

AES CORP  
Form 10-Q/A  
January 19, 2006

# UNITED STATES SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

---

## FORM 10-Q/A

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934

For the Quarterly Period Ended March 31, 2005

or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934

Commission file number 0-19281

## THE AES CORPORATION

(Exact name of registrant as specified in its charter)

**Delaware**

(State or Other Jurisdiction of  
Incorporation or Organization)

**4300 Wilson Boulevard, Suite 1100,  
Arlington, Virginia**

(Address of Principal Executive Offices)

**54-1163725**

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

**22203**

(Zip Code)

**(703) 522-1315**

(Registrant's Telephone Number, Including Area Code)

---

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  No

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

---

The number of shares outstanding of Registrant's Common Stock, par value \$0.01 per share, at April 28, 2005, was 653,174,893.



**THE AES CORPORATION**  
**FORM 10-Q/A**  
**EXPLANATORY NOTE**

This Form 10-Q/A (the Amendment ) is being filed for the purpose of amending Items 1, 2 and 4 of Part I and Item 6 of Part II of Form 10-Q for the quarterly period ended March 31, 2005, that was originally filed with the Securities and Exchange Commission on May 5, 2005. This Amendment is being filed to correct accounting errors in the consolidated financial statements in our previously filed Form 10-Q as of March 31, 2005 and December 31, 2004, and for the three months ended March 31, 2005 and 2004.

This Form 10-Q/A should be read in conjunction with the Company s Form 10-K/A filed with the U.S. Securities and Exchange Commission on January 19, 2006. Refer to Note 1 to the condensed consolidated financial statements in Item 1 of this Form 10-Q/A for a discussion of the nature of the errors and the impact of the errors on the restated condensed consolidated financial statements.

We included as exhibits to this Amendment new certifications of our principal executive officer and principal financial and accounting officer.

This Form 10-Q/A has also been amended to reflect a prior interim period adjustment as required by Statement of Financial Accounting Standards No. 16 (FAS 16) as discussed in Note 1 to the condensed consolidated financial statements. Except for errors and the FAS 16 adjustment disclosed in Note 1, no attempt has been made in this Amendment to amend or update other disclosures presented in this Form 10-Q/A. This Amendment does not reflect events occurring after the filing of Form 10-Q on May 5, 2005 (except as required by Statement of Financial Accounting Standard No. 16), or amend or update those disclosures, including exhibits to the Form 10-Q affected by subsequent events. Accordingly, this Amendment should be read in conjunction with our filings with the SEC subsequent to the filing of the Form 10-Q, including any amendments to those filings.

**THE AES CORPORATION**  
**FORM 10-Q/A**  
**FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2005**  
**TABLE OF CONTENTS**

**PART I: Financial Information** (unaudited)

Item 1. Financial Statements

Condensed Consolidated Statements of Operations for the Three Months Ended March 31, 2005 (as restated) and 2004 (as restated) 4

Condensed Consolidated Balance Sheets as of March 31, 2005 (as restated) and December 31, 2004 (as restated) 5

Condensed Consolidated Statements of Cash Flows for the Three Months Ended March 31, 2005 (as restated) and 2004 (as restated) 6

Notes to Condensed Consolidated Financial Statements (as restated) 7

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (as restated) 27

Item 3. Quantitative and Qualitative Disclosures about Market Risk 42

Item 4. Controls and Procedures 42

**PART II: Other Information**

Item 1. Legal Proceedings 47

Item 2. Unregistered Sales of Securities and Use of Proceeds 50

Item 3. Defaults Upon Senior Securities 50

Item 4. Submissions of Matters to a Vote of Security Holders 50

Item 5. Other Information 50

Item 6. Exhibits 51

Signatures 52

**PART I: FINANCIAL INFORMATION****ITEM 1. FINANCIAL STATEMENTS**

**THE AES CORPORATION**  
**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**  
**(Unaudited)**  
**(Amounts in Millions, Except per Share Amounts)**

	<b>Three Months Ended</b>	
	<b>March 31,</b>	
	<b>2005</b>	<b>2004</b>
	<b>(Restated)*</b>	<b>(Restated)*</b>
Revenues		
Regulated	\$ 1,399	\$ 1,145
Non-regulated	1,264	1,111
Total revenues	2,663	2,256
Cost of sales		
Regulated	(1,032 )	(883 )
Non-regulated	(807 )	(689 )
Total cost of sales	(1,839 )	(1,572 )
Gross margin	824	684
General and administrative expenses	(49 )	(48 )
Interest expense	(467 )	(501 )
Interest income	90	69
Other income	22	11
Other expense	(37 )	(25 )
Loss on sale of investments and asset impairment expense		(1 )
Foreign currency transaction losses, net	(31 )	(34 )
Equity in earnings of affiliates	25	16
INCOME BEFORE INCOME TAXES AND MINORITY INTEREST	377	171
Income tax expense	(147 )	(75 )
Minority interest expense	(106 )	(54 )
INCOME FROM CONTINUING OPERATIONS	124	42
Loss from operations of discontinued businesses (net of income tax expense of \$2 in 2004)		(26 )
NET INCOME	\$ 124	\$ 16
Basic Earnings Per Share:		
Income from continuing operations	\$ 0.19	\$ 0.07
Discontinued operations		(0.04 )
BASIC EARNINGS PER SHARE	\$ 0.19	\$ 0.03
Diluted Earnings Per Share:		
Income from continuing operations	\$ 0.19	\$ 0.07
Discontinued operations		(0.04 )
DILUTED EARNINGS PER SHARE	\$ 0.19	\$ 0.03

\* See Note 1

See Notes to Condensed Consolidated Financial Statements.

**THE AES CORPORATION**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**  
(Amounts in Millions, Except Shares and Par Value)  
(Unaudited)

	March 31, 2005 (Restated)*	December 31, 2004 (Restated)*
<b>ASSETS</b>		
Current Assets:		
Cash and cash equivalents	\$ 1,499	\$ 1,281
Restricted cash	334	395
Short-term investments	114	268
Accounts receivable, net of allowances (\$322 and \$303, respectively)	1,547	1,575
Inventory	413	418
Receivable from affiliate	7	8
Deferred income taxes - current	288	218
Prepaid expenses	110	87
Other current assets	732	736
Total current assets	5,044	4,986
Property, Plant and Equipment:		
Land	783	788
Electric generation and distribution assets	21,761	21,729
Accumulated depreciation and amortization	(5,431 )	(5,259 )
Construction in progress	1,107	919
Property, plant and equipment - net	18,220	18,177
Other Assets:		
Deferred financing costs - net	327	343
Investments in and advances to affiliates	684	655
Debt service reserves and other deposits	678	737
Goodwill - net	1,460	1,419
Deferred income taxes - noncurrent	740	774
Other assets	1,792	1,832
Total other assets	5,681	5,760
Total	\$ 28,945	\$ 28,923
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current Liabilities:		
Accounts payable	\$ 1,106	\$ 1,142
Accrued interest	409	335
Accrued and other liabilities	1,769	1,656
Recourse debt - current portion	146	142
Non-recourse debt - current portion	1,749	1,619
Total current liabilities	5,179	4,894
Long-Term Liabilities:		
Non-recourse debt	11,438	11,817
Recourse debt	5,016	5,010
Deferred income taxes	781	685
Pension liabilities and other post-retirement liabilities	869	891
Other long-term liabilities	3,217	3,375
Total long-term liabilities	21,321	21,778
Minority Interest	1,352	1,279
Commitments and contingent liabilities (See Note 5)		
Stockholders' Equity:		
Common stock (\$.01 par value, 1,200,000,000 shares authorized; 652,510,917 and 650,093,402 shares issued and outstanding, respectively)	7	7
Additional paid-in capital	6,454	6,423
Accumulated deficit	(1,691 )	(1,815 )
Accumulated other comprehensive loss	(3,677 )	(3,643 )
Total stockholders' equity	1,093	972
Total	\$ 28,945	\$ 28,923

\* See Note 1

See Notes to Condensed Consolidated Financial Statements.



**THE AES CORPORATION**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(Amounts in millions)  
(Unaudited)

	Three months ended March 31,	
	2005 (Restated)*	2004 (Restated)*
<b>OPERATING ACTIVITIES:</b>		
Net cash provided by operating activities	\$ 518	\$ 401
<b>INVESTING ACTIVITIES:</b>		
Property additions	(271 )	(190 )
Acquisitions net of cash acquired	(85 )	
Proceeds from the sales of assets	3	27
Proceeds from the sales of emission allowances	2	
Sale of short-term investments	493	419
Purchase of short-term investments	(335 )	(478 )
Decrease (increase) in restricted cash	67	(435 )
Decrease (increase) in debt service reserves and other assets	27	(4 )
Other investing	(7 )	7
Net cash used in investing activities	(106 )	(654 )
<b>FINANCING ACTIVITIES:</b>		
Borrowings under the revolving credit facilities	10	
Issuance of recourse debt	5	491
Issuance of non-recourse debt and other coupon bearing securities	411	642
Repayments of recourse debt		(806 )
Repayments of non-recourse debt and other coupon bearing securities	(586 )	(667 )
Payments for deferred financing costs	(1 )	(40 )
Dividends to minority interests, net	(21 )	(8 )
Issuance of common stock	8	2
Other financing	(2 )	(1 )
Net cash used in financing activities	(176 )	(387 )
Effect of exchange rate changes on cash	(18 )	(15 )
Total increase (decrease) in cash and cash equivalents	218	(655 )
Cash and cash equivalents, beginning	1,281	1,663
Cash and cash equivalents, ending	\$ 1,499	\$ 1,008
<b>SUPPLEMENTAL DISCLOSURES:</b>		
Cash payments for interest net of amounts capitalized	\$ 374	\$ 373
Cash payments for income taxes net of refunds	\$ 73	\$ 35
<b>SCHEDULE OF NONCASH INVESTING AND FINANCING ACTIVITIES:</b>		
Common stock issued for debt retirement	\$	\$ 51
Brasiliana Energia debt exchange	\$	\$ 773

\* See Note 1

See Notes to Condensed Consolidated Financial Statements.



**THE AES CORPORATION**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**1. FINANCIAL STATEMENT PRESENTATION**

**Consolidation**

The condensed consolidated financial statements include the accounts of The AES Corporation, its subsidiaries and controlled affiliates ( Company or AES ). Furthermore, variable interest entities in which the Company has an interest have been consolidated where the Company is identified as the primary beneficiary. In all cases, AES holds a majority ownership interest in those variable interest entities that have been consolidated. Investments in which the Company has the ability to exercise significant influence but not control are accounted for using the equity method. All intercompany transactions and balances have been eliminated in consolidation.

**Interim Financial Presentation**

The accompanying unaudited condensed consolidated financial statements and footnotes have been prepared in accordance with generally accepted accounting principles in the United States of America for interim financial information and Article 10 of Regulation S-X of the Securities and Exchange Commission ( SEC ). Accordingly, they do not include all the information and footnotes required by generally accepted accounting principles in the United States of America for annual fiscal reporting periods. In the opinion of management, the interim financial information includes all adjustments of a normal recurring nature necessary for a fair statement of the results of operations, financial position and cash flows for the interim periods. The results of operations for the three months ended March 31, 2005 are not necessarily indicative of results that may be expected for the year ending December 31, 2005. The accompanying condensed consolidated financial statements are unaudited and should be read in conjunction with the audited 2004 consolidated financial statements and notes thereto, which are included in the Company s Annual Report on Form 10-K/A for the year ended December 31, 2004 as filed with the SEC on January 19, 2006.

**New Accounting Standards**

*Share-Based Payment.* In December 2004, the Financial Accounting Standards Board ( FASB ) issued a revised Statement of Financial Accounting Standard ( SFAS ) No. 123 ( SFAS No. 123R ), Share-Based Payment, which is a revision of SFAS No. 123. SFAS No. 123R eliminates the intrinsic value method under Accounting Principles Board No. 25 ( APB 25 ) as an alternative method of accounting for stock-based awards by requiring that all share-based payments to employees, including grants of stock options for all outstanding years be recognized in the financial statements based on their fair values. It also revises the fair-value based method of accounting for share-based payment liabilities, forfeitures and modifications of stock-based awards and clarifies the guidance under SFAS No. 123 related to measurement of fair value, classifying an award as equity or as a liability and attributing compensation to reporting periods. In addition, SFAS No. 123R amends SFAS No. 95, Statement of Cash Flows, to require that excess tax benefits be reported as a financing cash flow rather than as an operating cash flow.

Management is currently evaluating the effect of adoption of SFAS No. 123R under the modified prospective application transition method, but does not expect the adoption to have a material effect on the Company s financial condition, results of operations or cash flows, as the Company had previously adopted income statement treatment for compensation related to share-based payments under SFAS No. 123.

On April 14, 2005, the SEC deferred the effective date of SFAS No. 123R until the beginning of 2006 for calendar year companies.

*Implicit Variable Interest Entities.* In March 2005, the FASB issued Staff Position ( FSP ) No. FIN 46(R)-5, *Implicit Variable Interests under FASB Interpretation No. 46 (revised December 2003), Consolidation of Variable Interest Entities* . This FSP clarifies that when applying the variable interest consolidation model, a reporting enterprise should consider whether it holds an implicit variable interest in a variable interest entity (VIE) or potential VIE. FSP No. FIN 46(R)-5 is effective as of April 1, 2005. Management is currently evaluating the effect that adoption of FSP No. FIN 46(R)-5 will have on the Company's financial position and results of operations.

*Asset Retirement Obligations.* In March 2005, the FASB issued FASB Interpretation No. ( FIN ) 47 *Accounting for Conditional Asset Retirement Obligations*, an interpretation of FASB Statement No. 143 , which clarifies the term *conditional asset retirement obligation* as used in SFAS No. 143 *Accounting for Asset Retirement Obligations* . Specifically, FIN 47 provides that an asset retirement obligation is conditional when either the timing and/or method of settling the obligation is conditioned on a future event. Accordingly, an entity is required to recognize a liability for the fair value of a conditional asset retirement obligation if the fair value of the liability can be reasonably estimated. Uncertainty about the timing and/or method of settlement of a conditional asset retirement obligation should be factored into the measurement of the liability when sufficient information exists. This interpretation also clarifies when an entity would have sufficient information to reasonably estimate the fair value of an asset retirement obligation. FIN 47 is effective for fiscal years ending after December 15, 2005. Management is currently evaluating the effect that adoption of FIN 47 will have on the Company's financial position and results of operations.

#### **Restatement of Financial Statements**

In our previously filed Form 10-K, for the year ended December 31, 2004, management reported that a material weakness existed in its internal controls over financial reporting related to accounting for income taxes. Specifically, the Company lacked effective controls for the proper reconciliation of the components of its foreign subsidiaries' income tax assets and liabilities to related consolidated balance sheet accounts.

After examining certain historical purchase transactions from 1999 - 2002 and reviewing the reconciliations of detailed historical income tax return records to reported book/income tax differences, various accounting errors were identified. As a result of these initial findings, on July 27, 2005 the Company announced that it would restate its previously filed financial statements. Management also expanded the scope of the review to include the composition of other material current and deferred income tax related balances including those recorded by, or on behalf of, our domestic subsidiaries and the parent company. As a result of this expanded review, additional non-tax items also were identified and corrected. A discussion of both income tax and non-tax adjustments follows.

The errors identified from the income tax review can be categorized into three types of deferred tax issues. Details regarding material findings associated with each issue are provided below:

#### **1. Deferred income tax adjustments associated with foreign acquisitions and restructurings**

##### *La Electricidad de Caracas ( EDC )*

The most significant deferred income tax restatement adjustment related to the purchase of a majority interest in EDC, a private integrated utility in Venezuela in June, 2000. At that time, a deferred income tax liability was recorded representing the difference between the non-inflation indexed income tax basis and the resulting adjusted purchase basis (assigned carrying value) of fixed assets. However, Venezuelan income tax provisions allow for the indexing of EDC's non-monetary assets and equity, as a result of inflation. This indexing created an additional layer of tax basis that should have been included as part of the acquisition income tax basis at the time of the acquisition.

In addition, several other purchase accounting adjustments were recorded to correctly account for the treatment of deferred charges and the fair value applied to an equity investment held by EDC at the time of acquisition. The recording of the deferred income tax asset related to indexation and the other noted



adjustments affected the allocation of the excess fair value over cost (commonly referred to as negative goodwill) to non-monetary assets.

*Eletropaulo Metropolitana Electricidade de Sao Paulo S.A. ( Eletropaulo )*

At the time of the acquisition of Eletropaulo, a regulated utility located in Brazil, the Company did not record certain deferred income taxes on the difference between the tax basis of land and the related book basis which was adjusted to fair value under acquisition accounting guidelines. The correction of this error resulted in the recording of additional deferred income tax liabilities at the initial date of consolidation in February 2002. This increase in deferred income tax liability increased the original goodwill calculated as the excess purchase price over the fair value of assets and liabilities. As a further result, this adjustment also increased goodwill impairment expense subsequently recognized in 2002.

*Brasiliiana Energia, S.A. ( Brasiliiana )*

In January, 2004 the Company entered into a debt restructuring transaction with the Brazilian National Bank for Economic and Social Development ( BNDES ), whereby BNDES received a 54% economic interest in our Brazil distribution business and two generating facilities in exchange for the cancellation of \$863 million of debt and accrued interest owed by AES Elpa and AES Transgas, holding companies for the Brazilian operations. After the Company made a cash payment of \$90 million, the remaining indebtedness of \$510 million, was re-profiled at a 9% stated interest rate with extended maturities. This exchange was accounted for as a modification of debt. The terms of the agreement state that penalty interest as of December 31, 2004 of \$194 million would be cancelled in the future ratably as the principal of the new \$510 million debentures are paid within the stated timeframes. This treatment gave rise to a deferred income tax liability. As a result of the income tax review, it was determined that a deferred income tax liability should have been recorded for \$194 million of penalty interest anticipated to be forgiven in the future. To correct this error, the additional deferred income tax liability was recorded as part of the stock issued for debt restructuring transaction, with the following impacts:

- A deferred income tax liability at Brasiliiana (the new parent company of the restructured entities), was recorded as of January, 2004. This deferred liability is also subject to foreign currency remeasurement in each subsequent reporting period.
- Debt modification calculations were adjusted to include the fair value of the increased income tax expense due to the forgiveness of debt compared to the book value of debt remaining. The resulting impact reduced the debt discount and decreased the effective interest rate. This adjustment did not change our conclusion regarding the accounting treatment of the transaction as a modification of debt.

These adjustments also impacted the amounts recorded to reflect the BNDES debt restructuring described above. This impact is described below in the Other Non Income Tax Adjustments section.

*Other Acquisition Related Income Tax Adjustments*

As a result of the comprehensive review of income tax accounting, certain other adjustments were made to correct errors identified at other subsidiaries, primarily related to recording of deferred income taxes arising from the step up of acquired assets to fair value and/or from other purchase accounting items. These adjustments increased or decreased fixed assets or concession assets and as a result impacted depreciation or amortization charges recorded within the Company's statements of operations.

**2. Foreign currency remeasurement of deferred income tax balances where the U.S. dollar is the functional currency at certain subsidiaries**

The functional currency for certain of the Company's foreign subsidiaries is the U.S. dollar. After reviewing the income tax balances for certain of the Company's U.S. dollar entities in Venezuela, Brazil, Chile, Colombia, Dominican Republic, Argentina and Mexico, the Company discovered that deferred income taxes were remeasured from local currency to the U.S. dollar using the historical exchange rate

versus the current exchange rate as prescribed by Statement of Financial Accounting Standard ( SFAS ) No. 52, Foreign Currency Translation and SFAS No. 109, Accounting for Income Taxes, starting in the year of acquisition or formation. In addition, as noted above, certain additional deferred tax amounts were recorded in these entities, which also required remeasurement the largest of which was the additional deferred tax asset related to the EDC purchase accounting indexation adjustment described above.

### **3. Reconciliation of income tax returns to U.S. GAAP income tax balances**

The remediation plan involved a detailed review of current and temporary differences identified through an analysis of local income tax return filings. The completion of this review also required the Company to fully evaluate adjustments which had been previously recorded in consolidation, but which should have been recorded at a subsidiary level where the appropriate analysis of the tax jurisdiction could be made. This process led to the identification of errors that accounted for the remainder of the deferred income tax entries.

*Establishment of Deferred Tax Liability for Brazilian Unrealized Foreign Currency Gains* Certain of the Company's Brazilian subsidiaries have designated the U.S. dollar as the functional currency for accounting purposes. For Brazilian tax purposes, these companies have elected to treat these exchange gains or losses as taxable or deductible only when cash payments are made. The Company did not record deferred assets or liabilities related to the unrealized gains and losses that occur on an interim basis related to its U.S. dollar denominated debt. Under U.S. GAAP, these increases/decreases in deferred liabilities/assets are permanent differences that are recorded as an adjustment to tax expense.

*Establishment of a U.S. Liability Related to Brazilian Deferred Tax Assets* One of the Company's Brazilian subsidiaries, Sul, which has designated its functional currency as the Brazilian real, has generated deferred tax assets mainly related to net operating losses, unrealized tax losses on foreign currency transactions and certain other taxable temporary differences. A restructuring transaction was undertaken in relation to this subsidiary in July 2002. At the time of this restructuring, the Company should have recorded a reduction to the deferred tax assets for the U.S. income tax liability associated with the future projected Brazilian taxable income.

*Establishment of Other Valuation Allowances* The Company determined that certain valuation allowances should have been provided at various subsidiaries in Chile, Colombia, Brazil and Argentina related to deferred tax assets recorded primarily related to net operating loss carryforwards. Under U.S. GAAP, the Company is required to assess its ability to utilize deferred tax assets under a more likely than not standard and provide a valuation allowance to the extent the asset or any part of it does not meet this test. As part of the deferred tax review, the Company determined that these deferred tax assets were unlikely to be utilized in full or in part, based on information available in these historical periods and consequently did not meet the more likely than not standard.

*Other Tax Expense Items* The Company undertook a detailed comparison of the tax returns filed to accounting records in a majority of the countries in which we operate and identified certain other adjustments related to this reconciliation. Most significantly, these adjustments included the following:

- non-deductibility of certain holding company interest and goodwill;
- capitalized interest on tax holiday projects;
- treatment of certain foreign investment tax credits;
- reconciliation of other deferred tax balances; and
- changes in pre-tax book income related to other non-tax restatement adjustments.

### ***Other Non-Income Tax Adjustments***

## Edgar Filing: AES CORP - Form 10-Q/A

Other non-income tax accounting errors were also identified as part of the Company's review of certain other historical transactions. The Company has concluded that the reasons for these errors primarily related to the lack of sufficient control and documentation procedures in 2002 and prior years

10

---

related to certain consolidation and foreign currency translation processes. Significant non-income tax errors are described below:

*AES SONEL*

AES acquired 56% of SONEL located in Cameroon in July, 2001. Since that time, AES SONEL experienced a high degree of turnover of its senior accounting personnel. SONEL's accounting systems required a significant degree of manual intervention including the conversion of local GAAP financial statements into U.S. GAAP.

During the Company's 2004 year-end process, the Company discovered errors in minority interest calculations that were corrected in the Company's restated financial statements as of and for the years ended December 31, 2003 and 2002 as filed with the Securities and Exchange Commission on Form 10-K on March 30, 2005. Subsequently, as part of the Corporate process to ensure the correct communication and documentation of the correction of the initial error at the subsidiary level, a comprehensive additional review of the preparation of the U.S. GAAP financial statements was performed and the following errors were identified:

- translation errors from local currency to U.S. dollar financial statements;
- the omission of certain purchase accounting adjustments related to the final valuation of our concession assets and recording of severance provisions from the U.S. GAAP financial statements; and
- incorrect treatment related to the accounting for dividends.

*AES Elpa*

As a result of the income tax review performed at AES Elpa, one of the Company's Brazilian holding companies, the Company identified a long-term liability which had been recorded for Brazilian GAAP but which had been omitted from U.S. GAAP financial statements at the acquisition date. The proper recording of this liability at the acquisition date would have increased the opening balance of goodwill, which was subsequently impaired and thereby written off as of the end of December, 2002. The impact of this adjustment as of December 31, 2002, increased long term liabilities and increased goodwill impairment expense and prior retained earnings by the same combined amount. This long-term liability is accreted by an interest expense component on a monthly basis.

*AES Tiete*

The Company determined that an error had been made in the initial accounting for a debt instrument which had been assumed at the date of purchase of Tiete, a generation company in Brazil, in 1999. The debt requires an annual adjustment to principal based on changes in the local rate of inflation. The Company accounted for this by using estimates of future inflation over the life of the debt and amortizing these adjustments as a component of interest expense over the term of the loan. These future inflation estimates were recorded on the balance sheet as a deferred financing cost within long-term assets. Periodically, adjustments were made to these estimates when the actual annual inflation calculations were charged to the principal balance. Subsequently, it was determined that inflation changes should be calculated and adjusted on a monthly basis through interest expense based on the rate of inflation in that month, regardless of how the actual cash payment would finally be determined.

*SUL and Eletropaulo*

The Company determined that an error had been made regarding the timing of the recognition of certain revenues recorded by its Brazilian utilities - Eletropaulo and Sul. The tariff rates, as set by the Brazilian regulatory authority (ANEEL) provide that a percentage of a distributor's revenue is added to the consumer tariff rate in return for the Company's future spending of these amounts on capital or operating expense projects approved by ANEEL for the express purpose of improving the efficiency of the electrical system. Eletropaulo and Sul had previously recognized the revenue related to this portion of the

tariff when billed, and recorded the future operating expense and capital project expenditures when incurred, since the expenditures were not considered pass through costs for purpose of a future tariff reset. However, under the guidance of SFAS 71 Accounting for the Effects of Certain Types of Regulation, Eletropaulo and Sul should have deferred this portion of revenue until such time that the related expenditures were incurred.

#### *Brasiliiana Energia*

The correction of the error related to AES Elpa described above and other adjustments prior to January 2004 which impacted the net assets of Eletropaulo, Tiete and Uruguaiana, also impacted the recording of the Brazilian debt restructuring transaction with our lender, BNDES, as described earlier. The impact on the 2004 restated financials decreased the minority interest share allocated to BNDES and increased additional paid-in capital, a component of stockholders' equity. The adjustment to additional paid-in capital was recorded in accordance with the Company's previously established accounting policy pertaining to gains or losses resulting from subsidiary sales of stock as permitted under SEC Staff Accounting Bulletin No. 51, Accounting for Sales of Stock by a Subsidiary.

#### *Corporate Consolidation Accounting*

During the restatement period, the Company undertook additional reviews of the consolidation process, including a review of consolidation journal entries to ascertain that appropriate supporting documentation existed and that current personnel who were performing the consolidation understood the basis for these entries. Several historical consolidation elimination adjustments were identified as errors which primarily affected deferred income taxes and other accumulated comprehensive income balances. The errors originated in years prior to 2002 and generally resulted from an inadequately controlled consolidation process including the elimination of investment accounts against subsidiary equity balances, general balancing controls related to the income statements and balance sheets submitted by our subsidiaries, and inadequate balance sheet reconciliations of consolidated deferred income tax accounts. The correcting entries resulted primarily in a decrease in deferred income tax liabilities and an increase in foreign currency translation, a component of other comprehensive income.

#### *Cash Classifications*

As part of an ongoing balance sheet review process, it came to the Company's attention that several of its subsidiaries incorrectly included certain short-term investments as cash and cash equivalents in the balance sheet. The restatement impact was a decrease in cash and cash equivalents and an increase in short-term investments as of March 31, 2005 and December 31, 2004, respectively.

#### *Cash Flow Reclassification*

The Company includes components of the cash flows for its discontinued operations within the Consolidated Statements of Cash Flows ( Cash Flow Statement ) in operating, investing and financing activities. A separate line entitled Decrease in cash and cash equivalents of discontinued operations and businesses held for sale was previously presented on the face of Cash Flow Statement to reconcile back to the Company's cash balance on the face of the Consolidated Balance Sheets, which excludes cash from discontinued operations. As part of the restatement, the Company has changed its presentation to include the net change in cash balances for discontinued operations as a component of net cash from operating activities.

#### *Other Immaterial Errors*

Certain other immaterial errors were identified and corrected in the appropriate periods.

The following tables set forth the previously reported and restated amounts of selected items within the condensed consolidated balance sheets as of March 31, 2005 and December 31, 2004, within the condensed consolidated statements of operations and comprehensive income for the three months ended



Edgar Filing: AES CORP - Form 10-Q/A

March 31, 2005 and 2004, and within the condensed consolidated statements of cash flows for the three months ended March 31, 2005 and 2004.

**Selected Balance Sheet Data: (\$ in millions)**

	March 31, 2005		December 31, 2004	
	As Previously Reported	As Restated	As Previously Reported	As Restated
<b>Assets</b>				
Cash & cash equivalents	\$ 1,555	\$ 1,499	\$ 1,408	\$ 1,281
Short term investments	\$ 57	\$ 114	\$ 141	\$ 268
Deferred income taxes - current	\$ 193	\$ 288	\$ 187	\$ 218
Prepaid expenses	\$ 116	\$ 110	\$ 93	\$ 87
Other current assets	\$ 674	\$ 732	\$ 713	\$ 736
Total current assets	\$ 4,896	\$ 5,044	\$ 4,938	\$ 4,986
Electric generation and distribution assets	\$ 22,463	\$ 21,761	\$ 22,434	\$ 21,729
Accumulated depreciation	\$ 5,530	\$ 5,431	\$ 5,353	\$ 5,259
Property, plant and equipment, net	\$ 18,823	\$ 18,220	\$ 18,788	\$ 18,177
Deferred financing costs, net	\$ 496	\$ 327	\$ 513	\$ 343
Goodwill, net	\$ 1,422	\$ 1,460	\$ 1,378	\$ 1,419
Deferred income taxes-noncurrent	\$ 798	\$ 740	\$ 813	\$ 774
Other assets	\$ 1,866	\$ 1,792	\$ 1,910	\$ 1,832
Total other assets	\$ 5,944	\$ 5,681	\$ 6,006	\$ 5,760
Total assets	\$ 29,663	\$ 28,945	\$ 29,732	\$ 28,923
<b>Liabilities and Stockholders' Equity</b>				
Accrued and other liabilities	\$ 1,686	\$ 1,769	\$ 1,583	\$ 1,656
Non-recourse debt-current	\$ 1,748	\$ 1,749	\$ 1,618	\$ 1,619
Total current liabilities	\$ 5,095	\$ 5,179	\$ 4,822	\$ 4,894
Non-recourse debt-noncurrent	\$ 11,435	\$ 11,438	\$ 11,813	\$ 11,817
Deferred income taxes -noncurrent	\$ 729	\$ 781	\$ 685	\$ 685
Other long-term liabilities	\$ 3,108	\$ 3,217	\$ 3,261	\$ 3,375
Total long-term liabilities	\$ 21,157	\$ 21,321	\$ 21,660	\$ 21,778
Minority interest	\$ 1,663	\$ 1,352	\$ 1,605	\$ 1,279
Additional paid-in-capital	\$ 6,368	\$ 6,454	\$ 6,341	\$ 6,423
Accumulated deficit	\$ 680	\$ 1,691	\$ 813	\$ 1,815
Accumulated other comprehensive loss	\$ 3,947	\$ 3,677	\$ 3,890	\$ 3,643
Total stockholders' equity	\$ 1,748	\$ 1,093	\$ 1,645	\$ 972
Total liabilities and stockholders' equity	\$ 29,663	\$ 28,945	\$ 29,732	\$ 28,923

**Selected Statement of Operations and Comprehensive Income Data: (\$ in millions)**

	March 31, 2005		March 31, 2004	
	As Previously Reported	As Restated	As Previously Reported	As Restated
Regulated revenues	\$ 1,381	\$ 1,399	\$ 1,146	\$ 1,145
Regulated cost of sales	\$ 1,056	\$ 1,032	\$ 889	\$ 883
Non-regulated cost of sales	\$ 807	\$ 807	\$ 688	\$ 689
Total cost of sales	\$ 1,863	\$ 1,839	\$ 1,577	\$ 1,572
Gross margin	\$ 782	\$ 824	\$ 680	\$ 684
Interest expense	\$ 467	\$ 467	\$ 493	\$ 501
Foreign currency transaction losses, net	\$ 12	\$ 31	\$ 8	\$ 34
Income before income taxes and minority interest	\$ 350	\$ 377	\$ 201	\$ 171
Income tax expense	\$ 126	\$ 147	\$ 64	\$ 75
Minority interest expense	\$ 91	\$ 106	\$ 63	\$ 54
Income from continuing operations	\$ 133	\$ 124	\$ 74	\$ 42
Net income	\$ 133	\$ 124	\$ 48	\$ 16
Unrealized currency translation (losses) gains	\$ (18 )	\$ (10 )	\$ 10	\$ 18
Change in fair value of derivatives in comprehensive loss	\$ 39	\$ 24	\$ 107	\$ 107
Comprehensive income (loss)	\$ 76	\$ 90	\$ (49 )	\$ (73 )
<b>BASIC EARNINGS PER SHARE:</b>				
Income from continuing operations	\$ 0.20	\$ 0.19	\$ 0.12	\$ 0.07
Discontinued operations			(0.04 )	(0.04 )
Cumulative effect of accounting change				
<b>BASIC EARNINGS PER SHARE:</b>	\$ 0.20	\$ 0.19	\$ 0.08	\$ 0.03
<b>DILUTED EARNINGS PER SHARE:</b>				
Income from continuing operations	\$ 0.20	\$ 0.19	\$ 0.12	\$ 0.07
Discontinued operations			(0.04 )	(0.04 )
Cumulative effect of accounting change				
<b>DILUTED EARNINGS PER SHARE:</b>	\$ 0.20	\$ 0.19	\$ 0.08	\$ 0.03

**Selected Statement of Cash Flow Data: (\$ in millions)**

	March 31, 2005		March 31, 2004	
	As Previously Reported	As Restated	As Previously Reported	As Restated
Net cash provided by operating activities	\$ 520	\$ 518	\$ 402	\$ 401
Net cash used in investing activities	\$ 166	\$ 106	\$ 631	\$ 654
Net cash used in financing activities	\$ 176	\$ 176	\$ 387	\$ 387
Cash and cash equivalents, beginning	\$ 1,396	\$ 1,281	\$ 1,727	\$ 1,663
Cash and cash equivalents, ending	\$ 1,555	\$ 1,499	\$ 1,095	\$ 1,008

**Prior Interim Period Adjustment**

On July 4, 2005, the National Electric Energy Agency ( ANEEL ), an independent federal regulatory agency which has exclusive authority over the Brazilian power industry, concluded its assessment and determination of prior year tariff adjustments (the Tariff Reset ) for Eletropaulo, a distribution company in Brazil included in the Large Utilities segment. The Tariff Reset includes an adjustment to the regulatory base rate and to the associated operating costs for services performed and costs incurred during the period July 2003 through June 2005. The Tariff Reset also includes an adjustment for the recovery of other costs



incurred during the period July 2004 through June 2005, not recovered in the 2004 tariff adjustment. The collection and recovery period for the Tariff Reset will be July 2005 through July 2006.

