from 06.01.2002 to 06.01.2004—IGP-M + 11.2% p.a.
from 06.02.2004 to 06.01.2013—IGP-M + 9.4% p.a.

The amortization of the principal amount of the debentures will be made in annual installments; amortization of the 1st series started on December 1, 2004, with final maturity on December 1, 2013 and amortization of the 2nd series, started on June 1, 2004, with final maturity on June 1. 2013.

NOTE 13—ESTIMATED OBLIGATIONS

	2004			2003
	Current	Long-term	Total	Total
Provision for labor legislation	8,616	—	8,616	7,706
Provision for extensive maintenance	15,921	14,788	30,709	23,549
Provision for management bonus	4,000	—	4,000	3,500
Provision for profit-sharing	6,500	—	6,500	8,500
Provision for purchase of electric energy	1,467	—	1,467	62,731
Other	36	2,545	2,581	894
	36,540	17,333	53,873	106,880

Provision for labor legislation refers to estimated vacation pay, vacation bonus and corresponding social charges.

Seeking to properly measure income of future years, the Company records provisions for extensive maintenance of the generation complex, based on an executive plan to preserve the operating conditions of plants.

The provision for purchase of electric energy refers to the amount for which the Company is responsible, due to ITASA exposure in MAE during the period from June 2001 to February 2002, as a result of ANEEL Order N. 288/2002. The amounts resulting from such exposure were recognized by ITASA under "prepaid expenses" and were being amortized simultaneously to the realization of revenues coming from the extraordinary adjustment of the energy price contracted by its shareholders, granted to maintain the economic and financial balance of the corresponding agreements of purchase

and sale of electric energy entered into between the parties. The appendixes to the agreements executed for such purpose were valid until 01.31.2005.

However, studies conducted by ITASA management showed that extraordinary adjustments invoiced to partners, up to June 2004, were enough to ensure the economic and financial balance of the agreements mentioned above. Therefore, on 06.21.2004, a new appendix to the Agreement of Purchase and Sale of Electric Energy was executed, accelerating the end of the validity of the temporary extraordinary adjustment, in connection with 167 MW, from 01.31.2005 to 06.30.2004. As a result, the Company made the reversal of the provision existing for such purpose, in the amount of R$23,777.

The extraordinary adjustment resulting from the appendix to the agreement of 61 MW, entered into with ITASA, will continue to be effective until the end of its term, on 01.31.2005 (see Note 23).

NOTE 14—PROVISIONS FOR CONTINGENCIES

There are tax delinquency notices and preliminary judicial notices against the Company that are being contested administratively, as well as lawsuits at various court levels, which in the opinion of legal advisors imply probable risks. All such lawsuits are provisioned at amounts deemed sufficient to cover contingencies, as shown below:

	2004		2003	
	Provision	Deposits in court	Provision	Deposits in court
Labor Contingencies				
Employment relationship and rehiring	19,182	11,824	18,642	12,405
Risk premium	974	491	904	388
Overtime	698	281	716	274
Salary parity and job classification	689	179	852	293
Overtime while in commuter transportation	820	190	1,478	188
Other	2,062	2,408	2,853	2,141
	24,425	15,373	25,445	15,689
Civil Lawsuit Contingencies				
Suppliers	31,020	—	25,734	—
Affected by UHE Itá	2,451	—	7,327	—
Actual damages and loss of profits	967	—	1,649	—
Occupational illness and accident	18,419	—	18,160	—
Other	2,654	2	2,061	—
	55,511	2	54,931	—
Tax Contingencies				
Social Contribution	11,066	5,034	9,540	4,477
INSS (Social security)	18,366	5,641	6,983	3,029
	29,432	10,675	16,523	7,506
	109,368	26,050	96,899	23,195

The Company is a party in lawsuits that, in the opinion of legal advisors based on experiences of similar cases, do not pose a probable risk and, therefore, have not been recognized in the financial statements, The amounts involved are detailed below:

	2004			2003		
	Possible risk	Remote risk	Total	Possible risk	Remote risk	Total
Labor Contingencies	9,261	11,269	20,530	7,215	9,568	16,783
Civil Lawsuit Contingencies	19,090	24,048	43,138	38,275	12,129	50,404
	28,351	35,317	63,668	45,490	21,697	67,187

NOTE 15—CONCESSIONS PAYABLE

The subsidiary Companhia Energética Meridional—CEM will pay to the Federal Government the amounts shown below for the concession for exploitation of the hydraulic energy potential of the hydroelectric utilization of Cana Brava, in monthly installments equivalent to 1/12 of the corresponding amounts of annual payment, adjusted based on the annual variation of the General Price Index—Market—IGP-M:

Year	Payment starts on	Annual amount	Total amount
1	—	1	1
2-6	—	—	—
7-25	08.30.2004	680	12,920
26-35	08.30.2023	61,280	612,800
			625,721

The flow of payments above is set forth under Section Six of the Concession Agreement. In order to adequately reflect the granting of remunerated concession and corresponding obligation before the Federal Government in assets and liabilities, CEM recorded this amount under intangible assets and current and noncurrent liabilities.

Taking into consideration that values under the agreement are determined at future prices, CEM adjusted them to present value based on a discount rate of 10% p.a., as provided in the Invitation to Bid N. 04/97 for the bidding of the concession under reference. Until the commercial start-up of the Cana Brava plant, the adjustment of liabilities based on the discount rate and variation of IGP-M price index was capitalized in intangible assets and, thereafter, recognized directly in income.

The net present value balance of this obligation, adjusted up to 12.31.2004, amounts to R$161,889, R$1,472 under current liabilities and R$160,417 under noncurrent liabilities (up to 12.31.2003, R$131,347, R$115 under current liabilities and R$131,232 under noncurrent liabilities).

The total net present value amount due on a long-term basis has the following scheduled maturities:

	2004	2003
2005	—	1,350
2006	1,506	1,350
2007	1,506	1,350
2008	1,506	1,350
2009	1,506	1,350
2010	1,506	1,350
From 2011 to 2023	152,887	123,132
	160,417	131,232

NOTE 16—POST-EMPLOYMENT BENEFITS

Actuarial liabilities of the Company are determined by an independent actuary, based on the Projected Unit Credit Method.

Post-employment benefits maintained by the Company are the following:

a) Pension plan

Through PREVIG—Sociedade de Previdência Complementar the Company maintains a Pension Plan for its employees.

PREVIG is a closed pension entity, a nonprofit private legal entity sponsored exclusively by Tractebel Energia.

The Benefit Plan managed by PREVIG is a Defined Benefit plan, with a financial regime of capitalization for retirement and pension benefits and pension and simple sharing for benefits, as specified below:

- Retirement for length of service;
- Retirement for disability;
- Retirement for age;
- Special retirement and retirement of ex-combatants;
- Pension;
- Assistance in commitment to an institution; and
- Funeral expense payment.

The initial retirement benefit is basically the difference between the arithmetic mean of the employee's last 36 actual salaries of contribution to the Plan, adjusted on a monthly basis by the same indexes adopted by the Social Security, and the hypothetical amount of the Social Security retirement benefit, determined by using rules in force before Law 9876 of 11.26.1999 became effective. After being granted, the benefit complement is adjusted annually based on the INPC variation.

The funding of the Benefit Plan is covered by contributions made by participants and the sponsor. The Company's contribution is equal to twice the contribution of its employees. In addition, the Company contributed with 1.7825% of the payroll (percentage adjusted monthly by a factor determined according to the fluctuation in the number of employees that participate in the Plan) in order to amortize reserves in connection with length of past service recognized by it, adjusted on an actuarial

basis, whose liability ends on December 2023. The amount of such contributions in the year of 2004 was R$7,300 (R$7,246 in 2003, R$6,202 in 2002).

Before the organization of PREVIG, the benefit plan was managed by Fundação Eletrosul de Previdência e Assistência Social—ELOS, sponsored by the Company and another company, with no joint and several liabilities between the sponsors.

In October 2002, the Pension Secretariat approved the termination of the Adhesion Agreement with ELOS and the complete transfer of the benefit plan management to PREVIG, by means of Order N. 1.755/SPC/GAB/COA.

Despite the termination of the Adhesion Agreement, the Benefit Plan composed of the participants who started to enjoy benefits until 12.23.1997, date of ELETROSUL spin-off, as well as by participants who opted for the Deferred Proportional Benefit until that date, continues under the responsibility of the Company.

While this situation lasts, the Company is responsible for funding 57% of the value of administrative expenses of ELOS (the remaining 43% is funded by the Benefit Plan of the other sponsor of this foundation) and for funding 100% of the value of administrative expenses of PREVIG. Both expenses are limited to 15% of the total corresponding pension income and the value borne by the Company in 2004 amounted to R$3,577 (R$2,702 in 2003, R$1,544 in 2002).

The parties continue to seek alternatives to that approved by SPC to regularize the current situation.

In addition to the benefit plan described above, PREVIG started to manage another plan, a Defined Contribution Plan, and new enrollments in the Defined Benefit plan ended on 10.05.2004, date of approval of the new plan, communicated by the Pension Secretariat—SPC by means of Order N. 1998 DAJUR/SPC.

On the same date, the Company entered into an Adhesion Agreement with Previg and started to offer the Defined Contribution plan to its employees and the migration process provided under its regulation also started. The actual enrollment of participants in the Defined Contribution plan started on January 2005.

b) Confidentiality bonus

A compensation paid to the employee of management at the termination of its employment relationship.

The reconciliation of liabilities resulting from post-employment benefits, recognized in the Company's financial statements is as follows:

	2004		2003	
	Retirement plan	Confidentiality bonus	Retirement plan	Confidentiality bonus
Present value of actuarial obligations totally or partially secured	1,102,860	—	1,085,789	—
Fair value of assets	(695,397)	—	(642,113)	—
Present value of actuarial obligations totally unsecured	—	1,143	—	1,075
Subtotal	407,463	1,143	443,676	1,075
Net value of actuarial losses not recognized in the balance sheet	(158,295)	(184)	(200,369)	(281)
Liabilities recognized in the balance sheet	249,168	959	243,307	794

The amount of actuarial losses exceeding 10% of the present value of actuarial obligations will be amortized annually, on a linear basis, for approximately 11 years, which corresponds to the average remaining work period estimated for employees taking part in the plan.

Part of the actuarial liabilities recognized in the balance sheet, resulting from "post-employment benefits", is secured by liabilities agreed to/recognized by an instrument of acknowledgement of indebtedness and agreement, entered into by the Company. The liabilities in the financial statements are composed as follows:

	2004			2003
	Current	Long-term	Total	Total
Agreed to/recognized obligations				
Agreement of acknowledgement of past debts, including the financing of administrative expenses	21,187	76,439	97,626	103,104
Coverage of costs relating to conversion of special retirement into retirement by length of service (SB-40) and extraordinary contributions	30,432	10,785	41,217	62,975
Actuarial liabilities not agreed to	—	111,284	111,284	78,022
	51,619	198,508	250,127	244,101

Entries made to actuarial liabilities, recognized in the balance sheet of 2004, are summarized below:

	Retirement plan	Confidentiality bonus	Total
Liabilities on 12.31.2001	269,861	657	270,518
Expenses of 2002	28,979	106	29,085
Actual contributions by the Company in 2002	(46,420)	—	(46,420)
Benefits paid by the Company in 2002	—	(30)	(30)
Liabilities on 12.31.2002	252,420	733	253,153
Expenses of 2003	39,075	147	39,222
Actual contributions by the Company in 2003	(48,188)	—	(48,188)
Benefits paid by the Company in 2003	—	(86)	(86)
Liabilities on 12.31.2003	243,307	794	244,101
Expenses of 2004	57,062	186	57,248
Actual contributions by the Company in 2004	(51,201)	—	(51,201)
Benefits paid by the Company the in 2004	—	(21)	(21)
Liabilities on 12.31.2004	249,168	959	250,127

The estimated amounts to be recognized in the income for 2005 as expenses are the following:

	Retirement plan	Confidentiality bonus	Total
Cost of current service	16,502	60	16,562
Cost of interest	130,620	122	130,742
Earnings expected from plan's asset	(86,184)	—	(86,184)
Amortization of actuarial losses	4,278	6	4,284
Contribution of employees	(3,828)	—	(3,828)
Total	61,388	188	61,576

Actuarial assumptions used in the evaluation of benefits are described below.

Economic hypotheses (nominal)

Discount rate—12.25% p. a.

Expected rate of return on assets—12.50% p. a.

Future salary growth

- Active participant—8% p. a.
- Self-sponsored participant—6.00% p. a.

Growth of social security benefits—6.00% p.a.

Growth benefits of the Plan sponsored by the Company—6.00% p.a.

Inflation—6.00% p. a.

Capacity factor

- Salaries—100%
- Benefits—100%

Demographic hypotheses
Mortality Table (assets)—GAM 1983, with age adjustment of -1
Disabled Mortality Table—IAPB 57
Disability Start Table—TASA27
Turnover Table—T-1 Experience
Age of Retirement—First date in which all grace periods are complete
% of active participants married on the date of retirement—90.00%
Age difference between participant and spouse—Wives are 4 years younger than their husbands

Other hypotheses
% of participants entitled to conversion of special retirement into retirement by length of service (SB-40) who will opt for the conversion—100%.
Conversion factor of SB-40—140%

NOTE 17—DEFERRED TAX DEBITS

Recorded under this entry are income tax and social contribution on net income, in the amount of R$39,616 (R$48,603 in 2003), calculated on the provision for sale of electric energy within MAE, in the amount of R$116,516 (R$142,949 in 2003), corresponding to the period from September 2000 to September 2002. Considering that the amount of revenue is being challenged in court by agents who disagree with the interpretation adopted by MAE in the application of certain accounting rules, as provided under ANEEL Order N. 288, of 05.16.2002, if the petitioner agents win, both the revenue and the corresponding asset will no longer exist, and therefore it is being treated as a provision and deemed a timing difference for tax purposes.

NOTE 18—SHAREHOLDERS' EQUITY

a) Authorized share capital

The Company is authorized to increase its share capital up to the limit of R$4,500,000, regardless of an amendment to its by-laws.

b) Share capital and dividends

The share capital of the Company, as at December 31, 2004, is R$2,445,766, and is represented by 652,742,193,511 shares: 464,052,075,236 common shares, 75,069,876 preferred class A shares and 188,615,048,399 preferred class B shares, all with no par value. The equity value per thousand share as at December 31, 2004 is R$4.27 (R$3.99 on 12.31.2003).

Preferred shares are nonvoting shares and are not convertible into common shares. Such shares have priority in the distribution of dividends, at the rate of 8% for class "A" shares and 6% for class "B" shares, determined on the share capital of the corresponding classes of shares, and such dividends should be equally apportioned among them. For both classes of shares, the dividend will be determined at the rate of 3% of the shareholders' equity value corresponding thereto, in the event such dividends exceed those determined based on the rates mentioned above.

The Company's ownership structure on 12.31.2004 is as follows:

	% of capital			
Shareholders	ON	PNA	PNB	Total
Tractebel EGI South America Ltda.	80.40	31.82	73.16	78.30
Banco Clássico S.A.	10.51	—	8.75	10.00
BNDES Participações S.A.—BNDESPAR	3.66	—	10.43	5.62
União Federal	2.68	—	—	1.90
Banco Nordeste do Brasil S.A.	0.53	—	—	0.38
Caixa de Previd. dos Funcionários do Banco do Brasil	0.52	—	—	0.37
Others	1.70	68.18	7.66	3.43
	100.00	100.00	100.00	100.00

	2004	2003	2002
Composition of reserves:			
Capital Reserve			
Compensation of assets and rights created with equity capital	91,695	91,695	91,695
Surplus Reserves			
Statutory reserve	102,252	63,492	37,635
Retained earnings reserve	147,243	843	185,203
	249,495	64,335	222,838

The Management of the Company, based on a capital budget to be submitted to the Annual Shareholders Meeting, proposes that a retained earnings reserve be created in the amount of R$146,400, without adverse effects to the distribution of dividends.

NOTE 19—PROPOSED DIVIDENDS

On 12.09.2004, the Board of Directors of the Company approved a credit of interest on shareholders' equity, in compliance with Law 9,249/95 and CVM Resolution 207/96, in the amount of R$255,000, corresponding to R$0.465589 per thousand Preferred Class A Shares, R$0.390651 per thousand Preferred Class B Shares and Common Shares, Pursuant to the Notice to Shareholders published on 12.10.2004, the Company's shares started to be traded ex-interest on shareholders' equity as of 12.15.2004 and the interest amount will be paid on a date to be defined later and communicated by means of a Notice to Shareholders.

