 **TC PIPELINES, LP** is a United States limited partnership that offers investors stable cash flow and growth prospects. TC Pipelines owns a 30 percent interest in Northern Border Pipeline Company and a 49 percent interest in Tuscarora Gas Transmission Company. Both Northern Border Pipeline and Tuscarora own interstate pipeline systems that transport western Canadian natural gas to growing natural gas consuming markets in the midwestern United States and northern Nevada areas, respectively. The Partnership is managed by its general partner, TC Pipelines GP, Inc., a wholly owned subsidiary of TransCanada Corporation, a leading North American energy company.

DISCIPLINED STRATEGY



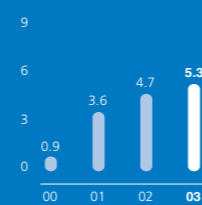
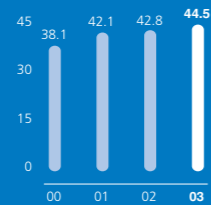


- 1 Northern Border Pipeline
- 2 Tuscarora

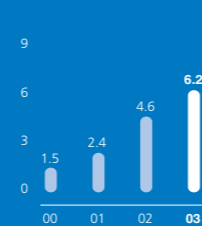
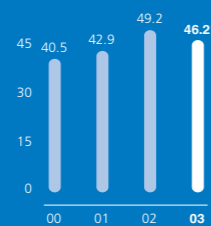
## OUR ASSETS

|   | Northern Border Pipeline | Tuscarora                |
|---|--------------------------|--------------------------|
| TC PIPELINES OWNERSHIP ACQUIRED BY TC PIPELINES | 30%<br>May 28, 1999      | 49%<br>September 1, 2000 |
| COMMENCED OPERATIONS                            | 1982                     | 1995                     |
| ORIGINATES NEAR                                 | Port of Morgan, MT       | Malin, OR                |
| TERMINATES NEAR                                 | North Hayden, IN         | Wadsworth, NV            |
| LENGTH (MILES)                                  | 1,249                    | 240                      |
| RECEIPT CAPACITY (MMcfd <sup>1</sup> )          | 2,370                    | 190                      |

### EQUITY INCOME — TC PIPELINES' SHARE (MILLIONS OF DOLLARS)



### CASH FLOW — TC PIPELINES' SHARE (MILLIONS OF DOLLARS)



<sup>1</sup> Millions of cubic feet per day.

Financial Highlights **1** Letter to Unitholders **2** Form 10-K **3** Financial Statements **F-1**

## TC PIPELINES, LP

110 Turnpike Road, Suite 203, Westborough, Massachusetts, US 01581 Telephone (508) 871-7046 Facsimile (508) 871-7047

450 – First Street SW, Calgary, Alberta, Canada T2P 5H1 Telephone (877) 290-2772 Facsimile (403) 920-2457

### BOARD OF DIRECTORS OF THE GENERAL PARTNER OF TC PIPELINES, LP

#### Albrecht W.A. Bellstedt

Executive Vice-President, Law and General Counsel  
TransCanada Corporation  
Calgary, Alberta

#### Kristine L. Delkus

Vice-President, Law, Power and Regulatory  
TransCanada Corporation  
Calgary, Alberta

#### Russell K. Girling

Executive Vice-President, Corporate Development  
and Chief Financial Officer  
TransCanada Corporation  
Calgary, Alberta

#### Robert A. Helman <sup>(2)</sup>

Partner  
Mayer, Brown, Rowe & Maw  
Chicago, Illinois

#### Jack F. Jenkins-Stark <sup>(2)</sup>

Vice-President, Business Operations and Technology  
Itron Inc.  
Alameda, California

#### David L. Marshall <sup>(1)</sup>

Retired Vice-Chairman and Chief Financial Officer  
The Brinks Company  
Incline Village, Nevada

#### Ronald J. Turner

Executive Vice-President, Gas Transmission  
TransCanada Corporation  
Calgary, Alberta

### EXECUTIVE OFFICERS OF THE GENERAL PARTNER OF TC PIPELINES, LP

#### Ronald J. Turner

President and Chief Executive Officer

#### Russell K. Girling

Chief Financial Officer

#### Steven D. Becker

Vice-President, Business Development

#### Donald R. Marchand

Vice-President and Treasurer

#### Ronald L. Cook

Vice-President, Taxation

#### Max Feldman

Vice-President

#### Wendy L. Hanrahan

Vice-President

#### Amy W. Leong

Controller

#### Maryse C. St-Laurent

Secretary

<sup>(1)</sup> Chair, Audit Committee

<sup>(2)</sup> Member, Audit Committee

**Investor Relations** Telephone (877) 290-2772 Facsimile (403) 920-2457 E-mail: investor\_relations@tcpipelineslp.com

**Internet Site** www.tcpipelineslp.com

**K-1 Information** Telephone (877) 699-1091

**Stock Exchange Listing** NASDAQ Stock Market: TCLP

**Auditors** KPMG LLP, Calgary, Alberta

**Transfer Agent** Mellon Investor Services LLC, Ridgfield Park, New Jersey Telephone (800) 756-3353

Please recycle March 2004 Printed in Canada

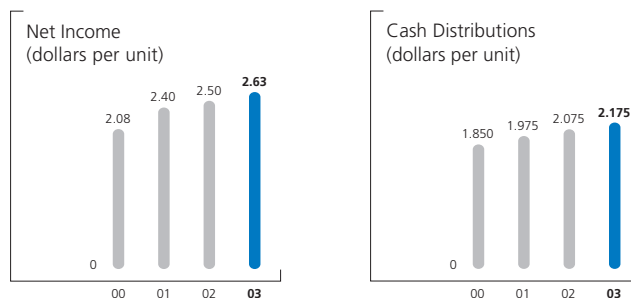
Designed and produced by smith + associates www.smithandassoc.com

**OUR GOAL** is to deliver stable, sustainable cash flows to our unitholders and to find opportunities to increase cash distributions while maintaining our low-risk profile.

**OUR STRATEGY** is to focus on natural gas transmission assets that connect supply to growing natural gas consuming markets. We focus on assets that have organic growth potential. We leverage TransCanada's expertise in the natural gas transmission industry. We are disciplined in our approach and strive to maintain a strong financial position.


## FINANCIAL HIGHLIGHTS

| Year ended December 31                         | 2003     | 2002     | 2001     | 2000     |
|--|----------|----------|----------|----------|
| (millions of dollars, except per unit amounts) |          |          |          |          |
| <b>Income Statement</b>                        |          |          |          |          |
| Net income                                     | 48.0     | 45.5     | 43.5     | 37.2     |
| Net income per unit                            | \$ 2.63  | \$ 2.50  | \$ 2.40  | \$ 2.08  |
| <b>Cash Flow</b>                               |          |          |          |          |
| Cash generated from operations                 | 49.6     | 52.1     | 42.9     | 40.3     |
| Cash distributions paid                        | 39.4     | 37.4     | 35.2     | 32.6     |
| Cash distributions declared per unit           | \$ 2.175 | \$ 2.075 | \$ 1.975 | \$ 1.850 |
| <b>Balance Sheet</b>                           |          |          |          |          |
| Total assets                                   | 288.1    | 286.0    | 288.7    | 277.5    |
| Long-term debt                                 | 5.5      | 11.5     | 21.5     | 21.5     |
| Partners' equity                               | 282.0    | 273.9    | 266.7    | 255.4    |



Common units of TC PipeLines are listed on the NASDAQ Stock Market and trade under the symbol "TCLP".

**Cautionary Statement Regarding Forward-Looking Information** This annual report includes forward-looking statements regarding future events and our future financial performance. All forward-looking statements are based on our beliefs as well as assumptions made by and information currently available to us. Words such as "believes," "expects," "intends," "forecasts," "projects," and similar expressions, identify forward-looking statements within the meaning of the Securities Litigation Reform Act. These statements reflect our current views with respect to future events and are subject to various risks, uncertainties and assumptions which we discuss in detail in our Form 10-K for the year ended December 31, 2003 and other filings made with the SEC. If one or more of these risks or uncertainties materialize, or if the underlying assumptions prove incorrect, actual results may vary materially from those described in the forward-looking statement.

 We are pleased to report that TC PipeLines has achieved another year of solid financial performance. Our success in delivering stable cash distributions to shareholders is the result of the sound business fundamentals underlying our 30% interest in Northern Border Pipeline and our 49% interest in Tuscarora Gas Transmission Company, as well as our disciplined approach to growth. TC PipeLines continues to focus on natural gas transmission assets that connect supply to growing natural gas consuming markets.

## LETTER TO UNITHOLDERS



TC PipeLines expects that North American natural gas demand will continue to grow in large part due to the needs of the power generation sector. While we see signs that the Western Canadian Sedimentary Basin is maturing, this

increase in demand together with the strong competitive position of both Northern Border Pipeline and Tuscarora makes us confident that these pipelines will continue to be attractive to shippers. This was evidenced by the successful recontracting by Northern Border Pipeline of approximately 40% of its capacity in 2003.

This successful recontracting, together with additional earnings and cash flow resulting from Tuscarora's 2002 expansion, allowed TC PipeLines to increase 2003 cash distributions paid to shareholders by almost 5%, marking our fourth distribution increase since we began operations in May 1999. In addition, we reduced debt outstanding from \$11.5 million to \$5.5 million, continuing our approach of maintaining a strong balance sheet.

Looking forward, approximately 30% of Northern Border's capacity will come up for renewal by the end of 2004, continuing a trend we see emerging of an annual recontracting process. We continue to view Northern Border Pipeline as one of the most competitive routes to transport natural gas out of Western Canada and believe that Northern Border Pipeline is well positioned to replace those expiring contracts in a manner consistent with its current toll levels. In addition, Northern Border Pipeline is making changes to its capital structure to appropriately reflect the current business environment.

As for Tuscarora, plans are underway for an expansion to meet increased demand in the Reno area. The expansion will include the addition of a new gas turbine driven compressor at Likely, California and the installation of a new reciprocating compressor at Wadsworth. The new facilities, backed by 15 year firm contracts, will add additional capacity of about 50 MMcfd and are expected to come onstream in November, 2005. This expansion follows major expansions of the Tuscarora system in both 2001 and 2002, and demonstrates the opportunity for organic growth for TC PipeLines assets.

In summary, we believe our existing assets are well positioned and are generating solid cash flows. TC PipeLines will continue to pursue opportunities to grow in a disciplined manner by expanding existing facilities or through acquisitions that create long term value for our unitholders.

*On behalf of TC PipeLines, LP*

**Ronald J. Turner**  
President and Chief Executive Officer  
TC PipeLines GP, Inc.

March 12, 2004

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549**

**F O R M 10-K**

**[X] Annual Report Pursuant to Section 13 or 15 (d) of the  
Securities Exchange Act of 1934**

For the fiscal year ended December 31, 2003

or

**[ ] Transition Report Pursuant to Section 13 or 15(d) of the  
Securities Exchange Act of 1934**

Commission file number: 000-26091

**TC PIPELINES, LP**

(Exact name of registrant as specified in its charter)

**DELAWARE**

(State or other jurisdiction  
of incorporation or organization)

**52-2135448**

(I.R.S. Employer  
Identification No.)

**110 TURNPIKE ROAD, SUITE 203**

**WESTBOROUGH, MASSACHUSETTS 01581**

(Address of principal executive offices) (zip code)

Registrant's telephone number, including area code: **508-871-7046**

**Securities registered pursuant to Section 12(b) of the Act:**

Title of each class

Name of each exchange on which registered

**NONE**

**Securities registered pursuant to Section 12(g) of the Act:**

Title of class

**COMMON UNITS REPRESENTING LIMITED PARTNER INTERESTS**

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes [X] No [ ]

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. [X]

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Act) Yes [X] No [ ]

Aggregate market value of the voting and non-voting common equity held by non-affiliates of the registrant, as at June 30, 2003, was approximately \$350.1 million.

As of February 23, 2004, there were 16,563,564 of the registrant's common units outstanding.

**TC PIPELINES, LP****TABLE OF CONTENTS**

Page No.

**PART I**

|         |   |    |
|---------|---|----|
| Item 1. | Business  | 5  |
| Item 2. | Properties  | 16 |
| Item 3. | Legal Proceedings                                   | 17 |
| Item 4. | Submission of Matters to a Vote of Security Holders | 17 |

**PART II**

|          |   |    |
|----------|---|----|
| Item 5.  | Market for Registrant's Common Units and Related Security Holder Matters              | 18 |
| Item 6.  | Selected Financial Data   | 20 |
| Item 7.  | Management's Discussion and Analysis of Financial Condition and Results of Operations | 20 |
| Item 7A. | Quantitative and Qualitative Disclosures about Market Risk                            | 45 |
| Item 8.  | Financial Statements and Supplementary Data   | 45 |
| Item 9.  | Changes in and Disagreements with Accountants on Accounting and Financial Disclosure  | 45 |
| Item 9A. | Controls and Procedures   | 45 |

**PART III**

|          |  |    |
|----------|--|----|
| Item 10. | Directors and Executive Officers of the General Partner  | 46 |
| Item 11. | Executive Compensation   | 49 |
| Item 12. | Security Ownership of Certain Beneficial Owners and Management and Related Security Holder Matters | 50 |
| Item 13. | Certain Relationships and Related Transactions   | 51 |
| Item 14. | Principal Accountants Fees and Services  | 52 |

**PART IV**

|          |   |    |
|----------|---|----|
| Item 15. | Exhibits, Financial Statement Schedules and Reports on Form 8-K | 53 |
|----------|---|----|

**All amounts are stated in United States dollars unless otherwise indicated.**

## PART I

### Item 1. Business

#### **BUSINESS OF TC PIPELINES, LP**

TC PipeLines, LP was formed in 1998 as a Delaware limited partnership to acquire, own and participate in the management of United States-based pipeline assets. TC PipeLines, LP and its subsidiary limited partnerships, TC PipeLines Intermediate Limited Partnership and TC Tuscarora Intermediate Limited Partnership are collectively referred to herein as “TC PipeLines” or “the Partnership.” TC PipeLines GP, Inc., an indirect wholly owned subsidiary of TransCanada PipeLines Limited, which is a wholly owned subsidiary of TransCanada Corporation (collectively referred to herein as TransCanada), is the general partner of the Partnership.

The Partnership owns a 30% general partner interest in Northern Border Pipeline Company. The remaining 70% general partner interest in Northern Border Pipeline is held by Northern Border Partners, L.P., a publicly traded limited partnership that is controlled by affiliates of Enron Corp. TransCanada holds a minority general partner interest in Northern Border Partners which entitles it to 12.25% of the voting power of Northern Border Pipeline.

TC PipeLines also owns a 49% general partner interest in Tuscarora Gas Transmission Company. The Partnership acquired this interest from TCPL Tuscarora Ltd., an indirect subsidiary of TransCanada, in September 2000.

At December 31, 2003, the Partnership had 16,563,564 common units outstanding, of which 11,890,694 were held by the public, 2,800,000 were held by an affiliate of the general partner and 1,872,870 were held by the general partner.

TransCanada, by virtue of its ownership of the Partnership’s general partner, holds an aggregate 2% general partner interest in the Partnership. The general partner also owns 1,872,870 common units and 936,436 subordinated units and receives incentive distributions if quarterly cash distributions on the common and subordinated units exceed levels specified in the partnership agreement (see Item 5. “Market for Registrant’s Common Units and Related Security Holder Matters”).

The Partnership’s 30% general partner interest in Northern Border Pipeline and 49% general partner interest in Tuscarora represent its only material assets.

#### **BUSINESS OF NORTHERN BORDER PIPELINE COMPANY**

##### **General**

Northern Border Pipeline Company is a general partnership formed in 1978. Northern Border Pipeline’s general partners are TC PipeLines, LP and Northern Border Partners, L.P., both of which are publicly traded partnerships. Each of TC PipeLines and Northern Border Partners holds its interest in Northern Border Pipeline, representing 30% and 70% of voting power, respectively, through a subsidiary limited partnership. The general partner of TC PipeLines and its subsidiary limited partnership, TC PipeLines GP, Inc., is an indirect subsidiary of TransCanada. The general partners of Northern Border Partners and its subsidiary limited partnership are Northern Plains Natural Gas Company (Northern Plains) and Pan Border Gas Company, both subsidiaries of Enron Corp., and Northwest Border Pipeline Company, a subsidiary of TransCanada.

Northern Border Pipeline owns an interstate pipeline system that transports natural gas from the Montana-Saskatchewan border to natural gas markets in the midwestern United States. This pipeline system connects with multiple pipelines that provide shippers with access to the various natural gas markets served by those pipelines. TC PipeLines estimates that, in the year ended December 31, 2003, Northern Border Pipeline transported

approximately 22% of the total amount of natural gas imported from Canada to the United States. Over the same period, approximately 88% of the natural gas transported was produced in the Western Canadian Sedimentary Basin located in the provinces of Alberta, British Columbia and Saskatchewan.

Northern Border Pipeline transports gas for shippers under a tariff regulated by the Federal Energy Regulatory Commission (FERC). The tariff specifies the maximum and minimum transportation rates and the general terms and conditions of transportation service on the pipeline system. Northern Border Pipeline's revenues are derived from agreements for the receipt and delivery of gas at points along the pipeline system as specified in each shipper's individual transportation contract. Northern Border Pipeline does not own the gas that it transports, and therefore it does not assume natural gas commodity price risk for quantities transported. Any exposure to commodity risk for imbalances on Northern Border Pipeline's system that may result from under or over deliveries to customers or interconnecting pipelines is either recovered through provisions in Northern Border Pipeline's tariff or is immaterial. Northern Border Pipeline owns the line pack, which is the amount of gas necessary to maintain efficient operations of the pipeline. Northern Border Pipeline's shippers are responsible to provide fuel gas necessary for the operation of gas compressor stations.

Northern Border Pipeline's management is overseen by a four-member management committee. Three representatives are designated by Northern Border Partners, with each of its general partners selecting one representative and one representative is designated by TC PipeLines. Voting power on the management committee is allocated among Northern Border Partners' three representatives in proportion to their general partner interests in Northern Border Partners. As a result, the 70% voting power of Northern Border Partners' three representatives on the management committee is allocated as follows: 35% to the representative designated by Northern Plains, 22.75% to the representative designated by Pan Border and 12.25% to the representative designated by Northwest Border. Northern Plains and Pan Border are subsidiaries of Enron. Therefore, Enron controls 57.75% of the voting power of the management committee and has the right to select two of the members. On December 2, 2001, Enron filed a voluntary petition for Chapter 11 protection in bankruptcy court. On September 25, 2003, a motion by Enron to transfer Enron's interests in, among other entities, Northern Plains and Pan Border to CrossCountry Energy, a new pipeline operating entity, was approved. See Item 7. "Management's Discussion and Analysis of Financial Condition and Results of Operations – Results of Operations of Northern Border Pipeline Company – The Impact Of Enron's Chapter 11 Filing On Northern Border Pipeline's Business."

The Northern Border pipeline system is operated by Northern Plains pursuant to an operating agreement. As of December 31, 2003, Northern Plains employed approximately 216 individuals located at its headquarters in Omaha, Nebraska and at various locations along the pipeline route and also used employees and information technology systems of its affiliates to provide its services. Northern Plains' employees are not represented by any labor union and are not covered by any collective bargaining agreements.

#### **The Northern Border Pipeline System**

Northern Border Pipeline owns a 1,249-mile interstate pipeline system that transports natural gas from the Montana-Saskatchewan border near Port of Morgan, Montana to natural gas markets in the midwestern United States. Construction of the pipeline was initially completed in 1982. The Northern Border pipeline system was expanded and/or extended in 1991, 1992, 1998 and 2001. The Northern Border pipeline system connects directly and through multiple pipelines to various natural gas markets in the United States.

The Northern Border pipeline system consists of 822 miles of 42-inch diameter pipe from the Canadian border to Ventura, Iowa capable of transporting a total of 2,374 million cubic feet per day (mmcf); 30-inch diameter pipe and 36-inch diameter pipe, each approximately 147 miles in length, capable of transporting 1,484 mmcf in total from Ventura, Iowa to Harper, Iowa; 226 miles of 36-inch diameter pipe and 19 miles of 30-inch diameter pipe capable of transporting 844 mmcf from Harper, Iowa to Manhattan, Illinois (Chicago area); and 35 miles of 30-inch diameter



pipe capable of transporting 545 mmcf from Manhattan, Illinois to a terminus near North Hayden, Indiana. Along the pipeline there are 16 compressor stations with total rated horsepower of 499,000 and measurement facilities to support the receipt and delivery of gas at various points. Other facilities include four field offices and a microwave communication system with 50 tower sites.

The Northern Border pipeline system has pipeline access to natural gas reserves in the Western Canadian Sedimentary Basin in the provinces of Alberta, British Columbia and Saskatchewan in Canada, domestic natural gas produced within the Williston Basin and synthetic gas produced at the Dakota Gasification plant in North Dakota. In addition, the pipeline is capable of physically receiving natural gas at two locations near Chicago. At its northern end, the pipeline system's gas supplies are received through an interconnection with Foothills Pipe Lines (Sask.) Ltd. system in Canada. The Foothills system, owned by TransCanada, is connected to TransCanada's Alberta system and the pipeline system owned by Transgas Limited in Saskatchewan. Also at the north end, the pipeline system connects to a domestic natural gas gathering system owned by Omimex Ltd. Corporation. In North Dakota, the Northern Border pipeline system connects with facilities of Northern Natural Gas Company at Buford, which facilities in turn are connected to Williston Basin Interstate Pipeline and the gathering system owned by Bear Paw Energy, LLC, a wholly owned subsidiary of Northern Border Partners. In December 2003, an interconnection with a newly constructed pipeline owned by Williston Basin Interstate Pipeline near Manning, North Dakota was placed in service. The initial design capacity of the interconnect facilities is 200 mmcf. The pipeline, with an initial design capacity of 80 mmcf, was constructed to transport natural gas from coal bed and conventional natural gas supplies in the Powder River Basin of northeastern Wyoming and southeastern Montana as well as conventional supplies in the Rocky Mountain area. Other locations in North Dakota where Northern Border Pipeline can receive gas are interconnections with Williston Basin Interstate Pipeline at Glen Ullin and Amerada Hess Corporation at Watford City and facilities of Dakota Gasification Company at Hebron. Near its terminus, the pipeline system is capable of physically receiving natural gas from Northern Illinois Gas Company at Troy Grove, Illinois and from Midwestern Gas Transmission Company, a wholly owned subsidiary of Northern Border Partners, at Channahon, Illinois. For the year ended December 31, 2003, of the natural gas transported on the Northern Border pipeline system, approximately 88% was produced in Canada, approximately 5% was produced by the Dakota Gasification plant and approximately 6% was produced in the Williston Basin and 1% from other sources.

### **Interconnects**

The Northern Border pipeline system connects with multiple pipelines of various interstate, intrastate and local distribution companies, as well as with end-users. These interconnects provide its shippers with access to the various natural gas markets served by those pipelines. The larger interconnections are with the pipeline facilities of:

- Northern Natural Gas Company at Ventura, Iowa as well as multiple smaller interconnections in South Dakota, Minnesota and Iowa;
- Natural Gas Pipeline Company of America at Harper, Iowa;
- MidAmerican Energy Company at Iowa City and Davenport, Iowa and Cordova, Illinois;
- Alliant Power Company at Prophetstown, Illinois;
- Northern Illinois Gas Company at Troy Grove and Minooka, Illinois;
- Midwestern Gas Transmission Company near Channahon, Illinois;
- ANR Pipeline Company near Manhattan, Illinois;
- Vector Pipeline L.P. in Will County, Illinois;
- Guardian Pipeline, L.L.C., an affiliate of Northern Border Partners, in Will County, Illinois;
- The Peoples Gas Light and Coke Company near Manhattan, Illinois; and
- Northern Indiana Public Service Company near North Hayden, Indiana at the terminus of the pipeline system.

Several market centers, where natural gas transported on the Northern Border pipeline system is sold, traded and received for transport to significant consuming markets in the Midwest and to interconnecting pipeline facilities, have developed on the Northern Border pipeline system. The largest of these market centers is at the Ventura, Iowa

connection with Northern Natural Gas Company. Two other market center locations are the Harper, Iowa connection with Natural Gas Pipeline Company of America and the multiple interconnects in the Chicago area that include connections with Northern Illinois Gas Company, The Peoples Gas Light and Coke Company and Northern Indiana Public Service Company, as well as four interstate pipelines.

### **Shippers**

The Northern Border pipeline system serves more than 40 firm transportation shippers with diverse operating and financial profiles. Based upon shippers' contractual obligations, as of December 31, 2003, 94% of the firm capacity is contracted by producers and marketers. The remaining firm capacity is contracted primarily by local distribution companies (5%), and interstate pipelines (1%). As of December 31, 2003, the termination dates of these contracts ranged from March 31, 2004 to December 21, 2013, and the weighted average contract life, based upon contractual obligations, was approximately three and one-third years. All of Northern Border Pipeline's capacity was under contract through December 31, 2003 and, assuming no extensions of existing contracts or execution of new contracts, approximately 70% and 59% is under contract through December 31, 2004 and 2005 respectively. See Item 7. "Management's Discussion and Analysis of Financial Condition and Results of Operations – Results of Operations of Northern Border Pipeline Company – Overview."

Northern Border Pipeline's shippers may change throughout the year as a result of its shippers utilizing Northern Border Pipeline's capacity release provisions that allow them to release all or part of their capacity to other shippers, either permanently for the full term of their contract or temporarily. Under the terms of Northern Border Pipeline's tariff, a temporary capacity release does not relieve the original contract shipper from its payment obligations if the replacement shipper fails to pay.

For the year ended December 31, 2003, BP Canada Energy Marketing Corp. (BP Canada), EnCana Marketing U.S.A. Inc. (EnCana), and Pan Alberta Gas (U.S.) Inc. (Pan-Alberta) collectively accounted for approximately 41% of Northern Border Pipeline's revenues. As of December 31, 2003, Northern Border Pipeline's three largest shippers were BP Canada, EnCana and Cargill Incorporated who are obligated for approximately 21%, 19% and 9%, respectively, of the contracted firm capacity. In July 2003, Cargill Incorporated completed the assignment of all the firm capacity formerly held by Mirant Americas Energy Marketing, LP, which extends for terms into 2006 and 2008. Approximately half of the capacity contracted to BP Canada and EnCana is due to expire by November 1, 2004. During 2003, all of the contracted capacity due to expire by November 1, 2003, of which Pan-Alberta held approximately 20% was recontracted with 10 shippers. See Item 7. "Management's Discussion and Analysis of Financial Condition and Results of Operations – Results of Operations of Northern Border Pipeline Company – Overview."

### **Demand for Transportation Capacity**

Northern Border Pipeline's long-term financial condition is dependent on the continued availability of economic western Canadian natural gas supplies for import into the United States. Natural gas reserves may require significant capital expenditures by others for exploration and development drilling and the installation of production, gathering, storage, transportation and other facilities that permit natural gas to be produced and delivered to pipelines that interconnect with the interstate pipelines' systems. Prices for natural gas, the currency exchange rate between Canada and the United States, regulatory limitations or the lack of available capital for these projects could adversely affect the development of additional reserves and production, gathering, storage and pipeline transmission of western Canadian natural gas supplies. Increased Canadian consumption of natural gas related to the extraction process for oil sands projects as well as restrictions on gas production to protect oil sand reserves could also impact supplies of natural gas for export. Additional pipeline export capacity also could accelerate depletion of these reserves. Furthermore, the availability of export capacity could also affect the demand or value of the transport on the Northern Border pipeline system.

Northern Border Pipeline's business also depends on the level of demand for natural gas in the markets the Northern Border pipeline system serves. The volumes of natural gas delivered to these markets from other sources affect the

demand for both the natural gas supplies and the use of the Northern Border pipeline system. Demand for natural gas to serve other markets also influences the ability and willingness of shippers to use the Northern Border pipeline system to meet demand in the markets that it serves.

A variety of factors could affect the demand for natural gas in the markets that the Northern Border pipeline system serves. These factors include:

- economic conditions;
- fuel conservation measures;
- alternative energy requirements and prices;
- gas storage inventory levels;
- climatic conditions;
- government regulation; and
- technological advances in fuel economy and energy generation devices.

Interstate pipelines' primary exposure to market risk occurs at the time existing transportation contracts expire and are subject to renegotiation. A key determinant of the value that customers can realize from firm transportation on a pipeline is the basis differential, or market price spread, between two points on the pipeline. The difference in natural gas prices between the points along the pipeline where gas enters and where gas is delivered represents the gross margin that a customer can expect to achieve from holding transportation capacity at any point in time. This margin and its variability become important factors in determining the transportation rate customers are willing to pay when they renegotiate their transportation contracts. The basis differential between markets can be affected by trends in production, available capacity, storage inventories, weather and general market demand in the respective areas.

Throughput on the Northern Border pipeline system may experience seasonal fluctuations depending upon the level of winter heating load demand or summer electric generation usage in the markets it serves. However, since approximately 98% of Northern Border Pipeline's expected revenue is attributable to demand charges, Northern Border Pipeline's revenues and cash flows are not impacted materially by such seasonal throughput variations.

TC PipeLines cannot predict whether these or other factors will have an adverse effect on demand for use of the Northern Border pipeline system or how significant such adverse effect could be.

### **Interstate Pipeline Competition**

Northern Border Pipeline competes with other pipeline companies that transport natural gas from the Western Canadian Sedimentary Basin or that transport natural gas to end-use markets in the midwest. Northern Border Pipeline's competitive position is affected by the availability of Canadian natural gas for export, the availability of other sources of natural gas and demand for natural gas in the United States. Demand for transportation services on the Northern Border pipeline system is affected by natural gas prices, the relationship between export capacity from and production in the Western Canadian Sedimentary Basin and natural gas shipped from producing areas in the United States. Shippers of natural gas produced in the Western Canadian Sedimentary Basin also have other options to transport Canadian natural gas to the United States, including transportation on the Alliance Pipeline, on TransCanada's pipeline system through various interconnects with U.S. interstate pipelines, including Viking Gas Transmission Company which is owned by Northern Border Partners, or to markets on the West Coast.

The Alliance Pipeline competes directly with Northern Border Pipeline in the transportation of natural gas from the Western Canadian Sedimentary Basin to the Chicago area. Because it transports liquids-rich natural gas, the Alliance Pipeline has no interconnections with other pipelines upstream of liquids extraction facilities located near Chicago. This contrasts with the Northern Border pipeline system, which serves various markets through interconnections with other pipelines along its route. The Chicago market hub has absorbed the new supply from Alliance Pipeline as incremental pipeline capacity has been developed to transport natural gas from the Chicago area to other market regions.

In addition, Northern Border Pipeline competes in its markets with other interstate pipelines that provide access to other supply basins. Northern Border Pipeline's major deliveries into Northern Natural Gas at Ventura, Iowa compete with gas supplied from the Rockies, and mid-continent regions. Northern Border Pipeline also competes with these supply basins at its delivery interconnect with Natural Gas Pipeline at Harper, Iowa. In the Chicago area, Northern Border Pipeline competes with many interstate pipelines that transport gas from the Gulf Coast, mid-continent, Rockies and western Canada.

### **FERC Regulation**

Northern Border Pipeline is subject to extensive regulation by the FERC as a "natural gas company" under the Natural Gas Act. Under the Natural Gas Act and the Natural Gas Policy Act, the FERC has jurisdiction with respect to virtually all aspects of Northern Border Pipeline's business, including:

- transportation of natural gas;
- rates and charges;
- construction of new facilities;
- extension or abandonment of service and facilities;
- accounts and records;
- depreciation and amortization policies;
- the acquisition and disposition of facilities; and
- the initiation and discontinuation of services.

Where required, Northern Border Pipeline holds certificates of public convenience and necessity issued by the FERC covering its facilities, activities and services. Under Section 8 of the Natural Gas Act, the FERC has the power to prescribe the accounting treatment for items for regulatory purposes. Northern Border Pipeline's books and records may be periodically audited by the FERC under Section 8. Northern Border Pipeline was notified in November 2002 that it was one of the companies selected by the FERC to undergo an industry-wide audit of FERC-assessed annual charges. The overall audit objective was to determine compliance with FERC accounting requirements and regulations as they relate to the calculation and assessment of annual charges by validating the accuracy of the data filed annually with the FERC. The audit covered the period of January 1, 2001 to December 31, 2001. On April 10, 2003, the FERC issued its final report that found Northern Border Pipeline was in compliance.

