

BANCORPSOUTH INC  
Form 10-Q  
August 08, 2008

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

**FORM 10-Q**

(Mark One)

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

**For the quarterly period ended June 30, 2008**

**OR**

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

**For the transition period from \_\_\_\_\_ to \_\_\_\_\_**

**Commission File Number: 001-12991  
BANCORPSOUTH, INC.**

(Exact name of registrant as specified in its charter)

**Mississippi**

(State or other jurisdiction of incorporation or  
organization)

**64-0659571**

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

**One Mississippi Plaza, 201 South Spring Street**

**Tupelo, Mississippi**

(Address of principal executive offices)

**38804**

(Zip Code)

Registrant's telephone number, including area code: (662) 680-2000

**NOT APPLICABLE**

(Former name, former address, and former fiscal year, if changed since last report)

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes  No

As of August 5, 2008, the registrant had outstanding 82,393,037 shares of common stock, par value \$2.50 per share.

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**FORWARD-LOOKING STATEMENTS**

Certain statements contained in this Report may not be based on historical facts and are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. These forward-looking statements may be identified by reference to a future period(s) or by the use of forward-looking terminology, such as anticipate, believe, estimate, expect, foresee, might, will, intend, could, would or plan, or future or conditional verb tenses, and variations or negatives of such terms. These forward-looking statements include, without limitation, those relating to the Company's net interest margin, payment of dividends, prepayment of Junior Subordinated Debt Securities, credit losses, credit quality, core deposits, off-balance sheet commitments and arrangements, amortization expense, valuation of mortgage servicing rights, allowance for credit losses, continued weakness in the economic environment, deteriorating credit quality of borrowers, consideration for future acquisitions, estimation of pension and other postretirement benefit amounts, key indicators of the Company's financial performance (such as return on average assets and return on average shareholders' equity), liquidity needs and strategies, future acquisitions to further the Company's business strategies, the effect of certain legal claims, the impact of federal and state regulatory requirements for capital, additional share repurchases under the Company's stock repurchase program, diversification of the Company's revenue stream and the application and impact of recent accounting pronouncements. We caution you not to place undue reliance on the forward-looking statements contained in this report, in that actual results could differ materially from those indicated in such forward-looking statements as a result of a variety of factors. These factors include, but are not limited to, the ability of the Company to increase noninterest revenue and expand noninterest revenue business, the ability of the Company to fund growth with lower cost liabilities, the ability of the Company to maintain credit quality, the ability of the Company to provide and market competitive services and products, the ability of the Company to diversify revenue, the ability of the Company to attract, train and retain qualified personnel, the ability of the Company to operate and integrate new technology, changes in consumer preferences, changes in the Company's operating or expansion strategy, changes in economic conditions and government fiscal and monetary policies, legislation and court decisions related to the amount of damages recoverable in legal proceedings, fluctuations in prevailing interest

rates and the effectiveness of the Company's interest rate hedging strategies, the ability of the Company to balance interest rate, credit, liquidity and capital risks, the ability of the Company to collect amounts due under loan agreements and attract deposits, laws and regulations affecting financial institutions in general, the ability of the Company to identify and effectively integrate potential acquisitions, the ability of the Company to manage its growth and effectively serve an expanding customer and market base, geographic concentrations of the Company's assets and susceptibility to economic downturns in that area, availability of and costs associated with maintaining and/or obtaining adequate and timely sources of liquidity, the ability of the Company to compete with other financial services companies, the ability of the Company to repurchase its common stock on favorable terms, possible adverse rulings, judgments, settlements and other outcomes of pending or threatened litigation, other factors generally understood to affect the financial condition or results of financial services companies and other factors detailed from time to time in the Company's press releases and filings with the Securities and Exchange Commission. We undertake no obligation to update these forward-looking statements to reflect events or circumstances that occur after the date of this report.

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**PART I.**  
**FINANCIAL INFORMATION**

**ITEM 1. FINANCIAL STATEMENTS.**

BANCORPSOUTH, INC. AND SUBSIDIARIES  
Consolidated Balance Sheets

	June 30, 2008 (Unaudited)	December 31, 2007 (1)
	(Dollars in thousands, except per share amounts)	
<b>ASSETS</b>		
Cash and due from banks	\$ 307,038	\$ 322,926
Interest bearing deposits with other banks	15,531	12,710
Held-to-maturity securities, at amortized cost	1,447,806	1,625,916
Available-for-sale securities, at fair value	1,023,065	1,001,194
Loans and leases	9,529,978	9,227,495
Less: Unearned income	48,598	47,811
Allowance for credit losses	123,478	115,197
Net loans	9,357,902	9,064,487
Loans held for sale	171,765	128,532
Premises and equipment, net	334,869	317,379
Accrued interest receivable	83,739	96,027
Goodwill	270,807	254,889
Other assets	386,629	365,781
<b>TOTAL ASSETS</b>	<b>\$ 13,399,151</b>	<b>\$ 13,189,841</b>
<b>LIABILITIES</b>		
Deposits:		
Demand: Noninterest bearing	\$ 1,737,356	\$ 1,670,198
Interest bearing	3,364,873	3,276,275
Savings	740,207	698,449
Other time	3,964,117	4,419,177
Total deposits	9,806,553	10,064,099
Federal funds purchased and securities sold under agreement to repurchase	1,093,805	809,898
Short-term Federal Home Loan Bank and other short-term borrowings	643,427	706,586
Accrued interest payable	29,134	37,746
Junior subordinated debt securities	160,312	160,312
Long-term Federal Home Loan Bank borrowings	288,900	88,977
Other liabilities	143,244	125,597
<b>TOTAL LIABILITIES</b>	<b>12,165,375</b>	<b>11,993,215</b>

SHAREHOLDERS EQUITY

Common stock, \$2.50 par value per share Authorized - 500,000,000 shares, Issued - 82,377,811 and 82,299,297 shares, respectively	205,945	205,748
Capital surplus	201,612	198,620
Accumulated other comprehensive income (loss)	(9,232)	(7,214)
Retained earnings	835,451	799,472
<b>TOTAL SHAREHOLDERS EQUITY</b>	<b>1,233,776</b>	<b>1,196,626</b>
<b>TOTAL LIABILITIES AND SHAREHOLDERS EQUITY</b>	<b>\$ 13,399,151</b>	<b>\$ 13,189,841</b>

(1) Derived from audited financial statements.

See accompanying notes to consolidated financial statements.

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**BANCORPSOUTH, INC. AND SUBSIDIARIES**  
**Consolidated Statements of Income**  
(Unaudited)

	Three months ended June 30,		Six months ended June 30,	
	2008	2007	2008	2007
	(In thousands, except for per share amounts)			
<b>INTEREST REVENUE:</b>				
Loans and leases	\$ 147,289	\$ 169,717	\$ 306,473	\$ 322,958
Deposits with other banks	193	268	401	554
Federal funds sold and securities purchased under agreement to resell		633	67	3,144
Held-to-maturity securities:				
Taxable	15,044	16,962	30,991	33,667
Tax-exempt	2,025	2,044	4,100	4,059
Available-for-sale securities:				
Taxable	8,531	10,839	18,095	20,431
Tax-exempt	1,260	1,010	2,464	2,125
Loans held for sale	1,420	1,082	3,630	2,757
<b>Total interest revenue</b>	<b>175,762</b>	<b>202,555</b>	<b>366,221</b>	<b>389,695</b>
<b>INTEREST EXPENSE:</b>				
Deposits:				
Interest bearing demand	12,938	21,992	30,195	41,879
Savings	1,291	2,481	2,834	4,864
Other time	39,778	55,459	86,638	107,444
Federal funds purchased and securities sold under agreement to repurchase	3,321	9,283	8,516	17,107
FHLB borrowings	5,359	3,332	11,644	6,633
Other	3,232	3,350	6,481	6,442
<b>Total interest expense</b>	<b>65,919</b>	<b>95,897</b>	<b>146,308</b>	<b>184,369</b>
<b>Net interest revenue</b>	<b>109,843</b>	<b>106,658</b>	<b>219,913</b>	<b>205,326</b>
Provision for credit losses	11,237	7,843	22,048	9,198
<b>Net interest revenue, after provision for credit losses</b>	<b>98,606</b>	<b>98,815</b>	<b>197,865</b>	<b>196,128</b>
<b>NONINTEREST REVENUE:</b>				
Mortgage lending	9,507	5,484	11,050	7,263
Credit card, debit card and merchant fees	8,846	7,391	16,822	14,265
Service charges	17,093	17,677	32,932	33,073
Trust income	2,261	2,457	4,495	4,671
Security gains, net	199	10	277	17
Insurance commissions	21,462	17,665	46,130	37,459

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Other	13,898	9,548	27,791	21,843
Total noninterest revenue	73,266	60,232	139,497	118,591
NONINTEREST EXPENSE:				
Salaries and employee benefits	68,121	63,851	138,296	127,479
Occupancy, net of rental income	9,716	8,709	19,199	17,172
Equipment	6,245	6,053	12,678	12,079
Other	27,982	27,315	55,361	54,808
Total noninterest expense	112,064	105,928	225,534	211,538
Income before income taxes	59,808	53,119	111,828	103,181
Income tax expense	19,683	17,238	36,558	33,723
Net income	\$ 40,125	\$ 35,881	\$ 75,270	\$ 69,458
Earnings per share: Basic	\$ 0.49	\$ 0.44	\$ 0.91	\$ 0.86
Diluted	\$ 0.49	\$ 0.43	\$ 0.91	\$ 0.86
Dividends declared per common share	\$ 0.22	\$ 0.21	\$ 0.43	\$ 0.41

See accompanying notes to consolidated financial statements.

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BANCORPSOUTH, INC. AND SUBSIDIARIES  
Consolidated Statements of Cash Flows  
(Unaudited)

	Six months ended June 30,	
	2008	2007
	(In thousands)	
<b>Operating Activities:</b>		
Net income	\$ 75,270	\$ 69,458
Adjustment to reconcile net income to net cash provided by operating activities:		
Provision for credit losses	22,048	9,198
Depreciation and amortization	14,360	13,745
Deferred taxes	(1,016)	1,173
Amortization of intangibles	3,003	2,406
Amortization of debt securities premium and discount, net	1,382	3,670
Share-based compensation expense	1,381	925
Security gains, net	(277)	(17)
Net deferred loan origination expense	(4,731)	(4,093)
Excess tax benefit from exercise of stock options	(165)	(670)
Decrease (increase) in interest receivable	12,288	(2,393)
(Decrease) increase in interest payable	(8,612)	5,599
Realized gain on student loans sold	(17)	(2,158)
Proceeds from student loans sold	1,483	80,593
Origination of student loans held for sale	(43,101)	(46,240)
Realized gain on mortgages sold	(5,696)	(5,162)
Proceeds from mortgages sold	548,696	426,128
Origination of mortgages held for sale	(546,194)	(440,061)
Increase in bank-owned life insurance	(3,432)	(3,406)
Decrease (increase) in prepaid pension asset	668	(38,423)
Other, net	(3,695)	10,742
Net cash provided by operating activities	63,643	81,014
<b>Investing activities:</b>		
Proceeds from calls and maturities of held-to-maturity securities	186,681	79,043
Proceeds from calls and maturities of available-for-sale securities	249,015	302,399
Purchases of held-to-maturity securities	(8,860)	(141,788)
Purchases of available-for-sale securities	(274,541)	(388,836)
Net decrease in short-term investments		125,871
Net increase in loans and leases	(314,881)	(323,166)
Purchases of premises and equipment	(31,797)	(15,030)
Proceeds from sale of premises and equipment	490	667
Acquisition of businesses, net of cash acquired	(10,152)	(59,862)
Other, net	(440)	(717)
Net cash used in investing activities	(204,485)	(421,419)
<b>Financing activities:</b>		

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Net (decrease) increase in deposits	(257,546)	123,927
Net increase in short-term debt and other liabilities	219,602	129,386
Advances of long-term debt	200,000	
Repayment of long-term debt	(77)	(9,561)
Issuance of common stock	1,386	3,414
Purchase of common stock	(326)	(10,846)
Excess tax benefit from exercise of stock options	165	670
Payment of cash dividends	(35,429)	(32,994)
Net cash provided by financing activities	127,775	203,996
Decrease in cash and cash equivalents	(13,067)	(136,409)
Cash and cash equivalents at beginning of period	335,636	451,451
Cash and cash equivalents at end of period	\$ 322,569	\$ 315,042

See accompanying notes to consolidated financial statements.