The amount mentioned above, net of withholding tax, is being imputed to dividends in connection with the year of 2004.

Interest on shareholders' equity has been recorded under financial expenses and reverted in this same entry and is not shown in the income statement for the year, since it has no effect on operating income and only on the lines of income tax and social contribution.

Minimum mandatory dividends correspond to 25% of the net income, adjusted pursuant to the Brazilian Corporate Law (*Lei das Sociedades por Ações)*, as provided under § 1 of section 37 of the Company's By-laws.

	2004	2003
a) Determination of minimum mandatory dividends		
Net income in the year	775,192	517,154
Creation of statutory reserve (5%)	(38,760)	(25,857)
Tax basis	736,432	491,297
Minimum mandatory dividends (25%)	184,108	122,824
b) Proposed dividends/interest on shareholders' equity		
Interest on shareholders' equity, net of withholding tax (IRRF)	216,750	198,900
Balance of proposed dividends	335,032	257,297
Subtotal	551,782	456,197
Withholding tax on interest on shareholders' equity	38,250	35,100
Total	590,032	491,297
Dividends/interest on shareholders' equity before withholding tax, per thousand (1.000) shares (**in R$1.00**):		
Preferred class A shares	0.920260	0.773822
Preferred class B shares	0.845321	0.698884
Common shares	0.845321	0.698884

The balance of proposed dividends, in the amount of R$335,032, corresponding to R$0.513269 per thousand Preferred classes A and B shares and per thousand common shares, will be paid after the resolution of the Annual Shareholders Meeting approving the Financial Statements.

NOTE 20—OPERATING EXPENSES DETAILED BY TYPE

	2004					2003	2002
	Costs		Expenses				
	Production and sale	Services rendered	Selling expenses	General and administrative expenses	Total	Total	Total
Personnel	68,893	5,870	4,475	34,574	113,812	88,714	72,002
Material	16,995	184	34	718	17,931	10,068	9,637
Third-party services	38,337	1,859	1,442	24,930	66,568	54,289	44,729
Fuel to produce energy—CCC	275,502	—	—	—	275,502	223,129	216,294
Fuel to produce energy—without subvention	136,933	—	—	—	136,933	77,346	57,293
Financial compensation for use of water resources	59,182	—	—	—	59,182	46,099	43,810
Charges on the use of electric system	—	—	134,899	—	134,899	61,683	20,216
Uso de bem público—UBP	4,831	—	—	—	4,831	14,539	15,884
Depreciation and amortization	214,528	—	30	8,929	223,487	227,637	189,877
Creation/reversal of provisions for doubtful debtors	—	—	(12,095)	—	(12,095)	143,720	—
Creation/reversal of operating provisions, net	(54,102)	—	—	64,700	10,598	(142,840)	108,903
Insurance	10,013	411	—	328	10,752	15,265	12,106
Pension plan—SB-40	—	—	—	23,435	23,435	24,993	25,428
Severance pay	—	—	—	2,940	2,940	3,398	8,376
Inspection fee	—	—	—	7,138	7,138	6,429	4,878
Shares—CCC and CDE	2,119	—	—	—	2,119	3,431	1,914
Contributions and donations	1,111	20	13	3,948	5,092	4,333	3,372
Other expenses	15,987	217	4,614	15,661	36,479	17,330	11,980
	790,329	8,561	133,412	187,301	1,119,603	879,563	846,699

NOTE 21—LEASING

The Company uses leasing to renew its information technology equipment and fleet of vehicles.

Leasing agreements currently in force include the following assets:

a) Information technology equipment

The lease term is of 36 months and the purchase of assets by the lessee is ensured in the agreement for a value of R$1.00 per unit. On 12.31.2004, there are 341 personal computers leased (208 on 12.31.2003), which represents around 60% of the total.

The balance of amounts payable, on 12.31.2004, amounts to R$769, of which R$459 are due in the next 12 months and R$310 in the following months. The amount of payments during 2004 was R$441.

b) Fleet of vehicles

The Company has lease agreements for 36 vehicles on 12.31.2004. The term of the agreements is 36 months, and the purchase of assets at the end of the agreements at a value equivalent to 20% of the asset value is ensured to the lessee.

The balance of amounts payable, which started in this year, amounts to R$1,125, of which R$515 are due in the next 12 months and R$610 in the following months. The amount of payments during 2004 was R$658.

NOTE 22—FINANCIAL INSTRUMENTS

a) Risk management

(a.1) Market risk

The use of financial instruments by the Company aims to protect its assets and liabilities, minimizing its exposure to market risks, especially in connection with fluctuations of interest rates, price indexes and currencies. Such risks are monitored by the Financial Management Committee that assesses on a regular basis the Company's exposure and proposes operating strategies, control systems, position limits and credit limits with other partners in the market.

The Company has been recording on its books interest rate swap transactions in the international market and has a net liability balance at the average fixed rate of 5.272% p.a. and a net asset balance in Libor US$ six months, with flow starting on 10.15.2001 and ending on 04.15.2006, a principal amount of US$13,810 thousand, equivalent to R$36,657 on 12.31.2004, amortized every six months as from 04.15.2003. In 2004, this transaction generated an expense of R$1,416 (R$1,734 in 2003, R$1,482 in 2002), duly recognized in the financial statements.

On 12.31.2004, the Company had on its records over-the-counter derivative transactions representing 15% of its liabilities in foreign currency, with maturity on January 2005. Such transactions generated expenses of R$18,157, duly recognized in the financial statements based on the accrual basis of accounting.

In November 2004, taking advantage of the devaluation of the dollar as opposed to the real, the Company implemented a policy of increased protection of its liabilities in foreign currency by means of over-the-counter swap transactions, using its Exclusive Investment Fund a vehicle (see Note 3). The maturities of the swap transactions are simultaneous with the due dates of the flow of obligations of liabilities in foreign currency, considering a period of twenty-four months. Transactions are recorded in Cetip and are made with financial institutions known for their equity and financial solidness, within the credit limits defined by the Company. Swap transactions protect 22% of the Company's liabilities in foreign currency which, when added to the percentage amount invested in federal government bonds indexed to the US dollar, allow for a consolidated protection of 28% of the Company's liabilities in foreign currency.

(a.2) Credit risk

In long-term bilateral agreements and initial energy purchase and sale agreements, entered into with distributors, the Company seeks to minimize its credit risk by using a mechanism to create guarantees involving customers' receivables.

As of 2003, with the reduction in sales of electric energy linked to initial agreements, together with the beginning of operation of new plants, the Company started to broaden its customer portfolio by focusing on industrial customers, also known as Free Consumers. In order to minimize the credit risk with such commercial partners a credit area was created in the Company, whose job includes a prior

analysis and the determination of the credit limit and guarantees to be required from the other parties, in cooperation with the Credit Committee.

In financial market transactions, the Company also has credit limits with financial institutions that are regularly reviewed by its Financial Management Committee, based on an in-house evaluation and on ratings published by risk rating agencies.

As mentioned in Note 3, starting this year the Company has investments in an Exclusive Investment Fund. The amount of investments by financial institution is within the limits established by the Company in its credit policy for financial institutions.

b) Market value

In transactions involving financial instruments, significant differences between market values and book values were found only under loans and financing, mainly due to the fact that such financial instruments have quite extended settlement terms and significantly low costs when compared to the rates currently in force for similar agreements. The management of the Company used future cash flows discounted at rates adopted in the market for similar transactions or international market rates, when available, to determine average market values.

	2004		2003	
	Book value	Market value	Book value	Market value
Loans, interest and charges in foreign currency . . .	1,059,280	1,042,570	1,279,643	1,256,272
Loans, interest and charges in domestic currency . . .	757,841	749,581	838,309	816,481
	1,817,121	1,792,151	2,117,952	2,072,753

NOTE 23—RELATED PARTY TRANSACTIONS

The Company has agreements with its subsidiaries and joint subsidiary, as specified below:

Itá Energética S.A.—ITASA

Operation and Maintenance Services Agreement of ITÁ Hydroelectric Power Plant, rendered by the Company, entered into on 09.11.1998 in the context of Consortium Itá, valid until 10.16.2030, whose values are adjusted annually according to the IGP-M price index.

Agreement of Purchase and Sale of Electric Energy entered into on 01.15.2001, with the purpose of regulating the purchase, by the Company, of 61 MW average of energy owned by ITASA at Itá Hydroelectric Power Plant, governed by applicable laws and market rules, effective until 10.16.2030, adjusted annually according to the variation of the dollar plus US inflation.

Agreement of Purchase and Sale of Electric Energy entered into on 01.15.2001, with the purpose of regulating the purchase, by the Company, of 167 MW average of energy owned by ITASA at Itá Hydroelectric Power Plant, governed by applicable laws and market rules, effective until 10.16.2030, adjusted annually by IGP-M price index.

On 06.26.2003, the Company executed addenda to the two Agreements of Purchase and Sale of Electric Energy mentioned above, effective for the period of February 2004 to January 2005, whose purpose is to adjust, on an extraordinary basis, the price of electric energy agreed to, in order to cover the balance of ITASA's exposure at MAE, in the period from June 2001 to February 2002, settled on 07.03.2003.

On the same date of 06.26.2003, the Company entered into a Instrument of Commitment in order to accelerate the payment of the Extraordinary Adjustments provided in the addenda to the above mentioned agreements, with a discount rate of 0.949% p.m. on the total value of the extraordinary adjustment, and the amount of R$58,453 was paid to ITASA, on 07.04.2003 as an advance. Such advance started to be settled on 02.01.2004, and on 12.31.2004 a balance of R$1,453 remained in the account ''Advances to Suppliers''.

As discussed in Note 13, on 06.21.2004, a new addendum to the Agreement of Purchase and Sale of Electric Energy was executed, accelerating the end of the effectiveness of the temporary extraordinary adjustment, in connection with the agreement of 167 MW, from 01.31.2005 to 06.30.2004. The temporary extraordinary adjustment resulting from the addendum to the agreement of 61 MW will remain effective until its end, scheduled for 01.31.2005.

Companhia Energética Meridional—CEM

Agreement entered into on 04.09.1999, addenda made on 04.15.1999 and 11.09.2002, valid for an indefinite term, whose purpose is to render operational administration services, since CEM does not have its own staff. The value of the agreement is adjusted annually according to the IGP-M price index.

Agreement of Purchase and Sale of Electric Energy, entered into on 01.05.2001, addenda made on 03.06.2001 and 08.09.2002, valid until 2015, to purchase the electric energy produced at UHE Cana Brava. The agreement establishes the purchase of energy, by the Company, in the annual amounts of 1,125,616 MWh, 2,189,036 MWh and 2,395,903 MWh, starting on October 2002, November 2002 and December 2002, respectively. The value of the agreement is adjusted annually according to the IGP-M.

Operation and Maintenance Agreement of UHE Cana Brava, entered into on 01.05.2001, addenda made on 03.09.2001 and 06.01.2002, valid until the end of the plant concession and whose values are adjusted annually according to IGP-M, under which the Company undertakes to operate and perform maintenance of the business venture.

Lages Bioenergética Ltda.

Agreement entered into on 01.02.2003, valid for an indefinite term, whose purpose is to render operational administration services, since Lages does not have its own staff. The value of the agreement is adjusted annually according to the IGP-M.

Agreement of Purchase and Sale of Electric Energy entered into on 03.15.2004, with the purpose of regulating the purchase, by the subsidiary, of up to 26 MW average of energy per month owned by the Company, effective from 04.01.2004 to 03.31.2017.

Operation and Maintenance Agreement of Lages Cogeneration Unit, entered into on 04.01.2004, ending on 03.31.2012, under which the Company undertakes to operate and perform maintenances of the business venture. The value of the agreement is adjusted annually based on the variation of the compensation defined according to the Collective Labor Agreement of the Company's employees.

Tractebel Energia Comercializadora Ltda.

Agreement entered into on 11.01.2004, valid for an indefinite term, whose purpose is for the Company to render the services of management, planning, control and economic, accounting, tax, legal and financial administration of the subsidiary. The value of the agreement is adjusted at the shortest period allowed by law (currently, on an annual basis) according to the variation of IGP-M.

Agreement with Suez-Tractebel S.A. (indirect holding company)

On 05.02.2002, the Company entered into an agreement with Suez-Tractebel S.A. (current name of Tractebel S.A.), its indirect holding company, with its head office in Brussels, Belgium, whose purpose is for Suez-Tractebel to render consulting services in specific matters. The agreement was approved by unanimous vote by the minority shareholders of the Company at an Annual Shareholders Meeting held on 04.29.2002, and the controlling shareholder waived its voting right. The term of the agreement is of 36 months, conditioned to its revalidation, by minority shareholders, every 12 months, at a Meeting called for this purpose, and whose effectiveness is conditioned to the approval by ANEEL, that happened on 04.23.2003, by Order N. 526/2003-SFF/ANEEL. The amount of fees during the validity of the agreement is limited to the annual noncumulative amount of 1,500,000 EUROS and the services rendered and corresponding fees will be submitted to the Company's Audit Committee, in which there is a member elected by the minority shareholders. The first revalidation by minority shareholders occurred at the Extraordinary General Meeting held on 04.12.2004.

The amounts recognized in assets and liabilities accounts and equity accounts are shown below:

	2004								2003	2002
	Tractebel EGI South America Ltda.	Suez Tractebel S.A.	CEM	ITASA	Lages	Tractebel Energia Comerc. Ltda	CESS	Total	Total	Total
Assets										
Accounts Receivable	633	—	359	5,630	7,041	2,810	58	16,531	114,701	2,766
Liabilities										
Suppliers	—	—	29,839	12,472	1	—	—	42,312	38,571	24,472
Dividends and interest on shareholders' equity	432,054	—	—	—	—	—	—	432,054	357,234	—
Income										
Operating Revenue										
Supply of energy	—	—	—	—	3,070	9,030	—	12,100	—	—
Service income										
Management	—	—	590	—	84	—	120	794	620	316
Operation and maintenance	—	—	1,561	8,733	960	—	—	11,254	10,096	7,248
Cost of Electric Energy and Services										
Purchase of energy	—	—	236,968	177,833	—	—	—	414,801	412,490	146,163
Other	—	—	—	—	7	—	—	7	—	—
General and administrative expenses										
Consulting	—	5,254	—	—	—	—	—	5,254	6,521	—
Financial										
Revenue	—		—	3,291	—	—	—	3,291	6,745	143
Expenses	—	—	—	—	—	—	—	—	—	4,752

NOTE 24—GUARANTEES TO THIRD PARTIES

Itá Energética S.A.—ITASA

The Company and other shareholders of ITASA are intervening parties in the agreements entered into by and between the investee and BNDES and other financial agents, linked to the construction of UHE Itá. The intervening parties have given as collateral the total amount of shares issued by ITASA, owned by them, until the final settlement of all obligations undertaken in the agreements under reference. The debt totals R$623,048 on 12.31.2004 (R$671,828 on 12.31.2003).

In order to ensure the payment of the obligations resulting from the above mentioned agreements, ITASA has given the following guarantees to BNDES and the Financial Agents: a) Pledge of Concession Emerging Rights to exploit UHE Itá; and b) Pledge of Credit Rights resulting from the Agreements of Purchase and Sale of Electric Energy entered into with its investors.

Companhia Energética Meridional—CEM

Tractebel Energia is an intervening party to the Agreement of Subscription and Payment of Debentures Nonconvertible into Shares n° 98.2.654.3.1 and to the Financing Agreement by Opening of Credit Facility n° 98.2.654.3.3, entered into by and between CEM and BNDES, the first on 05.19.1999, addendum made on 05.25.1999, and the second on 04.05.2000. It is also an intervening party to the Loan Agreement n° 1260/OC/BR executed on 12.08.2000 and amended on 03.06.2001, with the Inter-American Development Bank—BID, and the following main obligations regarding the agreements have been undertaken with both financial agents:

ensure the prepayment in the following exclusive events: a) end of concession by reason imputable to CEM, to the intervening parties or their subsidiaries, associated companies or holding companies; and b) agreement entered into with the Granting Authority by CEM, by the intervening parties or by any of their subsidiaries, associated companies or holding companies, with the purpose of ending the concession;

assignment to BNDES and IDB of any amounts resulting from indemnity received as a result of the end of concession of UHE Cana Brava, by the Granting Authority.