In accordance with SFAS No. 16, Prior Period Adjustments, the Company has accounted for and reported the adjustment of utility revenue under rate-making processes that relates to prior interim periods of the current fiscal year in its consolidated financial statements as follows:

- The portion of the Tariff Reset related to business activities for the period of July 2003 through December 2004 are included in the determination of net income for the three months ended March 31, 2005. The increase to revenues, gross margin, income from continuing operations, net income and diluted earnings per share for this portion of the Tariff Reset was \$17 million, \$31 million, \$7 million, \$7 million, and \$0.01 per share, respectively.
- The portion of the Tariff Reset related to business activities for the period of January through March 2005 are included in the determination of net income for the three months ended March 31, 2005. The increase to revenues, gross margin, income from continuing operations, net income and diluted earnings per share for this portion of the Tariff Reset was \$5 million, \$8 million, \$2 million, \$2 million, and \$0.00 per share, respectively.

The adjustment to the three months ended March 31, 2005 is required pursuant to SFAS No. 16 and is not an accounting error pursuant to Accounting Principles Board ( APB ) Opinion No. 20, Accounting Changes.

## 2. INVENTORY

Inventory consists of the following (in millions):

	March 31, 2005	December 31, 2004
Coal, fuel oil and other raw materials	\$ 175	\$ 193
Spare parts and supplies	238	225
Total	\$ 413	\$ 418

## 3. EARNINGS PER SHARE

Basic and diluted earnings per share are based on the weighted average number of shares of common stock and potential common stock outstanding during the period, after giving effect to stock splits, as applicable. Potential common stock, for purposes of determining diluted earnings per share, includes the effects of dilutive stock options, warrants, deferred compensation arrangements, and convertible securities. The effect of such potential common stock is computed using the treasury stock method or the if-converted method, as applicable.

The following table presents a reconciliation (in millions) of the numerators and denominators of the basic and diluted earnings per share computations for income from continuing operations. In the table below, income represents the numerator and shares represent the denominator:

	Three Months Ended March 31, 2005			2004		
	Income	Shares	\$ per Share	Income	Shares	\$ per Share
<b>BASIC EARNINGS PER SHARE:</b>						
Income from continuing operations	\$ 124	651	\$ 0.19	\$ 42	627	\$ 0.07
<b>EFFECT OF DILUTIVE SECURITIES:</b>						
Stock options and warrants		11			7	
Restricted stock units		1				
<b>DILUTED EARNINGS PER SHARE</b>	<b>\$ 124</b>	<b>663</b>	<b>\$ 0.19</b>	<b>\$ 42</b>	<b>634</b>	<b>\$ 0.07</b>

There were approximately 8,609,769 and 27,024,582 options outstanding at March 31, 2005 and 2004, respectively, that were omitted from the earnings per share calculation because they were anti-dilutive. In addition, all convertible debentures were omitted from the earnings per share calculation because they were anti-dilutive.

#### 4. SUMMARIZED INCOME STATEMENT INFORMATION OF AFFILIATES

The following table summarizes financial information (in millions) of the entities in which the Company has the ability to exercise significant influence but does not control, and that are accounted for using the equity method.

	Three Months Ended March 31,	
	2005	2004
Revenues	\$ 250	\$ 230
Gross Margin	\$ 77	\$ 77
Net Income	\$ 51	\$ 46

In accordance with APB 18, the Company discontinues the application of the equity method when an investment is reduced to zero and does not provide for additional losses when the Company does not guarantee the obligations of the investee, or is not otherwise committed to provide further financial support for the investee. The above table excludes income statement information for the Company's investments in which the Company has discontinued the application of the equity method. Furthermore, in accordance with APB 18, the Company's policy is to resume the application of the equity method if the investee subsequently reports net income only after the Company's share of that net income equals the share of net losses not recognized during the period the equity method was suspended.

#### 5. CONTINGENCIES

##### *Environmental*

The Company reviews its obligations as they relate to compliance with environmental laws, including site restoration and remediation. As of March 31, 2005, the Company has recorded liabilities of \$10 million for projected environmental remediation costs. Because of the uncertainties associated with environmental assessment and remediation activities, future costs of compliance or remediation could be higher or lower than the amount currently accrued. Based on currently available information and analysis, the Company believes that it is possible that costs associated with such liabilities or as yet unknown liabilities may exceed current reserves in amounts that could be material but cannot be estimated as of March 31, 2005.

### *Financial Commitments*

At March 31, 2005, AES had provided outstanding financial and performance related guarantees or other credit support commitments for the benefit of its subsidiaries, which were limited by the terms of the agreements to an aggregate of approximately \$442 million (excluding those collateralized by letter of credit and surety bond obligations discussed below).

At March 31, 2005, the Company had \$222 million in letters of credit outstanding under the revolver that operate to guarantee performance relating to certain project development activities and subsidiary operations. The Company pays a letter of credit fee ranging from 0.50% to 2.75% per annum on the outstanding amounts. In addition, the Company had \$4 million in surety bonds outstanding at March 31, 2005.

### *Litigation*

The Company is involved in certain claims, suits and legal proceedings in the normal course of business. The Company has accrued for litigation and claims where it is probable that a liability has been incurred and the amount of loss can be reasonably estimated. The Company believes, based upon information it currently possesses and taking into account established reserves for estimated liabilities and its insurance coverage, that the ultimate outcome of these proceedings and actions is unlikely to have a material adverse effect on the Company's financial statements. It is possible, however, that some matters could be decided unfavorably to the Company, and could require the Company to pay damages or to make expenditures in amounts that could be material but cannot be estimated as of March 31, 2005.

In September 1999, a judge in the Brazilian appellate state court of Minas Gerais granted a temporary injunction suspending the effectiveness of a shareholders' agreement between Southern Electric Brasil Participacoes, Ltda. ( SEB ) and the state of Minas Gerais concerning CEMIG. AES's investment in CEMIG is through SEB. This shareholders' agreement granted SEB certain rights and powers in respect of CEMIG ( Special Rights ). In March 2000, a lower state court in Minas Gerais held the shareholders' agreement invalid where it purported to grant SEB the Special Rights and enjoined the exercise of Special Rights. In August 2001, the state appellate court denied an appeal of the merits decision, and extended the injunction. In October 2001, SEB filed two appeals against the decision on the merits of the state appellate court, one to the Federal Superior Court and the other to the Supreme Court of Justice. The state appellate court denied access of these two appeals to the higher courts, and in August 2002, SEB filed two interlocutory appeals against such decision, one directed to the Federal Superior Court and the other to the Supreme Court of Justice. These appeals continue to be pending. SEB intends to vigorously pursue by all legal means a restoration of the value of its investment in CEMIG; however, there can be no assurances that it will be successful in its efforts. Failure to prevail in this matter may limit SEB's influence on the daily operation of CEMIG.

In November 2000, the Company was named in a purported class action suit along with six other defendants, alleging unlawful manipulation of the California wholesale electricity market, resulting in inflated wholesale electricity prices throughout California. The alleged causes of action include violation of the Cartwright Act, the California Unfair Trade Practices Act and the California Consumers Legal Remedies Act. In December 2000, the case was removed from the San Diego County Superior Court to the U.S. District Court for the Southern District of California. On July 30, 2001, the Court remanded the case back to San Diego Superior Court. The case was consolidated with five other lawsuits alleging similar claims against other defendants. In March 2002, the plaintiffs filed a new master complaint in the consolidated action, which asserted the claims asserted in the earlier action and names AES, AES Redondo Beach, L.L.C., AES Alamitos, L.L.C., and AES Huntington Beach, L.L.C. as defendants. In May 2002, the case was removed by certain cross-defendants from the San Diego County Superior Court to the United States District Court for the Southern District of California. The plaintiffs filed a motion to remand the case to state court, which was granted on December 13, 2002. Certain defendants appealed

aspects of that decision to the United States Court of Appeals for the Ninth Circuit. On December 8, 2004, a panel of the Ninth Circuit issued an opinion affirming in part and reversing in part the decision of the District Court, and permitting the remand of the case to state court. The Company believes that it has meritorious defenses to any actions asserted against it and expects that it will defend itself vigorously against the allegations.

In August 2000, the Federal Energy Regulatory Commission (FERC) announced an investigation into the organized California wholesale power markets in order to determine whether rates were just and reasonable. Further investigations have involved alleged market manipulation. The FERC has requested documents from each of the AES Southland plants and AES Placerita. AES Southland and AES Placerita have cooperated fully with the FERC investigation. AES Southland is not subject to refund liability because it did not sell into the organized spot markets due to the nature of its tolling agreement. The Ninth Circuit recently heard oral argument on the time scope of the refunds. The Ninth Circuit Court of Appeals also addressed the appeal of the FERC's decision not to impose refunds for the alleged failure to file rates including transaction specific data for sales to the California Independent System Operator (ISO) for 2000 and 2001. See *State of California ex rel. Bill Lockyer*. Although in its order issued September 9, 2004 the Ninth Circuit did not order refunds, the Ninth Circuit remanded the case to the FERC for a refund proceeding to consider remedial options. Placerita made sales during the referenced time period. Depending on the method of calculating refunds and the time period to which the method is applied, the alleged refunds sought from AES Placerita could approximate \$23 million.

In July 2001, a petition was filed against CESCO, an affiliate of the Company, by the Grid Corporation of Orissa, India (Gridco), with the Orissa Electricity Regulatory Commission (OERC), alleging that CESCO had defaulted on its obligations as a government licensed distribution company, that CESCO management abandoned the management of CESCO, and asking for interim measures of protection, including the appointment of a government regulator to manage CESCO. Gridco, a state owned entity, is the sole energy wholesaler to CESCO. In August 2001, the management of CESCO was handed over by the OERC to a government administrator that was appointed by the OERC. By its order of August 2001, the OERC held that the Company and other CESCO shareholders were not proper parties to the OERC proceeding and terminated the proceedings against the Company and other CESCO shareholders. In August 2004, the OERC issued a notice to CESCO, the Company and others giving the recipients of the notice until November 2004 to show cause why CESCO's distribution license should not be revoked. In response, CESCO submitted a business plan to the OERC. On February 26, 2005, the OERC issued an order rejecting the proposed business plan. The order also stated the CESCO distribution license would be revoked if an acceptable business plan for CESCO was not submitted to, and approved by the OERC prior to March 31, 2005. OERC revoked the CESCO distribution license on April 2, 2005. An appeal of the April 2, 2005 OERC has been filed. Gridco also has asserted that a Letter of Comfort issued by the Company in connection with the Company's investment in CESCO obligates the Company to provide additional financial support to cover CESCO's financial obligations. In December 2001, a notice to arbitrate pursuant to the Indian Arbitration and Conciliation Act of 1996 was served on the Company by Gridco pursuant to the terms of the CESCO Shareholder's Agreement (SHA), between Gridco, the Company, AES ODPL, CESCO and Jyoti Structures. The parties have filed their respective statement of claims, counter claims, defenses and answers. Gridco appears to seek approximately \$188.5 million in damages, plus undisclosed penalties and interest, but a detailed alleged damages analysis has yet to be filed by Gridco. On or about April 15, 2005, the parties filed their initial witness statements. A hearing on the merits has been scheduled for August 2005. A petition remains pending before the Indian Supreme Court concerning fees of the third neutral arbitrator and the venue of future hearings. In addition, in December 2001, a petition was filed by Gridco in the local India Court system seeking an injunction prohibiting the Company and its subsidiaries from selling their shares in Orissa Power Generation Company Pvt. Ltd. (OPGC), a 420 MW coal based electricity generation business located in India, and restraining the Company and its subsidiaries from receiving any dividend from OPGC in respect of shares held by them in OPGC until the completion of the CESCO arbitration. The injunctive relief was initially granted on December 23, 2001. Eventually, the injunction was overturned. In January 2005, a new

injunction was issued prohibiting the transfer of ownership of the shares of OPGC pending the resolution of the CESCO arbitration. On May 2, 2005, the hearing on the appeal of the new injunction was adjourned until August 2005. Also, in March 2005, the Orissa High Court upheld a decision by the OERC permitting the OERC, as requested by Gridco, to initiate proceedings regarding the terms of the existing power purchase agreement ( PPA ) at OPGC. The decision was appealed by OPGC to the Supreme Court of India. On April 29, 2005, the Supreme Court granted a stay of the OERC proceedings regarding the PPA as well as the order of the Orissa High Court. A further hearing date on the stay Order has been scheduled for August 2005. The Company believes that it has meritorious defenses to any actions asserted against it and expects that it will defend itself vigorously against the allegations.

In April 2002, the Company's subsidiary IPALCO Enterprises, Inc. ( IPALCO ) and certain former officers and directors of IPALCO were named as defendants in a purported class action lawsuit filed in the United States District Court for the Southern District of Indiana. On May 28, 2002, an amended complaint was filed in the lawsuit. The amended complaint asserts that IPALCO and former members of the pension committee for the Indianapolis Power & Light Company thrift plan breached their fiduciary duties to the plaintiffs under the Employees Retirement Income Security Act by investing assets of the thrift plan in the common stock of IPALCO prior to the acquisition of IPALCO by the Company. In December 2002, plaintiffs moved to certify this case as a class action. The Court granted the motion for class certification on September 30, 2003. On October 31, 2003, the parties filed cross-motions for summary judgment on liability. Those motions currently are pending before the Court. IPALCO believes it has meritorious defenses to the claims asserted against it and intends to defend this lawsuit vigorously.

In July 2002, the Company, Dennis W. Bakke, Roger W. Sant, and Barry J. Sharp were named as defendants in a purported class action filed in the United States District Court for the Southern District of Indiana. In September 2002, two virtually identical complaints were filed against the same defendants in the same court. All three lawsuits purport to be filed on behalf of a class of all persons who exchanged their shares of IPALCO common stock for shares of AES common stock issued pursuant to a registration statement dated and filed with the SEC on August 16, 2000, (the Share Exchange ). The complaints purport to allege violations of Sections 11, 12(a)(2) and 15 of the Securities Act of 1933 based on statements in or omissions from the registration statement concerning certain secured equity-linked loans by AES subsidiaries; the supposedly volatile nature of AES stock, as well as AES's allegedly unhedged operations in the United Kingdom at that time, and the alleged effect of the New Electrical Trading Agreements ( NETA ) on AES's United Kingdom operations. On April 14, 2003, lead plaintiffs filed an amended and consolidated complaint, which added former IPALCO directors and officers John R. Hodowal, Ramon L. Humke and John R. Brehm as defendants and, in addition to the purported claims in the original complaint, purports to allege against the newly added defendants violations of Sections 10(b) and 14(a) of the Securities Exchange Act of 1934 and Rules 10b-5 and 14a-9 promulgated thereunder. The amended complaint also purports to add a claim based on alleged misstatements or omissions concerning an alleged breach by AES of alleged obligations AES owed to Williams Energy Services Co. ( Williams ) under an agreement between the two companies in connection with the California energy market. On September 26, 2003, defendants filed a motion to dismiss the amended and consolidated complaint. By Order dated November 17, 2004, the Court dismissed all of the claims asserted in the amended and consolidated complaint against all defendants with one exception. The exception consists of claims against Bakke, Sant, Sharp and AES (the AES Defendants ), under Sections 11, 12 and 15 of the Securities Act of 1933, 15 U.S.C. §§ 77k, 77l and 77o, based on the alleged failure of the Registration Statement and Prospectus disseminated to the IPALCO stockholders for purposes of the Share Exchange to disclose AES's purported temporary default on its contract with Williams. On December 15, 2004, the AES Defendants filed a motion for judgment on the pleadings dismissing the remaining claims. In April 2005, plaintiffs served their first discovery requests to defendants. The Company and the individual defendants believe that they have meritorious defenses to the claims asserted against them and intend to defend these lawsuits vigorously.



Commencing on May 2, 2003, the Indiana Securities Commissioner of Indiana's Office of the Secretary of State, Securities Division, pursuant to Indiana Code 23-2-1, served subpoenas on 30 former officers and directors of IPALCO, AES, and others, requesting the production of documents in connection with the March 27, 2001 share exchange between the Company and IPALCO pursuant to which stockholders exchanged shares of IPALCO common stock for shares of the Company's common stock and IPALCO became a wholly-owned subsidiary of the Company. IPALCO and the Company have produced documents pursuant to the subpoenas served on them. In addition, the Indiana Securities Commissioner's office has taken testimony from various individuals. On January 27, 2004, Indiana's Secretary of State issued a statement which provided that the investigative staff had determined that there did not appear to be a justifiable reason to focus further specific attention upon six non-employee former members of IPALCO's board of directors. The investigation otherwise remains pending. In addition, although the press release characterized the investigation as criminal, the Company and IPALCO do not believe that the Indiana Securities Commissioner has criminal jurisdiction, and the Company and IPALCO are unaware at this time of any participation by any government office or agency with such jurisdiction.