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**BANCORPSOUTH, INC. AND SUBSIDIARIES**  
**Notes to Consolidated Financial Statements**  
**(Unaudited)**

**NOTE 1 BASIS OF FINANCIAL STATEMENT PRESENTATION AND PRINCIPLES OF CONSOLIDATION**

The accompanying unaudited interim consolidated financial statements of BancorpSouth, Inc. (the Company) have been prepared in conformity with accounting principles generally accepted in the United States of America and follow general practices within the industries in which the Company operates. For further information, refer to the audited consolidated financial statements and footnotes included in the Company's Annual Report on Form 10-K for the year ended December 31, 2007. In the opinion of management, all adjustments necessary for a fair presentation of the consolidated financial statements have been included and all such adjustments were of a normal recurring nature. The results of operations for the three-month and six-month periods ended June 30, 2008 are not necessarily indicative of the results to be expected for the full year. Certain 2007 amounts have been reclassified to conform with the 2008 presentation. Also, beginning March 1, 2007, the financial statements include the accounts of The Signature Bank. See Note 11, Business Combinations, for further information regarding The Signature Bank.

The consolidated financial statements include the accounts of the Company, its wholly-owned subsidiaries, BancorpSouth Bank (the Bank) and Risk Advantage, Inc., and the Bank's wholly-owned subsidiaries, Century Credit Life Insurance Company, Personal Finance Corporation of Tennessee, BancorpSouth Insurance Services, Inc., BancorpSouth Investment Services, Inc. and BancorpSouth Municipal Development Corporation.

**NOTE 2 LOANS AND LEASES**

The composition of the loan and lease portfolio by collateral type as of the dates indicated was as follows:

	June 30, 2008	June 30, 2007	December 31, 2007
		(In thousands)	
Commercial and agricultural	\$ 1,302,595	\$ 1,250,113	\$ 1,236,776
Consumer and installment	419,789	391,075	450,882
Real estate mortgage:			
One-to-four family	2,573,784	2,540,356	2,529,986
Other	4,757,771	4,275,168	4,490,445
Lease financing	276,860	292,752	285,865
Other	199,179	262,898	233,541
Total	\$ 9,529,978	\$ 9,012,362	\$ 9,227,495

The following table presents information concerning non-performing loans as of the dates indicated:

	June 30, 2008	June 30, 2007	December 31, 2007
		(In thousands)	
Non-accrual loans	\$ 17,710	\$ 9,135	\$ 9,789
Loans 90 days or more past due	25,719	13,706	18,671
Restructured loans	2,620	1,066	721
Total non-performing loans	\$ 46,049	\$ 23,907	\$ 29,181



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The following table summarizes the changes in the allowance for credit losses for the periods indicated:

	Six months ended		Year ended
	June 30,		December
	2008	2007	2007
	(In thousands)		
Balance at beginning of period	\$ 115,197	\$ 98,834	\$ 98,834
Provision charged to expense	22,048	9,198	22,696
Recoveries	2,169	1,840	4,355
Loans and leases charged off	(15,936)	(6,682)	(16,841)
Acquisitions		6,138	6,153
Balance at end of period	\$ 123,478	\$ 109,328	\$ 115,197

**NOTE 4 SECURITIES**

The following table summarizes information pertaining to temporarily impaired held-to-maturity and available-for-sale securities with continuous unrealized loss positions at June 30, 2008:

	Continuous Unrealized Loss Position						
	Less Than 12 Months		12 Months or Longer		Total		
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	
	(In thousands)						
<b>Held-to-maturity securities:</b>					<b>0.58</b>	18.7	0.42
Prior period regulatory decision	<b>3.3</b>	<b>0.07</b>	(11.0)	(0.25)			
EBIT before corporate allocations	<b>244.6</b>	<b>5.22</b>	354.2	8.03			
Corporate allocations	<b>(70.6)</b>	<b>(1.51)</b>	(82.5)	(1.87)			
EBIT	<b>\$ 174.0</b>	<b>\$ 3.71</b>	\$ 271.7	\$ 6.16			

Generation's revenues are derived from the production of electricity, of which, on an annualized basis, approximately 90 per cent are based upon contracted prices, including capacity payments, and approximately 10 per cent are subject to market pricing.

Revenues received under long-term contractual arrangements are not subject to major fluctuations in the spot price for electricity. In the fourth quarter of 2002, long-term contracts covered 91 per cent of production (2001 - 94 per cent) with the remaining nine per cent (2001 - six per cent) subject to market pricing. For the year ended Dec. 31, 2002, long-term contracts covered 90 per cent of total production (2001 - 92 per cent) with the remaining 10 per cent (2001 - eight per cent) subject to market pricing.

The existing contracts have remaining terms ranging from one to 22 years. Contracted production, as a percentage of existing production and forecasted production from assets currently under construction, over the next five years are as follows:

Contracted output				
2003	2004	2005	2006	2007
88%	87%	87%	86%	85%

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Generation also derives revenue from the provision of ancillary services such as steam and system support. Revenues are subject to seasonal variations: during the summer months, warmer temperatures result in less efficient fuel conversion rates (higher heat rates), and increased hydro production from spring run-off results in lower electricity prices.

A breakdown of revenues and average pricing applicable to each category are summarized in the following table:

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TRANSALTACORPORATION

QUARTERLYREPORT2002

<b>3 months ended Dec. 31</b>	<b>2002</b>		<b>2001</b>	
	<b>Revenue</b>	<b>Per MWh</b>	<b>Revenue</b>	<b>Per MWh</b>
Contract	\$ 405.3	\$ 34.53	\$ 373.8	\$ 33.96
Merchant	54.8	62.78	48.7	46.47
Ancillary services and other	38.6	-	9.3	-
	<b>\$ 498.7</b>	<b>\$ 39.75</b>	<b>\$ 431.8</b>	<b>\$ 37.29</b>

<b>Year ended Dec. 31</b>	<b>2002</b>		<b>2001</b>	
	<b>Revenue</b>	<b>Per MWh</b>	<b>Revenue</b>	<b>Per MWh</b>
Contract	\$ 1,448.2	\$ 33.26	\$ 1,374.1	\$ 33.23
Merchant	171.0	51.64	681.2	142.91
Ancillary services and other	93.6	-	103.1	-
Wabamun arbitration decision	(38.9)	-	-	-
	<b>\$ 1,673.9</b>	<b>\$ 35.71</b>	<b>\$ 2,158.4</b>	<b>\$ 48.90</b>

A reconciliation between production, revenue and EBIT for the fourth quarter and year ended Dec. 31, 2002 compared to the same periods in 2001 is presented below:

	Production (GWh)	Revenue	EBIT
3 months ended Dec. 31, 2001	11,579	\$ 431.8	\$ 55.4
Increased production	868	32.4	23.5
New gas plants in service (Sarnia and Big Hanaford)	388	39.9	(11.7)
Accelerated Alberta thermal plant maintenance	(290)	(10.6)	(27.7)
Wabamun impairment and equipment cancellation charges	-	-	(152.5)
Higher market prices	-	5.3	5.3
Lower purchased power requirements	-	-	66.8
Increased operations, maintenance and administration expense	-	-	(24.9)
Increased depreciation	-	-	(11.2)
Wabamun unit four TSR settlement for 2000	-	-	(11.0)
Other	-	(0.1)	8.9

<b>3 months ended Dec. 31, 2002</b>	<b>12,545</b>	<b>\$ 498.7</b>	<b>\$ (79.1)</b>
	Production (GWh)	Revenue	EBIT
Year ended Dec. 31, 2001	44,136	\$ 2,158.4	\$ 271.7
Net improved availability and production	2,538	91.1	53.5
New gas plants in service (Sarnia and Big Hanaford)	493	40.2	(13.1)
Accelerated Alberta thermal plant maintenance	(290)	(10.6)	(27.7)
Wabamun impairment and equipment cancellation charges	-	-	(152.5)
Lower market prices	-	(441.9)	(441.9)
Lower purchased power requirements	-	-	562.8
Wabamun arbitration decision	-	(38.9)	(38.9)
Impact of the Pierce Power plant monetization in 2001	-	(121.8)	(3.0)
Increased operations, maintenance and administration expense	-	-	(33.0)
Increased depreciation	-	-	(34.6)
Lower fuel costs per megawatt hour	-	-	39.4
Wabamun unit four TSR settlement for 2000 and prior period regulatory decision	-	-	(14.3)
Other	-	(2.6)	5.6
<b>Year ended Dec. 31, 2002</b>	<b>46,877</b>	<b>\$ 1,673.9</b>	<b>\$ 174.0</b>

As discussed in significant one-time items, the corporation recognized an impairment charge of \$110.0 million relating to the Wabamun plant, as the carrying value was determined to be in excess of fair value. TransAlta also cancelled the order for four natural gas turbines resulting in a \$42.5 million contract termination charge. In September 2001, TransAlta monetized its investment in the 154 MW Pierce Power plant as a result of weak economic conditions. Revenue hedges were realized resulting in the recognition of revenue of \$121.8 million, offset by an asset impairment charge of \$66.5 million and a recognition of anticipated future operating costs of \$52.3 million.

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## TRANSALTACORPORATION

## QUARTERLYREPORT2002

As a result of the corporation's forward view of the electricity market and its positive experience with improvements at the Centralia plant, the corporation accelerated its Alberta thermal plant maintenance schedule. This is being undertaken in order to improve reliability and increase availability when the economy turns around and electricity demand increases. This decision resulted in lower revenues and increased maintenance costs (\$27.7 million pre-tax) in the fourth quarter of 2002.

As discussed in significant one-time items, the Wabamun arbitration decision resulted in a \$38.9 million pre-tax payment that was recorded as a reduction of revenue in the second quarter of 2002.

As discussed in significant one-time items, the EUB rendered a negative decision of \$3.3 million pre-tax with respect to TransAlta's hydro bidding strategy in 2000, which was recorded in 2002 as a prior period regulatory decision.

Availability for the fourth quarter of 2002 was 87.2 per cent compared to 89.9 per cent in 2001, reflecting decreased availability at the Alberta thermal plants due to the accelerated maintenance schedule and the unplanned Wabamun unit three outage discussed previously. Availability for the year ended Dec. 31, 2002 was 88.4 per cent compared to 86.9 per cent in 2001 as a result of improved operational performance at the thermal and gas plants, partially offset by the accelerated maintenance at the Alberta thermal plants and the Wabamun outage. At various times during 2002, when the market price of electricity was lower than the variable costs of production at certain plants, the corporation reduced production at these plants, and purchased electricity from the market to fulfill contractual obligations (economic dispatch). During these periods of economic dispatch, the affected plants were available to generate the electricity if required.

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In the three months ended Dec. 31, 2002, production increased by 966 GWh compared to the same period in 2001 as a result of incremental production from the Sarnia and Big Hanaford plants and increased production from the Centralia plant, offset by lost production resulting from accelerated Alberta thermal plant maintenance. There was no economic dispatch in the fourth quarter of 2002. In the year ended Dec. 31, 2002, total production increased by 2,741 GWh compared to 2001. This increase was the result of the items discussed above and the return to service of Wabamun unit four as well as increased thermal production and availability, partially offset by 731 GWh decreased production resulting from economic dispatch decisions.

As shown in the above graphs, electricity spot prices in the fourth quarter of 2002 in both the Alberta and Pacific Northwest markets increased compared to the same period in 2001; however on an annual basis, electricity spot prices were lower in 2002 than in 2001. In the fourth quarter, spark spreads (power price less cost of gas consumed) increased in the Alberta market and decreased in the Pacific Northwest market. For the year ended Dec. 31, 2002, spark spreads decreased in both the Alberta and Pacific Northwest markets. Within these markets, prices were softer in 2002 due to reduced demand as a result of lower economic activity, increased hydro production, and additional generating capacity added to these markets.

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### TRANSALTA CORPORATION

#### QUARTERLY REPORT 2002

Generation's revenue for the fourth quarter of 2002 increased by \$66.9 million (\$2.46 per MWh) compared to the same period in 2001. The increase is due to higher production, higher ancillary services revenue, increased long-term contracted prices and higher electricity spot prices. The increase in contracted prices is due to higher gas prices, which are recovered under the terms of certain contracts. Revenue for the year ended Dec. 31, 2002 decreased by \$484.5 million (\$13.19 per MWh) compared to 2001. Adjusted for the Wabamun arbitration and Pierce Power decisions, revenue was \$1,712.8 million (\$36.54 per MWh) in 2002 compared to \$2,036.6 million (\$46.14 per MWh) in 2001. The decline in revenue in 2002 reflects lower electricity spot prices, partially offset by improved production and availability.

Fuel and purchased power decreased by \$19.5 million (\$3.19 per MWh) in the fourth quarter of 2002 and by \$527.0 million (\$12.87 per MWh) for the year ended Dec. 31, 2002. Purchased power is the cost incurred to acquire electricity from the market to fulfill contracted commitments during planned and unplanned outages. Any electricity not required to fulfill these commitments is sold back into the market at spot prices.

