

ENERGY CO OF MINAS GERAIS  
Form 20-F  
May 25, 2005

# SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

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## FORM 20 F

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**REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR  
(g) OF THE SECURITIES EXCHANGE ACT OF 1934**

OR

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

For the fiscal year ended December 31, 2004

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: 1-15224

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# COMPANHIA ENERGÉTICA DE MINAS GERAIS CEMIG

(Exact Name of Registrant as Specified in Its Charter)

**Energy Company of Minas Gerais**  
(Translation of Registrant's Name into English)

**The Federative Republic of Brazil**  
(Jurisdiction of Incorporation or Organization)

**Avenida Barbacena, 1200  
30190-131 Belo Horizonte, Minas Gerais, Brazil**

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(Address of Principal Executive Offices)

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

Title of Each Class	Name of Each Exchange on which Registered
American Depositary Shares (evidenced by American Depositary Receipts), each representing 1,000 Preferred Shares	New York Stock Exchange
Preferred Shares, R\$0.01 par value*	New York Stock Exchange*

\* Not for trading purposes, but only in connection with the registration of American Depositary Shares pursuant to the requirements of the Securities and Exchange Commission.

Securities registered or to be registered pursuant to Section 12(g) of the Act: **None**

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act: **None**

Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of the close of the period covered by the annual report.

70,874,167,923 Common Shares

91,210,522,699 Preferred Shares

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 which financial statement item the registrant has elected to follow.

Item 17  Item 18

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## PRESENTATION OF FINANCIAL INFORMATION

Companhia Energética de Minas Gerais CEMIG is a *sociedade de economia mista* (a state-controlled mixed capital company) organized and existing with limited liability under the laws of the Federative Republic of Brazil, or Brazil. References in this annual report to CEMIG, we or the Company are to Companhia Energética de Minas Gerais CEMIG and its consolidated subsidiaries, except when the reference is specifically to Companhia Energética de Minas Gerais CEMIG (parent company only) or the context otherwise requires. References to the *real*, *reais* or R\$ are to Brazilian *reais* (plural) and the Brazilian *real* (singular), the official currency of Brazil, and references to U.S. dollars, dollars or US\$ are to United States dollars.

We maintain our books and records in *reais*. We prepare our financial statements in accordance with accounting practices adopted in Brazil, including the principles that are established primarily through Law No. 6,404 of December 15, 1976, Law No. 9,457 of May 5, 1997 and Law No. 10,303 of October 31, 2001, which we refer to collectively as the Brazilian Corporate Law. For purposes of this annual report, we have presented, and in future reports to be filed with the United States Securities and Exchange Commission, or the Commission, we intend to present, our consolidated financial statements and other financial information in *reais* in accordance with accounting principles generally accepted in the United States, or U.S. GAAP. For purposes of this annual report we prepared balance sheets as of December 31, 2004 and 2003 and the related statements of operations and comprehensive income, cash flows and changes in shareholders' equity for the years ended December 31, 2004, 2003 and 2002, in *reais* all in accordance with U.S. GAAP. Deloitte Touche Tohmatsu Auditores Independentes has audited our consolidated financial statements at December 31, 2004 and 2003 and for each of the three years ended December 31, 2004, 2003 and 2002.

From and after January 1, 1998, Brazil ceased to be considered a highly inflationary economy under U.S. GAAP and we have not restated financial information to reflect the effects of inflation as from that date. Therefore, for subsequent periods and dates, our financial statements and other financial data are presented in nominal *reais* and do not reflect effects of inflation. See Note 2(b) to our consolidated financial statements.

This annual report contains translations of certain *real* amounts into U.S. dollars at specified rates solely for the convenience of the reader. Unless otherwise indicated, such U.S. dollar amounts have been translated from *reais* at an exchange rate of R\$2.6550 to US\$1.00, the noon buying rate in New York City for cable transfers in *reais* as certified for customs purposes by the Federal Reserve Bank of New York, or the noon buying rate, as of December 31, 2004. The *real* has recently experienced high volatility. See Item 3. Key Information Exchange Rates for additional information regarding exchange rates. We cannot guarantee that U.S. dollars can be converted into *reais*, or that *reais* can be converted into U.S. dollars, at the above rate or at any other rate.

## MARKET POSITION AND OTHER INFORMATION

The information contained in this annual report regarding our market position is, unless otherwise indicated, presented for the twelve-month period ended December 31, 2004 and is based on, or derived from, reports issued by the *Agência Nacional de Energia Elétrica* (The Brazilian National Electric Energy Agency), or ANEEL.

Certain terms are defined the first time they are used in this annual report. The Index of Defined Terms included in this annual report lists those terms and where they are defined. As used herein, all references to GW and GWh are to gigawatts and gigawatt hours, respectively, references to MW and MWh are to megawatts and megawatt-hours, respectively, and references to kW and kWh are to kilowatts and kilowatt-hours, respectively.

References in this annual report to the common shares and preferred shares are to our common shares and preferred shares, respectively. References to American Depositary Shares or ADSs are to American Depositary Shares, each representing 1,000 preferred shares. The ADSs are evidenced by American Depositary Receipts, or ADRs, issued pursuant to a Second Amended and Restated Deposit Agreement, dated as of August 10, 2001, by and among us, Citibank, N.A., as depository, and the holders and beneficial owners of ADSs evidenced by ADRs issued thereunder.

## FORWARD-LOOKING INFORMATION

This annual report includes forward-looking statements, principally in Item 3. Key Information and Item 11. Quantitative and Qualitative Disclosures about Market Risk. We have based these forward-looking statements largely on our current expectations and projections about future events and financial trends affecting our business. These forward-looking statements are subject to risks, uncertainties and assumptions relating to, among other things:

general economic, political and business conditions, principally in Latin America, Brazil and the State of Minas Gerais, Brazil, or Minas Gerais;

inflation and changes in currency exchange rates;

enforcement of legal regulation in Brazil's electricity sector;

changes in volumes and patterns of customer electricity usage;

competitive conditions in Brazil's electricity generation, transmission and distribution markets;

our expectations and estimates concerning future financial performance, financing plans and the effects of competition;

our level of debt;

the likelihood that we will receive payment in connection with accounts receivable;

Germais; trends in the electricity generation, transmission and distribution industry in Brazil and Minas

changes in rainfall and the water levels in the reservoirs used to run our hydroelectric power generation facilities;

our capital expenditure plans;

our ability to serve our customers on a satisfactory basis;

existing and future governmental regulation as to electricity rates, electricity usage, competition in our concession area and other matters;

existing and future policies of the Federal Government of Brazil, which we refer to as the Federal Government;

existing and future policies of the government of Minas Gerais, which we refer to as the State Government, including policies affecting its investment in us and the plans of the State Government for future expansion of electricity generation, transmission and distribution in Minas Gerais; and

other risk factors as set forth under Item 3. Key Information Risk Factors.

The forward-looking statements referred to above also include information with respect to our capacity expansion projects that are under way and those that we are currently evaluating. In addition to the above risks and uncertainties, our potential expansion projects involve engineering, construction, regulatory and other significant risks, which may:

delay or prevent successful completion of one or more projects;

increase the costs of projects; and

result in the failure of facilities to operate or generate income in accordance with our expectations.

The words believe, may, will, estimate, continue, anticipate, intend, expect and similar words are intended to identify forward-looking statements. We undertake no obligation to update publicly or revise any forward-looking statements because of new information, future events or otherwise. In light of these risks and uncertainties, the forward-looking information, events and circumstances discussed in this annual report might not occur. Our actual results and performance could differ substantially from those anticipated in our forward-looking statements.

Neither our independent auditors, nor any other independent accountants, have compiled, examined or performed any procedures with respect to the forward-looking financial information contained herein, nor have they expressed any opinion or any other form of assurance on such information or its achievability, and they assume no responsibility for, and disclaim any association with, such forward-looking financial information.





**PART I**



**Item 1. Identity of Directors, Senior Management and Advisers**



Not applicable.

Item 2. **Offer Statistics and Expected Timetable**



Not applicable.

Item 3. **Key Information**





**Selected Consolidated Financial Data**

The following tables present our selected consolidated financial and operating information in U.S. GAAP as of the dates and for each of the periods indicated. You should read the following information together with our consolidated financial statements, including the notes thereto, included in this annual report and the information set forth in Item 5. Operating and Financial Review and Prospects.

The selected consolidated financial data as of December 31, 2004 and 2003 and for each of the three years ended December 31, 2004, 2003 and 2002 have been derived from our audited consolidated financial statements and the notes thereto included elsewhere in this annual report. The selected consolidated data as of December 31, 2002, 2001 and 2000 and for the each of the two years ended December 31, 2001 and 2000 has been derived from our audited consolidated financial statements and notes thereto, which are not included in this annual report.

U.S. dollar amounts in the table below are presented for your convenience. Unless otherwise indicated, these U.S. dollar amounts have been translated from *reais* at R\$2.6550 per US\$1.00, the noon buying rate as of December 31, 2004. The *real* has recently experienced high volatility. We cannot guarantee that U.S. dollars can be converted into *reais*, or that *reais* can be converted into U.S. dollars, at the above rate or at any other rate. On May 18, 2005, the noon buying rate for *reais* was R\$2.4625 per US\$1.00. See Exchange Rates.

## Selected Consolidated Financial Data

	As of and for the year ended December 31,					
	2004	2004	2003	2002	2001	2000
	(in millions of US\$)(1)(2)	(In millions of R\$ except per share/ADS data or as otherwise indicated)				
<b>Income Statement Data:</b>						
Net operating revenues						
Electricity sales to final customers	3,224	8,561	7,179	5,458	4,587	4,478
Regulatory extraordinary rate adjustment(3)	34	89	63	281	789	
Deferred rate adjustment (3)	241	640	199			
Electricity sales to the interconnected power system	14	36	56	161	517	145
Use of basic transmission network	92	245	257	185	154	139
Other operating revenues	202	536	468	260	150	124
Tax on revenues	(924)	(2,453)	(2,190)	(1,473)	(1,191)	(1,130)
Total net operating revenues	2,883	7,654	6,032	4,872	5,006	3,756
Operating costs and expenses						
Electricity purchased for resale.	(556)	(1,477)	(1,396)	(1,333)	(1,914)	(819)
Natural gas purchased for resale	(101)	(268)	(246)	(152)	(84)	(60)
Use of basic transmission network	(221)	(586)	(310)	(298)	(251)	(243)
Depreciation and amortization	(255)	(677)	(686)	(666)	(641)	(583)
Personnel	(297)	(788)	(710)	(532)	(531)	(466)
Regulatory charges	(324)	(861)	(585)	(548)	(420)	(433)
Third-party services	(124)	(329)	(325)	(265)	(216)	(195)
Employee post-retirement benefits	(58)	(153)	(109)	(207)	(293)	(238)
Materials and supplies	(31)	(83)	(88)	(78)	(70)	(71)
Gain on Gasmig sale	38	102				
Other	(153)	(407)	(422)	(238)	(274)	(208)
Reversal (Provision) for loss on deferred regulatory assets (3)	(3)	(9)	174	(28)	(150)	
Provision for loss on account receivable from State Government			(754)			
Total operating costs and expenses	(2,085)	(5,536)	(4,703)	(4,345)	(5,598)	(3,316)
Operating income (loss)	798	2,118	1,329	527	(592)	440
Financial income (expenses), net	132	350	674	(525)	(48)	(42)
Income (loss) before income taxes and minority interests	930	2,468	2,003	2	(640)	398

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Income taxes (expense) benefit	(275)	(731)	(607)	(26)	(78)	(32)
Minority interests	1	2		12	(1)	
Net income (loss)	656	1,739	1,396	(12)	(719)	366
Other comprehensive income (loss)	(179)	(474)	(64)	242	203	19
Comprehensive income (loss)	477	1,265	1,332	230	(516)	385
Basic and diluted earnings (loss):						
Per thousand common shares	4.04	10.73	8.61	(0.07)	(4.52)	2.30
Per thousand preferred shares	4.04	10.73	8.61	(0.07)	(4.52)	2.30
Per ADS	4.04	10.73	8.61	(0.07)	(4.52)	2.30
<b>Balance Sheet Data:</b>						
<b>Assets</b>						
Current assets	1,268	3,366	2,630	1,845	1,752	1,064
Property, plant and equipment, net (in service)	3,498	9,288	9,361	9,322	9,325	9,705
Construction in progress	717	1,903	1,556	777	516	592
Deferred regulatory assets long-term	1,103	2,929	2,069	1,670	1,245	
Account receivable from State Government	413	1,097	891	755	451	953
Other assets	252	669	612	1,139	773	484
Total assets	7,251	19,252	17,119	15,508	14,062	12,798
<b>Liabilities</b>						
Current portion of long-term financing	534	1,417	1,660	946	451	502
Other current liabilities	895	2,376	1,869	2,097	1,713	1,042
Long-term financing	1,036	2,750	2,331	2,593	2,029	1,088
Employee post-retirement benefits-long-term	605	1,606	1,023	1,091	1,475	1,803
Shareholders equity	3,469	9,209	8,524	7,442	7,543	8,162
Capital stock	538	1,428	1,428	1,428	1,396	1,396

	2004 (US\$)(1)	As of and for the year ended December 31,									
		2004		2003		2002		2001		2000	
		(In R\$ or US\$ as indicated, except outstanding shares data)									
<b>Other Data:</b>											
Weighted average outstanding shares basic and diluted (thousands)											
Common		70,874,168		70,874,168		70,874,168		69,495,478		69,495,478	
Preferred		91,210,523		91,210,523		91,210,523		89,436,237		89,436,237	
Dividends per thousand shares											
Common	1.35	R\$	3.58	R\$	1.54	R\$	2.04	R\$	0.65	R\$	1.18
Preferred	1.35	R\$	3.58	R\$	1.54	R\$	2.04	R\$	0.65	R\$	1.18
Dividends per ADS											
Preferred	1.35	R\$	3.58	R\$	1.54	R\$	2.04	R\$	0.65	R\$	1.18
Dividends per thousand shares(4)											
Common		US\$	1.35	US\$	0.53	US\$	0.58	US\$	0.28	US\$	0.60
Preferred		US\$	1.35	US\$	0.53	US\$	0.58	US\$	0.28	US\$	0.60
Dividends per ADS(4)											
Preferred		US\$	1.35	US\$	0.53	US\$	0.58	US\$	0.28	US\$	0.60

(1) Converted at the exchange rate of US\$1.00 to R\$2.6550, the noon buying rate as of December 31, 2004. See Exchange Rates.

(2) In millions, except per share/ADS data.

(3) See Note 4 to our consolidated financial statements.

(4) This information is presented in U.S. dollars at the noon buying rate in effect as of the end of each year.

#### Exchange Rates



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Prior to March 14, 2005 there were two principal foreign exchange markets in Brazil - the commercial rate exchange market and the floating rate exchange market. Most trade and financial foreign-exchange transactions were carried out on the commercial rate exchange market. The floating market rate generally applied to transactions to which the commercial market rate did not apply. Prior to February 1999, the exchange rate in each market was established independently, resulting in different rates during some periods. As of February 1, 1999, the Central Bank of Brazil (Banco Central do Brazil), or the Central Bank, placed the commercial rate exchange market and the floating rate exchange market under identical operational limits, which led to a convergence in the pricing and liquidity of both markets.

On March 6, 2005, the National Monetary Council (Conselho Monetário Nacional) enacted Resolution No. 3,265 that, effective March 14, 2005, consolidated the two foreign exchange markets into one foreign exchange market for the general purpose of making foreign exchange transactions simpler and more efficient. All foreign exchange transactions are now carried out in this single foreign exchange market through financial institutions authorized to operate in the market. Additional regulations governing the new foreign exchange market are pending approval and enactment by the Brazilian government. We cannot predict the actual impact of the enactment of such new regulations on the new foreign exchange market.

Foreign exchange rates continue to be freely negotiated, but may be influenced by Central Bank intervention. From March 1995 through January 1999, the Central Bank allowed the gradual devaluation of the *real* against the U.S. dollar. In January 1999, the Central Bank allowed the *real*/U.S. dollar exchange rate to float freely. Since then, the *real*/U.S. dollar exchange rate has been established mainly by the Brazilian interbank market and has fluctuated considerably.

During 2000, 2001 and 2002 the *real* declined against the U.S. dollar. