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## MANAGEMENT REPORT

The Stockholders,

Companhia Hidro Elétrica do São Francisco – Chesf is pleased to submit its Annual Management Report and the Financial Statements for the year ended December 31, 2006, accompanied by the Independent Auditors' Report and the Fiscal Council's Report.

In 2006, as a public electric power service concessionaire Chesf had a good economic and financial performance, keeping itself solid and profitable.

The Company sought a balanced expansion for its business structure, focused on corporate sustainability, with the following achievements standing out:

- Net income of R\$ 457.4 million.
- Participated in the Transmission Auction Nr. 005/2006, held by ANEEL – National Electric Power Agency - ANEEL, whereby the Company was granted Lot F concession, corresponding to the 198-km long transmission line of 230 kV from Funil to Itapebi C3, with investments of R\$ 48 million.
- Participated in the Transmission Auction Nr. 003/2006, held by National Electric Power Agency- ANEEL, whereby the Company granted Lot D concession, corresponding to the 105-km long transmission line of Ibicoara/Brumado of 230 kV, one 230-kV line entry at Brumado substation and increase of sectors 500 kV, 230kV and 138 kV of Ibicoara substation, with the installation of one bench of autotransformers 500/230kV of 300 MVA and two transformers 230/138 kV of 55 MVA. Total investment of R\$ 67.64 million.
- Participated in the Transmission Auction No. 003/2006, held by ANEEL, whereby the Company was granted Lot F, corresponding to the 230-kV transmission lines of Picos / Tauá and Paraíso / Açu II C2, 180 km and 135 km long, respectively, 4 230-kV line entries at Paraíso, Açu, Picos and Tauá substations and the installation of one 15-MVA bar reactor at Tauá and Picos substations. Total investment of R\$ 84.77 million.
- Participated in the Auction of New Projects held in October 2006 by ANEEL through a consortium formed by Chesf (24.5%), Eletronorte (24.5%), Neoenergia (46%) and Construtora Norberto Odebrecht S.A. – CNO (5%), whereby the Company was granted a concession to build and explore a 261-MW hydroelectric power plant at the Dardanelos fall located in Aripuanã River, State of Mato Grosso. Chesf's expected investment totals R\$ 574,114 thousand.
- Finished the construction of Tauá substation of 230 kV, 100 MVA, located at the municipality of Tauá, State of Ceará and substation Joairam of 230 kV, 300 MVA, located at the municipality of Recife, State of Pernambuco.
- Incorporated the electronic platform into the energy business to hold auctions via internet, therefore increasing its competitiveness, making the process nimbler and obtaining higher gains on the sales of Company's products.
- Completed the mapping and tests of the relevant business and information technology processes, aiming at the Eletrobrás Certification in compliance with section 404 of US Law Sarbanes-Oxley – SOX.
- Intensified Social-Oriented Actions, consistently with the Federal Government's principles, through participation in multidisciplinary infrastructure, food security and human development programs in several regions where the Company operates.
- Encouraged cultural and artistic events by sponsoring 551 projects inspired in the Northeastern popular culture and sports.

Throughout its existence, Chesf has always played an entrepreneurial role, providing the infrastructure necessary for the social and economic development of the Northeast Region by working towards the increase of regional participation in the Brazilian economy and the reduction in regional differences.

As a socially-responsible company, Chesf seeks profitability and perennity compatible with society's sustainable development, the conservation of environmental resources and the reduction in social inequalities, as well as the promotion of the Northeast and Brazil's development.

## THE COMPANY'S PROFILE

Chesf, a mixed-economy, publicly-held company was formed pursuant to the Decree-Law number 8.031 of October 3, 1945, and organized at the 1st General Stockholders' Meeting held on March 15, 1948.

The generation system is composed of hydrothermal plants, majority of hydraulic plants that are responsible for over 97% of its total production. Its current generating complex with 10.618 MW of installed capacity is composed of 14 power plants supplied by 9 reservoirs with storage capacity of 52 billion cu.m of water and 1 bio-fuel thermoelectric power plant with 350 MW of installed capacity, as detailed below:

Power Plants	River	Installed Capacity (MW)
<b>HYDROELECTRIC:</b>	-	<b>10,268,328</b>
Paulo Afonso I	São Francisco	180,001
Paulo Afonso II	São Francisco	443,000
Paulo Afonso III	São Francisco	794,200
Paulo Afonso IV	São Francisco	2,462,400
Apolônio Sales (Moxotó)	São Francisco	400,000
Luiz Gonzaga (Itaparica)	São Francisco	1,479,600
Xingó	São Francisco	3,162,000
Funil	das Contas	30,000
Pedra	das Contas	20,007
Castelo Branco	Parnaíba	237,300
Sobradinho	São Francisco	1,050,300
Curemas	Piancó	3,520
Araras	Acaraú	4,000
Piloto	São Francisco	2,000
<b>THERMOELECTRIC:</b>		<b>350,000</b>
Camaçari	-	350,000
<b>TOTAL</b>		<b>10,618,328</b>

As part of the SIN – National Interconnected System, Chesf exchanges energy with the North, South and Southeast/Mid-West systems.

Given the location of its main plants, Chesf is under the influence of the Northeast and Southeast hydrologic cycles, and accordingly, in the period 2005/2006, the main reservoir in the Northeastern region, Sobradinho, was at a mere 54.5% of its total useful volume at the end of the year.

In 2006, the Company generated 54,718 GWh against 49,480 GWh in 2005, with a 10.6% growth. This increase was mostly due to a market on the rising, the SIN's conditions, and the policy of centralizing dispatches put into practice by the ONS – National Electric System Operator.

The transmission system, the first units of which became operative in 1954, covers the states of Alagoas, Bahia, Ceará, Paraíba, Pernambuco, Piauí, Rio Grande do Norte and Sergipe, with 18,260 km of transmission lines in operation, of which 5,122 km are 500 kV transmission circuits; 12,329 km of 230 kV transmission circuits; 809 km of lower tension transmission circuits; 97 substations with higher than 69 kV tension and 698 transformers in operation, with a total transformation capacity of 40,994 MVA, plus 4,907 Km of optical fiber cables.

## RELATIONS WITH INVESTORS

The Company follows management procedures aligned with standards it has to meet and continually monitors the implementation and application of established practices.

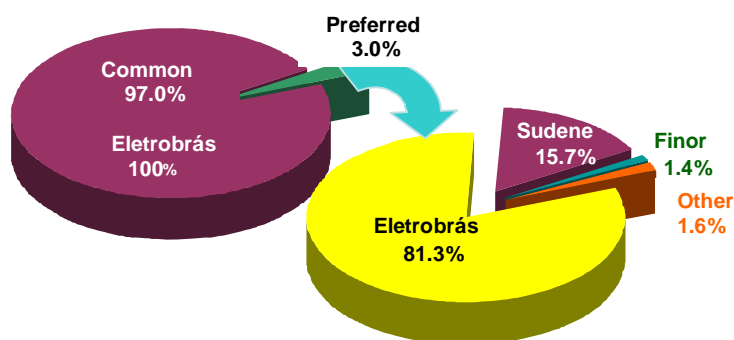
Chesf constantly updates the document called “Policy to Disclose Information about Company Relevant Act or Fact to the Capital Markets”, which establishes guidelines for good relationship between the Company and the Market and through an information channel for disclosing information at its website on the Internet, [www.chesf.gov.br](http://www.chesf.gov.br), under the link “Relations with Investors”.

As a publicly-traded company, Chesf is subject to the rules laid down by the Brazilian Securities Exchange Commission (CVM), although its shares are traded in the over-the-counter securities market.

Relations with investors are maintained by telephone, mail, e-mail and live contact.

### *Ownership*

Capital of company, in the amount of R\$ 1,696.3 million, is comprised in 41,709,653 shares, of which 40,477,564 are common and 1,232,089 are preferred, all without nominal value. Of these, 99.45% is held by Eletrobrás, 0.46% by SUDENE, 0.04% by FINOR and 0.05% by other shareholders.



## **CORPORATE GOVERNANCE**

### ***Administration***

The Company is administered by an Administrative Council and a Board of Directors.

The Board of Directors is composed of a Chairman, elected among the members of the Administrative Council, and up to 5 Directors, all Brazilian, who are elected by the Administrative Council for a three-year tenure on a full time basis.

The Administrative Council is composed of a President and five (5) members, all shareholders elected at the General Stockholders' Meeting for a three-year tenure, who are entitled to re-election. One of the Administrative Council's members is appointed by the Ministry of Planning, Budgeting and Management.

The Fiscal Council is formed by three (3) regular members and three (3) substitutes, all Brazilian elected at the General Stockholders' Meeting for a one-year tenure. One regular member of the Fiscal Council and their substitute will be representatives of the Federal Treasury.

### ***Code of Ethics***

Chesf's principles and values follow its code of ethics and the Corporate Governance standards, all of which serve as a reference for its personnel.

### ***Internal Controls and Auditing***

The Internal Audit, which reports to the Administrative Council, plans, executes and evaluates the Company's audit activities and acts on the requests made by top management and internal and external control bodies. The Annual Plan of Internal Audit Activities - PAINT is submitted to the Federal Government's Controllershship - CGU.

In compliance with Corporate Law, independent auditors engaged through a bidding procedure and approved by the Administrative Council audit Chesf's financial statements. The auditors engaged for the audit are not allowed to render services other than the audit and are rotated every five years.

With the objective of ensuring the best corporate governance practices, in 2006 the Company completed the mapping and tests of the main business and information technology processes, aiming at the Certification of Eletrobrás in compliance with section 404 of US Law Sarbanes-Oxley – SOX, of United States of America.

## **ELECTRIC POWER ENERGY MARKET**

The market projections point to an annual increase of 5.0% in the Brazilian electric power consumption to the period from 2006 through 2016. This increase represents more 30,265 MW average at the end of 2016, i.e., an increase from the current 48,124 MW average to 78,388 MW average by 2016. The Northeast will see an average expansion of 5.1% p.a., increasing from 6,920 MW average to 11,404 MW average, on a single horizon.

The figures show the need for new sources of energy generation, with a strong presence of thermoelectric power plants in the Northeast submarket, according to the Electric Power Expansion Ten-Year Plan for 2006-2015 (PDEE 2006-2015), offering opportunities to expand and diversify the Company's businesses, which is now focused on the National Interconnected System – SIN as a whole.

## **ELECTRIC POWER TRADING**

The energy traded in 2006 reached 47 million MWh, distributed among 21 States of Brazil and the Federal District, with Sales to distributors within the Regulated Contracting Environment (ACR) accounting for 63% of that total. States with the largest share of sales in the segment of distribution were São Paulo (22.12%), Rio de Janeiro (11.70%), Paraná (9.18%), Minas Gerais (8.45%) and Bahia (8.39%).

Sales to the Northeast accounted for about 48% of the total sold by Chesf. Part of this energy was sold directly to the thirteen major industries located in this region.

In 2006, the Electric Power Trade Chamber (CCEE) held an auction of energy from existing projects within the ACR. Chesf sold a total of 130 MW on average, which accounted for approximately 64% of the energy negotiated at this auction, which will be supplied from 2007 for eight years.

Chesf also took part in auctions held at the Free Contracting Environment (ACL), both as a promoting entity (sales auctions) and those held by third parties (purchase auctions), which lead to the signing of 85 contracts with free traders and consumers for various supply periods. When compared with 2005, the number of contracts signed within ACL increased by more than 100%. In terms of energy traded within this environment, it grew 58%, increasing from 1.9 million in 2005 to 3 million MWh in 2006.

The business process got the support of a modern computer platform on which Chesf energy auctions are held. Business transactions are conducted in a virtual environment through a world network of computers, making short-term, medium-term and long-term sales more transparent, competitive and quicker.

## **OPERATING PERFORMANCE**

In 2006, continuous investments were made to train human resources, improve intervention-planning instruments and implement new techniques and processes for maintenance of equipment, transmission lines and protection, control and supervision appliances.

Several actions stand out: the constant improvement in transmission and generation systems, with the replacement of obsolete equipment, digitalization of protection systems and installation of appliances to supervise and control the electric systems, the modernization of the operation centers with the implementation of advanced functions, such as the state estimator, network configurator, alarm address system and operator training simulator.

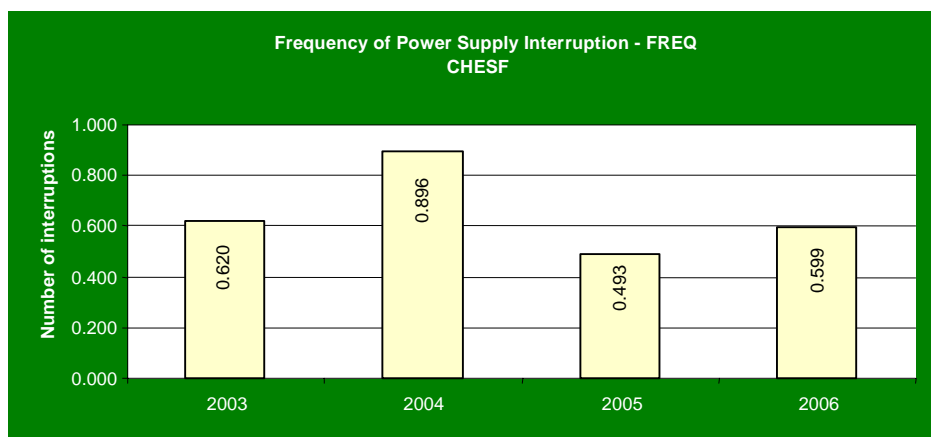
In an effort to enhance the Chesf Telecommunications network, the new optical-digital transmission system services were put in place, Boa Esperança power plant and substation were included in the system thereby increasing the data transmission capacity, adding flexibility and availability to the services due to the increase in the number of alternatives for conveying operating data.

### ***Performance Indicators***

The targets established for indicators of Frequency of Power Supply Interruption – FREQ and Equivalent Power Interruption Duration - DREQ were fully hit, with a significant improvement of DREQ in relation to the previous year. A slight downward trend marked the Operational Availability Equivalent due to problems with the elevator transformers of Luiz Gonzaga Power Plant that affected the available generation and with the synchronous of Substations Recife II and Teresina II that had an impact on available transmission.

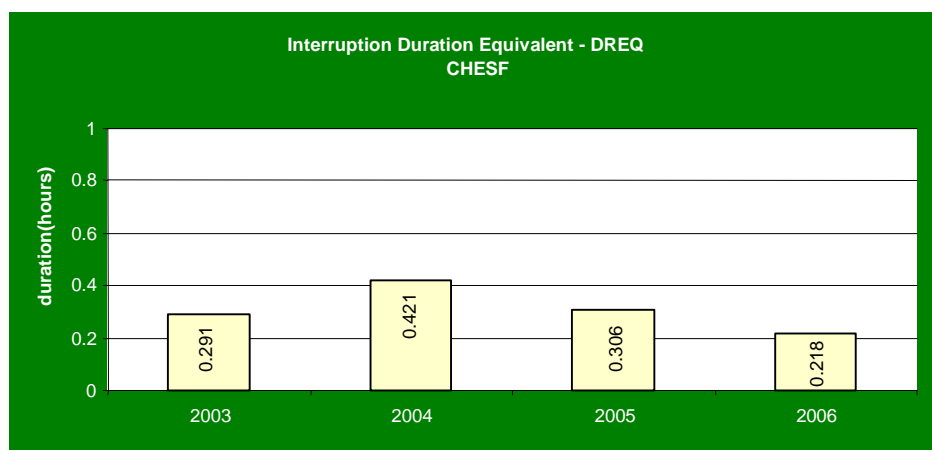
### ***Frequency of Power Supply Interruption - FREQ***

This indicates the equivalent number of electric power supply interruptions.



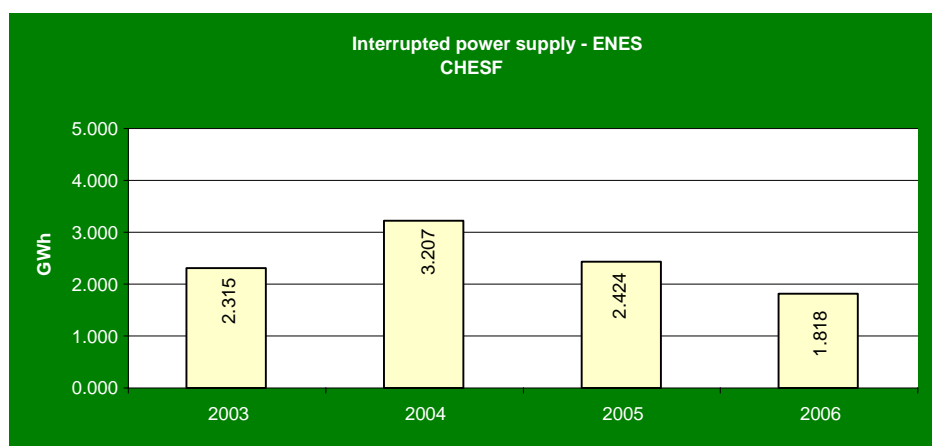
### ***Interruption Duration Equivalent - DREQ***

This indicates the equivalent duration, in hours, of electric power supply interruptions.



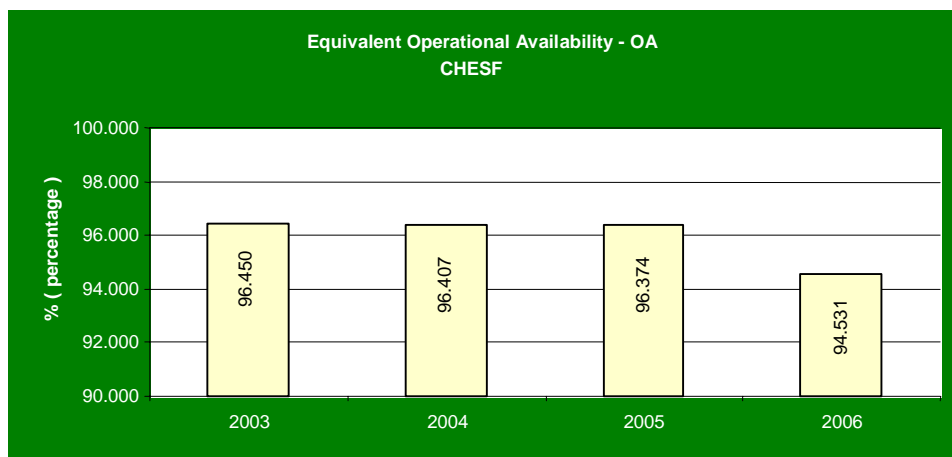
### ***Interrupted Power – ENES***

This indicates the equivalent amount of electric power, in GWh, during supply interruptions.



## Operational Availability - OA

This indicates the likelihood of the equipment being operational, performing its functions, or ready to operate, at any given moment.

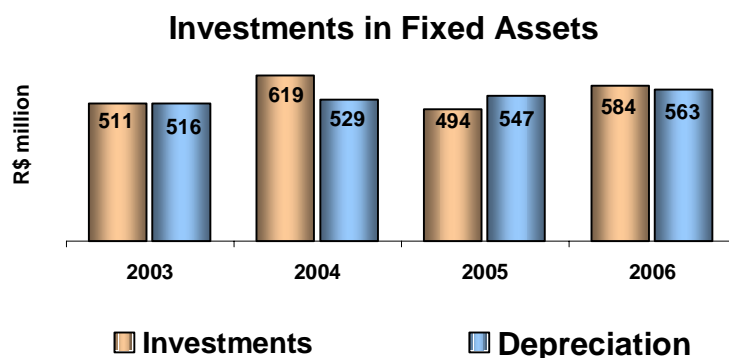


## INVESTMENTS

Chesf made investments to expand and modernize its electric system, increase productivity and improve infrastructure. The amount recorded, considering only additions to property, plant and equipment and intangible assets, totaled R\$ 584 million, distributed as follows:

Summary of investments – R\$ million	2003	2004	2005	2006
▪ Generation – studies, services and equipment.....	209	191	66	57
▪ Transmission – studies, services and equipment.....	189	301	284	335
▪ Relocation of Itaparica – maintenance and indemnities.....	77	90	101	149
▪ Infrastructure – renovations and maintenance.....	36	37	43	43
<b>TOTAL.....</b>	<b>511</b>	<b>619</b>	<b>494</b>	<b>584</b>

The graph below shows investments in fixed assets over the last four years, compared with depreciation expense.





## ***Generation***

Chesf concluded the feasibility studies to implement a combined cycle at the thermoelectric power plant of Camaçari by closing the thermal cycle with the inclusion of a steam turbine, which will allow an increase of 200 MW in capacity.

The digitalization work at 13 generating units of the hydroelectric power plants Paulo Afonso I, II and III was continued. This work will enable centralization of command and higher operating reliability.

In the Hydroelectric Power Potentials Program, the following key actions were taken to increase the supply of power generation in the Northeast:

- In partnership with Construtora Queiroz Galvão and CNEC Engenharia S.A., the Company concluded technical, economic and environmental feasibility studies involving three potential hydroelectric sites detected in the inventory studies carried out on the River Parnaíba basin sites: Ribeiro Gonçalves (113 MW), Uruçuí (134 MW), and Estreito (56 MW). Two other studies of the Cachoeira (63 MW) and Castelhana (64 MW) sites at the same river basin, will be completed in 2007.
- In other partnership with Construtora Norberto Odebrecht, Engevix Engenharia S.A. and Desenvix S.A. the technical, economic and environmental feasibility studies involving two potential hydroelectric sites identified by the inventory studies conducted by Desenvix on the lower-mid São Francisco: Pedra Branca (320 MW) and Riacho Seco (240 MW).