Purchased power declined significantly in the fourth quarter and the year ended Dec. 31, 2002 to \$5.1 million and \$32.1 million, respectively (2001 - \$71.9 million and \$594.9 million). The purchased power in the fourth quarter was the result of plant outages, while the majority of the purchased power requirement for the remainder of 2002 was due to the economic dispatch decisions discussed earlier. Due to high market power prices in the fourth quarter of 2002, no economic dispatch occurred in the quarter. In the fourth quarter of 2001, expected lower availability at the Centralia plant resulted in the purchase of 551 GWh of electricity, totalling \$71.9 million. In the year ended Dec. 31, 2001, 2,707 GWh of electricity was purchased totalling \$594.9 million. Pre-tax losses as a result of these purchases in the three and twelve months ended Dec. 31, 2001 were US\$28.0 million (approximately Cdn\$47 million) and US\$77.7 million (approximately Cdn\$124 million), respectively.

Fuel costs, excluding purchased power, consist primarily of coal and natural gas costs. Total fuel costs, excluding purchased power, were \$221.8 million (\$17.68 per MWh) in the fourth quarter of 2002 compared to \$174.5 million (\$15.07 per MWh) in 2001. For the year ended Dec. 31, 2002, coal and natural gas costs totalled \$671.5 million (\$14.32 per MWh) compared to \$635.7 million (\$14.40 per MWh) in 2001. TransAlta's average fuel costs per MWh are shown below:

3 months ended Dec. 31      Year ended Dec. 31



	2002	2001	2002	2001
Coal	<b>\$12.40</b>	\$ 13.91	<b>\$11.70</b>	\$ 12.34
Gas	<b>\$40.51</b>	\$ 21.87	<b>\$27.86</b>	\$ 26.16
Average fuel costs, excluding purchased power	<b>\$17.68</b>	\$ 15.07	<b>\$14.32</b>	\$ 14.40

TransAlta is subject to fluctuations in natural gas and coal costs, however the majority of the coal used in generation is from coal reserves owned by TransAlta. This allows the corporation to control the cost of coal. As a result of cost reduction programs, TransAlta reduced coal costs by 11 per cent in the fourth quarter of 2002 and five per cent for the year ended Dec. 31, 2002 compared to the same periods in 2001. The fourth quarter increase in fuel costs per MWh, excluding purchased power, is attributable to the 85 per cent increase in natural gas costs, partially offset by the decrease in coal costs. The increase in gas costs is due to higher natural gas market prices at the Big Hanaford plant and higher gas prices and heat rates at the Sarnia plant. For contracted plants, a portion of the gas costs have been hedged by the corporation, and in some cases, the corporation has hedged plants' spark spreads. In certain contracted plants the gas cost is a flow through to the customer and is not hedged by the corporation, therefore TransAlta is still subject to fluctuations in gas prices, but the increased gas costs are recovered through increased revenues. Gas costs for electricity to be sold in spot markets are matched to power sales and hedged accordingly. Fuel costs, excluding purchased power, on a per MWh basis, decreased for the year ended Dec. 31, 2002 as a result of the decrease in coal costs, partially offset by increased natural gas costs as discussed above.

In the fourth quarter of 2002, operations, maintenance and administration (OM&A) expenses increased by \$46.6 million (\$3.26 per MWh) over the same period in 2001. The increase represents the impact of the accelerated maintenance at the Alberta thermal plants, the commissioning of the Sarnia and Big Hanaford plants, increased business development costs, inventory obsolescence costs and increased project management costs related to plants under construction. For the year ended Dec. 31, 2002, OM&A increased by \$55.7 million (\$0.81 per MWh) from 2001. This reflects the impact of the items discussed above and increased insurance premiums partially offset by cost reduction initiatives.

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## TRANSALTACORPORATION

## QUARTERLYREPORT2002

Depreciation and amortization increased by \$16.0 million (\$1.00 per MWh) for the fourth quarter of 2002 and \$39.8 million (\$0.64 per MWh) for the year ended Dec. 31, 2002 compared to the same periods in 2001. The increase is the result of the addition of the Big Hanaford plant and increased capital projects at thermal plants.

The increase in taxes other than income taxes in the three and twelve months ended Dec. 31, 2002 relates to higher property tax assessments by local municipalities on the majority of the corporation's plants.

**ENERGY MARKETING: Derives revenue and earnings from the wholesale trading of electricity and other energy-related commodities and derivatives. These activities also provide critical market knowledge to help identify growth opportunities and support corporate investment decisions.**

The results of Energy Marketing are as follows:

	3 months ended Dec. 31		Year ended Dec. 31	
	2002	2001	2002	2001
Gross revenues	\$ <b>992.4</b>	\$ 526.9	\$ <b>3,703.8</b>	\$ 2,694.7
Trading purchases	<b>(974.5)</b>	(524.3)	<b>(3,654.8)</b>	(2,533.7)
Net revenues	<b>17.9</b>	2.6	<b>49.0</b>	161.0
Operations, maintenance and administration	<b>3.6</b>	1.6	<b>15.1</b>	36.2
Depreciation and amortization	<b>0.5</b>	4.0	<b>2.5</b>	11.0

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Taxes, other than income taxes	-	-	<b>0.1</b>	-
EBIT before corporate allocations	<b>13.8</b>	(3.0)	<b>31.3</b>	113.8
Corporate allocations	<b>(2.3)</b>	(1.9)	<b>(8.3)</b>	(6.6)
EBIT	<b>\$ 11.5</b>	\$ (4.9)	<b>\$ 23.0</b>	\$ 107.2

Gross physical and financial settled sales transactions are as follows:

<b>Electricity (GWh)</b>	3 months ended Dec. 31		Year ended Dec. 31	
	<b>2002</b>	2001	<b>2002</b>	2001
Physical	<b>18,619</b>	10,131	<b>63,015</b>	18,504
Financial	<b>13,167</b>	4,990	<b>40,061</b>	9,115
	<b>31,786</b>	15,121	<b>103,076</b>	27,619

<b>Gas (million GJ)</b>	3 months ended Dec. 31		Year ended Dec. 31	
	<b>2002</b>	2001	<b>2002</b>	2001
Physical	<b>26.5</b>	12.2	<b>96.2</b>	30.6
Financial	<b>19.4</b>	24.3	<b>63.6</b>	68.7
	<b>45.9</b>	36.5	<b>159.8</b>	99.3

The Energy Marketing group uses energy derivatives, including physical and financial swaps, forwards and options to earn trading revenues and gain market information. Energy contracts that meet the definition of a derivative in the Financial Accounting Standards Board (FASB) Statement 133, *Accounting for Derivative Instruments and Hedging Activities*, are accounted for at fair value in accordance with Canadian and U.S. GAAP.

Derivatives are used to hedge the corporation's exposure to changes in electricity and natural gas prices. Under Canadian GAAP, settlement accounting is used for hedging activities if certain criteria are met. Under U.S. GAAP, hedging activities are accounted for in accordance with FASB Statement 133.

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TRANSALTA CORPORATION

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Gross trading sales volumes during the fourth quarter of 2002 increased by 16,665 GWh of electricity and by 9.4 million giga-joules (GJ) of gas compared to 2001. In the year ended Dec. 31, 2002, trading volumes increased by 75,457 GWh of electricity and 60.5 million GJ of gas compared to 2001. Liquidity in the medium- to long-term markets remained low and as a result, Energy Marketing continued to have a low level of activity in these markets. Coincidentally, activity levels in the short-term market increased. As expected, increased market liquidity and pricing efficiencies resulted in margins on individual trades being reduced. TransAlta's trading activity comprised mainly short-term transactions, the majority of which were settled within ninety days thereby limiting risk and maintaining low working capital requirements. Value at risk levels throughout 2002 were consistent with 2001 levels. The increase in gas trading volumes relates to the settlement of trading positions offset in early 2002 when the

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gas trading book was closed. In addition, the trading of heat rate swaps, which include a gas element and are therefore presented as settled gas transactions, increased in 2002.

Gross sales increased by \$465.5 million in the three months ended Dec. 31 and increased by \$1,009.1 million for the year ended Dec. 31, 2002 compared to 2001. Increased electricity trading volumes in 2002 more than offset lower market prices and the reduced gas trading activities in the first and second quarters of 2002.

Net revenues increased by \$15.3 million for the fourth quarter of 2002 as a result of increased trading activity and higher percentage margins. Net revenues decreased by \$112.0 million for the year ended Dec. 31, 2002 due to significantly lower market prices and margins compared to 2001, particularly in the Pacific Northwest. The 2001 Pacific Northwest prices were influenced by the process of deregulation in California, exacerbated by a drought in the Pacific Northwest and historically high natural gas prices.

In the fourth quarter of 2002, OM&A expense increased by \$2.0 million due primarily to higher incentive compensation recognized during the quarter. Incentive compensation is based on net revenues which increased in the quarter, as discussed above. OM&A decreased by \$21.1 million for the year ended Dec. 31, 2002 due to lower annual incentive compensation resulting from lower annual net revenue and one-time costs associated with the acquisition of the remaining 50 per cent of Merchant Energy Group of the Americas, Inc. (MEGA) in June 2001.

Depreciation and amortization decreased by \$3.5 million in the fourth quarter of 2002 and by \$8.5 million for the year ended Dec. 31, 2002. The decrease is due to \$29.3 million of goodwill arising from the acquisition of MEGA, previously recorded as acquired intangibles, which is no longer being amortized. This treatment is in accordance with the new accounting standard issued by the CICA. There was no impairment of goodwill upon adoption of the standard on Jan. 1, 2002, nor was there an impairment at Dec. 31, 2002.

Energy Marketing's price risk management assets and liabilities represent the fair value of unsettled (unrealized) trading transactions. With the exception of transmission contracts, the fair value of all energy trading activities is based on quoted market prices. The fair value of physical transmission contracts is based on quoted market prices and a spread option valuation model. The fair value of financial transmission contracts is based upon statistical analysis of historical data.

The following table illustrates movements in the fair value of the corporation's price risk management assets (liabilities) during the twelve months ended Dec. 31, 2002:

Fair value of net price risk management assets outstanding at Dec. 31, 2001	\$	<b>25.8</b>
Fair value of new contracts entered into during the period		<b>(2.7)</b>
Changes in fair values attributable to market price and other market changes		<b>7.6</b>
Contracts realized or settled during the period		<b>(36.6)</b>
Changes in fair values attributable to changes in valuation techniques and assumptions		-
<hr/>		
Fair value of net price risk management liabilities outstanding at Dec. 31, 2002	\$	<b>(5.9)</b>

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### TRANSALTACORPORATION

#### QUARTERLY REPORT 2002

The source of the valuations of the above contracts and maturities over each of the next five calendar years and thereafter is as follows:

		2003	2004	2005	2006	2007	2008 and thereafter	Total
Prices actively quoted	\$	(17.6)	\$ 3.3	\$ 3.2	\$ 2.1	\$ 1.5	\$ -	\$ (7.5)
Prices based on models		1.6	-	-	-	-	-	1.6
<hr/>								
Asset (liability)	\$	(16.0)	\$ 3.3	\$ 3.2	\$ 2.1	\$ 1.5	\$ -	\$ (5.9)

In 2002, TransAlta responded to a number of inquiries from various U.S. State and Federal bodies regarding trading activities in California and states in the Pacific Northwest during 2000 and 2001. TransAlta believes it operated in accordance with all applicable laws, rules, regulations and tariffs. No significant developments have occurred on these issues as a result of TransAlta's responses.

In the fourth quarter of 2002, two class action lawsuits on behalf of all persons and businesses in the states of Oregon and Washington were initiated in respect of alleged unlawful practices in the purchase and sale of wholesale energy. TransAlta believes these are without merit and will vigorously defend its actions.

In 2000, TransAlta made a provision of US\$28.8 million against US\$58.0 million owing from the California Independent System Operator and the California Power Exchange. During 2001, US\$5.0 million was collected. No change has been made to the provision due to the continuing uncertainty in California. The amount has been reclassified to long-term, as collection is no longer expected in 2003, although ultimate collection is still expected. On Dec. 12, 2002, a U.S. Federal Energy Regulatory Commission (FERC) Administrative Law Judge proposed that TransAlta receive approximately US\$44.0 million, however FERC has indicated that further adjustments in respect of power and gas prices may occur, which could result in further alterations of the amount TransAlta is to receive. As a result, TransAlta has not adjusted the amount receivable or the provision.