The FERC regulates the rates and charges for transportation in interstate commerce. Natural gas companies may not charge rates exceeding rates judged just and reasonable by the FERC. Generally, rates are based on the cost of service including recovery of and a return on the pipeline's actual historical cost investment. In addition, the FERC prohibits natural gas companies from unduly preferring or unreasonably discriminating against any person with respect to pipeline rates or terms and conditions of service. Some types of rates may be discounted without further FERC authorization and rates may be negotiated subject to FERC approval. The rates and terms and conditions for Northern Border Pipeline's service are found in its FERC approved tariff.

Transportation rates are established periodically in FERC proceedings known as rate cases. Under Northern Border Pipeline's tariff, Northern Border Pipeline is allowed to charge for its services on the basis of stated transportation rates established in its 1999 rate case. Northern Border Pipeline may also provide services under negotiated and discounted rates. Firm shippers that contract for the stated transportation rate are obligated to pay a monthly demand charge, regardless of the amount of natural gas they actually transport, for the term of their contracts. Approximately 98% of the revenue generated is attributed to demand charges. The remaining 2% of the agreed upon revenue level is attributed to commodity charges based on the volumes of gas actually transported.

Under the terms of settlement in Northern Border Pipeline's 1999 rate case, neither Northern Border Pipeline's existing shippers nor Northern Border Pipeline can seek rate changes until November 1, 2005, at which time Northern Border

Pipeline must file a rate case. Prior to this rate case, Northern Border Pipeline will not be permitted to increase rates if costs increase, nor will Northern Border Pipeline be required to reduce rates based on cost savings. As a result, Northern Border Pipeline's earnings and cash flow will depend on future costs, contracted capacity, the volumes of gas transported and its ability to recontract capacity at acceptable rates.

Until new depreciation rates are approved by FERC, Northern Border Pipeline continues to depreciate its transmission plant at the FERC approved annual depreciation rate. Northern Border Pipeline's annual depreciation rate on transmission plant in service is 2.25%. In order to avoid a decline in transportation rates set in future rate cases as a result of accumulated depreciation, Northern Border Pipeline must maintain or increase its rate base by acquiring or constructing assets that replace or add to existing pipeline facilities or by adding new facilities.

In Northern Border Pipeline's 1995 rate case, the FERC addressed the issue of whether the federal income tax allowance included in Northern Border Pipeline's proposed cost of service was reasonable in light of previous FERC rulings. In those rulings, the FERC held that an interstate pipeline is not entitled to a tax allowance for income attributable to limited partnership interests held by individuals. The settlement of Northern Border Pipeline's 1995 rate case provided that until at least December 2005, Northern Border Pipeline could continue to calculate the allowance for income taxes in the manner it had historically used. In addition, a settlement adjustment mechanism was implemented, which effectively reduced the return on rate base. These provisions of the 1995 rate case were maintained in the settlement of Northern Border Pipeline's 1999 rate case.

Northern Border Pipeline also provides interruptible transportation service. Interruptible transportation service is transportation in circumstances when capacity is available after satisfying firm service requests. The maximum rate that may be charged to interruptible shippers is the sum of the firm transportation maximum demand and commodity charges. From the settlement of its 1999 rate case through October 31, 2003, Northern Border Pipeline shared net interruptible transportation service revenue and any new services revenue on an equal basis with its firm shippers, however, Northern Border Pipeline was permitted to retain revenue from interruptible transportation service to offset any decontracted firm capacity. Beginning November 1, 2003, Northern Border Pipeline retains all revenues from these services.

Northern Border Pipeline is subject to the requirements of FERC Order Nos. 497 and 566, which prohibit preferential treatment by interstate natural gas pipelines of their marketing affiliates and govern how information may be provided to those marketing affiliates. On November 25, 2003, the FERC issued a final rule, Order No. 2004, adopting new standards of conduct for transmission providers when dealing with their energy affiliates. All transmission providers must comply with the standards of conduct by June 1, 2004. The standards of conduct are designed to prevent transmission providers from giving undue preferences to any of their energy affiliates. The final rule generally requires that transmission function employees operate independently of the marketing function employees and energy affiliates. As required of all transmission providers, Northern Border Pipeline posted a compliance plan to its website on February 9, 2004. By definition, two of Northern Border Pipeline's energy affiliates are Bear Paw Energy, LLC and Crestone Energy L.L.C., both of which are gathering companies owned by Northern Border Partners. Northern Border Pipeline's operator, Northern Plains, provides after hours and weekend gas control services for Bear Paw and Crestone that results in some cost savings to Northern Border Pipeline. Northern Border Pipeline has requested a waiver to permit Northern Plains to continue to provide after hours and weekend gas control services for Bear Paw Energy and Crestone. If the waiver is not granted, the cost to maintain gas control for Northern border Pipeline will increase slightly. Several parties have filed for rehearing on a number of issues, including whether gathering companies should be included in the definition of energy affiliate.

On August 1, 2002, the FERC issued a Notice of Proposed Rulemaking regarding the regulation of cash management practices of the natural gas and other companies that it regulates. On June 26, 2003, the FERC issued an interim rule in that proceeding that amended the FERC's regulations to provide for documentation requirements for cash management programs and to implement new reporting requirements. Specifically, under the interim rule, all cash

management agreements between regulated entities and their affiliates must be in writing, must specify the duties and responsibilities of cash management participants and administrators, must specify the methods for calculating interest and for allocating interest income and expense, and must specify any restrictions on deposits or borrowings by participants. A FERC-regulated entity must file with the FERC any cash management agreements to which it is a party, as well as any subsequent changes to such agreements. In addition, a FERC-regulated entity must notify the FERC when its equity component of proprietary capital ratio falls below 30%. Northern Border Pipeline does not have a cash management agreement nor is Northern Border Pipeline required to have one and the FERC was notified. Northern Border Pipeline advises that it does not expect that the FERC policy will have an impact on Northern Border Pipeline's cash management practices.

On July 17, 2002, the FERC issued a Notice of Inquiry Concerning Natural Gas Pipeline Negotiated Rate Policies and Practices. Subsequently, the FERC issued an order on July 25, 2003, modifying its prior policy on negotiated rates. The FERC ruled that it would no longer permit the pricing of negotiated rates based upon natural gas commodity price indices. Negotiated rates based upon such indices may continue until the end of the contract period for which such rates were negotiated, but such rates will not be prospectively approved by FERC. FERC also imposed certain requirements on other types of negotiated rate transactions to ensure that the agreements embodying such transactions do not materially differ from the terms and conditions set forth in the tariff of the pipeline entering into the transaction. Since Northern Border Pipeline's business does not derive a significant amount of its revenues from negotiated rate transactions, Northern Border Pipeline advises that it does not expect this FERC ruling to have a material effect on its business.

Recent FERC orders in proceedings involving other natural gas pipelines have addressed certain aspects of the pipelines' creditworthiness provisions set forth in their tariffs. In addition, industry groups, such as the North American Energy Standards Board (NAESB), are studying creditworthiness standards. On February 12, 2004, FERC issued a Notice of Proposed Rulemaking to require interstate pipelines to follow standardized procedures for determining the creditworthiness of their shippers. The proposed rule would incorporate by reference ten consensus standards passed within NAESB and would adopt additional standards requiring, among other things, standardization of information shippers provide to establish credit, collateral requirements for service, procedures for suspension and termination for non-creditworthy shippers and procedures governing capacity release transactions. Comments are due on the proposed rule by March 26, 2004. Recent FERC orders, and this proposed rule, support greater collateral requirements for credit on shippers for the construction of new facilities by a pipeline. The enactment of some of these standards may have the effect of easing certain creditworthiness requirements and parameters currently reflected in Northern Border Pipeline's tariff. Recent FERC orders have indicated, however, that pipelines are free to negotiate credit terms relative to the construction of new facilities by a pipeline, which are then effective for the term of the contract and are not superseded by tariff provisions once the facilities are completed. Northern Border Pipeline advises that, at this time, it cannot predict the ultimate impact, if any, on Northern Border Pipeline of any resulting final rule.

In February 2004, the FERC adopted new quarterly financial reporting requirements and accelerated the filing date for interstate pipeline's annual financial report. The quarterly reports will include a basic set of financial statements and other selected data and will be submitted electronically. For 2004, each quarterly report will be due approximately 70 days following the end of the quarter except for the first quarter report which is due on or before July 9, 2004. Subsequent reports will be due 60 days after the end of each quarter. The annual report, previously required to be filed each year on or before April 30, will be required on or before April 25, 2005 for 2004 and on April 18 thereafter. Northern Border Pipeline advises that it does not anticipate any impact for complying with these requirements other than the time and additional expenses for preparation of these reports.

From time to time, Northern Border Pipeline files to make changes to its tariff to clarify provisions, to reflect current industry practices and to reflect recent FERC rulings. In February 2003, Northern Border Pipeline filed to amend the definition of company use gas, which is gas supplied by Northern Border Pipeline's shippers for the operation of its compressor stations, to clarify the language by adding detail to the broad categories that comprise company use gas.

However, in its March 2003 order, the FERC directed Northern Border Pipeline to cease collecting electric costs through its company use gas provisions and to refund with interest, within 90 days, all electric costs that had been collected through the company use gas provisions. Refunds of approximately \$10.0 million were made in May 2003.

In August 2003 Northern Border Pipeline filed revised tariff sheets to clarify its procedures for the awarding of capacity. Several parties protested the filing. One party requested a show cause proceeding to examine past tariff practices alleging that Northern Border Pipeline had violated its tariff by denying a service request that would have involved a short distance for less than one year. On September 10, 2003, the FERC rejected Northern Border Pipeline's tariff sheets based upon the conclusion that certain aspects of the proposal were not in accordance with Commission policy. The FERC did affirm that, up to ninety days prior to the effective date, Northern Border Pipeline had the right not to sell capacity requested for short distances or on a short-term basis. Northern Border Pipeline filed a timely request for rehearing of the Commission's Order in October 2003 which is still pending. Northern Border Pipeline also filed responses to requests for further information on the award of capacity in the summer of 2003. Northern Border Pipeline filed its compliance tariff sheets in early December 2003 and is awaiting a Commission decision on these tariff sheets. Northern Border Pipeline's tariff sheets and the final orders to be entered in this proceeding will impact how Northern Border Pipeline awards available capacity. With contracts expiring before November 1, 2004, if timely bids for one year of service or longer on the entire transportation path available are not received, Northern Border Pipeline advises that it may potentially be required to accept bids for shorter distances that may result in creating segments of capacity of minimal value.

In March 2004, Northern Border Pipeline filed tariff sheets to implement two balancing services to assist deliveries at variable load points, such as electrical generation plant. Northern Border Pipeline also filed with the FERC certain agreements for third party balancing which it believes are administrative in nature and which will be terminated upon approval of the new balancing services. Under current orders and rulings in other proceedings before the FERC, it is unclear whether these agreements would be deemed non-conforming. However, Northern Border Pipeline advises that it does not expect that orders on these tariff sheets and agreements will have a material adverse impact on its business.

#### **Environmental and Safety Matters**

Northern Border Pipeline's operations are subject to federal, state and local laws and regulations relating to safety and the protection of the environment, which include the Resource Conservation and Recovery Act, the Comprehensive Environmental Response, Compensation and Liability Act of 1980, as amended, Clean Air Act, as amended, the Clean Water Act, as amended, the Natural Gas Pipeline Safety Act of 1969, as amended, the Pipeline Safety Act of 1992 and the Pipeline Safety Improvement Act of 2002.

The Pipeline Safety Improvement Act (Act) of 2002 was signed into law in December 2002, providing guidelines for interstate pipelines in the areas of risk analysis and integrity management, public education programs, verification of operator qualification programs and filings with the National Pipeline Mapping System. The Act requires pipeline companies to perform integrity assessments on pipeline segments that exist in high population density areas or near specifically identified sites that are designated as high consequence areas. Pipeline companies are required to perform the integrity assessments within ten years of the date of enactment and must perform subsequent integrity assessments on a seven-year cycle. At least 50% of the highest risk segments must be assessed within five years of the enactment date. In addition, within one year of enactment, the pipeline's operator qualification programs, in force since the mandatory compliance date of October 2002, must also conform to standards provided by the Department of Transportation. The regulations implementing the Act are not yet final. Rules on integrity management, direct assessment usage, and the operator qualification standards have been issued. Northern Border Pipeline has made the required filings with the National Pipeline Mapping System and has reviewed and revised its public education program. Compliance with the Act is expected to increase Northern Border Pipeline's operating costs particularly related to integrity assessments for its interstate pipeline. As required, Northern Border Pipeline has developed an overall plan for pipeline integrity

management. Detailed analysis is being performed to determine the priorities and costs for inspecting and testing its pipeline. However, the plan will be modified as a result of the findings noted and could result in additional assessment or remediation costs. Although TC PipeLines expects Northern Border Pipeline to include these costs in future rate case filings, total recovery is not assured. Northern Border Pipeline advises that, presently, it expects its costs for 2004 for integrity management to be approximately \$0.5 million.

TC PipeLines believes that Northern Border Pipeline's operations and facilities are in general compliance in all material respects with applicable environmental and safety regulations, however, risks of substantial costs and liabilities are inherent in pipeline operations, and TC PipeLines cannot provide any assurances that Northern Border Pipeline will not incur such costs and liabilities. Moreover, it is possible that other developments, such as the enactment of increasingly strict environmental and safety laws, regulations and enforcement policies by Congress, the FERC, the Department of Transportation and other federal agencies, state regulatory bodies and the courts, and claims for damages to property or persons resulting from Northern Border Pipeline's operations, could result in substantial costs and liabilities to Northern Border Pipeline. If Northern Border Pipeline is unable to recover such resulting costs, earnings and cash distributions could be adversely affected.

#### **BUSINESS OF TUSCARORA GAS TRANSMISSION COMPANY**

Tuscarora is a Nevada general partnership formed in 1993. Its general partners are TC Tuscarora Intermediate Limited Partnership, a direct subsidiary of TC PipeLines, which holds a 49% general partner interest, Tuscarora Gas Pipeline Co., a wholly owned subsidiary of Sierra Pacific Resources, which holds a 50% general partner interest and TCPL Tuscarora Ltd., an indirect wholly owned subsidiary of TransCanada, which holds a 1% general partner interest.

The management of Tuscarora is overseen by a management committee that determines the policies of, has authority over the affairs of, and approves the actions of Tuscarora. The management committee participates in the management of the construction, maintenance and operation of the Tuscarora pipeline system.

Under the Tuscarora partnership agreement, voting control is allocated among Tuscarora's three general partners in proportion to their general partner interests in Tuscarora. As a result, TC PipeLines has a 49% voting interest, Sierra Pacific Resources has a 50% voting interest, and TransCanada has a 1% voting interest on the Tuscarora management committee. Tuscarora Gas Operating Company, a subsidiary of Sierra Pacific Resources, operates the Tuscarora pipeline system pursuant to an operating agreement. Effective December 1, 2002, TransCanada is under contract to provide gas control services for the Tuscarora pipeline system, including monitoring and control of the compressor units, as well as emergency call out functions and other operational co-ordination.

#### **The Tuscarora Pipeline System**

Tuscarora owns a 240-mile, 20-inch diameter, United States interstate pipeline system that originates at an interconnection point with facilities of Gas Transmission Northwest Corporation (GTN) near Malin, Oregon and runs southeast through northeastern California and northwestern Nevada. The Tuscarora pipeline system terminates near Wadsworth, Nevada. Deliveries are also made directly to the local gas distribution system of Sierra Pacific Power Company, a subsidiary of Sierra Pacific Resources. Along its route, deliveries are made in Oregon, northern California and northwestern Nevada.

The Tuscarora pipeline system was constructed in 1995 and was placed into service in December 1995. The Tuscarora pipeline system has firm capacity contracts to transport approximately 180 mmcf/d of natural gas.

On December 1, 2002, Tuscarora completed and placed into service an expansion of its pipeline system. This expansion consisted of two compressor stations and an 11-mile pipeline extension from the previous terminus of the Tuscarora pipeline system near Reno, Nevada to Wadsworth, Nevada. The expansion increased Tuscarora's contracted capacity from 127 mmcf/d to approximately 180 mmcf/d. The new capacity was contracted under long-term firm transportation



contracts ranging from ten to fifteen years from the in-service date. Sierra Pacific Power had contracted for approximately 11 mmcf of the expansion capacity. The project had a capital budget of approximately \$43.0 million and was completed at a capital cost of approximately \$39.0 million. At the request of the Public Utilities Commission of Nevada, Tuscarora will submit a cost and revenue study to the FERC within 3 years of the in-service date of the expansion.

Tuscarora has firm transportation contracts for over 94% of its capacity, including contracts held by Sierra Pacific Power for 68.1% of the total available capacity, the majority of which expires on November 30, 2015. As of December 31, 2003, the weighted average contract life on the Tuscarora pipeline system was approximately 11.5 years.

In June 2003, Tuscarora held an open season to determine the demand for incremental firm capacity by winter 2005. The open season resulted in the execution of firm transportation service agreements for a net increase of approximately 50 mmcf. Tuscarora has begun preliminary planning activities for construction of additional facilities to meet the additional capacity requirements. Tuscarora has advised that it anticipates that an application for a Certificate of Public Convenience and Necessity for authorization to construct and operate the new pipeline facilities, will be filed with the FERC by the second quarter 2004. Construction of the project is anticipated to commence in late spring of 2005, with newly commissioned facilities on line by November 1, 2005. Total capital cost is estimated to be approximately \$16.6 million. This expansion project will increase Tuscarora's contracted capacity by approximately 28%.

Tuscarora's competitive position is dependent on the continued availability of commercially attractive western Canadian natural gas for import into the United States and on the level of demand for western Canadian natural gas in the markets the Tuscarora pipeline system serves. Shippers of natural gas from the Western Canadian Sedimentary Basin have other options for transporting Canadian natural gas to the United States, including transportation on pipelines eastward in Canada or to markets on the west coast of the United States and Canada. Similarly, natural gas produced in the United States serves the same markets as Tuscarora in northern Nevada. Tuscarora is able to transport both Canadian and United States natural gas, providing Tuscarora with a well-diversified supply of natural gas to serve its markets.

#### **FERC Regulation**

Tuscarora is subject to regulation by the FERC as a "natural gas company" under the Natural Gas Act, and is subject to the FERC's rules, regulations and accounting procedures.

Tuscarora generates revenues from individual transportation contracts with shippers that provide for the receipt and delivery of natural gas at points along the Tuscarora pipeline system. Tuscarora's transportation rates are based on its cost of service as approved by the FERC. Tuscarora's cost of service includes administrative and operating costs, depreciation and amortization, taxes other than income taxes, an allowance for income taxes and a regulated return on capital employed.

On November 25, 2003, the FERC issued a final rule, Order No. 2004, adopting new standards of conduct for transmission providers when dealing with their energy affiliates. All transmission providers must comply with the standards of conduct by June 1, 2004. The standards of conduct are designed to prevent transmission providers from giving undue preferences to any of their energy affiliates. The final rule generally requires that transmission function employees operate independently of the marketing function employees and energy affiliates. Tuscarora advises that it will be in compliance with these new standards by June 1, 2004.

In February 2004, the FERC amended its financial reporting regulations to establish new quarterly financial reporting requirements. The reports will include a basic set of financial statements and other selected data and will be submitted electronically. The first report for Tuscarora will be due on or before July 23, 2004. Tuscarora advises that it does not anticipate any impact from complying with these requirements other than the time and additional expenses for preparation of these reports.

### **Environmental and Safety Matters**

Tuscarora's operations are subject to federal, state and local laws and regulations relating to safety and protection of the environment. TC PipeLines believes that Tuscarora's operations and facilities comply in all material respects with applicable United States environmental and safety regulations.

### **Available Information**

The Partnership's annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and any amendments to these reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act are made available free of charge on the Partnership's website at [www.tcpipelineslp.com/investor/reports.htm](http://www.tcpipelineslp.com/investor/reports.htm) as soon as reasonably practicable after the Partnership electronically files these materials with, or furnishes them to, the Securities and Exchange Commission (SEC).

## **Item 2. Properties**

TC PipeLines does not hold the right, title or interest in any properties.

### **Properties of Northern Border Pipeline Company**

Northern Border Pipeline holds the right, title and interest in its pipeline system. With respect to real property, the pipeline system falls into two basic categories: (a) parcels which are owned in fee, such as sites for compressor stations, meter stations, pipeline field offices, and microwave towers; and (b) parcels where the interest derives from leases, easements, rights-of-way, permits or licenses from landowners or governmental authorities permitting the use of such land for the construction and operation of the pipeline system. The right to construct and operate the pipeline system across certain property was obtained through exercise of the power of eminent domain. Northern Border Pipeline continues to have the power of eminent domain in each of the states in which it operates, although Northern Border Pipeline may not have the power of eminent domain with respect to Native American tribal lands.

Approximately 90 miles of the Northern Border pipeline system is located on fee, allotted and tribal lands within the exterior boundaries of the Fort Peck Indian Reservation in Montana. Tribal lands are lands owned in trust by the United States for the Fort Peck Tribes and allotted lands are lands owned in trust by the United States for an individual Indian or Indians. Northern Border Pipeline does have the right of eminent domain with respect to allotted lands.

In 1980, Northern Border Pipeline entered into a pipeline right-of-way lease with the Fort Peck Tribal Executive Board, for and on behalf of the Assiniboine and Sioux Tribes of the Fort Peck Indian Reservation (Tribes). This pipeline right-of-way lease, which was approved by the Department of the Interior in 1981, granted to Northern Border Pipeline the right and privilege to construct and operate its pipeline on certain tribal lands. This pipeline right-of-way lease expires in 2011. See Item 3. "Legal Proceedings."

In conjunction with obtaining a pipeline right-of-way lease across tribal lands located within the exterior boundaries of the Fort Peck Indian Reservation, Northern Border Pipeline also obtained a right-of-way across allotted lands located within the reservation boundaries. Most of the allotted lands are subject to a perpetual easement either granted by the Bureau of Indian Affairs for and on behalf of individual Indian owners or obtained through condemnation. Several tracts are subject to a right-of-way grant that has a term of 15 years, expiring in 2015.

### **Properties of Tuscarora Gas Transmission Company**

Tuscarora holds the right, title and interest in its pipeline system. Tuscarora owns all of its material equipment and personal property and leases office space in Reno, Nevada. With respect to real property, Tuscarora's ownership falls into two basic categories: (a) parcels which it owns in fee; and (b) parcels where its interest derives from leases, easements, grants, permits or licenses from landowners or governmental authorities permitting the use of the land for the construction and operation of its pipeline system.

### Item 3. Legal Proceedings

TC PipeLines is not currently a party to any material legal proceedings.

On July 31, 2001, the Tribes of the Fort Peck Indian Reservation filed a lawsuit in Tribal Court against Northern Border Pipeline to collect more than \$3.0 million in back taxes, together with interest and penalties. The lawsuit relates to a utilities tax on certain of Northern Border Pipeline's properties within the Fort Peck Indian Reservation. Northern Border Pipeline and the Tribes, through a mediation process, reached a settlement in principle on pipeline right-of-way lease and taxation issues. Final documentation has been completed and is subject to the approval of the Bureau of Indian Affairs, which the parties believe will be obtained in the very near term. This settlement grants to Northern Border Pipeline, among other things, (i) an option to renew the pipeline right-of-way lease upon agreed terms and conditions on or before April 1, 2011 for a term of 25 years with a renewal right for an additional 25 years; (ii) a present right to use additional tribal lands for expanded facilities; and (iii) release and satisfaction of all tribal taxes against us. In consideration of this option and other benefits, Northern Border Pipeline will pay a lump sum amount of \$5.9 million and an annual amount of approximately \$1.5 million beginning April 2004. Northern Border Pipeline advises that it intends to seek regulatory recovery of the costs resulting from the settlement. See Item 7. "Management's Discussion and Analysis of Financial Condition and Results of Operations – Risk Factors and Cautionary Statement Regarding Forward-Looking Statements."

See Item 1. "Business – Business of Northern Border Pipeline Company – FERC Regulation" for a discussion on the proceedings before the FERC.

Northern Border Pipeline advises that it is not currently party to any other legal proceedings that, individually or in the aggregate, would reasonably be expected to have a material adverse impact on it or TC PipeLines' results of operations or financial position.

Tuscarora is not currently a party to any material legal proceedings.

### Item 4. Submission of Matters to a Vote of Security Holders

There were no matters submitted to a vote of security holders, through solicitation of proxies or otherwise, during the year ended December 31, 2003.

## PART II

### Item 5. Market for Registrant's Common Units and Related Security Holder Matters

The common units representing limited partner interests in the Partnership were issued pursuant to an initial public offering on May 28, 1999 at a price of \$20.50 per common unit. The common units are quoted on the Nasdaq Stock Market and trade under the symbol "TCLP."

The following table sets forth, for the periods indicated, the high and low sale prices per common unit, as reported by the Nasdaq Stock Market, and the amount of cash distributions per common unit declared with respect to the corresponding periods. Cash distributions are paid within 45 days after the end of each quarter to unitholders of record as of the record date.

|                       | Price Range |          | Cash Distributions<br>Declared per Unit |
|-----------------------|-------------|----------|---|
|                       | High        | Low      |   |
| <b>2003</b>           |             |          |   |
| <b>First Quarter</b>  | \$ 27.35    | \$ 24.74 | \$ 0.525                                |
| <b>Second Quarter</b> | \$ 30.00    | \$ 25.50 | \$ 0.550                                |
| <b>Third Quarter</b>  | \$ 33.70    | \$ 28.80 | \$ 0.550                                |
| <b>Fourth Quarter</b> | \$ 33.70    | \$ 30.60 | \$ 0.550                                |
| <b>2002</b>           |             |          |   |
| First Quarter         | \$ 27.38    | \$ 23.90 | \$ 0.500                                |
| Second Quarter        | \$ 26.00    | \$ 23.31 | \$ 0.525                                |
| Third Quarter         | \$ 26.99    | \$ 21.30 | \$ 0.525                                |
| Fourth Quarter        | \$ 27.88    | \$ 24.02 | \$ 0.525                                |

As of February 23, 2004, there were 97 record holders of common units and approximately 7,500 beneficial owners of common units, including common units held in street name.

The Partnership currently has 16,563,564 common units outstanding, of which 11,890,694 are held by the public, 2,800,000 are held by an affiliate of the general partner, and 1,872,870 are held by the general partner. The Partnership also has 936,436 subordinated units outstanding, all of which are held by the general partner, for which there is no established public trading market. The common units and the subordinated units represent an aggregate 98% limited partner interest and the general partner interest represents an aggregate 2% general partner interest in the Partnership.

The general partner receives 2% of all cash distributions and the holders of common units and subordinated units (collectively referred to as unitholders) receive the remaining 98% of all cash distributions. The general partner is also entitled to incentive distributions as described below. The Partnership's quarterly cash distributions to its unitholders are comprised of all of its Available Cash. Available Cash is defined in the partnership agreement and generally means, with respect to any quarter of the Partnership, all cash on hand at the end of a quarter less the amount of cash reserves that are necessary or appropriate, in the reasonable discretion of the general partner, to:

- provide for the proper conduct of the business of the Partnership (including reserves for future capital expenditures and for anticipated credit needs);
- comply with applicable laws or any Partnership debt instrument or agreement; or
- provide funds for cash distributions to unitholders and the general partner in respect of any one or more of the next four quarters.

Distributions of Available Cash to the holder of subordinated units are subject to the prior rights of the holders of common units to receive the minimum quarterly distribution for each quarter while the subordinated units are outstanding (subordination period), and to receive any arrearages in the cash distribution of minimum quarterly distributions on the common units for prior quarters during the subordination period. The partnership agreement defines the minimum quarterly distribution as \$0.45 for each full fiscal quarter.

The general partner receives incentive distributions if the amount distributed with respect to any quarter exceeds the minimum quarterly distribution of \$0.45 per unit. Under the incentive distribution provisions, the general partner receives 15% of amounts distributed in excess of \$0.45 per unit, 25% of amounts distributed in excess of \$0.5275 per unit, and 50% of amounts distributed in excess of \$0.69 per unit provided the balance has been first distributed to unitholders on a pro rata basis. The amounts that trigger incentive distributions at various levels are subject to adjustment in certain events, as described in the partnership agreement.

In 2003, the Partnership made cash distributions to unitholders and the general partner that amounted to \$39.4 million compared to \$37.4 million in 2002. These payments represented \$0.525 per unit for the quarters ended December 31, 2002 and March 31, 2003 and \$0.55 per unit for the quarters ended June 30, 2003 and September 30, 2003. On February 13, 2004, the Partnership paid a cash distribution of \$10.1 million to unitholders and the general partner, representing a cash distribution of \$0.55 per unit for the quarter ended December 31, 2003. The distribution was allocated in the following manner: \$9.1 million to the holders of common units as of the close of business on January 30, 2004 (including \$1.5 million to an affiliate of the general partner as holder of 2,800,000 common units and \$1.0 million to the general partner as holder of 1,872,870 common units), \$0.5 million to the general partner as holder of the subordinated units, \$0.3 million to the general partner as holder of incentive distribution rights, and \$0.2 million to the general partner in respect of its 2% general partner interest.

#### **Subordination Period**

The subordination period extends until the first day of any quarter beginning after June 30, 2004 in respect of which:

- distributions of Available Cash from operating surplus on the common units and the subordinated units for each of the three non-overlapping four-quarter periods immediately preceding that date equaled or exceeded the sum of the minimum quarterly distribution on all of the outstanding common units and subordinated units during those periods;
- the adjusted operating surplus generated during each of the three non-overlapping four-quarter periods immediately preceding that date equaled or exceeded the sum of the minimum quarterly distribution on all of the common units and the subordinated units that were outstanding on a fully diluted basis and the related distributions on the general partner interest during those periods; and
- there are no arrearages in payment of the minimum quarterly distribution on the common units.

On August 1, 2002, 936,435 subordinated units, representing one-third of the outstanding subordinated units held by the general partner, upon satisfaction of the financial tests set forth in the partnership agreement of TC PipeLines, automatically converted into an equal number of common units.

On August 1, 2003, an additional 936,435 subordinated units held by the general partner, upon satisfaction of the financial tests set forth in the partnership agreement, automatically converted into an equal number of common units.

The remaining 936,436 outstanding subordinated units will, upon satisfaction of the financial tests, automatically convert into common units on the first day after the record date for distributions for the quarter ending June 30, 2004, and will thereafter participate, pro rata, with the other common units in distributions of Available Cash.

## Item 6. Selected Financial Data

The selected financial data should be read in conjunction with the financial statements, including the notes thereto, and Item 7. “Management’s Discussion and Analysis of Financial Condition and Results of Operations.”

| TC PIPELINES, LP  | Year Ended December 31 |         |         | May 28 <sup>(1)</sup> – |              |
|---|------------------------|---------|---------|-------------------------|--------------|
|   | 2003                   | 2002    | 2001    | 2000                    | Dec 31, 1999 |
| <i>(millions of dollars, except per unit amounts)</i>     |                        |         |         |                         |              |
| <b>Income Data</b>  |                        |         |         |                         |              |
| Equity income from investment in Northern Border Pipeline | 44.5                   | 42.8    | 42.1    | 38.1                    | 20.9         |
| Equity income from investment in Tuscarora <sup>(2)</sup> | 5.3                    | 4.7     | 3.6     | 0.9                     | –            |
| General and administrative expenses                       | (1.7)                  | (1.5)   | (1.2)   | (1.3)                   | (0.7)        |
| Financial charges   | (0.1)                  | (0.5)   | (1.0)   | (0.5)                   | –            |
| Net income  | 48.0                   | 45.5    | 43.5    | 37.2                    | 20.2         |
| Basic and diluted net income per unit                     | \$ 2.63                | \$ 2.50 | \$ 2.40 | \$ 2.08                 | \$ 1.13      |
| Units outstanding ( <i>millions</i> )                     | 17.5                   | 17.5    | 17.5    | 17.5                    | 17.5         |
| <b>Cash Flow Data</b>                                     |                        |         |         |                         |              |
| Net cash provided by operating activities                 | 49.6                   | 52.1    | 42.9    | 40.3                    | 11.8         |
| Distributions paid  | 39.4                   | 37.4    | 35.2    | 32.6                    | 11.0         |
| <b>Balance Sheet Data (at end of year)</b>                |                        |         |         |                         |              |
| Investment in Northern Border Pipeline                    | 240.7                  | 242.9   | 250.1   | 248.1                   | 250.5        |
| Investment in Tuscarora <sup>(2)</sup>                    | 39.9                   | 36.7    | 29.3    | 27.9                    | –            |
| Total assets  | 288.1                  | 286.0   | 288.7   | 277.5                   | 251.2        |
| Long-term debt  | 5.5                    | 11.5    | 21.5    | 21.5                    | –            |
| Partners’ equity  | 282.0                  | 273.9   | 266.7   | 255.4                   | 250.8        |

(1) The Partnership commenced operations on May 28, 1999.