In November 2002, a lawsuit was filed against AES Wolf Hollow, L.P. ( AESWH ) and AES Frontier, L.P. ( AESF ), two of our indirect subsidiaries, in the District Court of Hood County, Texas by Stone & Webster, Inc. ( S&W ). At the time of filing, AESWH and AESF were two indirect subsidiaries of the Company. In December 2004, the Company finalized agreements to transfer the ownership of AESWH and AESF. S&W contracted to perform the engineering, procurement and construction of the Wolf Hollow project, a gas-fired combined cycle power plant in Hood County, Texas. In its initial complaint, S&W requested a declaratory judgment that a fire that took place at the project on June 16, 2002 constituted a force majeure event and that S&W was not required to pay rebates assessed for associated delays. As part of the initial complaint, S&W also sought to enjoin AESWH and AESF from drawing down on letters of credit provided by S&W. The Court refused to issue the injunction. S&W has since amended its complaint four times and joined additional parties, including the Company and Parsons Energy & Chemicals Group, Inc. In addition to the claims already mentioned, the current claims by S&W include claims for breach of contract, breach of warranty, wrongful liquidated damages, foreclosure of lien, fraud and negligent misrepresentation. In January 2004, the Company filed a counterclaim against S&W and its parent, the Shaw Group, Inc. ( Shaw ). AESWH and AESF filed answers and counterclaims against S&W, which since have been amended. The exact amount of AESWH and AESF's counterclaims will be identified at the appropriate time in the lawsuit. In January 2004, the Company filed a counterclaim against S&W and its parent, the Shaw Group, Inc. ( Shaw ). Although S&W has yet to provide a detailed damage claim, it has filed a lien against AESWH and AESF, with each lien allegedly valued, after amendment on March 14, 2005, at approximately \$87 million. In March 2004, S&W and Shaw each filed an answer to the counterclaim. The counterclaim and answers subsequently were amended. In March 2005, the Court rescheduled the trial date for October 24, 2005. The Company and subsidiaries believe that the allegations in S&W's complaint are meritless, and that each defendant has meritorious defenses to the claims asserted by S&W. They each intend to defend the lawsuit vigorously.

In March 2003, the office of the Federal Public Prosecutor for the State of Sao Paulo, Brazil ( MPF ) notified AES Eletropaulo that it had commenced an inquiry related to the BNDES financings provided to AES Elpa and AES Transgas and the rationing loan provided to AES Eletropaulo, changes in the control of AES Eletropaulo, sales of assets by AES Eletropaulo and the quality of service provided by AES Eletropaulo to its customers and requested various documents from AES Eletropaulo relating to these matters. In October 2003 this inquiry was sent to the MPF for continuing investigation. Also in March 2003, the Commission for Public Works and Services of the Sao Paulo Congress requested AES Eletropaulo to appear at a hearing concerning the default by AES Elpa and AES Transgas on the BNDES financings and the quality of service rendered by AES Eletropaulo. This hearing was postponed indefinitely. In addition, in April 2003, the office of the MPF notified AES Eletropaulo that it is conducting an inquiry into possible errors related to the collection by AES Eletropaulo of customers

unpaid past-due debt and requesting the company to justify its procedures. In December 2003, ANEEL answered, as requested by the MPF, that the issue regarding the past-due debts are to be included in the analysis to the revision of the General Conditions for the Electric Energy Supply.

In May 2003, there were press reports of allegations that in April 1998 Light Serviços de Eletricidade S.A. ( Light ) colluded with Enron in connection with the auction of AES Eletropaulo. Enron and Light were among three potential bidders for AES Eletropaulo. At the time of the transaction in 1998, AES owned less than 15% of the stock of Light and shared representation in Light's management and Board with three other shareholders. In June 2003, the Secretariat of Economic Law for the Brazilian Department of Economic Protection and Defense ( SDE ) issued a notice of preliminary investigation seeking information from a number of entities, including AES Brasil Energia, with respect to certain allegations arising out of the privatization of AES Eletropaulo. On August 1, 2003, AES Elpa responded on behalf of AES-affiliated companies and denied knowledge of these allegations. The SDE began a follow-up administrative proceeding as reported in a notice published on October 31, 2003. In response to the Secretary of Economic Law's official letters requesting explanations on such accusation, AES Eletropaulo filed its defense on January 19, 2004. On April 7, 2005 AES Eletropaulo responded to a SDE request for additional information.

AES Florestal, Ltd., ( Florestal ) a wholly-owned subsidiary of AES Sul, is a wooden utility pole manufacturer located in Triunfo, in the state of Rio Grande do Sul, Brazil. In October 1997, AES Sul acquired Florestal as part of the original privatization transaction by the Government of the State of Rio Grande do Sul, Brazil, that created AES Sul. From 1997 to the present, the chemical compound chromated copper arsenate has been used by Florestal to chemically treat the poles under an operating license issued by the Brazilian government. Prior to the acquisition of Florestal by AES Sul, another chemical, creosote, was used to treat the poles. After acquiring Florestal, AES Sul discovered approximately 200 barrels of solid creosote waste on the Florestal property. In 2002 a civil inquiry (Civil Inquiry No. 02/02) was initiated and a criminal lawsuit was filed in the city of Triunfo's Judiciary both by the Public Prosecutors' office of the city of Triunfo. The civil lawsuit was settled in 2003. The criminal lawsuit has been suspended for a period of two years pending a certification of environmental compliance for Florestal and the occurrence of no further violations of environmental regulations. Florestal has hired an independent environmental assessment company to perform an environmental audit of the entire operational cycle at Florestal. Florestal submitted a preliminary action plan that the environmental authority is reviewing. Florestal continues to review and evaluate the site and to determine if any additional remedial actions are necessary.

On January 27, 2004, the Company received notice of a Formulation of Charges filed against the Company by the Superintendence of Electricity of the Dominican Republic. In the Formulation of Charges, the Superintendence asserts that the existence of three generation companies (Empresa Generadora de Electricidad Itabo, S.A., Dominican Power Partners, and AES Andres BV) and one distribution company (Empresa Distribuidora de Electricidad del Este, S.A.) in the Dominican Republic, violates certain cross ownership restrictions contained in the General Electricity law of the Dominican Republic. On February 10, 2004, the Company filed in the First Instance Court of the National District of the Dominican Republic ( Court ) an action seeking injunctive relief based on several constitutional due process violations contained in the Formulation of Charges ( Constitutional Injunction ). On or about February 24, 2004, the Court granted the Constitutional Injunction and ordered the immediate cessation of any effects of the Formulation of Charges and the enactment by the Superintendence of Electricity of a special procedure to prosecute alleged antitrust complaints under the General Electricity Law. On March 1, 2004, the Superintendence of Electricity appealed the Court's decision. The appeal is pending.

In late July 2004, the Corporación Dominicana de Empresas Eléctricas Estatales ( CDEEE ), which is the government entity that currently owns 50% of Empresa Generadora de Electricidad Itabo, S.A. ( Itabo ), filed separate lawsuits in the Dominican Republic against Ede Este, a former subsidiary of AES, and Itabo, an AES affiliate. The lawsuit against Itabo also names the president of Itabo as a defendant. In

the action against Itabo, CDEEE requested a rendering of accountability for the accounts of Itabo with regard to all transactions between Itabo and related parties. On September 29, 2004, the Court rejected CDEEE's request. CDEEE also requested that the court order Itabo to deliver its accounting books and records for the period from September 1999 to July 2004 to CDEEE, and that an independent expert audit the accounting records and present a report to CDEEE and the court. At a hearing that was held on March 30, 2005, Itabo argued that the court did not have jurisdiction to hear the case and that the case should be decided in an arbitration proceeding. The judge asked the parties to submit briefs on the matter and reserved on the issue. In the Ede Este lawsuit, CDEEE requests a rendering of accountability of the accounts of Itabo of all Ede Este's commercial and financial operations with affiliate companies since August 5, 1999. On February 9, 2005, Itabo filed a lawsuit against CDEEE and the Fondo Patrimonial para el Desarrollo ( FONPER ) seeking among other relief, to enforce the arbitration/dispute resolution processes set forth in the contracts among the parties.

On February 18, 2004, AES Gener S.A. ( Gener SA ), a subsidiary of the Company, filed a lawsuit in the Federal District Court for the Southern District of New York. Gener SA is co-venturer with Coastal Itabo, Ltd. ( Coastal ) in Itabo, a Dominican Republic electric generation Company. The lawsuit sought to enjoin the efforts initiated by Coastal to hire an alleged independent expert, purportedly pursuant to the Shareholder Agreement between the parties, to perform a valuation of Gener SA's aggregate interests in Itabo. Coastal asserts that Gener SA has committed a material breach under the parties' Shareholder Agreement, and therefore, Gener is required if requested by Coastal to sell its aggregate interests in Itabo to Coastal at a price equal to 75% of the independent expert's valuation. Coastal claims a breach occurred based on alleged violations by Gener SA of purported antitrust laws of the Dominican Republic. Gener SA disputes that any default has occurred. On March 11, 2004, upon motion by Gener SA, the court enjoined the evaluation being performed by the expert and ordered the parties to arbitration. On March 11, 2004, Gener SA commenced arbitration proceedings. The arbitration is ongoing.

Pursuant to the pesification established by the Public Emergency Law and related decrees in Argentina, since the beginning of 2002, the Company's subsidiary TermoAndes has converted its obligations under its gas supply and gas transportation contracts into pesos. In accordance with the Argentine regulations, payments must be made in Argentine pesos at a 1:1 exchange rate. Some gas suppliers (Tecpetrol, Mobil and Compañía General de Combustibles S.A.) have objected to the payment in pesos. On January 30, 2004, such gas suppliers presented a demand for arbitration at the ICC (International Chamber of Commerce) requesting the re-dollarization of the gas price. TermoAndes replied on March 10, 2004 with a counter-lawsuit related to (i) the default of suppliers regarding the most favored nation clause, (ii) the unilateral modification of the point of gas injection by the suppliers, (iii) the obligations to supply the contracted quantities and (iv) the ability of TermoAndes to resell the gas not consumed. On May 12, 2004, the plaintiffs responded to TermoAndes' counterclaims. In October 2004, the case was submitted to a court of arbitration for determination of the Terms of Reference. The arbitration seeks approximately \$10 million for past gas supplies. The parties are in the process of submitting evidence to the arbitrator.

On or about October 27, 2004, AES Red Oak LLC ( Red Oak ) was named as a defendant in a lawsuit filed by Raytheon Company ( Raytheon ) in the Supreme Court of the State of New York, County of New York. The complaint purports to allege claims for breach of contract, fraud, interference with contractual rights and equitable relief concerning alleged issues related to the construction and/or performance of the Red Oak project. The complaint seeks the return from Red Oak of approximately \$30 million that was drawn by Red Oak under a letter of credit that was posted by Raytheon related to the construction and/or performance of the Red Oak project. Raytheon also seeks \$110 million in purported additional expense allegedly incurred by Raytheon in connection with the guaranty and construction agreements entered with Red Oak. In December 2004, Red Oak answered the complaint and filed counterclaims against Raytheon. In January 2005, Raytheon moved for dismissal of Red Oak's

counterclaims. In March 2005, the motion to dismiss was withdrawn and a partial motion for summary judgment was filed by Raytheon seeking return of approximately \$16 million of the letter of credit draw. Red Oak submitted its opposition to the partial motion for summary judgment in April, and expects the Court to schedule a hearing to address the motion in May or June. Meanwhile, Raytheon re-filed its motion to dismiss the fraud allegations in the counterclaim. In late April 2005, Red Oak filed its response opposing the renewed motion to dismiss. The parties are conducting discovery. Red Oak expects to defend itself vigorously in the action.

On or about January 26, 2005, the City of Redondo Beach, California, provided AES Redondo Beach LLC ( AES Redondo Beach ), a subsidiary of the Company, a notice of assessment for utility user s tax ( UUT ) for the period of May 1998 through September 2004. The assessment includes alleged amounts owing of \$32.8 million for gas usage and \$38.9 million for interest and penalties. AES Redondo Beach has objected to the assessment. An administrative hearing before the City s Tax Administrator was scheduled and subsequently cancelled. In addition, AES Redondo Beach and the City are engaging in multiple discovery and procedural disputes involving the alleged UUT assessment. In April 2005, in connection with these disputes, the City filed a lawsuit against AES Redondo Beach alleging violations of certain State of California government codes regarding the disclosure of confidential information.

On April 26, 2003 approximately 4,000 gallons of distillate fuel oil spilled as a result of incorrect loading and storage tank valve settings at the Company s gas turbine plant at Condado del Rey, Panama. Remediation efforts were promptly conducted and completed. AES Panama agreed with Autoridad Nacional del Ambiente ( ANAM ), the Panamanian National Environmental Authority, to improve auditing and environmental management plans at the plant. In addition, AES Panama is in discussions with ANAM to improve adjacent watershed conditions. As part of these recent discussions and in response to a letter received by AES Panama from ANAM on February 21, 2005, regarding the spill and watershed conditions, AES Panama has agreed to pay a fine of \$250 thousand. The Company does not expect that the costs to institute new auditing and management plans, the anticipated fine or efforts to improve watershed conditions to be material to our operations or results.

#### *Tax Examinations*

The Company and certain of its subsidiaries are under examination by the relevant taxing authorities for various tax years. The Company regularly assesses the potential outcome of these examinations in each of the taxing jurisdictions when determining the adequacy of the provision for income taxes. Tax reserves have been established, which the Company believes to be adequate in relation to the potential for additional assessments. Once established, reserves are adjusted only when there is more information available or when an event occurs necessitating a change to the reserves. While the Company believes that the amount of the tax estimates is reasonable, it is possible that the ultimate outcome of current or future examinations may exceed current reserves in amounts that could be material but cannot be estimated as of March 31, 2005.

#### *Other*

In exchange for the termination of \$863 million of outstanding Brasiliana Energia debt and accrued interest during 2004, the Brazilian National Development Bank ( BNDES ) received \$90 million in cash, 53.85% ownership of Brasiliana Energia and a one-year call option ( Sul Option ) to acquire a 53.85% ownership interest of AES Sul. The Sul Option, which would require the Company to contribute its equity interest in AES Sul to Brasiliana Energia, will be exercisable at the earlier of the Company s announcement to BNDES of the completion of the AES Sul restructuring or June 22, 2005, subject to AES s right to a six month extension under certain circumstances. BNDES s ability to exercise the Sul Option is contingent upon several factors. The most significant factor requires BNDES to obtain consent for the exercise of the option from the AES Sul syndicated lenders. The probability of BNDES exercising

the Sul Option is unknown at this time. In the event BNDES exercises its option, 53.85% of our ownership in AES Sul would be transferred to BNDES and the Company would be required to recognize a non-cash after-tax loss on its investment in Sul currently estimated at \$464 million. This amount primarily includes the recognition of currency translation losses and recording minority interest for BNDES's share of Sul offset by the recorded estimated fair value of the Sul Option.

## 6. COMPREHENSIVE INCOME (LOSS)

The components of comprehensive income for the three months ended March 31, 2005 and 2004 are as follows (in millions):

	Three Months Ended	
	March 31,	
	2005	2004
Net income	\$ 124	\$ 16
Foreign currency translation adjustments (net of income taxes of \$- and \$-, respectively)	(10 )	18
Derivative activity:		
Reclassification to earnings (net of income tax benefit of \$9 and \$14, respectively)	19	41
Change in derivative fair value (net of income tax benefit of \$27 and \$35, respectively)	(43 )	(148 )
Change in fair value of derivatives	(24 )	(107 )
Comprehensive income (loss)	\$ 90	\$ (73 )

Accumulated other comprehensive loss is as follows at March 31, 2005:

Accumulated other comprehensive loss December 31, 2004	\$ (3,643 )
Total foreign currency translation adjustments	(10 )
Change in fair value of derivatives	(24 )
Accumulated other comprehensive loss March 31, 2005	\$ (3,677 )

## 7. SEGMENTS

AES reports its financial results in four business segments of the electricity industry: large utilities, growth distribution, contract generation and competitive supply. Although the nature of the product is the same, the segments are differentiated by the nature of the customers, operational differences, cost structure and risk exposure.

- The large utility segment primarily consists of three large utilities located in the U.S. (Indianapolis Power & Light Company or IPL), Brazil (Eletropaulo) and Venezuela (EDC). Each of these three utilities is of significant size and each maintains a monopoly franchise within a defined service area.
- The growth distribution segment consists of distribution facilities located in developing countries where the demand for electricity is expected to grow at a higher rate than in more developed parts of the world.
- The contract generation segment consists of facilities that have contractually limited their exposure to electricity price volatility by entering into long-term (five years or longer) power sales agreements for 75% or more of their output capacity. Exposure to fuel supply risks is also limited through long-term fuel supply contracts or through tolling arrangements. These contractual agreements generally reduce exposure to fuel commodity and electricity price volatility, and thereby increase the predictability of their cash flows and earnings.

- The competitive supply segment consists primarily of power plants selling electricity to wholesale customers through competitive markets, and as a result, the cash flows and earnings of such businesses are more sensitive to fluctuations in the market price of electricity, natural gas, coal, oil and other fuels.

All income statement information for businesses that were discontinued during the period is segregated and is shown in the line Loss from operations of discontinued businesses in the accompanying consolidated statements of operations.

Information about the Company's operations and assets by segment is as follows (in millions):

Three Months Ended March 31,	Revenue(1)		Gross Margin(2)	
	2005	2004	2005	2004
Large Utilities	\$ 1,025	\$ 816	\$ 292	\$ 198
Growth Distribution	374	329	75	64
Contract Generation	985	868	392	358
Competitive Supply	279	243	65	64
Total	\$ 2,663	\$ 2,256	\$ 824	\$ 684

(1) Sales between the segments ( intersegment revenues ) are accounted for at fair value as if the sales were to third parties. Intersegment revenues for the three months ended March 31, 2005 and 2004 were \$158 million and \$100 million, respectively. These amounts have been eliminated in the appropriate segment.

(2) For consolidated subsidiaries, the measure of profit or loss used for the Company's reportable segments is gross margin. Gross margin equals revenues less cost of sales on the consolidated statement of operations for each period presented.

	Total Assets	
	March 31, 2005	December 31, 2004
Large Utilities	\$ 9,135	\$ 9,330
Growth Distribution	2,212	2,216
Contract Generation	14,100	14,034
Competitive Supply	2,158	2,156
Corporate	1,340	1,187
Total	\$ 28,945	\$ 28,923

## 8. BENEFIT PLANS

Certain of the Company's subsidiaries have defined benefit pension plans covering substantially all of their respective employees. Pension benefits are based on years of credited service, age of the participant and average earnings. Of the thirteen defined benefit plans, two are at U.S. subsidiaries and the remaining plans are at foreign subsidiaries.

Total pension cost for the three months ended March 31, 2005 and 2004 includes the following components (in millions):

	Three Months Ended March 31,			
	2005		2004	
	U.S.	Foreign	U.S.	Foreign
Service cost	\$ 1	\$ 2	\$ 1	\$ 1
Interest cost on projected benefit obligation	7	67	7	57
Expected return on plan assets	(7 )	(45 )	(7 )	(33 )
Amortization of unrecognized actuarial loss	1	1	1	1
Total pension cost	\$ 2	\$ 25	\$ 2	\$ 26

The scheduled cash flows for employer contributions have not changed significantly from previous disclosures.

## 9. RECENT TAX LEGISLATION

On October 22, 2004, the American Jobs Creation Act ( the AJCA ) was signed into law. The AJCA includes a deduction of 85% of certain foreign earnings that are repatriated, as defined in the AJCA. The Company may elect to apply this provision to qualifying earnings repatriations in 2005. The Company is in the process of evaluating the effects of the repatriation provision in accordance with recently issued Treasury Department guidance. The range of possible amounts that the Company is considering for repatriation under this provision is between zero and \$150 million. The amount of income tax expense related to the potential repatriation cannot be reasonably estimated at this time.

**ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.**

**Restatement of Previously Issued Quarterly Financial Statements**

This Form 10-Q/A is being filed to correct accounting errors contained in our consolidated financial statements included in our previously filed Form 10-Q for the quarter ended March 31, 2005. This Form 10-Q/A has also been amended to reflect a prior interim period adjustment as required by Statement of Financial Accounting Standard No. 16. See Note 1 to the condensed consolidated financial statements for a discussion of the nature of these errors and this adjustment and their impact on the restated condensed consolidated financial statements. The discussion set forth below has been amended to reflect the adjustments made in the restatement to the financial statements as described in Note 1 to the consolidated financial statements, however no attempt has been made to modify or update any other information presented below.

**Executive Summary**

AES is a global power company managed to meet the growing demand for electricity in ways that benefit all of our stakeholders. AES is a holding company that through its subsidiaries and affiliates owns and operates a portfolio of electricity generation and distribution businesses in 27 countries. We seek to capture the benefits of our global expertise and economies of scale in our operations. Predictable cash flow, an efficient capital structure and world-class operating performance are the focus of our management efforts.

We operate two principal types of businesses within the power sector. The first is the generation of power for sale to utilities and other wholesale customers. The second is the operation of utilities which distribute power to retail, commercial, industrial and governmental customers. Each principal business generates approximately one half of the Company's revenues. Our financial results are reported as four business segments on a regulated and non-regulated basis by region, which further refines our core business structure.

Our generation business segments Contract Generation and Competitive Supply consist of approximately 37 gigawatts of generating capacity from 99 power plants in 23 countries. Our contract generation plants have contractually limited their exposure to electricity price volatility by entering into power sales agreements of five years or longer for 75% or more of their output capacity at the time of origination. Exposure to fuel supply risks is also limited through long-term fuel supply contracts or through fuel tolling arrangements. Through these contractual agreements, the businesses generally reduce commodity and electricity price volatility and thereby increase the predictability of their cash flows and earnings. Our competitive supply segment consists primarily of power plants selling electricity to wholesale customers through competitive markets and, as a result, the cash flows and earnings of such businesses are more sensitive to fluctuations in the market price of electricity and of natural gas, coal and other fuels. However, for our U.S. competitive supply business which includes a fleet of low-cost coal fired plants in New York, we typically hedge the majority of our fuel exposure on a rolling two-year basis.

The utility business segments Large Utilities and Growth Distribution consist of 15 distribution companies in eight countries with over 11.2 million end-user customers. The Large Utilities segment includes three large utilities located in the U.S. (IPL), Brazil (Eletropaulo) and Venezuela (EDC) all of which maintain a monopoly franchise within a defined service area. Our Growth Distribution segment is comprised of our interests in electricity distribution facilities located in Argentina, Brazil (Rio Grande do Sul), Cameroon, El Salvador, and Ukraine where the demand for electricity is expected to grow at a higher rate than in more developed parts of the world.



*First Quarter Operating Highlights*

We achieved solid results in the first quarter of 2005 as compared to the first quarter of 2004 with positive improvements in most key financial drivers as noted below:

	Three Months Ended		% Change
	March 31, 2005	2004	
	(\$ in millions, except per share amounts)		
Revenue	\$ 2,663	\$ 2,256	18%
Gross Margin	\$ 824	\$ 684	20%
Gross Margin as a % of Revenue	30.9 %	30.3 %	N/A
Diluted Earnings Per Share from Continuing Operations	\$ 0.19	\$ 0.07	171%
Net Cash Provided By Operating Activities	\$ 518	\$ 401	29%

**Revenue** increased 18% to \$2.7 billion in the first quarter of 2005 from \$2.3 billion in the first quarter of 2004 with contributions from all of our segments, led by our large utility in Brazil, Eletropaulo. **Key factors leading to the increase were higher tariffs, positive impacts from foreign currency translation and higher demand in certain segments.**

**Gross margin** increased 20% to **\$824 million** in the first quarter of 2005 from \$684 million in the first quarter of 2004 based on higher year over year revenues. Gross margin as a percent of sales increased slightly from 30.3% in 2004 to 30.9% in 2005 due to higher margin earnings from Eletropaulo partially offset by higher fuel costs in our Argentine and Chilean businesses and the delay in the tariff increase for our Venezuelan utility.

**Diluted earnings per share from continuing operations** increased 171% to **\$0.19** from \$0.07 in the first quarter of 2004. Improvements from higher gross margins and lower interest expense were partially offset by an estimated higher effective tax rate and an increase in our minority interest expense due to higher earnings in our large utility business in Brazil.

**Net cash from operating activities** increased 29% to \$518 million from \$401 million for the first quarter of 2004. This year over year increase was largely driven by higher earnings and proceeds from the favorable termination of a currency hedge, offset by an increase in working capital.

*Strategic Highlights*

In support of our growth strategy to increase our presence in the wind generation business, in March 2005 we closed our acquisition of SeaWest Holdings, Inc. ( SeaWest ), a leading wind generation operator and developer, for approximately \$60 million. We also provided \$25 million to fund the initial construction costs for our first wind power project, a 120 MW project called Buffalo Gap 1, in Texas. Through the acquisition, AES gains operational control of 500 MW of wind facilities in California, Wyoming and Oregon and 1,800 MW of development sites in 10 states in the western U.S., including the Buffalo Gap 1 project, and options on more than 100,000 acres of land for potential sites in SeaWest's development pipeline. AES's acquisition of SeaWest, combined with its 2004 investment in US Wind Force, LLC, and its recent joint venture with EHN to develop wind projects in New York, gives the Company a strong base of wind projects operating or in development in fourteen states.

In February 2005, the Bulgarian Government issued a Government Support Letter to the Maritza East I project, effectively approving the project. Concurrently, AES signed an amendment to the fifteen year power purchase agreement entered into in 2001 with NEK, the Bulgarian state owned electric utility. Under the terms of the amended agreement, AES has the right to build a 600 megawatt (net) lignite fired power plant near Galabovo, Bulgaria. The completion of the project is dependent upon AES finalizing



amendments to the engineering and construction contract, securing necessary permits, and obtaining site acquisition and construction debt financing.

We also have recently initiated some organizational changes to drive business performance and position the Company for long-term quality growth. Under the new structure, we will organize our businesses by four regions, North America, Latin America, Asia and Europe, Africa and Middle East, each led by a regional president who reports directly to the CEO. This will allow us to place senior leaders and resources closer to the businesses to further improve operating performance and integrate operations and development on a more localized level. The new structure will help us leverage regional market trends to enhance our competitiveness and identify and capitalize on key business development opportunities. The organizational changes also streamline some corporate functions in order to more effectively support AES businesses around the globe.

## Results of Operations

	Three Months Ended			
	March 31, 2005	2004	\$ change	% change
(\$ in millions, except per share amounts)				
<b>Gross margin:</b>				
Large Utilities	\$ 292	\$ 198	\$ 94	47 %
Growth Distribution	75	64	11	17
Contract Generation	392	358	34	9
Competitive Supply	65	64	1	2
Total gross margin	824	684	140	20
General and administrative expenses(1)	(49 )	(48 )	(1 )	2
Interest expense	(467 )	(501 )	34	(7 )
Interest income	90	69	21	30
Other expense, net	(15 )	(14 )	(1 )	7
Loss on sale of investments, asset and goodwill impairment expense		(1 )	1	(100 )
Foreign currency transaction losses	(31 )	(34 )	3	(9 )
Equity in earnings of affiliates	25	16	9	56
Income tax expense	(147 )	(75 )	(72 )	96
Minority interest expense	(106 )	(54 )	(52 )	96
Income from continuing operations	124	42	82	195
Loss from operations of discontinued businesses		(26 )	26	(100 )
Net income	\$ 124	\$ 16	\$ 108	675 %
<b>Per Share Data:</b>				
Basic income per share from continuing operations	\$ 0.19	\$ 0.07	\$ 0.12	171 %
Diluted income per share from continuing operations	\$ 0.19	\$ 0.07	\$ 0.12	171 %

(1) General and administrative expenses are corporate and business development expenses.

**Overview****Revenue**

	For the Three Months Ended March 31, 2005		2004	
	Revenue (\$ in millions)	% of Total Revenues	Revenue	% of Total Revenues
Large Utilities	\$ 1,025	39%	\$ 816	36%
Growth Distribution	374	14%	329	15%
Regulated	1,399	53%	1,145	51%
Contract Generation	985	37%	868	38%
Competitive Supply	279	10%	243	11%
Non-Regulated	1,264	47%	1,111	49%
Total	\$ 2,663	100%	\$ 2,256	100%

Revenues increased \$407 million, or 18%, to \$2.7 billion for the three months ended March 31, 2005 from \$2.3 billion for the three months ended March 31, 2004. Excluding the estimated impacts of foreign currency translation, revenues would have increased approximately 14% for the three months ended March 31, 2005 from the three months ended March 31, 2004. The increase in revenues occurred across all segments, particularly in our Large Utilities and Contract Generation businesses and was driven by higher realized prices, the positive impacts of foreign currency translation and improved demand.

**Gross Margin**

	For the Three Months Ended March 31, 2005		2004	
	Gross Margin (\$ in millions)	% of Total Gross Margin	Gross Margin	% of Total Gross Margin
Large Utilities	\$ 292	36%	\$ 198	29%
Growth Distribution	75	9%	64	9%
Regulated	367	45%	262	38%
Contract Generation	392	47%	358	52%
Competitive Supply	65	8%	64	10%
Non-Regulated	457	55%	422	62%
Total	\$ 824	100%	\$ 684	100%

Gross margin increased \$140 million, or 20%, to \$824 million for the three months ended March 31, 2005 from \$684 million for the three months ended March 31, 2004. This increase was due to gross margin increases from our Large Utilities, Contract Generation and Growth Distribution segments due to higher revenues partially offset by higher fuel, purchased electricity and other fixed costs in certain of our segments.

*Segment Analysis***Large Utilities Revenue**

	For the Three Months Ended March 31, 2005		2004	
	Revenue (\$ in millions)	% of Total Revenues	Revenue	% of Total Revenues
North America	\$ 227	9%	\$ 215	10%
South America	654	25%	455	20%
Caribbean*	144	5%	146	6%
Total	\$ 1,025	39%	\$ 816	36%

\* Includes Venezuela

Revenue from the large utilities segment for the three months ended March 31, 2005 increased \$209 million, or 26%, compared to the three months ended March 31, 2004. Excluding the estimated impacts of foreign currency translation, revenues would have increased 20% for the three months ended March 31, 2005 as compared to the same period in 2004. Revenue increases were due to an increase in revenue in Brazil (Eletropaulo) of \$218 million due to higher overall tariffs, including the final realization of prior year tariff increases related to lost margin during the 2002 rationing period, favorable foreign currency translation impacts and improved demand; and in the U.S. (IPL) resulting from favorable price variances driven by improved revenue mix slightly offset by lower demand as a result of a warmer winter; offset by revenue decreases of \$2 million in Venezuela (EDC) as a result of the unfavorable effect of exchange rates on revenue only partially offset by favorable price and demand variances.

**Large Utilities Gross Margin**

	For the Three Months Ended March 31, 2005		2004	
	Gross Margin (\$ in millions)	% of Total Gross Margin	Gross Margin	% of Total Gross Margin
North America	\$ 82	10%	\$ 77	11%
South America	167	21%	62	9%
Caribbean*	43	5%	59	9%
Total	\$ 292	36%	\$ 198	29%
Large Utilities Gross Margin as a% of Large Utilities Revenue	28.5	%	24.3	%

\* Includes Venezuela

Gross margin from our large utilities segment increased \$94 million, or 47%, for the three months ended March 31, 2005 compared to the three months ended March 31, 2004. The increase was primarily due to a gross margin increase of \$105 million in Brazil (Eletropaulo) driven by the revenue gains noted above offset partially by transmission costs, a gross margin improvement of \$5 million in the U.S. (IPL) resulting from the revenue gains described above substantially offset by higher fixed costs (including wages and depreciation) and higher variable costs (primarily purchased electricity and fuel costs) and a gross margin decline of \$17 million in Venezuela (EDC) primarily due to a delay in the tariff increase and higher fixed costs (including labor and taxes). Gross margin as a percentage of revenue increased to 28.5% in the first three months of 2005 versus 24.3% in 2004 as a result of the higher margin revenue in Brazil partially offset by the impact of no tariff increases in Venezuela.

**Growth Distribution Revenue**

	For the Three Months Ended March 31, 2005		2004	
	Revenue (\$ in millions)	% of Total Revenues	Revenue	% of Total Revenues
South America	\$ 153	6%	\$ 125	6%
Caribbean*	88	3%	84	4%
Europe/Africa	133	5%	120	5%
Total	\$ 374	14%	\$ 329	15%

\* Includes El Salvador

Revenue from the growth distribution segment for the three months ended March 31, 2005 increased \$45 million, or 14%, compared to the three months ended March 31, 2004. Excluding the estimated impacts of foreign currency translation, revenues would have increased 9% for the three months ended March 31, 2005 when compared to the same period in 2004. Revenue increases in Brazil (Sul) were due to an increase in revenue of \$23 million due to favorable price variances driven by favorable exchange rates, higher tariffs and improved demand; revenue growth of \$10 million in Cameroon (AES Sonel) resulting from improved demand and favorable exchange rates; revenue increase of \$8 million in Argentina (Eden, Edes and Edelap) as a result of favorable price and demand variances; and a combined revenue expansion of \$6 million in our Ukraine and El Salvador utilities primarily driven by higher tariffs and demand.

**Growth Distribution Gross Margin**

	For the Three Months Ended March 31, 2005		2004	
	Gross Margin (\$ in millions)	% of Total Gross Margin	Gross Margin	% of Total Gross Margin
South America	\$ 23	3%	\$ 32	5%
Caribbean*	17	2%	17	2%
Europe/Africa	36	4%	16	2%
Asia	(1 )	%	(1 )	%
Total	\$ 75	9%	\$ 64	9%
Growth Distribution Gross Margin as a % of Growth Distribution Revenue	20.1	%	19.5	%

\* Includes El Salvador

Gross margin from our growth distribution segment increased \$11 million, or 17%, for the three months ended March 31, 2005 compared to the three months ended March 31, 2004. The increase was primarily due to a gross margin increase of \$20 million in Cameroon (AES SONEL) driven by the revenue gains noted above, coupled with lower variable costs primarily as a result of lower fuel and fixed costs; a gross margin decline of \$11 million in Brazil (Sul) resulting from the revenue gains described above being more than offset by higher purchased electricity costs; and a combined gross margin decline of \$2 million in our Ukraine, Argentina, and El Salvador utilities attributable primarily to higher purchased electricity costs. Gross margin as a percent of revenue increased to 20.1 % in the first three months of 2005 versus

19.5% in 2004 as lower costs in Cameroon were largely offset by higher purchased electricity costs in Brazil and Argentina.

### Contract Generation Revenue

	For the Three Months Ended March 31, 2005		2004	
	Revenue (\$ in millions)	% of Total Revenues	Revenue	% of Total Revenues
North America	\$ 196	8%	\$ 217	9%
South America	351	13%	265	12%
Caribbean	142	5%	131	6%
Europe/Africa	141	5%	124	5%
Asia	155	6%	131	6%
Total	\$ 985	37%	\$ 868	38%

Revenue from our contract generation segment for the three months ended March 31, 2005 increased \$117 million, or 13%, compared to the three months ended March 31, 2004. Excluding the estimated impacts of foreign currency translation, revenues would have increased approximately 11% for the first quarter of 2005 versus 2004. Revenue increases are attributable to increased contract pricing in Chile (Gener), Brazil (Tiete, consisting of a group of hydro-electric plants providing electricity primarily to Eletropaulo) and Brazil (Uruguaiana, a gas-fired plant in Brazil providing electricity to Sul and Eletropaulo as well as other third-party customers), partially offset by scheduled decreases in the contracted capacity payments in the U.S. (Shady Point). Higher production volumes favorably impacted revenues in Gener and Ras Laffan (Qatar), with the latter operated as a combined cycle facility in the first quarter of 2005 versus a simple cycle facility in 2004. Favorable foreign currency translation effects positively impacted revenues in Tiete, Gener and Hungary (Tisza).

### Contract Generation Gross Margin

	For the Three Months Ended March 31, 2005		2004	
	Gross Margin (\$ in millions)	% of Total Gross Margin	Gross Margin	% of Total Gross Margin
North America	\$ 74	9%	\$ 96	14%
South America	148	18%	119	17%
Caribbean	41	5%	34	5%
Europe/Africa	60	7%	52	8%
Asia	69	8%	57	8%
Total	\$ 392	47%	\$ 358	52%
Contract Generation Gross Margin as a % of Contract Generation Revenue	39.8	%	41.2	%

Gross margin from our contract generation segment increased \$34 million, or 9%, for the three months ended March 31, 2005 compared to the three months ended March 31, 2004 primarily due to

increased contract pricing in Chile (Gener) and Brazil (Tiete and Uruguaiana), and higher production volumes in Qatar (Ras Laffan) and Gener. The contract generation gross margin as a percentage of revenues decreased to 39.8% for the first quarter of 2005 versus 41.2% for 2004. This decrease was primarily due to Gener procuring higher priced fuel and purchased electricity as a result of gas shortages caused by restrictions on imports of natural gas from Argentina and the scheduled decreases in the contracted capacity payments in the U.S. (Shady Point).

### Competitive Supply Revenue

	For the Three Months Ended March 31, 2005		2004	
	Revenue (\$ in millions)	% of Total Revenues	Revenue	% of Total Revenues
North America	\$ 117	4%	\$ 114	5%
South America	52	2%	31	1%
Caribbean	29	1%	30	1%
Europe/Africa	35	1%	32	2%
Asia	46	2%	36	2%
Total	\$ 279	10%	\$ 243	11%

Revenue from our competitive supply segment for the three months ended March 31, 2005 increased \$36 million, or 15%, compared to the three months ended March 31, 2004. Excluding the estimated impacts of foreign currency translation, revenues would have increased approximately 13% for the first quarter of 2005 versus 2004. Revenue increases are primarily due to significantly higher dispatch of AES's coal-fired plant in Argentina (CTSN) as a result of increased demand caused by gas shortages in Argentina and higher competitive market prices for electricity sold in Argentina (Parana), the U.S. (New York) and Kazakhstan (Ekibastuz). Favorable foreign currency translation effects positively impacted revenues in Hungary (Borsod) and Kazakhstan (Ekibastuz and Altai).

### Competitive Supply Gross Margin

	For the Three Months Ended March 31, 2005		2004	
	Gross Margin (\$ in millions)	% of Total Gross Margin	Gross Margin	% of Total Gross Margin
North America	\$ 28	3%	\$ 28	4%
South America	9	1%	10	2%
Caribbean	15	2%	10	2%
Europe/Africa	(2 )	%	3	%
Asia	15	2%	13	2%
Total	\$ 65	8%	\$ 64	10%
Competitive Supply Gross Margin as a % of Competitive Supply Revenue	23.3	%	26.3	%



Gross margin from our competitive supply segment remained stable for the three months ended March 31, 2005 increasing \$1 million, or 2% compared to the three months ended March 31, 2004. The competitive supply gross margin as a percentage of revenues decreased to 23.3% for the first quarter of 2005 compared to 26.3% for 2004. This decrease was primarily due to higher fuel costs for our businesses in South America (CTSN and Parana) and forced outages in the U.S. (New York).

***General and administrative expenses***

General and administrative expenses increased \$1 million to \$49 million for the three months ended March 31, 2005 from \$48 million for the three months ended March 31, 2004. General and administrative expenses as a percentage of total revenues was 2% in 2005 and 2004.

***Interest expense***

Interest expense decreased \$34 million, or 7%, to \$467 million for the three months ended March 31, 2005 from \$501 million for the three months ended March 31, 2004. Interest expense decreased primarily due to the benefits of debt retirements at the parent company and lower hedge related costs, partially offset by negative impacts from foreign currency translation and increased debt related to new projects.

***Interest income***

Interest income increased \$21 million to \$90 million for the three months ended March 31, 2005 from \$69 million for the three months ended March 31, 2004. Interest income increased primarily due to increased interest rates and higher cash balances.

***Other income***

Other income increased \$11 million to \$22 million for the three months ended March 31, 2005 from \$11 million for the three months ended March 31, 2004. Other income in 2005 primarily consists of gains on contract settlements. Included in 2004 was a gain resulting from a land sale.

***Other expense***

Other expense increased \$12 million to \$37 million for the three months ended March 31, 2005 from \$25 million for the three months ended March 31, 2004. Other expense primarily consists of losses on short-term investments and a write-down of fixed assets to be disposed of.

***Loss on sale of investments and asset impairments***

Loss on sale of investments and asset impairment expense was \$1 million for the three months ended March 31, 2004 as a result of an adjustment to an estimate related to the December 2003 sale of approximately 39% of AES's interest in AES Oasis Limited. There were no sales of investments or asset impairments for the three months ended March 31, 2005.

***Foreign currency transaction losses***

The Company recognized foreign currency transaction losses of \$31 million for the three months ended March 31, 2005 compared to \$34 million for the three months ended March 31, 2004. The \$3 million decrease was primarily related to gains in Venezuela offset by losses in Brazil. The decrease in losses primarily related to foreign currency transaction gains recorded at EDC during the first quarter of 2005 due to an 11% devaluation of the Venezuelan bolivar. EDC's functional currency is the U.S. dollar, and a portion of its debt is denominated in the Venezuelan bolivar. When the Venezuelan bolivar experiences devaluation, gains are recorded related to the bolivar denominated debt. These gains were partially offset by losses at Eletropaulo primarily due to mark-to-market losses on foreign currency transaction hedges.

Foreign currency transaction gains (losses) at certain of the Company's foreign subsidiaries and affiliates were as follows (in millions):

	<b>Three Months Ended March 31,</b>	
	<b>2005</b>	<b>2004</b>
	<b>(in millions)</b>	
Argentina	\$ 4	\$ 7
Brazil	(29 )	(9 )
Venezuela	11	(23 )
Dominican Republic	(7 )	(1 )
Pakistan	(6 )	(4 )
Other	(4 )	(4 )
<b>Total(1)</b>	<b>\$ (31 )</b>	<b>\$ (34 )</b>

(1) Includes \$23 million and \$7 million, respectively, of losses on foreign currency derivative contracts.

#### *Equity in earnings of affiliates*

Equity in earnings of affiliates increased \$9 million, or 56%, to \$25 million for the three months ended March 31, 2005 from \$16 million for the three months ended March 31, 2004. The increase was primarily due to improved operations at our Canadian affiliate and our affiliates in Chile partially offset by a decline at our affiliate in China.

#### *Income taxes*

Income tax expense on continuing operations increased \$72 million to \$147 million for the three months ended March 31, 2005 from \$75 million for the three months ended March 31, 2004. The Company's effective tax rates were 39% and 44% for the three months ended March 31, 2005 and 2004, respectively. The effective tax rate decrease in 2005 from the same period in 2004 was driven by the impact of U.S. taxes on distributions from and earnings of certain non-U.S. subsidiaries.

#### *Minority Interest*

Minority interest expense increased \$52 million to \$106 million for the three months ended March 31, 2005 from \$54 million for the three months ended March 31, 2004. The increase is primarily due to higher earnings from our Brazilian subsidiaries.

#### **Contingent Matters**

As disclosed in Note 5 to the Condensed Consolidated Financial Statements included in Item 1 of this Form 10-Q/A, in exchange for the termination of \$863 million of outstanding Brasiliana Energia debt and accrued interest during 2004, the Brazilian National Development Bank (BNDES) received \$90 million in cash, 53.85% ownership of Brasiliana Energia and a one-year call option (Sul Option) to acquire a 53.85% ownership interest of AES Sul. The Sul Option, which would require the Company to contribute its equity interest in AES Sul to Brasiliana Energia, will be exercisable at the earlier of the Company's announcement to BNDES of the completion of the AES Sul restructuring or June 22, 2005, subject to AES's right to a six month extension under certain circumstances. BNDES's ability to exercise the Sul Option is contingent upon several factors. The most significant factor requires BNDES to obtain consent for the exercise of the option from the AES Sul syndicated lenders. The probability of BNDES exercising the Sul Option is unknown at this time. In the event BNDES exercises its option, 53.85% of our ownership in AES Sul would be transferred to BNDES and the Company would be required to recognize a non-cash after-tax loss on its investment in Sul currently estimated at \$464 million. This amount primarily includes

the recognition of currency translation losses and recording minority interest for BNDES's share of Sul offset by the recorded estimated fair value of the Sul Option.

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

The consolidated financial statements of AES are prepared in conformity with generally accepted accounting principles in the United States of America, which requires the use of estimates, judgments, and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the periods presented. The Company's significant accounting policies are described in Note 1 to the consolidated financial statements included in the Company's Annual Report on Form 10-K/A for the fiscal year ended December 31, 2004 filed with the Securities and Exchange Commission on January 19, 2006. The Company's critical accounting estimates are described in Management's Discussion and Analysis included in the Company's 2004 Form 10-K/A. An accounting estimate is considered critical if: the estimate requires management to make assumption about matters that were highly uncertain at the time the estimate was made; different estimates reasonably could have been used; or if changes in the estimate that would have a material impact on the Company's financial condition or results of operations are reasonably likely to occur from period to period. Management believes that the accounting estimates employed are appropriate and resulting balances are reasonable; however, actual accounting estimates could differ from the original estimates, requiring adjustments to these balances in future periods.

The Company has reviewed and determined that those policies remain the Company's critical accounting policies as of and for the three months ended March 31, 2005. The Company did not make any changes to those policies during the period.

### **Recent Accounting Developments**

See Note 1 to the condensed consolidated financial statements included in this Form 10-Q/A for a discussion of new accounting standards.

### **Capital Resources and Liquidity**

#### *Overview*

We are a holding company that conducts all of our operations through subsidiaries. We have, to the extent achievable, utilized non-recourse debt to fund a significant portion of the capital expenditures and investments required to construct and acquire our electric power plants, distribution companies and related assets. This type of financing is non-recourse to other subsidiaries and affiliates and to us (as parent company), and is generally secured by the capital stock, physical assets, contracts and cash flows of the related subsidiary or affiliate. At March 31, 2005, we had \$5.2 billion of recourse debt and \$13.2 billion of non-recourse debt outstanding.

In addition to the non-recourse debt, if available, we, as the parent company, provide a portion, or in certain instances all, of the remaining long-term financing or credit required to fund development, construction or acquisition. These investments have generally taken the form of equity investments or loans, which are subordinated to the project's non-recourse loans. We generally obtain the funds for these investments from our cash flows from operations and/or the proceeds from our issuances of debt, common stock and other securities. Similarly, in certain of our businesses, we may provide financial guarantees or other credit support for the benefit of counterparties who have entered into contracts for the purchase or sale of electricity with our subsidiaries. In such circumstances, if a subsidiary defaults on its payment or supply obligation, we will be responsible for the subsidiary's obligations up to the amount provided for in the relevant guarantee or other credit support.

We intend to continue to seek where possible non-recourse debt financing in connection with the assets or businesses that our affiliates or we may develop, construct or acquire. However, depending on market conditions and the unique characteristics of individual businesses, non-recourse debt may not be available or available on economically attractive terms. If we decide not to provide any additional funding or credit support to a subsidiary that has a project under construction or has near-term debt payment obligations and that subsidiary is unable to obtain additional non-recourse debt, such subsidiary may become insolvent and we may lose our investment in such subsidiary. Additionally, if any of our subsidiaries lose a significant customer, the subsidiary may need to restructure the non-recourse debt financing. If such subsidiary is unable to successfully complete a restructuring of the non-recourse debt, we may lose our investment in such subsidiary.

As a result of AES parent's below-investment-grade rating, counter-parties may be unwilling to accept our general unsecured commitments to provide credit support. Accordingly, with respect to both new and existing commitments, we may be required to provide some other form of assurance, such as a letter of credit, to backstop or replace our credit support. We may not be able to provide adequate assurances to such counter-parties. In addition, to the extent we are required and able to provide letters of credit or other collateral to such counterparties, this will reduce the amount of credit available to us to meet our other liquidity needs. At March 31, 2005, we had provided outstanding financial and performance related guarantees or other credit support commitments to or for the benefit of our subsidiaries, which were limited by the terms of the agreements, in an aggregate of approximately \$442 million (excluding those collateralized by letters of credit and other obligations discussed below).

At March 31, 2005, we had \$222 million in letters of credit outstanding, which operate to guarantee performance relating to certain project development activities and subsidiary operations. All of these letters of credit were provided under our revolver. We pay letter of credit fees ranging from 0.5% to 2.75% per annum on the outstanding amounts. In addition, we had \$4 million in surety bonds outstanding at March 31, 2005.

Many of our subsidiaries including those in the Caribbean and South America depend on timely and continued access to capital markets to manage their liquidity needs. The inability to raise capital on favorable terms, to refinance existing indebtedness or to fund operations and other commitments during times of political or economic uncertainty may adversely affect those subsidiaries' financial condition and results of operations. In addition, changes in the timing of tariff increases or delays in the regulatory determinations under the relevant concessions could affect the cash flows and results of operations of our businesses in Brazil and Venezuela. Management believes that cash on hand, along with cash generated through operations, and our financing availability will be sufficient to fund normal operations, capital expenditures, and debt service requirements.

#### ***Cash Flows***

At March 31, 2005, we increased cash and cash equivalents by \$218 million from December 31, 2004 to a total of \$1,499 million. The change in cash balances was impacted by \$518 million of cash provided by operating activities offset by the use of cash for investing and financing activities of \$106 million and \$176 million, respectively, and by the negative effect of exchange rates on cash of \$18 million. Cash used for financing activities included a net reduction in debt of \$160 million for the quarter.

*Operating Activities*

Net cash provided by operating activities increased by \$117 million to \$518 million during the first quarter of 2005, versus \$401 million during the same period in 2004 due to an increase in net earnings (adjusted for non-cash items) of \$70 million and a net increase in other assets and liabilities of \$89 million, offset by an increase in working capital of \$42 million. The net increase in other assets and liabilities is due largely to higher non-cash mark-to-market derivative liabilities and proceeds related to a hedge termination payment from the settlement of a foreign currency derivative contract. Working capital changed due to an increase in accounts payable offset by increases in accounts receivable and prepaid expenses and other current assets. The primary reason for the increase in working capital was an increase in current regulatory assets in Brazil due to previously incurred costs which are now allowed to be passed on to the customer.

*Investing Activities*

Net cash used in investing activities totaled \$106 million during the first quarter of 2005 as compared to \$654 million in the first quarter of 2004. In 2005, cash used in investing activities includes \$271 million for property additions and \$85 million for acquisitions, partially offset by the net sale of short term investments of \$158 million and a decrease in restricted cash and debt service reserves of \$94 million.

Property additions increased \$81 million due to additional expenditures of \$126 million at our construction project in Spain offset by a reduction in spending at IPALCO of approximately \$26 million due to spending in the first quarter of 2004 for environmental compliance projects that did not continue at the same level in the first quarter of 2005.

In the first quarter of 2005, we spent a total of \$85 million related to the purchase of the SeaWest wind development business including \$60 million for the existing net assets of the business and an additional \$25 million advance payment for pre-construction costs for SeaWest's development of Buffalo Gap 1, a wind power project in Texas.

The reduction in the net sales of short-term investments of \$217 million quarter over quarter was mainly due to a release of collateral at EDC of \$132 million in March 2005 as a result of a repayment of approximately \$264 million of related debt. In addition, Brazil had net proceeds of \$57 million in the first quarter of 2005 compared to net purchases of \$23 million in the first quarter of 2004. The increase in the sale of investments by Brazil in the first quarter of 2005 were used to pay down debt and various operational expenses, including taxes.

Restricted cash balances decreased by \$502 million during the first quarter of 2005 as compared to the first quarter of 2004 primarily due to AES Gener's issuance of \$400 million of bonds in the first quarter of 2004. Proceeds received from the bond issuance were placed in restricted deposits to be used to complete other refinancing transactions which occurred in the second quarter of 2004.

*Financing Activities*

Net cash used in financing activities was \$176 million during the first quarter of 2005 as compared to \$387 million during the first quarter of 2004 as we reduced debt, net of issuances, by \$160 million in 2005 versus \$340 million in 2004.

Debt issuances declined quarter over quarter by \$707 million primarily due to parent company debt issuances of \$487 million and the AES Gener bond issuance of \$400 million in the first quarter of 2004.

Debt repayments declined quarter over quarter by \$887 million primarily due to parent company debt repayments of \$806 million in the first quarter of 2004.

**Parent Company Liquidity**

Because of the non-recourse nature of most of our indebtedness, we believe that unconsolidated parent company liquidity is an important measure of liquidity. Our principal sources of liquidity at the parent company level are:

- dividends and other distributions from our subsidiaries, including refinancing proceeds;
- proceeds from debt and equity financings at the parent company level, including borrowings under our revolving credit facility; and
- proceeds from asset sales.

Our cash requirements at the parent company level are primarily to fund:

- interest and preferred dividends;
- principal repayments of debt;
- construction commitments;
- other equity commitments;
- taxes; and
- parent company overhead and development costs.

During the past three years, we undertook numerous actions designed to increase parent liquidity, lengthen parent debt maturities, and reduce parent debt and other contractual obligations, both contingent and non-contingent. These actions are consistent with our strategic goals of improving the credit profile of both the parent and the consolidated company in order to reduce our financial risk and improve our credit rating by the major rating agencies. Parent liquidity was as follows at March 31, 2005 and December 31, 2004:

	March 31, 2005	December 31, 2004
	(in millions)	
Cash and cash equivalents	\$ 1,499	\$ 1,281
Less: cash and cash equivalents at subsidiaries	1,243	994
Parent cash and cash equivalents	256	287
Borrowing available under revolving credit facility	218	352
Cash at qualified holding companies(1)	3	4
Total parent liquidity	\$ 477	\$ 643

(1) The cash held at qualified holding companies represents cash sent to subsidiaries of the Company domiciled outside of the U.S. Such subsidiaries have no contractual restrictions on their ability to send cash to the parent company.

## Edgar Filing: AES CORP - Form 10-Q/A

The following table sets forth our parent company contingent contractual obligations as of March 31, 2005:

Contingent contractual obligations	Amount (\$ in millions)	Number of Agreements	Term Range (years)	Exposure Range for Each Agreement
Guarantees(1)	\$ 442	42	<1 - 20+	<\$1 - \$100
Letters of credit under the Revolver	222	15	<1 - 3	<\$1 - \$95
Surety bonds	4	3	<1	<\$1 - \$3
Total	\$ 668	60		

(1) Excluding those collateralized by letters of credit and other obligations

We have a varied portfolio of performance related contingent contractual obligations. Amounts related to the balance sheet items represent credit enhancements made by us at the parent company level and by other third parties for the benefit of the lenders associated with the non-recourse debt recorded as liabilities in the accompanying consolidated balance sheets. These obligations are designed to cover potential risks and only require payment if certain targets are not met or certain contingencies occur. The risks associated with these obligations include change of control, construction cost overruns, political risk, tax indemnities, spot market power prices, supplier support and liquidated damages under power sales agreements for projects in development, under construction and operating. While we do not expect that we will be required to fund any material amounts under these contingent contractual obligations during 2005 or beyond that are not recorded on the balance sheet, many of the events which would give rise to such an obligation are beyond our control. We can provide no assurance that we will be able to fund our obligations under these contingent contractual obligations if we are required to make substantial payments thereunder.

While we believe that our sources of liquidity will be adequate to meet our needs through the end of 2005, this belief is based on a number of material assumptions, including, without limitation, assumptions about exchange rates, power market pool prices and the ability of our subsidiaries to pay dividends. In addition, our project subsidiaries' ability to declare and pay cash dividends to us (at the parent company level) is subject to certain limitations contained in project loans, governmental provisions and other agreements. We can provide no assurance that these sources will be available when needed or that our actual cash requirements will not be greater than anticipated. We have met our interim needs for shorter-term and working capital financing at the parent company level with a secured revolving credit facility of \$450 million. We had \$10 million of outstanding borrowings under the revolving credit facility at March 31, 2005. At March 31, 2005, we had \$222 million of letters of credit outstanding under the revolving credit facility.

Various debt instruments at the parent company level, including our senior secured credit facilities, senior secured notes and senior subordinated notes contain certain restrictive covenants. The covenants provide for, among other items:

- limitations on other indebtedness, liens, investments and guarantees;
- restrictions on dividends and redemptions and payments of unsecured and subordinated debt and the use of proceeds of project financings and asset sales;
- restrictions on mergers and acquisitions, sales of assets, leases, transactions with affiliates and off balance sheet and derivative arrangements; and
- maintenance of certain financial ratios.

### ***Non-Recourse Debt Financing***

While the lenders under our non-recourse debt financings generally do not have direct recourse to the parent company, defaults thereunder can still have important consequences for our results of operations and liquidity, including, without limitation:

- reducing our cash flows as the subsidiary will typically be prohibited from distributing cash to the parent level during the time period of any default;
- triggering our obligation to make payments under any financial guarantee, letter of credit or other credit support we have provided to or on behalf of such subsidiary;
- causing us to record a loss in the event the lender forecloses on the assets; and
- triggering defaults in our outstanding debt at the parent level. For example, our revolving credit agreement and outstanding senior notes, senior subordinated notes and junior subordinated notes at the parent level include events of default for certain bankruptcy related events involving material subsidiaries. In addition, our revolving credit agreement at the parent level includes events of default related to payment defaults and accelerations of outstanding debt of material subsidiaries.

Some of our subsidiaries are currently in default with respect to all or a portion of their outstanding indebtedness. The total debt classified as current in the accompanying consolidated balance sheets related to such defaults was \$291 million at March 31, 2005.

None of the subsidiaries that are currently in default meet the applicable definition of materiality in AES's corporate debt agreements in order for such defaults to trigger an event of default or permit an acceleration under such indebtedness. However, as a result of additional dispositions of assets, other significant reductions in asset carrying values or other matters in the future that may impact our financial position and results of operations, it is possible that one or more of these subsidiaries could fall within the definition of a material subsidiary and thereby upon an acceleration trigger an event of default and possible acceleration of the indebtedness under the AES parent company's senior notes, senior subordinated notes and junior subordinated notes.

### ***ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK***

The Company believes that there have been no material changes in its exposure to market risks during the three months ended March 31, 2005 compared with the exposure set forth in the Company's Annual Report filed with the Commission on Form 10-K/A for the year ended December 31, 2004.

We have performed a company wide value at risk analysis ( VaR ) of all of our material financial assets, liabilities and derivative instruments. The VaR calculation incorporates numerous variables that could impact the fair value of our instruments, including interest rates, foreign exchange rates and commodity prices, as well as correlation within and across these variables. We express Analytic VaR herein as a dollar amount of the potential loss in the fair value of our portfolio based on a 95% confidence level and a one day holding period. Our commodity analysis is an Analytic VaR utilizing a variance-covariance analysis within the commodity transaction management system.

The Value at Risk as of March 31, 2005 for foreign exchange, interest rate and commodities was \$31 million, \$101 million and \$9 million, respectively.

### ***ITEM 4. CONTROLS AND PROCEDURES***

#### ***Conclusion Regarding the Effectiveness of Disclosure Controls and Procedures***

The Company maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in the reports that the Company files or submits under the Securities





and Exchange Act of 1934, as amended (the Exchange Act), is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to the chief executive officer (CEO) and chief financial officer (CFO), as appropriate, to allow timely decisions regarding required disclosures.

The Company carried out the evaluation required by paragraph (b) of the Exchange Act Rules 13a-15 and 15d-15, under the supervision and with the participation of our management, including the CEO and CFO, of the effectiveness of our disclosure controls and procedures (as defined in the Exchange Act Rules 13a-15(e) and 15d-15(e)). Based upon this evaluation, the CEO and CFO concluded that as of March 31, 2005, our disclosure controls and procedures were ineffective. Based upon the initial evaluation completed with the filing of the Form 10-Q, the CEO and CFO concluded that as of March 31, 2005, our disclosure controls and procedures were effective. Due to the subsequent identification of errors requiring the Company to file this Form 10-Q/A, the Company, including the CEO and CFO, revised its evaluation and has concluded that as of March 31, 2005, our disclosure controls and procedures were ineffective.

As reported in Item 9A of the Company's 2004 Form 10-K/A, management reported that material weaknesses existed in our internal controls as of December 31, 2004 and is in the process of taking remedial steps to correct these weaknesses. Due to the fact that these remedial steps have not been completed as of March 31, 2005, the Company performed additional analysis and other post-closing procedures in order to prepare the consolidated financial statements in accordance with generally accepted accounting principles in the United States of America.

#### Changes in Internal Controls

As reported in Item 9A of our 2004 Form 10-K/A, the Company determined that the following material weaknesses in internal control over financial reporting existed as of December 31, 2004:

#### *Income Taxes:*

The Company lacked effective controls for the proper reconciliation of the components of its parent company and subsidiaries' income tax assets and liabilities to related consolidated balance sheet accounts, including a detailed comparison of items filed in the subsidiaries' tax returns to the corresponding calculation of U.S. GAAP balance sheet tax accounts. Management determined that the Company lacked an effective control to ensure that foreign subsidiaries whose functional currency is the U.S. dollar had properly classified income tax accounts as monetary, rather than non-monetary, assets and liabilities at the time of acquisition. These subsidiaries were not re-measuring their deferred tax balances each period in accordance with Statement of Financial Accounting Standard (SFAS) No. 52, Foreign Currency Translation and SFAS No. 109, Accounting for Income Taxes. Finally, the Company determined that it lacked effective controls and procedures for evaluating and recording tax related purchase accounting adjustments to the financial statements.

Although the Company believes it has taken appropriate steps to correct the errors identified and record the appropriate adjustments to the financial statements, it is currently in the process of implementing new controls and procedures related to income tax accounting. These controls include the following:

- Adopting a more rigorous approach to communicate, document and reconcile the detailed components of subsidiary income tax assets and liabilities;
- Expanding staffing and resources, including the continued use of external third party assistance, along with providing training related to the income tax accounting function throughout the Company;
- Continuing to identify and implement additional best practice solutions regarding efficient data collection, integration and controls, including processes to ensure tax related purchase accounting adjustments are properly evaluated and recorded;

- Implementing additional procedures for tax and accounting personnel in the identification and evaluation of non-recurring tax adjustments and in tracking movements in deferred tax accounts recorded by the parent company and its subsidiaries; and
- Recording all tax accounting adjustments on the appropriate subsidiaries' books for ongoing tracking, reconciliation and translation, where appropriate.

*Aggregation of Control Deficiencies at our Cameroonian Subsidiary:*

AES SONEL, a 56% owned subsidiary of the Company located in Cameroon, lacked adequate and effective controls related to transactional accounting and financial reporting. These deficiencies included a lack of timely and sufficient financial statement account reconciliation and analysis, lack of sufficient support resources within the accounting and finance group, and inadequate preparation and review of purchase accounting adjustments incorrectly recorded in 2002, that were not identified or corrected until 2004 and 2005. Management previously reported to the Audit Committee that the aggregation of control deficiencies identified at AES SONEL represented a significant deficiency as of December 31, 2004. Management believed that certain review procedures executed at the parent company mitigated the risk of a more than remote likelihood that a material misstatement to the Company's consolidated financial statements would not be prevented or detected. However, subsequent to the filing of our 2004 Form 10-K, additional accounting errors were identified in 2005 related to the application of purchase accounting principles in 2002 and the translation of local currency financial statements to the U.S. dollar. As a result, the Company revised its previous assessment and determined that the aggregate of control deficiencies constituted a material weakness.

The Company currently is engaged in carrying out its remediation plan that includes the following:

- Hired a new local chief financial officer during the second quarter of 2005 and other key accounting personnel at AES SONEL during the second and third quarters of 2005;
- Implementing controls related to the preparation and review of key balance sheet account analyses and conversion of local currency financial statements to the U.S. dollar;
- Utilizing the Company's internal audit resources to provide remediation assistance and review and evaluate new control procedures; and
- Providing additional detailed accounting policy and procedures guidance for the identification of and accounting for complex or unusual transactions by the subsidiaries, including specific guidance on the proper application of U.S. GAAP.

*Lack of U.S. GAAP Expertise in Brazilian Businesses:*

The Company lacked effective controls to ensure the proper application of SFAS No. 95, Statement of Cash Flows, at Tiete, our 24% owned subsidiary located in Brazil. Although the business had appropriately classified these investments as cash under Brazilian GAAP, the nature of the financial instruments required that they be classified as short term investments in accordance with U.S. GAAP. The Company also lacked effective controls to ensure appropriate conversion and analysis of Brazilian GAAP to U.S. GAAP financial statements for Elpa, one of our Brazilian holding companies, where a long term liability had been appropriately recorded in Brazilian GAAP in 2002 but had been improperly excluded from the U.S. GAAP financial statements. Finally, the Company lacked effective controls at its Brazilian distribution businesses, Eletropaulo and Sul, to ensure the proper application of SFAS No. 71, Accounting for the Effects of Certain Types of Regulation, as it relates to recording a deferral of revenue and corresponding liability associated with costs yet to be incurred for energy efficiency projects.

Management previously reported to the Audit Committee that a lack of U.S. GAAP expertise at Eletropaulo represented a significant deficiency as of December 31, 2004. This determination was made after the discovery of the errors in the calculation of minority interest expense and deferred taxes, as reported in our 2004 Form 10-K filed on March 30, 2005. At that time, management concluded that these errors, in and of themselves, did not constitute material weaknesses and believed that certain review



procedures executed at the parent mitigated the risk of a more than remote likelihood that a material misstatement to the Company's consolidated financial statements would not be prevented or detected. However, as a result of the subsequent identification of control failures resulting in the restatement adjustments described above, the Company revised its previous assessment and determined that the aggregate of control deficiencies and the need for U.S. GAAP expertise in our Brazilian businesses constituted a material weakness.

The Company currently is engaged in carrying out its remediation plan that includes the following:

- Performed a detailed evaluation of all material cash balances at all our subsidiaries to ensure appropriate application of SFAS No. 95. In addition, the Company supplemented its existing accounting policies with additional guidance related to the proper classification of cash and investments in accordance with SFAS No. 95 and communicated this additional guidance to all subsidiaries;
- Added additional supervisory personnel with U.S. GAAP knowledge who are responsible for reviewing and analyzing the financial results of the businesses in Brazil, including an experienced chief financial officer at the regional office level and a chief financial officer at the Brazil country office level, during the second and third quarters of 2005; and
- Providing additional detailed accounting policy and procedures guidance for the identification of and accounting for complex or unusual transactions by the subsidiaries, including specific guidance on the proper application of U.S. GAAP.

*Consolidation Accounting:*

The Company lacked effective controls related to adequate evaluation and documentation of certain journal entries made as part of the preparation of the consolidated financial statements. During the course of the Company's tax remediation activities and in conjunction with other post-closing procedures initiated during the first quarter of 2005, management determined that there were errors in certain entries made in the consolidation process that were initially recorded prior to 2002 and carried forward as unchanged amounts from 2002 through 2004. Management reported in the 2004 Form 10-K/A that it has adequately remediated this material weakness.

*Treatment of Intercompany Loans Denominated in Other Than the Functional Currency:*

The Company lacked effective controls to ensure the proper application of SFAS No. 52, Foreign Currency Translation, related to the treatment of foreign currency gains or losses on certain long term intercompany loan balances denominated in other than the entity's functional currency. In addition, the Company lacked appropriate documentation for the determination of certain of its holding companies' functional currencies. According to SFAS No. 52, intercompany loans, advances or other receivable or payable instruments denominated in other than the entity's functional currency are re-measured with resulting gains or losses recorded to the statement of operations, if payments are being made currently or will be made within the foreseeable future. If settlement is not anticipated in the foreseeable future, then foreign currency exchange gains and losses are to be recorded within other comprehensive income within the equity section of the balance sheet, as the transactions and balances are considered to be part of the net investment. The Company determined it was incorrectly translating certain loan balances due to the fact that it lacked an effective assessment process to identify and document whether or not a loan was to be repaid in the foreseeable future at inception and to update this determination on a periodic basis. Also, the Company had incorrectly determined the functional currency for one of its holding companies which impacted the proper translation of its intercompany loan balances.

The Company currently is engaged in carrying out its remediation plan that includes the following:

- Performed a review and confirmation of the correct evaluation and documentation of certain material intercompany loans with the parent denominated in currencies other than the entity's functional currency to ensure proper application of SFAS No. 52;

- Re-evaluated and documented the functional currencies of certain U.S. and non U.S. holding companies to ensure that proper SFAS No. 52 translations were being performed;
- Providing additional guidance to its subsidiaries to communicate the requirements of SFAS No. 52 related to intercompany loan transactions to ensure proper evaluation of existing and future transactions; and
- Implementing additional procedures to ensure documentation and testing of the proper determination of an entity's functional currency on a periodic basis, particularly as it relates to the company's active material holding company structures.

Although the Company has made progress in this area, additional steps need to be taken, as indicated above, and sufficient time needs to elapse before management can conclude that newly implemented controls are operating effectively and that the material weakness has been adequately remediated.

*Derivative Accounting:*

The Company lacked effective controls related to accounting for certain derivatives under SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities. Specifically, a deficiency was identified related to sufficient controls designed to adequately ensure that the analysis and documentation of whether or not certain fuel contracts or power purchase contracts met the criteria of being accounted for as a derivative instrument at inception and on an ongoing basis. No adjustments to the consolidated financial statements were required to be recorded as a result of this deficiency; however, management concluded that the potential likelihood of a future material error was greater than remote and therefore constituted a material weakness.

The Company currently is engaged in carrying out its remediation plan that includes the following:

- Performed a reassessment of certain material fuel contracts and power purchase contracts to confirm that appropriate documentation existed or that the contracts did not qualify as derivatives;
- Provided additional training regarding identification of derivative instruments and embedded derivatives and the application of the Company's approval policy. Continuing education in this area will be provided on a routine basis and include other non-financial employees who are responsible for hedging activities, development of power purchase agreements and negotiation of significant purchase contracts;
- Enhancing risk management policies and procedures related to the review and approval of material purchase or sale contracts that may qualify as derivatives; and
- Continuing to expand the technical accounting personnel who will support our subsidiaries in the evaluation of derivative implications within hedge instruments and purchase/sale contracts.

Although the Company has made progress in this area, additional steps need to be taken, as indicated above, and sufficient time needs to elapse before management can conclude that newly implemented controls are operating effectively and that the material weakness has been adequately remediated.

In the course of our evaluation of disclosure controls and procedures, management considered certain internal control areas in which we have made and are continuing to make changes to improve and enhance controls. Based upon that evaluation, the CEO and CFO concluded that there were no changes in our internal control over financial reporting identified in connection with the evaluation required by paragraph (d) of Exchange Act Rules 13a-15 or 15d-15 that occurred during the quarter ended March 31, 2005 that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.



**PART II**

**ITEM 1. LEGAL PROCEEDINGS**

The following disclosure provides a summary and update of significant changes, if any, from December 31, 2004, related to our significant claims, suits and legal proceedings. Readers should also refer to Item 3 in Part I of our Annual Report on Form 10-K/A for the fiscal year ended December 31, 2004 filed with the Securities and Exchange Commission on March 30, 2005 and Note 11 of the notes to our consolidated financial statements in Part II of such Annual Report on Form 10-K/A for a more detailed description of each claim.

The Company is involved in certain claims, suits and legal proceedings in the normal course of business. The Company has accrued for litigation and claims where it is probable that a liability has been incurred and the amount of loss can be reasonably estimated. The Company believes, based upon information it currently possesses and taking into account established reserves for estimated liabilities and its insurance coverage that the ultimate outcome of these proceedings and actions is unlikely to have a material adverse effect on the Company's financial statements. It is possible, however, that some matters could be decided unfavorably to the Company, and could require the Company to pay damages or to make expenditures in amounts that could be material but cannot be estimated as of March 31, 2005.

In August 2000, the Federal Energy Regulatory Commission (FERC) announced an investigation into the organized California wholesale power markets in order to determine whether rates were just and reasonable. Further investigations have involved alleged market manipulation. The FERC has requested documents from each of the AES Southland plants and AES Placerita. AES Southland and AES Placerita have cooperated fully with the FERC investigation. AES Southland is not subject to refund liability because it did not sell into the organized spot markets due to the nature of its tolling agreement. The Ninth Circuit recently heard oral argument on the time scope of the refunds. The Ninth Circuit Court of Appeals also addressed the appeal of the FERC's decision not to impose refunds for the alleged failure to file rates including transaction specific data for sales to the California Independent System Operator (ISO) for 2000 and 2001. See *State of California ex rel. Bill Lockyer*. Although in its order issued September 9, 2004 the Ninth Circuit did not order refunds, the Ninth Circuit remanded the case to the FERC for a refund proceeding to consider remedial options. Placerita made sales during the referenced time period. Depending on the method of calculating refunds and the time period to which the method is applied, the alleged refunds sought from AES Placerita could approximate \$23 million.

In July 2001, a petition was filed against CESCO, an affiliate of the Company, by the Grid Corporation of Orissa, India (Gridco), with the Orissa Electricity Regulatory Commission (OERC), alleging that CESCO had defaulted on its obligations as a government licensed distribution company, that CESCO management abandoned the management of CESCO, and asking for interim measures of protection, including the appointment of a government regulator to manage CESCO. Gridco, a state owned entity, is the sole energy wholesaler to CESCO. In August 2001, the management of CESCO was handed over by the OERC to a government administrator that was appointed by the OERC. By its order of August 2001, the OERC held that the Company and other CESCO shareholders were not proper parties to the OERC proceeding and terminated the proceedings against the Company and other CESCO shareholders. In August 2004, the OERC issued a notice to CESCO, the Company and others giving the recipients of the notice until November 2004 to show cause why CESCO's distribution license should not be revoked. In response, CESCO submitted a business plan to the OERC. On February 26, 2005, the OERC issued an order rejecting the proposed business plan. The order also stated the CESCO distribution license would be revoked if an acceptable business plan for CESCO was not submitted to, and approved by the OERC prior to March 31, 2005. On or about March 31, OERC revoke the CESCO distribution license. An appeal of the April 2, 2005 OERC order has been filed. Gridco also has asserted that a Letter of Comfort issued by the Company in connection with the Company's investment in CESCO obligates the



Company to provide additional financial support to cover CESCO's financial obligations. In December 2001, a notice to arbitrate pursuant to the Indian Arbitration and Conciliation Act of 1996 was served on the Company by Gridco pursuant to the terms of the CESCO Shareholder's Agreement (SHA), between Gridco, the Company, AES ODPL, CESCO and Jyoti Structures. The parties have filed their respective statement of claims, counter claims, defenses and answers. Gridco appears to seek approximately \$188.5 million in damages, plus undisclosed penalties and interest, but a detailed alleged damages analysis has yet to be filed by Gridco. On or about April 15, 2005, the parties filed their initial witness statements. A hearing on the merits has been scheduled for August 2005. Other matters that had been pending before the Indian courts were resolved with the exception of a petition before the Indian Supreme Court concerning fees of the third neutral arbitrator and the venue of future hearings. In addition, in December 2001, a petition was filed by Gridco in the local India Court system seeking an injunction prohibiting the Company and its subsidiaries from selling their shares in Orissa Power Generation Company Pvt. Ltd. (OPGC), a 420 MW coal based electricity generation business located in India, and restraining the Company and its subsidiaries from receiving any dividend from OPGC in respect of shares held by them in OPGC until the completion of the CESCO arbitration. The injunctive relief was initially granted on December 23, 2001. Eventually, the injunction was overturned. In January 2005, a new injunction was issued prohibiting the transfer of ownership of the shares of OPGC pending the resolution of the CESCO arbitration. On May 2, 2005, the hearing on the appeal of the new injunction was adjourned until August 2005. Also, in March 2005, the Orissa High Court upheld a decision by the OERC permitting the OERC, as requested by Gridco, to initiate proceedings regarding the terms of the existing power purchase agreement (PPA) at OPGC. The decision was appealed by OPGC to the Supreme Court of India. On April 29, 2005, the Supreme Court granted a stay of the OERC proceedings regarding the PPA as well as the order of the Orissa High Court. A further hearing date on the stay Order has been scheduled for August 2005. The Company believes that it has meritorious defenses to any actions asserted against it and expects that it will defend itself vigorously against the allegations.

In July 2002, the Company, Dennis W. Bakke, Roger W. Sant, and Barry J. Sharp were named as defendants in a purported class action filed in the United States District Court for the Southern District of Indiana. In September 2002, two virtually identical complaints were filed against the same defendants in the same court. All three lawsuits purport to be filed on behalf of a class of all persons who exchanged their shares of IPALCO common stock for shares of AES common stock issued pursuant to a registration statement dated and filed with the SEC on August 16, 2000, (the Share Exchange). The complaints purport to allege violations of Sections 11, 12(a)(2) and 15 of the Securities Act of 1933 based on statements in or omissions from the registration statement concerning certain secured equity-linked loans by AES subsidiaries; the supposedly volatile nature of AES stock, as well as AES's allegedly unhedged operations in the United Kingdom at that time, and the alleged effect of the New Electrical Trading Agreements (NETA) on AES's United Kingdom operations. On April 14, 2003, lead plaintiffs filed an amended and consolidated complaint, which added former IPALCO directors and officers John R. Hodowal, Ramon L. Humke and John R. Brehm as defendants and, in addition to the purported claims in the original complaint, purports to allege against the newly added defendants violations of Sections 10(b) and 14(a) of the Securities Exchange Act of 1934 and Rules 10b-5 and 14a-9 promulgated thereunder. The amended complaint also purports to add a claim based on alleged misstatements or omissions concerning an alleged breach by AES of alleged obligations AES owed to Williams Energy Services Co. (Williams) under an agreement between the two companies in connection with the California energy market. On September 26, 2003, defendants filed a motion to dismiss the amended and consolidated complaint. By Order dated November 17, 2004, the Court dismissed all of the claims asserted in the amended and consolidated complaint against all defendants with one exception. The exception consists of claims against Bakke, Sant, Sharp and AES (the AES Defendants), under Sections 11, 12 and 15 of the Securities Act of 1933, 15 U.S.C. §§ 77k, 77l and 77o, based on the alleged failure of the Registration Statement and Prospectus disseminated to the IPALCO stockholders for purposes of the

Share Exchange to disclose AES's purported temporary default on its contract with Williams. On December 15, 2004, the AES Defendants filed a motion for judgment on the pleadings dismissing the remaining claims. In April 2005, plaintiffs served their first discovery requests to defendants. The Company and the individual defendants believe that they have meritorious defenses to the claims asserted against them and intend to defend these lawsuits vigorously.

In November 2002, a lawsuit was filed against AES Wolf Hollow, L.P. ( AESWH ) and AES Frontier, L.P. ( AESF ), two of our indirect subsidiaries, in the District Court of Hood County, Texas by Stone & Webster, Inc. ( S&W ). At the time of filing, AESWH and AESF were two indirect subsidiaries of the Company. In December 2004, the Company finalized agreements to transfer the ownership of AESWH and AESF. S&W contracted to perform the engineering, procurement and construction of the Wolf Hollow project, a gas-fired combined cycle power plant in Hood County, Texas. In its initial complaint, S&W requested a declaratory judgment that a fire that took place at the project on June 16, 2002 constituted a force majeure event and that S&W was not required to pay rebates assessed for associated delays. As part of the initial complaint, S&W also sought to enjoin AESWH and AESF from drawing down on letters of credit provided by S&W. The Court refused to issue the injunction. S&W has since amended its complaint four times and joined additional parties, including the Company and Parsons Energy & Chemicals Group, Inc. In addition to the claims already mentioned, the current claims by S&W include claims for breach of contract, breach of warranty, wrongful liquidated damages, foreclosure of lien, fraud and negligent misrepresentation. In January 2004, the Company filed a counterclaim against S&W and its parent, the Shaw Group, Inc. ( Shaw ). AESWH and AESF filed answers and counterclaims against S&W, which since have been amended. The exact amount of AESWH and AESF's counterclaims will be identified at the appropriate time in the lawsuit. In January 2004, the Company filed a counterclaim against S&W and its parent, the Shaw Group, Inc. ( Shaw ). Although S&W has yet to provide a detailed damage claim, it has filed a lien against AESWH and AESF, with each lien allegedly valued, after amendment on March 14, 2005, at approximately \$87 million. In March 2004, S&W and Shaw each filed an answer to the counterclaim. The counterclaim and answers subsequently were amended. In March 2005, the Court rescheduled the trial date for October 24, 2005. The Company and subsidiaries believe that the allegations in S&W's complaint are meritless, and that each defendant has meritorious defenses to the claims asserted by S&W. They each intend to defend the lawsuit vigorously.

In late July 2004, the Corporación Dominicana de Empresas Eléctricas Estatales ( CDEEE ), which is the government entity that currently owns 50% of Empresa Generadora de Electricidad Itabo, S.A. ( Itabo ), filed separate lawsuits in the Dominican Republic against Ede Este, a former subsidiary of AES, and Itabo, an AES affiliate. The lawsuit against Itabo also names the president of Itabo as a defendant. In the action against Itabo, CDEEE requested a rendering of accountability for the accounts of Itabo with regard to all transactions between Itabo and related parties. On September 29, 2004, the Court rejected CDEEE's request. CDEEE also requested that the court order Itabo to deliver its accounting books and records for the period from September 1999 to July 2004 to CDEEE, and that an independent expert audit the accounting records and present a report to CDEEE and the court. At a hearing that was held on March 30, 2005, Itabo argued that the court did not have jurisdiction to hear the case and that the case should be decided in an arbitration proceeding. The judge asked the parties to submit briefs on the matter and reserved on the issue. In the Ede Este lawsuit, CDEEE requests a rendering of accountability of the accounts of Itabo of all Ede Este's commercial and financial operations with affiliate companies since August 5, 1999. On February 9, 2005, Itabo filed a lawsuit against CDEEE and the Fondo Patrimonial para el Desarrollo ( FONPER ) seeking among other relief, to enforce the arbitration/dispute resolution processes set forth in the contracts among the parties.

On or about October 27, 2004, AES Red Oak LLC ( Red Oak ) was named as a defendant in a lawsuit filed by Raytheon Company ( Raytheon ) in the Supreme Court of the State of New York, County of New York. The complaint purports to allege claims for breach of contract, fraud, interference with

contractual rights and equitable relief concerning alleged issues related to the construction and/or performance of the Red Oak project. The complaint seeks the return from Red Oak of approximately \$30 million that was drawn by Red Oak under a letter of credit that was posted by Raytheon related to the construction and/or performance of the Red Oak project. Raytheon also seeks \$110 million in purported additional expense allegedly incurred by Raytheon in connection with the guaranty and construction agreements entered with Red Oak. In December 2004, Red Oak answered the complaint and filed counterclaims against Raytheon. In January 2005, Raytheon moved for dismissal of Red Oak's counterclaims. In March 2005, the motion to dismiss was withdrawn and a partial motion for summary judgment was filed by Raytheon seeking return of approximately \$16 million of the letter of credit draw. Red Oak submitted its opposition to the partial motion for summary judgment in April, and expects the Court to schedule a hearing to address the motion in May or June. Meanwhile, Raytheon re-filed its motion to dismiss the fraud allegations in the counterclaim. In late April 2005, Red Oak filed its response opposing the renewed motion to dismiss. The parties are conducting discovery. Red Oak expects to defend itself vigorously in the action.

On or about January 26, 2005, the City of Redondo Beach, California, provided AES Redondo Beach LLC (AES Redondo Beach), a subsidiary of the Company, a notice of assessment for utility user's tax (UUT) for the period of May 1998 through September 2004. The assessment includes alleged amounts owing of \$32.8 million for gas usage and \$38.9 million for interest and penalties. AES Redondo Beach has objected to the assessment. An administrative hearing before the City's Tax Administrator was scheduled and subsequently cancelled. In addition, AES Redondo Beach and the City are engaging in multiple discovery and procedural disputes involving the alleged UUT assessment. In April 2005, in connection with these disputes, the City filed a lawsuit against AES Redondo Beach alleging violations of certain State of California government codes regarding the disclosure of confidential information.

**ITEM 2. UNREGISTERED SALE OF EQUITY SECURITIES AND USE OF PROCEEDS**

None.

**ITEM 3. DEFAULTS UPON SENIOR SECURITIES**

None.

**ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

None.

**ITEM 5. OTHER INFORMATION**

The Securities and Exchange Commission's Rule 10b5-1 permits directors, officers, and other key personnel to establish purchase and sale programs. The rule permits such persons to adopt written plans at a time before becoming aware of material nonpublic information and to sell shares according to a plan on a regular basis (for example, weekly or monthly), regardless of any subsequent nonpublic information they receive. Rule 10b5-1 plans allow systematic, pre-planned sales that take place over an extended period and should have a less disruptive influence on the price of our stock. Plans of this type inform the marketplace about the nature of the trading activities of our directors and officers. We recognize that our directors and officers may have reasons totally unrelated to their assessment of the company or its prospects in determining to effect transaction in our common stock. Such reasons might include, for example, tax and estate planning, the purchase of a home, the payment of college tuition, the establishment of a trust, the balancing of assets, or other personal reasons.

Mr. Paul Hanrahan, Mr. Robert Hemphill, Mr. William Luraschi and Mr. John Ruggirello have adopted trading plans pursuant to Rule 10b5-1.

**ITEM 6.**        **EXHIBITS**

- 31.1    Certification of principal executive officer required by Rule 13a-14(a) of the Exchange Act.
- 31.2    Certification of principal financial officer required by Rule 13a-14(a) of the Exchange Act.
- 32.1    Certification of principal executive officer required by Rule 13a-14(b) or 15d-14(b) of the Exchange Act.
- 32.2    Certification of principal financial officer required by Rule 13a-14(b) or 15d-14(b) of the Exchange Act.

51

---

**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the Company has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Date: January 19, 2006

THE AES CORPORATION  
(Registrant)

By:

/s/ BARRY J. SHARP  
Name: Barry J. Sharp  
Title: *Executive Vice President and Chief  
Financial Officer*

52

---