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Pre-tax amounts recorded in Other Comprehensive Income were as follows:

| | 2008 | | | 2007 | | |
|---|---|---|---|---|---|---|
| *December 31 (millions of dollars)* | **Pension Benefits** | **Other Benefits** | **Total** | Pension Benefits | Other Benefits | Total |
| Amortization of net loss from AOCI to net income | **(1)** | **(1)** | **(2)** | (9) | (1) | (10) |
| Amortization of prior service cost (credit) from AOCI to net income | **(2)** | **(1)** | **(3)** | (1) | | (1) |
| Funded status adjustment | **56** | **(2)** | **54** | 38 | 21 | 59 |
| | **53** | **(4)** | **49** | 28 | 20 | 48 |

The funded status based on the accumulated benefit obligation for all defined benefit pension plans as at December 31, 2008 is as follows:

| *December 31 (millions of dollars)* | **2008** | 2007 |
|---|---|---|
| Accumulated benefit obligation | **1,136** | 1,244 |
| Fair value of plan assets | **1,164** | 1,358 |
| Funded Status surplus | **28** | 114 |

Included in the above accumulated benefit obligation and fair value of plan assets as at December 31, 2008 are the following amounts in respect of plans that are not fully funded:

| *December 31 (millions of dollars)* | **2008** | 2007 |
|---|---|---|
| Accumulated benefit obligation | **149** | |
| Fair value of plan assets | **133** | |
| Funded Status (deficit) | **(16)** | |

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The estimated net loss and prior service cost for the defined benefit pension plans that will be amortized from Accumulated Other Comprehensive Income into net periodic benefit cost over the next fiscal year are $1 million and $1 million, respectively. The estimated net loss and prior service cost for the other defined benefit postretirement plans that will be amortized from Accumulated Other Comprehensive Income into net periodic benefit cost over the next fiscal year is $2 million and $1 million, respectively.

The rate used to discount pension and other post-retirement benefit plan obligations was based on a yield curve from Moody's corporate AA bond yields at December 31, 2008 developed by the Company's third party actuary. This yield curve is used to develop spot rates that vary based on the duration of the obligations. The estimated future cash flows for the pension and other post retirement obligations were matched to the corresponding rates on the yield curve to derive a weighted average discount rate.

(7)

Under Canadian GAAP, the Company accounts for certain investments using the proportionate consolidation basis whereby the Company's proportionate share of the assets, liabilities, revenues, expenses and cash flows are included in the Company's financial statements. U.S. GAAP does not allow the use of proportionate consolidation and requires that such investments be recorded on an equity accounting basis. Information on the balances that have been proportionately consolidated is located in Note 8 to the Company's 2008 audited consolidated annual financial statements. As a consequence of using equity accounting for U.S. GAAP, the Company is required to reflect an additional liability of $51 million at December 31, 2008 (December 31, 2007 $21 million) for the estimated fair value of certain guarantees related to debt and other performance commitments of the joint venture operations that were not required to be recorded when the underlying liability was reflected on the balance sheet under the proportionate consolidation method of accounting. The distributed earnings from long-term investments for the year ended December 31, 2008 were $295 million (2007 $376 million; 2006 $494 million). The undistributed earnings from long-term investments for the year ended December 31, 2008 were $892 million (2007 $821 million; 2006 $836 million).

(8)

Under U.S. GAAP, the Company is required to record a deferred income tax liability for its cost-of-service regulated businesses. As these deferred income taxes are recoverable through future revenues, a corresponding regulatory asset is recorded for U.S. GAAP purposes.

(9)

In accordance with U.S. GAAP, debt issue costs are recorded as a deferred asset rather than being included in long-term debt as required by Canadian GAAP.

(10)

At December 31, 2008, Accumulated Other Comprehensive Income in accordance with U.S. GAAP is $197 million higher than under Canadian GAAP. The difference relates primarily to the accounting treatment for defined benefit pension and other postretirement plans.