(2) The Partnership acquired a 49% interest in Tuscarora on September 1, 2000.

## Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations

*As a result of the Partnership’s ownership of investments in both Northern Border Pipeline and Tuscarora, the following discusses first the results of operations and liquidity and capital resources of TC PipeLines, then those of each of Northern Border Pipeline and Tuscarora in their entirety.*

The following discussions of the financial condition and results of operations of the Partnership, Northern Border Pipeline and Tuscarora should be read in conjunction with the financial statements and notes thereto of the Partnership and Northern Border Pipeline included elsewhere in this report (see Item 8. “Financial Statements and Supplementary Data”). For more detailed information regarding the basis of presentation for the following financial information, see the notes to the financial statements of the Partnership and Northern Border Pipeline. As of December 31, 2003, TC PipeLines’ interest in Northern Border Pipeline represents approximately 84% of TC PipeLines’ total assets and for the year ended December 31, 2003 provided approximately 89% of TC PipeLines’ equity income. All amounts are stated in United States dollars.

### OVERVIEW

TC PipeLines owns a 30% general partner interest in Northern Border Pipeline Company. The remaining 70% general partner interest in Northern Border Pipeline is held by Northern Border Partners, L.P., a publicly traded limited partnership that is controlled by affiliates of Enron Corp. TransCanada holds a minority general partner interest in Northern Border Partners which entitles it to 12.25% of the voting power of Northern Border Pipeline. Northern Border Pipeline owns a 1,249-mile interstate pipeline system that transports natural gas from the Montana-Saskatchewan border near Port of Morgan, Montana to natural gas markets in the midwestern United States. Construction of the pipeline was initially completed in 1982. The Northern Border pipeline system was expanded

and/or extended in 1991, 1992, 1998 and 2001. The Northern Border pipeline system connects directly and through multiple pipelines to various natural gas markets in the United States.

TC PipeLines also owns a 49% general partner interest in Tuscarora Gas Transmission Company. The Partnership acquired this interest from TCPL Tuscarora Ltd., an indirect subsidiary of TransCanada, in September 2000. Tuscarora owns a 240-mile, 20-inch diameter, United States interstate pipeline system that originates at an interconnection point with facilities of Gas Transmission Northwest Corporation (GTN) near Malin, Oregon and runs southeast through northeastern California and northwestern Nevada. The Tuscarora pipeline system terminates near Wadsworth, Nevada. Deliveries are also made directly to the local gas distribution system of Sierra Pacific Resources. Along its route, deliveries are made in Oregon, northern California and northwestern Nevada.

The Tuscarora pipeline system was constructed in 1995 and was placed into service in December 1995. In January 2001, Tuscarora completed construction of the Hungry Valley lateral, a 14-mile, 16-inch pipeline extension that serves as Tuscarora's second connection into Reno, Nevada. On December 1, 2002, Tuscarora completed and placed into service another expansion of its pipeline system. The 2002 expansion consisted of two compressor stations and an 11-mile pipeline extension from the previous terminus of the Tuscarora pipeline system near Reno, Nevada to Wadsworth, Nevada. The expansion increased Tuscarora's contracted capacity from 127 mmcf to approximately 180 mmcf. The new capacity is contracted under long-term firm transportation contracts.

The Partnership's 30% general partner interest in Northern Border Pipeline and 49% general partner interest in Tuscarora represent its only material assets. As a result, the Partnership is dependent upon Northern Border Pipeline and Tuscarora for all of its available cash. Northern Border Pipeline represents approximately 90% of TC PipeLines' equity income. For an overview discussing the important factors impacting Northern Border Pipeline's business, such as the continued availability of western Canadian natural gas in the U.S., see "Results of Operations of Northern Border Pipeline Company – Overview" below.

## **RESULTS OF OPERATIONS OF TC PIPELINES, LP**

### **Critical Accounting Policy**

TC PipeLines accounts for its investments in both Northern Border Pipeline and Tuscarora using the equity method of accounting as detailed in Note 3 and Note 4 to the Partnership's Financial Statements, included elsewhere in this report. The equity method of accounting is appropriate where the investor does not control an investee, but rather is able to exercise significant influence over the operating and financial policies of an investee. TC PipeLines is able to exercise significant influence over its investments in Northern Border Pipeline and Tuscarora as evidenced by its representation on their respective management committees.

Since the 30% general partner interest in Northern Border Pipeline and the 49% general partner interest in Tuscarora are currently the Partnership's only material sources of income, the Partnership's results of operations are influenced by and reflect the same factors that influence the financial results of Northern Border Pipeline and Tuscarora (see Item 1. "Business – Business of Northern Border Pipeline Company" and "Business – Business of Tuscarora Gas Transmission Company").

### **Year Ended December 31, 2003 Compared with the Year Ended December 31, 2002**

Net income increased \$2.5 million, or 5%, to \$48.0 million for the year ended December 31, 2003, compared to \$45.5 million for 2002. The increase is primarily due to higher equity income from the Partnership's investments in Northern Border Pipeline and Tuscarora.

Equity income from the Partnership's investment in Northern Border Pipeline increased \$1.7 million, or 4%, to \$44.5 million for the year ended December 31, 2003 compared to \$42.8 million for 2002. Northern Border Pipeline's revenues for 2003 were higher than the same period last year due to the uncollected revenues associated with the transportation capacity previously held by Enron North America which reduced 2002 revenues, as well as additional

incremental revenues received in 2003. These factors increased the Partnership's 2003 equity income by \$0.9 million. Also, Northern Border Pipeline's interest expense was lower during 2003 compared to the same period last year due primarily to lower average interest rates and lower average debt balances outstanding, resulting in an increase of \$2.0 million to the Partnership's equity income. These increases were partially offset by higher operations and maintenance expenses and taxes other than income as well as a decrease in other income. The increase in 2003 operations and maintenance expense is primarily due to a provision recorded by Northern Border Pipeline in 2003 related to its share of Enron's cash balance plan underfunding (see "Results of Operations of Northern Border Pipeline Company – Impact of Enron's Chapter 11 Filing on Northern Border Pipeline's Business"), partially offset by lower electric power costs in 2003 as compared to 2002, resulting in a net decrease to the Partnership's equity income of \$0.3 million. The increase in 2003 taxes other than income is primarily due to a refund of use taxes received by Northern Border Pipeline during 2002 as well as higher property taxes in 2003 as compared to 2002. These increases resulted in a decrease in equity income to the Partnership of \$0.4 million. Other income (expense) was lower during 2003 as compared to the prior year. The 2003 amount includes interest expense for refunds required by the order issued by the FERC on March 27, 2003 (see Item 1. "Business – Business of Northern Border Pipeline Company – FERC Regulation") whereas the 2002 amount includes income mostly related to interest received on the refund of use taxes previously discussed and income for previously vacated frequency bands. The impact on the Partnership of this decrease in other income was a \$0.5 million reduction in equity income from Northern Border Pipeline.

Equity income from the Partnership's investment in Tuscarora increased \$0.6 million, or 13%, to \$5.3 million for the year ended December 31, 2003, compared to \$4.7 million for the prior year. Tuscarora's revenues increased primarily due to new transportation contracts from the expansion, increasing the Partnership's equity income from Tuscarora by \$3.2 million. This increase was partially offset by increased operations and maintenance expense and increased depreciation expense, both resulting from Tuscarora's expansion. The combined effect of these increased expenses reduced the Partnership's equity income from Tuscarora by \$1.8 million. In addition, higher interest expense due to Tuscarora's expansion, partially offset by a decrease in Tuscarora's other income, resulted in a \$0.8 million reduction in the Partnership's equity income for the year ended December 31, 2003.

The Partnership recorded general and administrative expenses of \$1.7 million and \$1.5 million for the years ended December 31, 2003 and 2002, respectively.

The Partnership recorded financial charges of \$0.1 million and \$0.5 million for the years ended December 31, 2003 and 2002, respectively. This decrease is primarily attributed to the Partnership repaying \$6.0 million of the balance outstanding on its Revolving Credit Facility during 2003, which reduced the balance outstanding from \$11.5 million to \$5.5 million.

#### **Year Ended December 31, 2002 Compared with the Year Ended December 31, 2001**

Net income increased \$2.0 million, or 5%, to \$45.5 million for the year ended December 31, 2002, compared to \$43.5 million for 2001. The increase is primarily due to higher equity income from the Partnership's investments in Northern Border Pipeline and Tuscarora.

Equity income from the Partnership's investment in Northern Border Pipeline increased \$0.7 million, or 2%, to \$42.8 million for the year ended December 31, 2002 compared to \$42.1 million for 2001. Northern Border Pipeline's revenues increased in 2002 due to Project 2000, Northern Border Pipeline's expansion and extension that was placed into service in October 2001. This had the impact of increasing the Partnership's 2002 equity income by approximately \$2.4 million. Also, favorable interest rates decreased Northern Border Pipeline's interest expense in 2002 further increasing 2002 equity income to the Partnership by \$1.1 million. These increases were largely offset by a reserve recorded by Northern Border Pipeline in 2002 for costs that arose from the treatment of previously collected quantities of natural gas used in utility operations to cover electric power costs, resulting in a \$3.0 million decrease in 2002 equity income to the Partnership (see Item 1. "Business – Business of Northern Border Pipeline Company – FERC Regulation").



Equity income from the Partnership's investment in Tuscarora increased \$1.1 million, or 31%, to \$4.7 million for the year ended December 31, 2002, compared to \$3.6 million for 2001. This increase is attributed to incremental revenue from new transportation contracts, the completion of Tuscarora's expansion facilities, which were placed into service on December 1, 2002, as well as lower interest expense, resulting from the capitalization of interest expense related to funds being used for the expansion.

The Partnership recorded general and administrative expenses of \$1.5 million and \$1.2 million for the years ended December 31, 2002 and 2001, respectively.

The Partnership recorded financial charges of \$0.5 million and \$1.0 million for the years ended December 31, 2002 and 2001, respectively. This decrease is primarily attributed to the Partnership repaying \$10.0 million of the balance outstanding on its Revolving Credit Facility during 2002, which reduced the balance outstanding from \$21.5 million to \$11.5 million, and to lower average interest rates during 2002.

## **LIQUIDITY AND CAPITAL RESOURCES OF TC PIPELINES, LP**

### **Cash Distribution Policy of TC Pipelines**

During the subordination period, which generally cannot end before June 30, 2004, the Partnership makes distributions of Available Cash in the following manner:

- First, 98% to the common units, pro rata, and 2% to the general partner, until there is distributed for each outstanding common unit an amount equal to the minimum quarterly distribution for that quarter;
- Second, 98% to the common units, pro rata, and 2% to the general partner, until there is distributed for each outstanding common unit an amount equal to any arrearages in payment of the minimum quarterly distribution on the common units for that quarter and for any prior quarters during the subordination period;
- Third, 98% to the subordinated units, pro rata, and 2% to the general partner, until there is distributed for each outstanding subordinated unit an amount equal to the minimum quarterly distribution for that quarter; and
- Thereafter, in a manner whereby the general partner has rights (referred to as incentive distribution rights) to receive increasing percentages of excess quarterly cash distributions over specified cash distribution thresholds.

The general partner receives incentive distributions if the amount distributed with respect to any quarter exceeds the minimum quarterly distribution of \$0.45 per unit. Under the incentive distribution provisions, the general partner receives 15% of amounts distributed in excess of \$0.45 per unit, 25% of amounts distributed in excess of \$0.5275 per unit, and 50% of amounts distributed in excess of \$0.69 per unit provided the balance has been first distributed to unitholders on a pro rata basis. The amounts that trigger incentive distributions at various levels are subject to adjustment in certain events, as described in the partnership agreement.

### **Conversion of Subordinated Units**

On August 1, 2002, 936,435 subordinated units, representing one-third of the outstanding subordinated units held by the general partner, upon satisfaction of the financial tests set forth in the partnership agreement of TC Pipelines, automatically converted into an equal number of common units.

On August 1, 2003, an additional 936,435 subordinated units held by the general partner, upon satisfaction of the financial tests set forth in the partnership agreement, automatically converted into an equal number of common units.

The remaining 936,436 outstanding subordinated units will, upon satisfaction of the financial tests, automatically convert into common units on the first day after the record date for distributions for the quarter ending June 30, 2004, and will thereafter participate, pro rata, with the other common units in distributions of Available Cash.

### **General**

On January 30, 2004, the Partnership paid \$19.5 million related to its 30% share of a capital contribution to Northern Border Pipeline in response to a \$65.0 million cash call issued by Northern Border Pipeline to its partners on

January 27, 2004. The funds will be used by Northern Border Pipeline to repay a portion of its existing indebtedness under the 2002 Pipeline Credit Agreement. This payment was funded through the use of cash from operations and existing credit facilities.

On January 16, 2004, the board of directors of the general partner declared the Partnership's 2003 fourth quarter cash distribution. The fourth quarter cash distribution, which was paid on February 13, 2004 to unitholders of record as of January 30, 2004, totaled \$10.1 million and was paid in the following manner: \$9.1 million to common unitholders (including \$1.5 million to an affiliate of the general partner as holder of 2,800,000 common units and \$1.0 million to the general partner as holder of 1,871,870 common units), \$0.5 million to the general partner as holder of the subordinated units, \$0.3 million to the general partner as the holder of incentive distribution rights, and \$0.2 million to the general partner in respect of its 2% general partner interest.

### Summary of Certain Contractual Obligations

| Payments Due by Period    | Total  | Less Than<br>1 Year | 1-3 Years | 4-5 Years | After<br>5 Years |
|---------------------------|--------|---------------------|-----------|-----------|------------------|
| <i>(in millions)</i>      |        |                     |           |           |                  |
| Revolving Credit Facility | 5.5    | 5.5                 | —         | —         | —                |
| Total                     | \$ 5.5 | \$ 5.5              | \$ —      | \$ —      | \$ —             |

### Debt and Credit Facilities

On May 28, 2003, the Partnership renewed its \$40.0 million unsecured two-year revolving credit facility (TransCanada Credit Facility) with TransCanada PipeLine USA Ltd., an affiliate of the general partner. The TransCanada Credit Facility bears interest at the London Interbank Offered Rate (LIBOR) plus 1.25%. The purpose of the TransCanada Credit Facility is to provide borrowings to fund capital expenditures, to fund capital contributions to Northern Border Pipeline, Tuscarora and any other entity in which the Partnership directly or indirectly acquires an interest, to fund working capital and for other general business purposes, including temporary funding of cash distributions to unitholders and the general partner, if necessary. At December 31, 2003 and 2002, the Partnership had no borrowings outstanding under the TransCanada Credit Facility. As at March 12, 2004, \$9.0 million is outstanding under the TransCanada Credit Facility.

On March 8, 2004 the Partnership renewed its unsecured credit facility (Revolving Credit Facility) with Bank One, NA, as administrative agent. Under the Revolving Credit Facility, the Partnership may borrow up to an aggregate principal amount of \$30.0 million. Loans under the Revolving Credit Facility may bear interest, at the option of the Partnership, at a one-, two-, three-, or six-month LIBOR plus 1.25%, or at a floating rate based on the higher of the federal funds effective rate plus 0.5% and the prime rate. The Revolving Credit Facility matures on February 28, 2006. Amounts borrowed may be repaid in part or in full prior to that time without penalty. The Revolving Credit Facility may be used to finance capital expenditures and for other general purposes. The Partnership had \$5.5 million and \$11.5 million outstanding under the Revolving Credit Facility at December 31, 2003 and 2002, respectively. The interest rate on the Revolving Credit Facility at December 31, 2003 and 2002 was 2.4% and 2.7%, respectively. As at March 12, 2004, \$5.5 million is outstanding under the Revolving Credit Facility.

On April 23, 2002, the Partnership filed a shelf registration statement with the SEC to sell, from time to time, up to \$200.0 million of common units representing limited partner interests and/or debt securities. The Partnership intends to use the net proceeds for general purposes, repayment of debt, future acquisitions, capital expenditures and working capital. As at March 12, 2004, no additional units of the Partnership had been issued.

### Cash Flows from Operating Activities

Cash flows provided by operating activities decreased \$2.5 million, or 5%, to \$49.6 million for the year ended December 31, 2003, compared to \$52.1 million for 2002. The decrease is primarily due to lower distributions received

from Northern Border Pipeline in 2003 as compared to 2002. In 2003, Northern Border Pipeline was ordered by the FERC to refund \$10.0 million (TC PipeLines' share is \$3.0 million) to its shippers related to company use gas (see Item 1. "Business – Business of Northern Border Pipeline Company – FERC Regulation"). In 2003, the Partnership's cash from operations included cash distributions of \$45.2 million and \$6.2 million from its investments in Northern Border Pipeline and Tuscarora, respectively, compared to \$49.2 million and \$4.6 million, respectively, in 2002.

Cash flows provided by operating activities increased \$9.2 million, or 21%, to \$52.1 million for the year ended December 31, 2002, compared to \$42.9 million for 2001. In 2001, the Partnership received cash distributions of \$42.9 million and \$2.4 million from Northern Border Pipeline and Tuscarora, respectively.

#### **Cash Flows from Investing Activities**

For the year ended December 31, 2003, the Partnership made equity contributions totaling \$4.9 million to Tuscarora related to Tuscarora's expansion project, which was partially offset by a \$0.8 million return of capital from Tuscarora. As well, a \$1.0 million return of capital was received by the Partnership from Northern Border Pipeline in 2003. During 2002, the Partnership made equity contributions totaling \$7.6 million to Tuscarora related to Tuscarora's expansion project, partially offset by a \$0.2 million return of capital received from Tuscarora in 2002.

The Partnership did not have any material sources or uses of cash relating to investing activities in 2001.

#### **Cash Flows from Financing Activities**

For the year ended December 31, 2003, the Partnership paid cash distributions of \$39.4 million, compared to \$37.4 million in 2002. The increase is due to the Partnership increasing its quarterly cash distribution from \$0.525 per unit to \$0.55 per unit beginning with the 2003 second quarter cash distribution. In 2001, the Partnership paid cash distributions of \$35.2 million.

For the year ended December 31, 2003, the Partnership repaid \$6.0 million of the balance outstanding on the Revolving Credit Facility, compared to repayments of \$10.0 million during 2002. The Partnership did not make any drawings or repayments on the Revolving Credit Facility in 2001. At December 31, 2003, the Partnership had \$5.5 million outstanding under the Revolving Credit Facility.

#### **Capital Requirements**

On January 30, 2004, TC PipeLines paid \$19.5 million related to its 30% share of a capital contribution to Northern Border Pipeline in response to a \$65.0 million cash call issued by Northern Border Pipeline to its partners on January 27, 2004.

To the extent TC PipeLines has any additional capital requirements with respect to its investments in Northern Border Pipeline and Tuscarora or makes acquisitions in 2004, TC PipeLines expects to finance these requirements with operating cash flows, debt and/or equity.

#### **Impact of Enron's Chapter 11 Filing on TC PipeLines' Business**

In 2001, Enron filed a voluntary petition for bankruptcy protection under Chapter 11 of the United States Bankruptcy Code. For more details see "Results of Operations of Northern Border Pipeline Company – Impact of Enron's Chapter 11 Filing on Northern Border Pipeline's Business."

Based on currently available information, TC PipeLines does not expect the impact of Enron's bankruptcy protection filing to have a material impact on the business or financial condition of Northern Border Pipeline or TC PipeLines.

TC PipeLines continues to monitor developments at Enron and to assess any impact of Enron's Chapter 11 proceedings on Northern Border Pipeline in light of Northern Border Pipeline's existing agreements and relationships with Enron and its subsidiaries, and to take all appropriate action to protect the interests of TC PipeLines and its unitholders.

## Outlook

On December 19, 2003, Northern Border Pipeline advised that its Management Committee had unanimously agreed to issue equity cash calls to its partners in the total amount of \$130.0 million (TC PipeLines' share is \$39.0 million) in early 2004, the first of which was issued on January 27, 2004, and \$90.0 million (TC PipeLines' share is \$27.0 million) in 2007 and to change the cash distribution policy of Northern Border Pipeline as of January 1, 2004. Effective January 1, 2008, Northern Border Pipeline's cash distribution policy will be adjusted to maintain a consistent capital structure. TC PipeLines expects to fund a portion of the 2004 equity cash calls with borrowings under its existing credit facilities. As at March 12, 2004, the Partnership has paid Northern Border Pipeline \$19.5 million related to the equity cash calls previously discussed.

## RESULTS OF OPERATIONS OF NORTHERN BORDER PIPELINE COMPANY

*In the following discussion of the results of Northern Border Pipeline, all amounts represent 100% of the operations of Northern Border Pipeline, in which the Partnership has held a 30% interest since May 28, 1999.*

The discussion and analysis of Northern Border Pipeline's financial condition and operations are based on Northern Border Pipeline's financial statements, which were prepared in accordance with accounting principles generally accepted in the United States of America. The following discussion and analysis should be read in conjunction with Northern Border Pipeline's financial statements included elsewhere in this report.

### Overview

For Northern Border Pipeline, there are several major business drivers. First, a healthy long-term supply outlook is critical. Because the primary source of gas supply that is transported on its system is in the Western Canadian Sedimentary Basin, western Canadian supply trends are particularly important to Northern Border Pipeline. The current outlook for western Canadian supply looks stable for the foreseeable future however production has exceeded new reserve additions in recent years. Increased Canadian consumption related to the extraction process for oil sands projects as well as restrictions on gas production to protect oil sand reserves could also impact supplies of natural gas for export. The supply outlook may be significantly enhanced over time by new Alaskan and Mackenzie Delta supplies reaching the western Canadian pipeline grid potentially beginning by the end of this decade.

Natural gas markets are also critical to Northern Border Pipeline's financial performance. The Northern Border pipeline system serves natural gas markets in the upper midwestern area of the United States and accesses a major trading hub in the Chicago area. Market growth has been steady with both heating load growth and direct end-user growth such as power plants and ethanol plants. However, competitive pipeline projects may have a negative impact on Northern Border Pipeline's profitability.

Northern Border Pipeline charges fees for transportation which are primarily fixed and are based on the amount of capacity reserved for each shipper. Contracting with shippers to reserve the available pipeline capacity as existing contracts expire is a critical factor in Northern Border Pipeline's success. The weighted average life of Northern Border Pipeline's contracts as of December 31, 2003 was approximately three and one third years. During 2003, Northern Border Pipeline was successful in recontracting, at maximum rates, all the capacity under contracts that expired on or before November 2003.

The composition of natural gas affects the volume of natural gas that is transported through a pipeline system. Beginning in 2000, the energy content of natural gas that Northern Border Pipeline receives at the Canadian border has declined modestly from 1,023 British Thermal Units (Btus) per cubic feet (cf) to 1,005 Btus/cf. The Btu level affects the heating value of the natural gas. Northern Border Pipeline's transportation contracts in conjunction with its tariff define both the volume and equivalent Btu value of the gas to be transported. A reduction in the Btu level results in a higher volume of natural gas to be transported to meet an overall equivalent Btu value of the gas. The Btu level decline that is being experienced is primarily the result of greater processing capacity in Alberta, Canada. The change has caused

Northern Border Pipeline to reduce its capacity by almost 2 percent to be able to maintain its high standard of system reliability for its customers. Although Btu levels could theoretically go lower, Northern Border Pipeline advises that it believes the Btu level will stabilize near the current level of 1,005 Btus/cf.

As was the case last year, Northern Border Pipeline is in re-contracting discussions with its customers for contracts that will expire prior to November 1, 2004, which represents approximately 30% of its system capacity. The value of capacity on interstate pipelines is driven by supply and demand conditions. In particular, the relationship between gas prices in Canada and prices in the midwestern U.S. markets will determine the underlying value of transportation. The current gas balance in western Canada is such that Northern Border Pipeline's transportation has been commercially attractive for available supply that is not consumed within western Canada or committed to transportation capacity on other pipelines reaching downstream markets. To maintain an adequate gas balance in western Canada, production will need to grow moderately in the future to meet anticipated demand primarily driven by gas consumption in the extraction and processing associated with Canadian oil sands development. Canada holds an estimated 1.6 trillion barrels of bitumen reserves. Bitumen, after it is extracted from sand, can be upgraded to synthesized crude oil through several processes. The extraction and processing of bitumen require significant quantities of natural gas. Northern Border Pipeline advises that it does not know how many of the announced oil sands development projects will be approved and constructed but the demand for transportation on its pipeline system could be affected adversely by the additional competition for Canadian gas supply that would result.

Northern Border Pipeline advises that it continues to work with producers and marketers to develop the contractual support for a new proposed 300-mile pipeline project, the Bison Pipeline, to connect the coal bed methane reserves in the Powder River Basin to markets served by Northern Border Pipeline. Northern Border Pipeline advises that it intends to hold a new open season for the Bison Pipeline when production increases to levels that Northern Border Pipeline believes will support the project. If sufficient interest commitments are received, Northern Border Pipeline advises that it will pursue regulatory approvals.

Northern Border Pipeline advises that it will continue to focus on safe, efficient, and reliable operations and the further development of its pipeline. Northern Border Pipeline further advises that it is working to maintain its position as a low cost transporter of Canadian gas to the midwestern U.S. and provide highly valued services to its customers. Growth may occur through incremental projects intended to access new markets or supply areas and supported by long-term contracts.

#### **Critical Accounting Policies and Estimates**

Certain amounts included in or affecting Northern Border Pipeline's financial statements and related disclosures must be estimated, requiring Northern Border Pipeline to make certain assumptions with respect to values or conditions that cannot be known with certainty at the time the financial statements are prepared. The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Any effects on Northern Border Pipeline's business, financial position or results of operations resulting from revisions to these estimates are recorded in the period in which the facts that gave rise to the revision become known.

Northern Border Pipeline's significant accounting policies are summarized in Note 2 – Notes to Northern Border Pipeline's Financial Statements included elsewhere in this report. Certain of Northern Border Pipeline's accounting policies are of more significance in its financial statement preparation process than others. Northern Border Pipeline's accounting policies conform to Statement of Financial Accounting Standards (SFAS) No. 71, "Accounting for the Effects of Certain Types of Regulation." Accordingly, certain assets that result from the regulated ratemaking process are recorded that would not be recorded under accounting principles generally accepted in the United States of America for nonregulated entities. Northern Border Pipeline continually assesses whether the regulatory assets are probable of

future recovery by considering such factors as regulatory changes and the impact of competition. If future recovery ceases to be probable, Northern Border Pipeline would be required to write-off the regulatory assets at that time. At December 31, 2003, Northern Border Pipeline has reflected regulatory assets of \$8.2 million, which are being recovered from its shippers over varying periods of time.

Northern Border Pipeline's long-lived assets are stated at original cost. Northern Border Pipeline must use estimates in determining the economic useful lives of those assets. For utility property, no retirement gain or loss is included in income except in the case of retirements or sales of entire regulated operating units. The original cost of utility property retired is charged to accumulated depreciation and amortization, net of salvage and cost of removal.

Northern Border Pipeline's accounting for financial instruments is in accordance with SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities." SFAS No. 133 requires that every derivative instrument be recorded on the balance sheet as either an asset or liability measured at its fair value. The statement requires that changes in the derivative's fair value be recognized currently in earnings unless specific hedge accounting criteria are met. Special accounting for qualifying hedges allows a derivative's gains and losses to offset related results on the hedged item in the income statement. At December 31, 2003, Northern Border Pipeline's balance sheet included assets from derivative financial instruments of \$16.6 million.

### **Results of Operations**

Northern Border Pipeline's net income to partners was \$148.2 million in 2003, compared to net income of \$142.7 million in 2002 and \$140.5 million in 2001. Northern Border Pipeline's 2003 operating results benefited from increased operating revenues from Northern Border Pipeline's Order 637 Compliance filing which went into effect October 1, 2003 and the ability to enter into short-term contracts effective November 1, 2003, the re-contracting of capacity previously held by Enron North America Corp. (ENA), and reductions in interest expense due to lower interest rates. Partially offsetting these increases to Northern Border Pipeline's operating results were higher operations and maintenance expenses for 2003 as compared to 2002. Northern Border Pipeline's increase in net income in 2002 over 2001 resulted from reductions in interest rates, which reduced its interest expense for 2002 as compared to 2001. In addition, Northern Border Pipeline realized increased operating revenues in 2002 resulting from Project 2000, Northern Border Pipeline's expansion and extension placed in service in October 2001. Northern Border Pipeline's 2001 results were reduced by reserves for uncollectible receivables.

Operating revenues were \$324.2 million in 2003, \$321.1 million in 2002 and \$313.1 million in 2001. The \$3.1 million increase in operating revenues in 2003 over 2002 resulted primarily from additional revenues of approximately \$1.8 million related to the re-contracted capacity of ENA contracts. ENA filed for Chapter 11 bankruptcy protection in December 2001 (see "Impact Of Enron's Chapter 11 Filing On Northern Border Pipeline's Business"). In addition, Northern Border Pipeline recognized revenues from its ability to now offer short-term firm contracts and also transportation service beyond a shipper's contracted transportation path. The increase in operating revenues in 2002 over 2001 was primarily due to additional revenues of approximately \$10.3 million associated with the completion of Project 2000 in October 2001. The impact of the additional revenues associated with Project 2000 was partially offset by uncollected revenues associated with the transportation capacity formerly held by ENA. For 2002, the revenues lost on this capacity totaled approximately \$1.8 million.

Operations and maintenance expenses were \$43.8 million in 2003, \$41.4 million in 2002 and \$33.7 million in 2001. The 2003 expense included a \$3.1 million charge for Northern Border Pipeline's allocation from Northern Plains related to the Enron cash balance plan under funding (see "Results of Operations of Northern Border Pipeline Company – Impact of Enron's Chapter 11 Filing on Northern Border Pipeline's Business"). In 2003, Northern Border Pipeline also had increases in salaries and benefits, rights-of-way damages, and telecommunication expenses offset by decreases in electric power costs, as compared to 2002. The 2002 expense included a \$10.0 million reserve for costs associated with

the treatment of previously collected quantities of natural gas used in utility operations to cover electric power costs. The FERC ordered refunds for these costs in 2003 (see Item 1. “Business – Business of Northern Border Pipeline – FERC Regulation”). The 2002 expense also included an increase in regulatory commission expense, and decreases in employee benefit expense, administrative expense, and bad debt expense as compared to 2001.

Depreciation and amortization expense was \$57.8 million in 2003, \$58.7 million in 2002 and \$57.5 million in 2001. The decrease from 2002 to 2003 primarily reflects asset retirements. The increase between 2001 and 2002 reflects additional expense for assets related to Project 2000, placed in service in October 2001.

Taxes other than income were \$29.6 million in 2003, \$28.4 million in 2002 and \$25.6 million in 2001. The increase in 2003 from 2002 is due primarily to a refund from Minnesota for previously paid use taxes. The decrease in taxes other than income in 2002 from 2001 was due primarily to adjustments to ad valorem taxes. Northern Border Pipeline periodically reviews and adjusts its estimates of ad valorem taxes. Reductions to previous estimates in 2001 exceeded reductions to previous estimates in 2002 by approximately \$2.1 million. As a result of a ruling by the Minnesota Supreme Court, Northern Border Pipeline filed for a refund of use taxes previously paid on exempt purchases. Northern Border Pipeline received the refund in March 2002.

Interest expense was \$44.9 million in 2003, \$51.5 million in 2002 and \$55.4 million in 2001. Interest expense for both 2003 and 2002 decreased from prior year levels due to a decrease in Northern Border Pipeline’s average interest rate as well as a decrease in its average debt outstanding. The 2001 results included \$0.9 million of interest expense capitalized primarily related to the construction of Project 2000 facilities.

Other income (expense) was \$0.1 million in 2003, \$1.8 million in 2002 and (\$0.4 million) in 2001. In 2003, Northern Border Pipeline recorded expense of approximately \$0.6 million for a repayment of amounts previously received for vacated microwave frequency bands, interest expense of \$0.3 million due to the FERC-ordered refunds of electric power costs and \$0.2 million of interest income received related to a sales tax refund on exempt purchases. The amount for 2002 includes approximately \$0.6 million for amounts received for previously vacated microwave frequency bands and income of \$0.2 million due to a reduction in reserves previously established. The amount for 2001 includes a charge of approximately \$1.5 million for an uncollectible receivable from a telecommunications company that had purchased excess capacity on Northern Border Pipeline’s communication system and a \$0.7 million charge for reserves established. Northern Border Pipeline recorded an allowance for equity funds used during construction of \$0.9 million in 2001 primarily due to the construction of Project 2000 facilities.