In addition to the obligations specified above, Tractebel Energia has given to BNDES and to BID, as collateral, the total amount of shares owned by it, representing the share capital of CEM, until the final settlement of all obligations undertaken in the above mentioned agreements. The debt totals R$558,525 on 12.31.2004 (R$627,294 on 12.31.2003).

CEM has assigned receivables resulting from the generation and sale of energy from UHE Cana Brava as a guarantee for payment of its loans and financing.

Lages Bioenergética Ltda.

The Company is the intervening guarantor in the Agreement of Fixed Credit Facility entered into by and between Lages Bioenergética and Banco Regional de Desenvolvimento do Extremo Sul—BRDE, on 07.25.2003, and gave as collateral the shares in the share capital of the subsidiary, owned by it, until the final settlement of all obligations undertaken in the agreement under reference. The debt totals R$48,743 on 12.31.2004 (R$33,247 on 12.31.2003).

In order to ensure the payment of the obligations resulting from the above mentioned agreement, Lages Bioenergética has given as collateral the receivables resulting from the sale of electric energy from the Cogeneration Unit.

NOTE 25—INSURANCE

The Company has a comprehensive operating risk insurance policy with a declared value for property damage of US$3,515,233 thousand, equivalent to R$9,330,834 thousand on 12.31.2004, and with a declared value for loss of profits of US$459,900 thousand, equivalent to R$1,220,758 thousand on 12.31.2004. The maximum combined limit for indemnification of damage to property and loss of profits is US$150,000 thousand, equivalent to R$398,160 thousand on 12.31.2004, per event.

The policy and values above refer to property owned by Company's, UHE Cana Brava, whose concession belongs to the subsidiary CEM, was included in the insurance policy of Tractebel Energia

starting on 12.19.2003, with a declared amount for damages to property of US$320,000 thousand equivalent to R$849,408 thousand on 12.31.2004 and loss of profits of US$71,000 thousand equivalent to R$188,462 thousand on 12.31.2004, by means of endorsement N. 1095000026.

The subsidiary CEM maintains a comprehensive maintenance coverage for a period of two years after the beginning of operations of the 3rd unit in the plant, scheduled for 01.15.2003 in the policy.

In addition to such coverage, the Company has liability insurance policies with coverage of US$50,000 thousand, equivalent to R$132,720 thousand on 12.31.2004. Such policies include UHE Itá, built and exploited in consortium with the joint subsidiary ITASA.

The subsidiary Lages Bioenergética Ltda. has Operating Risk insurance with coverage of US$20,000 thousand equivalent to R$53,088 thousand on 12.31.2004, and Engineering Risks insurance with coverage of civil engineering works in construction, installation and assembly, including during the test phase and during 12 months of comprehensive maintenance, as well as general and cross liability coverage, with the following validities:

- Civil engineering works in construction/installation and assembly—11.01.2002 to 12.31.2003
- Tests—11.28.2003 to 12.12.2004
- Maintenance—02.12.2004 to 02.12.2005

The maximum indemnity limits are the following:

- Civil engineering works in construction/installation and assembly—R$44,712 thousand
- General and cross liability—R$1,806 thousand

NOTE 26—LONG-TERM AGREEMENTS

In addition to the agreements with subsidiary companies and the indirect holding company mentioned under Note 23, the Company has long-term rights and undertakings, including:

a) Connection agreement

In agreement with Law n° 9.648/98 and Decree n° 2.655/98, setting forth that the access and use of electric energy transmission systems be contracted separately from the purchase and sale of the energy itself, on August 20, 1998, the Company entered into the Connection Agreement with Empresa Transmissora de Energia Elétrica do Sul do Brasil S.A.—ELETROSUL, effective as of September 1, 1998;

b) Agreement of use of transmission system

The Company entered into an agreement of use of the transmission system, in compliance with Law n° 9.648/98 and Decree n° 2.655/98, with Empresa Transmissora de Energia Elétrica do Sul do Brasil S.A.—ELETROSUL, ensuring the use of the Basic Transmission System for delivery of the electric energy sold by means of the Initial Agreements. The agreement is effective as of September 1, 1998 and resulting charges will be fully attributed to the distribution concessionaires, pursuant to ANEEL Resolution N. 248, of August 07. 1998, and therefore do not represent a burden for the Company.

In order to meet the agreements of sale of electric energy released from the Initial Agreements and of the electric energy coming from plants that started their commercial operation as of 01.01.2002, the Company has entered into agreements with the National Operator of the Electric System—ONS, by means of which it undertook 50% of the transmission costs, and the remaining 50% will be borne by

the distribution concessionaires. The costs for the Company totaled R$100,964 in 2004 (R$33,617 in 2003);

c) Initial agreements of purchase and sale of Electric Energy

Based on Law n° 9.648/98, article 10 and GCOI standards, the Company entered into the Initial Agreements of Purchase and Sale of Electric Energy with the concessionaires listed below, which are being reduced by 25% per year, starting on 2003, until their complete end on 12.31.2005. The amounts indicated below refer to the contractual balances for supply in the period from 01.01.2005 to 12.31.2005:

- Rio Grande Energia S.A.—RGE:—Total of 740,220 MWh;
- Centrais Elétricas de Santa Catarina S.A.—CELESC:—Total of 2,555,730 MWh;
- Companhia Estadual de Energia Elétrica—CEEE:—Total of 269,370 MWh;
- Empresa Energética de Mato Grosso do Sul S.A.—ENERSUL:—Total of 617,580 MWh;
- Furnas Centrais Elétricas S.A.:—Total of 1,145,370 MWh;
- AES Sul—Distribuidora Gaúcha de Energia S.A.:—Total of 860,670 MWh;

d) Bilateral agreements of sale of Electric Energy

The energy not committed to the Initial Agreements, including that which is being released from such agreements starting in 2003, has been subject to agreements with distributors and free consumers. Therefore, the Company has the following main agreements for sale of electric energy, among others:

- Rio Grande Energia S.A.—RGE: From 01.01.2005 to 12.31.2014—Total of 34,333,312 MWh;
- Centrais Elétricas de Santa Catarina S.A.—CELESC: From 01.01.2005 to 12.31.2008—Total of 23,850,323 MWh;
- Companhia Paulista de Força e Luz: From 01.01.2005 to 12.31.2010—Total of 9,832,987 MWh;
- Companhia Piratininga de Força e Luz: From 01.01.2005 to 12.31.2010 —Total amount of 5,770,269 MWh;
- Centrais Elétricas de Santa Catarina S.A.—CELESC: From 01.01.2005 to 12.31.2007—Total of 394,560 MWh;
- Light Serviços de Eletricidade S.A.: From 01.01.2005 to 12.31.2005 —Total of 105,120 MWh; and from 01.01.2005 to 12.31.2007—Total of 999,552 MWh;
- Sellers: The overall total of agreements with selling concessionaires, for the period of 01.01.2005 to 12.31.2007 amounts to 11,156,534 MWh, from 01.01.2005 to 12.31.2010 amounts to 6,926,416 MWh and from 01.01.2005 to 12.31.2014 amounts to 10,051,613 MWh;
- Free consumers: Agreements with Free Consumers for the period of 01.01.2005 to 12.31.2007, total 8,913,109 MWh; from 01.01.2005 to 12.31.2010, 6,399,197 MWh and from 01.01.2005 to 12.31.2012, 7,243,352 MWh;

e) Purchase of Electric Energy from Argentina

The Company entered into an agreement with CIEN—Companhia de Interconexão Energética, for a term of 20 years, starting on 06.21.2000, to purchase 300 MW of firm power with associated energy, to be made available at substation of Itá, of ELETROSUL.

f) Purchase of natural gas

On November 10, 2000, the Company entered into an agreement to purchase natural gas with Companhia de Gás do Mato Grosso do Sul—MSGÁS, effective for 5 years as of 2001, where the Thermoelectric Power Plant of William Arjona, located in Campo Grande—MS has started its commercial operation;

g) Revitalization of generators of Hydroelectric Power Plant of Santo Osório

On December 19, 2003, the Company entered into an agreement with GE Hydro Inepar do Brasil S.A., valid for four years, for the complete renovation of the six generation units of UHE Salto Osório.

NOTE 27—AUDIT SERVICES

The independent auditors of the Company and its subsidiaries do not render any services other than audit services.

Accountants' review report

To the Board of Directors and Shareholders of
Tractebel Energia S.A.
Florianópolis—SC

1. We have performed a special review of the consolidated balance sheet of Tractebel Energia S.A. as of September 30, 2005 and the consolidated statements of income for the periods of nine months ended September 30, 2005 and September 30 ,2004, prepared for the specific purpose mentioned in paragraph 3 and under the responsibility of the Company's management.
2. Our review was performed in accordance with standards established by the Brazilian Institute of Independent Auditors—Ibracon, in conjunction with the Federal Accounting Council, and consisted principally of: (a) inquiries and discussions with the Company's management responsible for the accounting, financial and operational areas of the Company and its subsidiaries, as to the criteria adopted in preparing the consolidated balance sheets and the consolidated statements of income referred to in paragraph 1; and (b) a review of the information and subsequent events that had or could have material effects on the financial position and results of operations of the Company and its subsidiaries.
3. The consolidated balance sheet of Tractebel Energia S.A as of September 30, 2005 and the consolidated statements of income for the periods of nine months ended September 30, 2005 and September 30, 2004 were initially prepared for inclusion in the obligatory quarterly information (ITR) submissions and complied with the specific requirements applicable to such ITR; such requirements having been determined by the Brazilian Securities Commission (CVM). Consequently, since various components of the financial statements which would normally be required to be presented in order to represent complete disclosure are not required for ITR's, such components, such as the statements of changes in shareholders equity and source and applications of funds, are not being presented.
4. Based on our special review, we are not aware of any material modifications that should be made to the consolidated balance sheet and the consolidated statements of income referred to in paragraph 1 in order for them to be in accordance with the accounting practices adopted in Brazil, prepared for the specific purpose mentioned in paragraph 3.
5. The Company, based on its internal future cash flow projections, discounted to present value, estimated that certain assets would not be recovered with its future operations. The Company's management understands that these assets together with the rest of Company's operational assets will produce positive future cash flows.
6. We have previously audited the consolidated balance sheet as of December 31, 2004 and issued our unqualified independent auditors' report, dated January 31, 2005, containing an emphasis related to the subject referred to in paragraph 5, above.

DELOITTE TOUCHE TOHMATSU
Auditores Independentes
CRC—SP 011609/O-S-SC

Celso de Almeida Moraes
Contador
CRC—SP 124669/O-S-SC

October 31, 2005

Consolidated balance sheets

	09.30.2005	12.31.2004
	(Unaudited)	
	(In thousands of Brazilian reais)	
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	9,940	7,710
Securities	538,485	651,704
(–) Provision for investment losses	(17,427)	(17,427)
Consumers, concessionaires and holder of permissions	407,992	412,272
(–) Provision for doubtful debtors	(122,499)	(131,625)
Pledges and restricted deposits—CCEE	11,039	10,427
Miscellaneous receivables—concessionaires	15,630	7,809
Advances to suppliers	4,920	8,849
Credits from fuel consumption account—CCC/CDE	30,889	35,538
Disposals, services in progress and expenditures to reimburse	7,130	8,050
Taxes and social contributions recoverable	77,311	107,684
(–) Provision for losses in recovery of ICMS credit	(38,271)	(32,977)
Deferred taxes	65,122	98,173
Warehouse/materials in stock	16,666	13,610
Prepaid expenses	13,117	5,800
Other	8,198	7,817
	1,028,242	1,193,414
LONG-TERM ASSETS		
Concessionaires and holders of permission	7,846	14,920
Miscellaneous receivables	31,203	16,572
Securities	36,125	35,550
Taxes and social contributions recoverable	10,451	8,684
Pledges and restricted deposits	29,074	53,536
Deposits in court	47,744	26,050
Disposal of assets and rights	59,914	29,303
Deferred taxes	180,115	186,643
Prepaid expenses	1,614	—
Other	483	483
	404,569	371,741
PERMANENT ASSETS		
Investments	45,305	50,365
Property, plant and equipment	4,389,449	4,536,430
Deferred	46,289	53,202
	4,481,043	4,639,997
TOTAL ASSETS	5,913,854	6,205,152

The accompanying notes are an integral part of these statements.

Consolidated balance sheets

	09.30.2005	12.31.2004
	(Unaudited) (In thousands of Brazilian reais)	
LIABILITIES		
CURRENT LIABILITIES		
Suppliers	110,034	117,286
Dividends and interest on shareholders' equity	3,408	553,045
Loans and financing	221,583	265,410
Interest and charges on loans and financing	19,346	12,302
Debentures	16,176	18,599
Charges on debentures	18,780	4,761
Current taxes and social contributions	31,062	74,897
Taxes and social contributions on installments	1,003	979
Estimated obligations	31,845	36,540
Provision for contingencies	1,974	731
Post-employment benefits	40,800	51,619
Deferred taxes	36,532	39,616
Concession payable	1,528	1,472
Derivatives	78,902	28,002
Other	30,499	27,998
	643,472	1,233,257
LONG-TERM LIABILITIES		
Loans and financing	963,566	1,539,409
Debentures	344,652	153,619
Derivatives	21,619	—
Taxes and social contributions on installments	6,433	7,016
Estimated obligations	13,989	17,333
Provisions for contingencies	143,505	108,637
Concession payable	173,390	160,417
Post-employment benefits	226,220	198,508
	1,893,374	2,184,939
SHAREHOLDERS' EQUITY		
Share capital	2,445,766	2,445,766
Capital reserves	91,695	91,695
Profit reserves	249,495	249,495
Retained earnings	590,052	—
	3,377,008	2,786,956
TOTAL LIABILITIES	5,913,854	6,205,152

The accompanying notes are an integral part of these statements.

Consolidated statements of income

For the nine-month period ended

	09.30.2005	09.30.2004
	(unaudited)	(unaudited)
	(In thousands of Brazilian reais)	
GROSS OPERATING REVENUE		
Provision of electric energy	343,646	276,367
Supply of electric energy	1,578,150	1,499,170
Fuel subvention—CCC/CDE	257,796	198,344
Services rendered	4,007	3,470
Sales of ash	5,713	7,269
Other income	2,732	1,010
	2,192,044	1,985,630
DEDUCTIONS FROM OPERATING REVENUE		
Income tax and contributions	(227,590)	(129,671)
Sales of ash, net of taxes—CCC/CDE	(4,358)	(2,957)
	(231,948)	(132,628)
NET INCOME FROM SALES AND SERVICES	1,960,096	1,853,002
COSTS OF ELECTRIC ENERGY AND SERVICES		
Electric energy purchased for resale	(128,774)	(245,942)
Production cost of electric energy	(658,059)	(567,651)
Cost of services rendered	(6,719)	(6,442)
	(793,552)	(820,035)
GROSS PROFIT	1,166,544	1,032,967
OPERATING EXPENSES		
Selling expenses	(121,164)	(111,359)
General and administrative expenses	(118,977)	(128,499)
	(240,141)	(239,858)
SERVICE INCOME	926,403	793,109
Income from interests held in other companies		
Amortization of goodwill	(5,060)	(5,060)
	(5,060)	(5,060)
Financial Income/(Expenses)		
Income from investments	70,058	41,229
Charges on debts	(92,304)	(133,816)
Charges on debentures	(25,200)	(16,297)
Charges on ANEEL concessions	(11,716)	(9,736)
Losses with exchange rate swap /interest	(125,745)	(1,150)
Monetary variation on loans	155,090	8,068
Monetary variation on debentures	2,664	(7,613)
Monetary variation on ANEEL concessions	(2,409)	(14,282)
Monetary variation—others, net	(6,596)	(5,170)
Other	(32,266)	(9,971)
	(68,424)	(148,738)
OPERATING INCOME	852,919	639,311
NON OPERATING INCOME (LOSS)	3,515	(2,635)
INCOME BEFORE TAXES	856,434	636,676
Social Contribution	(66,774)	(57,389)
Income tax	(89,608)	(45,386)
NET INCOME FOR THE PERIOD	700,052	533,901
NET INCOME PER SHARE (09.30.2005) AND PER THOUSAND SHARES (09.30.2004)	1.0725	0.8179

The accompanying notes are an integral part of these statements.