**Fair Value Measurements**

The Company adopted the provisions of Statement of Financial Accounting Standards (SFAS) No. 157, "Fair Value Measurements" (SFAS No. 157) for its financial assets and liabilities measured at fair value on a recurring basis effective January 1, 2008. The statement defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. In February 2008, the U.S. Financial Accounting Standards Board (FASB) issued FASB Staff Position No. 157-2, "Effective Date of FASB Statement No. 157", which delayed the effective date of SFAS No. 157 for all non-financial assets and liabilities that are measured at fair value on a non-recurring basis, until fiscal years beginning after November 15, 2008. These non-financial items include assets and liabilities such as non-financial assets and liabilities assumed in a business combination, reporting units measured at fair value in a goodwill impairment test and asset retirement obligations initially measured at fair value.

Under SFAS No. 157, fair value is defined as the price that would be received to sell an asset or paid to transfer a liability (i.e., the 'exit price') in an orderly transaction between market participants at the measurement date.

The Company's financial assets and liabilities that are recorded at fair value on a recurring basis have been categorized into one of three categories based upon a fair value hierarchy in accordance with SFAS No. 157. Fair values of assets and liabilities included in Level I are determined by reference to quoted prices in active markets for identical assets and liabilities. Assets and liabilities in Level II include valuations using inputs other than quoted prices for which all significant outputs are observable, either directly or indirectly. This includes comparisons with similar instruments that have observable market prices, option pricing models and other valuation techniques commonly used by market participants, which may require the use of assumptions about the amount and timing of estimated future cash flows and discount rates. In making these assumptions, the Company looks primarily to readily observable external market input factors such as interest rate yield curves, currency rates, and price and rate volatilities as applicable. Level III valuations are based on inputs that are unobservable and significant to the overall fair value measurement. TransCanada does not have any assets or liabilities that are included in Level III.

Assets and liabilities measured at fair value on a recurring basis as of December 31, 2008 are categorized in accordance with SFAS No. 157 as follows:

| *(millions of dollars)* | Quoted prices in active markets (Level I) | Significant other observable inputs (Level II) | Significant unobservable inputs (Level III) | Total |
|---|---|---|---|---|
| Derivative Financial Instruments Held for Trading: | | | | |
| Assets | 130 | 254 | | 384 |
| Liabilities | (127) | (347) | | (474) |
| Derivative Financial Instruments in Hedging Relationships: | | | | |
| Assets | 42 | 150 | | 192 |
| Liabilities | (100) | (545) | | (645) |
| Non-Derivative Financial Instruments Available for Sale: | | | | |
| Assets | 24 | | | 24 |
| Liabilities | | | | |
| Total | (31) | (488) | | (519) |

**Income Taxes**

The income tax effects of differences between the accounting value and the tax value of assets and liabilities are as follows:

| *December 31 (millions of dollars)* | **2008** | 2007 |
|---|---|---|
| **Deferred Tax Liabilities** | | |
| Difference in accounting and tax bases of plant, equipment and power purchase arrangements | **2,182** | 1,763 |
| Taxes on future revenue requirement | **387** | 433 |
| Investments in subsidiaries and partnerships | **313** | 443 |
| Unrealized foreign exchange gains on long-term debt | **14** | 110 |
| Pension benefit | **6** | 11 |
| Other comprehensive income | | 8 |
| Other | **81** | 81 |
| | **2,983** | 2,849 |
| **Deferred Tax Assets** | | |
| Deferred amounts | **119** | 45 |
| Other post-employment benefits | **38** | 25 |
| Other comprehensive income | **62** | 22 |
| Non-capital loss carry-forwards | **24** | |
| Unrealized foreign exchange losses on long-term debt | **77** | |
| Other | **138** | 77 |
| | **458** | 169 |
| Less: Valuation allowance | **77** | 13 |
| | **381** | 156 |
| Net deferred tax liabilities | **2,602** | 2,693 |

TransCanada adopted FASB Financial Interpretation 48, Accounting for Uncertainty in Income Taxes ("FIN 48"), January 1, 2007. The implementation of the provisions under FIN 48 did not have a material impact on the U.S. GAAP financial statements of the Company and no adjustment to the beginning balance of retained earnings was required due to the adoption of FIN 48.