## **LIQUIDITY AND CAPITAL RESOURCES OF NORTHERN BORDER PIPELINE COMPANY**

### **Cash Distribution Policy of Northern Border Pipeline**

Under the terms of the cash distribution policy of Northern Border Pipeline, distributions to the general partners of Northern Border Pipeline are to be made on a proportionate basis according to each general partner’s capital account balance. The Northern Border Pipeline management committee determines the amount and timing of distributions. In December, 2003, Northern Border Pipeline’s management committee voted to, among other things, change its cash distribution policy effective January 1, 2004. Under this new policy, cash distributions are based upon 100% of distributable cash flow which is earnings before interest, taxes, depreciation and amortization less interest expense and maintenance capital expenditures. Effective January 1, 2008, the cash distribution policy will be adjusted to maintain a consistent capital structure at a level to be determined. Prior to January 1, 2004, cash distributions were computed as the sum of 100% of net income, excluding specific non-cash items, 100% of the current portion of any allowance for income taxes and 35% of the sum of deferred tax expense, depreciation expense and amortization of regulatory assets, minus 35% of maintenance capital expenditures. Cash distributions are currently made by Northern Border Pipeline on a quarterly basis approximately one month after the end of the quarter.

### Summary of Certain Contractual Obligations

| Payments Due by Period          | Total           | Less Than<br>1 Year | 1-3 Years       | 4-5 Years       | After<br>5 Years |
|---------------------------------|-----------------|---------------------|-----------------|-----------------|------------------|
| <i>(in millions)</i>            |                 |                     |                 |                 |                  |
| Senior Notes due 2007           | \$ 225.0        | \$ —                | \$ 225.0        | \$ —            | \$ —             |
| Senior Notes due 2009           | 200.0           | —                   | —               | 200.0           | —                |
| Senior Notes due 2021           | 250.0           | —                   | —               | —               | 250.0            |
| Credit Agreement due 2005       | 131.0           | —                   | 131.0           | —               | —                |
| Operating Leases <sup>(1)</sup> | 19.3            | 5.8                 | 4.8             | 4.8             | 3.9              |
| <b>Total</b>                    | <b>\$ 825.3</b> | <b>\$ 5.8</b>       | <b>\$ 360.8</b> | <b>\$ 204.8</b> | <b>\$ 253.9</b>  |

(1) See Note 7 – Notes to Northern Border Pipeline's Financial Statements.

### Debt and Credit Facilities

Northern Border Pipeline entered into a \$175 million three-year credit agreement (2002 Pipeline Credit Agreement) with certain financial institutions in May 2002. The 2002 Pipeline Credit Agreement replaced a previous credit agreement. The 2002 Pipeline Credit Agreement is to be used to refinance existing indebtedness and for general business purposes. At December 31, 2003, \$131 million was outstanding under the 2002 Pipeline Credit Agreement at an average interest rate of 1.95%. The 2002 Pipeline Credit Agreement requires the maintenance of a ratio of EBITDA (net income plus interest expense, income taxes and depreciation and amortization) to interest expense of greater than 3 to 1. The 2002 Pipeline Credit Agreement also requires the maintenance of the ratio of indebtedness to EBITDA of no more than 4.5 to 1. At December 31, 2003, Northern Border Pipeline was in compliance with these covenants.

At December 31, 2002, Northern Border Pipeline had outstanding \$65 million of Series D Senior Notes issued in a \$250 million private placement under a July 1992 note purchase agreement. The Series D Senior Notes matured in August 2003. Northern Border Pipeline borrowed under the 2002 Pipeline Credit Agreement to repay the Series D Senior Notes.

In April 2002, Northern Border Pipeline completed a private offering of \$225 million of 6.25% Senior Notes due 2007 (2002 Pipeline Senior Notes). In September 2001, Northern Border Pipeline completed a private offering of \$250 million of 7.50% Senior Notes due 2021 (2001 Pipeline Senior Notes). In August 1999, Northern Border Pipeline completed a private offering of \$200 million of 7.75% Senior Notes due 2009 (1999 Pipeline Senior Notes). The 2002 Pipeline Senior Notes, 2001 Pipeline Senior Notes and 1999 Pipeline Senior Notes (collectively Pipeline Senior Notes) were subsequently exchanged in registered offerings for notes with substantially identical terms. The indentures under which the Pipeline Senior Notes were issued do not limit the amount of unsecured debt Northern Border Pipeline incurs, but do contain material financial covenants, including restrictions on incurrence of secured indebtedness. The proceeds from the Pipeline Senior Notes were used to reduce indebtedness outstanding.

Northern Border Pipeline entered into interest rate swap agreements with notional amounts totaling \$225 million in May 2002. Under the interest rate swap agreements, Northern Border Pipeline makes payments to counter parties at variable rates based on the London Interbank Offered Rate and in return receives payments based on a 6.25% fixed rate. The swaps were entered into to hedge the fluctuations in the market value of the 2002 Pipeline Senior Notes. At December 31, 2003, the average effective interest rate on Northern Border Pipeline's interest rate swap agreements was 2.31%.

Northern Border Pipeline's short-term liquidity needs will be met by operating cash flows and through the 2002 Pipeline Credit Agreement. Northern Border Pipeline's long-term capital needs may be met through the ability to issue long-term indebtedness.

### Cash Flows From Operating Activities

Cash flows provided by operating activities were \$193.3 million in 2003, \$224.4 million in 2002 and \$197.3 million in 2001. The \$31.1 million decrease in 2003 from 2002 was primarily due to the payment of the FERC-ordered refunds related to



the electric power costs and the discontinuance of certain shipper transportation repayments. The \$27.1 million increase in 2002 from 2001 was primarily due to an increase in operating revenues and the impact of rate case refunds in 2001. In 2001, Northern Border Pipeline realized net cash outflows of approximately \$4.7 million related to its rate case refunds. During the first quarter of 2001, Northern Border Pipeline made refunds to its shippers totaling \$6.8 million, which included approximately \$2.1 million collected in the first quarter of 2001 with the remainder collected previously.

#### **Cash Flows From Investing Activities**

Cash used in investing was \$12.9 million for 2003 as compared to \$9.2 million for 2002 and \$54.7 million for 2001. The 2003, 2002 and 2001 amounts include \$0.9 million, \$0.3 million and \$49.0 million, respectively, for Project 2000. The remaining capital expenditures for 2003, 2002 and 2001 were primarily related to renewals and replacements of existing facilities.

Total capital expenditures for 2004 are estimated to be \$14.0 million primarily related to renewals and replacements of existing facilities. Northern Border Pipeline advises that it currently anticipates funding its 2004 capital expenditures primarily by borrowing on its credit facility and using operating cash flows.

#### **Cash Flows From Financing Activities**

Cash flows used in financing activities were \$177.0 million for the year ended December 31, 2003 as compared to \$200.8 million for the same period in 2002 and \$160.7 million for the same period in 2001. Distributions to Northern Border Pipeline's partners were \$154.0 million, \$164.1 million and \$143.0 million for 2003, 2002 and 2001, respectively. The decrease from 2002 to 2003 in distributions was primarily due to the impact of the electric power refunds ordered by FERC on March 27, 2003. The increase from 2001 to 2002 in distributions was primarily due to Northern Border Pipeline's improved operating results.

For 2003, 2002 and 2001, Northern Border Pipeline's borrowings on long-term debt totaled \$142.0 million, \$431.9 million and \$385.4 million, respectively, which were primarily used to repay previously existing indebtedness. For 2002, Northern Border Pipeline received net proceeds from the 2002 Pipeline Senior Notes of approximately \$223.5 million. The net proceeds from the issuance of the 2001 Pipeline Senior Notes totaled approximately \$247.2 million in 2001. Northern Border Pipeline's borrowings under its credit agreements were \$131.0 million in 2003, \$207.0 million in 2002 and \$136.0 million in 2001. Total payments on debt were \$165.0 million, \$468.0 million and \$374.0 million in 2003, 2002 and 2001, respectively.

In April 2002, Northern Border Pipeline received \$2.4 million from the termination of forward starting interest rate swaps upon issuance of the 2002 Pipeline Senior Notes (see Note 6 – Notes to Northern Border Pipeline's Financial Statements). In September 2001, Northern Border Pipeline paid approximately \$4.1 million to terminate interest rate swap agreements upon issuance of the 2001 Pipeline Senior Notes. The swaps were entered into to hedge the fluctuations in Treasury rates and spreads between the execution date of the swaps and the issuance of the 2002 and 2001 Pipeline Senior Notes. For 2001, Northern Border Pipeline recognized a decrease in bank overdraft of \$22.4 million. At December 31, 2000, Northern Border Pipeline reflected the bank overdraft primarily due to rate refund checks outstanding.

#### **Impact of Enron's Chapter 11 Filing on Northern Border Pipeline's Business**

On December 2, 2001, Enron filed a voluntary petition for bankruptcy protection under Chapter 11 of the United States Bankruptcy Code. Certain wholly owned Enron subsidiaries also filed for Chapter 11 bankruptcy protection on December 2, 2001 and thereafter. Northern Border Pipeline has not filed for bankruptcy protection. Northern Plains, Pan Border and Northwest Border are Northern Border Partners' general partners. Each of Northern Plains and Pan Border are wholly owned subsidiaries of Enron, and Northwest Border is a wholly owned subsidiary of TransCanada. Northern Plains and Pan Border were not among the Enron companies filing for Chapter 11 protection.

The business of Enron and its subsidiaries that have filed for bankruptcy protection are currently being administered under the direction and control of the bankruptcy court. An unsecured creditors committee has been appointed in the Chapter 11 cases. The creditors committee is responsible for general oversight of the bankruptcy case, and has the power, among other things, to: investigate the acts, conduct, assets, liabilities, and financial condition of the debtor, the operation of the debtor's business and the desirability of the continuance of such business; participate in the formulation of a plan of reorganization; and file acceptances or rejections to such a plan.

On June 25, 2003, Enron announced the organization of CrossCountry Energy Corp., a newly formed holding company, to hold, among other assets, Enron's ownership interest in Northern Plains and Pan Border. The motion filed in Bankruptcy Court to approve the proposed transfer of those ownership interests was approved on September 25, 2003. An amended order on December 18, 2003 made the approval applicable to CrossCountry Energy, LLC (CrossCountry). In connection with the closing, CrossCountry and Enron will enter into a transition services agreement pursuant to which Enron will provide to CrossCountry, on an interim, transitional basis, various services, including but not limited to (i) information technology services, (ii) accounting system usage rights and administrative support (iii) contract management and purchasing support services (iv) corporate secretary services, and (v) payroll, employee benefits and administrative services. In turn, these services are provided to Northern Border Pipeline through Northern Plains.

On January 9, 2004, the Bankruptcy Court approved as complete the amended joint Chapter 11 plan and related disclosure statement (Chapter 11 Plan). The Chapter 11 Plan has been submitted to the creditors for approval. Several creditors have filed objections to the Chapter 11 Plan, including the Pension Benefit Guaranty Corporation (PBGC). The Bankruptcy Court has scheduled a hearing for April 20, 2004 on the approval. Under the Chapter 11 Plan, it is anticipated that if CrossCountry is not sold to a third party, as permitted by the Chapter 11 Plan, its shares would be distributed directly or indirectly to creditors of the debtors.

Enron's filing for bankruptcy protection has impacted Northern Border Pipeline. At the time of the filing of the bankruptcy petition, Northern Border Pipeline had a number of contractual relationships with Enron and its subsidiaries. Northern Plains provided and continues to provide operating and administrative services for Northern Border Pipeline. Northern Plains has continued to meet its operational and administrative service obligations under the existing agreement, and, in its Form 10-K for the year ended December 31, 2003, Northern Border Pipeline states that it believes Northern Plains will continue to do so.

ENA, a wholly owned subsidiary of Enron that is in bankruptcy, was a party to transportation contracts which obligated ENA to pay for 3.5% of Northern Border Pipeline's capacity. In 2002, ENA rejected and terminated all of its contracts on the Northern Border pipeline system. Northern Border Pipeline filed claims against ENA for damages for breach of contract and other claims. These claims are unsecured claims against Enron and ENA's bankruptcy estate. Northern Border Pipeline advises that it is uncertain regarding the ultimate amount of damages for breach of contract or other claims that Northern Border Pipeline will be able to establish in the bankruptcy proceeding, and Northern Border Pipeline cannot predict the amounts that it will collect or the timing of collection. Northern Border Pipeline further states that it believes, however, that any such delay in collecting or failure to collect will not have a material adverse effect on its financial condition.

On December 31, 2003, Enron filed a motion seeking approval of the Bankruptcy Court to provide additional funding to, and for authority to terminate the Enron Corp. Cash Balance Plan (Plan) and certain other defined benefit plans of Enron's affiliated in 'standard terminations' within the meaning of Section 4041 of the Employee Retirement Income Security Act of 1974, as amended (ERISA). Such standard terminations would satisfy all of the obligations of Enron and its affiliates with respect to funding liabilities under the Plan. In addition, a standard termination would eliminate the contingent claims of the PBGC against Enron and its affiliates with respect to the funding liabilities under the Plan. On January 30, 2004, the Bankruptcy Court entered an order authorizing termination, additional funding and other actions necessary to effect the relief requested. Pursuant to the Bankruptcy Court order, any contributions to the Plan are

subject to the prior receipt of a favorable determination by the Internal Revenue Service that the Plan is tax-qualified as of the date of termination. In addition, the Bankruptcy Court order provides that the rights of PBGC and others to assert that their filed claims have not been released or adjudicated as a result of the Bankruptcy order and Enron and all other interested parties retained the right to assert that such claims had been adjudicated or released.

Northern Border Pipeline advises that Enron management has informed Northern Border Pipeline that it will seek funding contributions from each member of its ERISA controlled group of corporations that employs or employed individuals who are, or were, covered under the Plan. Northern Border Pipeline further advises that Northern Plains has advised Northern Border Pipeline that Northern Plains is a member of a controlled group of corporations covered under the Plan and that an amount of approximately \$3.1 million has been estimated for Northern Border Pipeline's share of Northern Plains' proportionate share of the up to \$200 million estimated termination costs authorized by the Bankruptcy Court order. Under the operating agreement with Northern Plains, these increased costs may be Northern Border Pipeline's responsibility. Northern Border Pipeline has accrued this amount to satisfy claims of reimbursement for these termination costs. While the final amounts have not been determined, Northern Border Pipeline advises that it believes this accrual is adequate to cover the allocation of these costs to Northern Border Pipeline.

Enron is the grantor of the Enron Gas Pipeline Employee Benefit Trust (the Trust), which when taken together with the Enron Corp. Medical Plan for Inactive Participants (the Medical Plan) constitutes a "voluntary employees' beneficiary association" or "VEBA" under Section 501(c)(9) of the Internal Revenue Code. In October 2002, Northern Plains was advised that Enron had notified the committee that has administrative and fiduciary oversight related to the Trust and the Medical Plan, that Enron had made the determination to begin necessary steps to partition the assets of the Trust and the related liabilities of the Medical Plan among all of the participating employers of the Trust. The Trust was established as a regulatory requirement for inclusion of certain costs for post-employment medical benefits in the rates established for the affected pipelines, including Northern Border Pipeline. Enron requested the enrolled actuary to prepare an analysis and recommendation for the allocation of the Trust's assets and associated liabilities among all the participating employers. On July 22, 2003, Enron sought approval of the Bankruptcy Court to terminate the Trust and to distribute its assets among certain identified pipeline companies, one being Northern Plains. If Enron's relief as requested is granted, Northern Plains would assume retiree benefit liabilities, estimated as of June 30, 2002, of \$1.9 million with an asset allocation of \$0.8 million. An objection to the motion has been filed and no hearing date has been set. An additional actuary has been engaged by Enron to review the analysis and recommendations for allocations. There can be no assurances that the allocation of liabilities and assets will not change from those set forth in the motion.

Enron's filing for bankruptcy protection and related developments have had other impacts on Northern Border Pipeline's business and management. Numerous shareholder and employee class action lawsuits have been initiated against Enron, its former independent accountants, legal advisors, executives, and board members. Enron has received several requests for information from different federal and state agencies, including the FERC, and committees of the United States House of Representatives and Senate. Some of the information requested from Enron may include information about Northern Border Pipeline. While Northern Border Pipeline has not been subject to these investigations or lawsuits, it is possible that in the documentation production by Enron and others, confidential proprietary or commercially sensitive information concerning Northern Border Pipeline may have been produced. It is also possible that some of this information may be made available to the public.

While Northern Plains and Pan Border have not filed for Chapter 11 bankruptcy protection, their stock is owned by Enron, which is in bankruptcy. As noted above, Enron could sell its interest in Northern Plains and/or Pan Border, or take other action with respect to their investment in Northern Border Pipeline. Enron could also cause Northern Plains and Pan Border to file for bankruptcy protection. In its Form 10-K for the year ended December 31, 2003, Northern Border Pipeline states that it has had no indication from Enron that it intends to cause such companies to file for bankruptcy protection.

Northern Border Pipeline is managed by a four-member management committee. Three representatives are designated by Northern Border Partners, with each of its general partners selecting one representative, and one representative is designated by TC PipeLines. The vote among Northern Border Partners' representatives is in proportion to their general partner interests in Northern Border Partners. As a result, the 70% voting interest of Northern Border Partners' three representatives is allocated 35%, 22.75% and 12.25% among Northern Plains, Pan Border and Northwest Border, respectively. If Enron were to sell the stock of Northern Plains and Pan Border, the purchaser would have the right to appoint a majority of Northern Border Pipeline's management committee and control Northern Border Pipeline's activities, except for those activities requiring a unanimous vote which include changes to Northern Border Pipeline's cash distribution policy, certain expansions and extensions of the pipeline, some transfers of general partner interests and settlement of rate cases.

If Northern Plains and Pan Border were to file for bankruptcy protection, Northern Border Partners' Partnership Agreement provides that they would automatically be deemed to have withdrawn as general partners of Northern Border Partners. It is possible that the enforceability of the automatic withdrawal provisions in this partnership agreement may be challenged. The success and impact of a challenge are unknown. Upon the occurrence of such an event of withdrawal, the remaining general partner of Northern Border Partners would have the right to purchase the withdrawing partners' general partnership interests. If the remaining general partner does not purchase such general partnership interests, the limited partners of Northern Border Partners would have the right to elect new general partners. In the event that the remaining general partner does not elect to purchase the general partner interests or a successor is not so elected by the limited partners, then the partnership shall be dissolved. In either event, the party acquiring the general partner interests currently held by Northern Plains and Pan Border would have the right to appoint a majority of Northern Border Pipeline's management committee and control Northern Border Pipeline's activities, except for those activities requiring a unanimous vote.

Northern Plains also serves as Northern Border Pipeline's operator. If Northern Plains were to file for bankruptcy protection, it could potentially be removed as operator. Northern Border Pipeline's credit agreement provides that it would be an event of default thereunder if Northern Plains were replaced as operator without the consent of the lenders.

Other than the items identified above, Northern Border Pipeline states in its Form 10-K for the year ended December 31, 2003 that it is not aware of any claims made against it that arise out of the Enron bankruptcy cases. Northern Border Pipeline continues to monitor developments at Enron, to assess the impact on Northern Border Pipeline of its existing agreements and relationships with Enron and its subsidiaries, and to take appropriate action to protect its interests.

#### **Public Utility Holding Company Act (PUHCA) Regulation**

Besides its ownership in Northern Plains and Pan Border, all of the common stock of Portland General Electric Company (PGE) is owned by Enron. As the owner of PGE's common stock, Enron is a holding company for purposes of the Public Utility Holding Company Act of 1935 (PUHCA). Following Enron's acquisition of PGE in 1997, Enron annually filed a statement claiming an exemption from all provisions of PUHCA (except the provision which addresses the acquisition of public utility company affiliates) under Section 3(a)(1). Due to Enron's bankruptcy filing in December 2001, Enron was no longer able to provide necessary financial information needed to file the exemption statement. As a result, in February 2002, Enron applied to the SEC for an order of exemption under Sections 3(a)(1), 3(a)(3) and 3(a)(5).

On December 29, 2003, the SEC issued an order denying the two applications filed by Enron seeking exemption as a public utility holding company under Sections 3(a)(1), 3(a)(3) and 3(a)(5) of PUHCA. The SEC order found, relative to the application under Section 3(a)(1), that Enron's subsidiary, PGE, is not predominantly and substantially intrastate in character and does not carry on business substantially in a single state. Relative to the application under Sections 3(a)(3) and 3(a)(5), the SEC found that Enron was unable to establish that it is only incidentally a holding company and that it derives no material part of its income from an electric utility subsidiary.

On December 31, 2003, Enron and other related entities filed an application under Section 3(a)(4) of PUHCA (the 3(a)(4) Application). This application claims, for each of the applicants, an exemption as a public utility holding company based on the temporary nature of the applicants' current or proposed interest in PGE under the Chapter 11 Plan filed by Enron and certain of its subsidiaries. By SEC order entered January 30, 2004, the hearing date on Enron's pending application for exemption under PUHCA was postponed until February 9, 2004 and by SEC order entered February 6, 2004, the hearing date was postponed until further notice. On March 9, 2004, pursuant to an offer of settlement that had been previously made to the SEC, Enron withdrew the 3(a)(4) Application and registered as a holding company under PUHCA. Immediately after Enron registered, the SEC issued two orders, one granting Enron and its subsidiaries authority to undertake certain transactions without further authorization from the SEC under PUHCA (referred to as the Omnibus Order) and the other approving Enron's Fifth Amended Bankruptcy Plan (referred to as the Plan Order).

The Omnibus Order authorizes, among other items, certain transactions specific to Northern Border Partners, L.P. and its subsidiaries, including authority for Northern Border Partners and Northern Border Pipeline to declare and pay distributions out of capital. Further, the Omnibus Order authorizes Northern Border Partners to invest as much as an additional \$1 billion in natural gas gathering, processing, storage and transportation assets and to issue and sell debt and equity securities as may be required to fund such investments or acquisitions. The authorizations are effective until the earlier of the deregistration of Enron under PUHCA or July 31, 2005. Northern Border Pipeline advises that it believes that the authority relating to Northern Border Partners and its affiliates in the Omnibus Order minimizes the likelihood that its business will be adversely impacted by Enron's registration under PUHCA.

However, PUHCA imposes a number of restrictions on the operations of a registered holding company and its subsidiaries within the registered holding company system that can become materially more expensive and cumbersome than operations by companies that are not subject to, or exempt, from PUHCA. As a subsidiary of a registered holding company, Northern Border Pipeline is subject to regulation by the SEC with respect to the acquisition of the securities of public utilities; the acquisition of assets and interests in any other business, declaration and payment of certain cash distributions; intra-system borrowings or indemnifications; sales, services or construction transactions with other holding company system companies; and the issuance of debt or equity securities, among other matters. To the extent those regulated activities are not approved under the Omnibus Order or otherwise exempt under various rules and regulations promulgated under PUHCA, Northern Border Pipeline advises that it would need to seek additional approvals from the SEC. At this time, Northern Border Pipeline advises that it does not believe there is a need for it to seek any additional authorizations from the SEC in order to conduct its operations. Nevertheless, Northern Border Pipeline advises that there can be no assurance that PUHCA will not have an adverse impact on its operations as a result of Enron's registration as a holding company.

While TC PipeLines currently does not anticipate that the registration of Enron as a holding company under PUHCA will have a material impact on its ability to conduct its operations or to meet its obligations, further regulatory developments could adversely impact Northern Border Pipeline and therefore have an indirect adverse impact on TC PipeLines' operations.

## **RESULTS OF OPERATIONS OF TUSCARORA GAS TRANSMISSION COMPANY**

*In the following discussion of the results of Tuscarora, all amounts represent 100% of the operations of Tuscarora, in which the Partnership has held a 49% interest since September 1, 2000.*

### **Overview**

Tuscarora is a Nevada general partnership formed in 1993. Its general partners are TC Tuscarora Intermediate Limited Partnership, a direct subsidiary of TC PipeLines, which holds a 49% general partner interest, Tuscarora Gas Pipeline Co., a wholly owned subsidiary of Sierra Pacific Resources, which holds a 50% general partner interest and TCPL Tuscarora Ltd., an indirect wholly owned subsidiary of TransCanada, which holds a 1% general partner interest.

The management of Tuscarora is overseen by a management committee that determines the policies of, has authority over the affairs of, and approves the actions of Tuscarora. The management committee participates in the management of the construction, maintenance and operation of the Tuscarora pipeline system.

Tuscarora owns a 240-mile, 20-inch diameter, United States interstate pipeline system that originates at an interconnection point with facilities of Gas Transmission Northwest Corporation (GTN) near Malin, Oregon and runs southeast through northeastern California and northwestern Nevada. The Tuscarora pipeline system terminates near Wadsworth, Nevada. Deliveries are also made directly to the local gas distribution system of Sierra Pacific Resources. Along its route, deliveries are made in Oregon, northern California and northwestern Nevada.

The Tuscarora pipeline system was constructed in 1995 and was placed into service in December 1995. In January 2001, Tuscarora completed construction of the Hungry Valley lateral, a 14-mile, 16-inch pipeline extension that serves as Tuscarora's second connection into Reno, Nevada. On December 1, 2002, Tuscarora completed and placed into service another expansion of its pipeline system. The 2002 Tuscarora expansion consisted of two compressor stations and an 11-mile pipeline extension from the previous terminus of the Tuscarora pipeline system near Reno, Nevada to Wadsworth, Nevada. The expansion increased Tuscarora's contracted capacity from 127 mmcf to approximately 180 mmcf. The new capacity is contracted under long-term firm transportation contracts ranging from ten to fifteen years.

#### **Critical Accounting Policy**

Tuscarora's accounting policies conform to SFAS No. 71, "Accounting for the Effects of Certain Types of Regulation." Accordingly, certain assets that result from the regulated ratemaking process are recorded that would not be recorded under generally accepted accounting principles for nonregulated entities.

#### **Year Ended December 31, 2003 Compared to the Year Ended December 31, 2002**

Tuscarora's net income increased \$1.4 million, or 13%, to \$11.8 million for the year ended December 31, 2003, compared to \$10.4 million in 2002. This increase is primarily due to higher revenues, partially offset by higher costs and expenses and higher depreciation expense.

Revenues generated by Tuscarora increased \$6.6 million, or 29%, to \$29.7 million for the year ended December 31, 2003, compared to \$23.1 million for 2002. This increase is primarily due to incremental revenues generated from new transportation contracts, including those related to Tuscarora's expansion facilities that were placed into service December 1, 2002.

Costs and expenses incurred by Tuscarora increased \$2.2 million, or 79%, to \$5.0 million for the year ended December 31, 2003, compared to \$2.8 million for the year ended December 31, 2002. This increase is primarily due to the higher costs of operating two new compressor stations that were placed into service December 1, 2002.

Depreciation recorded by Tuscarora increased \$1.5 million, or 31%, to \$6.4 million for the year ended December 31, 2003, compared to \$4.9 million for the prior year. The increase reflects the larger asset base resulting from the expansion in December 2002.

Financial charges recorded by Tuscarora increased \$0.8 million, or 14%, to \$6.5 million for the year ended December 31, 2003, compared to \$5.7 million for 2002. This increase is due to the fact that no interest was capitalized in 2003. In 2002, financial charges were lower due to the capitalization of interest expense related to funds used for the expansion.

Tuscarora recorded other income of zero and \$0.7 million for the years ended December 31, 2003 and 2002, respectively. This decrease is primarily due to the allowance recorded in 2002 related to equity funds used during construction of the expansion. No such allowance was recorded in 2003.

#### **Year Ended December 31, 2002 Compared to the Year Ended December 31, 2001**

Tuscarora's net income increased \$2.1 million, or 25%, to \$10.4 million for the year ended December 31, 2002, compared to \$8.3 million in 2001. This increase is primarily due to higher revenues, lower financial charges and higher other income.

Revenues generated by Tuscarora increased \$1.8 million, or 8%, to \$23.1 million for the year ended December 31, 2002, compared to \$21.3 million for 2001. This increase is primarily due to incremental revenues being generated from new transportation contracts, including those related to Tuscarora's expansion facilities which were placed into service December 1, 2002.

Costs and expenses incurred by Tuscarora totaled \$2.8 million and \$2.6 million for the years ended December 31, 2002 and 2001, respectively.

Tuscarora recorded depreciation of \$4.9 million and \$4.6 million for the years ended December 31, 2002 and 2001, respectively.

Tuscarora recorded financial charges of \$5.7 million and \$6.1 million for the years ended December 31, 2002 and 2001, respectively. This decrease is due to the capitalization of interest expense in 2002 related to funds being used for the expansion.

Tuscarora recorded other income of \$0.7 million and \$0.3 million for the years ended December 31, 2002 and 2001, respectively. This increase is primarily due to a higher allowance recorded in 2002 related to equity funds used during construction of the expansion compared to the allowance recorded in 2001 related to the Hungry Valley lateral project.

## LIQUIDITY AND CAPITAL RESOURCES OF TUSCARORA GAS TRANSMISSION COMPANY

### Cash Distribution Policy of Tuscarora

In September 2000, Tuscarora adopted a cash distribution policy that became effective January 1, 2001. Under the terms of the cash distribution policy and at the discretion of the Tuscarora Management Committee, Tuscarora makes quarterly cash distributions to its general partners in accordance with their respective general partner interests. Cash distributions will generally be computed as the sum of Tuscarora's net income before taxes and depreciation and amortization, less amounts required for debt repayments, net of refinancings, maintenance capital expenditures, certain non-cash items, and any cash reserves deemed necessary by the Tuscarora management committee. Cash distributions will be computed at the end of each calendar quarter and the distribution will be made on or before the last day of the month following the quarter end.

### Summary of Certain Contractual Obligations

| Payments Due by Period         | Total          | Less Than<br>1 Year | 1-3 Years      | 4-5 Years      | After<br>5 Years |
|--------------------------------|----------------|---------------------|----------------|----------------|------------------|
| <i>(in millions)</i>           |                |                     |                |                |                  |
| Series A Senior Notes due 2010 | \$ 68.9        | \$ 3.6              | \$ 7.3         | \$ 6.7         | \$ 51.3          |
| Series B Senior Notes due 2010 | 7.1            | 0.3                 | 0.8            | 1.0            | 5.0              |
| Series C Senior Notes due 2012 | 9.4            | 0.7                 | 1.5            | 1.7            | 5.5              |
| Operating Leases               | 0.5            | 0.1                 | 0.2            | 0.2            | —                |
| Commitments <sup>(1)</sup>     | 4.6            | 1.2                 | 2.3            | 1.1            | —                |
| <b>Total</b>                   | <b>\$ 90.5</b> | <b>\$ 5.9</b>       | <b>\$ 12.1</b> | <b>\$ 10.7</b> | <b>\$ 61.8</b>   |

(1) Tuscarora is party to a contract with a third party for maintenance services on certain components of its pipeline-related equipment. The contract expires in November 2007.

### Debt and Credit Facilities

On March 15, 2002, Tuscarora issued Series C Senior Secured Notes in the amount of \$10.0 million. These notes bear interest at 6.89% and are due in 2012. The proceeds from these notes were used to finance the construction of Tuscarora's expansion facilities.

On January 4, 2002, Tuscarora entered into a credit agreement with Bank One for a \$5.0 million, 364-day revolving credit facility (Credit Facility), which bears interest at either LIBOR plus 1% or the prime rate. As at December 31, 2002, the balance outstanding on this facility was \$4.6 million. The Credit Facility expired on January 3, 2003, where upon Tuscarora elected not to renew this facility and repaid the outstanding balance.

In November 2001 and January 2002, Tuscarora entered into forward starting interest rate swaps with notional amounts of \$10.0 million and \$8.0 million, respectively, related to the planned issuance of Series C Senior Secured Notes. The swaps were settled on February 15, 2002 for net proceeds of approximately \$0.2 million. The swaps were entered into to hedge the fluctuations in treasury rates and spreads between the execution date of the swaps and the issuance date of the Series C Senior Secured Notes.

Short-term liquidity needs will be met by operating cash flows. Long-term capital needs may be met through the ability to issue long-term indebtedness.

#### **Cash Flows from Operating Activities**

Cash flows provided by operating activities increased \$1.4 million, or 9%, to \$16.4 million for the year ended December 31, 2003, compared to \$15.0 million for 2002. This increase is the result of increased earnings during 2003, as well as decreased working capital during the same period.

Cash flows provided by operating activities increased \$1.6 million, or 12%, to \$15.0 million for the year ended December 31, 2002 compared to \$13.4 million for 2001. This increase is the result of increased earnings during 2002, partially offset by increased working capital during the same period.

#### **Cash Flows from Investing Activities**

Capital expenditures of \$1.3 million for the year ended December 31, 2003 primarily related to the expansion that went into service December 1, 2002. Capital expenditures of \$31.9 million for the year ended December 31, 2002 included \$31.6 million for Tuscarora's expansion.