Explanatory notes to unaudited consolidated financial statements

NOTE 1—OPERATING CONTEXT

The Company is an independent producer holding electric power utility concessions with its head office in the city of Florianopolis—SC, and its activity is the generation and sale of electric energy. It is regulated by the National Agency of Electric Energy—ANEEL, linked to the Ministry of Mines and Energy.

Its installed capacity, including the indirect ownership of Hydroelectric Power Plants (UHEs) of Itá and Cana Brava and Cogeneration Unit of Lages, is of 5.859 MW, of which 79.30% in hydroelectric plants and 20.0% in thermoelectric plants, composed of the following generation plants in operation: UHE Salto Osório (PR), UHE Salto Santiago (PR), UHE Passo Fundo (RS), UHE Itá (RS/SC), UHE Machadinho (SC/RS), UHE Cana Brava (GO), UTE Charqueadas (RS), UTE Alegrete (RS), UTE William Arjona (MS), Themoelectric Complex Jorge Lacerda (SC) and Cogeneration Unit of Lages (SC).

The Company's capacity to provide electric energy, including the long-term purchase agreements entered into with the subsidiary Itá Energética S.A.—ITASA and with Companhia de Interconexão Energética—CIEN, totals 5.968 MW.

The concessions and authorizations held by the Company and its subsidiaries are listed under Note 9-d.

Company's controlling interest is owned by Suez Energy South America Participation Ltda., a Company organized in Brazil and controlled by Suez-Tractebel Sociètè Anonyme, with its head office in Brussels, Belgium, a member of Suez Group, headquartered in France.

The Company holds interests in the following companies:

Company	Interests held	Location	Plant
Itá Energética S.A.—ITASA	48.75%	Border SC/RS	Hydroelectric plant- Itá
Companhia Energética Meridional—CEM	99.99%	Goiás—GO	Hydroelectric plant—Cana Brava
Lages Bioenergética Ltda	99.99%	Lages— SC	Co-generation Unit Lages
Tractebel Energia Comercializadora Ltda ..	99.99%	Florianópolis—SC	—
Delta Energética S.A.	99.99%	Florianópolis—SC	—

The main characteristics of the Company's subsidiaries and their businesses are described in Note 8-b.

NOTE 2—SUMMARY OF MAIN ACCOUNTING PRINCIPLES USED IN THE QUARTERLY INFORMATION

All figures (texts and tables) presented in the financial statements and explanatory notes are expressed in thousands of Brazilian reais, except when indicated otherwise.

Recognition of inflation effects

Only the effects of monetary variations on assets and liabilities indexed as a result of legal and contractual provisions are reflected. In compliance with Law No. 9.249, of 12.26.1995, beginning January 1996 the accounting for inflation was discoutined. Therefore, amounts corresponding to property, plant and equipment and shareholders' equity are adjusted only through 12.31.1995.

General evaluation criteria

a) Current and long-term assets

Securities are recorded at cost, with corresponding accrued interest earned until the Quarterly Information date. Book values are adjusted by creating a provision whenever they exceed average market prices;

the provision for doubtful debtors is associated with credits resulting from transactions made in the Wholesale Electric Energy Market—MAE from September 2000 to September 2002. Other accounts receivable have guarantees or no record of losses, and therefore no provision is needed (see Note 4);

deferred income tax and social contribution (deferred tax credits) are determined at the rates of 25% and 9%, respectively, in force on the date of the balance sheet, and are recognized based on tax losses and timing differences. The separation between current and long-term assets is in agreement with the expectation of realization of amounts that give origin to such assets;

materials in stock are recorded at their average weighted purchase cost, which does not exceed the market value.

Indexed assets are adjusted up to the date of the Quarterly Information.

b) Permanent assets

Investments in subsidiaries and joint subsidiaries are assessed by the equity method of accounting and other investments are recognized at their acquisition cost, which does not exceed the market value;

property, plant and equipment are recorded at the acquisition or construction cost. Depreciation is determined on the straight-line basis, based on annual rates shown on the table attached to ANEEL Resolution No. 002, of 12.24.1997, and No. 044, of 03.17.1999, based on the book balances recorded at the Registration Units—UC that form the business ventures, as set forth by DNAEE Ordinance No. 815, of 11.30.1994. Average annual depreciation rates determined by the Company and its subsidiaries, in compliance with the above regulations, are shown under Note 9;

Interest and other financial charges and effects of inflation resulting from financing obtained from third-parties, actually used in property, plant and equipment under construction, are calculated as a cost of the corresponding asset;

up to 12.31.1998 interest on shareholders' equity linked to construction work in progress was capitalized, in compliance with the specific laws of the electric industry. As of January 01, 1999, such procedure was discontinued by the Company and starting on 01.01.2002, it was no longer used by Brazil's electric industry due to the change of ANEEL standards regulating the subject.

c) Current and long-term liabilities

Future benefits to employees (post-employment benefits) are recorded based on actuarial evaluation by the Projected Unit Credit Method and adjusted monthly according to contractual indexes for agreed to obligations and complemented by amounts projected by actuarial evaluation (see Note 17);

Loans, financing and debentures, and resulting interest and charges, allocated until the Quarterly Information date, are adjusted by exchange rates or contractual indexes (see Note 12 and Note 13)

and other obligations are recorded at amounts known or determinable, plus corresponding charges and monetary variation incurred, when applicable.

d) Income for the period

Income and expenses are recorded in accordance with the accrual basis of accounting.

e) Leasing

Leasing transactions existing in the Company do not have relevant amounts and are recognized directly in expense, based on payments provided for in the agreement (see Note 21).

Consolidated financial statements

Investor's investments in the capital of investees are removed, as well as assets and liabilities balances and income and expenses resulting from transactions among consolidated companies.

Components of assets and liabilities and income and expenses of ITASA are consolidated in the proportion of Company's interest in its share capital, due to the shared control (see Note 8-b.1).

Due to the high proportion of interest of the holding company in the other subsidiaries (see Note 8-b), there was no effect of the minority shareholders' interest in the consolidated financial statements.

NOTE 3—SECURITIES

	09.30.2005	12.31.2004
Current		
Certificates of Deposit—CDB	106,111	440,035
Treasury Bonds—LFT	125,394	167,666
Treasury Bonds—LTN	185,644	—
Negative adjustments in swap transactions	—	(13,698)
Committed transactions	85,314	33,925
Treasury Bonds—NTN	4,707	—
Central Bank Notes—NBC-E	31,315	23,776
	538,485	651,704
(–) Provision for financial investments losses	(17,427)	(17,427)
	521,058	634,277
Long-Term		
Certificate of Deposit—CDB	36,125	35,550

Securities are recorded at cost plus corresponding accrued interest earned until 09.30.2005 and 12.31.2004, whose amounts do not exceed average market prices, and may be negotiated regardless of their maturities, without prejudice to earnings. The Company has Certificates of Deposit and Brazilian Treasury Bills in an Exclusive Investment Fund, both indexed to the CDI, and swap transactions carried out in the over-the-counter market recorded and settled at Cetip, in which the Fund has assets in exchange rates and liabilities in CDI.

The provision for financial investments losses refers to investment in CDB that the Company has with the Banco Santos S.A., whose bankruptcy was ordered on 09.20.2005.

NOTE 4—CONSUMERS, CONCESSIONAIRES AND GRANTEES

	09.30.2005				12.31.2004
		Overdue			
	Becoming due	Up to 90 days	More than 90 days	Total	Total
Current					
Free consumers	46,106	451	2,333	48,890	35,286
Concessionaires	168,357	4	—	168,361	170,250
Sellers	50,154	—	—	50,154	40,524
Exports	75	—	740	815	740
Transactions within MAE	125,822	—	13,950	139,772	165,472
	390,514	455	17,023	407,992	412,272
(–) Provision for Doubtful Accounts	(110,470)	—	(12,029)	(122,499)	(131,625)
	280,044	455	4,994	285,493	280,647
Long-term					
Transactions within MAE	7,846	—	—	7,846	14,920
	7,846	—	—	7,846	14,920

The invoices of electric energy provided to customers classified as "Free consumers" are due on the 15th of the month following the energy provision.

The energy supply invoices issued to concessionaires are divided in three equal payments, due on the 15th and 25th day of the month following the supply and on the 5th day of the second following month.

The values indicated in the account "Free-Contracting Consumers" as overdue, in the amounts of R$451 and R$2,333 are under negotiation with clients.

The amount of R$13,950 overdue for more than 90 days, indicated in the account "Transactions within MAE" refers to a debit of a defaulting agent in the 1st settlement of the Wholesale Electric Energy Market—MAE, carried out on 12.30.2002. Such amount is subject to bilateral negotiations. Nevertheless, due to the uncertainties of receiving such debt, the Company maintains an allowance for doubtful accounts amounting R$12,029, regardless of the measures in progress.

In September 2003, the Company made a provision in the amount of R$143,720 due to the uncertainties regarding the realization of credits resulting from transactions made within MAE in the period from September 2000 through September 2002, whose debtor agents filed lawsuits because they disagreed with the interpretation adopted by such body in connection with ANEEL Order N. 288, of 05.16.2002. The mentioned provision has been adjusted in view of agreements with some of the authors of the suits filed

On 07.22.2005, CCEE (Electric Power Trade Chamber) communicated that one more of the agents in debt gave up the lawsuit and that its debt with the company representing R$9,126, was settled, which resulted in an adjustment to the provision and resulted in the September 30, 2005 balance of R$110,470.

NOTE 5—DEFERRED TAX ASSETS

	09.30.2005				12.31.2004
Nature of credits	Calculation base	Income tax	Social contribution	Total	Total
Provision for losses UTE Jacuí	303,131	—	27,282	27,282	54,555
Remuneration of Construction Work in Progress—RIC	238,882	33,433	—	33,433	33,433
Post-employment benefits	131,565	32,891	11,841	44,732	51,316
Provision for doubtful debtors	122,499	30,625	11,025	41,650	44,752
Provision for contingencies	144,235	36,059	12,980	49,039	37,844
Provision for accelerated depreciation UTE William Arjona	32,708	8,177	2,944	11,121	11,972
Provision for losses with ICMS credits	38,271	9,568	3,444	13,012	11,212
Provision for extensive maintenance	30,703	7,676	2,763	10,439	10,442
Provision for financial investments losses	17,427	4,357	1,569	5,926	5,926
Employees profit-sharing program	6,500	—	—	—	2,210
Provision for management bonus	701	175	63	238	1,360
Provision for energy acquisition	1,467	—	—	—	499
Provision for lawyers' fees	624	156	56	212	206
Tax loss	11,017	2,754	—	2,754	4,501
Social contribution negative base	59,991	—	5,399	5,399	14,588
		165,871	79,366	245,237	284,816
Classification of deferred tax assets:					
Current assets		48,772	16,350	65,122	98,173
Long-term assets		117,099	63,016	180,115	186,643
		165,871	79,366	245,237	284,816

The realization of deferred tax assets, arising from temporary differences, will occur through the payment of accruals made or, when applicable, realization of the losses accrued for. In regards deferred tax assets from social contribution negative base, the realization will occur through its offsetting with taxable income, limited to 30% of taxable income in the subsequent fiscal years.

As mentioned in Note 9, in July 2004 the company transferred 33.33% of the interest in the project Jacuí to Elétrica Jacuí S.A.—ELEJA. Under the terms of the transfer agreement, the remaining percentage of the Company in the project, corresponding to 66.66%, was submitted to mutual trade options, purchase by ELEJA and sale by the Company. As of 07.29.2005, ELEJA acquired from the Company an additional percentage of 33.33% of the interest in the project, becoming the holder of 66.66%, by using its purchase option provided for in the contract. As a result, there was the reversal of part of the accrual for economic losses, in the amount of R$303,040.

The realization of the provision for economic losses of the Thermo-electric plant Jacuí in 2006 is based on the assumption of the exercise of sale and purchase options by the Company and by ELEJA in 2006 regarding the remaining 33.34% interest held in project Jacuí. The value of the deferred tax assets already accounted for refers to Social Contribution on Net Income and was recorded in 1997. The Company's management is waiting for definitions as to the purchase and sale options before recognizing the Income Tax on the mentioned provision, in the amount of R$75,783.

Technical feasibility studies, examined by the fiscal board and approved by the management board of the Company, indicate that the existing deferred tax assets will be totally recovered through future taxable profit. The said technical studies are in compliance with Instruction CVM 371 of 06.27. 2002.

The timeline for realization of those assets and recovery through the generation of future taxable profit were estimated as follows:

Nature of assets	2005	2006	2007	2008	2009	Next 2 Years	Next 3 Years	After 2014	Total
Provision for losses—UTE—Jacuí	—	27,282	—	—	—	—	—	—	27,282
Remuneration of Construction Work in Progress—RIC	836	3,343	3,343	3,343	3,344	6,687	10,030	2,507	33,433
Other timing differences	9,814	18,496	11,983	15,693	23,019	85,159	11,876	329	176,369
Tax loss	82	808	1,302	562	—	—	—	—	2,754
Negative basis for social contribution	4,399	287	464	249	—	—	—	—	5,399
Recorded deferred tax assets	15,131	50,216	17,092	19,847	26,363	91,846	21,906	2,836	245,237
Deferred tax credits, non registered									
Deferred tax credits—Jacuí	—	75,783	—	—	—	—	—	—	75,783
Deferred tax credits—RIC	—	—	—	—	—	—	—	26,288	26,288
	—	75,783	—	—	—	—	—	26,288	102,071

In the preparation of the above table, the year 2005 comprises only 3 months (October to December).

The realization of the compensation of fixed assets in progress occurs based on the ratio of depreciation of the respective assets, which currently is over 10 years, resulting in deferred tax assets not recognized in the amount of R$26,288 (R$28,843 as of 12.31.2004).

NOTE 6—RECONCILIATION OF TAXES, IN INCOME

	09.30.2005		09.30.2004	
	Social contribution	Income tax	Social contribution	Income tax
Income before taxes	856,434	856,434	636,676	636,676
Permanent differences				
Additions				
Amortization of goodwill	—	5,060	—	5,060
Management bonuses and 13th salaries	—	1,371	—	1,065
Donations with tax incentives	924	924	150	150
Non-deductible donations	115	115	758	758
Fines	(291)	(291)	—	—
Adjustment for subsidiary taxed by presumed profit	(5,711)	(6,805)	(1,196)	(1,824)
Other non-deductible expenses	254	254	468	468
Exclusions				
Reversal of interest on shareholders' equity	(110,000)	(110,000)	—	—
Provision for losses—UTE Jacuí	—	(303,040)	—	(365,581)
Remuneration of Construction work in Progress—RIC	—	(81,465)	—	(95,085)
Tax basis on income	741,725	362,557	636,856	181,687
Rates	9%	25%	9%	25%
Social contribution and income tax	(66,755)	(90,639)	(57,317)	(45,422)
Tax incentives	—	924	—	150
Additional 10% on income over R$20 per month	—	81	—	54
Social contribution and income tax on tax losses of subsidiaries not recorded in the deferred tax assets	—	—	(132)	(337)
Others	(19)	26	60	169
Social contribution and income tax on income	(66,774)	(89,608)	(57,389)	(45,386)
Composition of taxes:				
Current	(30,766)	(89,124)	(18,214)	(44,005)
Deferred	(36,008)	(484)	(39,175)	(1,381)
	(66,774)	(89,608)	(57,389)	(45,386)

NOTE 7—SALE OF ASSETS AND RIGHTS

On 06.04.2004, the Company transferred 33.33% of its interest in the project Jacuí to Elétrica Jacuí S.A.—ELEJA, for R$29,000, and on 07.29.2005 ELEJA acquired an additional interest of 33.33% of the mentioned project for R$31,181, by exercising the first purchase option provided in the contract entered into on 06.04.2002. As a result ELEJA currently holds 66.66% of the project.

In accordance with the contract, the above-mentioned amounts are adjusted by the index IGP-DI. On 09.30.2005, they amounted R$29,812 (R$29,303 on 12.31.2004) and R$30,102, respectively.

NOTE 8—INVESTMENTS

a) Composition

	09.30.2005	12.31.2004
Investments valued by the equity method of accounting		
Itá Energética S.A. — ITASA		
Goodwill	10,871	12,587
Companhia Energética Meridional — CEM		
Goodwill	32,318	35,662
	43,189	48,249
Investment valued at acquisition cost		
Electric Energy Sales Chamber		
Interest quota	3	3
	43,192	48,252
Assets and rights for future use and designated for disposal	1,742	1,742
Other investments	371	371
	45,305	50,365

b) Permanent interests

b.1—Itá Energética S.A.—ITASA (jointly controlled subsidiary)

The shares representing the share capital of ITASA are held by Tractebel Energia, Companhia Siderúrgica Nacional—CSN and Companhia de Cimento Itambé, in the proportion of 48.75%, 48.75% and 2.50%, respectively.

ITASA's purpose is to exploit the Hydroelectric Power Plant Itá in joint venture, by means of consortium, based on the concession granted by the Federal Government through the National Agency of Electric Energy—ANEEL. The business venture is located on the Uruguay River, on the border of the States of Santa Catarina and Rio Grande do Sul, between the Municipalities of Itá (SC) and Aratiba (RS) and has an installed capacity of 1,450 MW resulting from 5 generation units of 290 MW, and the last unit started to operate in March 2001.

Pursuant to the Consortium Agreement, ITASA is entitled to 60.5% of 668 MW average, which corresponds to the Assured Energy of UHE Itá.

The information relating to the interest in the joint subsidiary is shown below:

	09.30.2005	12.31.2004
Number of capital stock shares	520,219,172	520,219,172
Quantity of shares owned by Tractebel Energia	253,606,840	253,606.840
Interest held (%)	48.75	48.75
Capital stock	426,300	426,300
Stockholders' Equity	551,762	520,516
Net Income for the period	31,246	13,613

The economic basis for the goodwill arising from the investment acquisition is the expectation of future income and it is being amortized over 10 years.

The determination of the goodwill is based on the cash flow calculated by an expert financial institution, according to assumptions applicable to the context of the investee, projected for the concession period.

The valuation considered the debt/equity ratio of 50/50 to implement the Itá project, using discount rates of 11.0% for third-party capital and 11.5% for equity capital.

The goodwill amortized from January to September 2005 amounted to R$1,716 (R$1,716 in the same period of 2004).

The main account groups under assets, liabilities and shareholders' equity of the joint subsidiary are shown below, and they have been consolidated in proportion to Company's investment in the share capital of the subsidiary:

	09.30.2005	12.31.2004
ASSETS		
Current assets	77,766	54,885
Long-term assets	10,204	13,942
Permanent assets	1,074,201	1,105,752
	1,162,171	1,174,579
LIABILITIES		
Current liabilities	103,018	108,855
Long-term liabilities	507,391	545,208
Shareholders' equity	551,762	520,516
	1,162,171	1,174,579

	09.30.2005	09.30.2004
RESULT		
Gross operating income	185,352	251,309
Deductions from operating income	(17,145)	(21,949)
NET SALES INCOME	168,207	229,360
ELECTRIC ENERGY COSTS		
Electric energy purchased for resale	(1,331)	(89,928)
Electric energy production cost	(40,098)	(35,046)
	(41,429)	(124,974)
GROSS PROFIT	126,778	104,386
OPERATING EXPENSES		
Selling expenses	(14,469)	(16,746)
General and administrative expenses	(14,295)	(14,532)
	(28,764)	(31,278)
SERVICE INCOME	98,014	73,108
NET FINANCIAL EXPENSES	(50,613)	(76,011)
OPERATING INCOME (LOSS)	47,401	(2,903)
NON OPERATING LOSS	—	(1)
INCOME BEFORE TAXES	47,401	(2,904)
Income and social contribution taxes	(16,155)	—
NET INCOME (LOSS) FOR THE PERIOD	31,246	(2,904)

b.2—Companhia Energética Meridional—CEM (subsidiary)

CEM holds the concession for the Cana Brava Hydroelectric Power Plant, located on the Tocantins River, in the north of the State of Goiás, with an installed capacity of 450 MW and 273.4 MW average of assured energy. The concession to build and exploit the business venture is valid for 35 years, as from 08.27.1998.

The information relating to the interest in the subsidiary is shown below:

	09.30.2005 Type of shares			12.31.2004
	Ordinary shares	Preferred shares	Total	Total
Amount of shares of share capital	118,849,336	225,678,665	344,528,001	225,170,692
Amount of shares owned by Tractebel Energia	118,849,332	225,678,665	344,527,997	225,170,688
Interest %	99.99	100.00	99.99	99.99
Share capital	145,415	278,807	424,222	224,222
Shareholders' equity	—	—	572,141	348,563
Net Income for the period	—	—	53,578	68,785

The economic basis for the goodwill in the acquisition of the controlling interest is the expectation of future income and it is being amortized over 10 years, starting in January 2003.

The determination of the goodwill is based on cash flows calculated by an expert financial institution, according to assumptions applicable to the context of the investee, projected for 35 years, the concession period of the plant, adjusted to present value using a discount rate of 14% p.a.

The valuation considered a debt/equity ration of 70/30 for the plant construction. Part of the goodwill is associated with the subscription bonuses purchased in the transaction, which have been used to make investments during the pre-operating stage of the investee.

The goodwill amortized from January to September of 2005 amounted R$3,344 (R$3,344 in the same period of 2004).

b.3—Lages Bioenergética Ltda. (subsidiary)

Company formed on 06.26.2002, authorized by the National Agency of Electric Energy—ANEEL on 10.30.2002 to be an Independent Producer, upon implementation of the thermoelectric generation center of Lages, located in the municipality of Lages, State of Santa Catarina, with a steam turbogenerator of 28 MW, using wood waste as fuel. The cogeneration unit has a restricted interest transmission system, composed of a substation with transformer of 31,250 kVA—13.8/138 kV and a transmission line of 138 kV, in a simple circuit, approximately 5 km long. The authorization to implement and exploit the business venture is valid for 30 years, starting on 10.30.2002. The construction work started in January 2003 and was scheduled to be completed by April 2004, however, the schedule advanced and the work was completed on 12.16.2003. The National Agency of Electric Energy—ANEEL, by means of Order N. 990, of 12.19.2003, authorized the beginning of the commercial operations of the generation center as of 12.23.2003.

The information relating to the interest in the subsidiary is shown below:

	09.30.2005	12.31.2004
Shares that compose the share capital	30,529,984	30,529,984
Shares owned by Tractebel Energia	30,529,983	30,529,983
Interest %	99.99	99.99
Share capital	30,530	30,530
Shareholders' equity	39,905	37,067
Net income for the period	9,375	6,537

b.4—Tractebel Energia Comercializadora Ltda. (subsidiary)

Tractebel Energia Comercializadora Ltda., headquartered in Florianópolis—SC, was constituted on 10.16.2000. It business purpose is the sale of electric power at the free trade market and includes the purchase, sale, import and export of power, as well as intermediation of any of those operations.

The information regarding the interest in the said subsidiary is as follows:

	09.30.2005	12.31.2004
Shares that compose the share capital	2,200,000	1,000,000
Shares owned by Tractebel Energia	2,199,999	999,999
Interest %	99.99	99.99
Share capital	2,200	1,000
Shareholders' equity	13,851	1,423
Income for the period	11,228	439

b.5—Delta Energética S.A. (subsidiary)

The Company owns 9,999 of the 10,000 shares that compose the share capital of Delta. This subsidiary was formed on 10.31.2001, under the name Delta Participações S.A. and on 04.26.2004 its company name was changed to Delta Energética S.A. To this date, the subsidiary has not been in operation.

NOTE 9—PROPERTY, PLANT AND EQUIPMENT

a) Composition

	Average depreciation rate	09.30.2005 Cost	12.31.2004 Cost
Property, plant and equipment in operation			
Intangible assets			
Right to exploit UHE Cana Brava		88,664	88,664
(–) Accumulated amortization	3.2	(9,084)	(6,950)
		79,580	81,714
Tangible assets			
Hydro generation			
Hydroelectric plant Salto Santiago	2.5	638,934	638,767
Hydroelectric plant Salto Osório	2.8	297,054	288,901
Hydroelectric plant Passo Fundo	2.5	123,120	123,257
Hydroelectric plant Itá (consortium)	2.3	1,779,342	1,779,329
Hydroelectric plant Cana Brava	2.5	871,278	869,322
Hydroelectric plant Machadinho (consortium)	2.5	178,969	178,888
		3,888,697	3,878,464
(–) Accumulated depreciation		(1,076,339)	(1,011,868)
		2,812,358	2,866,596
Thermal generation			
Complex Jorge Lacerda	4.3	2,456,991	2,453,365
Thermo-electric plant Charqueadas	4.4	54,808	55,006
Thermo-electric plant Alegrete	4.1	8,101	8,101
Thermo-electric plant William Arjona	4.3	174,498	139,900
Lages Cogeneration Unit	4.3	68,048	57,843
		2,762,446	2,714,215
(–) Accumulated depreciation		(1,289,411)	(1,180,899)
		1,473,035	1,533,316
Communication system	6.1	1,102	1,102
(–) Accumulated depreciation		(778)	(433)
		324	669
General equipment and others	10.0	36,700	31,388
(–) Accumulated depreciation		(19,849)	(17,101)
		16,851	14,287
Total fixed assets in operation		4,382,148	4,496,582

	Average depreciation rate	09.30.2005 Cost	12.31.2004 Cost
Fixed assets in progress			
Hydro-electric power generation			
Plant Salto Santiago (expansion work)		776	890
Plant Salto Osório (expansion work)		8,658	16,504
Plant Itá (late costs)		6,702	5,471
Plant Cana Brava		367	1,602
Others		666	194
		17,169	24,661
Thermo-electric power generation			
Plant Jacuí		26,541	52,320
Complex Jorge Lacerda (expansion work)		12,770	7,680
Plant Charqueadas (expansion work)		1,253	421
Plant Lages		2,708	9,646
Others		83	15
		43,355	70,082
Others		3,466	1,794
		63,990	96,537
Total fixed assets		4,446,138	4,593,119
Special obligations		(56,689)	(56,689)
Total fixed assets		4,389,449	4,536,430

b) Changes in the period

	In operation	In progress	Total
Balance as of 12.31.2004	4,496,582	96,537	4,593,119
Acquisitions	2,291	29,974	32,265
Transfers	36,096	(36,096)	—
Depreciation	(151,260)	—	(151,260)
Write-offs	(1,561)	(26,425)	(27,986)
	4,382,148	63,990	4,446,138
Special obligations	(56,689)	—	(56,689)
Balance as of 09.30.2005	4,325,459	63,990	4,389,449

c) Special obligations

Special obligations refer to liabilities linked to the electric energy utility and represent amounts invested in the business ventures under concession, with Federal Government funds and funds from donations

not conditioned to any return for the benefit of the donor. The settlement of such obligations will happen at the end of the corresponding concessions, established by the Granting Authority. These obligations as of 09.30.2005 and 12.31.2004 are composed as follows:

Donations and subventions destined for investments	48,062
Reversal and amortization	2,230
Participation of the Federal Government	3,758
Others	2,639
	56,689

d) Concessions and permits of the government

The Company and its subsidiaries hold the following concessions and permits for exploitation of electric power:

	Holder of concession or authorization	Installed capacity MW	Date of the concession/ authorization	Maturity
I—Concessions				
Hydroelectric plant Salto Santiago	Parent Company	1,420	09.28.1998	09.28.2028
Hydroelectric plant Salto Osório	Parent Company	1,078	09.28.1998	09.28.2028
Hydroelectric plant Passo Fundo	Parent Company	226	09.28.1998	09.28.2028
Hydroelectric plant Itá	Parent Company/ITASA	1,450	12.28.1995	10.16.2030
Hydroelectric plant Machadinho	Parent Company	1,140	07.15.1997	07.15.2032
Hydroelectric plant Cana Brava	CEM	450	08.27.1998	08.27.2033
II—Authorizations				
Complex Jorge Lacerda	Parent Company	857	09.25.1998	09.28.2028
Thermoelectric plant Charqueadas	Parent Company	72	09.25.1998	09.28.2028
Thermo-electric plant Alegrete	Parent Company	66	09.25.1998	09.28.2028
Thermo-electric plant William Arjona	Parent Company	190	06.02.2000	04.28.2029
Thermo-electric plant Jacuí	Parent Company	350	02.07.2002	02.07.2032
Thermo-electric plant Lages	Lages Bioenergética	28	10.30.2002	10.30.2032

The concession regarding the hydroelectric plant Itá is shared with the joint subsidiary Itá Energética S.A.—ITASA (see Note 8-b.1).

The concession of the hydroelectric plant Machadinho is shared with other concessionaires that compose the consortium Machadinho, of which the Company is the leader and holds 16,94% interest.

e) Jacuí thermo-electric plant

In June 2004, after concluding a bidding process among potential third parties interested in the project Jacuí, the Company transferred 33.33% of the project to Elétrica Jacuí S.A.—ELEJA, for R$29,000. ELEJA is a specific purpose company, controlled by the entity that holds the exploitation rights of coal mines in the region of project Jacuí. Under the terms of the transfer agreement, the remaining percentage of the Company in the project, corresponding to 66.66%, was submitted to mutual options, purchase by ELEJA and sale by the Company. As of 07.29.2005, ELEJA acquired from the Tractebel an additional percentage of 33.33% of interest in the project, in the amount of R$31,181, becoming the holder of 66.66%, by exercising the purchase option provided in the agreement. In 2006, both the Company and ELEJA can mutually use their sale and purchase options in regard to the remaining interest of the project Jacuí. If the option is exercised, ELEJA will hold 100% of the interest

in the project. Under the terms of the agreement ELEJA undertook the responsibility for the conclusion of the project. In 2005, the permit for implantation and exploitation of the Thermo-electric plant Jacuí was transferred from Tractebel to ELEJA, as per approval of ANEEL.

The associated amounts of assets written-off by the Company in this quarter as a result of the facts above informed are the following:

Gross cost	400,696
Compensation of fixed assets in progress—RIC	(71,242)
Sub-total	329,454
Reversal of the provision	(303,040)
Net carrying amount	26,414

f) Restricted assets

Pursuant to Articles 63 and 64 of Decree 41.019, of February 26, 1957, assets and facilities used in the production, transmission, distribution, including sale of electric energy, are restricted to such services, and may not be removed, disposed of, assigned or given as mortgage guarantee without the previous and express consent of the Regulating Authority. Resolution 20/99 of ANEEL regulates the removal of restrictions on assets of Electric Power Utility concessions, granting previous authorization for the removal of restrictions on assets unserviceable to the concession, when meant for disposal, and further sets forth that the proceeds of disposals be deposited in a blocked bank account and that such funds be invested in the concession.

g) Assets of the federal government used by the company

The Company exercises possession and operates the Alegrete Thermoelectric Power Plant, composed of two generation units with a total capacity of 66 MW and a residential village with 15 houses, located in the Municipality of Alegrete, RS, owned by the Federal Government and granted under special use.

NOTE 10—UNITS 4 AND 5 OF THE UTE WILLIAM ARJONA

Generation units 4 and 5 of the thermoelectric plant of William Arjona, with a total power of 70 MW, use natural gas to generate electric energy and have been implemented with the specific purpose of meeting the needs of Brazilian Trader of Emergency Energy—CBEE, governed by the Electric Energy Supply Agreement executed on 01.10.2002, effective until 12.31.2004.

The Company's management was studying the possibility of ceasing the operation of such generation units at the end of the agreement with CBEE. In line with this possibility, the Company amortized the economic value of such assets over the period they were used, reaching a residual value of R$68,485 on 12.31.2004, compatible with the estimated disposal value, in the event such hypothesis was confirmed. The amount amortized in the period from 2002 to 2004 was R$35,214.

On 10.26.2004 the Management of the Company communicated to the Advisory Department of the Ministry of Mines and Energy that, after the end of the agreement with CBEE, the generation units will be maintained and will remain available for centralized operation, according to the standards and procedures of the National Electric System Operator—ONS, as of January 1st, 2005, on the same conditions as units 1, 2 and 3.

Therefore, the depreciation process will continue with no effects on future income, since the accelerated amortization carried out during the agreement with CBEE will be reverted simultaneously with the depreciation.