**NET INTEREST EXPENSE, OTHER EXPENSE, FOREIGN EXCHANGE, NON-CONTROLLING INTERESTS AND PREFERRED SECURITIES DISTRIBUTIONS**

	3 months ended Dec. 31		Year ended Dec. 31	
	2002	2001	2002	2001
Gross interest expense	\$ 46.7	\$ 42.4	\$ 172.9	\$ 170.3
Interest income	(1.7)	(8.7)	(8.7)	(24.2)
Interest allocated to discontinued operations	-	(0.6)	(2.4)	(9.7)
Capitalized interest	(21.0)	(20.7)	(79.1)	(48.3)
Net interest expense	24.0	12.4	82.7	88.1
Other income	(1.0)	(1.2)	(0.1)	(1.5)
Foreign exchange gain	(0.9)	(2.9)	(1.2)	(0.8)
Non-controlling interests	5.6	5.0	20.1	20.6
Preferred securities distributions, net of tax	4.7	3.5	20.9	13.1
	\$ 32.4	\$ 16.8	\$ 122.4	\$ 119.5

On June 20, 2002, the corporation issued US\$300.0 million of senior notes under a US\$1.0 billion shelf prospectus filed May 14, 2002. The proceeds of the issuance were used to repay short-term debt and U.S. denominated commercial paper. The notes are unsecured and bear interest at 6.75 per cent and mature on July 15, 2012.

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**TRANSALTACORPORATION**

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Net interest expense increased by \$11.6 million in the three months ended Dec. 31, 2002 compared to the same period of 2001. The increase was primarily due to a higher proportion of debt subject to long-term interest rates and lower interest income due to the receipt of the \$180.3 million receivable from Aquila Networks Canada (formerly UtiliCorp Networks Canada) that arose from the sale of the Alberta Distribution and Retail (D&R) operation. Net interest expense decreased by \$5.4 million for the year ended Dec. 31, 2002 as a result of an overall decline in average debt levels and higher capitalized interest, offset by a higher proportion of debt subject to long-term interest rates and receipt of the interest-bearing receivable from Aquila Networks Canada.

The increase in earnings attributable to non-controlling interests in the fourth quarter of 2002 compared to 2001 is attributable to increased quarterly earnings relating to the 49.99 per cent non-controlling interest in TransAlta Cogeneration, L.P. The decrease for the year ended Dec. 31, 2002 compared to 2001 is the result of the redemption of the preferred shares of TransAlta Utilities

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Corporation for \$121.6 million in September 2001, resulting in lower subsidiary preferred share dividends, offset by higher earnings from TransAlta Cogeneration, L.P.

The increases in preferred securities distributions, net of tax, reflect the issuance of \$175.0 million of 7.75 per cent preferred securities in November 2001.

### I N C O M E T A X E S

Income tax expense (recovery) Effective tax rate

2002	3 months ended Dec. 31 2001	Year ended Dec. 31 2002	2001
\$ (35.1)	\$ 0.5	\$ 18.1	\$ 89.9
39.4%	1.2%	15.6%	30.7%

An income tax recovery of \$35.1 million was recorded for the three months ended Dec. 31, 2002, compared to income tax expense of \$0.5 million for the same period in 2001. The recovery reflects the loss incurred in the current quarter. Income taxes decreased by \$71.8 million for the year ended Dec. 31, 2002 due to lower earnings and the impact of the Wabamun decommissioning and the turbine cancellation charges, which were recognized at the marginal rate. The decrease also reflects the benefit of previously unrecognized tax losses that were recognized in the third quarter of 2002 as it became more likely than not that they would be utilized. The effective income tax rate, expressed as a percentage of earnings from continuing operations before income taxes and non-controlling interests, decreased to 15.6 per cent in 2002 from 30.7 per cent in 2001. The effective tax rate in 2002 reflects the impact of the issues discussed above. Due to lower earnings in the three months ended Dec. 31, 2001, the 1.2 per cent effective rate reflects the impact of the financing arrangements of TransAlta's foreign operations. The benefits of these arrangements do not vary with earnings.

### D I S C O N T I N U E D                      O P E R A T I O N S

	3 months ended Dec. 31 2002	2001	Year ended Dec. 31 2002	2001
Transmission operation	\$-	\$ 13.3	\$ 12.8	\$ 44.4
Gain on disposal of Transmission operation	10.0	-	120.0	-
Edmonton Composter operation	-	-	-	0.7
	<b>\$10.0</b>	\$ 13.3	<b>\$ 132.8</b>	\$ 45.1

As discussed in significant one-time items, TransAlta sold its Transmission operation in April 2002 for proceeds of \$820.7 million. The disposal resulted in an after-tax gain on sale of \$120.0 million (\$0.71 per common share).

On June 29, 2001, TransAlta sold its Edmonton Composter for proceeds of \$97.0 million, which approximated its book value.

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T R A N S A L T A C O R P O R A T I O N

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### F I N A N C I A L P O S I T I O N

The following chart outlines significant changes in the consolidated balance sheet from Dec. 31, 2001 to Dec. 31, 2002:

Increase / (decrease)	Explanation
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Cash and cash equivalents	\$ 81.3	Refer to Consolidated Statements of Cash Flows.
Accounts receivable and other	(156.9)	Decrease primarily due to collection of receivable related to monetized Pierce Power hedges (\$82.0 million), reclassification of California receivables to long-term (US\$24.2 million) and the sale of the Transmission business, (\$31.7 million).
Materials and supplies, at average cost	27.2	Higher coal inventory balances as a result of second and third quarter economic dispatch decisions, increased coal production and advanced maintenance at the Alberta thermal plants.
Long-term receivables	(181.5)	Receipt of amount due from Aquila (formerly UtiliCorp) relating to the sale of the discontinued D&R operation (\$180.3 million) and reclass of sulphur tax abatement (\$45.0 million) to current receivables, offset by reclassification of California receivables to long-term (US\$24.2 million).
Property, plant and equipment, net of accumulated depreciation	(59.7)	Capital expenditures and construction activity during the period and acquisition of Vision Quest, more than offset by depreciation, the sale of the Transmission business, the impairment charge relating to the decommissioning of the Wabamun plant and equipment cancellation charges.
Goodwill	27.2	Acquisition of Vision Quest in December 2002.
Future income tax assets	56.6	2001 U.S. operating losses that will be recovered in future years.
Other assets	29.5	Long-term prepayments related to the Sarnia plant and financing costs related to US\$300.0 million debt issuance and financing costs related to the Mexican projects.
Short-term debt	(247.2)	Repayment with a portion of the proceeds from US\$300.0 million debt issuance and proceeds from disposal of the Transmission operation.
Accounts payable and accrued liabilities	(155.3)	Decrease due to lower capital expenditures in the quarter.
Price risk management liabilities (current and long-term)	41.3	Decrease in margins on energy trading activities.
Long-term debt (including current portion)	195.5	US\$300.0 million debt issuance, offset by maturity of debentures of \$100 million and net decrease in long-term commercial paper repaid with proceeds on disposal of the Transmission business.
Non-controlling interests	(18.0)	Acquisition of remaining interest in Southern Cross Energy (\$7.2 million) and decreased non-controlling interest in TransAlta Cogeneration, L.P. as a result of distributions in excess of net income.
Shareholders' equity	49.9	Net earnings and issuance of common shares for Vision Quest acquisition, partially offset by dividends and net redemption of common shares.

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TRANSALTACORPORATION

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**STATEMENTS OF CASH FLOWS :**

<i>3 months ended Dec. 31</i>		<b>2002</b>	2001
Cash and cash equivalents, beginning of period	\$	<b>120.6</b>	61.5
Provided by (used in):			
Operating activities		<b>189.5</b>	131.7
Investing activities		<b>(261.0)</b>	(366.1)
Financing activities		<b>96.7</b>	230.9
Translation of foreign currency cash		<b>(2.5)</b>	4.0
Cash and cash equivalents, end of period	\$	<b>143.3</b>	62.0
<i>Year ended Dec. 31</i>		<b>2002</b>	2001
Cash and cash equivalents, beginning of period	\$	<b>62.0</b>	53.8
Provided by (used in):			
Operating activities		<b>437.7</b>	715.6
Investing activities		<b>(36.2)</b>	(1,076.9)

Financing activities	<b>(320.9)</b>	368.7
Translation of foreign currency cash	<b>0.7</b>	0.8
Cash and cash equivalents, of period	<b>\$ 143.3\$</b>	62.0

Explanation

Lower cash operating earnings offset by decreased working capital requirements due to collection of income taxes receivable related to U.S. operations in 2001.

In 2002, capital expenditures of \$194.6 million relating primarily to construction of Sarnia and the Mexico plants, acquisition of Vision Quest for \$41.1 million (less cash acquired of \$8.2 million) and acquisition of remaining interest in Southern Cross Energy (SCE) for \$7.2 million. In 2001, capital expenditures included the installation of the scrubber at the Centralia plant and construction of the Big Hanaford plant.

In 2002, net increase in short-term debt, offset by \$100.0 million debenture maturity, net repayment of commercial paper and cash dividends of \$29.5 million.

In 2001, debt issuances of \$125.0 million and \$169.4 million proceeds on issuance of preferred securities, offset by dividends of \$28.7 million and redemption of common shares of \$14.2 million.

Explanation

Lower cash operating earnings as a result of the impact of the Wabamun arbitration and prior period regulatory decisions, offset by increased working capital requirements due to the timing of the ancillary revenue settlement (\$49.9 million), timing of accounts receivable relating to the Alberta Power Pool for Generation due to deregulation on Jan. 1, 2001 (\$170.0 million), and the final instalment of 2001 income taxes paid in the first quarter of 2002 (\$109.0 million).

In 2002, proceeds on the disposal of the Transmission operation and collection of amounts receivable from Aquila (formerly UtiliCorp) related to the sale of the discontinued Alberta D&R operation in 2000, offset by capital expenditures relating to the construction of the Sarnia, Big Hanaford, Campeche and Chihuahua plants, the acquisition of Vision Quest and the remaining portion of SCE as well as the installation of the scrubber at the Centralia plant during the second quarter.

In 2001, capital expenditures relating primarily to the installation of the scrubber at the Centralia plant and construction of the Sarnia, Big Hanaford and Campeche plants were offset by proceeds on the disposal of the Edmonton Composter, Mildred Lake, Fort Nelson and Fort Saskatchewan plants.

In 2002, the issuance of US\$300.0 million in long-term notes offset by the repayment of short- and long-term debt, payment of common share and preferred securities distributions, and repurchase of common shares.

In 2001, net long-term borrowings offset by redemption of preferred shares of a subsidiary, common and preferred share dividends and repurchase of common shares.



## TRANSALTA CORPORATION

## QUARTERLY REPORT 2002

## OUTLOOK

The key factors affecting the financial results for 2003 continue to be the megawatt capacity in place, the availability of and production from generating assets, the pricing applicable to non-contracted production, the costs of production, and the volumes traded and margins achieved on Energy Marketing activities.

Generating capacity in 2003 will be higher than in 2002 due to the addition of the 575 MW Sarnia plant which will commence commercial operations in the first quarter of 2003. 55 MW of added capacity at Sarnia is forecasted for 2005. The acquisition of Vision Quest in December 2002 added 44 MW of capacity with a further 37.5 MW scheduled to commence operation in the second quarter of 2003. The 252 MW Campeche and 259 MW Chihuahua plants in Mexico are scheduled to commence commercial operations in the first and third quarters of 2003, respectively. These increases will be partially offset by the shutdown in November 2002 of unit three at the Wabamun facility (147 MW). Availability for 2003 is expected to be similar to 2002, however production is expected to be higher than in 2002 due to the increased capacity.

Electricity spot prices in 2003 are expected to be similar to those in 2002 for the Alberta market and higher in the Pacific Northwest. However, spark spreads (the difference between electricity prices and cost of gas consumed) are expected to compress due to the proportionately higher increase in the cost of natural gas. Expected electricity demand compared to levels of supply is expected to prevent prices from materially increasing over the medium term.

Legislation was passed in Ontario in late 2002 capping retail market prices at \$43 per MWh. However, wholesale market prices have not been directly impacted by this decision. Some of the legislation has not yet been clarified and as a result, revenues for merchant capacity at the Sarnia plant may be affected.

Exposure to volatility in electricity prices is substantially mitigated through firm price long-term electricity sales contracts. Exposure to volatility in gas prices is substantially mitigated by the flow-through of the costs of natural gas to customers in some of these contracts and the existence of price caps in certain natural gas supply contracts. For 2003, approximately 88 per cent of output will be contracted, a significant portion of which relates to the Alberta PPAs which are capacity related based on achieving agreed availability rates. The corporation will continue to focus on the maximization of revenues from these contracts. For non-contracted sales, the historic correlation between natural gas and electricity prices is expected to weaken in 2003, resulting in a compression of spark spreads for non-contracted plants compared to 2002.

TransAlta is continuing its focus on reducing coal costs and ongoing operating (OM&A) expenses. The areas for reductions were identified in the fourth quarter of 2001 and have been, and continue to be, implemented. The benefits of these initiatives are beginning to be realized, and are expected to become fully apparent in 2003 and beyond. However, it is expected there will be more planned maintenance in the Alberta thermal plants in 2003 than in 2002.

Energy Marketing anticipates that short-term markets will continue to be active. Liquidity in the medium- and longer-term markets continues to be low, however there is a need for the types of products offered in these markets and the corporation hopes that additional creditworthy counterparties will begin to emerge and thereby increase liquidity. The financial performance of Energy Marketing activities is expected to be similar to that achieved in 2002.

In 2003, capital expenditures will be approximately \$830 million, of which approximately \$275 million will be spent on the Genesee Phase three project, described below, approximately \$170 million will be spent to complete the two Mexican plants, \$60 million on other growth projects and approximately \$325 million on maintenance and productivity expenditures as a result of the planned outages and preventative maintenance. Included in the maintenance and productivity expenditures is \$25 million in respect of CE Generation LLC (CE Gen), described below. Financing for these expenditures is expected to come from a combination of cash flow from operations, monetization of selected assets, issuance of common shares and the issuance of debt. TransAlta has access to a wide variety of sources of capital including: a \$1.5 billion medium-term note program; a US\$1.0 billion shelf prospectus; a \$1.0 billion commercial paper program; and approximately \$2.0 billion of bank credit facilities.

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On Jan. 24, 2003 the corporation announced the acquisition of 50 per cent of the membership interests in CE Gen for US\$205.0 million (approximately Cdn\$312 million) plus approximately US\$35.0 million of working capital (approximately Cdn\$53 million) and the assumption of non-recourse debt of approximately US\$500.0 million (approximately Cdn\$762 million). MidAmerican Energy Holdings Company is the other 50 per cent member of CE Gen. CE Gen, through its subsidiaries, is primarily engaged in the development, ownership and operation of independent power production facilities in the United States utilizing geothermal and natural gas resources. CE Gen has 13 facilities with an aggregate operating capacity of 820 MW. The transaction closed on Jan. 29, 2003.

On Jan. 13, 2003, TransAlta and EPCOR Utilities Inc. (EPCOR) announced an agreement for TransAlta to acquire a 50 per cent interest in EPCOR's Genesee Phase three project for \$395.0 million. On the same date, TransAlta paid EPCOR \$157.0 million for TransAlta's share of project costs incurred to date. The 450 MW addition to the existing Genesee Generating Station is currently under construction southwest of Edmonton, Alberta. The two corporations will own and share costs for Genesee Phase 3 equally. EPCOR will continue to manage the project's construction and will operate the plant upon commercial operation in early 2005. Both parties will independently dispatch and market their share of the electrical output from the unit through the Alberta Power Pool. Included in the arrangement is an option for EPCOR to purchase a 50 per cent interest in TransAlta's Centennial one project described below. The option expires Dec. 31, 2005. EPCOR also has the option to purchase a 50 per cent interest in TransAlta's Sarnia plant, which may be exercised between January 2003 and March 2004.

In February 2002, the EUB approved the previously announced Centennial project, which is a 900 MW merchant expansion at the Keephills site. Phase one of the project is now part of the arrangement with EPCOR and the two corporations will jointly proceed with the development phase of the project. The decision to construct phase one will be made in sufficient time to ensure that the plant is operational when market conditions are appropriate. EPCOR has an option to participate in the construction and ownership of the project.

TransAlta will continue to focus on exploring strategic acquisitions and additional greenfield opportunities. Growth will only be undertaken to the extent that is affordable and supported by the balance sheet.

On Dec. 16, 2002, the Canadian government ratified the Kyoto Protocol. The Kyoto Protocol will have no impact on TransAlta's U.S., Mexican or Australian operations as these countries have not ratified the Protocol. TransAlta is not able to estimate the full impact the Protocol will have on its Canadian operations, as the Canadian government has not yet established an implementation plan. However, the PPAs for TransAlta's coal-fired plants in Alberta contain 'Change in Law' provisions that provide an opportunity to recover compliance costs from the PPA customers. As a member of the Canadian Clean Power Coalition, TransAlta, along with its peers, is exploring other means to reduce greenhouse gas emissions, including the purchase of offset credits. The acquisition of Vision Quest and its prospects for further developments has resulted in the additional amounts of zero-emissions facilities consistent with the strategy of the corporation. Since 1990 the corporation has reduced net emissions by 18 per cent and is on track to reach zero net emissions by 2024.

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## TRANSALTACORPORATION

## QUARTERLY REPORT 2002

## TRANSALTACORPORATION

## CONSOLIDATED STATEMENTS OF EARNINGS AND RETAINED EARNINGS

(in millions of Canadian dollars except per share amounts)

	3 months ended Dec. 31		Year ended Dec. 31	
	Unaudited 2002	2001	Unaudited 2002	Audited* 2001
<b>Revenues</b>	<b>\$517.6</b>	\$ 434.4	<b>\$ 1,723.9</b>	\$ 2,319.4
Fuel and purchased power	<b>(226.9)</b>	(246.4)	<b>(703.6)</b>	(1,230.6)
<b>Gross margin</b>	<b>290.7</b>	188.0	<b>1,020.3</b>	1,088.8

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**Operating expenses**

Operations, maintenance and administration	<b>135.1</b>	89.4	<b>420.5</b>	392.2
Depreciation and amortization	<b>62.5</b>	51.8	<b>219.0</b>	191.2
Asset impairment and equipment cancellation charges <i>(Note 6)</i>	<b>152.5</b>	2.7	<b>152.5</b>	118.8
Taxes, other than income taxes	<b>7.6</b>	4.6	<b>27.4</b>	18.7

	<b>357.7</b>	148.5	<b>819.4</b>	720.9
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**Operating income (loss)**

Other income	<b>1.0</b>	1.2	<b>0.1</b>	1.5
Foreign exchange gain	<b>0.9</b>	2.9	<b>1.2</b>	0.8
Net interest expense	<b>(24.0)</b>	(12.4)	<b>(82.7)</b>	(88.1)

**Earnings (loss) from continuing operations before regulatory**

<b>decisions, income taxes and non-controlling interests</b>	<b>(89.1)</b>	31.2	<b>119.5</b>	282.1
Prior period regulatory decisions <i>(Note 10)</i>	-	11.0	<b>(3.3)</b>	11.0

**Earnings (loss) from continuing operations before income taxes**

<b>and non-controlling interests</b>	<b>(89.1)</b>	42.2	<b>116.2</b>	293.1
Income tax expense (recovery)	<b>(35.1)</b>	0.5	<b>18.1</b>	89.9
Non-controlling interests	<b>5.6</b>	5.0	<b>20.1</b>	20.6

**Earnings (loss) from continuing operations**

Earnings from discontinued operations <i>(Note 3)</i>	-	13.3	<b>12.8</b>	45.1
Gain on disposal of discontinued operations <i>(Note 3)</i>	<b>10.0</b>	-	<b>120.0</b>	-

**Net earnings (loss)**

Preferred securities distributions, net of tax	<b>4.7</b>	3.5	<b>20.9</b>	13.1
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<b>Net earnings (loss) applicable to common shareholders</b>	<b>\$(54.3)</b>	\$ 46.5	<b>\$ 189.9</b>	\$ 214.6
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<b>Common share dividends</b>	<b>(42.3)</b>	(41.7)	<b>(169.0)</b>	(168.4)
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<b>Adjustment arising from normal course issuer bid</b>	-	(14.1)	<b>(27.0)</b>	(34.8)
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**Retained earnings**

Opening balance	<b>928.8</b>	847.6	<b>838.3</b>	826.9
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Closing balance	<b>\$832.2</b>	\$ 838.3	<b>\$ 832.2</b>	\$ 838.3
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**Weighted average common shares outstanding in the period**

	<b>169.3</b>	168.9	<b>169.6</b>	168.9
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**Basic earnings (loss) per share**

Continuing operations	<b>\$(0.38)</b>	\$ 0.19	<b>\$ 0.34</b>	\$ 1.00
Earnings from discontinued operations	-	0.08	<b>0.07</b>	0.27

**Net earnings (loss) from operations**

Gain on disposal of discontinued operations, net of tax	<b>0.06</b>	-	<b>0.71</b>	-
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<b>Net earnings (loss)</b>	<b>\$(0.32)</b>	\$ 0.27	<b>\$ 1.12</b>	\$ 1.27
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<b>Diluted earnings (loss) per share</b>				
Earnings (loss) from continuing operations	<b>\$(0.38)</b>	\$ 0.19	<b>\$ 0.34</b>	\$ 0.98
Earnings from discontinued operations	-	0.08	<b>0.07</b>	0.27
<b>Net earnings (loss) from operations</b>				
	<b>(0.38)</b>	0.27	<b>0.41</b>	1.25
Gain on disposal of discontinued operations, net of tax	<b>0.06</b>	-	<b>0.71</b>	-
<b>Net earnings (loss)</b>				
	<b>\$(0.32)</b>	\$ 0.27	<b>\$ 1.12</b>	\$ 1.25

See accompanying notes.

\* Derived from the audited Dec. 31, 2001 consolidated financial statements.

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TRANSALTACORPORATION

QUARTERLY REPORT 2002

**TRANSALTACORPORATION  
CONSOLIDATED STATEMENTS OF CASH FLOWS**

(in millions of Canadian dollars)

	3 months ended Dec. 31		Year ended Dec. 31	
	<b>Unaudited 2002</b>	2001	<b>Unaudited 2002</b>	Audited* 2001
<b>Operating activities</b>				
Net earnings	\$ (49.6)	\$ 50.0	\$ 210.8	\$ 227.7
Depreciation and amortization	79.7	82.6	314.8	312.3
Asset impairment and equipment cancellation charges	152.5	-	152.5	66.5
Non-controlling interests	5.6	5.0	20.1	20.6
Loss (gain) on sale of property, plant and equipment	12.3	2.1	15.6	(5.4)
Site restoration costs incurred	(3.5)	(4.6)	(15.6)	(14.8)
Future income taxes (recovery)	(43.8)	33.2	(60.4)	39.9
Unrealized (gain) loss from energy marketing activities	(10.9)	6.0	(5.9)	(6.3)
Gain on disposal of Transmission operation (Note 3)	(10.0)	-	(120.0)	-
Other non-cash items	(17.2)	(0.7)	(24.8)	9.5
	<b>115.1</b>	173.6	<b>487.1</b>	650.0
Change in non-cash operating working capital balances	<b>74.4</b>	(41.9)	<b>(49.4)</b>	65.6
	<b>189.5</b>	131.7	<b>437.7</b>	715.6

**Investing activities**

Additions to property, plant and equipment	<b>(194.6)</b>	(419.0)	<b>(945.8)</b>	(1,246.5)
Acquisitions (Note 2)	<b>(40.1)</b>	-	<b>(40.1)</b>	(9.8)
Proceeds on sale of property, plant and equipment to Limited Partnership	-	35.0	-	35.0
Disposals (Note 3)	-	-	<b>818.0</b>	-
Proceeds on sale of property, plant and equipment	<b>2.3</b>	0.2	<b>2.3</b>	201.6
Long-term receivables	<b>(5.4)</b>	20.3	<b>165.3</b>	(46.3)
Long-term investments (Note 5)	-	-	<b>(6.1)</b>	-
Deferred charges and other	<b>(23.2)</b>	(2.6)	<b>(29.8)</b>	(10.9)
<b>Cash flow used in investing activities</b>	<b>(261.0)</b>	(366.1)	<b>(36.2)</b>	(1,076.9)

**Financing activities**

Net increase (decrease) in short-term debt	<b>289.3</b>	(7.8)	<b>(247.1)</b>	61.9
Issuance of long-term debt	-	125.0	<b>611.3</b>	789.9
Repayment of long-term debt	<b>(149.4)</b>	(0.8)	<b>(454.5)</b>	(292.7)
Redemption of preferred shares of a subsidiary	-	-	-	(122.1)
Issuance of common shares	-	0.1	<b>1.8</b>	14.1
Redemption of common shares	-	(14.2)	<b>(49.9)</b>	(44.4)
Distributions on preferred securities	<b>(8.2)</b>	(6.2)	<b>(34.9)</b>	(23.4)
Dividends on common shares	<b>(29.5)</b>	(28.7)	<b>(115.5)</b>	(149.6)
Net proceeds on issuance of preferred securities	-	169.4	-	169.4
Dividends to subsidiary's non-controlling preferred shareholders	-	-	-	(8.3)
Distributions to subsidiary's non-controlling limited partner	<b>(5.5)</b>	(6.0)	<b>(24.5)</b>	(26.3)
Deferred financing charges and other	-	0.1	<b>(7.6)</b>	0.2
<b>Cash flow from (used in) financing activities</b>	<b>96.7</b>	230.9	<b>(320.9)</b>	368.7
<b>Cash flow from (used in) operating, investing and financing activities</b>	<b>25.2</b>	(3.5)	<b>80.6</b>	7.4
<b>Effect of translation on foreign currency cash</b>	<b>(2.5)</b>	4.0	<b>0.7</b>	0.8

**Increase in cash and cash equivalents**  
**Cash and cash equivalents, beginning of period**

<b>Increase in cash and cash equivalents</b>	<b>22.7</b>	0.5	<b>81.3</b>	8.2
<b>Cash and cash equivalents, beginning of period</b>	<b>120.6</b>	61.5	<b>62.0</b>	53.8
<b>Cash and cash equivalents, end of period</b>	<b>\$ 143.3</b>	\$ 62.0	<b>\$ 143.3</b>	\$ 62.0

See accompanying notes.

\* Derived from the audited Dec. 31, 2001 consolidated financial statements.

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**TRANSALTACORPORATION**  
**CONSOLIDATED BALANCE SHEETS**

(in millions of Canadian dollars)

	<b>Dec. 31,</b>		Dec. 31,
	<b>2002</b>		2001
	<b>Unaudited</b>		Audited*
<b>ASSETS</b>			
<b>Current assets</b>			
Cash and cash equivalents	\$ 143.3	\$	62.0
Accounts receivable and other	468.4		625.3
Price risk management assets (Note 4)	157.8		137.6
Future income tax assets	18.7		16.9
Income taxes receivable	111.5		128.3
Materials and supplies at average cost	112.7		85.5
	<b>1,012.4</b>		1,055.6
<b>Investments (Note 5)</b>	<b>32.2</b>		37.3
<b>Long-term receivables (Note 7)</b>	<b>39.9</b>		221.4
<b>Property, plant and equipment (Note 3)</b>			
Cost	8,124.9		8,766.7
Accumulated depreciation	(2,089.8)		(2,671.9)
	<b>6,035.1</b>		6,094.8
<b>Goodwill (Note 2)</b>	<b>56.5</b>		29.3
<b>Future income tax assets</b>	<b>72.2</b>		15.6
<b>Price risk management assets (Note 4)</b>	<b>60.7</b>		71.3
<b>Other assets</b>	<b>110.6</b>		81.1
<b>Total assets</b>	<b>\$ 7,419.6</b>	\$	7,606.4
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>			
<b>Current liabilities</b>			
Short-term debt	\$ 290.0	\$	537.2
Accounts payable and accrued liabilities	472.2		627.5
Price risk management liabilities (Note 4)	173.8		114.1
Future income tax liabilities	17.1		11.8
Dividends payable	42.9		42.8
Current portion of long-term debt (Note 8)	355.4		104.3
	<b>1,351.4</b>		1,437.7
<b>Long-term debt (Note 8)</b>	<b>2,351.2</b>		2,406.8
<b>Deferred credits and other long-term liabilities</b>	<b>540.2</b>		560.5

<b>Future income tax liabilities</b>	<b>371.9</b>	409.1
<b>Price risk management liabilities</b> (Note 4)	<b>50.6</b>	69.0
<b>Non-controlling interests</b>	<b>263.0</b>	281.0
<b>Preferred securities</b>	<b>451.7</b>	452.6
<b>Common shareholders' equity</b>		
Common shares (Note 9)	<b>1,226.2</b>	1,170.9
Retained earnings	<b>832.2</b>	838.3
Cumulative translation adjustment	<b>(18.8)</b>	(19.5)
	<b>2,039.6</b>	1,989.7
<b>Total liabilities and shareholders' equity</b>	<b>\$ 7,419.6</b>	\$ 7,606.4

**Contingencies** (Note 11)

See accompanying notes.

\* Derived from the audited Dec. 31, 2001 consolidated financial statements.

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## TRANSALTACORPORATION

## QUARTERLYREPORT2002

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## (UNAUDITED)

(Tabular amounts in millions of Canadian dollars, except as otherwise noted)

## 1. ACCOUNTING POLICIES

These unaudited interim consolidated financial statements do not include all of the disclosures included in the corporation's annual consolidated financial statements. Accordingly, these unaudited interim consolidated financial statements should be read in conjunction with the corporation's most recent annual consolidated financial statements.

The accounting policies used in the preparation of these unaudited interim consolidated financial statements conform with those used in the corporation's most recent annual consolidated financial statements, except for accounting for goodwill, stock-based compensation, exchange gains and losses on translation of long-term foreign currency denominated monetary items, impairment of long-lived assets and the presentation of energy-trading activities.

Effective Jan. 1, 2002, the corporation prospectively adopted the new Canadian Institute of Chartered Accountants (CICA) standard for goodwill and other intangibles. Under the new standard, goodwill and certain intangibles are no longer subject to amortization, but are instead tested for impairment at least annually. The adoption of this standard resulted in the reclassification of \$29.3 million from acquired intangibles to goodwill, which will no longer be subject to amortization under the new standard.

There was no impairment of goodwill upon adoption of this standard, nor was there an impairment at Dec. 31, 2002.

Net income and earnings per share for the three and twelve months ended Dec. 31, 2001 adjusted to exclude the amortization of the above amount are as follows:

3 months ended Dec. 31, 2001	Year ended Dec. 31, 2001
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Reported net earnings applicable to common shareholders	\$	46.5	\$	214.6
Amortization of acquired intangibles		2.3		7.7
Adjusted net earnings applicable to common shareholders	\$	48.8	\$	222.3
Reported basic earnings per share	\$	0.27	\$	1.27
Amortization of acquired intangibles per share		0.01		0.05
Adjusted basic earnings per share	\$	0.28	\$	1.32
Reported diluted earnings per share	\$	0.27	\$	1.25
Amortization of acquired intangibles per share		0.01		0.05
Adjusted diluted earnings per share	\$	0.28	\$	1.30

On Jan. 1, 2002, the corporation retroactively adopted the new CICA standard for stock-based compensation. The new standard requires that stock-based payments to non-employees, direct awards of stock and awards that call for settlement in cash or other assets be accounted for using the fair value method of accounting. The fair value method is encouraged for other stock-based compensation plans, but other methods of accounting, such as the intrinsic value method, are permitted. Under the fair value method, compensation expense is measured at the grant date and recognized over the service period. Under the intrinsic value method, compensation expense is determined as the difference between the market price of the underlying stock and the exercise price of the equity instrument granted. If the intrinsic value method is used, disclosure is made of earnings and per share amounts as if the fair value method had been used. The corporation has elected to use the intrinsic value method of accounting for its fixed stock option plans and its performance stock option plan. Accordingly, no compensation cost has been recognized for these plans. The following table provides pro forma measures of net earnings (loss) and earnings (loss) per share had compensation expense been recognized based on the estimated fair value of the options on the grant date in accordance with the fair value method of accounting for stock-based compensation:

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TRANSALTACORPORATION

QUARTERLY REPORT 2002

	3 months ended Dec. 31		Year ended Dec. 31	
	2002	2001	2002	2001
Reported net earnings (loss) applicable to common shareholders	<b>\$(54.3 )</b>	\$ 46.5	<b>\$ 189.9</b>	\$ 214.6
Compensation expense	<b>1.0</b>	0.5	<b>3.7</b>	2.0
Pro forma net earnings (loss) applicable to common shareholders	<b>\$(55.3 )</b>	\$ 46.0	<b>\$ 186.2</b>	\$ 212.6
Reported basic earnings (loss) per share	<b>\$(0.32 )</b>	\$ 0.27	<b>\$ 1.12</b>	\$ 1.27
Compensation expense per share	<b>0.01</b>	-	<b>0.02</b>	0.01
Pro forma basic earnings (loss) per share	<b>\$(0.33 )</b>	\$ 0.27	<b>\$ 1.10</b>	\$ 1.26



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Reported diluted earnings (loss) per share	<b>\$(0.32)</b>	\$ 0.27	<b>\$ 1.12</b>	\$ 1.25
Compensation expense per share	<b>0.01</b>	-	<b>0.02</b>	0.01
<hr/>				
Pro forma diluted earnings (loss) per share	<b>\$(0.33)</b>	\$ 0.27	<b>\$ 1.10</b>	\$ 1.24

Options were granted only in the first quarter of 2002. The estimated fair value of these stock options was determined using the binomial model using the following assumptions, resulting in a weighted-average fair value of \$4.25 per option (2001 - \$4.35):

	<b>2002</b>	2001
Risk-free interest rate	<b>5.9%</b>	5.4%
Expected hold period to exercise (years)	<b>7.0</b>	7.0
Volatility in the price of the corporation's shares	<b>28.3%</b>	28.2%

The accounting treatment for the corporation's performance share ownership plan remains unchanged from the year ended Dec. 31, 2001. Under this plan, compensation expense recognized in the three and twelve months ended Dec. 31, 2002 was \$1.0 million and \$5.3 million, respectively (2001 - \$1.2 million and \$6.6 million, respectively). Compensation expense is included in operations, maintenance and administration (OM&A) in the statements of earnings. Effective Jan. 1, 2003, TransAlta has elected to account for stock-based compensation in accordance with the fair value method, and will expense stock-based compensation in respect of stock options on a prospective basis.

The CICA amended its standard on foreign currency translation effective Jan. 1, 2002. The changes require that translation gains and losses arising on long-term foreign currency denominated monetary items be included in income in the current period. Previously, these gains and losses were to be amortized over the life of the related item. As TransAlta designates long-term foreign currency denominated items as hedges of net investments in foreign operations, all gains and losses arising on the translation of these items are deferred and included in the cumulative translation adjustment account in shareholders' equity, therefore this amendment has no impact on TransAlta.

The CICA has amended its standard on the recognition, measurement, and disclosure of the impairment of long-lived assets. This standard is effective April 1, 2003 and requires that an impairment loss be recognized when the carrying amount of a long-lived asset exceeds the sum of the undiscounted cash flows expected from its use and eventual disposition. The impairment loss is measured as the amount that the long-lived asset's carrying value exceeds its fair value. TransAlta early adopted this standard in the fourth quarter of 2002. In accordance with the standard, the impairment calculation for the Wabamun plant resulted in the recognition of an impairment loss of \$110.0 million, which is included in asset impairment and equipment cancellation charges in the statements of earnings.

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### TRANSALTACORPORATION

#### QUARTERLYREPORT2002

In the third quarter of 2002, in response to changes in accounting standards in the U.S. with respect to energy trading activities, the corporation has adopted a policy that all gains and losses on energy trading contracts be shown in the statement of earnings. Consistent with these recommendations, the corporation has chosen to disclose the gross transaction volumes of those energy trading contracts that are physically settled.

TransAlta's results are seasonal in nature due to the nature of the electricity market and related fuel costs.

## 2 . A C Q U I S I T I O N S

On Dec. 6, 2002, the corporation completed a step acquisition of Vision Quest Windelectric Inc. (Vision Quest). The initial steps resulted in 41 per cent ownership of Vision Quest for \$13.5 million, accounted for using the equity method. Book values approximated fair values. The final step brought TransAlta's ownership to 100 per cent and TransAlta's total investment in Vision Quest to \$68.8 million. The results of Vision Quest's operations have been included in the corporate segment of the consolidated financial statements since the date of acquisition. Vision Quest owns and operates 67 wind power turbine power plants with a total capacity of 44 MW with a further 37.5 MW under construction.

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The aggregate purchase price includes the previous investments of \$13.5 million, plus \$21.3 million of cash and 745,791 common shares valued at \$14.2 million. In addition, a loan of \$19.8 million was previously advanced to Vision Quest. The value of the common shares issued was determined based on the average market price of TransAlta's common shares for the five days before and after the terms of the acquisition were agreed to and announced. 136,287 of the shares will be issued over the next three years.

The following table summarizes the estimated fair value of the assets acquired and liabilities assumed at the date of acquisition.

Due to the timing of the purchase, it was impractical to complete the allocations process satisfactory without causing undue delay in issuing the financial statements for the period in which the combination occurred. Therefore, the purchase price allocation was prepared based on the best allocations that could be made in the time available and, if necessary, the allocations in the purchase equation may be adjusted when the process is completed in the first quarter of 2003.

### Net assets acquired at assigned values:

Working capital, including cash of \$8.2 million	\$	6.5
Property, plant and equipment		70.1
Goodwill		27.2
Power Purchase Arrangement		2.5
Short-term debt		(32.2)
Future income tax liability		(4.7)
Interest rate swaps		(0.6)
<hr/>		
Total	\$	68.8

### Consideration:

Initial investments	\$	13.5
Cash, including previous advances of \$19.8 million		41.1
Common shares		14.2
<hr/>		
Total	\$	68.8

On Dec. 6, 2002, the corporation purchased the remaining 15 per cent interest in the Southern Cross Energy Partnership, located in western Australia, for AUD\$8.5 million (Cdn\$7.2 million). At the time of acquisition, book values approximated fair values.

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## TRANSALTACORPORATION

### QUARTERLY REPORT 2002

### 3. DISCONTINUED OPERATIONS

On July 4, 2001, the corporation signed a purchase and sale agreement for the disposal of its Transmission operation. Regulatory approval was received on March 28, 2002. On April 29, 2002, the Transmission operation was sold for proceeds of \$820.7 million, of which \$818.0 million has been collected. The proceeds excluded accounts receivable of \$31.7 million, which were retained and collected by TransAlta, and accounts payable of \$4.4 million. The disposal resulted in a final gain on sale of \$120.0 million (\$0.71 per common share), net of income taxes of \$32.9 million. The previously reported gain included a number of estimates, therefore the gain was adjusted in the fourth quarter of 2002 to reflect agreed working capital adjustments and actual amounts paid and received.

For reporting purposes, the results of the Transmission operation have been presented as discontinued operations in the statement of earnings.

	<b>2002</b>	2001
<i>3 months ended Dec. 31</i>	<b>Transmission</b>	Transmission

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Revenues		\$	-	\$	42.8
Operating expenses			-		(19.1)
Operating income			-		23.7
Net interest expense			-		(0.6)
Earnings before income taxes			-		23.1
Income taxes			-		9.8
Earnings before gain on disposal			-		13.3
Gain on disposal			<b>10.0</b>		-
Earnings from discontinued operations		\$	<b>10.0</b>	\$	13.3

Year ended Dec. 31	2002		2001		Total
	Transmission	Transmission	Edmonton Composter		
Revenues	\$ <b>55.8</b>	\$ 171.1	\$ 6.6	\$ 177.7	
Operating expenses	<b>(30.8)</b>	(84.6)	(5.4)	(90.0)	
Operating income	<b>25.0</b>	86.5	1.2	87.7	
Net interest expense	<b>(2.4)</b>	(9.7)	-	(9.7)	
Earnings before income taxes	<b>22.6</b>	76.8	1.2	78.0	
Income taxes	<b>9.8</b>	32.4	0.5	32.9	
Earnings before gain on disposal	<b>12.8</b>	44.4	0.7	45.1	
Gain on disposal	<b>120.0</b>	--	-	-	
Earnings from discontinued operations	\$ <b>132.8</b>	\$ 44.4	\$ 0.7	\$ 45.1	

At Dec. 31, 2002, all of the corporation's discontinued operations had been sold. At Dec. 31, 2001, all of the corporation's discontinued operations had been sold with the exception of the Transmission operation. Balance sheet amounts are as follows:

	Dec. 31, 2002	Dec. 31, 2001
Current assets	\$ -	\$ 36.1
Capital assets	-	637.5
Other assets	-	3.3
Current liabilities	-	(15.5)
Net assets	\$ -	\$ 661.4

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## TRANSALTACORPORATION

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## 4. PRICE RISK MANAGEMENT ASSETS AND LIABILITIES

The Energy Marketing group uses energy derivatives, including physical and financial swaps, forwards and options to optimize returns from assets, earn trading revenues and gain market information. Energy contracts that meet the definition of a derivative in FASB Statement 133, *Accounting for Derivative Instruments and Hedging Activities*, are accounted for at fair value in accordance with Canadian and U.S. generally accepted accounting principles (GAAP). Derivatives are used to hedge the corporation's exposure to changes in electricity and natural gas prices. Under Canadian GAAP, settlement accounting is used for hedging activities if certain criteria are met. Under U.S. GAAP, hedging activities are accounted for in accordance with FASB Statement 133.

Energy Marketing's price risk management assets and liabilities represent the fair value of unsettled (unrealized) trading transactions. With the exception of transmission contracts, the fair value of all energy trading activities is based on quoted market prices. The fair value of physical transmission contracts is based on quoted market prices and a spread option valuation model. The fair value of financial transmission contracts is based upon statistical analysis of historical data.

	Dec. 31, 2002	Dec. 31, 2001
<b>Price risk management assets</b>		
Current	\$ 157.8	\$ 137.6
Long-term	60.7	71.3
<b>Price risk management liabilities</b>		
Current	(173.8)	(114.1)
Long-term	(50.6)	(69.0)
	\$ (5.9)	\$ 25.8

The following table illustrates movements in the fair value of the corporation's price risk assets and liabilities during the year ended Dec. 31, 2002:

Fair value of net price risk management assets outstanding at Dec. 31, 2001	\$ 25.8
Fair value of new contracts entered into during the period	(2.7)
Changes in fair values attributable to market price and other market changes	7.6
Contracts realized or settled during the period	(36.6)
Changes in fair values attributable to changes in valuation techniques and assumptions	-
Fair value of net price risk management liabilities outstanding at Dec. 31, 2002	\$ (5.9)

The source of the valuations of the above contracts and maturities over each of the next five calendar years and thereafter is as follows:

	2003	2004	2005	2006	2007	2008 and thereafter	Total
Prices actively quoted	\$ (17.6)	\$ 3.3	\$ 3.2	\$ 2.1	\$ 1.5	\$ -	\$ (7.5)
Prices based on models	1.6	-	-	-	-	-	1.6
Asset (liability)	\$ (16.0)	\$ 3.3	\$ 3.2	\$ 2.1	\$ 1.5	\$ -	\$ (5.9)

## TRANSALTA CORPORATION

## QUARTERLY REPORT 2002

**5. INVESTMENTS**

In January 2002, an additional \$2.9 million was invested in Vision Quest. In December 2002, the corporation purchased the remaining interest in Vision Quest as described in *Note 2*.

In April 2002, an additional \$2.5 million was invested in a distributed generation company. This investment is accounted for using the equity method.

In April 2002, an initial \$0.2 million was invested in a biomass generation company. An additional \$0.5 million was invested in September 2002. The investment is accounted for using the cost method.

A foreign exchange revaluation of \$1.9 million occurred during the twelve months ended Dec. 31, 2002 on the investment in the Australian gas transmission pipeline.

**6. ASSET IMPAIRMENT AND EQUIPMENT CANCELLATION CHARGES**

After a detailed engineering assessment, a review of environmental issues and a review of short- and long-term market forecasts, the corporation decided to implement a phased decommissioning of its 569 MW coal-fired Wabamun facility in November 2002. As a result of this decision, the corporation recorded an impairment charge of \$110.0 million during the quarter. The impairment charge was calculated as the excess of carrying value over fair value. The fair value of the facility was determined by estimating the present value of future cash flows.

In November 2002, the corporation cancelled orders for four natural gas turbines and as a result recorded a cancellation charge of \$42.5 million for contract termination costs. The costs consist of progress payments made to date.

In September 2001, the corporation monetized its investment in the 154 MW Pierce Power plant, resulting in the recognition of revenue of \$121.8 million, an impairment charge of \$66.5 million and \$52.3 million in anticipated future operating costs.

**7. LONG-TERM RECEIVABLES**

In August 2002, the remaining \$180.3 million due from Aquila Networks Canada (formerly UtiliCorp Networks Canada) that arose from the August 2000 sale of the discontinued Alberta Distribution and Retail operation was collected in full.

The net California accounts receivable of US\$24.2 million has been reclassified to long-term receivables, as collection is no longer expected in 2003, although ultimate collection of the net receivable is expected.

On Dec. 12, 2002, a U.S. Federal Energy Regulatory Commission (FERC) Administrative Law Judge issued proposed findings of fact that TransAlta be entitled to receive approximately US\$44.0 million for electricity sales to California. However, FERC has proposed further adjustments in respect of power and gas prices, which could result in further adjustments to the amount to be received by TransAlta. Until a final ruling is made with respect to these issues, TransAlta will maintain the provision for these receivables.

**8. LONG-TERM DEBT**

On June 20, 2002, the corporation issued debt of US\$300.0 million under a US\$1.0 billion shelf prospectus filed

May 14, 2002. The notes are unsecured and bear interest at 6.75 per cent, and mature on July 15, 2012. Net proceeds on the issuance were \$456.9 million.

TRANSALTACORPORATION

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**9 . C O M M O N S H A R E S I S S U E D A N D O U T S T A N D I N G**

TransAlta Corporation is authorized to issue an unlimited number of voting common shares without nominal or par value. At Dec. 31, 2002, the corporation had 169.8 million (Dec. 31, 2001 - 168.3 million) common shares issued and outstanding plus outstanding employee stock options to purchase an additional 3.2 million shares (Dec. 31, 2001 - 2.8 million).

In February 2002, TransAlta announced a normal course issuer bid to repurchase up to 3.0 million common shares for cancellation. For the year ended Dec. 31, 2002, 2.0 million common shares had been repurchased under the normal course issuer bid.

On Dec. 6, 2002, the corporation issued 609,504 common shares as a portion of the aggregate purchase price of Vision Quest (Note 2).

**1 0 . . P R I O R P E R I O D R E G U L A T O R Y D E C I S I O N S**

Financial results for 2002 were affected by Alberta Energy and Utilities Board (EUB) decisions related to other reporting periods. The impact of such regulatory decisions is recorded when the effect of such decisions is known, without adjustment to the financial statements of prior periods.

On April 16, 2002, the EUB rendered a negative decision of \$3.3 million pre-tax with respect to TransAlta's hydro bidding strategy in 2000.

In December 2001, the EUB ruled that the Wabamun unit four outage qualified for relief under the Temporary Suspension Regulation (TSR) and ordered that TransAlta would receive \$11.0 million (\$7.0 million after-tax) to compensate the corporation for obligation payments incurred in 2000 as a result of the outage.

**1 1 . . C O N T I N G E N C I E S**

In August 2000, a single thermal generating unit at the Wabamun plant was shut down due to safety concerns related to possible corrosion fatigue cracks within the waterwall tubing of its boiler. Repairs were completed late in the second quarter of 2001 and the unit returned to service in June 2001.

Since Jan. 1, 2001, the unit has been subject to the terms of a power purchase arrangement (PPA). Under the PPA's *force majeure* article, the corporation is not obligated to supply electricity during the period of repair, subject to confirmation by the administrator of the PPAs. Had such confirmation not occurred, the corporation would have been obligated to pay a penalty equal to the cost of obtaining an alternative source of electricity to fulfill its PPA supply obligations during the affected period. The *force majeure* decision went to arbitration in July 2001. On May 23, 2002, the arbitrators confirmed in their ruling that the outage qualified as a *force majeure* event, but also ruled that the corporation should have returned the unit to service more quickly. As a result of the decision, the corporation was required to pay \$38.9 million plus interest of \$2.7 million, all pre-tax. The payment was recorded as reduction to revenue.

On May 8, 2002, FERC requested that 150 sellers of wholesale electricity and ancillary services to the California electricity market, including TransAlta, respond to questions regarding their trading strategies in California during 2000 and 2001. TransAlta has responded to the FERC request and believes it operated in accordance with all applicable laws, rules, regulations and tariffs.

On May 21 and 22, 2002, FERC issued two additional requests for information regarding 'round-trip' trading activities, to which TransAlta responded, stating that the corporation does not believe it participated in any round-trip trades during 2000 and 2001. In addition, Reliant Energy Inc. issued a statement that it engaged in round-trip trades in 1999 with Merchant Energy Group of the Americas, Inc. (MEGA). TransAlta acquired an initial 50 per cent interest in MEGA in June 2000, and acquired the remaining 50 per cent in June 2001. TransAlta contends that no round-trip trading occurred between Reliant Energy Inc. and MEGA during any period in which TransAlta had an ownership interest in MEGA. TransAlta will continue to cooperate with the regulators and supply all information requested.

## TRANSALTACORPORATION

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On May 30, 2002, the California Attorney General's Office (CAGO) filed civil complaints in the state court of California against eight additional wholesale power companies, including TransAlta. The complaint alleges violations of California's unfair business practices law in connection with rates charged for wholesale electricity sales. TransAlta believes that it has complied with applicable laws in regard to this complaint. In particular, the company is of the view that the basis of the complaint is a matter of federal rather than state jurisdiction. FERC has previously rejected allegations made by CAGO that TransAlta's subsidiaries violated rate filing requirements. On June 26, 2002, TransAlta filed a Notice of Motion to dismiss the complaint.

On Sept. 9, 2002, the Commodities Futures Trading Commission requested information on similar issues. TransAlta has provided the requested information.

On Dec. 16 and 20, 2002, two class action lawsuits on behalf of all persons and businesses in the states of Oregon and Washington were initiated in respect of alleged unlawful practices in the purchase and sale of wholesale energy. TransAlta believes these are without merit and will vigorously defend its actions. No amount has been accrued in these financial statements as neither the amount of the claim nor the outcome was determinable at the reporting date.

On Dec. 16, 2002, the Canadian government ratified the Kyoto Protocol. The Kyoto Protocol will have no impact on TransAlta's U.S., Mexican or Australian operations as these countries have not ratified the Protocol. TransAlta is not able to estimate the full impact the Protocol will have on its Canadian operations, as the Canadian government has not yet established an implementation plan. However, the PPAs for TransAlta's coal-fired plants in Alberta contain 'Change in Law' provisions that provide an opportunity to recover compliance costs from the PPA customers. As a member of the Canadian Clean Power Coalition, TransAlta, along with its peers, is exploring other means to reduce greenhouse gas emissions, including the purchase of offset credits. The acquisition of Vision Quest and its prospects for further development has resulted in additional amounts of zero-emissions facilities consistent with the strategy of the corporation. Since 1990, the corporation has reduced net emissions in Canada by 18 per cent and is on track to reach zero net emissions by 2024.

## 12 .. COMPARATIVE FIGURES

Certain comparative figures have been reclassified to conform with the current period's presentation.

## TRANSALTACORPORATION

## QUARTERLYREPORT2002

## 13 .. SEGMENTED DISCLOSURES

Effective Jan. 1, 2002, the Generation and Independent Power Projects business segments were combined into one Generation segment to reflect changes in TransAlta's organizational structure. Prior period amounts have been reclassified.

## I. Earnings information

<b>3 months ended Dec. 31, 2002</b>	Generation	Unaudited		
		Energy Marketing	Corporate	Total
<b>Revenues</b>	\$ 498.7	\$ 992.4	\$ 1.0	\$ 1,492.1
Trading purchases	-	(974.5)	-	(974.5)

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<b>Net segment revenues</b>	<b>498.7</b>	<b>17.9</b>	<b>1.0</b>	<b>517.6</b>
Fuel and purchased power	(226.9)	-	-	(226.9)
<b>Gross margin</b>	<b>271.8</b>	<b>17.9</b>	<b>1.0</b>	<b>290.7</b>
Operations, maintenance and administration	115.3	3.6	16.2	135.1
Depreciation and amortization	57.4	0.5	4.6	62.5
Asset impairment and equipment cancellation charges (Note 6)	152.5	-	-	152.5
Taxes, other than income taxes	7.6	-	-	7.6
<b>EBIT before corporate allocations</b>	<b>(61.0)</b>	<b>13.8</b>	<b>(19.8)</b>	<b>(67.0)</b>
Corporate allocations	(18.1)	(2.3)	20.4	-
<b>EBIT</b>	<b>\$ (79.1)</b>	<b>\$ 11.5</b>	<b>\$ 0.6</b>	<b>(67.0)</b>
Other income				1.0
Foreign exchange gain				0.9
Net interest expense				(24.0)
<b>Earnings from continuing operations before income taxes and non-controlling interests</b>				<b>\$ (89.1)</b>

3 months ended Dec. 31, 2001		Unaudited Energy Marketing	Corporate	Total
<b>Revenues</b>	\$ 431.8	\$ 526.9	\$ -	\$ 958.7
Trading purchases	-	(524.3)	-	(524.3)
<b>Net segment revenues</b>	431.8	2.6	-	434.4
Fuel and purchased power	(246.4)	-	-	(246.4)
<b>Gross margin</b>	185.4	2.6	-	188.0
Operations, maintenance and administration	68.7	1.6	19.1	89.4
Depreciation and amortization	41.4	4.0	6.4	51.8
Asset impairment and equipment cancellation charges (Note 6)	2.7	-	-	2.7
Taxes, other than income taxes	4.6	-	-	4.6
Prior period regulatory decisions (Note 10)	(11.0)	-	-	(11.0)
<b>EBIT before corporate allocations</b>	79.0	(3.0)	(25.5)	50.5
Corporate allocations	(23.6)	(1.9)	25.5	-
<b>EBIT</b>	\$ 55.4	\$ (4.9)	\$ -	50.5
Other income				1.2
Foreign exchange gain				2.9
Net interest expense				(12.4)
<b>Earnings from continuing operations before income taxes and non-controlling interests</b>				<b>\$ 42.2</b>



## TRANSALTACORPORATION

## QUARTERLYREPORT2002

## Earnings information

Year ended Dec. 31, 2002	Generation	Unaudited		Total
		Energy Marketing	Corporate	
<b>Revenues</b>	\$ 1,673.9	\$ 3,703.8	\$ 1.0	\$ 5,378.7
Trading purchases	-	(3,654.8)	-	(3,654.8)
<b>Net segment revenues</b>	<b>1,673.9</b>	<b>49.0</b>	<b>1.0</b>	<b>1,723.9</b>
Fuel and purchased power	(703.6)	-	-	(703.6)
<b>Gross margin</b>	<b>970.3</b>	<b>49.0</b>	<b>1.0</b>	<b>1,020.3</b>
Operations, maintenance and administration	346.3	15.1	59.1	420.5
Depreciation and amortization	196.3	2.5	20.2	219.0
Asset impairment and equipment cancellation charges (Note 6)	152.5	-	-	152.5
Taxes, other than income taxes	27.3	0.1	-	27.4
Prior period regulatory decisions (Note 10)	3.3	-	-	3.3
<b>EBIT before corporate allocations</b>	<b>244.6</b>	<b>31.3</b>	<b>(78.3)</b>	<b>197.6</b>
Corporate allocations	(70.6)	(8.3)	78.9	-
<b>EBIT</b>	<b>\$ 174.0</b>	<b>\$ 23.0</b>	<b>\$ 0.6</b>	<b>197.6</b>
Other income				0.1
Foreign exchange gain				1.2
Net interest expense				(82.7)
<b>Earnings from continuing operations before income taxes and non-controlling interests</b>				<b>\$ 116.2</b>

Year ended Dec. 31, 2001	Generation	Audited		Total
		Energy Marketing	Corporate	
<b>Revenues</b>	\$ 2,158.4	\$ 2,694.7	\$ -	\$ 4,853.1
Trading purchases	-	(2,533.7)	-	(2,533.7)
<b>Net segment revenues</b>	<b>2,158.4</b>	<b>161.0</b>	<b>-</b>	<b>2,319.4</b>
Fuel and purchased power	(1,230.6)	-	-	(1,230.6)

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<b>Gross margin</b>	927.8	161.0	-	1,088.8
Operations, maintenance and administration	290.6	36.2	65.4	392.2
Depreciation and amortization	156.5	11.0	23.7	191.2
Asset impairment and equipment cancellation charges <i>(Note 6)</i>	118.8	-	-	118.8
Taxes, other than income taxes	18.7	-	-	18.7
Prior period regulatory decisions <i>(Note 10)</i>	(11.0)	-	-	(11.0)
<b>EBIT before corporate allocations</b>	354.2	113.8	(89.1)	378.9
Corporate allocations	(82.5)	(6.6)	89.1	-
<b>EBIT</b>	\$ 271.7	\$ 107.2	\$ -	378.9
Other income				1.5
Foreign exchange gain				0.8
Net interest expense				(88.1)
<b>Earnings from continuing operations before income taxes and non-controlling interests</b>			\$	293.1

**II. Selected balance sheet information**

<i>Dec. 31, 2002 (unaudited)</i>	Generation	Energy Marketing	Corporate	Discontinued Operations	Total
Goodwill	\$ -	\$ 29.3	\$ 27.2	\$ -	\$ 56.5
Other assets	6,353.4	315.3	694.4	-	7,363.1
<b>Total segment assets</b>	\$ 6,353.4	\$ 344.6	\$ 721.6	\$ -	\$ 7,419.6
<i>Dec. 31, 2001 (audited)</i>					
Goodwill	\$ -	\$ 29.3	\$ -	\$ -	\$ 29.3
Other assets	5,873.2	384.0	643.0	676.9	7,577.1
<b>Total segment assets</b>	\$ 5,873.2	\$ 413.3	\$ 643.0	\$ 676.9	\$ 7,606.4

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**III. Selected cash flow information**

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<b>3 months ended Dec. 31, 2002</b>	Generation	Energy		Discontinued		Total
		Marketing	Corporate	Operations		
<b>Capital expenditures</b>	\$	<b>190.8</b>	<b>2.1</b>	\$ <b>1.7</b>	\$ -	\$ <b>194.6</b>
<i>3 months ended Dec. 31, 2001</i>						
Capital expenditures	\$	415.5	2.0	\$ (6.3)	\$ 7.8	\$ 419.0
<b>Year ended Dec. 31, 2002</b>						
<b>Capital expenditures</b>	\$	<b>909.1</b>	<b>4.2</b>	\$ <b>10.7</b>	\$ <b>21.8</b>	\$ <b>945.8</b>
<i>Year ended Dec. 31, 2001</i>						
Capital expenditures	\$	1,147.6	43.8	\$ 15.1	\$ 40.0	\$ 1,246.5

**IV. Reconciliation**

**Depreciation and amortization (D&A) expense per statement of cash flows**

	3 months ended Dec. 31		12 months ended Dec. 31	
	2002	2001	2002	2001
D&A expense for reportable segments	\$ <b>62.5</b>	\$ 51.8	\$ <b>219.0</b>	\$ 191.2
Discontinued operations	-	12.9	<b>15.6</b>	46.5
Mining equipment depreciation, included in fuel and purchased power	<b>9.3</b>	7.0	<b>37.1</b>	31.8
Site restoration accrual, included in fuel and purchased power	<b>7.7</b>	9.1	<b>38.9</b>	37.3
Other	<b>0.2</b>	1.8	<b>4.2</b>	5.5
	\$ <b>79.7</b>	\$ 82.6	\$ <b>314.8</b>	\$ 312.3

**14 .. UNITED STATES GENERALLY ACCEPTED ACCOUNTING PRINCIPLES**

These interim consolidated financial statements have been prepared in accordance with Canadian GAAP and follow the same accounting policies and methods of computation as, and should be read in conjunction with, the most recent annual financial statements.

In connection with the corporation's May 12, 2002 shelf debt prospectus, TransAlta is required to reconcile these interim consolidated financial statements to U.S. GAAP. This reconciliation will be included with the corporation's annual report, and it shall be deemed to be incorporated by reference into these interim consolidated financial statements.

**15 .. SUBSEQUENT EVENTS**

On Jan. 13, 2003, TransAlta and EPCOR Utilities Inc. (EPCOR) announced an agreement whereby TransAlta will acquire a 50 per cent interest in EPCOR's Genesee Phase three project for \$395.0 million. On the same date, TransAlta made a \$157.0 million payment to EPCOR for TransAlta's share of project costs incurred to date. A 450 MW addition to the existing Genesee Generating station is currently under construction and expected to commence commercial operations in early 2005. Included in the arrangement is an option for EPCOR to purchase a 50 per cent interest in TransAlta's Centennial one project, formerly referred to as Keephills three. The option expires Dec. 31, 2005. EPCOR also has the option to purchase a 50 per cent interest in TransAlta's Sarnia plant, which may be exercised between January 2003 and March 2004.

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On Jan. 24, 2003, the corporation announced the acquisition of 50 per cent of the membership interests in CE Generation LLC (CE Gen) for US\$205.0 million (approximately Cdn\$312 million) plus approximately US\$35.0 million (approximately Cdn\$53 million) and the assumption of debt of approximately US\$500.0 million (approximately Cdn\$762 million). The acquisition will be accounted for using the purchase method of accounting. CE Gen is controlled jointly by TransAlta and MidAmerican Energy Holdings Company. As such, the financial results of CE Gen will be proportionately consolidated with those of TransAlta. The transaction closed on Jan. 29, 2003.

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### Signatures

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

TransAlta Corporation

(Registrant)

By: /s/ Alison T. Love

(Signature)

Alison T. Love, Corporate Secretary

Date: January 31, 2003

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### CERTIFICATIONS

I, Stephen G. Snyder, certify that:

1.

I have reviewed this Report of Foreign Private Issuer on Form 6-K of TransAlta Corporation;

2.

Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3.

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Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4.

The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and have:

- a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
- b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this report (the Evaluation Date ); and
- c) presented in this report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5.

The registrant's other certifying officer and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):

- a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weakness in internal controls; and
- b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6.

The registrant's other certifying officer and I have indicated in this report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date:

January 31, 2003

/s/ Stephen G. Snyder

Stephen G. Snyder

President and Chief Executive Officer

I, Ian Bourne, certify that:

1.

I have reviewed this Report of Foreign Private Issuer on Form 6-K of TransAlta Corporation;

2.

Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3.

Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4.

The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and have:

- a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
- b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this report (the Evaluation Date ); and
- c) presented in this report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5.

The registrant's other certifying officer and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):

- a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weakness in internal controls; and
- b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6.

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The registrant's other certifying officer and I have indicated in this report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: January 31, 2003

/s/ Ian Bourne

Ian Bourne

Executive Vice President and Chief Financial Officer