Capital expenditures of \$10.2 million for the year ended December 31, 2001 included \$4.7 million for Tuscarora's expansion and \$2.4 million related to the construction of the Hungry Valley lateral.

Total capital expenditures for 2004 are estimated to be \$1.8 million of which approximately \$1.6 million relates to a planned expansion in 2005. The remainder relates to renewals and replacements of existing facilities. Tuscarora anticipates funding its 2004 capital expenditures by using a combination of partner contributions and operating cash flows.

#### **Cash Flows from Financing Activities**

Cash flows used in financing activities were \$14.1 million for the year ended December 31, 2003, compared to cash flows from financing activities of \$16.5 million for the year ended December 31, 2002.

In 2003, Tuscarora repaid its Credit Facility which had \$4.6 million outstanding at the beginning of the year. In 2002, Tuscarora received net proceeds of \$10.0 million from the issuance of its Series C Senior Secured Notes. The proceeds from these notes were used to finance the construction of Tuscarora's expansion facilities. Also, in 2002, Tuscarora drew on its Credit Facility to partially fund its 2002 expansion. At December 31, 2002, \$4.6 million was outstanding on the Credit Facility.

For the years ended December 31, 2003 and 2002 Tuscarora made debt repayments of \$4.7 million and \$4.1 million, respectively.

Tuscarora received contributions from its partners of \$10.0 million and \$15.5 million for the years ended December 31, 2003 and 2002, respectively. These contributions were used to fund the construction of Tuscarora's expansion facilities.

Tuscarora paid cash distributions of \$14.2 million and \$9.3 million to its general partners for the years ended December 31, 2003 and 2002, respectively.

Cash flows used in financing activities were \$9.3 million in 2001. In 2001, Tuscarora made debt repayments of \$4.2 million and paid cash distributions of \$5.0 million. Tuscarora's 2001 cash distributions represent three quarterly payments due to the timing of the implementation of Tuscarora's cash distribution policy.



### Sierra Pacific Resources

Sierra Pacific Resources, the parent company to Sierra Pacific Power Company (Sierra Pacific Power), Tuscarora's largest shipper with approximately 68% of contracted capacity through 2015, issued a press release on August 28, 2003 and filed a Current Report on Form 8-K with the SEC advising that the federal bankruptcy court judge overseeing the bankruptcy case of Enron Power Marketing Inc. (Enron Power Marketing) rendered a decision in the lawsuit filed by Enron Power Marketing in its bankruptcy case asserting claims for damages related to the termination of its power supply agreements with Nevada Power Company (Nevada Power) and Sierra Pacific Power (together, the Utilities). The bankruptcy court judge granted Enron Power Marketing's motion for summary judgment with respect to Enron Power Marketing's claims against Nevada Power and Sierra Pacific Power for approximately \$235 million and \$102 million, respectively, of liquidated damages, for power supply contracts terminated by Enron Power Marketing in May 2002. The bankruptcy court judge also dismissed the Utilities' counter claims against Enron Power Marketing, dismissed the Utilities' counter claims against Enron Corp., the parent of Enron Power Marketing, and denied the Utilities' motion to dismiss or stay the proceedings pending the final outcome of their FERC proceedings against Enron Power Marketing. In addition to the claims for termination payments described above, Nevada Power and Sierra Pacific Power had previously deposited approximately \$17.7 million and \$6.7 million, respectively, into an escrow account for energy delivered by Enron Power Marketing to each of Nevada Power and Sierra Pacific Power in April 2002, for which the Utilities had not paid.

Sierra Pacific Power to date remains current on its shipping contracts with Tuscarora.

### NEW ACCOUNTING PRONOUNCEMENTS

During 2003, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards (SFAS) No. 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities," SFAS No. 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity" and Interpretation (FIN) No. 46, "Consolidation of Variable Interest Entities," and reissued SFAS No. 132, "Employers' Disclosures about Pensions and Other Postretirement Benefits."

SFAS No. 149 amends and clarifies accounting for derivative instruments and hedging activities under SFAS No. 133. As at December 31, 2003, TC PipeLines does not engage in any hedging activities and is not affected by the changes resulting from this standard.

SFAS No. 150 establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. This standard is effective for financial instruments entered into or modified after May 31, 2003. As at December 31, 2003, TC PipeLines has not entered into any financial instruments that would be affected by this standard and, therefore, is not affected by the changes resulting from this standard.

FIN No. 46 is an interpretation of Accounting Research Bulletin No. 51 and provides guidance on the identification of, and financial reporting for, certain entities over which control is achieved through financial controls (variable interests) rather than voting rights. Such entities are referred to as variable interest entities. The holder of the majority of an entity's variable interests will be required to consolidate the variable interest entity. Neither Northern Border Pipeline nor Tuscarora qualifies as a variable interest entity of the Partnership and, therefore, the application of this Interpretation does not impact the financial statements of TC PipeLines.

SFAS No. 132 (Revised) revises employers' disclosures about pension plans and other postretirement benefits plans. It does not change the measurement or recognition of those plans in earlier Statements or the disclosure requirements contained in the original SFAS No. 132. This revision requires additional disclosures about the assets, obligations, cash flows, and net periodic benefit cost of defined benefit pension plans and other defined benefit postretirement plans. As at December 31, 2003, TC PipeLines does not have a pension plan or other postretirement benefit plans and is not affected by the changes resulting from this standard.

## RISK FACTORS AND CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING INFORMATION

### Cautionary Statement Regarding Forward-Looking Information

A number of statements made by TC PipeLines, LP, in this Form 10-K filing made with the SEC, are forward-looking and relate to, among other things, anticipated financial performance, business prospects, strategies, market forces and commitments. Much of this information appears in “Management’s Discussion and Analysis of Financial Condition and Results of Operations” found herein. All forward-looking statements are based on the Partnership’s beliefs as well as assumptions made by and information currently available to the Partnership. Words such as “anticipate,” “believe,” “estimate,” “expect,” “plan,” “intend,” “forecast,” and similar expressions, identify forward-looking statements within the meaning of the Private Securities Litigation Reform Act. By its nature, such forward-looking information is subject to various risks and uncertainties, which could cause TC PipeLines’ actual results and experience to differ materially from the anticipated results or other expectations expressed in this Form 10-K. Readers are cautioned not to place undue reliance on this forward-looking information, which is as of the date of this Form 10-K.

### Risk Factors

***TC PipeLines is dependent upon Northern Border Pipeline and Tuscarora and may not be able to generate sufficient cash from the distributions from each of Northern Border Pipeline and Tuscarora to pay the minimum quarterly distribution on the common units every quarter***

While TC PipeLines has a significant ownership interest in each of Northern Border Pipeline and Tuscarora, it does not control or operate either of these pipelines. The actual amount of cash TC PipeLines has available to pay the minimum quarterly distribution will depend upon numerous factors relating to each of Northern Border Pipeline’s and Tuscarora’s business, most of which are beyond the control of TC PipeLines or the general partner, including:

- the amount of cash distributed to TC PipeLines by each of Northern Border Pipeline and Tuscarora;
- the ability of Northern Border Pipeline to recontract capacity for maximum transportation rates as existing contracts terminate;
- the tariff and transportation charges collected by Northern Border Pipeline and Tuscarora for transportation services on their pipeline systems;
- increases in Northern Border Pipeline’s and Tuscarora’s operating and maintenance costs;
- payment defaults of shippers on Northern Border’s pipeline system and payment defaults of shippers on Tuscarora’s pipeline system;
- the amount of cash set aside and the adjustment in reserves made by the general partner at its discretion;
- the amount of cash required to be contributed by TC PipeLines to either Northern Border Pipeline or Tuscarora in the future;
- required principal and interest payments on TC PipeLines’ debt;
- the cost of acquisitions, including related debt service payments;
- TC PipeLines’ issuance of debt and equity securities;
- pipelines competing with Northern Border Pipeline and Tuscarora; and
- expansion costs related to these systems.

***Cash distributions are dependent primarily on TC PipeLines’ cash flow, financial reserves and working capital borrowings***

Cash distributions are not dependent solely on TC PipeLines’ profitability, which is affected by non-cash items. Therefore, TC PipeLines may make cash distributions during periods when losses are reported and may not make cash distributions during periods when profits are reported.

***Northern Border Pipeline’s and Tuscarora’s indebtedness may limit their ability to borrow additional funds, make distributions to TC PipeLines or capitalize on business opportunities***

Northern Border Pipeline is prohibited from making cash distributions during an event of default under its indebtedness. Provisions in Northern Border Pipeline’s indebtedness limit its ability to incur indebtedness and engage

in specific transactions which could reduce its ability to capitalize on business opportunities that arise in the course of its business. Tuscarora is prohibited from making cash distributions during an event of default under its indebtedness. Under Tuscarora's indebtedness, Tuscarora has granted a security interest in certain of its transportation contracts, which are available to noteholders during an event of default. Any future refinancing of Tuscarora's existing indebtedness or any new indebtedness could have similar or greater restrictions.

***If Northern Border Pipeline, as a subsidiary of Northern Border Partners, L.P. and Enron as defined under the Public Utility Holding Company Act (PUHCA), is unable to obtain an exemption from subsidiary status under PUHCA, it will become subject to regulation by the SEC***

The SEC would regulate the acquisition of assets and interests of Northern Border Pipeline, the declaration and payment of certain cash distributions; intra-system borrowings or indemnifications; sale, services or construction transactions with other holding system companies; the issuance of certain debt; equity securities and borrowings under credit facilities.

***If TC PipeLines is unable to make acquisitions on economically and operationally acceptable terms, either from third parties or TransCanada, TC PipeLines' future financial performance will be limited to participation in Northern Border Pipeline and Tuscarora***

The Partnership may not be able to:

- identify attractive acquisition candidates in the future;
- acquire assets on economically acceptable terms;
- make acquisitions that will not be dilutive to earnings and operating surplus; or
- incur additional debt to finance an acquisition without affecting its ability to make distributions to unitholders.

Future acquisitions may involve the expenditure of significant funds. Depending upon the nature, size and timing of future acquisitions, TC PipeLines may be required to secure additional financing. Additional financing may not be available to TC PipeLines on acceptable terms.

In addition, TC PipeLines may not be able to acquire any more of TransCanada's United States pipeline assets. Substantially all of TransCanada's United States pipeline assets are subject to restrictions on sale, such as rights of first refusal. Under a right of first refusal another party, usually a partner, has a right to acquire the particular asset at the price offered. Only if the other party declines to purchase the asset at the price offered could TransCanada sell it to TC PipeLines.

***Majority control of the Northern Border Pipeline management committee by affiliates of Enron may limit TC PipeLines' ability to influence Northern Border Pipeline***

TC PipeLines owns a 30% general partner interest in Northern Border Pipeline. The remaining 70% general partner interest in Northern Border Pipeline is owned by Northern Border Partners, a publicly traded limited partnership. The general partners of Northern Border Partners are Northern Plains and Pan Border, both subsidiaries of Enron, and Northwest Border, a subsidiary of TransCanada. Except as to any matters requiring unanimity, such as significant expansions or extensions to the pipeline system, the acceptance of rate cases and changes to, or suspensions of, the cash distribution policy, management committee members designated by subsidiaries of Enron have the voting power to approve a particular matter requiring a majority vote despite the fact that TC PipeLines' representative may vote against the project or matter. Conversely, with respect to any matter requiring a majority vote, management committee members designated by subsidiaries of Enron may disapprove of a particular matter despite the fact that TC PipeLines' representative may vote in favor of that matter.

***Northern Border Pipeline and Tuscarora are extensively regulated by the FERC***

If the FERC requires that Northern Border Pipeline's or Tuscarora's tariff be changed, Northern Border Pipeline's or Tuscarora's respective cash flows may be adversely affected.

Northern Border Pipeline and Tuscarora are subject to extensive regulation by the FERC. The FERC's regulatory authority extends to matters including:

- transportation of natural gas;
- rates and charges;
- construction of new facilities;
- acquisitions, extension or abandonment of services and facilities;
- accounts and records;
- depreciation and amortization policies; and
- operating terms and conditions of service.

Given the extent of regulation by the FERC and potential changes to regulations, the Partnership cannot give assurance regarding:

- the likely federal regulations under which Northern Border Pipeline or Tuscarora will operate in the future;
- the effect that regulation will have on Northern Border Pipeline's, Tuscarora's or the Partnership's financial positions, results of operations and cash flows; or
- whether the Partnership's cash flow will be adequate to make distributions to unitholders.

Northern Border Pipeline's ability to file for an increase of its rates before November 2005 to recover increases in most types of costs has been substantially eliminated by the settlement of its last rate case.

***If Northern Border Pipeline or Tuscarora do not maintain or increase their respective rate bases by successfully completing FERC-approved projects, the amount of revenue attributable to the return on the rate base they collect from their shippers will decrease over time***

The Northern Border and Tuscarora pipeline systems are generally allowed to collect from their customers a return on their assets or "rate base" as reflected in their financial records as well as recover that rate base through depreciation. The amount they may collect from customers decreases as the rate base declines as a result of, among other things, depreciation and amortization. In order to avoid a reduction in the level of cash available for distributions to its partners based on its current FERC-approved tariff, each of these pipelines must maintain or increase its rate base through projects that maintain or add to existing pipeline facilities. These projects will depend upon many factors including:

- sufficient demand for natural gas;
- an adequate supply of proved natural gas reserves;
- available capacity on pipelines that connect with these pipelines;
- the execution of natural gas transportation contracts;
- the approval of any expansion or extension of the pipeline systems by their respective management committees, or in some cases, a ruling from an arbitrator;
- obtaining financing for these projects; and
- receipt and acceptance of necessary regulatory approvals.

Northern Border Pipeline's and Tuscarora's ability to complete these projects is also dependent on numerous business, economic, regulatory, competitive and political uncertainties beyond its control, and neither Northern Border Pipeline nor Tuscarora may be able to complete these projects.

***If any shipper fails to perform its contractual obligations, Northern Border Pipeline's or Tuscarora's respective cash flows and financial condition could be adversely impacted***

If any shipper fails to perform its contractual obligations, Northern Border Pipeline's or Tuscarora's cash flows and financial condition could be adversely impacted. As a result, the cash available for distribution by TC PipeLines to unitholders could be reduced.

As of December 31, 2003, the three largest shippers on the Northern Border pipeline system accounted for approximately 49% of contracted capacity, with one shipper, BP Canada Energy Marketing Corp. (Canada), being obligated for approximately 21%.

Sierra Pacific Power, a wholly owned subsidiary of Sierra Pacific Resources, is Tuscarora's largest shipper with firm contracts for 68.1% of its capacity. Sierra Pacific Resources and Sierra Pacific Power have below-investment grade credit ratings. While TC PipeLines has no current indication that Sierra Pacific Power is unable to meet its ongoing contractual obligations, TC PipeLines is unable to predict the future financial condition of Sierra Pacific Power and its long-term ability to meet its obligations under existing agreements.

***Northern Border Pipeline's ability to operate its pipeline on certain tribal lands will depend on its success in renegotiating its right-of-way rights on tribal lands within the Fort Peck Reservation***

Northern Border Pipeline's ability to operate the pipeline on certain tribal lands will depend on its success in renegotiating before 2011 its right-of-way rights on tribal lands within the Fort Peck Reservation. See Item 2. "Properties – Properties of Northern Border Pipeline Company." Northern Border Pipeline and the Tribes, through a mediation process, have held settlement discussions and have reached a settlement in principle on the pipeline right-of-way lease and taxation issues, subject to final documentation and necessary governmental approvals. If Northern Border Pipeline is unable to recover the additional costs of the proposed settlement in its future rates, it could have a material adverse impact on Northern Border Pipeline's results of operations.

***The long-term financial conditions of Northern Border Pipeline and Tuscarora and as a result, of TC PipeLines, are dependent on the continued availability of western Canadian natural gas for import into the United States***

The development of additional natural gas reserves requires significant capital expenditures by others for exploration and development drilling and the installation of production, gathering, storage, transportation and other facilities that permit natural gas to be produced and delivered to pipelines that interconnect with Northern Border's and Tuscarora's pipeline systems. Low prices for natural gas, regulatory limitations, or the lack of available capital for these projects could adversely affect the development of additional reserves and production, gathering, storage and pipeline transmission and import and export of natural gas supplies. Contracts covering approximately 30% of Northern Border Pipeline's capacity expire prior to November 2004. Northern Border Pipeline may not be able to replace these contracts with new long-term contracts providing similarly attractive economic terms. Substantially all of Tuscarora's capacity is contractually committed through 2015. If the availability of western Canadian natural gas were to decline over these periods, existing shippers on the Northern Border and Tuscarora pipeline systems may be unlikely to extend their contracts and Northern Border Pipeline and Tuscarora may be unable to find replacement shippers for lost capacity. Furthermore, additional natural gas reserves may not be developed in commercial quantities and in sufficient amounts to fill the capacities of each of the Northern Border or Tuscarora pipeline systems.

***Northern Border Pipeline's and Tuscarora's business depends in part on the level of demand for western Canadian natural gas in the markets the pipeline systems serve***

Northern Border Pipeline's and Tuscarora's business depends in part on the level of demand for western Canadian natural gas in the markets the pipeline systems serve. The volumes of natural gas delivered to these markets from other sources affect the demand for both western Canadian natural gas and the use of these pipeline systems. Demand for western Canadian natural gas also influences the ability and willingness of shippers to use the Northern Border and Tuscarora pipeline systems to meet the demand that these pipeline systems serve.

The Partnership cannot predict whether or how these or other factors will affect the demand for use of the Northern Border or Tuscarora pipeline systems. If either of these pipeline systems are used less over the long term, the Partnership may have lower revenues and less cash to distribute to its unitholders.

***Because of the highly competitive nature of the natural gas transmission business, Northern Border Pipeline and Tuscarora may not be able to maintain existing customers or acquire new customers when the current shipper contracts expire***

Other pipeline systems that transport natural gas serve the same markets served by the Northern Border and Tuscarora pipeline systems. As a result, Northern Border Pipeline and Tuscarora face competition from other pipeline systems.

Northern Border Pipeline may not be able to renew or replace expiring contracts. The renewal or replacement of the existing contracts with customers of Northern Border Pipeline depends on a number of factors beyond Northern Border Pipeline's control, including:

- the supply of natural gas in Canada and the United States;
- competition from alternative sources of supply in the United States;
- competition from other pipelines; and
- the price of, and demand for, natural gas in markets served by the Northern Border pipeline system.

Contracts covering approximately 30% of Northern Border Pipeline's capacity expire prior to November 2004. Northern Border Pipeline may not be able to replace these contracts with new long-term contracts providing similarly attractive terms.

Tuscarora competes in the northern Nevada natural gas transmission market with Paiute Pipeline Co., owned by Southwest Gas Co. of Las Vegas, Nevada. The Paiute pipeline interconnects with Northwest Pipeline Corp. at the Nevada-Idaho border and transports gas from British Columbia and the U.S. Rocky Mountain Basin to the northern Nevada market.

TransCanada's main pipeline systems transport natural gas from the same natural gas reserves in western Canada that are used by Northern Border Pipeline's and Tuscarora's customers. TransCanada is not prohibited from actively competing with Northern Border Pipeline for the transport of western Canadian natural gas.

***Northern Border Pipeline's and Tuscarora's operations are regulated by federal and state agencies responsible for environmental protection and operational safety***

TC PipeLines believes that these operations comply in all material respects with applicable environmental and safety regulations. However, risks of substantial costs and liabilities are inherent in pipeline operations and each of Northern Border Pipeline and Tuscarora may incur substantial costs and liabilities in the future as a result of stricter environmental and safety laws, regulations and enforcement policies and claims for personal or property damages resulting from Northern Border Pipeline's or Tuscarora's operations. If either Northern Border Pipeline or Tuscarora, as applicable, was not able to recover these costs, cash distributions to TC PipeLines' unitholders could be adversely affected.

Northern Border Pipeline's and Tuscarora's operations are subject to operational hazards and unforeseen interruptions, including natural disasters, adverse weather, accidents or other events beyond its control. A casualty occurrence might result in a loss of equipment or life, as well as injury and extensive property or environmental damage.

***TC PipeLines does not have stand-alone management resources to operate without services provided by TransCanada***

TransCanada provides all of TC PipeLines' management resources. Further, TC PipeLines would not be able to evaluate potential acquisitions and successfully complete acquisitions without TransCanada's resources.

***The IRS could treat TC PipeLines as a corporation, which would substantially reduce the cash available for distribution to unitholders***

Current law may change so as to cause TC PipeLines to be taxable as a corporation for federal income tax purposes or otherwise to be subject to entity-level taxation. The partnership agreement provides that, if a law is enacted or existing law is modified or interpreted in a manner that subjects TC PipeLines to taxation as a corporation or otherwise subjects TC PipeLines to entity-level taxation for federal, state or local income tax purposes, then specified provisions of the

partnership agreement relating to distributions will be subject to change, including a decrease in distributions to reflect the impact of that law on TC PipeLines.

#### Item 7A. Quantitative and Qualitative Disclosures about Market Risk

TC PipeLines may be exposed to market risk through changes in interest rates. The Partnership does not have any foreign exchange risks. TC PipeLines' interest rate exposure results from its Revolving Credit Facility and its TransCanada Credit Facility, which are subject to variability in LIBOR interest rates. At December 31, 2003, TC PipeLines had \$5.5 million outstanding on its Revolving Credit Facility and zero outstanding on its TransCanada Credit Facility. If LIBOR interest rates change by one percent compared to the rates in effect as of December 31, 2003, annual interest expense would change by less than \$0.1 million. This amount has been determined by considering the impact of the hypothetical interest rates on variable rate borrowings outstanding as of December 31, 2003.

The Partnership's market risk sensitivity is also influenced by and reflects the same factors that influence Northern Border Pipeline.

Northern Border Pipeline's interest rate exposure results from variable rate borrowings from commercial banks. To mitigate potential fluctuations in interest rates, Northern Border Pipeline attempts to maintain a significant portion of its debt portfolio in fixed rate debt. Northern Border Pipeline also uses interest rate swaps as a means to manage interest expense by converting a portion of fixed rate debt into variable rate debt to take advantage of declining interest rates. At December 31, 2003, Northern Border Pipeline had \$356.0 million of variable rate debt outstanding, \$225.0 million of which was previously fixed rate debt but had been converted to variable rate debt through the use of interest rate swaps. For additional information on Northern Border Pipeline's debt obligations and derivative instruments, see Note 5 and Note 6 to Northern Border Pipeline's Financial Statements, included elsewhere in this report. As of December 31, 2003, approximately 56% of Northern Border Pipeline's debt portfolio was in fixed rate debt.

If average interest rates change by one percent compared to rates in effect as of December 31, 2003, annual interest expense would change by approximately \$3.6 million. This amount has been determined by considering the impact of the hypothetical interest rates on variable rate borrowings outstanding as of December 31, 2003.

#### Item 8. Financial Statements and Supplementary Data

The information required hereunder is included in this report as set forth in the "Index to Financial Statements" on page F-1.

#### Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

None.

#### Item 9A. Controls and Procedures

##### **Evaluation of Disclosure Controls and Procedures**

Based on their evaluation as of the end of the year covered by this annual report, the President and Chief Executive Officer and Chief Financial Officer of the general partner of the Partnership have concluded that the Partnership's disclosure controls and procedures referred to in paragraph 4(b) of their certifications included as exhibits to this report were effective.

## PART III

### Item 10. Directors and Executive Officers of the General Partner

TC PipeLines is a limited partnership and has no officers, directors or employees. Set forth below is certain information concerning the directors and officers of the general partner who manages the operations of TC PipeLines. Each director holds office for a one-year term or until his or her successor is earlier appointed. All officers of the general partner serve at the discretion of the Board of Directors of the general partner which is an indirect wholly owned subsidiary of TransCanada.

| Name                    | Age | Position with General Partner                   |
|-------------------------|-----|---|
| Ronald J. Turner        | 50  | President, Chief Executive Officer and Director |
| Russell K. Girling      | 41  | Chief Financial Officer and Director            |
| Robert A. Helman        | 69  | Independent Director                            |
| Jack F. Jenkins-Stark   | 52  | Independent Director                            |
| David L. Marshall       | 64  | Independent Director                            |
| Albrecht W.A. Bellstedt | 54  | Director  |
| Kristine L. Delkus      | 46  | Director  |
| Steven D. Becker        | 53  | Vice-President, Business Development            |
| Donald R. Marchand      | 41  | Vice-President and Treasurer                    |
| Ronald L. Cook          | 46  | Vice-President, Taxation                        |
| Max Feldman             | 55  | Vice-President                                  |
| Wendy L. Hanrahan       | 45  | Vice-President                                  |
| Amy W. Leong            | 36  | Controller                                      |
| Maryse C. St.-Laurent   | 44  | Secretary                                       |

Mr. Turner has been a director of the general partner since April 1999 and was appointed President and Chief Executive Officer in December 2000. Mr. Turner's principal occupation is Executive Vice-President, Gas Transmission of TransCanada, a position he has held since March 2003. From December 2000 until March 2003, Mr. Turner was Executive Vice-President, Operations and Engineering of TransCanada. From June 2000 until December 2000, Mr. Turner was Executive Vice-President, International of TransCanada. From April 2000 until June 2000, Mr. Turner was Senior Vice-President, International of TransCanada. From August 1999 until April 2000, Mr. Turner was President, International of TransCanada. From July 1998 until April 2000, Mr. Turner was Senior Vice-President of TransCanada.

Mr. Girling was appointed Chief Financial Officer and a director of the general partner in April 1999. Mr. Girling's principal occupation is Executive Vice-President, Corporate Development and Chief Financial Officer of TransCanada, a position he has held since March 2003. From June 2000 until March 2003, Mr. Girling was Executive Vice-President and Chief Financial Officer of TransCanada. From July 1999 until June 2000, Mr. Girling was Senior Vice-President and Chief Financial Officer of TransCanada. From January 1999 until July 1999, Mr. Girling was Vice-President, Finance of TransCanada. From July 1998 until January 1999, Mr. Girling was Executive Vice-President, Power (TransCanada Energy Ltd.).

Mr. Helman was appointed a director of the general partner in July 1999. Mr. Helman has been a partner of Mayer, Brown, Rowe & Maw LLP (law firm) since 1967. Mayer, Brown, Rowe & Maw LLP provides legal services on U.S. related matters to TransCanada, the parent of the general partner. In the first half of 2002, Mayer, Brown, Rowe & Maw LLP provided limited legal services to the general partner on behalf of the Partnership solely relating to matters arising from Enron's voluntary petition for bankruptcy protection. Mr. Helman did not participate, nor was he consulted in the provision of such services. Further, Mayer, Brown, Rowe & Maw LLP no longer provides such services to the Partnership. Mr. Helman serves as a director of Northern Trust Corporation and The Northern Trust Company.



Mr. Jenkins-Stark was appointed a director of the general partner in July 1999. Mr. Jenkins-Stark is currently Vice-President, Business Operations and Technology at Itron Inc. (a manufacturer of automated meter reading technology and a developer of energy management software), a position he has held since January 2004. In March 2003, Mr. Jenkins-Stark was named a Managing Director at Itron following the purchase of Silicon Energy Corp. (internet-based energy and data management software) by Itron. Prior to the acquisition, Mr. Jenkins-Stark was Chief Financial Officer of Silicon Energy, a position he held from April 2000 to March 2003. From December 1998 until April 2000, Mr. Jenkins-Stark was Senior Vice-President and Chief Financial Officer of GATX Capital (commercial finance). From September 1998 until December 1998, Mr. Jenkins-Stark was Senior Vice-President, Finance of GATX Capital.

Mr. Marshall was appointed a director of the general partner in July 1999. Mr. Marshall was Vice-Chairman of The Brinks Company (diversified energy, security and transportation services firm) from 1994 until 1998.

Mr. Bellstedt was appointed a director of the general partner in December 2001. Mr. Bellstedt's principal occupation is Executive Vice-President, Law and General Counsel of TransCanada, a position he has held since June 2000. From April 2000 until June 2000, Mr. Bellstedt was Senior Vice-President, Law and General Counsel of TransCanada. From August 1999 until April 2000, Mr. Bellstedt was Senior Vice-President, Law and Administration of TransCanada. From February 1999 until August 1999, Mr. Bellstedt was Senior Vice-President, Law and Chief Compliance Officer of TransCanada. Prior to February 1999, Mr. Bellstedt was a senior partner of Fraser Milner, a Canadian law firm.

Ms. Delkus was appointed a director of the general partner in November 2003. Ms. Delkus' principal occupation is Vice-President, Law, Power and Regulatory of TransCanada, a position she has held since July 2001. From July 2000 to July 2001, Ms. Delkus was Vice-President, Law, Trading & Business Development. From March 1997 to July 2000, Ms. Delkus was Senior Legal Counsel, U.S. Regulatory Law.

Mr. Becker was appointed Vice-President, Business Development of the general partner in September 2003. Mr. Becker's principal occupation is Vice-President, Gas Development of TransCanada, a position he has held since April 2003. From 1999 until April 2003, Mr. Becker was Vice-President, Market Development, and Vice-President, Gas Strategy.

Mr. Marchand was appointed Vice-President and Treasurer of the general partner in October 1999. Mr. Marchand's principal occupation is Vice-President, Finance and Treasurer of TransCanada, a position he has held since September 1999. From January 1998 until September 1999, Mr. Marchand was Director, Finance of TransCanada.

Mr. Cook was appointed Vice-President, Taxation of the general partner in April 2002. Mr. Cook's principal occupation is Vice-President, Taxation of TransCanada, a position he has held since April 2002. From June 1997 to April 2002, Mr. Cook served as Director, Taxation of TransCanada.

Mr. Feldman was appointed Vice-President of the general partner in September 2003. Mr. Feldman's principal occupation is Vice-President, Gas Transmission West of TransCanada, a position he has held since April 2003. From June 2000 until April 2003, Mr. Feldman was Senior Vice-President, Customer, Sales and Service of TransCanada. From September 1999 until June 2000, Mr. Feldman was Senior Vice-President, Customer Sales and Service, Transmission Division of TransCanada. Prior to September 1999, Mr. Feldman held several Vice-President positions in the operations, customer service and marketing areas of TransCanada.

Ms. Hanrahan was appointed Vice-President of the general partner in September 2003. Ms. Hanrahan's principal occupation is Director, Planning, Evaluation and Rates of TransCanada, a position she has held since May 2003. From September 2001 until April 2003, Ms. Hanrahan was Director, Corporate Strategy of TransCanada. From July 1998 until August 2001, Ms. Hanrahan was Director, Financial Services of TransCanada.

Ms. Leong was appointed Controller of the general partner in September 2003. Ms. Leong's principal occupation is Manager, Gas Transmission Accounting of TransCanada, a position she has held since April 2003. From January 2000 until April 2003, Ms. Leong was Manager, Regulatory Accounting and Capital Accounting of TransCanada. From

February 1999 until January 2000, Ms. Leong was Manager, Corporate Planning of TransCanada. From May 1997 until February 1999, Ms. Leong was Coordinator, Budgeting and Forecasting of TransCanada.

Ms. St.-Laurent was appointed Secretary of the general partner in September 2003. Prior to her appointment, Ms. St.-Laurent acted as recording Secretary of the general partner since January 2001. Ms. St.-Laurent's principal occupation is Senior Legal Counsel, Corporate Secretarial Department of TransCanada, a position she has held since April 2001. From June 1997 until April 2001, Ms. St.-Laurent was Legal Counsel, Corporate Secretarial Department of TransCanada.

#### **Audit Committee Financial Expert**

The board of directors has determined that David L. Marshall and Jack Jenkins-Stark are “audit committee financial experts” and “independent” as defined under applicable SEC and Nasdaq Stock Market Corporate Governance rules. The board's affirmative determination for both David L. Marshall and Jack Jenkins-Stark was based on their education and extensive experience as chief financial officers for corporations that presented a breadth and level of complexity of accounting issues that are generally comparable to those of TC PipeLines.

#### **Code of Ethics**

TC PipeLines believes that director, management and employee honesty and integrity are important factors in ensuring good corporate governance. The employees of the general partner, as employees of TransCanada, are subject to TransCanada's code of business ethics. In addition, the general partner has adopted a code of business ethics for its President and Chief Executive Officer, Chief Financial Officer and Controller and one which applies to its independent directors, being the code of business ethics for directors. All codes are published on its website at [www.tcpipelineslp.com](http://www.tcpipelineslp.com). If any substantive amendments are made to the code for senior officers or if any waivers are granted, the amendment or waiver will be published on TC PipeLines' website or filed in a report on Form 8-K.