NOTE 11—SUPPLIERS

	09.30.2005	12.31.2004
Electric energy	16,846	32,598
Fossil fuels	38,964	37,445
Charges for the use of the power grid	34,716	23,074
Material and services	19,508	24,169
	110,034	117,286

NOTE 12—LOANS AND FINANCING ARRANGEMENTS

The main information on loans and financing in domestic and foreign currency is as follows:

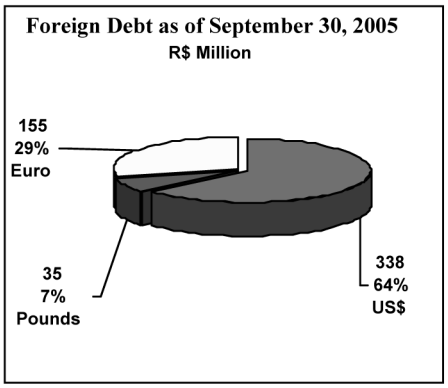
a) Composition

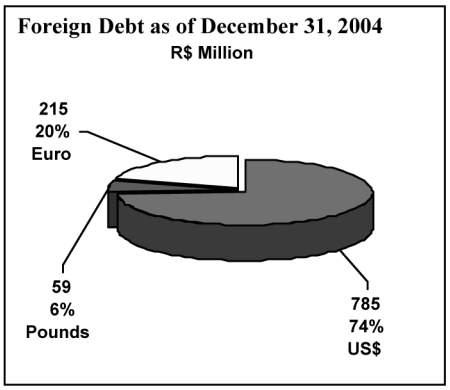
	09.30.2005			12.31.2004		
	Principal amount and charges			Principal amount and charges		
	Current	Long-term	Total	Current	Long-term	Total
In foreign currency						
Brazilian Finance Secretariat	89,297	288,133	377,430	104,561	414,074	518,635
Financial institutions	19,345	131,212	150,557	48,857	491,788	540,645
	108,642	419,345	527,987	153,418	905,862	1,059,280
In domestic currency						
ELETROBRÁS	71,555	193,473	265,028	66,406	247,802	314,208
Financial institutions	60,732	350,748	411,480	57,888	385,745	443,633
	132,287	544,221	676,508	124,294	633,547	757,841
	240,929	963,566	1,204,495	277,712	1,539,409	1,817,121

b) Changes in loans and financing operations

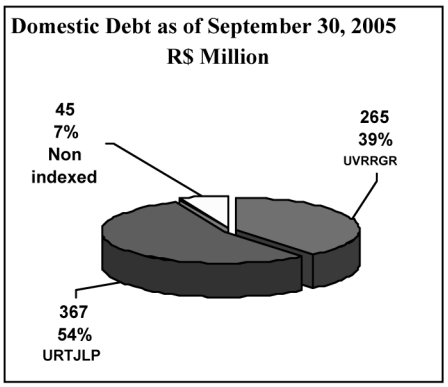
	Current	Long-term	Total
Balance as of 12.31.2004	277,712	1,539,409	1,817,121
Amortization	(549,838)	—	(549,838)
Transfers	439,362	(439,362)	—
Charges generated in the period	100,909	3,848	104,757
Compensation of guarantees deposited	—	(12,454)	(12,454)
Monetary variation generated in the period	(27,216)	(127,875)	(155,091)
Balance as of 09.30.2005	240,929	963,566	1,204.495

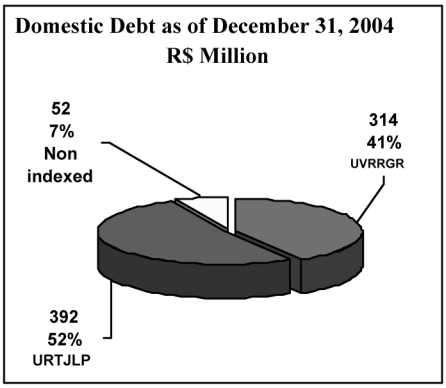
c) The total payable in the respective foreign currencies is divided as follows





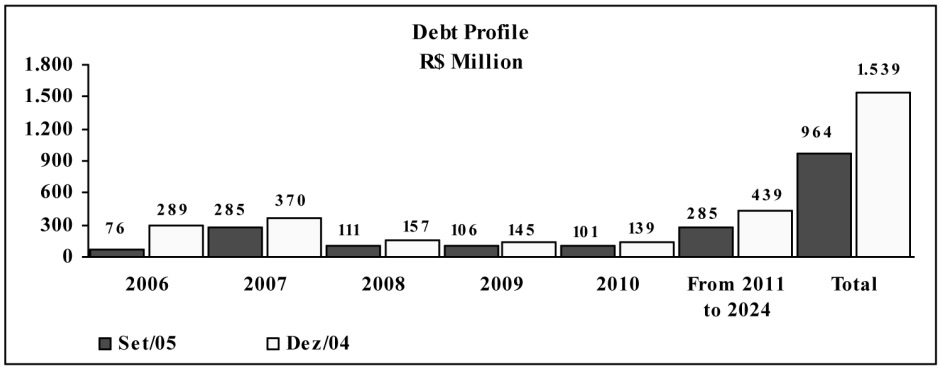
d) The total payable in domestic currency is divided as follows





IVRRGR—Index of Changes in RGR

e) Long-term loans, financing operations and charges have their maturities demonstrated below



f) Loans and financing operations are subject to charges at fixed and fluctuating rates, distributed as follows

Domestic market

Fixed rates: 11.90% to 12% p.a. (11.90% to 12.00% p.a, on 09.30.2004)
Fluctuating rates: 12% to 20.73% p.a. (12.00% to 18.18% p.a., on 09.30.2004)

International market

Fixed rates: 6% to 8.49% p.a. (6.00% to 10.43% p.a., on 09.30.2004)
Fluctuating rates: 2.91% to 9.30% p.a. (2.77% to 9.29% p.a, on 09.30.2004)

NOTE 13—DEBENTURES

a) Tractebel Energia

On May 11, 2005, the Brazilian Securities Commission—CVM approved the primary issuance of simple debentures, by means of public subscription, as per registrations CVM/SRE/DEB/2005/024 and 025. They are composed of 20,000 simple non-certificated debentures, not convertible into shares of the issuers, in two series, of the kind without guarantee or preference with nominal unit value of R$10,000.00 (ten thousand Reais), adding up to, at issuance date, 05.02.2005, the total amount of R$200,000. The 1st series, composed of 14,000 debentures, matures on 05.02.2011 and will have integral payment in only one installment. The 2nd series, composed of 6,000 debentures, will mature in 05.02.2010 and will have full amortization in only one installment. The debentures of the 1st series will be adjusted by the index IGP-M and will yield interest at a fixed rate of 9.29% per year, as from the issuance date, on the Unit Nominal Value of Debentures of the 1st series. The debentures of the 2nd series are entitled to a yield corresponding to 103.90% of the DI rate.

The total settlement of the public offer of debentures happened on 05.16.2005. The funds obtained from the Offer were used to increase the capital of the subsidiary Companhia Energética Meridional—CEM, to allow that company to anticipate the payment of the Loan Contracts with the Inter-American Development Bank (IDB).

The adjusted balance on 09.30.2005, amounts to R$207,211, R$10,208 under current liabilities and R$197,003 under long-term liabilities.

b) Itá Energética S.A.—ITASA

On 03.07.2001, the joint subsidiary issued two series of 8,400 nonconvertible debentures each, publicly issued, in the total amount of R$168,000, paid in on 03.23.2001. The adjusted balance on 09.30.2005, amounts to R$73,247, R$11,822 under current liabilities and R$61,425 under long-term liabilities (up to 12.31.2004, R$78,872, R$13,352 under current liabilities and R$65,520 under long-term liabilities).

Interest on debentures is paid annually; on the 1st series as from 12.01.2001 and on the 2nd series as from 06.01.2002 and are determined as set forth below:

1st series: from 12.01.2001 to 12.01.2003—IGP-M + 11.2% p.a. (completely paid)
from 12.02.2003 to 12.01.2013—IGP-M + 9.4% p.a.

2nd series: from 06.01.2002 to 06.01.2004—IGP-M + 11.2% p.a. (completely paid)
from 06.02.2004 to 06.01.2013—IGP-M + 9.4% p.a.

The amortization of the principal amount of the of debentures will be made in annual installments; amortization of the 1st series will start on 12.01.2004, with final maturity on 12.01.2103 and amortization of the 2nd series, will start on 06.01.2004, with final maturity on 06.01.2013.

The total of the long-term have their maturities demonstrated below:

	09.30.2005	12.31.2004
2006	4,095	8,190
2007	8,190	8,190
2008	8,190	8,190
2009	8,190	8,190
2010	8,190	8,190
From 2011 to 2013	24,570	24,570
	61,425	65,520

c) Companhia Energética Meridional—CEM

A Subscription and Payment of Debentures Agreement was entered into by and between the Subsidiary and the National Bank of Economic and Social Development—BNDES on 05.19.1999, and from May to December of 1999, 7,773 debentures were subscribed and paid-in, whose balance adjusted up to 09.30.2005 amounts to R$99,150, R$12,926 under current liabilities and R$86,224 under long-term liabilities (up to 12.31.2004, R$98,107, R$10,008 under current liabilities and R$88,099 under noncurrent liabilities.)

Interest on debentures is based on TJLP plus 4% p.a.; interest is paid every six months, from 10.01.1999 until 04.01.2013.

The amount corresponding to TJLP that exceeds 6% p.a. will be capitalized, and will become part of the principal amount of the of debentures.

The amortization of debentures' principal amount started on 10.01.2003 with final maturity on 04.01.2013, and occurs every six months based on an increasing amortization schedule that varies from 3.0625%, in the first amortization, to 7.5737% for the last installment, due on 04.01.2013

The total of the long-term have their maturities demonstrated below:

	09.30.2005	12.31.2004
2006	4,435	8,440
2007	9,532	9,284
2008	10,485	10,212
2009	11,534	11,234
2010	12,687	12,357
From 2011 to 2013	37,551	36,572
	86,224	88,099

NOTE 14—ESTIMATED OBLIGATIONS

	09.30.2005		12.31.2004	
	Current	Long-term	Current	Long-term
Provision for labor legislation	13,713	—	8,616	—
Provision for extensive maintenance	17,400	13,365	15,921	14,788
Provision for profit-sharing	—	—	6,500	—
Provision for management bonus	701	—	4,000	—
Provision for purchase of electric energy	—	—	1,467	—
Other	31	624	36	2,545
	31,845	13,989	36,540	17,333

Provision for labor legislation refers to estimated 13th month pay, vacation pay, vacation bonus and corresponding social charges.

Seeking to properly measure income of future years, the Company records provisions for extensive maintenance of the generation complex, based on an executive plan to preserve the operating conditions of plants.

NOTE 15—PROVISION FOR CONTINGENCIES

There are tax delinquency notices and preliminary judicial notices against the Company that are being contested administratively, as well as lawsuits at various court levels, which in the opinion of legal

advisors imply probable risks. All such lawsuits are provisioned at amounts deemed sufficient to cover contingencies, as shown below:

	09.30.2005		12.31.2004	
	Provision	Deposits in court	Provision	Deposits in court
Labor Contingencies				
Employment relationship and rehiring	16,510	13,418	19,182	11,824
Risk premium	727	608	974	491
Overtime	520	339	698	281
Salary parity and job classification	759	232	689	179
Overtime while in commuter transportation	738	169	820	190
Other	1,645	3,015	2,062	2,408
	20,899	17,781	24,425	15,373
Civil Lawsuit Contingencies				
Suppliers	59,633	—	31,020	—
Affected by UHE Itá	4,041	—	2,451	—
Actual damages and loss of profits	1,455	517	967	—
Occupational illness and accident	21,462	—	18,419	—
Other	3,547	—	2,654	2
	90,138	517	55,511	2
Tax Contingencies				
Social Contribution	14,173	6,338	11,066	5,034
INSS (Social security)	20,269	6,263	18,366	5,641
Income tax	—	2,134	—	—
PIS/COFINS	—	14,711	—	—
	34,442	29,446	29,432	10,675
	145,479	47,744	109,368	26,050
Classification of the balance				
Current	1,974	—	731	—
Long-term	143,505	47,744	108,367	26,050
	145,479	47,744	109,368	26,050

On 07.05.2005, the company filed an injunction against the Internal Revenue Service in Florianópolis, since the management understands that Regulation Instruction SRF 468/2004 overrode the limits of the Legislative Power by giving a new concept to the term ''pre-determined price'', provided in article 10 of Law 10.833/03. The company understands that the acceptance of the said term is already common practice in the Brazilian Tax System and has been in use since the enactment of Executive Law 1.598/1977, what implies that the indicated Regulatory Instruction is illegal.

As a consequence, the company is paying PIS and COFINS on revenue from contracts entered into before 10.31.2003 for periods longer than one year and at a pre-established price, based on the cumulative taxation system provided in the previous law, depositing the amounts the company understands to be undue in an account linked to court where the suit is in progress.

In the opinion of the company's legal advisors, the possibility of loss arising from such lawsuit is lower than the change of a favorable result, so the company has not been accruing for the amount not paid starting in June 2005.

The Company also is a party in lawsuits that, in the opinion of legal advisors based on experiences of similar cases, do not pose a probable risk and, therefore, have not been recognized in the financial statements.

The amounts involved are detailed below:

	09.30.2005			12.31.2004		
	Possible risk	Remote risk	Total	Possible risk	Remote risk	Total
Labor-related	8,953	11,506	20,459	9,261	11,269	20,530
Civil	26,085	24,089	50,174	19,090	24,048	43,138
Tax-related	17,530	3,549	21,079	—	—	—
	52,568	39,144	91,712	28,351	35,317	63,668

NOTE 16—CONCESSION PAYABLE

The subsidiary Companhia Energética Meridional—CEM will pay to the Federal Government the amounts shown below for the concession for exploitation of the hydraulic energy potential of hydroelectric utilization Cana Brava, in monthly installments equivalent to 1/12 of the corresponding amounts of annual payment, adjusted based on the annual variation of the General Price Index—Market—IGP-M:

Year	Payment starts on	Annual amount	Total amount
1	—	1	1
2-6	—	—	—
7-25	08.30.2004	680	12,920
26-35	08.30.2023	61,280	612,800
			625,721

The flow of payments above is set forth under Section Six of the Concession Agreement. In order to adequately reflect the granting of remunerated concession and corresponding obligation before the Federal Government in assets and liabilities, CEM recorded its amount under intangible assets and current and noncurrent liabilities.

Taking into consideration that values under the agreement are determined at future prices, CEM adjusted them to present value based on a discount rate of 10% p.a., as provided in the Invitation to Bid N. 04/97 for the bidding of the concession under reference. Until the commercial start-up of Cana Brava plant, the adjustment of liabilities based on the discount rate and variation of IGP-M price index was capitalized in intangible assets and, thereafter, recognized directly on income.

The net present value balance of this obligation, adjusted up to 09.30.2005, amounts to R$174,918, R$1,528 under current liabilities and R$173,390 under noncurrent liabilities (up to 12.31.2004, R$161,889, R$1,472 under current liabilities and R$160,417 under noncurrent liabilities).

The total net present value amount due on a long-term basis has the following scheduled maturities:

	09.30.2005	12.31.2004
2006	380	1,506
2007	1,520	1,506
2008	1,520	1,506
2009	1,520	1,506
2010	1,520	1,506
From 2011 to 2023	166,930	152,887
	173,390	160,417

NOTE 17—POST-EMPLOYMENT BENEFITS

Post-employment benefits offered by the Company are the following:

1. Supplementary pension plan

The Company, through the entity PREVIG—Sociedade de Previdência Complementar, keeps Supplementary Pension Plans to its employees. PREVIG is a non-profit closed supplementary pension entity governed by private law, sponsored by the company in the condition of its Founder and by companies of Suez Group.

The Benefit Plans managed by PREVIG are of the kinds *Defined Benefit*, which are closed to new participation of employees and of the kind *Defined Contribution*.

Defined benefit plans

Defined Benefit Plans are invested to earn profits for retirement and pension benefits. The following benefits have simple sharing for beneficiaries:

- Retirement plan for time of work;
- Retirement plan caused by disability;
- Retirement for old age;
- Special retirement an retirement for former military people;
- Pension;
- Inmate pension (auxílio reclusão); and
- Funeral allowance.