Below is the reconciliation of the annual changes in the total unrecognized tax benefit.

| *December 31 (millions of dollars)* | **2008** | 2007 |
|---|---|---|
| Unrecognized tax benefits, beginning of year | **70** | 80 |
| Gross increases tax positions in prior years | **13** | 9 |
| Gross decreases tax positions in prior years | **(1)** | (11) |
| Gross increases current year positions | **20** | 9 |
| Settlements | **(19)** | (6) |
| Lapses of statute of limitations | **(3)** | (11) |
| Unrecognized tax benefits, end of year | **80** | 70 |

TransCanada expects the enactment of certain Canadian Federal tax legislation in the next twelve months which is expected to result in a favourable income tax adjustment of approximately $12 million. Otherwise, subject to the results of audit examinations by taxing authorities and other legislative amendments, TransCanada does not anticipate further adjustments to the unrecognized tax benefits during the next twelve months that would have a material impact on its financial statements.

TransCanada and its subsidiaries are subject to either Canadian federal and provincial income tax, U.S. federal, state and local income tax or the relevant income tax in other international jurisdictions. The Company has substantially concluded all Canadian federal and provincial income tax matters for the years through 2003. Canadian federal income tax returns for years 2004 and 2005 are currently under examination by the Canada Revenue Agency, which has not proposed any significant adjustments. Substantially all material U.S. federal income tax matters have been concluded for years through 2004 and U.S. state and local income tax matters through 2002.

TransCanada's continuing practice is to recognize interest and penalties related to income tax uncertainties in income tax expense. Included in net tax expense for the year ended December 31, 2008 is $10 million for interest and nil for penalties (December 31, 2007 $1 million for interest and nil for penalties). At December 31, 2008, the Company had $24 million accrued for interest and nil accrued for penalties (December 31, 2007 $14 million accrued for interest and nil accrued for penalties).

**Other**

In February 2007, FASB issued SFAS No. 159 "The Fair Value Option for Financial Assets and Financial Liabilities Including an Amendment of FASB Statement No. 115", which allows an entity to choose to measure many financial instruments and certain other items at fair value for fiscal years beginning on or after November 15, 2007. TransCanada's U.S. GAAP financial statements were not materially impacted by SFAS No. 159.

In December 2007, FASB issued SFAS No. 160 "Noncontrolling Interests in Consolidated Financial Statements an amendment of ARB No. 51" and SFAS No. 141(R) "Business Combinations" both of which are effective for annual periods beginning after December 15, 2008. SFAS No. 160 requires that third party ownership interests in subsidiaries be presented separately in the equity section of the balance sheet. In addition, the income attributable to the noncontrolling interest will now be included in consolidated net income and will be deducted separately at the bottom of the income statement. SFAS No. 141(R) requires that most identifiable assets, liabilities (including obligations for contingent consideration), noncontrolling interests and goodwill be recorded at "full fair value". Also, for step acquisitions, the acquirer will be required to re-measure its noncontrolling equity investment in the acquiree at fair value as of the date control is obtained and recognize any gain or loss in income. The Company will adopt these standards on January 1, 2009.

In March 2008, FASB issued SFAS No. 161 "Disclosures about Derivative Instruments and Hedging Activities an amendment of FASB Statement No. 133", which is effective for fiscal years beginning after November 15, 2008. SFAS No. 161 expands the disclosure requirements for derivative instruments and hedging activities with respect to how and why entities use derivative instruments, how they are accounted for under SFAS No. 133

and the related impact on financial position, financial performance and cash flows. TransCanada does not expect a material affect on its financial disclosures as a result of adopting this standard on January 1, 2009.

In May 2008, FASB issued SFAS No. 162 "The Hierarchy of Generally Accepted Accounting Principles" which codifies the sources of accounting principles and the related framework to be utilized in preparing financial statements in conformity with U.S. GAAP. TransCanada's U.S. GAAP financial statements are not expected to be impacted by this standard.