#### **Corporate Governance**

The audit committee has adopted a charter which specifically provides that it is responsible for the appointment, compensation, retention and oversight of the work of the independent public accountants engaged in preparing or issuing TC PipeLines' audit report, that the committee has the authority to engage independent counsel and other advisors as it determines necessary to carry out its duties and for the committee to be responsible for establishing procedures for the receipt, retention and treatment of complaints regarding accounting, internal accounting controls or auditing matters, including procedures for the confidential, anonymous submission by employees of the general partner concerns regarding questionable accounting or auditing matters. The committee has adopted TransCanada's Ethics help line in fulfillment of its responsibility to establish a confidential and anonymous whistle blowing process. The toll free Ethics Help-Line number and the audit committee's charter are published on TC PipeLines website at [www.tcpipelineslp.com](http://www.tcpipelineslp.com).

Mr. Robert Helman has served on the Audit Committee of the Board since July, 1999. Mr. Helman has advised the Board that he will be retiring from his directorship pending appointment of his successor.

#### **Section 16(a) Beneficial Ownership Reporting Compliance**

Section 16(a) of the Exchange Act requires the Partnership's directors and executive officers, and persons who own more than 10% of the common units, to file initial reports of ownership and reports of changes in ownership (Forms 3, 4, and 5) of the common units with the SEC and the Nasdaq Stock Market. Executive officers, directors and greater than 10% unitholders are required by SEC regulation to furnish the Partnership with copies of all such forms that they file.

Based solely upon a review of reports on Forms 3 and 4 and amendments thereto furnished to the Partnership during its most recent fiscal year and reports on Form 5 and amendments thereto furnished to the Partnership with respect to its most recent fiscal year, and written representations from officers and directors of the general partner that no Form 5

was required, the Partnership believes that all filing requirements applicable to its officers, directors and beneficial owners under Section 16(a) were complied with during the year ended December 31, 2003.

## Item 11. Executive Compensation

The following table summarizes certain information regarding the annual salary of Ronald J. Turner, President and Chief Executive Officer of the general partner of the Partnership, for the years ended December 31, 2003, 2002 and 2001 paid by TransCanada, parent company of the general partner. Mr. Turner is an employee of TransCanada. TC PipeLines reimburses TransCanada for the services contributed to its operations by Mr. Turner.

| Name and Principal Position                             | Year | Annual TransCanada Base Salary <sup>(1)</sup> |  |
|---|------|---|--|
|   |      | Canadian Dollars                              | United States Dollar Equivalent <sup>(2)</sup> |
| Ronald J. Turner, President and Chief Executive Officer | 2003 | 447,501                                       | 346,000  |
|   | 2002 | 436,254                                       | 276,000  |
|   | 2001 | 412,503                                       | 259,000  |

(1) Annualized base salary paid by TransCanada. Based on services provided, approximately 10% of this base salary is allocated to the Partnership.

(2) The compensation of the Chief Executive Officer of the general partner is paid by TransCanada in Canadian dollars. The United States dollar equivalents have been calculated using the applicable December 31, 2003, 2002 and 2001 noon buying rates of 0.7738, 0.6331 and 0.6279, respectively, as reported by the Bank of Canada.

Each director who is not an employee of TransCanada, the general partner or its affiliates (independent director) is entitled to a directors' retainer fee of \$15,000 per annum and an additional fee of \$2,000 per annum for each committee of the board of which he is Chair. These fees are paid by the Partnership on a semi-annual basis. Each independent director is also paid a fee of \$1,500 for attendance at each meeting of the Board of Directors and a fee of \$750 for attendance at each meeting of a committee of the Board. The Chair of the Audit Committee receives an additional \$375 per meeting for his additional duties as committee chair. The independent directors are reimbursed for out-of-pocket expenses incurred in the course of attending such meetings. Under a directors' compensation plan adopted effective July 19, 1999, each independent director receives 50% of his annual board retainer that is payable on the applicable date in the form of common units of the Partnership. The common units are purchased by the general partner on the open market and the number of common units purchased under the directors' compensation plan is based on the trading price of common units on the day preceding the applicable payment date.

As the Partnership does not have any employees, the Audit and Compensation Committee of the Board of Directors and subsequently the Board of Directors of the general partner of TC PipeLines, have not been called upon to make any determination with respect to the amount of compensation to be paid to the Partnership's President and CEO. The board does, however, approve the allocation of the salary of the President and CEO to the Partnership on an annual basis. The executive officers' salaries are determined on a competitive and market basis by TransCanada.

## Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Matters

The following table sets forth the beneficial ownership of the voting securities of the Partnership as of February 23, 2004 by the general partner's directors, officers and certain beneficial owners. Executive Officers of the general partner own shares of TransCanada, which in the aggregate amount to less than 1% of TransCanada's issued and outstanding shares. Other than as set forth below, no person is known by the general partner to own beneficially more than 5% of the voting securities of the Partnership.

| Name and Business Address  | Amount and Nature of Beneficial Ownership |                  |                    |                  |   |
|--|---|------------------|--------------------|------------------|---|
|  | Common Units                              |                  | Subordinated Units |                  | Percentage of Interest for all Units <sup>(1)</sup> |
|  | Number of Units                           | Percent of Class | Number of Units    | Percent of Class |   |
| TC PipeLines GP, Inc. <sup>(2) (3)</sup><br>450 1st Street SW<br>Calgary, Alberta T2P 5H1    | 1,872,870                                 | 11.3             | 936,436            | 100              | 16.1  |
| TransCan Northern Ltd. <sup>(2)</sup><br>450 1st Street SW<br>Calgary, Alberta T2P 5H1       | 2,800,000                                 | 16.9             | —                  | —                | 16.0  |
| Goldman Sachs Group Inc. <sup>(4)</sup><br>85 Broad Street<br>New York, New York 10004       | 1,446,848                                 | 8.7              | —                  | —                | 8.3   |
| Robert A. Helman <sup>(5)</sup><br>190 S. LaSalle Street<br>Chicago, Illinois 60603          | 10,979                                    | *                | —                  | —                | *   |
| Jack F. Jenkins-Stark <sup>(6)</sup><br>1010 Atlantic Avenue<br>Alameda, California 94501    | 2,979                                     | *                | —                  | —                | *   |
| David L. Marshall <sup>(7)</sup><br>450 1st Street SW<br>Calgary, Alberta T2P 5H1            | 2,579                                     | *                | —                  | —                | *   |
| Ronald J. Turner<br>450 1st Street SW<br>Calgary, Alberta T2P 5H1                            | —   | —                | —                  | —                | —   |
| <b>Directors and Executive Officers as a Group <sup>(8) (9)</sup></b><br><b>(14 persons)</b> | <b>16,537</b>                             | <b>*</b>         | <b>—</b>           | <b>—</b>         | <b>*</b>  |

(1) A total of 17,500,000 common and subordinated units are issued and outstanding.

(2) TC PipeLines GP, Inc. and TransCan Northern Ltd. are wholly owned subsidiaries of TransCanada.

(3) TC PipeLines GP, Inc. owns an aggregate 2% general partner interest of TC PipeLines.

(4) As reported on a schedule 13G/A filed on February 12, 2004, the Goldman Sachs Group, Inc. (GS Group) and Goldman, Sachs & Co. (Goldman Sachs) each disclaim beneficial ownership of the securities beneficially owned by (i) any client accounts with respect to which Goldman Sachs or employees of Goldman Sachs have voting or investment discretion, or both and (ii) certain investment entities, of which a subsidiary of GS Group or Goldman Sachs is the general partner, managing general partner or other manager, to the extent interests in such entities are held by persons other than GS Group, Goldman Sachs or their affiliates.

(5) 10,979 units are held in trust accounts for Mr. Helman's benefit.

(6) 2,979 units are held by the Jenkins-Stark Family Trust dated June 16, 1995.

(7) 2,579 units are held directly by Mr. Marshall.

(8) With the exception of the three named directors above, none of the other directors and executive officers hold any units of TC PipeLines.

(9) Ronald J. Turner holds 322,850 options and 29,330 shares of TransCanada; Russell K. Girling holds 440,162 options and 9,725 shares of TransCanada; Albrecht W.A. Bellstedt holds 187,500 options and 12,206 shares of TransCanada; Kristine L. Delkus holds 73,048 options and 2,252 shares of TransCanada; Steven D. Becker holds 142,907 options and 888 shares of TransCanada; Donald R. Marchand holds 111,000 options and 4,397 shares of TransCanada; Ronald L. Cook holds 66,290 options and 8,486 shares of TransCanada; Max Feldman holds 157,481 options and 25,485 shares of TransCanada; Wendy L. Hanrahan holds 22,700 options and 977 shares of TransCanada; Amy W. Leong holds 5,600 options and 2,236 shares of TransCanada; and Maryse C. St.-Laurent holds 2,600 options and 2,056 shares of TransCanada. The directors and executive officers as a group hold 1,532,138 options and 98,038 shares of TransCanada.

\* Less than 1%.

### Item 13. Certain Relationships and Related Transactions

An indirect subsidiary of TransCanada owns 2,800,000 common units and the general partner owns 1,872,870 common units and 936,436 subordinated units, representing an aggregate 31.4% limited partner interest in the Partnership. In addition, the general partner owns an aggregate 2% general partner interest in the Partnership through which it manages and operates the Partnership. As a result, TransCanada's aggregate ownership interest in the Partnership is 33.4% by virtue of its indirect ownership of the general partner and a 31.4% aggregate limited partner interest.

The general partner is accountable to TC PipeLines and the unitholders as a fiduciary. Neither the Delaware Revised Uniform Limited Partnership Act (Delaware Act) nor case law defines with particularity the fiduciary duties owed by general partners to limited partners of a limited partnership. The Delaware Act does provide that Delaware limited partnerships may, in their partnership agreements, restrict or expand the fiduciary duties owed by a general partner to limited partners and the partnership.

In order to induce the general partner to manage the business of TC PipeLines, the partnership agreement contains various provisions restricting the fiduciary duties that might otherwise be owed by the general partner. The following is a summary of the material restrictions of the fiduciary duties owed by the general partner to the limited partners:

- The partnership agreement permits the general partner to make a number of decisions in its "sole discretion." This entitles the general partner to consider only the interests and factors that it desires and it shall have no duty or obligation to give any consideration to any interest of, or factors affecting, TC PipeLines, its affiliates or any limited partner. Other provisions of the partnership agreement provide that the general partner's actions must be made in its reasonable discretion.
- The partnership agreement generally provides that affiliated transactions and resolutions of conflicts of interest not involving a required vote of unitholders must be "fair and reasonable" to TC PipeLines. In determining whether a transaction or resolution is "fair and reasonable" the general partner may consider interests of all parties involved, including its own. Unless the general partner has acted in bad faith, the action taken by the general partner shall not constitute a breach of its fiduciary duty.
- The partnership agreement specifically provides that it shall not be a breach of the general partner's fiduciary duty if its affiliates engage in business interests and activities in competition with, or in preference or to the exclusion of, TC PipeLines. Further, the general partner and its affiliates have no obligation to present business opportunities to TC PipeLines.
- The partnership agreement provides that the general partner and its officers and directors will not be liable for monetary damages to TC PipeLines, the limited partners or assignees for errors of judgment or for any acts or omissions if the general partner and those other persons acted in good faith.

TC PipeLines is required to indemnify the general partner and its officers, directors, employees, affiliates, partners, members, agents and trustees (collectively referred to hereafter as the General Partner and others), to the fullest extent permitted by law, against liabilities, costs and expenses incurred by the General Partner and others. This indemnification is required if the General Partner and others acted in good faith and in a manner they reasonably believed to be in, or (in the case of a person other than the general partner) not opposed to, the best interests of TC PipeLines. Indemnification is required for criminal proceedings if the General Partner and others had no reasonable cause to believe their conduct was unlawful.

The Partnership does not have any employees. The management and operating functions are provided by the general partner. The general partner does not receive a management fee or other compensation in connection with its management of the Partnership. The Partnership reimburses the general partner for all costs of services provided, including the costs of employee, officer and director compensation and benefits, and all other expenses necessary or appropriate to the conduct of the business of, and allocable to the Partnership. The partnership agreement provides that the general partner will, in its sole discretion, determine the expenses that are allocable to the Partnership in any reasonable manner determined by it. Total costs reimbursed to the general partner by the Partnership were

approximately \$0.7 million for the year ended December 31, 2003. Such costs include personnel costs (such as salaries and employee benefits), overhead costs (such as office space and equipment) and out-of-pocket expenses related to the provision of services to the Partnership.

On May 28, 2003, the Partnership renewed its \$40.0 million unsecured two-year revolving credit facility (TransCanada Credit Facility) with TransCanada PipeLine USA Ltd., an affiliate of the general partner. The TransCanada Credit Facility bears interest at LIBOR plus 1.25%. The purpose of the TransCanada Credit Facility is to provide borrowings to fund capital expenditures, to fund capital contributions to Northern Border Pipeline, Tuscarora and any other entity in which the Partnership directly or indirectly acquires an interest, to fund working capital and for other general business purposes, including temporary funding of cash distributions to unitholders and the general partner, if necessary. At December 31, 2003, the Partnership had no amount outstanding under the TransCanada Credit Facility. As at March 12, 2004, \$9.0 million is outstanding under the TransCanada Credit Facility.

Mr. Helman, a director of the general partner of the Partnership, is a partner of the law firm Mayer, Brown, Rowe & Maw LLP, which provides legal services on U.S. related matters to TransCanada, the parent of the general partner. Also, in the first half of 2002, Mayer, Brown, Rowe & Maw LLP provided limited legal services to the general partner on behalf of the Partnership solely relating to matters arising from Enron's voluntary petition for bankruptcy protection. The payments made by the Partnership and those made by its parent during the last calendar year did not exceed 5% of Mayer, Brown, Rowe & Maw LLP's consolidated gross revenues for that year. Mr. Helman did not participate, nor was he consulted in the provision of services to the Partnership, and Mayer, Brown, Rowe & Maw LLP have not since the first half of 2002 provided any further services to the Partnership.

#### Item 14. Principal Accountants Fees and Services

The following table sets forth, for the periods indicated, the fees billed by the principal accountants.

|                                   | 2003                  | 2002   |
|-----------------------------------|-----------------------|--------|
| Audit Fees                        | 65,500 <sup>(1)</sup> | 79,660 |
| Audit-Related Fees <sup>(2)</sup> | -                     | -      |
| Tax Fees <sup>(2)</sup>           | -                     | -      |
| All Other Fees <sup>(2)</sup>     | -                     | -      |

(1) On April 23, 2002, the Partnership filed a shelf registration statement with the SEC. These charges include fees paid to KPMG, the Partnership's external auditors, for services performed related to this filing in the amount of \$3,000 (2002 - \$18,860).

(2) The Partnership has not engaged its external auditors for any tax services, audit-related services, or other services in 2003 or 2002.

## PART IV

## Item 15. Exhibits, Financial Statement Schedules and Reports on Form 8-K

## a) (1) and (2) Financial Statements and Financial Statement Schedules

The financial statements filed as part of this report are listed in the “Index to Financial Statements” on page F-1.

(3)

| <b>Exhibit No.</b> | <b>Description</b>   |
|--------------------|--|
| *3.1               | Amended and Restated Agreement of Limited Partnership of TC PipeLines, LP dated May 28, 1999 (Exhibit 3.1 to TC PipeLines, LP’s Form 10-K, March 28, 2000).  |
| *3.2               | Certificate of Limited Partnership of TC PipeLines, LP (Exhibit 3.2 to TC PipeLines, LP’s Form S-1 Registration Statement, Registration No. 333-69947, December 30, 1998).   |
| *3.3               | Certificate of Limited Partnership of TC PipeLines Intermediate Limited Partnership (Exhibit 3.3 to TC PipeLines, LP’s Form S-1, December 30, 1998).   |
| *3.4               | Certificate of Limited Partnership of TC Tuscarora Intermediate Limited Partnership (Exhibit 99.1 to TC PipeLines, LP’s Form 8-K, September 1, 2000).  |
| *3.5               | Agreement of Limited Partnership of TC Tuscarora Intermediate Limited Partnership dated July 19, 2000 (Exhibit 99.2 to TC PipeLines, LP’s Form 8-K, September 1, 2000).  |
| *3.6               | Amended and Restated Agreement of Limited Partnership of TC PipeLines Intermediate Limited Partnership dated May 28, 1999 (Exhibit 10.1 to TC PipeLines, LP’s Form 10-K, March 28, 2000).  |
| *4.1               | Indenture, dated as of August 17, 1999 between Northern Border Pipeline Company and Bank One Trust Company, NA, successor to The First National Bank of Chicago, as trustee (Exhibit 4.1 to Northern Border Pipeline Company, Form S-4 Registration Statement, Registration No. 333-88577, October 7, 1999).   |
| *4.2               | Indenture, Assignment and Security Agreement dated December 21, 1995 between Tuscarora Gas Transmission Company and Wilmington Trust Company, as trustee (Exhibit 99.1 to TC PipeLines, LP’s Form 10-Q, September 30, 2000).   |
| *4.3               | Indenture dated September 17, 2001, between Northern Border Pipeline Company and Bank One Trust Company, N.A. (Exhibit 4.2 to Northern Border Pipeline Company, Form S-4 Registration Statement, Registration No. 333-73282, November 13, 2001).   |
| *4.4               | Indenture dated April 29, 2002, between Northern Border Pipeline Company and Bank One Trust Company, NA, as trustee (Exhibit 4.1 to Northern Border Pipeline Company’s Form 10-Q, March 31, 2002).   |
| *10.1              | Contribution, Conveyance and Assumption Agreement among TC PipeLines, LP and certain other parties dated May 28, 1999 (Exhibit 10.2 to TC PipeLines, LP’s Form 10-K, March 28, 2000).  |
| *10.2              | Northern Border Pipeline Company General Partnership Agreement between Northern Border Intermediate Limited Partnership, TransCanada Border PipeLine Ltd., and TransCan Northern Ltd., effective March 9, 1978 as amended (Exhibit 3.2 to Northern Border Partners, L.P. Form S-1 Registration Statement No. 33-66158).                                  |
| *10.2.1            | Seventh Supplement Amending Northern Border Pipeline Company General Partnership Agreement dated as of September 23, 1993 (Exhibit 10.3.1 to TC PipeLines, LP’s Form S-1, December 30, 1998).  |
| *10.2.2            | Eighth Supplement Amending Northern Border Pipeline Company General Partnership Agreement dated May 21, 1999 by and among TransCan Border PipeLine Ltd., TransCanada Northern Ltd., Northern Border Intermediate Limited Partnership and TC PipeLines Intermediate Limited Partnership (Exhibit 10.3.2 to TC PipeLines, LP’s Form 10-K, March 28, 2000). |

- \*10.2.3 Ninth Supplement Amending Northern Border Pipeline Company General Partnership Agreement dated July 16, 2001 by and among Northern Border Intermediate Limited Partnership and TC PipeLines Intermediate Limited Partnership (Exhibit 10.37 to Northern Border Pipeline Company, Form S-4 Registration Statement, Registration No. 333-73282, November 13, 2001).
- \*10.3 Renewal of U.S. \$40,000,000 Two Year Revolving Credit Facility between TC PipeLines, LP, as borrower, and TransCanada PipeLine USA Ltd., as lender dated May 28, 2003 (Exhibit 10.1 to TC PipeLines, LP's Form 10-Q, August 14, 2003).
- \*10.4 Operating Agreement between Northern Border Pipeline Company and Northern Plains Natural Gas Company, dated February 28, 1980 (Exhibit 10.3 to Northern Border Partners, L.P.'s Form S-1 Registration Statement No. 33-66158).
- \*10.5 Agreement among Northern Plains Natural Gas Company, Pan Border Gas Company, Northwest Border Pipeline Company, TransCanada Border PipeLine Ltd., TransCan Northern Ltd., Northern Border Intermediate Limited Partnership, Northern Border Partners, L.P., and the Management Committee of Northern Border Pipeline, dated as of March 17, 1999 (Exhibit 10.21 to Northern Border Partners, L.P.'s 1998 Form 10-K/A, March 24, 1999).
- \*10.6 Directors' Compensation Plan of TC PipeLines, GP, Inc. dated effective July 19, 1999 (Exhibit 10.36 to TC PipeLines, LP's Form 10-K, March 28, 2000).
- \*10.7 Purchase and Sale Agreement dated July 19, 2000 among TCPL Tuscarora Ltd., TC Tuscarora Intermediate Limited Partnership, TC PipeLines GP, Inc., TransCanada PipeLines Limited and TransCanada PipeLine USA Ltd. (Exhibit 99.3 to TC PipeLines, LP's Form 8-K, September 1, 2000).
- \*10.8 Credit Agreement dated as of August 22, 2000 among TC PipeLines, LP, the Lenders Party thereto and Bank One N.A., as agent (Exhibit 99.2 to TC PipeLines, LP's Form 10-Q, September 30, 2000).
- \*10.8.1 First Amendment and Waiver to Credit Agreement among TC PipeLines, LP, the Lenders Party thereto and Bank One N.A., as agent, April 15, 2002 (Exhibit 10.1 to TC PipeLines, LP's Form 10-Q, September 30, 2002).
- \*10.8.2 Second Amendment to Credit Agreement among TC PipeLines, LP, the Lenders Party thereto and Bank One N.A., as agent, September 30, 2002 (Exhibit 10.2 to TC PipeLines, LP's Form 10-Q, September 30, 2002).
- 10.8.3 Third Amendment to Credit Agreement among TC PipeLines, LP, the Lenders Party thereto and Bank One N.A., as agent, March 8, 2004.
- \*10.9 Employment Agreement between Northern Plains Natural Gas Company and William R. Cordes effective June 1, 2002 (Exhibit 10.27 to Northern Border Partners, L.P.'s Form 10-Q, June 30, 2001).
- \*10.9.1 Amendment to Employment Agreement between Northern Plains Natural Gas Company and William R. Cordes, effective September 25, 2001 (Exhibit 10.36 to Northern Border Pipeline Company's Form S-4, November 13, 2001).
- \*10.10 Employment Agreement between Northern Plains Natural Gas Company and Jerry L. Peters effective April 1, 2002 (Exhibit 10.1 to Northern Border Pipeline Company's Form 10-Q, March 31, 2002).
- \*10.11 Credit Agreement, dated as of May 16, 2002, among Northern Border Pipeline Company, Bank One, NA, Citibank, N.A., Bank of Montreal, SunTrust Bank, Wachovia Bank, National Association, Banc One Capital Markets, Inc, and Lenders (as defined therein)(Exhibit 10.1 to Northern Border Partners, L.P.'s Current Report on Form 8-K dated June 26, 2002).
- 21.1 Subsidiaries of the Registrant.
- 23.1 Consent of KPMG LLP with respect to the financial statements of TC PipeLines, LP.
- 23.2 Consent of KPMG LLP with respect to the financial statements of Northern Border Pipeline Company.
- 31.1 Certification of President and Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2 Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.



- 32.1 Certification of President and Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 32.2 Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- \*99.1 Consolidated balance sheet at December 31, 2002 of TC PipeLines GP, Inc., general partner of TC PipeLines, LP (Exhibit 99.1 to TC PipeLines, LP's Form 10-Q, August 14, 2003).
- 99.2 Consolidated balance sheet at December 31, 2003 of TC PipeLines GP, Inc., general partner of TC PipeLines, LP.

\* Indicates exhibits incorporated by reference.

b) Reports on Form 8-K

1. Report on Form 8-K dated October 24, 2003 and filed on October 24, 2003 reporting that TC PipeLines, LP issued a press release announcing third quarter results for the period ended September 30, 2003.
2. Report on Form 8-K dated December 19, 2003 and filed on December 19, 2003 reporting that Northern Border Pipeline advised that its Management Committee had unanimously agreed to (i) issue equity cash calls to its partners in the total amount of \$130 million in early 2004 and \$90 million in 2007; (ii) fund future growth capital expenditures with 50% equity capital contributions from its partners; and (iii) change the cash distribution policy of Northern Border Pipeline to be effective January 1, 2004.
3. Report on Form 8-K dated December 31, 2003 and filed on December 31, 2003 reporting that Northern Border Pipeline filed a Form 8-K stating that the SEC issued an order on December 29, 2003 denying two applications filed by Enron seeking exemption under Section 3(a)(1), 3(a)(3) and 3(a)(5) of PUHCA. Northern Border Pipeline also stated that Enron filed for an exemption under Section 3(a)(4) of PUHCA, based on the temporary nature of the applicant's current or proposed interest in Portland General Electric Company, as described in Enron's and certain of its subsidiaries' chapter 11 plan.
4. Report on Form 8-K dated January 16, 2004 and filed on January 20, 2004 reporting that TC PipeLines, LP issued a press release announcing its fourth quarter distribution.
5. Report on Form 8-K dated January 29, 2004 and filed on January 30, 2004 reporting that TC PipeLines, LP issued a press release announcing fourth quarter and annual results for the period ended December 31, 2003.
6. Report on Form 8-K dated February 9, 2004 and filed on February 9, 2004 reporting that Northern Border Pipeline filed a Form 8-K stating that, as previously reported on December 31, 2003, Enron and other related entities had filed with the SEC an application for exemption under Section 3(a)(4) of PUHCA. By SEC order entered January 30, 2004, the hearing date on Enron's pending application for exemption under PUHCA was postponed until February 9, 2004 and by SEC order entered February 6, 2004, the hearing date has now been postponed until further notice on the condition that a status report on Enron's offer of settlement be provided no later than March 8, 2004.
7. Report on Form 8-K dated March 2, 2004 and filed on March 2, 2004, furnishing the presentation of Mr. Ron Turner, President and Chief Executive Officer of TC PipeLines, LP at the Master Limited Partnership Investor Conference 2004, held in New York City on March 2, 2004.
8. Report on Form 8-K dated March 10, 2004 and filed March 11, 2004, reporting that, on March 9, 2004, Enron registered as a holding company under the Public Utility Holding Company Act of 1935. This Form 8-K also reported that on March 10, 2004, Northern Border Pipeline filed a Form 8-K announcing that the SEC has granted Enron's request on behalf of Northern Border Partners, which includes its subsidiary Northern Border Pipeline, to allow Northern Border Partners to declare and pay distributions. The approval is part of the SEC order issued March 9, 2004, after Enron registered as a holding company under PUHCA. The authorizations are effective until the earlier of the deregistration of Enron under PUHCA or July 31, 2005.

c) None.

d) None.

**SIGNATURES**









Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized on this 12th day of March 2004.

TC PIPELINES, LP  
(A Delaware Limited Partnership)  
by its general partner, TC PipeLines GP, Inc.



By:  
Ronald J. Turner  
President and Chief Executive Officer  
TC PipeLines GP, Inc.

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons in the capacities and on the dates indicated.

| <b>Signature</b>  | <b>Title</b>  | <b>Date</b>    |
|---|---|----------------|
| <br>Ronald J. Turner<br>and Director (Principal Executive Officer) | President and Chief Executive Officer                                 | March 12, 2004 |
| <br>Russell K. Girling  | Chief Financial Officer<br>and Director (Principal Financial Officer) | March 12, 2004 |
| <br>Amy W. Leong   | Controller (Principal Accounting Officer)                             | March 12, 2004 |
| <br>Albrecht W. A. Bellstedt                                     | Director  | March 12, 2004 |
| <br>Kristine L. Delkus   | Director  | March 12, 2004 |
| <br>Robert A. Helman   | Director  | March 12, 2004 |
| <br>Jack F. Jenkins-Stark  | Director  | March 12, 2004 |
| <br>David L. Marshall  | Director  | March 12, 2004 |

**TC PIPELINES, LP****INDEX TO FINANCIAL STATEMENTS**

Page No.

**FINANCIAL STATEMENTS OF TC PIPELINES, LP**

|   |     |
|---|-----|
| Independent Auditors' Report  | F-2 |
| Balance Sheet – December 31, 2003 and 2002  | F-3 |
| Statement of Income – Years Ended December 31, 2003, 2002 and 2001                      | F-4 |
| Statement of Comprehensive Income – Years Ended December 31, 2003, 2002 and 2001        | F-4 |
| Statement of Cash Flows – Years Ended December 31, 2003, 2002 and 2001                  | F-5 |
| Statement of Changes in Partners' Equity – Years Ended December 31, 2003, 2002 and 2001 | F-6 |
| Notes to Financial Statements   | F-7 |

**FINANCIAL STATEMENTS OF NORTHERN BORDER PIPELINE COMPANY**

|   |      |
|---|------|
| Independent Auditors' Report  | F-13 |
| Balance Sheet – December 31, 2003 and 2002  | F-14 |
| Statement of Income – Years Ended December 31, 2003, 2002 and 2001                      | F-15 |
| Statement of Comprehensive Income – Years Ended December 31, 2003, 2002 and 2001        | F-15 |
| Statement of Cash Flows – Years Ended December 31, 2003, 2002 and 2001                  | F-16 |
| Statement of Changes in Partners' Equity – Years Ended December 31, 2003, 2002 and 2001 | F-17 |
| Notes to Financial Statements   | F-18 |

**FINANCIAL STATEMENTS SCHEDULE OF NORTHERN BORDER PIPELINE COMPANY**

|   |     |
|---|-----|
| Independent Auditors' Report on Schedule        | S-1 |
| Schedule II – Valuation and Qualifying Accounts | S-2 |

## INDEPENDENT AUDITORS' REPORT

**To the Board of Directors of TC PipeLines GP, Inc., General Partner of TC PipeLines, LP:**

We have audited the accompanying balance sheets of TC PipeLines, LP (a Delaware limited partnership) as of December 31, 2003 and 2002 and the related statements of income, comprehensive income, cash flows and changes in partners' equity for each of the years in the three year period ended December 31, 2003. These financial statements are the responsibility of the General Partner. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of TC PipeLines, LP as of December 31, 2003 and 2002 and the results of its operations and its cash flows for each of the years in the three year period ended December 31, 2003 in conformity with accounting principles generally accepted in the United States of America.