The initial retirement benefit consists basically of the difference between the arithmetic average of the last 36 contribution amounts of the employee to the Plans, adjusted on a monthly basis by the same indices adopted by the Public Social Security system, and the theoretical value of the retirement benefit payable by the Public Social Security system, calculated as per the rules that were in effect before the enactment of Law 9.876 dated 11.26.1999. After the beginning of the payment of the benefit, it is annually adjusted based on the variation of the index INPC.

The financing of the Benefit Plan is covered by contributions of participants and of the sponsor. The Company's contribution corresponds to twice the contribution of its employees. Additionally, the Company contributes with 1.7825% of the payroll (a percentage adjusted monthly by a factor determined by the fluctuation in the number of employees who take part in the plan) for the purpose

of amortizing amounts referring to time of service that is calculated by an actuarial. The obligation for payment of benefits ends in December 2023.

The Company is also responsible for 100% of the value of administrative expenses of PREVIG, limited to 15% of the total respective revenue the plan receives. The value of those expenses from January to September 2005 was R$1,768 (R$1,475 in the same period of 2004).

Before the incorporation of PREVIG, the Defined Benefit Plan was managed by Fundação Eletrosul de Previdência e Assistência Social—ELOS, sponsored by Tractebel and another company. In October 2002, Secretaria de Previdência Complementar (Supplementary Benefit Secretariat—SPC) approved the termination of the Agreement with ELOS and the total transfer of its management to PREVIG, through Order 1.755/SPC/GAB/COA. Despite the rescission of the Agreement, the Benefit Plan composed of participants who started receiving benefits before 12.23.1997, the date of split of ELETROSUL, as well as of participants who opted for Deferred Proportional Benefit until that date, continue under the responsibility of Tractebel.

While this situation lasts, the Company is responsible for financing 57% of the value of administrative expenses of ELOS (the remaining 43% portion is financed by the Benefit Plan of the other sponsor of that foundation). Expenses are limited to 15% of the total respective revenue received by the plans by ELOS. The value of payments of the Company from January to September of 2005 was R$1,516 (R$723 in the same period of 2004).

The parties continue searching for alternatives to the one approved by SPC to change the current situation.

Defined contribution plan

Besides the above-mentioned benefit plan, PREVIG started managing another plan of the kind *Defined Contribution,* closing the Defined Benefit plan to new participants on October 5, 2004, the date when the new plan was approved and communicated by the Secretaria de Previdência Complementar—SPC through Order N. 1998 DAJUR/SPC.

At the same date, the Company entered into an agreement with PREVIG that started to offer a *Defined Contribution* plan to its employees and began the process of migration provided in its regulations. The registration of participants in the Defined Contribution began in January 2005 and the migration process ended on 07.31.2005. As of 09.30.2005, 843 participants were registered with that plan.

In the defined contribution plan, of which 94% of the Company's employees take part, the financing is composed of basic contributions of the participants and of the sponsor. The basic contribution of the Company corresponds to the same value of the basic contribution of its employees. In addition, as an incentive to migration, the company undertook a special contribution that will be paid to each participant with at least 10 (ten) years of participation in the plan, calculated with the objective of increasing the mathematic accruals for the participant, with the purpose of neutralizing a possible impact the participant would have by opting for the migration.

The value of the contributions of the Company for both benefit plans from January to September 2005 was R$3,406 (R$4,103 in the same period of 2004).

As per instructions of CVM Decision 371, dated of 12.13.2000, the gains and losses from anticipated reductions and payment of a defined benefit plan should be recognized as they occur. For such purpose, independent actuaries are preparing a new actuarial appraisal, considering the impacts of the migration process between plans. The Company's management does not expect the occurrence of significant effects on the financial statements as a result of the new evaluation. Possible gains and losses will be recognized in the next quarter.

2. Bonus on confidentiality

It refers to the payment of a bonus to employees of management level when their work relationships are terminated.

The actuarial assumptions used in the assessment of those benefits (as on December 31, 2004) are described as follows:

Economic hypothesis (nominal)
Discount rate—12.25% p.a.

Expected return rate from assets—12.5% p.a.

Future salary growth

- Active participant—8% p.a.
- Self-sponsored participant—6% p.a.

Growth in public social security benefits—6% p.a.

Growth in benefits of the plan sponsored by the company—6% p.a.

Inflation—6% p.a.

Capacity factor

- Salaries—100%
- Benefits—100%

Demographic hypothesis
Life Span Table (active)—GAM 1983, with age adjustment of -1

Life Span Table of Disabled People—IAPB 57

Table of People Becoming Disabled—TASA27

Rotation Table—T-1 *Experience*

Retirement Age—First date when all grace periods finish

% of married active participants at retirement date—90%

Age difference between the participant and his/her spouse—Wives are 4 years younger than husbands

Other hypotheses
% of participants entitled to conversion of special retirement into retirement for time service (SB-40) who will opt for the conversion—100%
Conversion factor of SB-40–140%

The amounts recognized from January to September of 2005 and 2004, with effects on the net actuarial liabilities assessed as of 09.30.2005 and 2004, are as follows:

Net liabilities as of 12.31.2004 and 2003	250,127	244,101
Expenses recognized in the income statement:		
Interest and monetary restatements of contracted obligations	12,221	10,168
Contribution of the sponsor	4,792	4,064
Supplementary contribution	1,615	1,049
Supplement of actuarial expenses projected for the period	29,452	27,655
	298,207	287,037
Amortization of contracted obligations	(31,187)	(35,948)
Net liabilities as of 09.30.2005 and 2004	267,020	251,089
Classification of liabilities		
Current	40,800	52,768
Long-term liabilities	226,220	198,321
	267,020	251.089

NOTE 18—DEFERRED TAX LIABILITIES

As of 09.30.2005, income tax and social contribution on net income were recorded in this account in the amount of R$36,532 (R$39,616 on 12.31.2004), calculated on the provision for sale of electric energy at MAE in the amount of R$107,446 corresponding to the period between September 2000 to September 2002. Considering that the revenue amount is being contested at court by agents who disagree with the interpretation adopted by MAE in the application of certain accounting rules, as per the dispositions of ANEEL Order N. 288, dated of 05.16.2002. A possible success of the agents will characterize the non-existence of revenue and the respective asset. For that reason the Company is treating it as a provision and considered it as a temporary difference for tax purposes.

NOTE 19—SHAREHOLDERS' EQUITY

a) Authorized capital stock

The Company is authorized to increase its capital stock up to the limit of R$5.000.000, regardless of amendments to the Company's bylaws.

b) Grouping and conversion of shares

In compliance with a decision made during an Extraordinary Meeting held on April 7, 2005, the Company's shares of capital stock were grouped on 05.23.2005 at the ratio of 1,000 (one thousand) shares to 1 (one) share of the same existing kind and class.

In parallel to that operation in Brazil, the ratio of shares with ADR—American Depositary Receipts in the American market also changed, becoming 5 (five) shares to 1 (one) ADR.

The Company's Management Board, during a meeting held on 06.07.2005 approved a proposal for conversion of all preferred shares of the classes "A" and "B" into ordinary shares, at the proportion of one ordinary share to each preferred share.

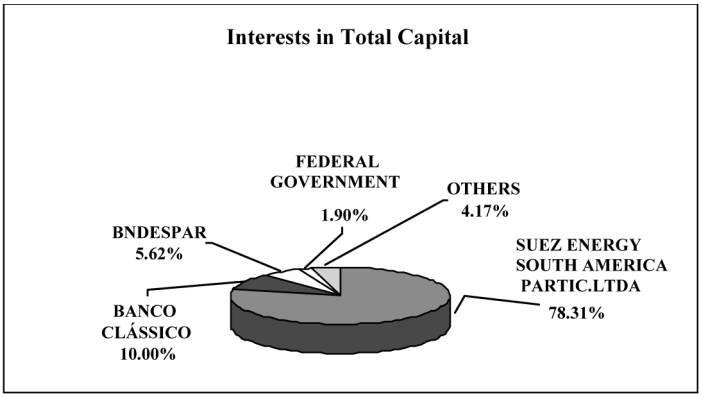
This proposal had as objectives: (i) equalize the rights entitled by the shares issued by the Company; (ii) adapt its stockholding structure to the most recommended procedures of corporate governance; (iii) assure more liquidity to all shares of the Company; and (iv) allow the Company in the future to have conditions for entering in the "New Market" of the Stock Exchange of São Paulo—BOVESPA.

Extraordinary Meetings of holders of preferred shares of the classes "A" and "B" were held on 06.27.2005 and only the conversion of all preferred shares of the class "B" and later consolidation of the company's bylaws was approved. On 08.17.2005 during a second Special Meeting of holders of preferred shares of class "A" (second call) the conversion of all preferred shares of the class "A" and also the subsequent consolidation of the bylaws was approved.

c) Subscribed and paid capital stock

As of 09.30.2005 and 12.31.2004, the Company's capital stock amounted R$2,445,766 represented, after grouping and conversions mentioned in item b above, by 652,742,192 shares, all ordinary, nominative and without face value. The equity value of shares as of 09.30.2005 was R$5.17 (R$4.27 on 12.31.2004).

As of 09.30.2005, the company's stockholding had the following g constitution:



d) Composition of reserves

	09.30.2005	12.31.2004
Capital Reserve		
Compensation of assets and rights created with equity capital	91,695	91,695
Profit Reserves		
Statutory reserve	102,252	102,252
Retained earnings reserve	147,243	147,243
	249,495	249,495

NOTE 20—OPERATING EXPENSES DETAILED BY TYPE

	09.30.2005					09.30.2004
	Costs		Expenses			
	Production and sale	Services rendered	Selling expenses	General and administrative expenses	Total	Total
Personnel	54,037	4,641	4,190	27,947	90,815	84,767
Material	14,897	167	31	897	15,992	11,664
Third-party services	32,496	1,520	1,727	17,063	52,806	42,759
Fuel to produce energy—CCC	257,511	—	—	—	257,511	193,912
Fuel to produce energy—without subvention	83,422	—	—	—	83,422	110,999
Financial compensation for use of water resources	48,805	—	—	—	48,805	42,332
Charges on the use of electric system	—	—	121,832	—	121,832	106,485
Use of Public Assets—UBP	3,128	—	—	—	3,128	3,588
Depreciation and amortization	148,141	—	26	7,756	155,923	156,697
Creation/reversal of provisions for doubtful debtors	—	—	(9,126)	—	(9,126)	(2,445)
Creation/reversal of operating provisions, net	(1,532)	—	—	16,364	14,832	8,208
Insurance	6,650	324	—	481	7,455	8,405
Pension plan—SB-40	—	—	—	12,909	12,909	16,801
Severance pay	—	—	—	14,530	14,530	—
Inspection fee	—	—	—	6,900	6,900	5,355
Other expenses	10,504	67	2,484	14,130	27,185	24,424
	658,059	6,719	121,164	118,977	904,919	813,951

NOTE 21—LEASING

The Company has commercial leasing operations for renewal of its computing equipment and fleet of vehicles.

The currently existing contracts involve the following assets:

a) Information technology equipment

The leasing term is 36 months and the acquisition of the goods by the leaseholder is assured in the contract based on the unit value of R$1.00 on 09.30.2005, there were 349 microcomputers contracted (341 as of 09.30.2004).

The balance of amounts payable on 09.30.2005 was R$781, from which R$442 will mature in 12 months and R$339 in the subsequent months. The amount of payments recognized in results from January to September 2005 was R$401 (R$305 in the same period of 2004).

b) Fleet of vehicles

As of September 30, 2005, the Company had a leasing contract for 40 vehicles. The contracts have a 36-month term and it is assured to the leaseholder the acquisition of the goods at the end of the contracts at amounts corresponding to 20% of the value of the goods.

The balance of the consideration payable as of 09.30.2005 was R$813, from which R$527 will mature within 12 months and R$286 in the subsequent months. The amount of consideration recognized in results from January to September of 2005 was R$616 (R$331 in the same period of 2004).

NOTE 22—FINANCIAL INSTRUMENTS

a) Risk management

a.1) Market risk

The use of financial instruments by the Company aims to protect its assets and liabilities, minimizing its exposure to market risks, especially in connection with fluctuations of interest rates, price indexes and currencies. Such risks are monitored by the Financial Management Committee that assesses on a regular basis the Company's exposure and proposes operating strategies, control system, position limits and credit limits with other partners in the market.

The Company has been recording on its books interest rate swap transactions in the international market and has a net liabilities balance at the average fixed rate of 5.72% p.a. and a net asset balance in Libor US$ six months, with flow starting on 10.15.2001 and ending on 04.15.2006, a principal amount of US$10,044 thousand, equivalent to R$22,320 on 09.30.2005 (R$36,657 in 12.31.2004), amortized every six months from 04.15.2003. From January to September of 2005, this transaction generated an expense of R$570 (R$1,416, in the same period of 2004), duly recognized in the financial statements.

In November 2004, taking advantage of the devaluation of the dollar as opposed to the real, the Company implemented a policy of increased protection of its liabilities in foreign currency by means of over-the-counter swap transactions, using its Exclusive Investment Fund as a vehicle (see Note 3). The maturity of the swap transactions are simultaneous with the due dates of the flow of obligations of liabilities in foreign currency, considering a period of twenty-four months. Transactions are recorded in Cetip and are made with financial institutions known for their equity and financial solidness, within the credit limits defined by the Company. Swap transactions protect 47.5% of Company's liabilities in foreign currency which, when added to the percentage amount invested in federal government bonds indexed to the US dollar, allow for a consolidated protection of 50.1% of Company's liabilities in foreign currency.

a.2) Credit risk

In long-term bilateral agreements and initial energy purchase and sale agreements, entered into with distributors, the Company seeks to minimize its credit risk by using a mechanism to create guarantees involving customers' receivables.

As of 2003, with the reduction in sales of electric energy linked to initial agreements, together with the beginning of operation of new plants, the Company started to broaden its customer portfolio by focusing on industrial customers, also known as Free Consumers. In order to minimize the credit risk with such commercial partners a credit area was created in the Company, whose job includes a prior analysis and the determination of the credit limit and guarantees to be required from the other parties, in cooperation with the Credit Committee.

In financial market transactions, the Company also has credit limits with financial institutions that are regularly reviewed by its Financial Management Committee, based on an in-house evaluation and on ratings published by risk rating agencies.

As mentioned in Note 3, starting in October 2004, the Company has investments in an Exclusive Investment Fund. The amount of investments per financial institution is within the limits established by the Company in its credit policy for financial institutions.

b) Market value

Regarding operations involving financial instruments, only in loans and financing arrangements significant differences were identified between market values and carrying amounts, mainly because those financial instruments have very long settlement maturities and costs significantly low in relation to the rates currently practiced in similar contracts. In the assessment of market values, the company's management used discounted future cash flows at rates deemed adequate for similar operations or international market prices, when available.

	09.30.2005		12.31.2004	
	Carrying amount	Market Value	Carrying amount	Market Value
Loans and charges in foreign currency	527,987	507,775	1,059,280	1,042,570
Loans and charges in domestic currency	676,508	670,212	757,841	749,581
	1,204,495	1,177,987	1,817,121	1,792,151

NOTE 23—RELATED PARTIES TRANSACTIONS

The Company has contracts with its subsidiaries and with its indirect controlling company, as follows:

Itá Energética S. A.—ITASA

Operation and Maintenance Services Agreement of ITÁ Hydroelectric Power Plant, rendered by the Company, entered into on 09.11.1998 in the context of Consortium Itá, valid until 10.16.2030, whose values are adjusted annually according to the IGP-M price index.

Agreement of Purchase and Sale of Electric Energy entered into on 01.15.2001, with the purpose of regulating the purchase, by the Company, of 61 MW average of energy owned by ITASA at Itá Hydroelectric Power Plant, governed by applicable laws and market rules, effective until 10.16.2030, adjusted annually according to the variation of the dollar plus US inflation.

Agreement of Purchase and Sale of Electric Energy entered into on 01.15.2001, with the purpose of regulating the purchase, by the Company, of 167 MW average of energy owned by ITASA at Itá Hydroelectric Power Plant, governed by applicable laws and market rules, effective until 10.16.2030, adjusted annually by the IGP-M price index.

Companhia Energética Meridional—CEM

Agreement entered into on 04.09.1999, addenda made on 04.15.1999 and 11.09.2002, valid for indefinite term, whose purpose is to render operational administration services, since CEM does not have its own staff. The value of the agreement is adjusted annually according to the IGP-M price index.

Agreement of Purchase and Sale of Electric Energy, entered into on 01.05.2001, appendix made on 03.06.2001 and 08.09.2002, valid until 2015, to purchase the electric energy produced at UHE Cana

Brava. The agreement establishes the purchase of energy, by the Company, in the annual amounts of 1,125,616 MWh, 2,189,036 MWh and 2,395,903 MWh, starting on October 2002, November 2002 and December 2002, respectively. The value of the agreement is adjusted annually according to the IGP-M.

Operation and Maintenance Agreement of UHE Cana Brava, entered into on 01.05.2001, appendix made on 03.09.2001 and 06.01.2002, valid until the end of the plant concession and whose values are adjusted annually according to IGP-M, under which the Company undertakes to operate and perform maintenance of the business venture.

Lages Bioenergética Ltda.

Agreement entered into on 01.02.2003, valid for an indefinite term, whose purpose is to render operational administration services, since Lages does not have its own staff. The value of the agreement is adjusted annually according to the IGP-M.

Agreement of Purchase and Sale of Electric Energy entered into on 03.15.2004, with the purpose of regulating the purchase, by the subsidiary, of up to 26 MW average of energy per month owned by the Company, effective from 04.01.2004 to 03.31.2017.

Operation and Maintenance Agreement of Lages Cogeneration Unit, entered into on 04.01.2004, ending on 03.31.2012, under which the Company undertakes to operate and perform maintenances of the business venture. The value of the agreement is adjusted annually based on the variation of the compensation defined according to the Collective Labor Agreement of the Company's employees.

Tractebel Energia Comercializadora Ltda.

A contract entered into on November 1, 2004, in effect for an undetermined period and that has as purpose the rendering of operating management services, since Tractebel Comercializadora does not have its own personnel. The contract value is annually adjusted based on the index IGP-M.

The amounts recognized in the balance sheet and income statement accounts are the following:

	09.30.2005							12.31.2004
	Suez Energy South America Partic. Ltda	CEM	ITASA	Lages	Tractebel Energia Comerc. Ltda	CESS	Total	Total
Assets								
Accounts receivable	659	181	2.232	851	5,152	222	9,297	16,531
Liabilities								
Suppliers	—	29,443	10,038	1	—	—	39,482	42,312
Dividends and shareholders' equity	—	—	—	—	—	—	—	432,054
								09.31.2004
Income statement								
Operating Revenue								
Supply of energy	—	—	—	4,173	32,641	—	36,814	4,534
Service income								
Management	—	485	—	76	22	302	885	494
Operation and maintenance	—	1,217	7,174	1,011	—	—	9,402	8,287
Cost of Electric Energy and Services								
Purchase of energy	—	183,998	96,253	—	—	—	280,251	312,429
Other		—	—	—	—	—	—	6
General and administrative expenses								
Consulting	—	—	—	—	—	—	—	2,561
Financial Revenue	—	—	14	—	—	—	14	3,165

NOTE 24—GUARANTEES GIVEN TO THIRD PARTIES

Itá Energética S.A.—ITASA

The Company and other shareholders of ITASA are intervening parties in the agreements entered into by and between the investee and BNDES and other financial agents, linked to the construction of UHE Itá. The intervening parties have given as collateral the total amount of shares issued by ITASA, owned by them, until the final settlement of all obligations undertaken in the agreements under reference. As of 09.30.2005, the debt presented in the consolidated financial statements of the company was R$284,275 (R$303,736 as of 12.31.2004).

In order to ensure the payment of the obligations resulting from the above mentioned agreements, ITASA has given the following guarantees to BNDES and the Financial Agents: a) Pledge of Concession Emerging Rights to exploit UHE Itá; and b) Pledge of Credit Rights resulting from the Agreements of Purchase and Sale of Electric Energy entered into with its investors.

Companhia Energética Meridional—CEM

Tractebel Energia is an intervening party to the Agreement of Subscription and Payment of Debentures Nonconvertible into Shares n° 98.2.654.3.1 and to the Financing Agreement by Opening of Credit Facility n°98.2.654.3.3, entered into by and between CEM and BNDES, the first on 05.19.1999, appendix made on 05.25.1999, and the second on 04.05.2000. As an intervening party, the following main obligations regarding the agreements have been undertaken with the financial agent:

ensure the prepayment in the following exclusive events: a) end of concession by reason imputable to CEM, to the intervening parties or their subsidiaries, associated companies or holding companies; and b) agreement entered into with the Granting Authority by CEM, by the intervening parties or by any of their subsidiaries, associated companies or holding companies, with the purpose of ending the concession;

assignment to BNDES of any amounts resulting from indemnity received as a result of the end of concession of UHE Cana Brava, by the Granting Authority.

In addition to the obligations specified above, Tractebel Energia has given to BNDES, as collateral, the total amount of shares owned by it, representing the share capital of CEM, until the final settlement of all obligations undertaken in the above mentioned agreements. The debt as of 09.30.2005 totaled R$209,292 (R$558,525 as of 12.31.2004).

CEM has assigned receivables resulting from the generation and sale of energy from UHE Cana Brava as a guarantee for payment of its loans and financing

Besides the above-mentioned contracts signed with BNDES, CEM took part in Loan Contract 1260/OC/BR, entered into on 12.08.2000 and amended on 03.06.2001 with Inter-American Development Bank—IDB, where the Company was intervener. The mentioned contract was settled in advance by CEM on 05.16.2005.

Lages Bioenergética Ltda.

The Company is the intervening guarantor in the Agreement of Fixed Credit Facility entered into by and between Lages Bioenergética and Banco Regional de Desenvolvimento do Extremo Sul—BRDE, on 07.25.2003, and gave as collateral, the shares in the share capital of the subsidiary, owned by it, until the final settlement of all obligations undertaken in the agreement under reference. The debt as of 09.30.2005 totaled R$45,849 (R$48,743 as of 12.31.2004).

In order to ensure the payment of the obligations resulting from the above mentioned agreement, Lages Bioenergética has given as collateral the receivables resulting from the sale of electric energy from the Cogeneration Unit.

NOTE 25—INSURANCE

The Company has a comprehensive operating risk insurance policy with a declared value for property damage of US$3,515,233 thousand, equivalent to R$7,811,551 thousand on 09.30.2005, and with a declared value for loss of profits of US$98,503 thousand, equivalent to R$218,893 thousand on 09.30.2005. The maximum combined limit for indemnification of damage to property and loss of profits is US$150,000 thousand, equivalent to R$333,330 thousand on 09.30.2005, per event.

The policy and values above refer to property of the Company's ownership. UHE Cana Brava, whose concession belongs to the subsidiary CEM, was included in the insurance policy of Tractebel Energia starting on 12.19.2003, with a declared amount for damages to property of US$320,000 thousand equivalent to R$711,104 thousand on 09.30.2005 and loss of profits of US$8,105 thousand equivalent to R$18,011 thousand on 09.30.2004, by means of endorsement N. 1095000026.

In addition to such coverage, the Company has liability insurance policies with coverage of US$50,000 thousand, equivalent to R$111,110 thousand on 09.30.2005. Such policies include UHE Itá, built and exploited in consortium with the joint subsidiary ITASA.

The subsidiary Lages Bioenergética Ltda. has Operating Risk insurance with coverage of US$20,000 thousand equivalent to R$44,444 thousand on 09.30.2005, and Engineering Risks insurance with coverage of a steam turbine with 27 MW of potency, during the test phase and during 12 months of comprehensive maintenance.

The maximum indemnity limits of engineering risk coverage are the following:

- Basic coverage, including tests—R$7,600 thousand
- Maintenance coverage—R$7,600 thousand

Besides these strategic insurances, the Company has insurance to cover risk of national and international transport, civil responsibility of executives, including the subsidiaries, and life insurance for the directors and employees.

NOTE 26—LONG-TERM AGREEMENTS

In addition to the agreements with subsidiary companies and the indirect holding company mentioned under Note 23, the Company has long-term rights and undertakings, including:

a) Connection contract

In agreement with Law n° 9.648/98 and Decree n° 2.655/98, setting forth that the access and use of electric energy transmission systems be contracted separately from the purchase and sale of the energy itself, on 08.20.1998, the Company entered into the Connection Agreement with Empresa Transmissora de Energia Elétrica do Sul do Brasil S.A.—ELETROSUL, effective as of 09.01.1998.

b) Contract for the use of transmission and distribution system

To meet the power sale contracts not covered by the Initial Contracts and electric power from plants that started their operations as from January 1, 2002, the Company entered into contracts with the Electric System National Operator—ONS, transmission companies and Empresa Energética do Mato Grosso do Sul S.A.—Enersul, in effect until the termination of the concessions or permits of the generation units of Tractebel Energia or termination of the transmission companies and distributors, whichever comes first. Through them, it undertook to cover 75% of transmission costs. The remaining 25% are under the responsibility of distribution concessionaires. The costs for the company totalized R$80,212 from January to September of 2005 (R$80,813 in the same period of 2004).

Also, the subsidiary CEM and ITASA entered into contracts with the ONS and transmission companies, with the same termination terms referred to above. The costs totalized R$21,491 from January to September of 2005 (R$19,777 in the same period of 2004).

c) Initial contracts of purchase and sale of Electric Power

Based on Law n° 9.648/98, article 10 and GCOI standards, the Company entered into the Initial Agreements of Purchase and Sale of Electric Energy with the concessionaires listed below, which are being reduced by 25% per year, starting in 2003, until their complete end on 12.31.2005. The

amounts indicated below refer to the contractual balances for supply in the period from 10.01.2005 to 12.31.2005:

- Rio Grande Energia S.A.—RGE:—Total of 186,576 MWh;
- Centrais Elétricas de Santa Catarina S.A.—CELESC:—Total of 644,184 MWh;
- Companhia Estadual de Energia Elétrica—CEEE:—Total of 67,896 MWh;
- Empresa Energética de Mato Grosso do Sul S.A.—ENERSUL:—Total of 155,664 MWh;
- Furnas Centrais Elétricas S.A.:—Total of 288,696 MWh;
- AES Sul—Distribuidora Gaúcha de Energia S.A.:—Total of 216,396 MWh.

d) Bilateral contracts of purchase and sale of Electric Power

The energy not committed to the Initial Contracts, including that which is being released from such agreements starting in 2003, has been subject to agreements with distributors and free consumers. Therefore, the Company has the following main agreements for sale of electric energy, among others:

Contracting party	Contract period	Contracted energy (MWh)
RGE	10.01.2005 to 12.31.2014	42,704,904
CELESC	10.01.2005 to 12.31.2007	296,010
	10.01.2005 to 12.31.2008	20,068,191
Companhia Paulista de Força e Luz	10.01.2005 to 12.31.2010	9,138,551
Companhia Piratininga de Força e Luz	10.01.2005 to 12.31.2010	5,338,554
Light	10.01.2005 to 12.31.2005	26,280
	10.01.2005 to 12.31.2007	749,892
Energy traders	10.01.2005 to 12.31.2007	7,265,863
	10.01.2005 to 12.31.2010	15,240,063
	10.01.2005 to 12.31.2014	10,675,948
Industrial consumers	10.01.2005 to 12.31.2007	5,020,374
	10.01.2005 to 12.31.2010	6,028,622
	10.01.2005 to 12.31.2012	9,959,289

e) Purchase of Electric Power from Argentina

The Company entered into an agreement with CIEN—Companhia de Interconexão Energética, for a period of 20 years, starting on 06.21.2000 for the purchase of 300 MW of stable energy with associated power, to be made available at substation Itá of ELETROSUL.

In the month of March 2005, Agência Nacional de Energia Elétrica—ANEEL made an inspection to check the conditions of physical delivery guarantee of power at the Thermo-electric plant Uruguainana and at the Interconnections of Garabi (CIEN). It was verified the non-availability of generation and transmission of electric power by the inspected agents at the contracted amounts. As a result of that fact, the Ministry of Mining and Energy issued Order 153 dated 03.30.2005, defining new amounts of physical guarantee for the respective generation facilities and interconnections.

On April 1, 2005, ANEEL published Regulation Instruction N. 155/05, establishing the criteria to be used by the Electric System National Operator—ONS and by the Câmara de Comercialização de Energia Elétrica—CCEE (Electric Power Trade Chamber) in the determination of availability limits for generation and physical guarantee of power at the Thermo-electric plant Uruguaina and for the Interconnections of Garabi. Based on these regulations, CIEN has conditions to assure the availability of only 72 MW, a volume much lower than the 300 MW provided in the contract.

This fact would submit the Company to the penalties established in the law for the sector, due to the lack of capacity, which led it to enter, in an emergency fashion, into a short-term agreements for the purchase of power from another agent.

f) Purchase of Natural Gas

On 11.10.2000, the Company entered into an agreement to purchase natural gas with Companhia de Gás do Mato Grosso do Sul—MSGÁS, effective for 5 years as of 2001, where the Thermoelectric Power Plant of William Arjona, located in Campo Grande—MS has started its commercial operation.

g) Revitalization of generators of the Hydroelectric Plant Salto Osório

On 12.19.2003, the Company entered into an agreement with GE Hydro Inepar do Brasil S.A., valid for four years, for the complete renovation of the six generation units of UHE Salto Osório.

NOTE 27—SUBSEQUENT EVENTS

As a Relevant Fact, the Company, on 10.10.2005, communicated to the market in general that:

> (i) The Board of Directors approved, during a meeting held on 10.07.2005, the inclusion and listing and trade of its shares in the New Market segment of the Stock Exchange of São Paulo—Bovespa. The actual inclusion of the Company, the listing and the trade of its shares in such segment of Bovespa is subject to the approval of the respective statutory changes by the General Meeting of the Company's Shareholders.
>
> (ii) With the purpose of increasing the liquidity of the shares traded at Bovespa, the controlling stockholder of the Company, Suez Energy South América Participações Ltda. ("SESA"), intends to make a secondary public offer that will comprise approximately 8% of the voting capital stock of the Company at the moment of the offer. The current percentage of interest of SESA in the capital stock of the company is 78.31%. It is not excluded the participation of other shareholders in the offer. It will be made by means of a secondary public distribution, in a non-organized over-the-counter market in Brazil, in accordance with the Instruction of the Brazilian Securities Commission number 400, dated of 12.29.2003. It will include sales overseas, based on the registration exemptions by the Securities Act of 1993 of the United States of America. The registration request for the mentioned secondary public offer was filed with the Brazilian Securities Commission on 10.07.2005.

The Company, through the Notice to Shareholders dated 10.19.2005, communicated to the market that the Board of Directors, during a meeting held on the same date, approved:

> (i) credit of interest on own capital referring to the period between June 1 and 11.10.2005, in accordance with article 9 of Law 9.249/95 and Decision CVM 207/96 of the Brazilian Securities Commission—CVM; (ii) distribution of dividends, based on the financial statements as of June 30, 2005; (iii) distribution of intermediate dividends, from the profit reserves existing on December 31, 2004, except for the legal reserve, and the last two having as basis the caput and paragraph 2 of article 204 of Law 6.404/76, respectively, with the following values and conditions:

I—Interest on own capital

The gross amount of interest on own capital will be R$122,000, corresponding to R$0.186904 per share.

The accounting effects will be recorded on 11.10.2005, based on the shareholding position on 10.31.2005.

The Company's shares will be traded "ex-dividend" on own capital as from 11.01.2005.

The amounts of interest on own capital will be subject to withholding income tax at the rate of 15%, except for stockholders proven to be immune or exempt.

Interest on own capital, net of withholding income tax will be attributed to mandatory dividends addressed by article 202 of Law 6.404/76.

The beginning of payment of interest on own capital will be 11.10.2005, based on the data recorded in Banco Itaú S.A.

II—Intermediate and "intercalar" dividends

The value of intermediate dividends will be R$147,000, corresponding to R$0.225204 per share, and "intercalar" dividends will be R$141,000 corresponding to R$0.216012 per share.

The Company's shares will be traded "ex-dividend" as from 11.01.2005.

The date for the beginning of payment of dividends will be 11.10.2005, based on the stockholding position of 10.31.2005 and on existing data at Banco Itaú S.A.

NOTE 28—AUDIT SERVICES

The independent auditors of the Company and its subsidiaries do not render any services other than audit services.