In October 2008, FASB issued Staff Position No. 157-3, "Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active", which clarifies the application of SFAS No. 157 in a market that is not active. This Staff Position is effective upon issuance and the Company's U.S. GAAP financial statements were not impacted by this standard.

In December 2008, FASB issued Staff Position No. 132(R)-1, "Employers' Disclosures about Postretirement Benefit Plan Assets", which requires more detailed disclosures regarding the employers' plan assets, concentrations of risk within plan assets and valuation techniques used to measure the fair value of plan assets. This Staff Position will be effective for fiscal years ending after December 15, 2009. The Company will adopt these standards for its 2009 year-end reporting.

**MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING**

Internal control over financial reporting is a process designed by or under the supervision of senior management of TransCanada Corporation ("TransCanada" or the "Company"), and effected by the Board of Directors, management and other personnel to provide reasonable assurance regarding the reliability of financial reporting and preparation of consolidated financial statements for external purposes in accordance with Canadian generally accepted accounting principles, including a reconciliation to U.S. GAAP.

Management is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting, no matter how well designed, has inherent limitations and can only provide reasonable assurance with respect to the preparation and fair presentation of published financial statements. Under the supervision and with the participation of the President and Chief Executive Officer and the Chief Financial Officer, management conducted an evaluation of the effectiveness of its internal control over financial reporting based on the framework in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Company acquired Keyspan-Ravenswood, LLC ("Ravenswood") in August 2008 and began consolidating the operations of Ravenswood from that date. Management has excluded this business from its evaluation of the effectiveness of the Company's internal control over financial reporting as of December 31, 2008. The net income attributable to this business represented less than one per cent of the Company's consolidated net income for the year ended December 31, 2008, and its aggregate total assets represented approximately nine per cent of the Company's consolidated total assets as at December 31, 2008.

Based on this evaluation, management concluded that internal control over financial reporting is effective as at December 31, 2008, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external reporting purposes.

In 2008, there was no change in TransCanada's internal control over financial reporting that materially affected or is reasonably likely to materially affect TransCanada's internal control over financial reporting.

KPMG LLP, the independent auditors appointed by the shareholders of TransCanada, who have audited the consolidated financial statements of TransCanada, have also audited the effectiveness of TransCanada's internal control over financial reporting as of December 31, 2008 and have issued the report entitled "Report of Independent Registered Public Accounting Firm".

February 23, 2009

| /s/ HAROLD N. KVISLE | /s/ GREGORY A. LOHNES |
|---|---|
| Harold N. Kvisle<br>*President and*<br>*Chief Executive Officer* | Gregory A. Lohnes<br>*Executive Vice-President and*<br>*Chief Financial Officer* |

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

To the Board of Directors of TransCanada Corporation

We have audited TransCanada Corporation's internal control over financial reporting as of December 31, 2008, based on the criteria established in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2008, based on criteria established in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

We also have conducted our audits on the consolidated financial statements in accordance with Canadian generally accepted auditing standards and in accordance with the standards of the Public Company Accounting Oversight Board (United States). Our report dated February 23, 2009 expressed an unqualified opinion on those consolidated financial statements.

/s/ KPMG LLP
Chartered Accountants
Calgary, Canada

February 23, 2009

**COMMENTS BY AUDITORS FOR UNITED STATES READERS ON CANADA    UNITED STATES REPORTING DIFFERENCES**

To the Board of Directors of TransCanada Corporation

In the United States, reporting standards for auditors require the addition of an explanatory paragraph (following the opinion paragraph) that refers to the audit report on the Company's internal control over financial reporting. Our report to the shareholders dated February 23, 2009 is expressed in accordance with Canadian reporting standards, which do not require a reference to the audit report on the Company's internal control over financial reporting in the financial statement auditors' report.

/s/  KPMG LLP
Chartered Accountants
Calgary, Canada

February 23, 2009

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