*KPMG LLP*

Calgary, Canada

March 4, 2004

## BALANCE SHEET

| December 31                             | 2003         | 2002  |
|---|--------------|-------|
| <i>(millions of dollars)</i>            |              |       |
| <b>Assets</b>                           |              |       |
| Current Assets                          |              |       |
| Cash                                    | 7.5          | 6.4   |
| Investment in Northern Border Pipeline  | 240.7        | 242.9 |
| Investment in Tuscarora                 | 39.9         | 36.7  |
|   | <b>288.1</b> | 286.0 |
| <b>Liabilities and Partners' Equity</b> |              |       |
| Current Liabilities                     |              |       |
| Accounts payable                        | 0.6          | 0.6   |
| Current portion of long-term debt       | 5.5          | –     |
|   | <b>6.1</b>   | 0.6   |
| Long-Term Debt                          | –            | 11.5  |
| Partners' Equity                        |              |       |
| Common units                            | 260.4        | 238.9 |
| Subordinated units                      | 13.9         | 27.0  |
| General partner                         | 6.1          | 5.9   |
| Other comprehensive income              | 1.6          | 2.1   |
|   | <b>282.0</b> | 273.9 |
|   | <b>288.1</b> | 286.0 |

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

## STATEMENT OF INCOME

| Year ended December 31                                    | 2003           | 2002           | 2001           |
|---|----------------|----------------|----------------|
| <i>(millions of dollars, except per unit amounts)</i>     |                |                |                |
| Equity Income from Investment in Northern Border Pipeline | 44.5           | 42.8           | 42.1           |
| Equity Income from Investment in Tuscarora                | 5.3            | 4.7            | 3.6            |
| General and Administrative Expenses                       | (1.7)          | (1.5)          | (1.2)          |
| Financial Charges   | (0.1)          | (0.5)          | (1.0)          |
| <b>Net Income</b>   | <b>48.0</b>    | <b>45.5</b>    | <b>43.5</b>    |
| <b>Net Income per Unit</b>                                | <b>\$ 2.63</b> | <b>\$ 2.50</b> | <b>\$ 2.40</b> |
| <b>Units Outstanding</b> <i>(millions)</i>                | <b>17.5</b>    | <b>17.5</b>    | <b>17.5</b>    |

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

## STATEMENT OF COMPREHENSIVE INCOME

| Year ended December 31                                     | 2003        | 2002        | 2001        |
|--|-------------|-------------|-------------|
| <i>(millions of dollars)</i>                               |             |             |             |
| Net Income   | 48.0        | 45.5        | 43.5        |
| Other Comprehensive Income                                 |             |             |             |
| Transition adjustment from adoption of SFAS No. 133        | —           | (0.5)       | —           |
| Change associated with current period hedging transactions | (0.9)       | 3.1         | (0.1)       |
| <b>Total Comprehensive Income</b>                          | <b>47.5</b> | <b>44.6</b> | <b>46.5</b> |

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

## STATEMENT OF CASH FLOWS

| Year ended December 31  | 2003          | 2002          | 2001          |
|---|---------------|---------------|---------------|
| <i>(millions of dollars)</i>                                  |               |               |               |
| <b>Cash Generated from Operations</b>                         |               |               |               |
| Net Income  | 48.0          | 45.5          | 43.5          |
| Add/(deduct):   |               |               |               |
| Equity income less than/(in excess of) distributions received | 1.6           | –             | 6.3           |
| Increase/(decrease) in accounts payable                       | 0.2           | (0.4)         | (0.1)         |
| (Decrease)/increase in accrued interest                       | –             | (0.1)         | (0.1)         |
| Other   | –             | 0.2           | –             |
|   | <b>49.6</b>   | <b>52.1</b>   | <b>42.9</b>   |
| <b>Investing Activities</b>                                   |               |               |               |
| Investment in Tuscarora                                       | (4.1)         | (7.4)         | –             |
| Return of Capital from Northern Border Pipeline Company       | 1.0           | –             | –             |
| Deferred amounts  | –             | –             | (0.1)         |
|   | <b>(3.1)</b>  | <b>(7.4)</b>  | <b>(0.1)</b>  |
| <b>Financing Activities</b>                                   |               |               |               |
| Distributions paid  | (39.4)        | (37.4)        | (35.2)        |
| Reduction of long-term debt                                   | (6.0)         | (10.0)        | –             |
| Other   | –             | (0.1)         | –             |
|   | <b>(45.4)</b> | <b>(47.5)</b> | <b>(35.2)</b> |
| <b>Increase/(Decrease) in Cash</b>                            | <b>1.1</b>    | <b>(2.8)</b>  | <b>7.6</b>    |
| <b>Cash, Beginning of Year</b>                                | <b>6.4</b>    | <b>9.2</b>    | <b>1.6</b>    |
| <b>Cash, End of Year</b>                                      | <b>7.5</b>    | <b>6.4</b>    | <b>9.2</b>    |

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

## STATEMENT OF CHANGES IN PARTNERS' EQUITY

|  | Common Units        |                       | Subordinated Units  |                       | General Partner | Other Comprehensive Income | Partners' Equity      |                     |
|--|---------------------|-----------------------|---------------------|-----------------------|-----------------|----------------------------|-----------------------|---------------------|
|  | (millions of units) | (millions of dollars) | (millions of units) | (millions of dollars) |                 |                            | (millions of dollars) | (millions of units) |
| Partners' Equity at December 31, 2000        | 14.7                | 212.3                 | 2.8                 | 37.9                  | 5.2             | —                          | 17.5                  | 255.4               |
| Net Income                                   | —                   | 35.3                  | —                   | 6.8                   | 1.4             | —                          | —                     | 43.5                |
| Distributions Paid                           | —                   | (28.6)                | —                   | (5.5)                 | (1.1)           | —                          | —                     | (35.2)              |
| Other Comprehensive Income                   | —                   | —                     | —                   | —                     | —               | 3.0                        | —                     | 3.0                 |
| Partners' Equity at December 31, 2001        | 14.7                | 219.0                 | 2.8                 | 39.2                  | 5.5             | 3.0                        | 17.5                  | 266.7               |
| Net Income                                   | —                   | 37.5                  | —                   | 6.2                   | 1.8             | —                          | —                     | 45.5                |
| Distributions Paid                           | —                   | (30.7)                | —                   | (5.3)                 | (1.4)           | —                          | —                     | (37.4)              |
| Subordinated Unit Conversion                 | 0.9                 | 13.1                  | (0.9)               | (13.1)                | —               | —                          | —                     | —                   |
| Other Comprehensive Income                   | —                   | —                     | —                   | —                     | —               | (0.9)                      | —                     | (0.9)               |
| Partners' Equity at December 31, 2002        | 15.6                | 238.9                 | 1.9                 | 27.0                  | 5.9             | 2.1                        | 17.5                  | 273.9               |
| <b>Net Income</b>                            | —                   | <b>42.1</b>           | —                   | <b>3.9</b>            | <b>2.0</b>      | —                          | —                     | <b>48.0</b>         |
| <b>Distributions Paid</b>                    | —                   | <b>(34.1)</b>         | —                   | <b>(3.5)</b>          | <b>(1.8)</b>    | —                          | —                     | <b>(39.4)</b>       |
| <b>Subordinated Unit Conversion</b>          | <b>0.9</b>          | <b>13.5</b>           | <b>(0.9)</b>        | <b>(13.5)</b>         | —               | —                          | —                     | —                   |
| <b>Other Comprehensive Income</b>            | —                   | —                     | —                   | —                     | —               | <b>(0.5)</b>               | —                     | <b>(0.5)</b>        |
| <b>Partners' Equity at December 31, 2003</b> | <b>16.5</b>         | <b>260.4</b>          | <b>1.0</b>          | <b>13.9</b>           | <b>6.1</b>      | <b>1.6</b>                 | <b>17.5</b>           | <b>282.0</b>        |

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



## NOTES TO FINANCIAL STATEMENTS

### NOTE 1 ORGANIZATION

TC PipeLines, LP, and its subsidiary limited partnerships, TC PipeLines Intermediate Limited Partnership and TC Tuscarora Intermediate Limited Partnership, all Delaware limited partnerships, are collectively referred to herein as TC PipeLines or the Partnership. TC PipeLines was formed by TransCanada PipeLines Limited, a subsidiary of TransCanada Corporation (collectively referred to herein as TransCanada), to acquire, own and participate in the management of United States-based pipeline assets.

TC PipeLines owns a 30% general partner interest in Northern Border Pipeline Company (Northern Border Pipeline), a Texas general partnership. Northern Border Pipeline owns a 1,249-mile United States interstate pipeline system that transports natural gas from the Montana-Saskatchewan border to markets in the midwestern United States.

TC PipeLines also owns a 49% general partner interest in Tuscarora Gas Transmission Company (Tuscarora), a Nevada general partnership. Tuscarora owns a 240-mile United States interstate pipeline system that transports natural gas from Oregon, where it interconnects with facilities of Gas Transmission Northwest Corporation, to northern Nevada.

TC PipeLines is managed by its general partner, TC PipeLines GP, Inc. (General Partner), an indirect wholly-owned subsidiary of TransCanada. The General Partner provides certain administrative services for the Partnership and is reimbursed for its costs and expenses. In addition to its 2% general partner interest, the General Partner owns 1,872,870 common units and 936,436 subordinated units, representing an effective 15.7% limited partner interest in the Partnership at December 31, 2003. TransCanada indirectly holds 2,800,000 common units representing an effective 15.7% limited partner interest in the Partnership at December 31, 2003.

### NOTE 2 SIGNIFICANT ACCOUNTING POLICIES

#### (a) Basis of Presentation

The accompanying financial statements and related notes present the financial position of the Partnership as of December 31, 2003 and 2002 and the results of its operations, cash flows and changes in partners' equity for the years ended December 31, 2003, 2002 and 2001. The Partnership uses the equity method of accounting for its investments in Northern Border Pipeline and Tuscarora, over which it is able to exercise significant influence. Other comprehensive income recorded by TC PipeLines arises through its equity investments in Northern Border Pipeline and Tuscarora and relates to cash flow hedges transacted by Northern Border Pipeline and Tuscarora. Amounts are stated in United States dollars.

#### (b) Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Although management believes these estimates are reasonable, actual results could differ from these estimates.

#### (c) Cash and Cash Equivalents

Cash equivalents consist of highly liquid investments with original maturities of three months or less. The carrying amount of cash and cash equivalents approximates fair value because of the short maturity of these investments.

#### (d) Partners' Equity

Costs incurred in connection with the issuance of units are deducted from the proceeds received. Costs incurred to convert subordinated units to common units were deducted from Partners' Equity.

**(e) Income Taxes**

No provision for income taxes related to the operations of the Partnership is included in the accompanying financial statements because, as a partnership, it is not subject to Federal or state income tax. The tax effect of the Partnership's activities accrues to its partners.

**NOTE 3 INVESTMENT IN NORTHERN BORDER PIPELINE COMPANY**

The Partnership owns a 30% general partner interest in Northern Border Pipeline. The remaining 70% partnership interest in Northern Border Pipeline is held by Northern Border Partners, L.P. (NBP), a publicly traded limited partnership. The Northern Border pipeline system is operated by Northern Plains Natural Gas Company, a wholly-owned subsidiary of Enron. Northern Border Pipeline is regulated by the Federal Energy Regulatory Commission (FERC).

TC PipeLines' equity income amounted to \$44.5 million, \$42.8 million and \$42.1 million for the years ended December 31, 2003, 2002 and 2001, respectively, representing 30% of the net income of Northern Border Pipeline for the same periods. Undistributed earnings of Northern Border Pipeline amounted to zero, \$1.3 million and \$8.4 million for the years ended December 31, 2003, 2002 and 2001, respectively.

The following sets out summarized financial information for Northern Border Pipeline as at December 31, 2003 and 2002 and for the years ended December 31, 2003, 2002 and 2001.

**Northern Border Pipeline Balance Sheet**

| <b>December 31</b>                      | <b>2003</b>    | <b>2002</b>    |
|---|----------------|----------------|
| <i>(millions of dollars)</i>            |                |                |
| <b>Assets</b>                           |                |                |
| Cash and cash equivalents               | 28.7           | 25.4           |
| Other current assets                    | 40.8           | 40.8           |
| Plant, property and equipment, net      | 1,591.8        | 1,636.0        |
| Other assets                            | 31.3           | 37.8           |
|   | <b>1,692.6</b> | <b>1,740.0</b> |
| <b>Liabilities and Partners' Equity</b> |                |                |
| Current liabilities                     | 62.3           | 130.9          |
| Reserves and deferred credits           | 6.4            | 15.4           |
| Long-term debt                          | 821.5          | 783.9          |
| Partners' Equity                        |                |                |
| Partners' capital                       | 797.2          | 803.0          |
| Accumulated other comprehensive income  | 5.2            | 6.8            |
|   | <b>1,692.6</b> | <b>1,740.0</b> |

**Northern Border Pipeline Income Statement**

| <b>Year ended December 31</b> | <b>2003</b>  | <b>2002</b>  | <b>2001</b>  |
|-------------------------------|--------------|--------------|--------------|
| <i>(millions of dollars)</i>  |              |              |              |
| Revenues                      | 324.2        | 321.0        | 313.1        |
| Costs and expenses            | (73.4)       | (69.9)       | (59.3)       |
| Depreciation                  | (57.8)       | (58.7)       | (57.5)       |
| Financial charges             | (44.9)       | (51.5)       | (55.4)       |
| Other income/(expense)        | 0.1          | 1.8          | (0.4)        |
| Net income                    | <b>148.2</b> | <b>142.7</b> | <b>140.5</b> |

#### NOTE 4 INVESTMENT IN TUSCARORA GAS TRANSMISSION COMPANY

The Partnership owns a 49% general partner interest in Tuscarora. The remaining general partner interests in Tuscarora are held 50% by Sierra Pacific Resources and 1% by TransCanada. Tuscarora is regulated by the FERC.

TC PipeLines' equity income from Tuscarora amounted to \$5.3 million, \$4.7 million and \$3.6 million for the years ended December 31, 2003, 2002 and 2001, respectively, representing 49% of the net income of Tuscarora for the same periods. Undistributed earnings of Tuscarora amounted to zero, \$0.8 million and \$0.9 million for the years ended December 31, 2003, 2002 and 2001, respectively.

The following sets out summarized financial information for Tuscarora as at December 31, 2003 and 2002 and for the years ended December 31, 2003, 2002 and 2001. TC PipeLines has held its general partner interest since September 1, 2000.

#### Tuscarora Balance Sheet

| December 31                             | 2003         | 2002         |
|---|--------------|--------------|
| <i>(millions of dollars)</i>            |              |              |
| <b>Assets</b>                           |              |              |
| Cash and cash equivalents               | 1.8          | 0.6          |
| Other current assets                    | 4.3          | 4.3          |
| Plant, property and equipment, net      | 141.9        | 148.4        |
| Other assets                            | 1.6          | 1.2          |
|   | <b>149.6</b> | <b>154.5</b> |
| <b>Liabilities and Partners' Equity</b> |              |              |
| Current liabilities                     | 6.7          | 14.6         |
| Long-term debt                          | 80.8         | 85.3         |
| Partners' Equity                        |              |              |
| Partners' capital                       | 62.0         | 54.2         |
| Accumulated other comprehensive income  | 0.1          | 0.4          |
|   | <b>149.6</b> | <b>154.5</b> |

#### Tuscarora Income Statement

| Year ended December 31       | 2003        | 2002        | 2001       |
|------------------------------|-------------|-------------|------------|
| <i>(millions of dollars)</i> |             |             |            |
| Revenues                     | 29.7        | 23.1        | 21.3       |
| Costs and expenses           | (5.0)       | (2.8)       | (2.6)      |
| Depreciation                 | (6.4)       | (4.9)       | (4.6)      |
| Financial charges            | (6.5)       | (5.7)       | (6.1)      |
| Other (expense)/income       | -           | 0.7         | 0.3        |
| Net income                   | <b>11.8</b> | <b>10.4</b> | <b>8.3</b> |

#### NOTE 5 CREDIT FACILITIES AND LONG-TERM DEBT

On March 8, 2004, the Partnership renewed its credit facility (Revolving Credit Facility) with Bank One, NA, as administrative agent under which the Partnership may borrow up to an aggregate principal amount of \$30.0 million. Loans under the Revolving Credit Facility bear interest at a floating rate. The Revolving Credit Facility matures on February 28, 2006. Amounts borrowed may be repaid in part or in full prior to that time without penalty. The Revolving Credit Facility may be used to finance capital expenditures and for other general purposes. At December 31, 2003, the Partnership had borrowings of \$5.5 million outstanding under the Revolving Credit Facility (2002 – \$11.5 million). The fair value of the Revolving Credit Facility approximates its carrying value because the interest rate is a floating rate. The interest rate on the Revolving Credit Facility averaged 2.58% for the year (2002 – 3.57%; 2001 – 5.19%) and was 2.42% at the end of the year (2002 – 2.70%). Interest paid during the years ended December 31, 2003, 2002 and 2001 was \$0.2 million, \$0.4 million and \$1.2 million, respectively.

On May 28, 2003, the Partnership renewed its \$40.0 million unsecured two-year revolving credit facility (TransCanada Credit Facility), with TransCanada PipeLine USA Ltd., an affiliate of the General Partner. The TransCanada Credit Facility bears interest at London Interbank Offered Rate plus 1.25%. The purpose of the TransCanada Credit Facility is to provide borrowings to fund capital expenditures, to fund capital contributions to Northern Border Pipeline, Tuscarora and any other entity in which the Partnership directly or indirectly acquires an interest, to fund working capital and for other general business purposes, including temporary funding of cash distributions to unitholders and the General Partner, if necessary. At December 31, 2003 and 2002, the Partnership had no amount outstanding under the TransCanada Credit Facility.

#### **NOTE 6 PARTNERS' CAPITAL AND CASH DISTRIBUTIONS**

Partners' capital consists of 16,563,564 common units representing a 92.8% limited partner interest (which number includes 1,872,870 common units are held by the General Partner and 2,800,000 common units are owned by an affiliate of the General Partner), 936,436 subordinated units owned by the General Partner representing a 5.2% limited partner interest and a 2% general partner interest. In aggregate the General Partner's and its affiliate's interests represent an effective 32% ownership of the Partnership's equity.

The Partnership makes cash distributions to its partners with respect to each calendar quarter within 45 days after the end of each quarter. Distributions are based on available cash, which includes all cash and cash equivalents of the Partnership and working capital borrowings less reserves established by the General Partner. The Unitholders currently receive a quarterly distribution of \$0.55 per unit if and to the extent there is sufficient available cash. Distributions to holders of the subordinated units are subject, while subordinated units remain outstanding (Subordination Period), to the prior rights of holders of the common units to receive the quarterly distribution. Common units will not accrue arrearages with respect to distributions for any quarter after the Subordination Period and subordinated units will not accrue any arrearages with respect to distributions for any quarter.

The Subordination Period generally cannot end before June 30, 2004. Upon expiration of the Subordination Period, all subordinated units will be converted on a one-for-one basis into common units and will participate pro rata with all other common units in future distributions. On August 1, 2002, 936,435 subordinated units, representing one-third of the outstanding subordinated units held by the General Partner, upon satisfaction of the financial tests set forth in the partnership agreement, automatically converted into an equal number of common units as provided for in the partnership agreement of TC PipeLines. On August 1, 2003, an additional 936,435 subordinated units, representing one-half of the then remaining subordinated units held by the General Partner, upon satisfaction of the financial tests set forth in the partnership agreement, automatically converted into an equal number of common units as provided for in the partnership agreement of TC PipeLines. This reduces the number of outstanding subordinated units to 936,436, which will, upon satisfaction of the financial tests, automatically convert into common units on the first date after the record date for distributions for the quarter ending June 30, 2004.

As an incentive, the General Partner's percentage interest in quarterly distributions is increased after certain specified target levels are met. The incremental incentive distributions payable to the General Partner are 15%, 25%, and 50% of all quarterly distributions of Available Cash that exceed target levels of \$0.45, \$0.5275 and \$0.69, respectively, per unit. For the years ended December 31, 2003, 2002 and 2001, the Partnership distributed \$2.175, \$2.075 and \$1.975, respectively, per unit. The distributions for the year ended December 31, 2003, 2002 and 2001 included incentive distributions to the General Partner in the amount of \$1.2 million, \$0.8 million and \$0.5 million, respectively.

Partnership income is allocated to the General Partner and the limited partners in accordance with their respective partnership percentages, after giving effect to any priority income allocations for incentive distributions that are allocated 100% to the General Partner.

**NOTE 7 NET INCOME PER UNIT**

Net income per unit is computed by dividing net income, after deduction of the General Partner's allocation, by the weighted average number of common and subordinated units outstanding. The General Partner's allocation is equal to an amount based upon the General Partner's 2% interest, adjusted to reflect an amount equal to incentive distributions. Net income per unit was determined as follows:

| Year ended December 31                                | 2003    | 2002    | 2001    |
|---|---------|---------|---------|
| <i>(millions of dollars, except per unit amounts)</i> |         |         |         |
| Net Income  | 48.0    | 45.5    | 43.5    |
| Net income allocated to General Partner               |         |         |         |
| General Partner interest                              | (1.0)   | (1.0)   | (0.9)   |
| Incentive distribution income allocation              | (0.9)   | (0.8)   | (0.6)   |
|   | (2.0)   | (1.8)   | (1.4)   |
| Net income allocable to units                         | 46.0    | 43.7    | 42.1    |
| Weighted average units outstanding <i>(millions)</i>  | 17.5    | 17.5    | 17.5    |
| Net income per unit                                   | \$ 2.63 | \$ 2.50 | \$ 2.40 |

**NOTE 8 RELATED PARTY TRANSACTIONS**

The Partnership does not have any employees. The management and operating functions are provided by the General Partner. The General Partner does not receive a management fee or other compensation in connection with its management of the Partnership. The Partnership reimburses the General Partner for all costs of services provided, including the costs of employee, officer and director compensation and benefits, and all other expenses necessary or appropriate to the conduct of the business of, and allocable to the Partnership. The Partnership Agreement provides that the General Partner will determine the expenses that are allocable to the Partnership in any reasonable manner determined by the General Partner in its sole discretion. Total costs reimbursed to the General Partner by the Partnership were approximately \$0.7 million, \$0.5 million and \$0.5 million for the years ended December 31, 2003, 2002 and 2001, respectively. Such costs include (i) personnel costs (such as salaries and employee benefits), (ii) overhead costs (such as office space and equipment) and (iii) out-of-pocket expenses related to the provision of such services.

**NOTE 9 QUARTERLY FINANCIAL DATA (unaudited)**

The following sets forth selected financial data for the four quarters of each of 2003 and 2002. Certain comparative figures have been redefined to conform to the 2003 presentation.

| Quarter ended   | Mar 31  | Jun 30  | Sep 30  | Dec 31  |
|---|---------|---------|---------|---------|
| <i>(millions of dollars, except per unit amounts)</i> |         |         |         |         |
| <b>2003</b>   |         |         |         |         |
| Equity Income   | 12.3    | 12.5    | 12.5    | 12.5    |
| Net Income  | 11.9    | 12.0    | 12.0    | 12.1    |
| Net Income per Unit                                   | \$ 0.66 | \$ 0.66 | \$ 0.65 | \$ 0.66 |
| Cash Distributions Paid                               | 9.6     | 9.6     | 10.1    | 10.1    |
| <b>2002</b>   |         |         |         |         |
| Equity Income   | 12.4    | 12.6    | 12.9    | 9.6     |
| Net Income  | 11.9    | 12.2    | 12.5    | 8.9     |
| Net Income per Unit                                   | \$ 0.66 | \$ 0.67 | \$ 0.68 | \$ 0.49 |
| Cash Distributions Paid                               | 9.1     | 9.1     | 9.6     | 9.6     |

**NOTE 10 ACCOUNTING PRONOUNCEMENTS**

During 2003, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards (SFAS) No. 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities", SFAS No. 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity" and Interpretation (FIN) No. 46, "Consolidation of Variable Interest Entities," and reissued SFAS No. 132, "Employers' Disclosures about Pensions and Other Postretirement Benefits."

SFAS No. 149 amends and clarifies accounting for derivative instruments and hedging activities under SFAS No. 133. As at December 31, 2003, TC PipeLines does not engage in any hedging activities and is not affected by the changes resulting from this standard other than any impact arising from the Partnership's equity investees.

SFAS No. 150 establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. This standard is effective for financial instruments entered into or modified after May 31, 2003. As at December 31, 2003, TC PipeLines has not entered into any financial instruments that would be affected by this standard and, therefore, is not affected by the changes resulting from this standard.

SFAS No. 132 (Revised) revises employers' disclosures about pension plans and other postretirement benefits plans. It does not change the measurement or recognition of those plans in earlier Statements or the disclosure requirements contained in the original SFAS No. 132. This revision requires additional disclosures about the assets, obligations, cash flows, and net periodic benefit cost of defined benefit pension plans and other defined benefit postretirement plans. As at December 31, 2003, TC PipeLines does not have a pension plan or other postretirement benefit plans and is not affected by the changes resulting from this standard.

FIN No. 46 is an interpretation of Accounting Research Bulletin No. 51 and provides guidance on the identification of, and financial reporting for, certain entities over which control is achieved through financial controls (variable interests) rather than voting rights. Such entities are referred to as variable interest entities. The holder of the majority of an entity's variable interests will be required to consolidate the variable interest entity. The application of this Interpretation does not impact the financial statements of TC PipeLines.

**NOTE 11 SUBSEQUENT EVENTS**

On January 16, 2004, the Board of Directors of the General Partner declared a cash distribution of \$0.55 per unit related to the three months ended December 31, 2003. The \$10.1 million distribution was paid on February 13, 2004 in the following manner: \$9.1 million to the holders of common units as of the close of business on January 30, 2003, \$0.5 million to the General Partner as holder of the subordinated units, \$0.3 million to the General Partner as holder of incentive distribution rights and \$0.2 million to the General Partner in respect of its 2% general partner interest.

On January 30, 2004, TC PipeLines paid \$19.5 million related to its share of a capital contribution to Northern Border Pipeline.

## INDEPENDENT AUDITORS' REPORT

### **Northern Border Pipeline Company:**

We have audited the accompanying balance sheets of Northern Border Pipeline Company (a Texas partnership) as of December 31, 2003 and 2002, and the related statements of income, comprehensive income, cash flows, and changes in partners' equity for each of the years in the three-year period ended December 31, 2003. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Northern Border Pipeline Company as of December 31, 2003 and 2002, and the results of its operations and its cash flows for each of the years in the three-year period ended December 31, 2003, in conformity with accounting principles generally accepted in the United States of America.

KPMG LLP

January 27, 2004  
Omaha, Nebraska

## NORTHERN BORDER PIPELINE COMPANY

## BALANCE SHEET

(In Thousands)

|   | December 31         |                     |
|---|---------------------|---------------------|
|   | 2003                | 2002                |
| <u>ASSETS</u>   |                     |                     |
| CURRENT ASSETS  |                     |                     |
| Cash and cash equivalents   | \$ 28,732           | \$ 25,358           |
| Accounts receivable   | 33,292              | 32,774              |
| Related party receivables (net of allowance for doubtful accounts<br>of \$4,815 and \$4,805 in 2003 and 2002, respectively) | 395                 | 1,552               |
| Materials and supplies, at cost   | 4,818               | 4,721               |
| Prepaid expenses and other  | 2,267               | 1,844               |
| Total current assets  | <u>69,504</u>       | <u>66,249</u>       |
| NATURAL GAS TRANSMISSION PLANT  |                     |                     |
| In service  | 2,434,369           | 2,427,459           |
| Construction work in progress   | 4,447               | 4,027               |
| Total property, plant and equipment   | <u>2,438,816</u>    | <u>2,431,486</u>    |
| Less: Accumulated provision for depreciation and amortization   | 847,061             | 795,525             |
| Property, plant and equipment, net  | <u>1,591,755</u>    | <u>1,635,961</u>    |
| OTHER ASSETS  |                     |                     |
| Derivative financial instruments  | 16,648              | 21,204              |
| Unamortized debt expense  | 5,206               | 6,142               |
| Regulatory asset  | 8,196               | 10,481              |
| Total other assets  | <u>30,050</u>       | <u>37,827</u>       |
| Total assets  | <u>\$ 1,691,309</u> | <u>\$ 1,740,037</u> |
| <u>LIABILITIES AND PARTNERS' EQUITY</u>   |                     |                     |
| CURRENT LIABILITIES   |                     |                     |
| Current maturities of long-term debt  | \$ —                | \$ 65,000           |
| Accounts payable  | 7,055               | 17,103              |
| Related party payables  | 15,582              | 7,323               |
| Accrued taxes other than income   | 28,947              | 28,374              |
| Accrued interest  | 10,717              | 13,173              |
| Total current liabilities   | <u>62,301</u>       | <u>130,973</u>      |
| LONG-TERM DEBT, NET OF CURRENT MATURITIES   | <u>821,498</u>      | <u>783,906</u>      |
| RESERVES AND DEFERRED CREDITS   | <u>5,072</u>        | <u>15,386</u>       |
| COMMITMENTS AND CONTINGENCIES (Note 7)  |                     |                     |
| PARTNERS' EQUITY  |                     |                     |
| Partners' capital   | 797,236             | 803,014             |
| Accumulated other comprehensive income  | 5,202               | 6,758               |
| Total partners' equity  | <u>802,438</u>      | <u>809,772</u>      |
| Total liabilities and partners' equity  | <u>\$ 1,691,309</u> | <u>\$ 1,740,037</u> |

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



## NORTHERN BORDER PIPELINE COMPANY

## STATEMENT OF INCOME

(In Thousands)

|   | Year Ended December 31 |            |            |
|---|------------------------|------------|------------|
|   | 2003                   | 2002       | 2001       |
| OPERATING REVENUES                                  |                        |            |            |
| Operating revenues                                  | \$ 324,185             | \$ 321,050 | \$ 315,145 |
| Provision for rate refunds                          | –                      | –          | (2,057)    |
| Operating revenues, net                             | 324,185                | 321,050    | 313,088    |
| OPERATING EXPENSES                                  |                        |            |            |
| Operations and maintenance                          | 43,791                 | 41,442     | 33,695     |
| Depreciation and amortization                       | 57,779                 | 58,714     | 57,516     |
| Taxes other than income                             | 29,634                 | 28,436     | 25,636     |
| Operating expenses                                  | 131,204                | 128,592    | 116,847    |
| OPERATING INCOME                                    | 192,981                | 192,458    | 196,241    |
| INTEREST EXPENSE                                    |                        |            |            |
| Interest expense                                    | 44,903                 | 51,550     | 56,262     |
| Interest expense capitalized                        | (46)                   | (25)       | (911)      |
| Interest expense, net                               | 44,857                 | 51,525     | 55,351     |
| OTHER INCOME (EXPENSE)                              |                        |            |            |
| Allowance for equity funds used during construction | 53                     | 26         | 925        |
| Other income  | 1,373                  | 2,476      | 1,417      |
| Other expense                                       | (1,350)                | (716)      | (2,774)    |
| Other income (expense)                              | 76                     | 1,786      | (432)      |
| NET INCOME TO PARTNERS                              | \$ 148,200             | \$ 142,719 | \$ 140,458 |

## STATEMENT OF COMPREHENSIVE INCOME

(In Thousands)

|  | Year Ended December 31 |            |            |
|--|------------------------|------------|------------|
|  | 2003                   | 2002       | 2001       |
| NET INCOME TO PARTNERS                                     | \$ 148,200             | \$ 142,719 | \$ 140,458 |
| OTHER COMPREHENSIVE INCOME:                                |                        |            |            |
| Transition adjustment from adoption of SFAS No. 133        | –                      | –          | 10,347     |
| Change associated with current period hedging transactions | (1,556)                | (2,415)    | (1,174)    |
| Total comprehensive income                                 | \$ 146,644             | \$ 140,304 | \$ 149,631 |

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

## NORTHERN BORDER PIPELINE COMPANY

## STATEMENT OF CASH FLOWS

(In Thousands)

|  | Year Ended December 31 |            |            |
|--|------------------------|------------|------------|
|  | 2003                   | 2002       | 2001       |
| CASH FLOWS FROM OPERATING ACTIVITIES:  |                        |            |            |
| Net income to partners   | \$ 148,200             | \$ 142,719 | \$ 140,458 |
| Adjustments to reconcile net income to partners<br>to net cash provided by operating activities: |                        |            |            |
| Depreciation and amortization  | 58,144                 | 59,079     | 57,881     |
| Provision for regulatory refunds   | 261                    | 10,000     | 2,036      |
| Regulatory refunds paid  | (10,261)               | –          | (6,762)    |
| Allowance for equity funds used during construction  | (53)                   | (26)       | (925)      |
| Reserves and deferred credits  | 1,001                  | (237)      | 736        |
| Changes in components of working capital   | (3,551)                | 13,268     | 4,583      |
| Other  | (471)                  | (447)      | (685)      |
| Total adjustments  | 45,070                 | 81,637     | 56,864     |
| Net cash provided by operating activities  | 193,270                | 224,356    | 197,322    |
| CASH FLOWS FROM INVESTING ACTIVITIES:  |                        |            |            |
| Capital expenditures for property, plant<br>and equipment, net                                   | (12,918)               | (9,243)    | (54,659)   |
| CASH FLOWS FROM FINANCING ACTIVITIES:  |                        |            |            |
| Distributions to partners  | (153,978)              | (164,126)  | (143,032)  |
| Issuance of long-term debt, net  | 142,000                | 431,894    | 385,400    |
| Retirement of long-term debt   | (165,000)              | (468,000)  | (374,000)  |
| Decrease in bank overdrafts  | –                      | –          | (22,437)   |
| Proceeds (payments) upon termination of derivatives  | –                      | 2,351      | (4,070)    |
| Long-term debt financing costs   | –                      | (2,877)    | (2,567)    |
| Net cash used in financing activities  | (176,978)              | (200,758)  | (160,706)  |
| NET CHANGE IN CASH AND CASH EQUIVALENTS  | 3,374                  | 14,355     | (18,043)   |
| Cash and cash equivalents – beginning of year  | 25,358                 | 11,003     | 29,046     |
| Cash and cash equivalents – end of year  | \$ 28,732              | \$ 25,358  | \$ 11,003  |
| Changes in components of working capital:  |                        |            |            |
| Accounts receivable  | \$ (4,908)             | \$ 5,369   | \$ 3,432   |
| Materials and supplies   | (97)                   | 152        | (163)      |
| Prepaid expenses and other   | (422)                  | (113)      | (1,484)    |
| Accounts payable   | 3,758                  | 10,006     | 1,643      |
| Accrued taxes other than income  | 573                    | 1,207      | (970)      |
| Accrued interest   | (2,455)                | (3,353)    | 2,125      |
| Total  | \$ (3,551)             | \$ 13,268  | \$ 4,583   |

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

**NORTHERN BORDER PIPELINE COMPANY**  
**STATEMENT OF CHANGES IN PARTNERS' EQUITY**  
(In Thousands)

|   | TC PipeLines<br>Intermediate<br>Limited<br>Partnership | Northern Border<br>Intermediate<br>Limited<br>Partnership | Accumulated<br>Other<br>Comprehensive<br>Income | Total<br>Partners'<br>Equity |
|---|--|---|---|------------------------------|
| Partners' Equity at December 31, 2000                         | \$ 248,098   | \$ 578,897  | \$ -  | \$ 826,995                   |
| Net income to partners  | 42,138   | 98,320  | -   | 140,458                      |
| Transition adjustment from adoption<br>of SFAS No. 133        | -  | -   | 10,347  | 10,347                       |
| Change associated with current period<br>hedging transactions | -  | -   | (1,174)   | (1,174)                      |
| Distributions paid  | (42,910)   | (100,122)   | -   | (143,032)                    |
| Partners' Equity at December 31, 2001                         | 247,326  | 577,095   | 9,173   | 833,594                      |
| Net income to partners  | 42,816   | 99,903  | -   | 142,719                      |
| Change associated with current period<br>hedging transactions | -  | -   | (2,415)   | (2,415)                      |
| Distributions paid  | (49,238)   | (114,888)   | -   | (164,126)                    |
| Partners' Equity at December 31, 2002                         | 240,904  | 562,110   | 6,758   | 809,772                      |
| Net income to partners  | 44,460   | 103,740   | -   | 148,200                      |
| Change associated with current period<br>hedging transactions | -  | -   | (1,556)   | (1,556)                      |
| Distributions paid  | (46,193)   | (107,785)   | -   | (153,978)                    |
| Partners' Equity at December 31, 2003                         | <u>\$ 239,171</u>                                      | <u>\$ 558,065</u>   | <u>\$ 5,202</u>                                 | <u>\$ 802,438</u>            |

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

## NORTHERN BORDER PIPELINE COMPANY

### NOTES TO FINANCIAL STATEMENTS

#### 1. ORGANIZATION AND MANAGEMENT

Northern Border Pipeline Company (Northern Border Pipeline) is a Texas general partnership formed in 1978. The ownership percentages of the partners in Northern Border Pipeline (Partners) at December 31, 2003 and 2002 are as follows:

| Partner  | Ownership Percentage |
|--|----------------------|
| Northern Border Intermediate Limited Partnership | 70                   |
| TC PipeLines Intermediate Limited Partnership    | 30                   |

Northern Border Pipeline owns a 1,249-mile natural gas transmission pipeline system extending from the United States-Canadian border near Port of Morgan, Montana, to a terminus near North Hayden, Indiana.

Northern Border Pipeline is managed by a Management Committee that includes three representatives from Northern Border Intermediate Limited Partnership (Partnership) and one representative from TC PipeLines Intermediate Limited Partnership (TC PipeLines). The Partnership's representatives selected by its general partners, Northern Plains Natural Gas Company (Northern Plains), a wholly-owned subsidiary of Enron Corp. (Enron), Pan Border Gas Company (Pan Border), a wholly-owned subsidiary of Northern Plains, and Northwest Border Pipeline Company, a wholly-owned subsidiary of TransCanada PipeLines Limited, which is a subsidiary of TransCanada Corporation, and affiliate of TC PipeLines, have 35%, 22.75% and 12.25%, respectively, of the voting interest on the Management Committee. The representative designated by TC PipeLines votes the remaining 30% interest. The day-to-day management of Northern Border Pipeline's affairs is the responsibility of Northern Plains, as defined by an operating agreement between Northern Border Pipeline and Northern Plains. Northern Border Pipeline is charged for the salaries, benefits and expenses of Northern Plains. Northern Plains also utilizes Enron affiliates for management services related to Northern Border Pipeline. For the years ended December 31, 2003, 2002, and 2001, Northern Border Pipeline's charges from Northern Plains and its affiliates totaled approximately \$25.6 million, \$22.8 million and \$29.5 million, respectively. See Note 10 for a discussion of Northern Border Pipeline's relationships with Enron and developments involving Enron.

#### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

##### (A) Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

##### (B) Government Regulation

Northern Border Pipeline is subject to regulation by the Federal Energy Regulatory Commission (FERC). Northern Border Pipeline's accounting policies conform to Statement of Financial Accounting Standards (SFAS) No. 71, "Accounting for the Effects of Certain Types of Regulation."

Accordingly, certain assets that result from the regulated ratemaking process are recorded that would not be recorded under accounting principles generally accepted in the United States of America for nonregulated entities. Northern Border Pipeline continually assesses whether the recovery of the regulatory assets is probable by considering such factors as regulatory changes and the impact of competition. Northern Border Pipeline believes the recovery of the existing regulatory assets is probable. If future recovery ceases to be probable, Northern Border Pipeline would be required to write off the regulatory assets at that time. At December 31, 2003 and 2002, Northern Border Pipeline has reflected regulatory assets of approximately \$8.2 million and \$10.5 million, respectively, in other assets on the balance sheet. Northern Border Pipeline is recovering the regulatory assets from its shippers over varying time periods, which range from five to 44 years.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

### (C) Revenue Recognition

Northern Border Pipeline transports gas for shippers under a tariff regulated by the FERC. The tariff specifies the calculation of amounts to be paid by shippers and the general terms and conditions of transportation service on the pipeline system. Northern Border Pipeline's revenues are derived from agreements for the receipt and delivery of gas at points along the pipeline system as specified in each shipper's individual transportation contract. Revenues for Northern Border Pipeline are recognized based upon contracted capacity and actual volumes transported under transportation service agreements. An allowance for doubtful accounts is recorded in situations where collectability is not reasonably assured. Northern Border Pipeline does not own the gas that it transports, and therefore it does not assume the related natural gas commodity risk.

### (D) Income Taxes

Income taxes are the responsibility of the Partners and are not reflected in these financial statements. However, the Northern Border Pipeline FERC tariff establishes the method of accounting for and calculating income taxes and requires Northern Border Pipeline to reflect in its rates the income taxes, which would have been paid or accrued if Northern Border Pipeline were organized during the period as a corporation. As a result, for purposes of determining transportation rates in calculating the return allowed by the FERC, Partners' capital and rate base are reduced by the amount equivalent to the net accumulated deferred income taxes. Such amounts were approximately \$350 million and \$343 million at December 31, 2003 and 2002, respectively, and are primarily related to accelerated depreciation and other plant-related differences.

### (E) Cash and Cash Equivalents

Cash equivalents consist of highly liquid investments with original maturities of three months or less. The carrying amount of cash and cash equivalents approximates fair value because of the short maturity of these investments.

### (F) Property, Plant and Equipment and Related Depreciation and Amortization

Property, plant and equipment is stated at original cost. During periods of construction, Northern Border Pipeline is permitted to capitalize an allowance for funds used during construction, which represents the estimated costs of funds used for construction purposes. The original cost of property retired is charged to accumulated depreciation and amortization, net of salvage and cost of removal. No retirement gain or loss is included in income except in the case of retirements or sales of entire regulated operating units.

Maintenance and repairs are charged to operations in the period incurred. The provision for depreciation and amortization of the transmission line is an integral part of Northern Border Pipeline's FERC tariff. The effective depreciation rate applied to Northern Border Pipeline's transmission plant is 2.25%. Composite rates are applied to all other functional groups of property having similar economic characteristics.

### (G) Risk Management

Financial instruments are used by Northern Border Pipeline in the management of its interest rate exposure. A control environment has been established which includes policies and procedures for risk assessment and the approval, reporting and monitoring of financial instrument activities. Northern Border Pipeline does not use these instruments for trading purposes. SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," as amended by SFAS No. 137 and SFAS No. 138, requires that every derivative instrument (including certain derivative instruments embedded in other contracts) be recorded on the balance sheet as either an asset or liability measured at its fair value. The statement requires that changes in the derivative's fair value be recognized currently in earnings unless specific hedge accounting criteria are met. Special accounting for qualifying hedges allows a derivative's gains and losses to offset related results on the hedged item in the income statement, and requires that a company formally document, designate and assess the effectiveness of transactions that receive hedge accounting. Northern Border Pipeline adopted SFAS No. 133 beginning January 1, 2001. See Note 6 for a discussion of Northern Border Pipeline's derivative instruments and hedging activities.

### (H) Reclassifications

Certain reclassifications have been made to the financial statements for prior years to conform with the current year presentation.

### 3. RATES AND REGULATORY ISSUES

Northern Border Pipeline filed a rate proceeding with the FERC in May 1999 for, among other things, a redetermination of its allowed equity rate of return. In September 2000, Northern Border Pipeline filed a stipulation and agreement with the FERC that documented the proposed settlement of its 1999 rate case. The settlement was approved by the FERC in December 2000. Under the settlement, both Northern Border Pipeline and its existing shippers will not be able to seek rate changes until November 1, 2005, at which time Northern Border Pipeline must file a new rate case.

After the FERC approved the rate case settlement and prior to the end of 2000, Northern Border Pipeline made estimated refund payments to its shippers totaling approximately \$22.7 million, primarily related to the period from December 1999 to November 2000. During the first quarter of 2001, Northern Border Pipeline paid the remaining refund obligation to its shippers totaling approximately \$6.8 million, which related to periods through January 2001.

On March 16, 2000, the FERC issued an order granting Northern Border Pipeline's application for a certificate to construct and operate an expansion and extension of its pipeline system into Indiana (Project 2000). The facilities for Project 2000 were placed into service on October 1, 2001.

In February 2003, Northern Border Pipeline filed to amend its FERC tariff to clarify the definition of company use gas, which is gas supplied by its shippers for its operations, by adding detailed language to the broad categories that comprise company use gas. Northern Border Pipeline had included in its collection of company use gas, quantities that were equivalent to the cost of electric power at its electric-driven compressor stations during the period of June 2001 through January 2003. On March 27, 2003, the FERC issued an order rejecting Northern Border Pipeline's proposed tariff sheet revision and requiring refunds with interest within 90 days of the order. Northern Border Pipeline made refunds to its shippers of \$10.3 million in May 2003.

### 4. TRANSPORTATION SERVICE AGREEMENTS

Operating revenues are collected pursuant to the FERC tariff through firm transportation service agreements. The firm service agreements extend for various terms with termination dates that range from March 2004 to December 2013. Northern Border Pipeline also has interruptible transportation service agreements and other transportation service agreements with numerous shippers.

Under the capacity release provisions of Northern Border Pipeline's FERC tariff, shippers are allowed to release all or part of their capacity either permanently for the full term of the contract or temporarily. A temporary capacity release does not relieve the original contract shipper from its payment obligations if the replacement shipper fails to pay for the capacity temporarily released to it.

For the year ended December 31, 2003, Northern Border Pipeline's largest shippers were BP Canada Energy Marketing Corp. (BP Canada), Pan-Alberta Gas (U.S.) Inc. (Pan-Alberta) and EnCana Marketing U.S.A. Inc. (EnCana). At December 31, 2003, BP Canada had approximately 21% of the contracted firm capacity and EnCana had approximately 19% of the contracted firm capacity. Pan-Alberta's firm service agreements, which had been managed by Mirant Americas Energy Marketing, LP, terminated October 31, 2003. The BP Canada firm service agreements extend for various terms with termination dates from October 2004 to February 2012. The EnCana firm service agreements extend for various terms with termination dates from March 2004 to June 2009. Operating revenues from BP Canada, EnCana, and Pan-Alberta for the year ended December 31, 2003, were \$54.7 million, \$32.9 million, and \$45.5 million, respectively. For the years ended December 31, 2002 and 2001, Northern Border Pipeline's largest shippers were Pan-Alberta and Mirant with combined operating revenues of \$105.5 million and \$80.7 million, respectively.

At December 31, 2003, there is no contracted firm capacity held by shippers affiliated with Northern Border Pipeline. Previously, some of Northern Border Pipeline's shippers have been affiliated with its general partners. Operating revenues from affiliates were \$1.4 million and \$52.1 million for the years ended December 31, 2002, and 2001, respectively.

## 5. CREDIT FACILITIES AND LONG-TERM DEBT

Detailed information on long-term debt is as follows:

| (in thousands)   | December 31       |                   |
|--|-------------------|-------------------|
|  | 2003              | 2002              |
| 1992 Pipeline Senior Notes – average 8.57%<br>at December 31, 2002, paid in 2003                                     | \$ –              | \$ 65,000         |
| 2002 Pipeline Credit Agreement – average 1.95%<br>and 2.05% at December 31, 2003 and 2002,<br>respectively, due 2005 | 131,000           | 89,000            |
| 1999 Pipeline Senior Notes – 7.75%, due 2009   | 200,000           | 200,000           |
| 2001 Pipeline Senior Notes – 7.50%, due 2021   | 250,000           | 250,000           |
| 2002 Pipeline Senior Notes – 6.25%, due 2007   | 225,000           | 225,000           |
| Fair value adjustment for interest rate swaps (Note 6)   | 16,648            | 21,204            |
| Unamortized debt discount  | (1,150)           | (1,298)           |
| Total  | 821,498           | 848,906           |
| Less: Current maturities of long-term debt   | –                 | 65,000            |
| Long-term debt   | <u>\$ 821,498</u> | <u>\$ 783,906</u> |

Northern Border Pipeline has entered into revolving credit facilities, which are used for capital expenditures, acquisitions and general business purposes and for refinancing existing indebtedness. Northern Border Pipeline entered into a \$175 million three-year credit agreement (2002 Pipeline Credit Agreement) with certain financial institutions in May 2002. The 2002 Pipeline Credit Agreement permits Northern Border Pipeline to choose among various interest rate options, to specify the portion of the borrowings to be covered by specific interest rate options and to specify the interest rate period. Northern Border Pipeline is required to pay a fee on the principal commitment amount of \$175 million.

In April 2002, Northern Border Pipeline completed a private offering of \$225 million of 6.25% Senior Notes due 2007 (2002 Pipeline Senior Notes) and in September 2001, Northern Border Pipeline completed a private offering of \$250 million of 7.50% Senior Notes due 2021 (2001 Pipeline Senior Notes). The 2002 Pipeline Senior Notes and 2001 Pipeline Senior Notes were subsequently exchanged in registered offerings for notes with substantially identical terms. The proceeds from the senior notes were used to reduce indebtedness outstanding.

Interest paid, net of amounts capitalized, during the years ended December 31, 2003, 2002 and 2001 was \$47.8 million, \$55.3 million and \$53.9 million, respectively.

Aggregate required repayments of long-term debt are as follows: \$131 million and \$225 million for 2005 and 2007, respectively. Aggregate required repayments of long-term debt thereafter total \$450 million. There are no required repayment obligations for 2004, 2006 or 2008.

Certain of Northern Border Pipeline's long-term debt and credit arrangements contain requirements as to the maintenance of minimum partners' capital and debt to capitalization ratios, leverage ratios and interest coverage ratios that restrict the incurrence of other indebtedness by Northern Border Pipeline and also place certain restrictions on distributions to the partners of Northern Border Pipeline. The 2002 Pipeline Credit Agreement requires the maintenance of a ratio of EBITDA (net income plus interest expense, income taxes and depreciation and amortization) to interest expense of greater than 3 to 1. The 2002 Pipeline Credit Agreement also requires the maintenance of the ratio of indebtedness to EBITDA of no more than 4.5 to 1. At December 31, 2003, Northern Border Pipeline was in compliance with its financial covenants.

## 5. CREDIT FACILITIES AND LONG-TERM DEBT (continued)

The following estimated fair values of financial instruments represent the amount at which each instrument could be exchanged in a current transaction between willing parties. Based on quoted market prices for similar issues with similar terms and remaining maturities, the estimated fair value of the 1992 Pipeline Senior Notes, 1999 Pipeline Senior Notes, 2001 Pipeline Senior Notes and 2002 Pipeline Senior Notes was approximately \$675 million and \$827 million at December 31, 2003 and 2002, respectively. Northern Border Pipeline presently intends to maintain the current schedule of maturities for the 1999 Pipeline Senior Notes, the 2001 Pipeline Senior Notes and the 2002 Pipeline Senior Notes, which will result in no gains or losses on their respective repayments. The fair value of Northern Border Pipeline's variable rate debt approximates the carrying value since the interest rates are periodically adjusted to reflect current market conditions.

## 6. DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES

As a result of the adoption of SFAS No. 133 on January 1, 2001, Northern Border Pipeline reclassified approximately \$11.1 million from long-term debt to accumulated other comprehensive income related to unamortized proceeds from the termination of interest rate swap agreements. Also upon adoption of SFAS No. 133, Northern Border Pipeline designated an outstanding interest rate swap agreement with a notional amount of \$40 million as a cash flow hedge. As a result, Northern Border Pipeline recorded a non-cash loss in accumulated other comprehensive income of approximately \$0.8 million. The \$40 million interest rate swap agreement terminated in November 2001.

Prior to the anticipated issuance of fixed rate debt, Northern Border Pipeline entered into forward starting interest rate swap agreements. The interest rate swaps were designated as cash flow hedges as they were entered into to hedge the fluctuations in Treasury rates and spreads between the execution date of the swaps and the issuance of the fixed rate debt. The notional amount of the interest rate swaps did not exceed the expected principal amount of fixed rate debt to be issued. Upon issuance of the fixed rate debt, the swaps were terminated and the proceeds received or amounts paid to terminate the swaps were recorded in accumulated other comprehensive income and amortized to interest expense over the term of the debt.

For the year ended December 31, 2002, Northern Border Pipeline received \$2.4 million from terminated interest rate swaps. For the year ended December 31, 2001, Northern Border Pipeline paid approximately \$4.1 million to terminate interest rate swaps.

During the years ended December 31, 2003, 2002, and 2001 respectively, Northern Border Pipeline amortized approximately \$1.6 million, \$1.4 million, and \$1.2 million related to the terminated derivatives as a reduction to interest expense from accumulated other comprehensive income. Northern Border Pipeline expects to amortize approximately \$1.6 million as a reduction to interest expense in 2004.

Northern Border Pipeline entered into interest rate swap agreements with notional amounts totaling \$225 million in May 2002. Under the interest rate swap agreements, Northern Border Pipeline makes payments to counterparties at variable rates based on the London Interbank Offered Rate and in return receives payments based on a 6.25% fixed rate. At December 31, 2003 and 2002, the average effective interest rate on Northern Border Pipeline's interest rate swap agreements was 2.31% and 2.70%, respectively. Northern Border Pipeline's interest rate swap agreements have been designated as fair value hedges as they were entered into to hedge the fluctuations in the market value of the 2002 Pipeline Senior Notes. The accompanying balance sheet at December 31, 2002, reflects a non-cash gain of approximately \$21.2 million in derivative financial assets with a corresponding increase in long-term debt. The accompanying balance sheet at December 31, 2003, reflects a non-cash gain of approximately \$16.6 million in derivative financial assets with a corresponding increase in long-term debt.



## 7. COMMITMENTS AND CONTINGENCIES

### Operating Leases

Future minimum lease payments under non-cancelable operating leases on office space and rights-of-way are as follows:

(in thousands)

|                          |                  |
|--------------------------|------------------|
| Year ending December 31, |                  |
| 2004                     | \$ 5,757         |
| 2005                     | 2,392            |
| 2006                     | 2,392            |
| 2007                     | 2,392            |
| 2008                     | 2,392            |
| Thereafter               | 3,929            |
|                          | <u>\$ 19,254</u> |

### Cash Balance Plan

As further discussed in Note 11, on December 31, 2003, Enron filed a motion seeking approval of the Bankruptcy Court to provide additional funding to, and for authority to terminate the Enron Corp. Cash Balance Plan and certain other defined benefit plans. Northern Border Pipeline recorded charges associated with the termination of the cash balance plan of \$3.1 million in 2003. Northern Border Pipeline believes this accrual is adequate to cover the likely allocation of these costs.

### Capital expenditures

Total capital expenditures for 2004 are estimated to be \$14 million. Funds required to meet the capital expenditures for 2004 are anticipated to be provided primarily by borrowings under the 2002 Pipeline Credit Agreement and using operating cash flows.

### Environmental Matters

Northern Border Pipeline is not aware of any material contingent liabilities with respect to compliance with applicable environmental laws and regulations.

### Other

On July 31, 2001, the Assiniboine and Sioux Tribes of the Fort Peck Indian Reservation (Tribes) filed a lawsuit in Tribal Court against Northern Border Pipeline to collect more than \$3 million in back taxes, together with interest and penalties. The lawsuit relates to a utilities tax on certain of Northern Border Pipeline's properties within the Fort Peck Indian Reservation. The Tribes and Northern Border Pipeline, through a mediation process, have held settlement discussions and have reached a settlement in principle on pipeline rights-of-way lease and taxation issues. Final documentation has been completed and is subject to the approval of the Bureau of Indian Affairs, which the parties believe will be obtained in the very near term. This settlement grants to Northern Border Pipeline, among other things, (i) an option to renew the pipeline rights-of-way lease upon agreed terms and conditions on or before April 11, 2011 for a term of 25 years with a renewal right for an additional 25 years; (ii) a present right to use additional tribal lands for expanded facilities; and (iii) release and satisfaction of all tribal taxes against Northern Border Pipeline. In consideration of this option and other benefits, Northern Border Pipeline will pay a lump sum amount of \$5.9 million and an annual amount of approximately \$1.5 million beginning April 2004. Northern Border Pipeline intends to seek regulatory recovery of the costs resulting from the settlement.

Various legal actions that have arisen in the ordinary course of business are pending. Northern Border Pipeline believes that the resolution of these issues will not have a material adverse impact on Northern Border Pipeline's results of operations or financial position.

## 8. QUARTERLY FINANCIAL DATA (Unaudited)

| (in thousands) | Operating<br>Revenues, net | Operating<br>Income | Net Income<br>to Partners |
|----------------|----------------------------|---------------------|---------------------------|
| 2003           |                            |                     |                           |
| First Quarter  | \$ 79,892                  | \$ 48,639           | \$ 36,734                 |
| Second Quarter | 80,659                     | 48,915              | 37,617                    |
| Third Quarter  | 81,192                     | 48,050              | 37,195                    |
| Fourth Quarter | 82,442                     | 47,377              | 36,654                    |
| 2002           |                            |                     |                           |
| First Quarter  | \$ 78,155                  | \$ 49,895           | \$ 37,670                 |
| Second Quarter | 80,173                     | 52,014              | 38,506                    |
| Third Quarter  | 81,553                     | 51,843              | 39,197                    |
| Fourth Quarter | 81,169                     | 38,706              | 27,346                    |

## 9. ACCOUNTING PRONOUNCEMENTS

In 2001, the Financial Accounting Standards Board ("FASB") issued SFAS No. 143, "Accounting for Asset Retirement Obligations." SFAS No. 143 requires entities to record the fair value of a liability for an asset retirement obligation in the period in which it is incurred, if the liability can be reasonably estimated. When the liability is initially recorded, the carrying amount of the related asset is increased by the same amount. Over time, the liability is accreted to its future value and the accretion is recorded to expense. The initial adjustment to the asset is depreciated over its useful life. Upon settlement of the liability, an entity either settles the obligation for its recorded amount or incurs a gain or loss. In some instances, Northern Border Pipeline is obligated by contractual terms or regulatory requirements to remove facilities or perform other remediation upon retirement. Northern Border Pipeline was unable to estimate and record liabilities for its obligations that fall under the provisions of this statement because it cannot reasonably estimate when such obligations would be settled. Effective January 1, 2003, Northern Border Pipeline adopted SFAS No. 143, which did not have a material impact on its financial position or results of operations.

In November 2002, the FASB issued Interpretation No. (FIN) 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others". This interpretation elaborates on the disclosures to be made by a guarantor in its interim and annual financial statements about its obligations under certain guarantees that it has issued. It also clarifies that a guarantor is required to recognize, at the inception of a guarantee, a liability for the fair value of the obligation undertaken in issuing the guarantee. The initial recognition and initial measurement provisions of this interpretation are applicable on a prospective basis to guarantees issued or modified after December 31, 2002. FIN 45 did not have a material impact on Northern Border Pipeline's financial position or results of operations.

In April 2003, the FASB issued SFAS No. 149, "Amendment of Statement No. 133 on Derivative Instruments and Hedging Activities." SFAS No. 149 amends and clarifies accounting for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities under SFAS No. 133. SFAS No. 149 did not have a material impact on Northern Border Pipeline's financial position or results of operations.

In May 2003, the FASB issued SFAS No. 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity." This statement establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. SFAS No. 150 is effective for financial instruments entered into or modified after May 31, 2003. SFAS No. 150 did not have a material impact on Northern Border Pipeline's financial position or results of operations.

In May 2003, the Emerging Issues Task Force of the FASB issued EITF No. 00-21, "Revenue Arrangements with Multiple Deliverables." EITF 00-21 requires companies to separate components of a complex contract into separate units of accounting. EITF 00-21 was effective for contracts signed after June 30, 2003, although retroactive application to existing contracts was permitted. EITF 00-21 did not have a material impact on Northern Border Pipeline's financial position or results of operations.

## 10. OTHER INCOME (EXPENSE)

Other income (expense) on the statement of income includes such items as investment income, nonoperating revenues and expenses, and nonrecurring other income and expense items. For the year ended December 31, 2003, other expense included \$0.6 million for a repayment of amounts previously received for vacated microwave frequency bands. For the year ended December 31, 2002, other income included \$0.6 million for amounts received for previously vacated microwave frequency bands. For the year ended December 31, 2001, other income included bad debt expense of \$1.5 million related to the bankruptcy of a telecommunications company that had purchased excess capacity on Northern Border Pipeline's communication system and a \$0.7 million charge for reserves established.

## 11. RELATIONSHIPS WITH ENRON

In December 2001, Enron and certain of its subsidiaries filed voluntary petitions for Chapter 11 reorganization with the U.S. Bankruptcy Court. Northern Plains was not included in the bankruptcy filing and management believes that Northern Plains will continue to be able to meet its operational and administrative service obligations under the existing operating agreement. Enron North America Corp. (ENA), a subsidiary of Enron, was included in the bankruptcy filing.

At the time of the bankruptcy filing, ENA had firm service agreements representing approximately 3.5% of contracted capacity, a portion of which (1.1%) had been temporarily released to a third party until October 31, 2002. Northern Border Pipeline recorded a bad debt expense of approximately \$1.3 million representing ENA's unpaid November and December 2001 transportation, which is included in operations and maintenance expense on the statement of income.

On June 13, 2002, the Bankruptcy Court approved a Stipulation and Order entered into on May 15, 2002, by ENA and Northern Border Pipeline pursuant to which ENA agreed that all but one of the shipper contracts, representing 1.7% of pipeline capacity, would be deemed rejected and terminated. The remaining contract was terminated in the third quarter of 2002. For the year ended December 31, 2002, Northern Border Pipeline has experienced lost revenues of approximately \$1.8 million related to ENA's capacity. Northern Border Pipeline has filed proofs of claims regarding the amount of damages for breach of contract and other claims in the bankruptcy proceeding. However, Northern Border Pipeline cannot predict the amounts, if any, that it will collect or the timing of collection. Northern Border Pipeline believes, however, that any amounts collected will not be material.

On December 31, 2003, Enron filed a motion seeking approval of the Bankruptcy Court to provide additional funding to, and for authority to terminate the Enron Corp. Cash Balance Plan (Plan) and certain other defined benefit plans of Enron's affiliates in 'standard terminations' within the meaning of Section 4041 of the Employee Retirement Income Security Act of 1974, as amended (ERISA). Such standard terminations would satisfy all of the obligations of Enron and its affiliates with respect to funding liabilities under the Plan. In addition, a standard termination would eliminate the contingent claims of Pension Benefit Guaranty Corporation (PBGC) against Enron and its affiliates with respect to funding liabilities under the Plan. On January 30, 2004, the Bankruptcy Court entered an order authorizing termination, additional funding and other actions necessary to effect the relief requested. Pursuant to the Bankruptcy Court order, any contributions to the Plan are subject to the prior receipt of a favorable determination by the Internal Revenue Service that the Plan is tax-qualified as of the date of termination. In addition, the Bankruptcy Court order provides that the rights of PBGC and others to assert that their filed claims have not been released or adjudicated as a result of the Bankruptcy Court order and Enron and all other interested parties retained the right to assert that such claims had been adjudicated or released.

Enron management has informed Northern Plains that it will seek funding contributions from each member of its ERISA controlled group of corporations that employs, or employed, individuals who are, or were, covered under the Plan. Northern Plains has advised Northern Border Pipeline that Northern Plains is a member of a controlled group of corporations of Enron that employs, or employed, individuals who are, or were, covered under the Plan and that an amount of approximately \$3.1 million has been assessed for Northern Border Pipeline's proportionate allocation of Northern Plains' proportionate share of the up to \$200 million estimated termination costs authorized by the Bankruptcy Court order. Under the operating agreement with Northern Plains, these increased costs may be Northern Border Pipeline's responsibility. While the final amounts have not been determined, Northern Border Pipeline believes this accrual is adequate to cover the allocation of these costs.

#### 11. RELATIONSHIPS WITH ENRON (continued)

Northern Border Pipeline continues to monitor developments at Enron, to assess the impact on Northern Border Pipeline of its existing agreements and relationships with Enron, and to take appropriate action to protect Northern Border Pipeline's interests.

#### 12. SUBSEQUENT EVENTS

In December 2003, Northern Border Pipeline's management committee voted to (i) issue equity cash calls to its partners in the total amount of \$130 million in early 2004 and \$90 million in 2007; (ii) fund future growth capital expenditures with 50% equity capital contributions from its partners; and (iii) change the cash distribution policy of Northern Border Pipeline. Effective January 1, 2004, cash distributions will be equal to 100% of distributable cash flow as determined from Northern Border Pipeline's financial statements based upon earnings before interest, taxes, depreciation and amortization less interest expense and less maintenance capital expenditures. Effective January 1, 2008 the cash distribution policy will be adjusted to maintain a consistent capital structure. Under the previous cash distribution policy, approximately \$28-\$30 million was retained annually within Northern Border Pipeline to periodically repay outstanding bank debt. The additional equity contributions in 2004 will be utilized to fully repay Northern Border Pipeline's existing bank debt and thereby reduce its debt leverage in light of existing business conditions. Upon repayment of the existing bank debt, Northern Border Pipeline's next scheduled debt maturity is May 2007.

Northern Border Pipeline makes distributions to its general partners approximately one month following the end of the quarter. The distribution for the fourth quarter of 2003 of approximately \$48.1 million was declared in January 2004 to be paid in January 2004.

In January 2004, the Partnership and TC PipeLines contributed \$45.5 million and \$19.5 million, respectively, to Northern Border Pipeline to be used by Northern Border Pipeline to repay a portion of its existing indebtedness under the 2002 Pipeline Credit Agreement.

## **INDEPENDENT AUDITORS' REPORT ON SCHEDULE**

### **Northern Border Pipeline Company:**

We have audited in accordance with auditing standards generally accepted in the United States of America, the financial statements of Northern Border Pipeline Company as of December 31, 2003 and 2002 and for each of the years in the three-year period ended December 31, 2003 included in this Form 10-K, and have issued our report thereon dated January 27, 2004.

Our audits were made for the purpose of forming an opinion on the basic financial statements taken as a whole. The schedule of Northern Border Pipeline Company listed in Item 14 of Part IV of this Form 10-K is the responsibility of the Company's management and is presented for purposes of complying with the Securities and Exchange Commission's rules and is not part of the basic financial statements. This schedule has been subjected to the auditing procedures applied in the audits of the basic financial statements and, in our opinion, fairly states in all material respects, the financial data required to be set forth therein in relation to the basic financial statements taken as a whole.

KPMG LLP

Omaha, Nebraska  
January 27, 2004

**NORTHERN BORDER PIPELINE COMPANY**  
**SCHEDULE II – VALUATION AND QUALIFYING ACCOUNTS**  
**FOR THE YEARS ENDED DECEMBER 31, 2003, 2002 AND 2001**

(In Thousands)

| Column A                        | Column B                           | Column C                            |                                 | Column D  | Column E                  |
|---------------------------------|------------------------------------|-------------------------------------|---------------------------------|---|---------------------------|
| Description                     | Balance at<br>Beginning<br>of Year | Additions                           |                                 | Deductions  | Balance at<br>End of Year |
|                                 |                                    | Charged to<br>Costs and<br>Expenses | Charged<br>to Other<br>Accounts | For Purpose For<br>Which Reserves<br>Were Created |                           |
| Reserve for regulatory issues   |                                    |                                     |                                 |   |                           |
| 2003                            | \$ 12,294                          | \$ 4,282                            | \$ –                            | \$ 10,261   | \$ 6,315                  |
| 2002                            | \$ 2,531                           | \$ 9,763                            | \$ –                            | \$ –  | \$ 12,294                 |
| 2001                            | \$ 1,800                           | \$ 731                              | \$ –                            | \$ –  | \$ 2,531                  |
| Allowance for doubtful accounts |                                    |                                     |                                 |   |                           |
| 2003                            | \$ 4,805                           | \$ 10                               | \$ –                            | \$ –  | \$ 4,815                  |
| 2002                            | \$ 3,176                           | \$ 3,452                            | \$ –                            | \$ 1,823  | \$ 4,805                  |
| 2001                            | \$ –                               | \$ 3,176                            | \$ –                            | \$ –  | \$ 3,176                  |