## ***Transmission***

The Chesf Transmission System was expanded with the completion of the following projects:

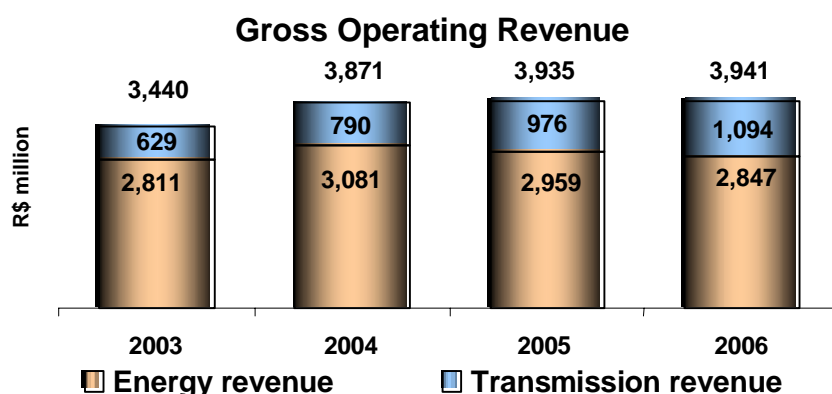
- Re-rating of the 230kV transmission line São João do Piauí – Eliseu Martins with 172.9 km
- Implementation of 434 km of OPGW cables in various transmission lines.
- Tauá substation in 230 kV, 100 MVA, located at the municipality of Tauá, State of Ceara
- Joairam substation in 230 kV, 300 MVA, located at the municipality of Recife, State of Pernambuco
- Increase in the transformation capacity of Goianinha substation, State of Pernambuco 230/69 kV – 100 MVA.
- Increase in the transformation capacity of Banabuiú substation, State of Ceará 230/69 kV – 50 MVA.
- Increase in the transformation capacity of Russas substation, State of Ceará - 230/69 kV – 100 MVA
- Increase in the transformation capacity of Fortaleza II substation, State of Ceará, 500/230kV – 600 MVA
- Construction, assembly and energization of 9 line entries by 230 kV, with 1 at Fortaleza substation, State of Ceará, 2 at Fortaleza II substation, State of Ceará, 2 at Delmiro Gouveia substation, State of Ceará, 1 at Banabuiú substation, State of Ceará, 2 at Milagres substation, State of Ceará and 1 at Coremas substation, State of Paraíba.
- Construction, assembly and energization of 2 line entries by 69 kV at Pau Ferro substation, State of Pernambuco.
- Installation of 2 circuit-breakers of 230 kV at Teresina I substation, State of Piauí.
- Replacement of 8 circuit-breakers of 69 kV, with 3 at Teresina I substation, State of Piauí, 3 at Itabaiana substation, State of Sergipe and 2 at Pirapama II substation, State of Pernambuco.

Chesf has been authorized by ANEEL to implement 1,900 MVA of transformation in the years 2007 and 2008, and it's necessary a further 4,160 MVA until 2009. Additionally, in order to serve the growing market of the Northeast Region, 1,650 km of transmission lines are expected to be installed by 2010, and the invitation to bid for construction and granting of concession, under the responsibility of ANEEL will start in 2007. Accordingly, there is the prospect of expansion of the Company's transmission system and the opportunity to participate in new businesses.

## ECONOMIC-FINANCIAL PERFORMANCE

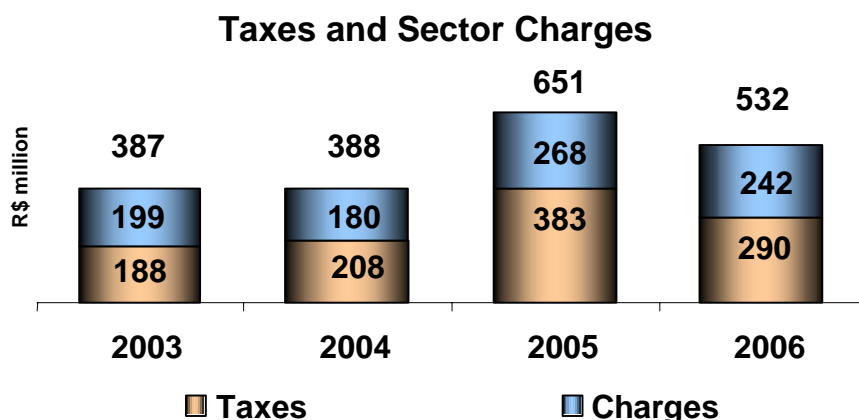
### Gross Operating Revenue

The Company's sales reached R\$ 3,949.8 million, maintaining the same level reported in 2005 (R\$ 3,949.6). Energy sales fell by 3.8%, due to the termination of some contracts for direct supply to industries and a reduction in the supply to distributors and sellers, even considering the increase in sales in the spot market managed by the Electric Power Trade Chamber, which reached R\$ 106.1 million in 2006, against R\$ 27.9 million in 2005. On the other hand, transmission revenues rose 12.1% compared with the prior year, due to the tariff adjustment and the new expansion and revamping work done at the basic network. The graph below shows the gross operating revenue by business segment, without considering other revenues.



### Taxes and Sector Charges on Sales

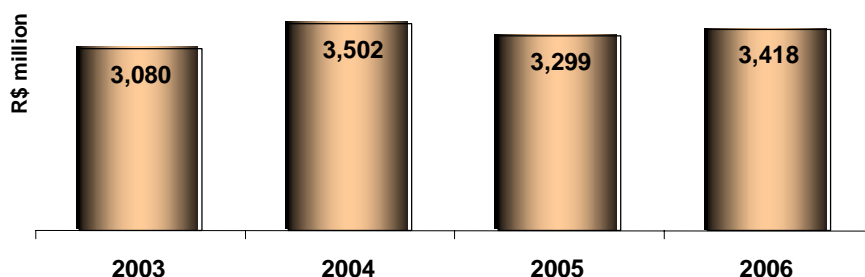
Chesf is one of the largest taxpayers of the Northeast. In 2006, sales taxes and charges reached the amount of R\$ 531.6 million, against R\$ 650.7 million in 2005, a reduction of 18.3% basically due to the interruption of the collection of the emergency capacity charge and the changes in the application of the Pis/Pasep and Cofins (taxes on revenue) rates for contracts signed before October 31, 2003.



### Net Operating Revenue

The net operating revenue - R\$ 3,418.2 million – increased by 3.6% in relation to the R\$ 3,298.9 million of 2005. This growth reflected, mainly due to the decrease in taxes and emergency capacity charge deductible from gross operating revenue.

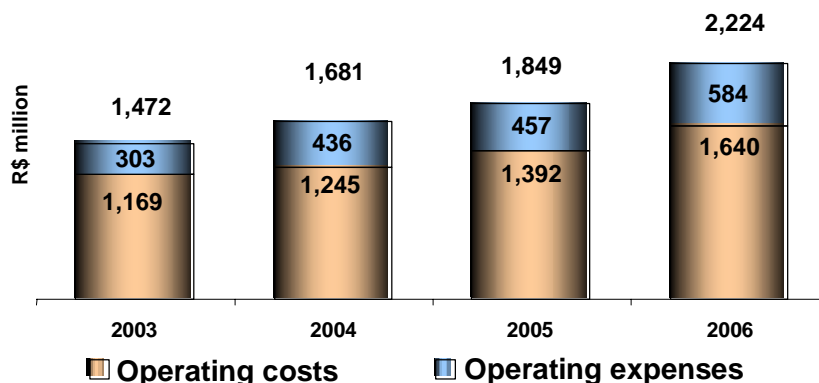
#### Net Operating Revenue



### Operating Costs and Expenses

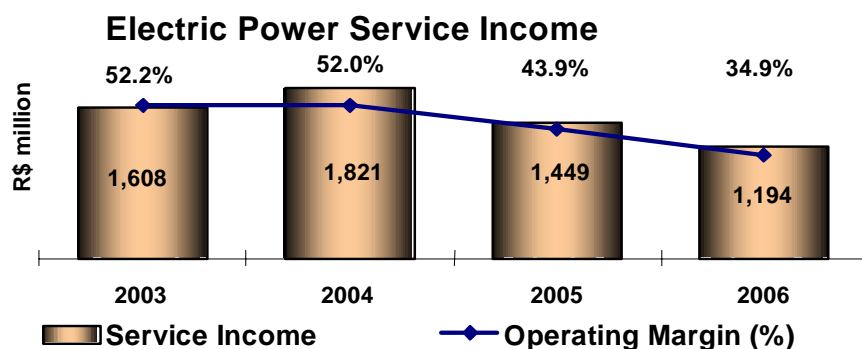
In 2006, the operating costs and expenses totaled R\$ 2,223.9 million, against R\$ 1,849.5 million in 2005, with a 20.2% growth. This growth basically reflected the high increase in non-manageable items *charges on use of the electric power network*, 56.7% (2006 - R\$ 575.5 million as compared to R\$ 367,3 million in 2005) and *financial compensation for water use*, which rose by 17,6% (R\$ 206,6 million in 2006, as compared to R\$ 175,6 million in 2005). On the other hand, the caption *Energy purchased for resale* fell from R\$ 88.5 million in 2005 to R\$ 1.5 million in 2006. Prior years' expenses were recognized under the caption *Research and Development* which, added to those of the year, totaled R\$ 152.2 million, up 928.4%, compared to the amounts reported in 2005 (R\$ 14.8 million). This year, an allowance for doubtful accounts was also recorded in the amount of R\$ 109 million to cover possible losses on the realization of receivables from the transfer of energy from independent suppliers, provided for in the General Electric Energy Sector Agreement.

#### Operating Costs and Expenses



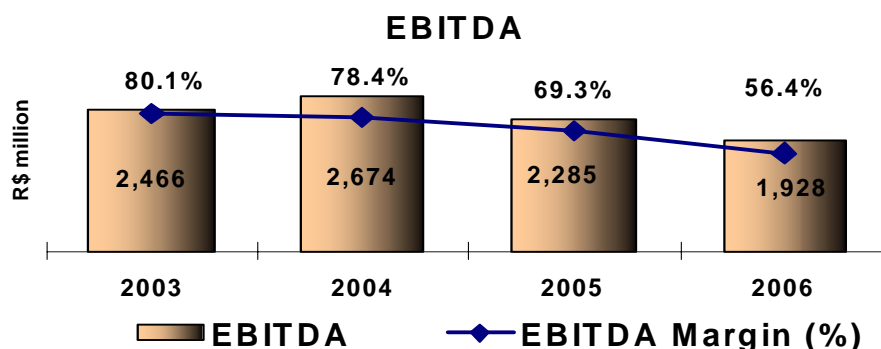
### Service Income and Operating Margin

The performance of operating revenues, costs and expenses resulted in Service Income of R\$ 1,194.3 million, directly reflecting the behavior of its main activity, the electric power business, which was 17.6% lower than the R\$ 1,449.4 million recorded in 2005. As a consequence, the Operating Margin (service income / net revenues) fell from 43.9% in 2005 to 34.9% in 2006.



### Operating Cash Generation (EBITDA)

The operating cash generation as measured by EBITDA (pretax income, interest, depreciation and amortization) fell to R\$ 1,928.2 million in 2006, from R\$ 2,285.0 million in 2005, with a 15.6% decrease. This was basically due to a lower operating margin. The EBITDA in relation to net revenues – 56.4% -, in turn fell by 12.9 percent points as compared to 2005.



#### Reconciliation of EBITDA (R\$ million)

	2006	2005
<b>Net income</b> .....	<b>457.3</b>	<b>746.4</b>
(+) Income and social contribution tax.....	120.5	247.3
(+) Profit sharing.....	47.9	41.5
(+) Non-operating income.....	5.8	7.3
(+) Financial expenses.....	735.4	652.6
(+) Depreciation.....	563.5	546.8
(+) Provisions for contingencies.....	(2.2)	43.1
<b>(=) EBITDA</b> .....	<b>1,928.2</b>	<b>2,285.0</b>

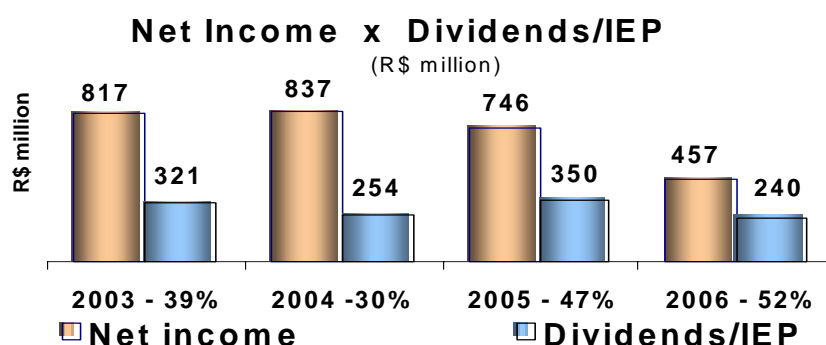
### Financial Income

The net financial income for the year rose by 38.3% compared to 2005, with debits of R\$ 562.8 million and R\$ 406.9 million, respectively. The main reason was the increased monetary variation on loans and financing and the reduced financial income.

Financial income (expenses) – R\$ million	2006	2005
Income from financial investments.....	22.2	21.8
Income from refinancing granted to clients.....	131.2	228.5
Interest and monetary variations on loans and financing.....	(617.2)	(564.5)
Other financial income (expenses).....	(99.0)	(92.7)
<b>(=) Financial result net.....</b>	<b>(562.8)</b>	<b>(406.9)</b>

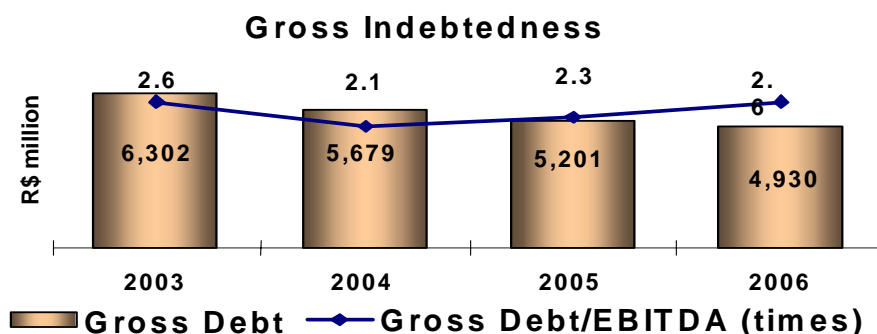
### Net Income and Stockholders' Compensation

As a result of the factors mentioned above, the Company closed 2006 with a net income of R\$ 457.4 million, against R\$ 746.4 million in 2005. The Company will propose to the General Stockholders' Meeting gross compensation of R\$ 240 million as interest on equity capital borne on dividends, equivalent to R\$ 5.75 per common and preferred share.

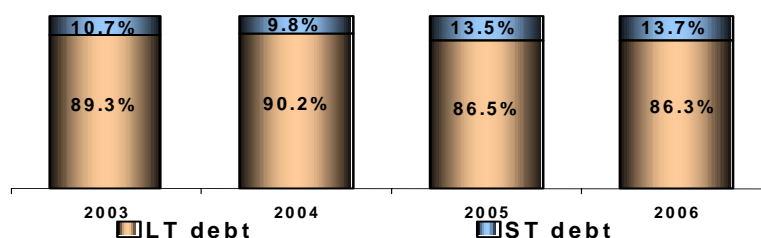


### Gross Indebtedness

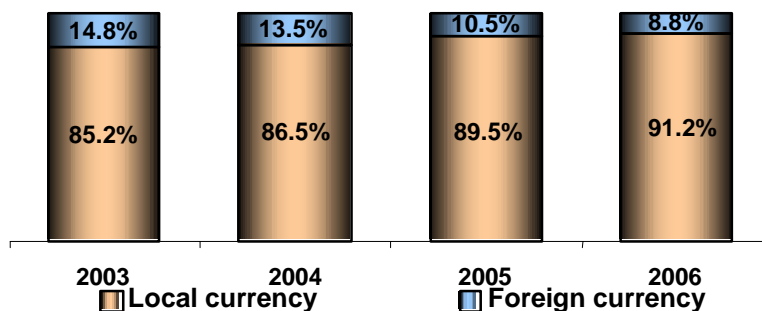
In 2006, Chesf improved its debt's composition and profile. Gross indebtedness (payables to financial institutions and the parent company) fell from R\$ 6,302.5 million in 2003 to R\$ 4,930.1 million at the end of 2006, a 21.8% reduction in the period. Compared to 2005, gross indebtedness fell by 5.5%. Short-term debts correspond to 13.7% of gross indebtedness. In 2006, the share of foreign-currency indebtedness is only 8.8% of total debt.



### Profile of Gross Debt %



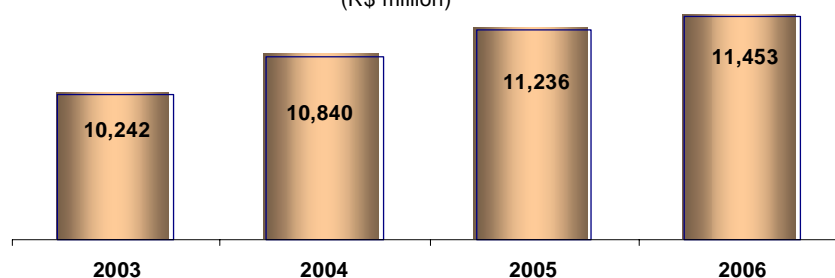
### Debt Breakdown %



### Changes in Stockholders' Equity

At the end of 2006, the Stockholders' Equity of the Company totaled R\$ 11,453.4 million against R\$ 11,236.0 million at the end of 2005, with a 1.9% growth. This increase was the result of earnings partially retained since 2003, in order to fund substantial portions of the Company's investments .

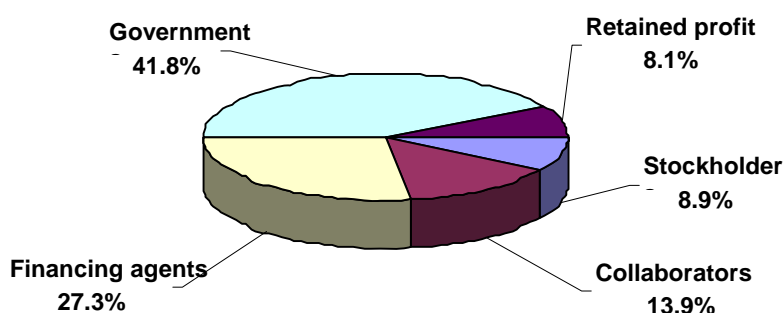
### Changes in Stockholders' Equity (R\$ million)



### **Value Added**

Chesf has been strongly promoting the Northeastern and Brazilian economies. The Company's contribution to the Brazilian economic growth was R\$ 2,686 million of value added, in 2006 the equivalent to 68.1 % of its net operating revenue, against the 75.5% recorded in 2005, with a 7.4% reduction. This amount was given in return to the society as a whole, by way of salaries, payroll taxes and benefits to its employees and their families (13.9%); taxes, fees and contributions to the municipal, state and federal governments (41.8%); interest paid to the financiers of assets and services (27.3%); stockholders' compensation (8.9%) and retention of profits (8.1%).

#### **Distribution of Value Added**



### **RELATIONS WITH INDEPENDENT AUDITORS**

The Company's policy for engagement of independent auditors relies on principles that preserve their independence. Accordingly, a service contract was signed with the auditing firm BDO Trevisan Auditores Independentes on 12/17/2002, covering the period from December 2002 through May 2007. It should be stressed that in compliance with CVM Instruction 381, of 01/14/2003, ratified by the Circular Letter/CVM/SNC/SEP/number 02/2005, of 08/24/2005, no other service contract exists with this firm.

### **SHAREHOLDING**

Following the federal government's policy of attracting private capital for investments in the energy sector, the Company formed partnerships that generated minority shareholdings in the following companies:

#### ***Sistemas de Transmissão Nordeste S.A – STN***

The Company has a 49% stake in the voting capital of Sistema de Transmissão Nordeste S.A – STN, set up in 2003 together with Companhia Técnica de Engenharia Elétrica – ALUSA, to explore the concession for installation of the National Interconnected System's basic network in Teresina II – Sobral III - Fortaleza II stretch, with 500kV. These works were completed on 12/19/2005 and the commercial operation stage started on 01/01/2006. STN had a net income of R\$ 27.4 million, and allocated R\$ 6.50 million for dividends, of which R\$ 3.2 million was paid to the Company.

### ***Energy Transmission Integration S.A – INTESA***

The Company formed one more energy transmission partnership acquiring a 12% stake in the capital stock of Integração Transmissora de Energia S.A – INTESA, which is engaged in building, implementing, operating and maintaining the Electric Power Transmission Public Service of the Interconnected Electric System's Basic Network, consisting of the 500-kv transmission line of Colinas/Serra da Mesa 2.3° circuit, related line entries and facilities, pursuant to Concession Agreement No. 002/2006-ANEEL, signed with the concession authority on April 27, 2006, through ANEEL for a period of 30 (thirty) years. INTESA has an authorized capital of R\$ 150 million in registered common shares, without par value, of which R\$ 15,600 thousand was subscribed and paid in by Chesf in the year. The other participants are Fundo de Investimentos em Participações Brasil Energia – FIP, with 48%, Eletronorte, with 37% and Engevix Engenharia S.A, with 3%. INTESA is expected to start operations on April 27, 2008.

### ***Aripuanã Consortium***

On October 10, 2006 the Company took part in auction Nr. 004/2006-ANEEL, for the acquisition of energy from new projects and subsequent granting of the concession within the Regulated Contracting Environment (ACR) to build the Dardanelos Hydroelectric Power Plant – UHE Dardanelos, as a member of the Aripuanã Consortium, winner of the auction. For the execution of the project, Aripuanã Energia S.A is being set up, whose shareholder composition is as follows: Chesf (24.5%), Eletronorte (24.5%), Neoenergia S.A (46.0%) and Construtora Norberto Odebrecht S.A. (5.0%).

The Dardanelos Hydroelectric Power Plant will be built in the Aripuanã River, in the north of the State of Mato Grosso, with a capacity of 261 MW and total guaranteed energy of 154.9 MW on average to supply energy to the municipality of Aripuanã and subsequently to the National Interconnected System. Expected investment is R\$ 574.114 thousand and the concession for energy generation is valid for 30 years. The first machines are scheduled to start operations in 2011. 147 MW on average was traded from 2011 to 2041.

## **RESEARCH AND DEVELOPMENT PROGRAM**

Chesf has been developing Research & Development programs with some of the most prestigious teaching and research entities in the country to cut costs, postpone investments, make processes more efficient and implement innovative solutions for its products. Chesf has been investing significant funds, pursuant to Law No. 9.991/2000, in projects that include the wide scope of activities directly and indirectly involved in the value chain of the Company's business.

In 2006, projects of the three first cycles underway were continued, and the approval process of new project cycles with ANEEL and their corresponding launch were intensified. In 2006 all first-cycle and 80% of the second-cycle projects were concluded, and important results were obtained, some of which, already implemented, made Chesf's system more efficient. In the same period, ANEEL approved the fifth cycle, adding 28 new projects, representing a total investment of R\$ 15 million, including those remaining of prior years. In addition, a Chesf submitted to that Agency 37 new sixth-cycle projects for approval.

Also noteworthy are projects under development by the Electric Power Research Center - CEPEL, using statutory contributions of the Eletrobrás's System supporting partners, among which is Chesf, whose contribution represents 8% of CEPEL's annual budget.



## **SOCIALLY-ORIENTED ACTIONS – AN ASSESSMENT**

Throughout its 59 years of existence, Chesf has played an important role in the development of the Northeastern Region.

The Company pursued existing programs and implemented new actions that contributed for a socially-responsible management of its employees, interaction with suppliers, and relations with the communities around the project and the society in general. The Company's social and environmental activities include environmental care and participation in Government's programs.

### **PEOPLE MANAGEMENT (EMPLOYEES)**

In 2006, 202 new employees were hired to be part of Chesf's personnel of 5,688 people. The turnover rate in the year was 3.03%. The Company proceeded with its Competency-based People Management Model. By adopting this model, the Company will improve the management of its intellectual assets and bring the human resources strategies into line with the business strategies, all for better corporate results. The commissions equally-composed by unions and Chesf continued to work on projects started in the prior year: Technical Responsibility Recording, Job, Career and Salary Plan, Labor Obligations, Labor Health and Security. The equally-composed commission for camping policies was set up again. Due to the actions performed according to suggestions of that commission, improvements were made in the rendering of public cleaning, paving and urbanization services; ambulances providing intensive care were made available for employees and their dependents in the camping areas of Boa Esperança, Sobradinho and Xingó and Chesf's houses were sold to their dwellers at the Company's camping areas.

#### ***Employees' Compensation and Benefits***

The Company's benefit plan is extensive and entitles employees to a wide range of food, education and health benefits, including profit sharing. In 2006, R\$ 43.5 million was distributed. Chesf's allowance to cover part of employee dependents' school monthly payments was extended to dependents up to 14 years of age. Chesf's Assistance and Social Security Foundation (Fatchesf) has 12,531 participants, 5,399 of whom are active and 7,132 assisted.

#### ***Training and Development***

The Company permanently invests in its employees' professional development. In 2006, the average number of hours of training per employee was 91.29, corresponding to 4.56% working hours. This represented an increase of 13.46 hours compared to 2005. The offer of long-duration courses was increased to develop the skills required by the Company's business, among which the Master's Degree in Electrical Engineering and Finance, graduate studies in Energy Trading and Electric Power Business Management stand out. The offer of courses for medium-level technicians and distance-training courses was significantly increased.

### ***Health, Security and Working Conditions***

In the health care field, several programs and campaigns planned based on the employees' health profile and absenteeism for medical reasons were put into practice. Many of these were of a preventive nature, namely: the collective vaccination against influenza; lectures, health advice, ergonomic exercises at work site. Chesf Health Club was opened at the head office, a special workplace exercise program was implemented to reduce bone and muscle problems and therapeutic massage sessions started to be offered at head and regional offices. Such actions helped to reduce absenteeism for medical reasons. The Bio-psycho-social Monitoring Program was expanded and served 581 employees. The Emergency Action Plan (PAE) was selected as one of the three best projects by Fundação COGE in the category of Occupational Safety and Health Management.

Preventive actions were pursued to improve workplace safety. A safety visa was established as a requirement to hire outsourced companies, as well as safety and health criteria to be met by contracted companies. Chesf's employees who work in heights received refresher training to learn to use new techniques and equipment.

### ***Diversity Valuation***

In Chesf's view, enhancing diversity is fundamental for ensuring a healthy and solidary organization atmosphere.

Regarding individual rights, Chesf authorized the inclusion of employees' homosexual partners as dependents for purposes of the Employer Assistance Plan (PAP). It started to include in its standards the repudiation of any type of discrimination. It pursued actions that increase the social inclusion of disabled people. Employees and trainees learnt the deaf language.

## **COMMUNITY-ORIENTED ACTIONS**

Committed to the Northeastern Region, Chesf opted to continue investing in social and environmental programs and projects oriented towards the communities of that region. The Company gave priority to structuring programs and projects that met previously defined criteria, entering into partnership with government agencies, civil entities, third sector's entities and communities. The main target publics are destitute people living around its generation facilities, communities of municipalities where substations are implemented or transmission lines are located, and communities of municipalities of the Metropolitan Regions of the States of Piauí, Ceará, Rio Grande do Norte, Paraíba, Pernambuco, Alagoas, Sergipe and Bahia, where the Company's main facilities are located.

Chesf's programs and projects have the following objectives.

### ***Food Aid, Job and Income Generation, and Regional Development***

The Company invested in vegetable gardens to generate jobs and income, directly benefiting 85 destitute families in Salvador, State of Bahia and Messias, State of Alagoas, and continued to support community vegetable gardens in roadside areas under transmission lines in Teresina, State of Piauí, which benefit 750 families. Various food security projects were carried out with the participation of Company volunteers in communities of the States of Alagoas, Bahia, Ceará, Paraíba and Pernambuco assisting approximately 620 families and 500 children and teenagers. Manjar project, in Campina Grande, State of Paraíba, includes food aid and actions to generate income for more than 120 destitute families, in a partnership with a church in that town.

Various projects were implemented to promote regional development, some of them aligned with the Federal Government's social programs. "Programa Luz Para Todos" (Light for All Program) is the most extensive. This program aims to supply electric power to people in the Brazilian rural area without access to this utility. Chesf's Director of Operations is in charge of coordinating the Program in the Northeastern Region. In 2006, 207,952 connections were made benefiting 1,039,760 people.

Various projects to generate jobs and income were pursued such as: goat and sheep raising, benefiting about 150 small ranchers; beekeeping with 40 families being assisted; paper recycling, benefiting 40 families; fish farming, covering 150 fishermen and farmers; 300 women were trained in sewing, phytotherapy and craftsmanship; education, craftsmanship and fishing seminars and workshops, with the participation of about 500 participants; "Menor Aprendiz", a job training program for 271 apprentices. Chesf invested, in a partnership with third-sector entities and Chesf's volunteers, in the training of 15 young electricians in Paulo Afonso, State of Bahia. In Recife, State of Pernambuco, 20 youngsters took the Building Installation course. 75 physically and visually disabled people and hearing-impaired people were trained and entered the job market earning income.

At the Regional Office of Paulo Afonso, Chesf granted areas and facilities to education, health and security public agencies. In Recife, State of Pernambuco, Praça Apolônio Sales was built in a partnership with the Municipal Government of Recife, to be used by the communities living around the head office building.

### ***Education and Dissemination of Knowledge***

The Company proceeded with distance teaching training for 250 teachers of municipalities of the States of Alagoas, Bahia, Pernambuco and Sergipe. Courses in various areas and high school equivalency programs on TV were offered to 175 students in the States of Alagoas and Pernambuco. In Paulo Afonso, State of Bahia, 82 workers from poor communities took primary and high school equivalency courses. Chesf invested in remedial courses for 300 poor children and adolescents under social risk in Recife, State of Pernambuco and Sobradinho, State of Bahia. In Recife, 324 youngsters learn computer skills together with voluntary employees from Chesf. "Programa Leia Mais" (Read More Program) to encourage reading, served 4,500 children and adolescents in Paulo Afonso, State of Bahia. In addition, the following were offered: training programs for 230 high-school and university level trainees at the head and regional offices; training programs for 40 students at Nair Alves de Souza Hospital, in Paulo Afonso and; remunerated training program for 56 disabled students.

### ***Health***

The Company invested approximately R\$ 7.6 million in Nair Alves de Souza Hospital, to improve management and physical structure, to purchase equipment and maintain the hospital. 289,866 people from more than 20 municipalities of the States of Bahia, Pernambuco, Alagoas and Sergipe were seen. Under "Programa Viva Mulher" to treat gynecological cancer 400 women were seen. In Salvador, 200 children of communities living around Chesf's building received medical care. Several workshops were held at the head and regional offices on breastfeeding, child nutrition, preparation of mixtures of water, oral rehydration solution, prevention of Hansen's disease, tuberculosis, hypertension, diabetes, breast and cervix cancer, sexually transmitted diseases and AIDS, mouth and sanitary hygiene and health promotion, benefiting approximately 1000 adolescents and adults. In Recife, State of Pernambuco, Salvador, State of Bahia, Paulo Afonso, State of Bahia, Sobradinho, State of Bahia and Teresina, State of Piauí 1,695 women underwent several specialized examinations and received medical care. 600 children and adolescents received advice on prevention of diseases and use of drugs.

### ***Environmental Quality***

Chesf is careful about the use of its generation and transmission assets and the storage and handling of hazardous products. In 2006, the Company invested R\$ 9.1 million in environmental conservation programs.

All the Company's generation units operate under environmental licenses. 137 old transmission enterprises are awaiting the conclusion of their regularization.

At all, 2,400 people from communities surrounding the transmission and generation enterprises were trained in environmental education.

The Company conducted studies and monitored water ecosystems, comprising the limnologic monitoring of water quality in Itaparica reservoirs, Paulo Afonso and Xingó complexes. The salt-water wedge was monitored and the preservation of water fauna and the fish rescue upon machine stop and spillway closing were provided for. A Chesf conducted studies and monitored the flora and fauna in areas of the São Francisco and Parnaíba river basin, which included the production of native caatinga cuts, monitoring of the flora in legal reserve areas and selective re-planting of roadside areas. Environmental risks caused by hazardous residues were monitored and an archeological Survey was conducted to rescue and preserve the social and cultural heritage.

In order to revitalize the São Francisco River, Chesf invested: in the production of 200,000 native caatinga cuts and recovery of 20 hectares of degraded areas in Xingó; in the recovery of the fish fauna of the middle and low São Francisco river, including the expansion of the fish farm in Paulo Afonso to produce two million sixty thousand fry of eight native species to populate the river and reservoirs. Health and sanitation actions were taken (sewage network projects and improvements in water treatment plants) and support was given to municipalities that already operate or will start operating the household water treatment systems in the irrigated areas of the Itaparica Relocation Program.

A study was conducted to assess the impact of Chesf's transmission lines on the Indigenous community of Fulni-ô. Based on the results of this study, the Company negotiated with the community and FUNAI the payment of damages of R\$ 3 million for potential damages caused in the past and those expected through 2015. The Conduct Adjustment Commitment, to be signed by Chesf / FUNAI and Fulni-ô community, define the manner funds will be invested.

Garbage disposal, recycling and material reuse projects were carried out benefiting hundreds of people from poor communities. Chesf prepared a guide on the fauna and flora of the Atlantic Forest of the Pituaçu complex and the children's magazine called "Conhecendo a Mata Atlântica da Chesf na Paralela", distributing the publications to public schools in Salvador. Also in Salvador, more than 2,500 public school students received instructions on the risks of flying kites near transmission lines.

### ***Culture and Sports***

In 2006, Chesf invested R\$ 23.8 million to sponsor 551 cultural and sports projects. Apart from generating thousands of direct and indirect jobs, the Company contributed to the development of the Northeast, helping to foster citizenship. The Company supported various artistic sectors, sports events and encouraged the recovery of Northeast's cultural heritage. This attitude goes beyond the financial incentive, showing the Company's commitment to preserve our history, our roots and our customs.

### ***Itaparica Relocation Program***

Chesf invested R\$ 148.8 million in the Itaparica Relocation Program, in works, services, purchase of equipment, assistance to relocated people and farming production, environmental protection programs, indemnity to the indigenous community of Tuxá and regularization of title to property. As far as relocation of this community is concerned, an amendment to the Conduct Adjustment Term - TAC, which sets forth each party's commitments to conclude the process, was signed whereby the obligation of implementing irrigation perimeters was converted into payable damages, about 55% of which was paid by Chesf. The water main system of the Barreiras Bloco 2 perimeter was completed and the implementation of distribution networks and development of the parcels of land that will be part of the perimeter were pursued.

Maintenance and expansion works were performed on the agricultural drainage system in the Apolônio Sales Projects and these services were commissioned for Brígida Project. Chesf assisted relocated people and production in the irrigated areas in use, and bore the costs to operate the irrigation infrastructure and to provide technical assistance and rural extension to irrigation users. In addition, it paid the Verba de Manutenção Temporária – VMT (Temporary Maintenance Allowance) to relocated people whose irrigated lot was not ready for production yet. Chesf supported the municipalities where the irrigated areas are located to enable them to provide the public health and road maintenance services to the population relocated in the agricultural settlements of those perimeters. Negotiations with Companhia de Desenvolvimento dos Vales do São Francisco e do Parnaíba - Codevasf were concluded to establish obligations of each of the parties and thus enter into a new agreement whereby the assets represented by the common use infrastructure of the perimeters will be transferred to Codevasf during the term of the agreement. In addition to the gradual reduction of operating costs, water will be used more efficiently and therefore the risk of overexploitation and overirrigation of the plots of land is decreased.

### **SOCIO-ENVIRONMENTAL INFORMATION**

The main social indicators representing Chesf social and corporate responsibility towards its co-workers and the community where it operates, are presented as follows:

## SOCIO-ENVIRONMENTAL INFORMATION

(Expresses in thousands of Reais)

1 - Wealth generation and distribution		In 2006: 2.686.020			In 2005: 2.975.427		
					Reclassified		
Value-Added Distribution The DVA - Value-Added Statement is fully disclosed jointly with the Financial Statements.		41,8% government 17,0% shareholders		13,9% employees 27,3% financiers	40,6% government employees 22,1 % financiers		12,2% 25,1% shareholders
2 - HUMAN RESOURCES		In 2006:			In 2005:		
2.1 - Compensation					Reclassified		
Payroll - Gross (FPB)		437.595			389.821		
- Employees		435.015			387.474		
- Management		2.580			2.347		
Relationship between the highest and the lowest compensation:							
- Employees		24,4			24,2		
- Management		1,0			1,0		
2.2 - Benefits Granted		Amount (000)	% Payroll	% on NI	Amount (000)	% Payroll	% on NI
Payroll taxes		94.039	21,5%	2,9%	84.819	21,8%	2,4%
Meals		30.442	7,0%	0,9%	28.052	7,2%	0,8%
Transportation		682	0,2%	0,0%	654	0,2%	0,0%
Private pension funds		25.234	5,8%	0,8%	20.414	5,2%	0,6%
Health care		29.230	6,7%	0,9%	28.558	7,3%	0,8%
Labor security and medicine		2.240	0,5%	0,1%	2.146	0,6%	0,1%
Education		5.040	1,2%	0,2%	4.567	1,2%	0,1%
Culture		-	0,0%	0,0%	-	0,0%	0,0%
Professional development		6.984	1,6%	0,2%	6.674	1,7%	0,2%
Day-care and day-care allowance		1.569	0,4%	0,0%	539	0,1%	0,0%
Profit sharing		48.200	11,0%	1,5%	43.476	11,2%	1,2%
Total		243.660	55,7%	7,4%	219.899	56,4%	6,3%
2.3 - Personnel Composition							
Number of employees at year end		5.688			5.628		
Number of employees hired		202			237		
Number of employees dismissed		142			234		
Number of trainees at year end		282			17		
Number of employees with special needs at year end		43			39		
Number of service providers on an outsourcing basis at year end		-			-		
Number of employees by gender:							
- Men		4.523			4.495		
- Women		1.165			1.133		
Number of employees by age:							
- Below 18 years of age		-			-		
- From 18 to 35 years of age		1.000			980		
- From 36 to 60 years of age		4.458			4.468		
- Above 60 years of age		230			180		
Number of employees by level of schooling :							
- Illiterate		21			21		
- Basic schooling		931			1.286		
- Intermediate schooling		437			858		
- Technical schooling		2.196			2.045		
- Superior schooling		1.754			1.247		
- Post-graduates		173			171		
Percent distribution of people in chief positions, by gender:							
- Men		86,7%			87,3%		
- Women		13,3%			12,7%		
2.4 - Labor contingencies and obligations:							
Number of labor actions filed against the entity		1.209			1.252		
Number of labor actions deemed valid		158			225		
Number of labor actions deemed unfounded		396			256		
Justice		10.723			1.050		
3 - Interaction between the Entity and the External Environment		Amount (000)	% on OI	% on NI	Amount (000)	% on OI	% on NI
3.1 - Relations with the Community							
Total investment in:							
Education		1.509	0,2%	0,0%	2.311	0,3%	0,1%
Culture		21.292	2,6%	0,6%	15.401	1,7%	0,4%
Health care and infrastructure		7.632	0,9%	0,2%	283	0,0%	0,0%
Sports and leisure		2.485	0,3%	0,1%	1.995	0,2%	0,1%
Meals		613	0,1%	0,0%	1.360	0,1%	0,0%
Employment and income generation		2.138	0,3%	0,1%	2.541	0,3%	0,1%
Relocation of families		148.787	18,3%	4,5%	100.755	10,9%	2,9%
Total investments		184.456	22,7%	5,6%	124.646	13,5%	3,6%
Taxes (payroll taxes excluded)		431.761	53,1%	13,1%	658.100	71,4%	18,8%
Financial compensagion for water use		206.552	25,4%	6,3%	175.566	19,0%	5,0%
Total - Relations with the Community		822.769	101,3%	24,9%	958.312	103,9%	27,4%
3.2 - Interaction with Suppliers		Required controls on :					
Social responsibility criteria used for selecting suppliers		Environmental risks, environmental work conditions, medical control on environmental health, work-by-night or unhealthful work practice by people under 18 years of age.					

4 - Interaction with the Environment	In 2006			In 2005		
	Amount (000)	% on OI	% on NR	Amount (000)	% on OI	% on NR
Investments in and maintenance expenses arising from operational processes for environmental improvement	5.931	0,7%	0,2%	5.730	0,6%	0,2%
Investments and expenses on preservation and/or recovery of degraded environments	1.825	0,2%	0,1%	972	0,1%	0,0%
Investments in expenses on environmental education of employees, outsourced personnel, autonomous employees and the entity's management	53	0,0%	0,0%	74	0,0%	0,0%
Investments in and expenses on environmental education of the community	1.368	0,2%	0,0%	1.707	0,2%	0,0%
Investments in and expenses on other environmental projects	-	0,0%	0,0%	-	0,0%	0,0%
Quantity of environmental, administrative and legal processes filed against the entity	7	0,0%	0,0%	6	0,0%	0,0%
Fines and indemnities relating to environmental issues, determined at administrative level and/or in court.	-	0,0%	0,0%	-	0,0%	0,0%
Environmental obligations and contingencies	-	0,0%	0,0%	-	0,0%	0,0%
<b>Total Interaction with the environment</b>	<b>9.184</b>	<b>1,1%</b>	<b>0,3%</b>	<b>8.489</b>	<b>0,9%</b>	<b>0,2%</b>
<b>5 - Additional information</b>	<b>2006</b>			<b>2005</b>		
Net Revenue (NR)	3.418.213			3.298.910		
Operating Income (OI)	391.539			812.484		

Recife, March 13, 2007

The Board of Directors

## BALANCE SHEET AS OF DECEMBER 31,

(In thousands of Reais)

	2006	2005 (Reclassified)
<b>ASSETS</b>		
<b>CURRENT ASSETS</b>		
Cash and cash equivalents	34,510	11,897
Money market investments – note 5	134,355	148,747
Consumers, concessionaires and permit grantees – note 6	882,495	875,718
Taxes and contributions to compensate – note 8	57,140	25,392
Advances to employees	5,629	12,074
Stocks	67,362	69,157
Tax credits – note 9	14,705	14,371
Advances to suppliers	3,636	4,287
Collateral security and linked deposits	3,923	4,480
Global Reversal Reserve	11,727	3,689
Others – note 10	106,020	103,829
	<b>1,321,502</b>	<b>1,273,641</b>
<b>NONCURRENT</b>		
<b>Long Term Receivables</b>		
Consumers, concessionaires and permit grantees – note 6	349,209	507,063
(-) Allowance for doubtful accounts	(108,962)	-
Transferred financing	2,036	4,895
Tax credits – note 9	191,990	174,630
Others	11,506	10,104
	<b>445,779</b>	<b>696,692</b>
<b>Investments – note 11</b>	<b>115,427</b>	<b>95,906</b>
<b>Property, plant and equipment – note 12</b>	<b>16,238,516</b>	<b>16,217,608</b>
<b>Intangible assets – note 13</b>	<b>117,622</b>	<b>111,020</b>
<b>Deferred charges</b>	<b>464</b>	<b>651</b>
<b>TOTAL ASSETS</b>	<b>18,239,310</b>	<b>18,395,518</b>

The accompanying notes are an integral part of these financial statements



## BALANCE SHEET AS OF DECEMBER 31

(In thousands of Reais)

### LIABILITIES

#### CURRENT LIABILITIES

	2006	2005 (Reclassified)
Suppliers – note 14	204,392	235,844
Payroll	6,878	5,079
Taxes and social contributions – note 15	70,993	57,823
Loans and financing – note 17	619,215	595,356
Charges on debts – note 17	54,265	108,814
Profit sharing – note 26	48,200	43,478
Stockholders' compensation – note 27	204,197	315,687
Estimated liabilities	55,910	50,285
Private pension plan entity – note 19	158,458	198,571
Research and development	118,571	-
Others – note 18	108,254	95,997
	<b>1,649,333</b>	<b>1,706,934</b>

#### NONCURRENT LIABILITIES

Suppliers – note 14	2,611	15,950
Taxes and social contributions – note 15	63,891	58,121
Loans and financing – note 17	4,256,636	4,496,744
Private pension plan entity – note 19	474,480	569,927
Provisions for contingencies – note 20	305,434	296,320
Others	33,551	15,498
	<b>5,136,603</b>	<b>5,452,560</b>

#### STOCKHOLDERS' EQUITY

Capital – note 21	1,696,306	1,278,585
Capital reserves – note 21	7,416,199	7,416,199
Profit reserves – note 21	2,046,473	2,246,844
	<b>11,158,978</b>	<b>10,941,628</b>
Funds for capital increase	294,396	294,396
	<b>11,453,374</b>	<b>11,236,024</b>
<b>TOTAL LIABILITIES</b>	<b>18,239,310</b>	<b>18,395,518</b>

The accompanying notes are an integral part of these financial statements

## STATEMENT OF OPERATIONS FOR THE YEARS ENDED DECEMBER 31 (In thousands of Reais)

	2006	2005 (Reclassified)
<b>OPERATING REVENUE</b>		
Electric power supply – note 22	589,205	664,702
Electric power bulk supply – note 22	2,258,227	2,294,733
Transmission system availability – note 22	1,094,172	976,122
Others operating revenues	8,176	14,021
	<b>3,949,780</b>	<b>3,949,578</b>
<b>Deductions from operating revenue</b>		
Global Reversal Reserve – RGR	(99,825)	(101,732)
ICMS on electric power (Added value tax)	(74,210)	(75,511)
Charge on emergency capacity	-	(47,825)
Fuel Consumption Account – CCC	(113,059)	(100,919)
Energy Development Account – CDE	(16,333)	(14,703)
PROINFA	(12,638)	(2,412)
PASEP (Civil servants savings program)	(40,392)	(60,458)
COFINS (Contribution for social security financing)	(175,110)	(247,108)
	<b>(531,567)</b>	<b>(650,668)</b>
<b>Net operating revenue</b>	<b>3,418,213</b>	<b>3,298,910</b>
<b>COST OF ELECTRIC POWER SERVICE</b> – note 24		
<b>Cost with electric power</b>		
Electric power purchased for resale – note 23	(1,490)	(88,532)
Charges on the use of electric power network	(575,476)	(367,334)
<b>Operating cost</b>		
Personnel	(134,216)	(123,009)
Material	(8,037)	(9,000)
Fuel for production of electric power	(3,173)	(10,504)
Third-party services	(38,697)	(54,354)
Financial compensation for the water use	(206,552)	(175,566)
Depreciation and amortization	(527,327)	(514,989)
Research and development	(152,172)	(14,830)
Others	12,847	(33,719)
	<b>(1,634,293)</b>	<b>(1,391,837)</b>
<b>COST OF SERVICE RENDERED TO THIRD PARTIES</b> – note 24	<b>(5,711)</b>	<b>(632)</b>
<b>GROSS OPERATING PROFIT</b>	<b>1,778,209</b>	<b>1,906,441</b>
<b>OPERATING EXPENSES</b> – note 24	<b>(583,884)</b>	<b>(457,016)</b>
<b>SERVICE RESULT</b>	<b>1,194,325</b>	<b>1,449,425</b>
<b>FINANCIAL REVENUE (EXPENSE)</b>		
Revenue from temporary cash investments	22,243	21,774
Monetary variation and additions – electric power sold	131,172	228,455
Other monetary variations – assets	14,827	5,345
Other financial revenues	4,346	(9,947)
Pis/Pasep and Cofins	(23)	(16)
Debt charges	(614,466)	(673,817)
Monetary variations on loans and financing	(2,716)	109,347
Other monetary variations – liabilities	(49,903)	(78,253)
Other financial expenses	(68,266)	(9,829)
	<b>(562,786)</b>	<b>(406,941)</b>
<b>Operating result before interest on equity</b>	<b>631,539</b>	<b>1,042,484</b>
Interest on equity capital – note 27	(240,000)	(230,000)
<b>OPERATING RESULT</b>	<b>391,539</b>	<b>812,484</b>
Non-operating revenues	2,328	2,214
Non-operating expenses	(8,176)	(9,506)
<b>Non-operating income</b>	<b>(5,848)</b>	<b>(7,292)</b>
<b>Profit before social contribution and income tax</b>	<b>385,691</b>	<b>805,192</b>
Social contribution – note 25	(32,798)	(54,808)
Income tax – note 25	(87,666)	(192,463)
<b>Profit before sharing and reversal of interest on equity capital</b>	<b>265,227</b>	<b>557,921</b>
Profit sharing – note 26	(47,877)	(41,516)
Reversal of interest on capital	240,000	230,000
<b>NET INCOME FOR THE YEAR</b>	<b>457,350</b>	<b>746,405</b>
Net income per share (R\$)	10,97	17,90

The accompanying notes are an integral part of these financial statements

## STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY

(In thousands of Reais)

	REALIZED SUBSCRIBED CAPITAL	CAPITAL RESERVES	PROFIT RESERVES	RETAINED EARNINGS	SUBTOTAL	FUNDS FOR CAPITAL INCREASE	TOTAL
<b>AT DECEMBER 31, 2004</b>	<b>1,278,585</b>	<b>7,416,199</b>	<b>1,850,439</b>	<b>-</b>	<b>10,545,223</b>	<b>294,396</b>	<b>10,839,619</b>
Realization of profit reserves	-	-	(22,312)	22,312	-	-	-
Net income for the year	-	-	-	746,405	746,405	-	<b>746,405</b>
Appropriations:							
Legal reserve	-	-	37,320	(37,320)	-	-	-
Interest on equity capital	-	-	-	(230,000)	(230,000)	-	<b>(230,000)</b>
Proposed dividends	-	-	-	(120,000)	(120,000)	-	<b>(120,000)</b>
Retained profit reserve	-	-	381,397	(381,397)	-	-	-
<b>AT DECEMBER 31, 2005</b>	<b>1,278,585</b>	<b>7,416,199</b>	<b>2,246,844</b>	<b>-</b>	<b>10,941,628</b>	<b>294,396</b>	<b>11,236,024</b>
Capital increase with profit reserve	417,721	-	(417,721)	-	-	-	-
Realization of profit reserves	-	-	(22,118)	22,118	-	-	-
Net income for the year	-	-	-	457,350	457,350	-	<b>457,350</b>
Appropriations:							
Legal reserve	-	-	22,867	(22,867)	-	-	-
Interest on equity capital	-	-	-	(240,000)	(240,000)	-	<b>(240,000)</b>
Retained profit reserve (*)	-	-	216,601	(216,601)	-	-	-
<b>AT DECEMBER 31, 2006</b>	<b>1,696,306</b>	<b>7,416,199</b>	<b>2,046,473</b>	<b>-</b>	<b>11,158,978</b>	<b>294,396</b>	<b>11,453,374</b>

(\*) The amount of R\$ 216,601 thousand, allocated to the Retained profit reserve, corresponds to the unpaid portion of net income of the year, is part of the source of funds that comprise the capital investment budget of the Company.

The accompanying notes are an integral part of these financial statements

**STATEMENT OF CHANGES IN FINANCIAL POSITION**  
**YEARS ENDED DECEMBER 31**

(In thousands of Reais)

	2006	2005 (Reclassified)
<b>FINANCIAL RESOURCES WERE PROVIDE BY:</b>		
From operations		
Net income for the year	457,350	746,405
Expenses (revenues) not affecting net working capital:		
Depreciation and amortization	563,528	546,812
Long-term monetary and exchange variations (net)	(16,425)	(71,288)
Deferred income tax and social contribution	(27,727)	(6,425)
Regulatory asset (Pis/Pasep and Cofins) – note 7	-	18,895
Free energy – note 32	151,896	65,194
Others	12,362	18,400
	<b>1,140,984</b>	<b>1,317,993</b>
From third parties		
Financing obtained	231,102	1,806
Transfer form current to noncurrent:		
Private pension plan entity	81,732	62,922
Taxes and social contributions	5,770	5,476
Noncurrent assets (LTR)transferred to current assets:		
Financing to third parties – local currency	3,980	3,371
Tax credits	33,350	40,964
Notes receivable – consumers	32,950	76,856
Collateral securities and linked deposits	-	2,497
Others	580	22,679
Allowance for doubtful accounts	108,962	-
Consumer charges payable	305	2,561
Provisions for contingencies	9,114	9,907
Other payables – Fachesf	26,346	10,467
Others	1,941	1,884
	<b>536,132</b>	<b>241,390</b>
<b>TOTAL FUNDS PROVIDED</b>	<b>1,677,116</b>	<b>1,559,383</b>
<b>FINANCIAL RESOURCES WERE USED FOR:</b>		
In increase in noncurrent assets (LTR):		
Financing to third parties – local currency	1,123	2,580
Tax credits	22,982	25,937
Notes receivable – consumers	1,514	7,021
Prepaid expenses	7,003	13,606
Others	1,980	680
In investment		
In permanent equity	19,521	44,067
In acquisitions of property, plant and equipment and intangible assets	584,396	493,753
Noncurrent liabilities transferred to current liabilities:		
Loans and financing	473,470	530,617
Private pension plan entity	158,153	175,074
Tax debts	-	4,025
Suppliers	31,723	31,928
Other payables – Fachesf	5,259	5,856
Consumer charges payable	3,366	11,208
Finance charges and effects of inflation	21,164	24,371
Stockholders' compensation - note 27	240,000	350,000
<b>TOTAL FUNDS USED</b>	<b>1,571,654</b>	<b>1,720,723</b>
<b>Increase/Decrease in net working capital</b>	<b>105,462</b>	<b>(161,340)</b>
<b>Current assets</b>		
At beginning of year	1,273,641	1,234,231
At end of year	1,321,502	1,273,641
	<b>47,861</b>	<b>39,410</b>
<b>Current liabilities</b>		
At beginning of year	1,706,934	1,506,184
At end of year	1,649,333	1,706,934
	<b>(57,601)</b>	<b>200,750</b>
	<b>105,462</b>	<b>(161,340)</b>

The accompanying notes are an integral part of these financial statements

## STATEMENT OF CASH FLOW YEARS ENDED DECEMBER 31 (In thousands of Reais)

### Operating activities

#### Net income for the period

Expenses (revenues) not affecting cash:

Depreciation and amortization	563,528	546,812
Long-term monetary and exchange variations (net)	(16,425)	(71,288)
Write-offs of property, plant and equipment in use	12,038	16,643
Deferred income tax and social contribution	(27,727)	(6,425)
Regulatory asset (Pis/Pasep and Cofins) – note 7	-	18,895
Free energy – note 32	151,896	65,194
Other	324	1,757

#### Variation in current assets

Consumers, concessionaires and permit grantees	(6,777)	(106,259)
Stocks	1,795	(5,604)
Taxes and contributions to compensate	(31,667)	43,957
Advances to employees	6,445	13,675
Collateral security and linked deposits	557	17,087
Tax credits	(334)	805
Services in progress	559	(28,367)
Other operating assets	(10,218)	15,211

#### Variation in current liabilities

Suppliers	(31,452)	16,588
Taxes and social contributions	13,170	(71,994)
Estimated obligations	5,625	7,484
Tax debts	(2,013)	(34,254)
Profit sharing	4,722	5,771
Consumer charges payable	147	(4,821)
Research and development	118,571	-
Other operating liabilities	15,922	(1,062)

#### Use of noncurrent assets

Securities	(38)	145,757
Notes receivable	31,436	69,835
Tax credits	(10,368)	15,027
Other	15,228	(5,964)

#### Increase in noncurrent liabilities

Provisions for contingencies	9,114	9,907
Consumer charges payable	305	2,561
Allowance for doubtful accounts	108,962	-
Other receivables – Fachesf	21,087	4,611

### Net cash provided by operating activities

#### Investing activities

Investments in property, plant and equipment and intangible assets	(584,396)	(493,753)
Permanent equity	(19,521)	(44,067)

#### Financing activities

Short-term loans and financing	-	230,000
Long-term loans and financing	231,102	1,806
Charges payable on loans and financing	566,208	618,762
Monetary variation on loans and financing	(454)	(21,884)
Payments of short-term installments of long-term loans and financing	(447,433)	(696,980)
Finance charges paid to stockholders and related parties	(385,865)	(439,109)
Finance charges paid to financial institutions and others	(257,780)	(98,571)
Stockholders' compensation	(340,603)	(216,286)
Private pension plan entity	(157,825)	(117,143)
Other	3,026	(15,005)

### TOTAL EFFECTS ON CASH BALANCE

Cash and cash equivalents, beginning of year	160,644	24,930
Cash and cash equivalents, end of year	168,865	160,644

### CASH VARIATION

2006	2005 (Reclassified)
457,350	746,405
563,528	546,812
(16,425)	(71,288)
12,038	16,643
(27,727)	(6,425)
-	18,895
151,896	65,194
324	1,757
<b>1,140,984</b>	<b>1,317,993</b>
(6,777)	(106,259)
1,795	(5,604)
(31,667)	43,957
6,445	13,675
557	17,087
(334)	805
559	(28,367)
(10,218)	15,211
<b>(39,640)</b>	<b>(49,495)</b>
(31,452)	16,588
13,170	(71,994)
5,625	7,484
(2,013)	(34,254)
4,722	5,771
147	(4,821)
118,571	-
15,922	(1,062)
<b>124,692</b>	<b>(82,288)</b>
(38)	145,757
31,436	69,835
(10,368)	15,027
15,228	(5,964)
<b>36,258</b>	<b>224,655</b>
9,114	9,907
305	2,561
108,962	-
21,087	4,611
<b>139,468</b>	<b>17,079</b>
<b>1,401,762</b>	<b>1,427,944</b>
(584,396)	(493,753)
(19,521)	(44,067)
<b>(603,917)</b>	<b>(537,820)</b>
-	230,000
231,102	1,806
566,208	618,762
(454)	(21,884)
(447,433)	(696,980)
(385,865)	(439,109)
(257,780)	(98,571)
(340,603)	(216,286)
(157,825)	(117,143)
3,026	(15,005)
<b>(789,624)</b>	<b>(754,410)</b>
<b>8,221</b>	<b>135,714</b>
160,644	24,930
168,865	160,644
<b>8,221</b>	<b>135,714</b>

The accompanying notes are an integral part of these financial statements

## VALUE-ADDED STATEMENT YEARS ENDED DECEMBER 31

(In thousands of Reais)

	2006	2005 (Reclassified)
<b>GENERATION OF ADDED VALUE</b>		
<b>Revenues</b>		
Electric power supply, transmission and others	3,949,780	3,949,578
Allowance for doubtful accounts	(108,962)	-
Non-operating income	(5,848)	(7,292)
	<b>3,834,970</b>	<b>3,942,286</b>
<b>(-) Input acquired from third parties</b>		
Material	28,272	29,527
Fuel for energy production	3,173	10,504
Third-party services	118,678	133,305
Electric power purchased for resale	1,490	88,532
Charges on the use of electric power network	575,476	367,334
Others	30,921	36,472
	<b>758,010</b>	<b>665,674</b>
<b>(=) Gross added value</b>	<b>3,076,960</b>	<b>3,276,612</b>
<b>(-) Retentions</b>		
Reintegration quotas (Depreciation and amortization)	<b>563,528</b>	<b>546,812</b>
<b>(=) Net added value</b>	<b>2,513,432</b>	<b>2,729,800</b>
<b>(+) Added value transferred</b>		
Financial income	<b>172,588</b>	<b>245,627</b>
<b>(=) Added value to be distributed</b>	<b>2,686,020</b>	<b>2,975,427</b>
<b>DISTRIBUTION OF ADDED VALUE</b>		
<b>Personnel:</b>		
Salaries/benefits/Severance pay fund (FGTS)	320,314	286,153
Profit sharing	47,877	41,516
Management fees	1,830	1,759
Provisions for labor contingencies/indemnities	(22,392)	13,727
Private pension plan entity – normal contributions	25,234	20,414
	<b>372,863</b>	<b>363,569</b>
<b>Governments:</b>		
Payroll charges	75,005	67,548
Taxes	431,761	658,100
Sector charges	616,882	481,606
	<b>1,123,648</b>	<b>1,207,254</b>
<b>Financing agents:</b>		
Finance charges, monetary variation and others		
Eletrobrás	510,491	482,946
Other financing agents	205,223	146,699
Rents	16,445	28,554
	<b>732,159</b>	<b>658,199</b>
<b>Stockholders:</b>		
Interest on equity capital	240,000	230,000
Dividends	-	120,000
	<b>240,000</b>	<b>350,000</b>
<b>Retained profit</b>	<b>217,350</b>	<b>396,405</b>
	<b>2,686,020</b>	<b>2,975,427</b>
<b>Average added value per employee</b>	<b>472</b>	<b>529</b>

The accompanying notes are an integral part of these financial statements

**NOTES TO THE FINANCIAL STATEMENTS**

**AS OF DECEMBER 31, 2005**

*(In thousands of Reais, unless otherwise stated)*

**1 - OPERATIONS**

Companhia Hidro Elétrica do São Francisco – Chesf, with central office at Rua Delmiro Gouveia, 333, Bairro do Bongi, CEP 50761-901, in the city of Recife, state of Pernambuco, is a listed mixed capital company, controlled by Eletrobrás. The Company was created through Decree-Law number 8.031/1945, and started its operations on March 15, 1948. Its key business activities are the generation and transmission of electric power. Its main market is located in the Northeast region of Brazil, where it serves directly the states of Bahia, Sergipe, Alagoas, Pernambuco, Paraíba, Rio Grande do Norte, Ceará, and Piauí, covering an area of more than 1.2 million square kilometers, equivalent to 14.3% of the Brazilian territory. As from 2002, with the gradual release of its supply contracts (initial contracts) at the rate of 25% per year, as established by Law 9.648, of May 27, 1998, the Company began to serve other Brazilian regions.

The Company's electric power is generated at 14 hydroelectric power plants and 1 thermoelectric power plant, for a total installed capacity of 10.618,328 MW. Power transmission takes place through a system comprised of 82 transmission substations, 15 step-up-substations and 18.260 kilometers of high voltage lines.

The electric power is sold through contracts entered into with distribution concessionaires, and also through power reserve contracts and electric power supply contracts, entered into with industrial consumers serviced directly by the Company; also through contracts in connection with electric power auctions promoted by the Electric Power Trading Chamber (CCEE) and through the electric power sale and purchase auctions, promoted by sellers or by free consumers. Any differences between generated electric power and sold under said agreements are commercialized on the spot market through CCEE, which is the successor of the Brazilian Wholesale Electric Power Market (MAE).

The Transmission Activity and the resulting RAP - Annual Revenue Permitted as determined by ANEEL - National Electric Power Agency - for an amount that is subject to annual reviews, is supported by the CPST - Transmission Services Contract and by the CCT - Transmission System Connection Contract, all connected to the Transmission Concession Contract. The latter provides for a periodical (every four years) review of the RAP, in order to ensure efficient and moderate tariffs.

As from March 1, 1999, the National Electric System Operator - ONS, a private civil rights and non-profit organization, whose operation was authorized by Resolution number 351/1998, issued by ANEEL, assumed the control and the operation of the National Interconnected System - SIN. In this context, the Company's power plants and transmission network are under the coordination, supervision and control of said entity.



## 2 - CONCESSIONS

The Company holds the following concessions:

Power plants	River	Installed Capacity (MW)	Capacity Used (MW average/year)	Concession Dates	Maturity Dates
<b>Hydroelectric</b>					
Paulo Afonso I	São Francisco	180,001	49,632	10/03/1945	10/02/2015
Paulo Afonso II	São Francisco	443,000	177,903	10/03/1945	10/02/2015
Paulo Afonso III	São Francisco	794,200	315,135	10/03/1945	10/02/2015
Paulo Afonso IV	São Francisco	2.462,400	1.467,713	10/03/1945	10/02/2015
Apolônio Sales (Moxotó)	São Francisco	400,000	130,958	10/03/1945	10/02/2015
Luiz Gonzaga (Itaparica)	São Francisco	1.479,600	1.004,303	10/03/1945	10/03/2015
Xingó	São Francisco	3.162,000	2.380,942	10/03/1945	10/02/2015
Piloto	São Francisco	2,000	-	02/16/1949	07/07/2015
Araras (*)	Acaraú	4,000	-	08/29/1958	07/07/2015
Funil	Das Contas	30,000	16,017	08/25/1961	07/07/2015
Pedra	Das Contas	20,007	7,276	08/25/1961	07/07/2015
Castelo Branco	Parnaíba	237,300	147,984	10/11/1965	10/10/2015
Sobradinho	São Francisco	1.050,300	546,651	02/10/1972	02/09/2022
Curemas	Piancó	3,520	1,316	11/26/1974	11/25/2024
<b>Thermoelectric</b>					
Camaçari	-	350,000	0,570	08/11/1977	08/10/2007

### TRANSMISSION SYSTEM

#### In use:

- 82 transmission substations, 15 elevator substations and 18.260 Km of high tension lines.

#### Under construction:

- Transmission line Milagres/Tauá (CE), in 230 kV, approximately 200 Km long.

- Transmission line Milagres / Coremas (CE), in 230 kV, approximately 120 Km long.

(\*) Transferred from DNOCS to Chesf as a donation.

Note: The used capacity corresponds to the average generation (in MW) for the period.

The maturity dates of these concessions are provided under the Generation Concession Contract number 006/2004-ANEEL, an excerpt of which was published in the Federal Government Official Gazette (the "D.O.U.") of November 22, 2004.

The plants' installed capacity is always higher than their production and considers:

- any periods, along the day and throughout the year, in which energy demand is either higher or lower in the system for which the plant or generation system is dimensioned.
- any periods in which equipment is shutdown for maintenance purposes, both preventive and corrective;
- the production of hydroelectric plants further relies on the availability of waters in the river where they are located. In periods of higher waters it may be possible to increase generation, as it may be reduced in periods of water scarcity, as it takes place in periods of energy rationing.



The production of the Chesf System's plants is connected with the Electro-Energy Operation Planning and Scheduling, with such horizons and breakdown that range from annual through daily and hourly scheduling; currently, the planning is prepared by the National Electrical Power Operator (ONS). ONS determines the generation amount and source that are required to meet the energy requirements of the country in an optimized way. It takes into account market requirements, water and equipment availability and the cost of generation and the feasibility of transmission of any such energy through a complex system that interconnects all regions.

### 3 – PRESENTATION OF THE FINANCIAL STATEMENTS

The financial statements are presented in accordance with the Brazilian Corporate Law (Law number 6404/76), the Brazilian Security Exchange Commission (CVM) standards and the National Electric Power Agency (ANEEL) regulations, in compliance with accounting practices.

For the purpose of comparison with this year, the Balance Sheet and the Statement of Income as of and for the previous year were reclassified as follows:

	2006	2005		
		Reclassified	Adjustment	Published
<b>Balance sheet</b>				
<b>Current assets</b>				
Taxes and contributions to compensate	57,140	25,392	(81)	25,473
Securities	-	-	(31)	31
Other	106,020	103,829	112	103,717
<b>Noncurrent</b>				
<b>Noncurrent assets</b>				
Linked deposits	-	-	(50,565)	50,565
<b>Property, plant and equipment</b>	16,238,516	16,217,608	(111,020)	16,328,628
<b>Intangible assets</b>	117,622	111,020	111,020	-
<b>Current liabilities</b>				
Tax debts	-	-	(2,013)	2,013
Provisions for contingencies	-	-	(93,907)	93,907
Other	108,254	95,997	2,013	93,984
<b>Noncurrent liabilities</b>				
Provisions for contingencies	305,434	296,320	43,342	252,978
<b>Statement of income</b>				
<b>Cost of Electric Power Service</b>				
<b>Cost of operations</b>				
Fuel Consumption Account - CCC	-	-	(5,911)	5,911
Energy Development Account – CDE	-	-	(958)	958
Research and Development	(152,172)	(14,830)	(14,830)	-
Others	12,847	(33,719)	21,699	(55,418)

### 4 - MAIN ACCOUNTING PRINCIPLES

#### a) Inflationary effects

- As provided by Law 9.249/1995, only the effects of monetary variations are reflected on indexed assets and liabilities, as contracted. The entries to headings such as permanent assets, stockholders' equity and concession liabilities are restated up to December 31, 1995 according to the monetary restatement method (recognition of the effects of inflation) then in force.

b) Current assets and noncurrent receivables

- Money market investments are recorded at cost plus the related earnings up to the balance sheet date;
- Securities are recorded at their acquisition cost plus yield up to the balance sheet date, where applicable, with a provision for adjustment to probable realizable value;
- Materials in stocks recorded as current assets are stated at their average acquisition costs; those for investment purposes are recorded in property, plant and equipment, at their acquisition cost;
- Deferred tax assets are recognized at the income tax and social contribution rates then ruling in connection with temporary differences and negative basis;
- Collateral Securities and linked deposits in connection with guarantees provided to suppliers are recorded at cost, plus yield as of the balance sheet date;
- Indexed assets are restated as of the balance sheet dates; other assets are recorded at cost, net of provision for losses.
- Permanent equity interest is recorded at acquisition cost, while those recorded before December 31, 1995 are recorded after monetarily restated up to that date.
- Property, plant and equipment are recorded at acquisition or construction cost, plus monetary restatement up to December 31, 1995; depreciation is calculated on the straight-line method. As from 1999, the Company adopted the depreciation rates set out in Resolution 44, of March 17, 1999, issued by ANEEL, ranging between 2% and 20% p.a. (see note 12).
- According to the Accounting Instruction 6.3.23 of the Accounting Manual for the Electric Power Public Utilities, the amount arising from liabilities in connection with concessions is stated as a deduction of Property, Plant and Equipment (see notes 12.a and 12.c).
- In compliance with the Accounting Instruction 6.3.10 of the Accounting Manual for the Electric Power Public Utilities, interest and other financial charges, as well as inflationary effects, in connection with third-party loans and financing that are used in works in progress are registered in this subgroup as cost (see note 12.c).

c) Current and noncurrent liabilities

- Stated at known or estimated amounts, plus, when applicable, the respective finance charges and monetary variations incurred through the balance sheet date;
- The costs of the pension plan held at Fundação Chesf de Assistência e Seguridade Social – Fachesf, are recognized as contributions are incurred. Actuarial liabilities and the costs and expenses arising from them are recorded according to CVM Resolution nr. 371/2000.

d) Stockholders' equity

- Unrealized income arising from monetary restatement credit balance are appropriated to a reserve up to 1995 and reversed to retained earnings ratably to write-offs, depreciation and amortization of permanent and intangible assets;
- Funds intended for capital increase are stated as such, providing that they are irreversible.

e) Results of operations

- Income is determined on the accrual basis, taking into account the tax credits arisen and realized in the period;
- The statement of operations accounts are recorded in accordance with the Accounting Manual for the Electric Power Public Utilities, as approved by the ANEEL Resolution 444 of October 26, 2001, and provides for segregation of revenues and expenses arising from generation and transmission activities, thereby allowing the calculation of each segment's book income;
- In compliance with Generally Accepted Accounting Principles, the exchange rate variations are fully recognized in the result for the period.

f) Statements of cash flow (DFC) and Value-Added Statement (DVA)

The Company has been publishing these statements in accordance with provisions set forth in the Accounting Manual for Electric Power Public Service and with Federal Accounting Council Resolution nr. 1.010/2005, in case of DVA.

**5 - INVESTMENTS IN THE MONEY MARKET AND SECURITIES**

Financial Institution	Type of investment	Maturity	Yield	2006	2005
<b><u>Money market investments</u></b>					
BB-DTVM	Extra Fund - Market	-	101% of certificates of interbank deposit rate	<b>134,355</b>	<b>148,747</b>
<b><u>Securities</u></b>					
Minority interest	Shares	-	Interest on equity capital/Dividends	42	42
	Allowance for losses			(12)	(11)
				<b>30</b>	<b>31</b>
National treasury	National treasury notes P series	07/09/2012	TR + 6% p.a.	300	285
	National treasury notes P series	07/09/2014	TR + 6% p.a.	142	134
	National treasury notes P series	12/28/2015	TR + 6% p.a.	261	246
				<b>703</b>	<b>665</b>
<b>TOTAL</b>				<b>733</b>	<b>696</b>
<b>Short-term</b>				<b>30</b>	<b>31</b>
<b>Long-term</b>				<b>703</b>	<b>665</b>

- Investments in the money market

Under this heading are short-term investments in Banco do Brasil Distribuidora de Títulos e Valores Mobiliários S.A. – BB-DTVM, under the specific legislation applicable to state-owned companies (Decree-Law 1.290 of 12/03/1973) as amended by the BACEN Resolution 3.284 of 25/05/2005, which established new mechanisms for investments by public companies and mixed-economy companies under Federal Indirect Administration.

- Securities

Common and preferred shares basically represent minority interest in the Telecommunications Sector; their value being adjusted to their probable realizable value and recorded as current assets:

Treasury Notes – P Series refer to sale of shares representing minority interest, deposited with the National Privatization Fund (the “FND”), pursuant to Decree 1.068/1994, and are stated in noncurrent assets.

## 6 - CONSUMERS, CONCESSIONAIRES AND PERMIT GRANTEES

Credits receivable from energy sales and availability of the transmission system, in the short- and the long-term can be summarized as follows:

	Falling due	Overdue			Total	
		In up to 90 days	For over 90 days	Total	2006	2005
Industrial consumers:						
Energy sales – Contracts	49,359	7,594	74,579 738	82,173	131,532	136,069
Extraordinary Tariff Recomposition (*)	67,921	-	-	-	67,921	87,531
Concessionaires:						
Energy sale – Contracts	397,807	2,864	7,889	10,753	408,560	458,238
Trading at CCEE	1,034	-	-	-	1,034	12,583
Free energy – Reimbursement	503,664	-	-	-	503,644	577,464
Connection to the transmission system	4,425	488	3,136	3,624	8,049	5,836
Transmission system availability	108,099	948	1,897	2,845	110,944	99,140
Regulatory Assets – Pis/Pasep and Cofins	-	-	-	-	-	5,920
	<b>1,132,309</b>	<b>11,894</b>	<b>87,501</b>	<b>99,395</b>	<b>1,231,704</b>	<b>1,382,781</b>
<b>Current</b>					<b>882,495</b>	<b>875,718</b>
<b>Noncurrent</b>					<b>349,209</b>	<b>507,063</b>

(\*) See note 32

• **RENEGOTIATED RECEIVABLES**

The following balances of receivables are being renegotiated:

<b>Debtor</b>	<b>2006</b>			<b>2005</b>
	<b>Current</b>	<b>Noncurrent</b>	<b>Total</b>	<b>Total</b>
Libra S.A.	4,407	-	<b>4,407</b>	<b>3,341</b>
Rio Doce Manganês S.A.	66,649	-	<b>66,649</b>	<b>72,391</b>
Cepisa	111,012	9,781	<b>120,793</b>	<b>132,387</b>
Celpe	2,615	-	<b>2,615</b>	-
Coelba	2,981	-	<b>2,981</b>	-
Cosern	1,346	-	<b>1,346</b>	-
<b>Total</b>	<b>189,010</b>	<b>9,781</b>	<b>198,791</b>	<b>208,119</b>

The receivables highlighted above, originated from electric power contracts, were renegotiated as follows:

- **Libra S.A.** – An acknowledgement of indebtedness statement was signed by Chesf and Ligas do Brasil S.A. – Libra dated September 1, 2004 in the amount of R\$ 3,423 thousand, repayable in 36 monthly installments from September 25, 2004 and bearing interest at the Central Bank Overnight (SELIC) rate plus 1% per month.
- **Rio Doce Manganês S.A.** – Private Instrument for Obligation Recognition and Payment Agreement signed between Chesf and SIBRA, currently Rio Doce Manganês S.A., dated June 30, 1995, in the amount of R\$ 21,915 thousand, repayable in 120 monthly installments from March 30, 1997 and bearing interest at the General Market Price Index (IGP-M) rate plus 6% per year.
- **Cepisa:**
  - a) An acknowledgement of indebtedness statement was signed by Chesf and Cepisa, dated December 19, 2003, in the amount of R\$ 80,083 thousand, repayable in 56 months from February 2004 based on a collection percentage bearing interest at the General Market Price Index (IGP-M) rate plus 1% per month;
  - b) Acknowledgement and payment of indebtedness statement No.016/2004 dated August 16, 2004, in the amount of R\$ 50,047 thousand, repayable in 36 monthly installments from June 25, 2005 and bearing interest at the General Market Price Index (IGP-M) rate plus 1% p.m.. 26 installments remain to be paid;
  - c) Acknowledgement and payment of indebtedness statement No. 018/2004 dated October 7, 2004, in the amount of R\$ 8,637 thousand, repayable in 36 monthly installments from June 25, 2005 and bearing interest at the General Market Price Index (IGP-M) rate plus 1% p.m.. 26 installments remain to be paid.
- **Celpe/Coelba/Cosern** – Statement of transactions and other covenants signed by Chesf and Celpe, Coelba and Cosern dated April 20, 2006, in the amounts of R\$ 7,773 thousand, R\$ 8,854 thousand and R\$ 4,002 thousand, respectively, repayable in 12 installments from May 15, 2006 and bearing interest at the General Market Price Index (IGP-M) rate plus 1% p.m. 10 installments remain to be paid.

## 7 - REGULATORY ASSETS – CONTRIBUTIONS TO PIS/PASEP AND COFINS

Due to the changes brought about by Laws 10.637/2002 and 10.833/2003, which increased the rates of the PIS/PASEP from 0.65% to 1.65%, and of the COFINS, from 3% to 7.6%, respectively, and considering the right to pass on to customers any increases in such rates, as provided under Law 8.987/1995 and the contracts signed by the Company, the PIS/PASEP and COFINS's Regulatory Assets were determined, corresponding to the differences not yet passed on to customers. This procedure is supported by Circular Letters 2.093/2004-SFF/SRT/ANEEL; 2.306/2004-SFF/ANEEL, 190/2005-SFF/ANEEL and 302/2005-SFF/ANEEL, dated, respectively, 12/3/2004, 12/24/2004, 2/1/2005 and 2/25/2005.

Through the Ratifying Resolution 149 of 06/30/2005 and the Publication 160/2005 SRT/ANEEL of 09/28/2005, aiming at counteracting the financial and economic impact of the increase in PIS/PASEP and COFINS rates, ANEEL approved part of these Regulatory Assets in the amount of R\$ 11,840 thousand, which began to be realized in July 2005, in twelve (12) monthly installments, through the billing of annual revenue allowed. The Company recorded the amount in current assets, and it was fully realized this year.

## 8 - TAXES AND CONTRIBUTIONS TO COMPENSATE

	2006	2005 (Reclassified)
<b>Current assets</b>		
Corporate income tax (IRPJ) / Social contribution (CSLL)	43,158	-
Pis/Pasep and Cofins	-	3,622
Finsocial	10,979	10,979
Other	3,003	10,791
<b>Total</b>	<b>57,140</b>	<b>25,392</b>

## 9 – TAX CREDITS

### ▪ Corporate Income Tax and Social Contribution

Pursuant to CVM Resolution 273 of 8/20/1998, the Company recognizes tax credits to be offset against future taxable income as its current assets and noncurrent assets. These credits, in the amount of R\$ 206,695 thousand, arise from temporary differences and negative social contribution basis, as detailed below:

	2006	2005 (Reclassified)
<b>Temporary differences</b>		
. DNAEE Administrative Act nr. 250/1985 - credit in 1994	104,409	109,876
. Provisions for contingencies	112,082	134,321
. Allowance for doubtful accounts	108,962	-
. Valuation allowance (securities)	12	11
. Other	14,337	13,658
	<b>339,802</b>	<b>257,866</b>
<b>Negative social contribution basis</b>	1,117,320	1,235,728
	<b>1,457,122</b>	<b>1,493,594</b>
<b>Tax credits</b>		
. Income tax on temporary differences	84,951	64,466
. Social contribution on temporary differences (provisions)	21,185	13,319
. Negative social contribution basis	100,559	111,216
	<b>206,695</b>	<b>189,001</b>
<b>Current</b>	<b>14,705</b>	<b>14,371</b>
<b>Noncurrent</b>	<b>191,990</b>	<b>174,630</b>

These tax effects consist of a 9% rate on social contribution and a 10% surtax over the 15% basic rate on the calculation basis to ascertain income tax payable, pursuant to Law 9.430, of 12/30/1996.

The amount of tax credits arising from Social Contribution (CSLL) negative basis totaled R\$ 10,657 thousand, this year. R\$ 100,559 thousand remains to be used: R\$ 13,064 thousand in current assets, and R\$ 87,495 thousand in long term receivables – against a negative tax basis of R\$ 1,117,320 thousand.

According to the Technical Study performed by the Management and reviewed on 12/31/2006, the estimates for the realization of said credit are:

	R\$ million				
	2007	2008	2009	2010	2011
Tax credits on CSLL negative basis	13.1	19.4	22.6	26.6	18.9

Other tax credits, in connection with temporary differences - provisions for contingencies, valuation allowance and provision for inflationary effects recorded under “Property, Plant and Equipment” - in the amount of R\$ 1,641 thousand and R\$ 104,495 thousand, in noncurrent assets, that will be realized in connection with the final court decision about lawsuits, with realization of marketable securities and property, plant and equipment, respectively.

These estimates are reviewed periodically to reflect any changes in the realization of any such values for financial statement purposes.

#### ▪ PIS/PASEP and COFINS

The STF – Supreme Court declared unconstitutional the section 1, art. 3 of Law 9.718/98, which increased the PIS/PASEP and COFINS bases of calculation, so that the sales concept was modified to cover all revenues earned by a company, irrespective of the type of activity performed and the accounting classification adopted. This provision had no legal supporting basis, having been the object of constitutional amendment subsequently.

Said decision benefits only the companies that filed the extraordinary appeals on which judgments have been passed.

The Company’s PIS/PASEP potential credits for the period from February 1999 through November 2002, and COFINS’s credits for the period from February 1999 through January 2004, which, adjusted through the end of this year, correspond respectively to R\$ 16,812 thousand and R\$ 116,302 thousand, totaling R\$ 133,114 thousand.

Based on the CTN – National Taxation Code, in June 2005 the Company filed an appeal to the Secretaria da Receita Federal (Federal Income Tax Authority), claiming for the recognition of its right to overpayment and refunding thereof. This overpayment was the result of unconstitutional increase in tax bases of calculation, on which there has been no pronouncement/judgment to the date of completion of these financial statements.

Considering the rejection of the appeal by the Federal Income Tax Authority, the Company filed lawsuits to recover these PIS/PASEP and COFINS credits. A favorable lower court decision on the PIS/PASEP case was obtained. The COFINS lawsuit awaits judgment.

## 10 – OTHER CURRENT ASSETS

	2006	2005 (Reclassified)
Financing to third-parties	3,143	3,189
Service in progress	81,268	81,827
Disposals in progress	1,913	2,879
Deactivations in progress	4,885	3,598
Lightpar	14,693	14,693
Lightpar (allowance for doubtful accounts)	(13,237)	(13,237)
Dividends receivable	3,193	-
Other	10,162	10,880
	<b>106,020</b>	<b>103,829</b>

## 11 - INVESTMENTS

### Composition:

	2006	2005
1. Permanent equity interest		
Affiliates		
• STN - Sistema de Transmissão Nordeste S.A.	97,020	93,100
• INTESA – Integração Transmissora de Energia S.A	15,600	-
Other equity interest	490	490
2. Other investments	2,316	2,316
<b>Total</b>	<b>115,427</b>	<b>95,906</b>

### Investment in STN

In line with the Federal Government policy of attracting private capital to enhance investments in the energy sector, and pursuant to Law 10.438/2002, the Consórcio AC Transmissão, formed by Chesf and Cia. Técnica de Engenharia Elétrica - Alusa, participated in auction 001/2003-ANEEL for concession of transmission lines; the Consórcio was the winner of Lot C, corresponding to a transmission line of 541 km, 500 kV, in the sections Teresina (state of Piauí), Sobral and Fortaleza (state of Ceará), with estimated annual revenues of R\$ 77.9 million.

For this purpose, the Company and Alusa organized the venture company STN – Sistema de Transmissão Nordeste S.A. - to build and operate the said transmission line; Alusa holds 51% of the equity interest of STN and Chesf holds 49%. The venture was completed in December 2005, and operations started in January 2006.

Still about this venture, Chesf was contracted by STN for the technical management of the works and for operation and maintenance of the transmission line. The Company received the total amount of R\$ 1,632 mil for the services rendered.



As of December 31, 2006, STN had total assets of R\$ 539,320 thousand and stockholders' equity of R\$ 218,918 thousand, obtaining net income of R\$ 27,433 thousand in the year and allocating R\$ 6,515 thousand to pay out dividends, and R\$ 3,192 thousand to the Company.

### Investment in INTESA

The Company formed one more energy transmission partnership acquiring a 12% stake in the capital stock of Integração Transmissora de Energia S.A – INTESA, which is engaged in building, implementing, operating and maintaining the Electric Power Transmission Public Service of the Interconnected Electric System's Basic Network, consisting of the 500-kv transmission line of Colinas/Serra da Mesa 2, 3<sup>rd</sup> circuit, related line entries and facilities, pursuant to Concession Agreement No. 002/2006-ANEEL, signed with the concession authority on April 27, 2006 through ANEEL for a period of 30 (thirty) years. INTESA has an authorized capital of R\$ 150 million in registered common shares, without par value, of which R\$ 15,600 thousand was subscribed and paid in by Chesf in the year. The other participants are Fundo de Investimentos em Participações Brasil Energia – FIP, with 48%, Eletronorte, with 37% and Engevix Engenharia S.A, with 3%. INTESA is expected to start operations on April 27, 2008.

## 12 – PROPERTY, PLANT AND EQUIPMENT

### a) Property, plant and equipment segregated by nature and activity

	2006	2005 (Reclassified)
In use	14,675,721	14,430,062
In progress	1,718,003	1,942,692
	<b>16,393,724</b>	<b>16,372,754</b>
Concession-related obligations	(155,208)	(155,146)
	<b>16,238,516</b>	<b>16,217,608</b>

		2006				2005 (Reclassified)
	Annual average depreciation rates (%)	Cost	Accumulated depreciation	(-) Concession-related obligations	Net amount	Net amount
<b>In use</b>						
Generation	2.47	16,919,707	(6,243,636)	(93,273)	10,582,798	10,540,778
Transmission	3.07	6,566,634	(2,954,095)	(25,795)	3,586,744	3,488,182
Management	5.10	803,293	(416,182)	(36,140)	350,971	245,956
		<b>24,289,634</b>	<b>(9,613,913)</b>	<b>(155,208)</b>	<b>14,520,513</b>	<b>14,274,916</b>
<b>In progress</b>						
Generation		225,602	-	-	225,602	370,227
Transmission		1,318,712	-	-	1,318,712	1,336,800
Management		173,689	-	-	173,689	235,665
		<b>1,718,003</b>	<b>-</b>	<b>-</b>	<b>1,718,003</b>	<b>1,942,692</b>
		<b>26,007,637</b>	<b>(9,613,913)</b>	<b>(155,208)</b>	<b>16,238,516</b>	<b>16,217,608</b>

## b) Annual depreciation rates

The depreciation quotas of each assets or facilities item are calculated and accounted for at rates established by ANEEL Resolution number 44, of 03/17/1999, taking as a basis the book balances shown in the respective UC – Reference File Units, as instructed by DNAEE Ordinance number 815 of 11/30/1994.

The main annual depreciation rates applicable to activities in general are as follows:

	Annual Depreciation Rates (%)
<b><u>Generation</u></b>	
Sluice gate	3.3
Reservoir	2.0
Control House	4.0
Generator	3.3
Panel – Control and Measurement	3.0
Hydraulic turbine	2.5
Overhead bridge, crane and gantry	3.3
Turbogenerator	4.0
<b><u>Transmission</u></b>	
Capacitors bench	5.0
Lathe bed	3.3
Key	4.0
Circuit breaker	4.0
Supporting structure	3.6
Access structure	4.0
LT structure	3.3
Control panel	3.6
Reactor	3.8
Ground-cabling system	3.3
Power transformer	3.3
Measure transformer	4.0
<b><u>Central Management</u></b>	
General equipment	10.0
Vehicles	20.0

## c) Finance charges and inflation effects

According to item 4 of Accounting Instruction 6.3.10 of the Accounting Manual for the Electric Power Public Utilities, and CVM Deliberation 193, of 7/11/1996, part of the financial charges and the effects of inflation were transferred to property, plant and equipment in progress, as shown below:

	2006			2005 (Reclassified)
	Generation	Transmission	Total	Total
Total financial charges	556,520	79,615	636,135	696,075
(-)Reclassification as property, plant and equipment in progress	(4,745)	(16,924)	(21,669)	(22,258)
<b>Net effect on income</b>	<b>551,775</b>	<b>62,691</b>	<b>614,466</b>	<b>673,817</b>
Total effects of inflation	(73)	1,880	1,807	(118,069)
(-)Reclassification of property, plant and equipment in progress	267	642	909	8,722
<b>Net effect on income</b>	<b>194</b>	<b>2,522</b>	<b>2,716</b>	<b>(109,347)</b>

#### d) Concession-related obligations

These represent amounts received from the Federal Government, states, municipalities and consumers, as well as donations not conditioned to return of any kind to the donor. The deadline to settle these liabilities is set out by the Regulatory Agency and will be due upon expiry of the Concession agreement.

As from January 1, 1996, these liabilities have ceased to be restated to reflect inflation, pursuant to legal provisions.

Composition:

	<b>2006</b>	<b>2005</b> (Reclassified)
Federal Government's participation	108,052	108,052
Amortization	20,269	20,269
Contributions from consumers	6,048	6,048
Donations and subventions for investments	20,839	20,777
	<b>155,208</b>	<b>155,146</b>

The Federal Government share relates to funds received from the federal government to be used in generation and transmission of electric power expansion.

The amortization balance arises from the "Reserve for Amortization" set up until 1971, under Federal Decree 41.019/1957; the funds were used, as of that year, in the expansion of the electric power utilities.

Contributions from consumers refer to funds used to perform the works that were necessary to meet the demand for energy supply connections.

Due to their nature, the accounts under this heading do not represent effective financial liabilities and therefore are not included as liabilities for the purpose of financial-economic index calculations.

According to Articles 63 and 64 of Federal Decree 41.019, of 2/26/1957, assets and facilities used in the production, transmission, distribution and sale, are tied to these services and cannot be retired, sold, assigned or subject to lien without the written consent of the Regulatory Agency. Resolution 20/1999 issued by ANEEL regulates the disentailment of assets from Public Electric Power Utilities, and provides a prior consent for the separation of assets that is not fit for the Concession, when put up for sale and determining that the sales product is deposited in a bank account for use at the Concession's sole discretion. In its operations, the Company has not identified assets of a significant value considered as unserviceable.

## 13 – INTANGIBLE ASSETS

- Intangible assets segregated by nature and activity

	2006	2005 (Reclassified)
<b>In use</b>		
Generation	297	-
Transmission	78,500	76,018
Management	94	95
	<b>78,891</b>	<b>76,113</b>
<b>In progress</b>		
Generation	155	382
Transmission	10,291	10,591
Management	28,285	23,934
	<b>38,731</b>	<b>34,907</b>
<b>Total</b>	<b>117,622</b>	<b>111,020</b>

## 14 - SUPPLIERS

Below, the “Suppliers” account composition:

	2006	2005
<b>Current</b>		
Materials and services	129,796	158,807
Electric power:		
Eletronorte	-	4,903
Furnas	-	5,374
Free energy refunding - note 32	8,338	20,436
Others	439	2,801
Charges on electric network use:		
Eletronorte	5,888	4,249
Eletrosul	5,306	3,833
Furnas	14,322	9,919
CTEEP	8,797	6,450
Cemig	3,194	2,544
TSN	2,706	2,051
Other	25,606	14,477
	<b>204,392</b>	<b>235,844</b>
<b>Noncurrent</b>		
Free energy refunding — note 32	2,611	15,950
<b>Total</b>	<b>207,003</b>	<b>251,794</b>

## 15 - TAXES AND SOCIAL CONTRIBUTIONS PAYABLE

Below, the Company's taxes and contributions payable as of 12/31/2006, which are recorded as current and noncurrent liabilities:

	2006		2005	
	Current	Noncurrent	Current	Noncurrent
COFINS	16,883	-	15,982	-
ICMS	10,214	-	8,922	-
Deferred ICMS	-	63,891	-	58,121
INSS*	8,407	-	9,500	-
PIS/PASEP	3,664	-	3,469	-
IRRF	17,230	-	6,051	-
FGTS	7,406	-	7,137	-
Other	7,189	-	6,762	-
	<b>70,993</b>	<b>63,891</b>	<b>57,823</b>	<b>58,121</b>

\* Social security contribution

## 16 – TAX DEBTS

The realization of deferred income tax and social contribution debts referring to regulatory asset (note 7) was completed this year, due to the realization of this asset.

## 17 – LOANS AND FINANCING

The main information about loans and financing denominated in foreign and local currencies is as follows:

a) Breakdown:

	Current		Noncurrent	Total	Total
	Principal	Charges	Principal	2006	2005
<b><u>Foreign currency</u></b>					
Eletrobrás	47,389	1,984	236,300	285,673	351,940
Financial institutions	48,634	829	97,269	146,732	192,125
	<b>96,023</b>	<b>2,813</b>	<b>333,569</b>	<b>432,405</b>	<b>544,065</b>
<b><u>Local currency</u></b>					
Eletrobrás	367,183	50,292	3,894,948	4,312,423	4,337,552
BNDES*	155,525	1,158	28,119	184,802	318,161
Other	484	2	-	486	1,136
	<b>523,192</b>	<b>51,452</b>	<b>3,923,067</b>	<b>4,497,711</b>	<b>4,656,849</b>
<b>Total</b>	<b>619,215</b>	<b>54,265</b>	<b>4,256,636</b>	<b>4,930,116</b>	<b>5,200,914</b>

\* National Bank for Economic and Social Development

- b) The above debt in foreign currency with financial institutions is guaranteed by the Federal Government's sureties. The BNDES loan is guaranteed by the proceeds of the Company's sales. For approximately R\$ 3.932.326 thousand in loans taken from Eletrobrás, no surety was required. However, at the discretion of the lender it may be claimed and the Company will have to provide it, under the risk of having the maturity dates anticipated.

The financing provided by the Parent Company (Eletrobrás) is funded by the Global Reversal Reserve (RGR) for the works at the Itaparica and the Xingó Hydroelectric power plants and their transmission systems as well.

- c) This year, the variation of the main indices used for restatement of loans and financing were as follows:

<u>Index</u>	<u>Annual variation (%)</u>	
	<u>2006</u>	<u>2005</u>
US\$	-8.65	11.82
Eur	1.85	-23.50
IGP-M*	3.83	1.21
SELIC**	15.08	19.05

\* General Market Price Index

\*\* Central Bank Overnight Rate

- d) Composition of loans and financing by currency and restatement index:

<u>Currency (equivalent in R\$)/Index</u>	<u>2006</u>		<u>2005</u>	
	<u>R\$ thousand</u>	<u>%</u>	<u>R\$ thousand</u>	<u>%</u>
<b><u>Foreign currency</u></b>				
US\$	285,673	5.79	351,940	6.77
Eur	146,732	2.98	192,125	3.69
	<b>432,405</b>	<b>8.77</b>	<b>544,065</b>	<b>10.46</b>
<b><u>Local currency</u></b>				
Not restated (*)	3,612,665	73.28	3,627,496	69.75
IGP-M	699,758	14.19	710,056	13.65
SELIC	184,802	3.75	318,161	6.12
Other	486	0.01	1,136	0.02
	<b>4,497,711</b>	<b>91.23</b>	<b>4,656,849</b>	<b>89.54</b>
<b>Total</b>	<b>4,930,116</b>	<b>100.00</b>	<b>5,200,914</b>	<b>100.00</b>

(\*) Of the total Eletrobrás loan, R\$ 3,612,665 thousand derives from the RGR – Global Reversal Reserve, collected by the Electric Sector and earmarked for reinvestment therein. Of this total amount, R\$ 3,577,029 thousand (99.01%) bears interest at 10% p.a. and administrative rate at 2% p.a.; whereas R\$ 30,434 thousand (0.84%) and R\$ 5,202 thousand (0.15%) bears interest at 5% p.a. and administrative rate at 2% and 1.5% p.a. These loans are not subject to monetary restatement, because the permanent assets' restatement method applicable to these loans, too, has been legally suspended.

e) The principal of long-term loans and financing, amount R\$ 4,256,636 thousand, matures as follows:

	Local currency	Foreign currency	2006	2005
2007	-	-	-	593,585
2008	398,185	94,057	492,242	498,453
2009	397,948	96,666	494,614	496,021
2010	409,220	44,906	454,126	422,560
2011	333,356	47,862	381,218	380,442
2012	367,927	50,078	418,005	417,298
2013	347,635	-	347,635	343,762
2014	383,697	-	383,697	379,735
After 2014	1,285,099	-	1,285,099	964,888
<b>Total</b>	<b>3,923,067</b>	<b>333,569</b>	<b>4,256,636</b>	<b>4,496,744</b>

f) Loans and financing are subject to the following interest rates:

	Domestic Market (% p.a.)	Foreign Market (% p.a.)
<u>Fixed rates</u>		
2006	5.00 to 10.00	-
2005	5.00 to 10.00	-
<u>Variable rates</u>		
2006	13.19	6.25 to 7.55
2005	18.05	4.55 to 7.55

g) Changes in Loans and Financing:

	Local currency		Foreign currency	
	Current	Noncurrent	Current	Noncurrent
<b>As of December 31, 2004</b>	<b>438,353</b>	<b>4,475,250</b>	<b>118,611</b>	<b>646,490</b>
Receipts	230,000	1,806	-	-
Charges	602,307	-	40,826	-
Monetary and exchange variation	196	8,407	(22,080)	(104,592)
Reclassifications	436,967	(436,967)	93,650	(93,650)
Payment of principal and charges	(1,099,470)	-	(135,190)	-
<b>As of December 31, 2005</b>	<b>608,353</b>	<b>4,048,496</b>	<b>95,817</b>	<b>448,248</b>
Receipts	-	231,102	-	-
Charges	551,979	-	35,393	-
Monetary and exchange variations	851	23,902	(1,305)	(21,642)
Reclassifications	380,433	(380,433)	93,037	(93,037)
Payment of principal and charges	(966,972)	-	(124,106)	-
<b>As of December 31, 2006</b>	<b>574,644</b>	<b>3,923,067</b>	<b>98,836</b>	<b>333,569</b>

## 18 - OTHER CURRENT LIABILITIES

	2006	2005 (Reclassified)
<b>Regulatory rates</b>		
Global reversal reserve - RGR	9,244	9,097
Financial compensation for water use	38,087	30,452
Fuel Consumption Account – CCC	19,674	15,345
ANEEL Inspection rates	1,359	1,396
Energetic Development Account – CDE	2,608	2,385
Emergency Capacity Charge	-	2,809
PROINFA	3,213	2,189
	<b>74,185</b>	<b>63,673</b>
<b>Others</b>		
Private pension entity – normal contribution	4,996	2,375
Other creditors – Fachesf	4,810	7,645
Codevasf agreement	4,000	4,000
Acquisition of properties – camping facilities	3,034	3,437
Others	17,229	14,867
	<b>34,069</b>	<b>32,324</b>
<b>Total</b>	<b>108,254</b>	<b>95,997</b>

## 19 – SOCIAL SECURITY PLAN AND OTHER BENEFITS TO EMPLOYEES

The Company sponsors the Fundação Chesf de Assistencia e Seguridade Social – Fachesf, a private not-for-profit entity, with the purpose of ensuring supplementary benefits to those provided by the Government-Sponsored Social Security.

Fachesf's actuarial model is one of capitalization and the Plan originally established is the Defined Benefit (BD Plan). On 06/29/2001, Defined Contribution Pension Plans (CD Plan) and Settled Benefit (BS Plan) were implemented, and Participants transference from the BD Plan to the new Plans, closed on 11/19/2001, reaching 97.1%.

Based on the actuarial evaluation results performed on the base date of 12/31/2006, the commitments assumed by the Company were reviewed and updated, and calculated per the CVM Deliberation 371/2000, reaching an actuarial liability in the amount of R\$ 632,938 thousand.

Since the accounting principles laid down in CVM Deliberation 371/2000 have been adopted, the plans jointly sponsored by the Company and Fachesf have accumulated losses, due to the difference between budgeted and actual figures – adjustments for deferrals permitted - which based on the independent actuarial report as of the base date 12/31/2006, added up to R\$ 165,017 thousand. Recognition of said losses, under items 53 and 54 of the above mentioned Deliberation, is being proceeded by the Participant's average service in the Plans, which, according to said actuarial report, will take place up to 8.4 years.

We emphasize that one of the main factors responsible for this increase in accumulated actuarial losses, that on 12/31/2005 totaled R\$ 106,456 thousand, was the change in actuarial figures budgeted for 2006. Among those changes is the general mortality table, changed for the AT83.

In the applicable legislation terms, the Complementary Social Security Secretariat – SPC, determines that contracts be drawn up between the sponsors and the Complementary Social Security entities, seeking full actuarial coverage for complementary benefit plans to that received from the Official Social Security. The contracted actuarial commitments with Fachesf until 12/31/2006 add up to R\$ 803,739 thousand.



As the balance of contracts signed with Fachesf in the amount of R\$ 803,739 thousand exceeded the amount of the actuarial liability calculated in accordance with the CVM Deliberation 371/2000, in order to adjust its accounting records to the net actuarial liability, in the amount of R\$ 632,938 thousand determined through the actuarial appraisal report issued on the base date of 12/31/2006, Chesf recorded the surplus of R\$ 170,801 thousand, as a reduction of the actuarial liability, under "Noncurrent liabilities" by way of deferral, as stipulated by the Deliberation. This portion is subject to annual reviews.

The following are detailed commitments related to Pension Plans, as described in the applicable paragraphs of item 81 of CVM Deliberation 371/2000, as of the base date 12/31/2006.

### Basic Characteristics of the Benefit Plan

On behalf of Chesf's employees, Fachesf administers 03 (three) Pension Plans: The Defined Benefit Plan, the Defined Contribution Pension Plan and the Settled Benefit Plan.

The Defined Benefit Plan guarantees to participants 100% benefit calculated based on the average of their last salaries.

The Defined Contribution Pension Plan is a plan in which the participants choose their level of contribution and the sponsor adds a variable percentage of the contribution chosen by the participants. The accumulation of these funds is what will determine the amount of the participant's benefit in the future. Chesf is responsible for the costs of the risk benefits and for managing the plan. This is the only plan open for enrollments.

The participants who chose to be transferred to the Defined Contribution Pension Plan had the option to maintain in the Settled Benefit Plan, the proportional amount, which they accumulated in the original plan, or transfer the present value of said benefits to the Defined Contribution Pension Plan.

#### 1. Accounting Policy Chosen by the Entity for Recognizing Actuarial Gains and Losses.

The amount of actuarial gains and losses recognized will correspond to the portion of gain or loss exceeding 10% of the Present Value of the Actuarial Obligation or 10% of the Fair Amount of the Plan's Assets, whichever is higher, amortized by the average future services of the plan's participants (Item 53 of the IBRACON Pronouncement on Accounting for Employee Benefits).

#### 2. Reconciliation of Assets and Liabilities Recognized in the Balance Sheet as of 12/31/2006

2.1. Present value of funded actuarial liabilities	2,999,667
2.2. Present value of unfunded actuarial liabilities (Plans without Financial Assets)	-
2.3. Present value of actuarial liabilities (2.1+2.2)	2,999,667
2.4. Fair value of the plan's assets	(2,201,712)
2.5. Present value of liabilities in excess of the fair value of assets (2.3 + 2.4)	797,955
2.6. Adjustments for deferrals permitted	
a) Actuarial (gains) or losses, not recognized	165,017
b) Cost of past service not recognized	-
c) Increase in (assets)/liabilities in adopting unrecognized pronouncement	-
d) Total (a + b + c)	165,017
2.7. Total actuarial liabilities / (Assets) to be provided for (2.5 – 2.6d) (*)	632,938

(\*) If asset, it will only be recognized by the sponsor if it reduces future contributions from the sponsor or could be reimbursed.

### 3. Deadlines for Recognition as from 31/12/2006 (in years)

3.1. Actuarial gains or losses, not recognized	8.4
3.2. Cost of past service not recognized	N/A
3.3. Increase in liabilities in adopting unrecognized pronouncement	N/A

### 4. Changes in Net Actuarial Liabilities (Assets)

4.1. Net Actuarial Liabilities /(Assets) at the beginning of the year	768,498
4.2. Expenses (revenues) recognized in previous year's statement of income	94,142
4.3. Sponsor's contributions during the year (*)	229,702
4.4. Impact of reduction on the benefit plan	-
4.5. Impact of early settlement on the benefit plan	-
4.6. Net Actuarial Liabilities /(Assets) at the end of the year (4.1 + 4.2 - 4.3 + 4.4 + 4.5)	632,938

(\*) In regard of CD Plan, consider only the values referring to risk benefits, and agreement amortization.

### 5. Reconciliation of Fair Value of the Plan's Assets

5.1. Fair value of the plan's assets at the beginning of the year	1,730,236
5.2. Benefits paid in the year	173,853
5.3. Participants' contributions paid in the year	21,060
5.4. Sponsor's contributions paid during the year	247,862
5.5. Actual income on assets in the year (5.6-(5.1-5.2+5.3+5.4))	376,407
5.6. Fair value of the plan's assets at the end of the year	2,201,712

### 6. Reconciliation of Present Value of Actuarial Liabilities

6.1. Amount of obligations at the beginning of the year	2,605,190
6.2. Gross costs of current service (with interest)	748
6.3. Regular Participants' and Sponsor's Contributions to Pension Plan	38,628
6.4. Interest on actuarial liabilities	311,155
6.5. Benefits paid in the year	173,853
6.6. Impact due to changes on actuarial budgeted figures	250,265
6.7. Obligations - (G)/P (6.7 - (6.1+6.2+6.3+6.4-6.5))	(32,466)
6.8. Amount of liabilities calculated at the end of the year	2,999,667

### 7. Calculations of (Gains) / Losses

7.1. Amount of (gain) / loss at the beginning of the year	106,456
7.2. Amortization in the year	-
7.3. (Gain) / loss on actuarial liabilities	217,799
7.4. (Gain) / loss on plan assets	(159,082)
7.5. (Gain) / loss on employees' contribution	(156)
7.6. Impact of reduction on the benefit plan	-
7.7. Impact of early settlement on the benefit plan	-

7.8. (Gain) / loss at the end of the year	165,017
7.9. Calculation of transition (10% equity or the obligation amount, whichever is higher)	299,967
7.10. Portion to be amortized (max 0; 7.8 -7.9)	34,141
7.11. Amortization (7.10 / 3.1)	3,342
<b>8. Expected Return on Assets for the Next Year</b>	
8.1. Fair value of the plan's assets as of 12/31/2006	2,201,712
8.2. Contributions expected from participants for the next year	2,201,712
8.3. Contributions expected from sponsor for the next year (*)	195,626
8.4. Expected benefits for the next year	190,312
8.5. Expected return on assets $(8.1 * \text{rate} + (8.2 + 8.3 - 8.4) * \text{rate}^{1/2})$	249,113
(*) In regard of CD Plan, consider only the values referring to risk benefits, and agreement amortization.	
<b>9. Interest on Actuarial Liabilities for the Next Year</b>	
9.1. Present value of actuarial liabilities as of 31/12/2006	2,999,667
9.2. Expected benefits for the next year	190,312
9.3. Interest on Actuarial Liabilities for the next year $(9.1 * \text{interest} - 9.2 * \text{interest}^{1/2})$	328,497
<b>10. Expenses (Revenues) to be Recognized in the Statement of Income for 2007</b>	
10.1. Current service costs (with interest)	791
10.2. Interest on Actuarial Liabilities	328,497
10.3. Expected Return on the Plan's Assets	249,113
10.4. Amortization costs	
a) Actuarial (gains) or losses, not recognized	3,342
b) Cost of past service not recognized	-
c) Increase of (asset)/liabilities in adopting unrecognized pronouncement	-
d) Total (a + b + c)	3,342
10.5. Total gross expenses (revenues) to be recognized $(10.1 + 10.2 - 10.3 + 10.4d)$	83,517
10.6. Contributions expected from participants for the next year	495
10.7. Total net expenses (revenues) to be recognized $(10.5 - 10.6)$	83,022
10.8. Expected administrative expenses for the next year	(A)
10.9. Total	83,022
(A) The total expense determined for the next year does not include administrative expenses forecast for the year, nor the contributions to CD Plan that must be recognized based on amounts actually paid	
<b>11. Summary of Registered Participants' Data (in R\$)</b>	
Active + Enrolled Participants	
Quantitative (*)	5,604
Average age (years)	46.3
Average length of service (years)	19.8
Average length of future service (years)	8.4
Average monthly salary/wages	3,938
Annual payroll (13x)	286,925,167
(*) All those participating in BS Plan participate in CD Plan, too.	
Participants awaiting benefits	
Quantitative	25
Average age (years)	49,7

Average monthly benefit	2,002
Participants assisted / Beneficiaries enjoying benefit	
Quantitative	7,321
Average age (years)	62.4
Average monthly benefit	1,804
Payroll benefits (13x)	171,691,080
Actual income in the year	268,921,324
Employee contribution	21,060,180
Sponsor's contribution	247,861,144
Actual expenses in the year	173,853,316

## 12. Actuarial Assumptions Adopted in Calculation

Nominal discount rate for actuarial liabilities	11.30%
Nominal yield rate expected on the plan's assets	11.30%
Estimated rate of nominal salary increase	6.79%
Estimated rate of nominal benefit increase	5.00%
Nominal growth rate of medical costs	N/A
Estimated long term inflation rate (basis for the determination of above rates)	5.00%

General mortality biometric table:	AT83 separated by sex
Biometric admittance for disability table	Mercer admittance for disability
Expected turnover rate	1% per year (Plans BD and BS) and 3.5% per year (Plan CD)

Likelihood of beginning retirement	100% on initial eligibility to a full plan benefit under the BD and BS Plans. Plan/CD Plan: 10% on eligibility to early Pension Plan, 3% between that date and eligibility to regular retirement, and 100% on eligibility to regular retirement date.
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## 13. Additional Information

- 1) The Plan's assets are set as of 12/31/2006.
- 2) Individually recorded asset data are set as of 09/30/2006 and were projected to 12/31/2006, while the Assisted and Beneficiaries' data are set as of 12/31/2006
- 3) The registered statistics presented consider the family group benefits as one benefit

## Additional Benefits

In addition to the benefits granted through the complementary social security plans, the Company offers advantages to its employees, such as: health care plan, meal allowance, transportation allowance and day-care assistance, which are periodically negotiated through a collective bargaining agreement. The expenses in connection therewith, during the year, amounted to R\$ 60,281 thousand (R\$ 47,275 thousand, in 2005).

## 20 – CONTINGENCIES

Contingencies	2006			2005
	Provision amount		(-) Judicial deposits	Net Provision
	In the year	Accumulated		
<b>Noncurrent liabilities</b>				<b>Net Provision (Reclassified)</b>
Labor	(23,851)	34,269	(34,192)	77
Civil	73.150	341.712	(36.552)	305.160
Tax	-	197	-	197
<b>Total</b>	<b>49,299</b>	<b>376,178</b>	<b>(70,744)</b>	<b>305,434</b>
				<b>296,320</b>

In compliance with the provisions of the Accounting Manual for Electric Power Public Utilities, approved by ANEEL Resolution 444, on 10/26/2001, Chesf adopts the procedure of classifying the intended cases against the Company due to the risk of loss, based on the opinion of its legal advisors, as follows:

- For legal actions for which a negative outcome for the company is considered **probable**, a provision is set up;
- For legal actions for which a negative outcome for the company is considered **possible**, the corresponding information is published in explanatory notes.
- For legal actions for which a negative outcome for the company is considered **remote**, only information deemed relevant for fully understanding of the financial statements is published in the explanatory notes.

Labor contingencies mostly refer to claims concerning risk, overtime, FGTS fine miscalculations due to the past economic recovery plans; and severance indemnities due by outsourced companies

More serious civil cases are compensation claims, expropriations, and those filed by suppliers.

Regarding taxes, there are minor legal disputes basically involving federal VAT (IPI) and import tax.

The Company, through the setup of pertinent escrow deposits when necessary, is properly handling all these contingencies.

I) The following actions, for which the risk of a negative outcome is **probable**, stand out:

- a) The Company filed a lawsuit claiming for partial invalidity of amendment (K Factor –Analytical Price Restatement) to the contract of civil work contracted for the Xingó Hydroelectric Power Plant, agreed on by the Consortium formed by Companhia Brasileira de Projetos e Obras – CBPO, CONSTRAIN S.A. – Construções e Comércio and Mendes Junior Engenharia S.A. and claiming the return of amounts paid - approximately R\$ 350 million.

The lawsuit was filed at Federal Justice, but a decision of the 5<sup>th</sup> Federal Regional Court established that lawsuit proceedings were moved Pernambuco's State Justice.

The Company's claim was deemed groundless. The counterclaim filed by the defendant was considered to have ground by the 12<sup>th</sup> Civil Court of the Judicial District of Recife, and the decision was maintained by the 2<sup>nd</sup> Civil Section of Pernambuco's Court of Justice, which led Chesf to enter a Motion to clarify certain issues of the Appeal, which were omitted from the decision of the 2<sup>nd</sup> Civil Chamber. Those motions were judged and rejected by the 2<sup>nd</sup> Civil Section. Chesf's lawyers then argued special and extraordinary appeals against the verdict of the 2<sup>nd</sup> Civil Section. On 03/31/2004 the special appeals filed by Chesf had been admitted by Pernambuco's Court of Justice and sent to the

Superior Court of Justice, while the extraordinary appeals also filed by Chesf, were not admitted. Against that negative, the Company entered the proper bills of review. On 06/31/2005, the referred appeals were sub judice at Higher Courts. After that date, and up to 03/31/2006, the bills of review filed by Chesf at the Federal Supreme Court were rejected. The Public Prosecutor Office passed an opinion on the special appeal filed by Chesf and by the Federal Government at the Supreme Court of Justice, declaring the annulment of the process due to the lack of jurisdiction of Pernambuco's State Justice to render a decision on the merits of the case, and ordering the reexamination of the merits by a court with proper jurisdiction. On 09/30/2006 the case was with the judge waiting for a decision.

In November 1998, the defendants requested temporary execution of anticipated custody, in the amount of R\$ 245 million, the case being suspended by determination of the 12th Civil Court Judge (PET 1621). This extension was the result of a Regimental Appeal by the Consortium, which was judged on 06/24/2002, unanimously maintaining the extension previously handed down by the STJ President, remaining, as such, discarded the possibility of obtaining by the Consortium, the advance protection.

Later, the defendants requested award calculation, in order to appraise the current amount of indemnity, in case all appeals by Chesf and Federal Government are rejected. On 09/30/2005, the expert work required by the judge in charge of the case was being done, for the purpose of determining the real amount involved. After the expert work was completed and the records sent to the judge, both parts requested clarifications, and reports are being examined again.

Based on the opinion of its legal advisers and on calculations that included the suspension of payment of the installments of K Factor, and its respective monetary restatements, the Management records a provision under noncurrent liabilities in the amount of R\$ 304,510 thousand, as of 12/31/2006. This provision is intended to cover possible losses resulting from this issue, and it corresponds to partial disallowance of K Factor between July 1990 and December 1993, in accordance to Law nr. 8,030/1990, and to full payment suspension of K Factor between January 1994 and January 1996, in accordance to the Company.

On 12/31/2006, the Special Appeal and the Bill of Review were waiting judgment at Superior Court of Justice and Federal Supreme Court, respectively.

The time required for this process to be completed cannot be foreseen.

- b) A lawsuit filed by the “Sindicato de Eletricitários da Bahia” (Bahia Electricity Sector Workers Union) is under way at the “Tribunal Regional do Trabalho do Estado da Bahia”(State of Bahia Regional Labor Court) claiming for payment of the salary difference due to employees from Paulo Afonso – BA, under the Amendment to the Decree Law 1971 – ADL and the Annuity on Risk Additional, to the “Gerência Regional de Paulo Afonso – GRP” (Regional Paulo Afonso Management), involving an estimated R\$ 21 million. The Company filed a bill of review under Review appeal with the TST – Superior Labor Court, which was sentenced unfounded. The lawsuit had a final judgment not subject to further appeal, after which the execution phase started, with the process now at the accounting department for settlement. Preliminary calculation established an approximate R\$ 1,500 thousand needed for settlement.
- c) An action was filed with the 8th Fortaleza Court by the SINDIELETRO - “Sindicato de Eletricitários do Ceará” (Ceará Electricity Sector Workers Union) claiming for refunding for losses borne by the “Gerência Regional Norte – GRN” (Northern Regional Management) (Ceará and Rio Grande do Norte) employees after interruption of the collective transportation services, involving an estimated R\$ 6 million. The request for resumption of the transportation services was partially accepted, and the Company obeyed the judicial order. The plaintiff claimed for supplementation of transportation and the condemnation of the Company to pay a daily fine, which the Company contested.



After a hearing on August 23, 2005, in which one of the parties and Chesf submitted their final arguments, the previous decision was modified, the resumption of transportation services being ordered only to the extent previously existing. Also in the same decision, the parameters for settlement of the sentence were defined, so that the labor credit was reduced to R\$ 1,344.2 thousand. The execution is under way at the Labor Justice of 1st Instance in Fortaleza, CE.

- d) Lawsuit filed at the 4<sup>th</sup> Labor Court of Recife – PE, by the “Sindicato dos Trabalhadores das Indústrias Urbanas do Estado de Pernambuco – Urbanitários” (Union of Industry Workers from Pernambuco) in the name of 460 employees transferred to Recife - PE, process nr. 01473-2005-004-06-00-0, requesting risk Premium on all wages and salaries, in the amount of R\$ 4,050 thousand. First instance judgment excluded about 300 of the transferred employees, due to pending lawsuits, and deemed the claim groundless. The Union filed regular appeal at the 6<sup>th</sup> Regional Labor Court.
- II) The following additional lawsuits filed against the Company involving *possible risk of loss* have not been provided for:

Contingencies	2006	2005
Labor	26,095	22,833
Civil and Tax	273,013	146,670
<b>Total</b>	<b>299,108</b>	<b>169,503</b>

- a) Among these, 2 (two) deserve special attention, the compensation lawsuits brought before the court by the Consortium formed by the following companies: CBPO/CONSTRAN/Mendes Junior, who claim for condemnation of the Company and payment of additional financial compensation, because of late payment on contract invoices relating to the Xingó Hydroelectric Power Plant. A petition dated 06/08/1999 refers to the invoices issued as of 04/30/1990 and the other, dated 05/31/2000, to the invoices issued up to that date. In these legal actions, the plaintiffs filed a generic request, limited to pointing out the existence of an alleged right to financial compensation, the calculation of the amounts involved being postponed to the date of settlement.

The Company contested the legal actions and requested that the Federal Government be admitted to the proceedings, which were sent to one of the courts in the Pernambuco Federal Justice. The Consortium presented a request mentioning the admission of the Federal Government in the proceedings.

In August 2005, after the results of the expert work and additional explanations, a hearing took place and the final arguments were scheduled to be presented on 10/17/2005. Currently, the processes are ready for dispatch and the final clearing and the sentence will follow.

- b) Also, a public civil action has been filed against Chesf by the “Associação Comunitária do Povoado do Cabeço e Adjacências” (Community Association of the Cabeço County and Surrounding Areas) in the state of Sergipe, involving R\$ 100 million, at the 2nd. Federal Court in Sergipe (process nr. 20028500002809-6), claiming for financial compensation for alleged material environmental damage caused to the fishermen from Cabeço, downstream UHE Xingo, all caused by the construction of this power plant.

The action was filed at the Federal Court, on 06/27/2002, and contested within the legal timeframe. After a series of events, which did not affect the process or the claims, on 08/31/2005 the judge in charge determined that IBAMA, IMA/AL, CRA/BA, the Federal Government and ADEMA/SE should be included as defendant in the action, while ordering that they be summoned.

On 09/30/2005 compliance with the summons was expected and on 09/30/2006 the records were completed for the Judge, after inclusion of the proxy of new Chesf's lawyers. As of 12/31/2006, the lawsuit was suspended by decision of the Judge and waits the judgment of the bill of review filed by the plaintiff at the 5<sup>th</sup> Federal Regional Court. Chesf's codefendants (Federal Government, IBAMA, IMA-AL, CRA-BA and ADEMA-SE) had already been mentioned.

According to its lawyers, an unfavorable outcome for the Company is *possible*, due to possible defense failure, but not concerning the amounts claimed for.

**III) Among legal actions for which a negative outcome for the Company is considered *remote* stands out:**

In spite of being deemed to involve a remote risk of loss, in the Company's legal counsel opinion, there is an ongoing case initiated by Mendes Junior, hired by the Company to build the Itaparica Hydroelectric Power Plant, for alleged financial losses due to late payment of invoices by the Company.

This collection action is based on the Declaratory Action judged valid for the purpose of declaring the existence of a Mendes Junior's credit against Chesf, thus ensuring financial refunding. To be entitled to financial refunding, in compliance with the decisions of the Pernambuco Justice Court, and the Supreme Court, Mendes Junior was expected to prove that it raised funds specifically for financing Itaparica works, due to Chesf's delay in paying some invoices and that these additional fund-raising expenses were higher than the arrears charges paid by Chesf.

As determined by the Federal Justice of the 12th Court's Section of Pernambuco, an expert accounting examination is under way, whereby, in reply to Chesf's inquiry, the expert declared that "it was impossible, based on an analysis of Mendes Junior's accounting records, to affirm that it raised funds in the money market in the periods of delay in payment of invoices, specifically for financing Itaparica works".

With the expert examination report on hand, the parties requested clarifications to the Expert, which have not been examined by the 12th Federal Court's Section Judge. The records were sent to the Federal Prosecution Office, which is completing its pronouncement on the matter for subsequent delivery to the Judge.

Given the cancellation of all deeds developed within the State Justice's sphere and the strict determinations of the Federal Judge regarding the new examination, requiring the complete identification of Mendes Junior's own or obtained resources, and proof of their actual use in the construction, it is not possible to estimate the litigation amount, not even as an expectation. If one considers that, thus far, the Expert has not been able to prove the existence of credit in favor of the plaintiff, even after having had access to the latter's accounting records and to those of the defendant, Chesf's legal counselors confirm the lawyer's opinion that currently the risk of loss is remote.

On 06/30/2005, the records of the process were completed for the Judge and ready for the notary public action, awaiting the pronouncement of the Public Prosecutor Office. On September 30, 2005, the expert had already handed over the Supplementary Appraisal Report, in reply to the parties' questions, but without adding anything new to the previous opinions. On 12/31/2005, the records were examined by the Public Prosecutor Office for issuance of their opinion. Between that date and 03/31/2006, the Public Prosecutor Office passed opinion for the annulment of the decision rendered at the declaratory action that recognized the credit relation of Mendes Júnior to Chesf, and for the groundlessness of the present lawsuit. On 03/31/2006 the case was with the judge waiting a decision.



On 09/30/2006, the issue waited for the scheduling of judgment to discuss the appraisal report from the expert. On 12/31/2006 the case was with the judge waiting a decision.

## 21 – STOCKHOLDERS’ EQUITY

### • Capital Social

Capital stock in the amount of R\$ 1,696,306 thousand, comprises shares without nominal value, thus distributed:

Shareholders	Number of shares in thousands					
	Common		Preferred		Total	%
	Qty.	%	Qty.	%		
Eletrobrás	40,478	100.000	1,002	81.351	41,480	99.449
Sudene	-	-	194	15.718	194	0.464
Finor	-	-	17	1.362	17	0.040
Others	-	-	19	1.569	19	0.047
	<b>40,478</b>	<b>100.000</b>	<b>1,232</b>	<b>100.000</b>	<b>41,710</b>	<b>100.000</b>

Common shares are nominative and entitled to vote. The preferred shares, also nominative, have no specific class nor are voting or convertible into common shares, although they take priority in dividend distribution at 10% p.a., as a minimum, calculated on capital corresponding to this class of share.

### • Capital reserves

	2006	2005
Premium on share issue	769,028	769,028
Donations/subventions for investments	4,759,353	4,759,353
Yield on assets and rights formed out of equity capital	1,691,475	1,691,475
Monetary restatement of property, plant and equipment	196,343	196,343
	<b>7,416,199</b>	<b>7,416,199</b>

### • Profit reserves

	2006	2005
Legal	232,583	209,715
Statutory	8,179	8,179
Unrealized profit	528,420	550,538
Retained profit	1,277,291	1,478,412
	<b>2,046,473</b>	<b>2,246,844</b>

The Legal Reserve is set up at 5% of the net income for the year, in accordance with corporate legislation and limited to 20% of the capital stock.

The Unrealized Profit Reserve, which is set up out of the credit balance of monetary restatement for years prior to 1995, is reversed to the retained earnings account, based on the realization of property, plant and equipment, and included in the stockholders’ compensation basis of calculation.

The Retained Profit Reserve, established by article 196 of Law nr. 6,404/1976 is composed of portions of the net income and is intended to compose the source of funds for use in the Company's investments. In the year, R\$ 216,601 thousand was appropriated to this reserve, based on the Company's capital budget, established by Law nr. 11,451/2007, of 02/07/2007, that defines investments of R\$ 802,643 thousand for 2007, with the following applications:

<b>Description</b>	<b>Budget Portion</b>
Maintenance of generation system	65,460
Studies for generation expansion in the Northeast area	12,806
Implementing of UTE Camaçari's combined cycle	797
<b>Total Generation</b>	<b>79,063</b>
UHE Itaparica relocation – Plots of land irrigation	102,250
<b>Total Itaparica</b>	<b>102,250</b>
Implementing of Northeast's transmission system	384,618
Expansion of Northeast's transmission system	144,685
<b>Total Transmission</b>	<b>529,303</b>
Infrastructure – Real state	9,975
Infrastructure - Equipment/Vehicles/Furniture	26,136
Infrastructure –	
Informatics/Telecommunication/Teleprocessing	55,916
<b>Total Infrastructure</b>	<b>92,027</b>
<b>Total General</b>	<b>802,643</b>

## 22 - ELECTRIC POWER SUPPLY/PROVISION AND THE TRANSMISSION SYSTEM AVAILABILITY

The Company's revenues arise substantially from the sale of electric power and availability of the Transmission System. These operations are backed by power sales and purchase contracts, by short-term transactions in the market, involving the Electric Power Commercialization Chamber – CCEE, and by contracts from the Transmission System.

This revenue is thus composed:

	<b>2006</b>			<b>2005</b>		
	<b>Number of clients</b>	<b>GWh</b>	<b>R\$ thousand</b>	<b>Number of clients</b>	<b>GWh</b>	<b>R\$ thousand</b>
Industrial supply	17	7,729	589,205	26	8,301	664,702
Energy provision (*)	53	39,175	2,258,227	51	41,610	2,294,733
Transmission system	154	-	1,094,172	134	-	976,122
<b>Total</b>		<b>46,904</b>	<b>3,941,604</b>		<b>49,911</b>	<b>3,935,557</b>

(\*) Including short-term operations (CCEE) worth R\$ 106,078 thousand (2005 - R\$ 27,891 thousand).

## 23 - ELECTRIC POWER PURCHASED FOR RESALE

In order to comply with sales agreements with its clients, the Company purchased electric power as follows:

Supplier	2006		2005	
	GWh	R\$ thousand	GWh	R\$ thousand
Eletronorte	-	-	703	41,086
Furnas	-	-	650	41,640
CCEE (short-term)	-	1,490	-	5,802
Others	-	-	-	4
<b>Total</b>		<b>1,490</b>		<b>88,532</b>

## 24 - OPERATING COSTS AND EXPENSES

The general and administrative costs and expenses shown in the income statement are thus composed:

Operating Costs and Expenses	2006			2005
	Operating costs	Operating expenses	Total	Total
Electric power purchased for resale	1,490	-	1,490	88,532
Charges on use of electric power network	575,476	-	575,476	367,334
Personnel	138,566	285,060	423,626	375,874
Material	8,127	20,145	28,272	29,527
Fuel for energy production	3,173	-	3,173	10,504
Third parties' services	39,740	78,938	118,678	133,305
Depreciation and amortization	527,327	36,201	563,528	546,812
Financial compensation for water use	206,552	-	206,552	175,566
Research and development	152,172	-	152,172	14,830
Leases and Rentals	4,920	11,526	16,446	28,554
Provisions for contingencies	-	(2,246)	(2,246)	43,151
Taxes	401	4,030	4,431	3,967
Allowance for doubtful accounts	-	108,962	108,962	-
Others	(17,940)	41,268	23,328	31,529
<b>Total</b>	<b>1,640,004</b>	<b>583,884</b>	<b>2,223,888</b>	<b>1,849,485</b>

## 25 - RECONCILIATION OF ACTUAL AND NOMINAL RATES OF PROVISIONS FOR INCOME TAX AND SOCIAL CONTRIBUTION

Below, the reconciliation of actual and nominal rates used in calculating provisions for income tax and social contribution:

	2006	
	Social Contribution	Income Tax
Income before tax and social contribution	385,691	385,691
Total income tax and social contribution burden calculated at 15% plus surtax and 9%, respectively.	34,712	96,399
Tax effects on permanent additions or exclusions	(1.914)	(8,733)
Income tax and social contribution for the year	<b>32,798</b>	<b>87,666</b>

## 26 – PROFIT SHARING

As a result of the Collective Bargaining Agreement and observing the legal determinations, the Company booked the amount of R\$ 48,200 thousand intended for employee profit sharing for the year, to be submitted to the Annual General Stockholders' Meeting - AGO. The amount of R\$ 47,877 thousand, recorded in the Statement of Operations, considers the reduction of R\$ 323 thousand, corresponding to the unrealized portion of 2005 profit sharing.

## 27 – STOCKHOLDERS' COMPENSATION

According to its policy for stockholders' compensation, the Company adopts credit of interest on equity capital, aiming the tax benefit of deductibility in income tax and social contribution calculation.

Management counsel, according to its by-laws, has established the following credits of interest on equity capital:

Date of approval	Total amount credited (R\$ thousand)	Amount credited per share (R\$)	Date of credit
06/16/2006	70,000	1.678268577	06/30/2006
09/23/2006	72,234	1.731829320	09/30/2006
12/01/2006	97,766 (*)	2.343965796	12/31/2006
<b>Total</b>	<b>240,000</b>	<b>-</b>	<b>-</b>

(\*) Paid on January 31, 2007.

Interest on equity capital benefit shareholders included in stockholders' register, on the date of credit in the Company's accounting registers.

Company's articles of incorporation establish that for each period's income, adjusted according to Law, 25% will be distributed as minimal compulsory dividends.

Pursuant to the Corporate Law and the Company's bylaw, the following dividend distribution is proposed for the year:

	2006	2005
Net income for the year	457,350	746,405
Legal reserve set up	(22,867)	(37,320)
Realization of unrealized earnings reserve	22,118	22,312
<b>Adjusted net income – basis of compensation calculation</b>	<b>456,601</b>	<b>731,397</b>
Minimum statutory dividends (25%)	114,150	182,849
<b>Compensation proposed:</b>		
Dividends	-	120,000
<b>Interest on equity capital – IEC</b>	<b>240,000</b>	<b>230,000</b>
Income tax	(35,814)	(34,322)
<b>Net compensation</b>	<b>204,186</b>	<b>315,678</b>
Percentage on adjusted net income	44.7%	43.2%
<b>Dividends/IEC per common/preferred share (R\$)</b>	<b>5.75</b>	<b>8.39</b>

Interest on equity capital is subject to withholding income tax at 15%, except for exempt shareholders, as established on Law nr. 9.249/95.

Stockholders' compensation will be paid on a date to be defined at the Annual General Stockholders' Meeting – AGO, or according to its bylaw in case AGO does not deal with the issue. Compensation will be monetarily revaluated, from December 31, 2006 up to payment, according to Brazil Central Bank overnight rate (SELIC) variation.

Interest on equity capital was accounted under operating income, as requested by tax legislation, and was reversed against retained earnings, according to CVM Deliberation nr. 207/96. That operation resulted on a tax credit from income tax and social contribution amounting R\$ 81,600 thousand (R\$ 78,200 thousand, in 2005).

## 28 - RELATED-PARTY TRANSACTIONS

These are performed under market terms and conditions, or based on contracts applicable to the Electric Sector.

Balances	2006										2005
	ELETROBRÁS	FURNAS	ELETROSUL	ELETRONORTE	ELETRONUCLEAR	CGTEE	LIGHTPAR	STN	INTESA	TOTAL	TOTAL
▪ Consumers, Concessionaires and permit grantees	-	4,770	-	6,443	545	57	-	-	-	11,815	8,124
▪ Accounts receivable	492	-	25	32	-	-	14,693	-	-	15,242	15,240
▪ Dividends receivable	-	-	-	-	-	-	-	3,192	-	3,192	-
▪ (-) Allowance for doubtful accounts	-	-	-	-	-	-	(13,237)	-	-	(13,237)	(13,237)
▪ Permanent shareholding	-	-	-	-	-	-	-	97,020	15,600	112,620	93,100
▪ Suppliers	-	(14,322)	(5,306)	(5,888)	-	-	-	-	-	(25,516)	(28,278)
▪ Loans and financing taken	(4,598,096)	-	-	-	-	-	-	-	-	(4,598,096)	(4,689,492)
▪ Interest on equity capital	(202, 876)	(4)	-	-	(3)	-	-	-	-	(202,883)	(313,774)
▪ Accounts payable	(333)	-	-	(57)	-	-	(1,456)	-	-	(1,846)	(1,815)
<b>Total</b>	<b>(4,800,737)</b>	<b>(9,556)</b>	<b>(5,281)</b>	<b>530</b>	<b>542</b>	<b>57</b>	<b>-</b>	<b>100,212</b>	<b>15,600</b>	<b>(4,698,709)</b>	<b>(4,930,132)</b>

CHANGES	01/01/2006 to 12/31/2006										2005
	ELETROBRÁS	FURNAS	ELETROSUL	ELETRONORTE	ELETRONUCLEAR	CGTEE	LIGHTPAR	STN	INTESA	TOTAL	TOTAL
▪ Revenue from use of electric network	-	39,898	-	54,429	4,635	480	-	-	-	99,442	69,126
▪ Service revenue	-	-	-	-	-	-	-	1,632	-	1,632	6,490
▪ Revenue from dividends	-	-	-	-	-	-	-	3,192	-	3,192	-
▪ Other revenues	-	-	-	-	-	-	-	-	-	-	(477)
▪ Energy purchased for resale	-	-	-	-	-	-	-	-	-	-	(82,726)
▪ Charge on use of electric network	-	(126,822)	(48,234)	(52,767)	-	-	-	(9,233)	-	(237,056)	(156,889)
▪ Financial expense on loans and financing taken	(510,491)	-	-	-	-	-	-	-	-	(510,491)	(482,946)
▪ Interest on equity capital /Dividends	(263,478)	(5)	-	-	(3)	-	-	-	-	(263,486)	(228,741)
▪ Capital contributed	-	-	-	-	-	-	-	(3,921)	(15,600)	(19,521)	(44,067)
▪ Other expenses	-	-	-	-	-	-	-	-	-	-	(16,345)
<b>Total</b>	<b>(773,969)</b>	<b>(86,929)</b>	<b>(48,234)</b>	<b>1,662</b>	<b>4,632</b>	<b>480</b>	<b>-</b>	<b>(8,330)</b>	<b>(15,600)</b>	<b>(926,288)</b>	<b>(936,575)</b>

Transactions for each company:

### **ELETROBRÁS**

- Loan agreements with average interest rate of 6.39%, for agreements in foreign currency (relending), and 10% for agreements in local currency, to be settled in short and long-term (note 17).
- Compensation on invested capital, with settlement due up to 12/31/2007.

### **FURNAS**

- Agreements for transmission system availability, authorized by ANEEL resolution.
- Agreements for the use of transmission system, authorized by ANEEL resolution.

### **ELETROSUL**

- Agreements for the use of transmission system network, authorized by ANEEL resolution.

### **ELETRONORTE**

- Agreements for transmission system availability, authorized by ANEEL resolution.
- Agreements for the use of transmission system, authorized by ANEEL resolution.

### **STN**

- Agreement for services of transmission line maintenance and operation.
- Rights granted as compensation for capital invested in the Company.
- Amount invested in shareholding, for capital contribution to the Company's capital stock.

### **INTESA**

- Amount invested in shareholding, for capital contribution to the Company's capital stock.

## **29 - FINANCIAL INSTRUMENTS**

Through its Instruction 235 of March 23, 1995, CVM established mechanisms for disclosure in explanatory notes of the market value of financial instruments, whether reflected in the financial statements or not.

The Company's financial instruments are as follows:

### **ASSETS**

- Investments in the Money Market

These are stated at market value, due to their maturity in extremely short-term.

## LIABILITIES

- Loans and financing

These local and foreign lending operations are restated based on currencies of the respective countries of origin up to the balance sheet date, being provided for at fixed or variable rates ruling at 12/31/2006, in domestic and foreign markets, and loan agreements with the parent company, Eletrobrás, which represent 93% of the total debt, almost all of which (93%) bearing interest at 10% p.a. The market rate for Eletrobrás is defined taking into account the risk premium compatible with the activities of the Electric Sector. Given the special circumstances surrounding the funding of its expansion projects, the market value of these loans is the same as their book value.

- Exchange risk

Of the total debt of the Company as of 12/31/2006, R\$ 432,405 thousand refers to agreements in foreign currency comprising US\$ 133,618 thousand (basically relending from Eletrobrás) and Eur 52,028 thousand (balances of UHE Xingó financing), which is why the Company is exposed to exchange risks from these currencies. This year, these two currencies varied in relation to the Real by -8.65% and 1.85%, respectively.



### 30 - STATEMENT OF OPERATIONS BY ACTIVITY

	2006			2005 (Reclassified)		
	Generation	Transmission	Total	Generation	Transmission	Total
<b>OPERATING REVENUE</b>						
Electric power supply	589,205	-	589,205	664,702	-	664,702
Electric power bulk supply	2,258,227	-	2,258,227	2,294,733	-	2,294,733
Transmission system availability	-	1,094,172	1,094,172	-	976,122	976,122
Other operating revenues	4,429	3,747	8,176	5,002	9,019	14,021
	<b>2,851,861</b>	<b>1,097,919</b>	<b>3,949,780</b>	<b>2,964,437</b>	<b>985,141</b>	<b>3,949,578</b>
<b>Deduction from operating revenue</b>						
Global Reversal Reserve – RGR	(71,609)	(28,216)	(99,825)	(76,686)	(25,046)	(101,732)
ICMS on electric power (added value tax)	(74,210)	-	(74,210)	(75,511)	-	(75,511)
Emergency capacity charge	-	-	-	(47,825)	-	(47,825)
Fuel consumption account - CCC	-	(113,059)	(113,059)	-	(100,919)	(100,919)
Energetic development account – CDE	-	(16,333)	(16,333)	-	(14,703)	(14,703)
PROINFA	-	(12,638)	(12,638)	-	(2,412)	(2,412)
PIS/PASEP	(39,590)	(802)	(40,392)	(45,566)	(14,892)	(60,458)
COFINS	(184,919)	9,809	(175,110)	(170,833)	(76,275)	(247,108)
	<b>(370,328)</b>	<b>(161,239)</b>	<b>(531,567)</b>	<b>(416,421)</b>	<b>(234,247)</b>	<b>(650,668)</b>
<b>NET OPERATING REVENUE</b>	<b>2,481,533</b>	<b>936,680</b>	<b>3,418,213</b>	<b>2,548,016</b>	<b>750,894</b>	<b>3,298,910</b>
<b>COST OF ELECTRIC POWER SERVICE</b>						
<b>Electric power cost</b>						
Electric power purchased for resale	(1,490)	-	(1,490)	(88,532)	-	(88,532)
Charges on use of electric power network	(575,476)	-	(575,476)	(367,334)	-	(367,334)
<b>Operating cost</b>						
Personnel	(39,865)	(94,351)	(134,216)	(36,087)	(86,922)	(123,009)
Material	(2,194)	(5,843)	(8,037)	(2,616)	(6,384)	(9,000)
Fuel for energy production	(3,173)	-	(3,173)	(10,504)	-	(10,504)
Third-parties' services	(12,615)	(26,082)	(38,697)	(13,509)	(40,845)	(54,354)
Financial compensation for water use	(206,552)	-	(206,552)	(175,566)	-	(175,566)
Depreciation and amortization	(348,070)	(179,257)	(527,327)	(345,533)	(169,456)	(514,989)
Research and development	(114,361)	(37,811)	(152,172)	(14,830)	-	(14,830)
Others	24,770	(11,923)	12,847	(9,659)	(24,060)	(33,719)
	<b>(1,279,026)</b>	<b>(355,267)</b>	<b>(1,634,293)</b>	<b>(1,064,170)</b>	<b>(327,667)</b>	<b>(1,391,837)</b>
<b>COST OF SERVICE RENDERED TO THIRD</b>	<b>(143)</b>	<b>(5,568)</b>	<b>(5,711)</b>	<b>(162)</b>	<b>(470)</b>	<b>(632)</b>
<b>GROSS OPERATING INCOME</b>	<b>1,202,364</b>	<b>575,845</b>	<b>1,778,209</b>	<b>1,483,684</b>	<b>422,757</b>	<b>1,906,441</b>
<b>OPERATING EXPENSES</b>	<b>(357,623)</b>	<b>(226,261)</b>	<b>(583,884)</b>	<b>(187,160)</b>	<b>(269,856)</b>	<b>(457,016)</b>
<b>SERVICE INCOME</b>	<b>844,741</b>	<b>349,584</b>	<b>1,194,325</b>	<b>1,296,524</b>	<b>152,901</b>	<b>1,449,425</b>
<b>FINANCIAL REVENUE (EXPENSE)</b>						
Revenue from temporary cash investments	16,032	6,211	22,243	16,844	4,930	21,774
Monetary variation and arrears charge – energy sold	130,665	507	131,172	228,244	211	228,455
Other monetary gains	6,195	8,632	14,827	4,406	939	5,345
Other financial revenues	4,205	141	4,346	(7,819)	(2,128)	(9,947)
Pis/Pasep and Cofins	(23)	-	(23)	(16)	-	(16)
Debt charges	(551,775)	(62,691)	(614,466)	(581,326)	(92,491)	(673,817)
Monetary variations on loans and financing	(194)	(2,522)	(2,716)	92,138	17,209	109,347
Other monetary losses	(22,626)	(27,277)	(49,903)	(22,838)	(55,415)	(78,253)
Other financial expenses	(50,622)	(17,644)	(68,266)	(25,243)	15,414	(9,829)
	<b>(468,143)</b>	<b>(94,643)</b>	<b>(562,786)</b>	<b>(295,610)</b>	<b>(111,331)</b>	<b>(406,941)</b>
<b>Operating income before interest on equity</b>	<b>376,598</b>	<b>254,941</b>	<b>631,539</b>	<b>1,000,914</b>	<b>41,570</b>	<b>1,042,484</b>
Interest on equity capital	(143,600)	(96,400)	(240,000)	(222,398)	(7,602)	(230,000)
<b>OPERATING RESULT</b>	<b>232,998</b>	<b>158,541</b>	<b>391,539</b>	<b>778,516</b>	<b>33,968</b>	<b>812,484</b>
Non-operating revenue	807	1,521	2,328	552	1,662	2,214
Non-operating expense	(3,033)	(5,143)	(8,176)	(491)	(9,015)	(9,506)
<b>Non-operating income</b>	<b>(2,226)</b>	<b>(3,622)</b>	<b>(5,848)</b>	<b>61</b>	<b>(7,353)</b>	<b>(7,292)</b>
<b>Profit before social contribution and income tax</b>	<b>230,772</b>	<b>154,919</b>	<b>385,691</b>	<b>778,577</b>	<b>26,615</b>	<b>805,192</b>
Social contribution	(16,796)	(16,002)	(32,798)	(63,082)	8,274	(54,808)
Income tax	(45,101)	(42,565)	(87,666)	(188,514)	(3,949)	(192,463)
<b>Profit before sharing and reversal of interest on equity capital</b>	<b>168,875</b>	<b>96,352</b>	<b>265,227</b>	<b>526,981</b>	<b>30,940</b>	<b>557,921</b>
Profit sharing	(19,988)	(27,889)	(47,877)	(14,502)	(27,014)	(41,516)
Reversal of interest on equity capital	143,600	96,400	240,000	222,398	7,602	230,000
<b>NET INCOME FOR THE YEAR</b>	<b>292,487</b>	<b>164,863</b>	<b>457,350</b>	<b>734,877</b>	<b>11,528</b>	<b>746,405</b>
Net earnings per share (R\$)	-	-	10.97	-	-	17.90

## 31 - INSURANCE

Under a contract signed with Bradesco Auto/RE – Cia. de Seguros, with 4-year duration as from 04/30/2005, the Company's main assets such as construction work and stored material are insured under annual policies for R\$ 2,951,466 thousand. The policy in force is valid from 04/30/2006 to 04/30/2007. Specification by risk is as follows:

<b><u>Policies</u></b>	<b><u>Insured Amount</u></b>	<b><u>Annual Premium</u></b>
<b>- Risks:</b>		
Fire, lightning strike, explosion, electric damage, engineering risks (operational functioning)	2,940,328	5,722
<b>- Aeronautic Risks</b>	11,138	489
	<b>2,951,466</b>	<b>6,211</b>

The amount insured under the aeronautic risk policy includes R\$ 713 thousand of third-party liability.

Besides these, the Company has transportation insurance policies to guarantee the handling of materials, which are valid from May 2005 through May 2009, totaling R\$ 181,786 thousand payable in monthly installments, with premiums amounting R\$508 thousand.

In setting the insurance and risk management policies, the physical location, level of exposure of assets and cost/benefit relationship are taken into consideration.

### 32 - GENERAL ELECTRIC SECTOR AGREEMENT – EXTRAORDINARY TARIFF RECOMPOSITION – RTE; VARIATION OF THE “PORTION A” ITEMS AND FREE ENERGY PASSED ON

1. RTE composition ratified by ANEEL, representing Loss of Revenue and Free Energy.

ITEMS	RATIFICATION INSTRUMENT NR.	RATIFIED AMOUNT	ACCUMULATED COMPENSATION 12/31/2006	AMORTIZED AMOUNT UP TO 12/31/2006	BALANCE TO BE PASSED ON AS OF 12/31/2006
		(1)	(2)	(3)	(4) = (1+2-3)
Loss of revenue	Resolution nrs 480/02, 481/02 and 01/04.	40.674	11.342	47.730	4.286
Free Energy	Resolutions nrs 01/04 and 45/04.	77.303	43.723	110.077	10.949
<b>Total</b>		<b>117.977</b>	<b>55.065</b>	<b>157.807</b>	<b>15.235</b>

2. The variation of Portion A Items (period from 01/01/2001 through 10/25/2001) ratified by ANEEL.

ITEMS	RATIFIED AMOUNT RESOLUTIONS NRS 482/02 AND 001/04	ACCUMULATED COMPENSATION UP TO 12/31/2006	ACCUMULATED AMOUNT UP TO 12/31/2006	AMORTIZED AMOUNT UP TO 12/31/2006	BALANCE TO BE PASSED ON AS OF 12/31/2006
	(1)	(2)	(3) = (1) + (2)	(4)	(5) = (3) - (4)
“Portion A” (period from 01/01 through 10/25/2001)	21,827	30,859	52,686	-	52,686

3. Composition of amounts ratified by ANEEL, representing Free Energy Passed On, i.e., energy purchased at the MAE – Wholesale Electric Power Market, currently CCEE – Electric Power Commercialization Chamber over the duration of the Emergency Reduction of Electric Power Consumption Program.

ITEMS	RATIFIED AMOUNT RESOLUTIONS NRS-001/04 AND 045/04	ACCUMULATED COMPENSATION UP TO 12/31/2006	ACCUMULATED AMOUNT UP TO 12/31/2006	AMORTIZED AMOUNT UP TO 12/31/2006	BALANCE TO BE PASSED ON AS OF 12/31/2006
	(1)	(2)	(3) = (1) + (2)	(4)	(5) = (3) - (4)
Free Energy Passed On	77,30	43,723	121,026	110,077	10,949

Under the Electric Sector General Agreement, signed by the generators and the distributors on 12/18/2001, this year the Company received R\$ 31,400 thousand and R\$ 163,947 thousand, corresponding to the Extraordinary Tariff Recomposition – RTE and the free energy refunding, respectively, and paid R\$ 27,042 thousand, for free energy.

Still under this General Agreement and in compliance with the Circular Letters nos. 2.212/2005-SFF/SRE/ANEEL, 2.218/2005-SFF/ANEEL and 074/2006-SFF/SRE/ANEEL, dated respectively, 12/20/2005, 12/23/2005 and 01/23/2006, a detailed analysis of free energy balances by debtor/creditor follows:

Receivables	12/31/2006	Payables	12/31/2006
Company	Amount (R\$ 000)	Company	Amount (R\$ 000)
CAIUÁ	3,020	AES TIETÊ	299
CEB-BRASÍLIA	8,946	CDSA	257
CELB	1,585	CEEE	133
CELG	29	CELESC	206
CELPA	6,057	CELTINS	14
CELPE	16,910	CEMIG	2,723
CELTINS	152	CESP	1,802
CEMAR	60	CGTEE	17
CEMAT	728	CHESF G	2,869
CEMIG	86,115	COPEL GERAÇÃO	113
CENF - NOVA FRIBURGO	240	CPFL PAULISTA	40
CEPISA	5,666	DUKE ENERGY	407
AMPLA (CERJ)	21,107	EEVP - VALE PARANAPANEMA	2
CESP	3,667	ELETRONORTE	880
CFLCL – CATAGUAZES	231	EMAE	223
CFLSC - SANTA CRUZ	46	EEB - BRAGANTINA	1
CHESF D	2,869	ENERGIPE	1
CJE – JAGUARI	156	FURNAS	734
CNEE – NACIONAL	81	RIO GRANDE ENERGIA – RGE	52
COELBA	24,633	TRACTEBEL ENERGIA	176
COELCE	15,619		
COSERN	9,267		
CPFL – PAULISTA	42,572		
CPFL – PIRATININGA	14,639		
CSPE - SUL PAULISTA	775		
EBE – BANDEIRANTE	21,562		
EEB – BRAGANTINA	93		
EEVP - VALE PARANAPANEMA	173		
ELEKTRO	6,562		
ELETRONORTE	57,172		
ELETROPAULO	62,290		
ENERGIPE	2,183		
ENERSUL	5,229		
ESCELSA	16,782		
LIGHT	61,564		
SAELPA	4,884		
<b>Total receivables</b>	<b>503,664</b>	<b>Total payables</b>	<b>10,949</b>
<b>Current</b>	<b>225,669</b>	<b>Current</b>	<b>8,338</b>
<b>Noncurrent</b>	<b>277,995</b>	<b>Noncurrent</b>	<b>2,611</b>

#### Allowance for losses

Chesf receives values from the distributors of free energy, according to the Overall Agreement for the Electric Energy Sector, during a period limited by ANEEL they collect the Extraordinary Tariff Adjustment (RTE) from customers and transfer the due values to the Company.

Based on a study prepared by the Company, the period established for some distributors to transfer free energy was found to be insufficient to recover the total of the values ratified by ANEEL. Therefore, an allowance of R\$ 108,962 thousand was established for losses on the realization of credits of free energy as of December 31, 2006.

### 33 - FEDERAL GOVERNMENT'S ASSETS AND RIGHTS USED BY THE CONCESSIONAIRE

According to the Accounting Instruction 6.3.13 of the Accounting Manual for the Electric Power Public Utilities, the Company keeps in auxiliary records Federal Government's assets and rights amounting to R\$ 68,465 thousand (restated cost), under special use scheme, segregated by activity, as shown below:

	2006								2005	
	Generation				Transmission				Generation	Tansm.
	Qty. Items	Restated Cost	Estimated Depreciation	Net	Qty. Items	Restated Cost	Estimated Depreciation	Net	Net	Net
UHE Castelo Branco Dam	1	56,858	(47,761)	9,097	-	-	-	-	10,235	-
Plots of land	10	2,958	-	2,958	4	223	-	223	2,958	223
Buildings	223	1,688	(1,688)	-	2	13	(10)	3	50	4
UHE Itaparica Relocation	1	5,201	(1,723)	3,478	-	-	-	-	3,686	-
Guadalupe-PI Airport	1	926	(926)	-	-	-	-	-	28	-
Access Road to UHE Castelo Branco	1	508	(508)	-	-	-	-	-	15	-
Others	-	-	-	-	3	90	(68)	22	221	25
<b>Total</b>	<b>237</b>	<b>68,139</b>	<b>(52,606)</b>	<b>15,533</b>	<b>9</b>	<b>326</b>	<b>(78)</b>	<b>248</b>	<b>17,193</b>	<b>252</b>

### 34 - EMPLOYEES' AND MANAGEMENT'S COMPENSATION

With December 2006 as a basis and pursuant to the Company's salary policy, the highest and the lowest monthly compensation paid to employees were R\$ 20,834.00 and R\$ 855.00, respectively; the highest fees paid to top management was R\$ 25,728.00. These compensations comprise permanent salaries, bonuses and additional fees.

### 35 – REVENUES – PUBLIC TRANSMISSION SERVICE CONCESSIONAIRES

The Annual Revenue Permitted (RAP) is defined on Clause First, item XIV, of the Concession Contract, and deals with revenues authorized by the National Electric Power Agency's (ANEEL) Resolution through the use of the facilities of the Transmission System listed on that Concession Contract. The transmitter's RAP comprises RPB's installments (installments referring to Base Network facilities) and RPC's (installment referring to remaining transmission and connections facilities). RPB itself comprises RBSE (revenues referring to transmission assets listed by ANEEL Resolution nr. 167/2000, for the transmission facilities existing then). Those revenues shall only be adjusted yearly by the General Market Price Index (IGP-M), plus RBNI (revenues referring to new assets to be incorporated to the Company's transmission system). It must be said that revenues earned from new investments in the transmission system will be adjusted by IGP-M (and/or Extended Consumer Price Index - IPCA, in the occasion of auctions of transmission functions), knowing that revenues will be reduced by half after 15 years of the beginning of its operations.

**BOARD OF DIRECTORS AND ADMINISTRATIVE AND FISCAL COUNCILS**

**BOARD OF DIRECTORS**

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**Dilton da Conti Oliveira**  
President

**Marcos José Mota de Cerqueira**  
Economic and Financial Director and  
Administrative Director Substitute

**José Ailton de Lima**  
Engineering and Construction Director

**Mozart Bandeira Arnaud**  
Operations Director

**SUPERINTENDENCY OF EXECUTION AND ECONOMIC-FINANCIAL CONTROL**

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**José Ivan Pereira Filho**  
Superintendent  
CRC-PE-007552/O-6 – Accountant  
CPF - 080.801.434-04

**ADMINISTRATIVE COUNCIL**

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**Aracilda Alves da Rocha**  
Chairman

**Dilton da Conti Oliveira**  
Council Member

**Swedenberger do Nascimento Barbosa**  
Council Member

**Ricardo Spanier Homrich**  
Council Member

**Erenice Alves Guerra**  
Council Member

**Maurício Moura Portugal Ribeiro**  
Council Member

**FISCAL COUNCIL**

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**Sonia Regina Jung**  
Council Member

**Marcelo Cruz**  
Council Member

**Paulo Henrique Feijó da Silva**  
Council Member

## THE INDEPENDENT AUDITORS' REPORT

To the Board of Directors and Stockholders of  
Companhia Hidro Elétrica do São Francisco - CHESF

- 1 We have examined the balance sheet of Companhia Hidro Elétrica do São Francisco - CHESF as of December 31, 2006 and 2005, and accompanying statements of operations, changes in the stockholders' equity and financial position for the years then ended, prepared under the responsibility of its management. Our responsibility is to express an opinion on such financial statements based on our audit.
- 2 Our exams were conducted in accordance with the auditing standards accepted in Brazil, and they comprised: (a) planning of the work, taking into consideration the significance of the balances, volume of transactions, as well as accounting and internal control system of the Company; (b) examining, on a test basis, evidence and records supporting the amounts and disclosures in the financial statements; and (c) assessing the accounting principles used and the more significant accounting estimates made by the management, as well as evaluating the presentation of the financial statements taken as a whole.
- 3 In our opinion, the financial statements referred to in paragraph 1 present fairly, in all material aspects, the equity and financial position of Companhia Hidro Elétrica do São Francisco - CHESF as of December 31, 2006 and 2005, as well as the result of its operations, changes in its stockholders' equity and in the financial position for the periods ended on such date, in compliance with the accounting practices adopted in Brazil.
- 4 The supplementary information, contained in the statements of added value and cash flow for the period ended as of December 31, 2006 and 2005, requested by "Agência Nacional de Energia Elétrica – ANEEL" (National Electric Power Agency), are presented with the purpose of allowing additional analyses and are not an integral part of the basic financial statements. We have examined such information in accordance with the audit procedures mentioned in paragraph 2 and, in our opinion, they are appropriately presented, in all material aspects, in relation to the financial statements taken as a whole.

Recife, March 7, 2007.

Mateus de Lima Soares  
Engagement Partner  
CRC 1RJ079681/O-0 "S" PE  
BDO Trevisan Auditores Independentes  
CRC 2SP013349/O-5 "S" PE

## THE FISCAL COUNCIL'S REPORT

The Fiscal Council of Companhia Hidro Elétrica do São Francisco – CHESF, under the use of its legal and statutory attributions, declares to have carried out the examination of **the Company's Financial Statements, relative to the fiscal year ended December 31, 2006**, having concluded, based on this examination and on the report by the Independent Auditors, BDO Trevisan Auditores Independentes, dated February 14, 2006, that such statements properly reflect the Company's financial and patrimonial situation and, through the undersigned members, recommends that these documents be submitted to the approval of the Stockholders during the Ordinary General Assembly.

Recife, March 27, 2007.

*Sonia Regina Jung*

*Marcelo Cruz*

*Paulo Henrique Feijó da Silva*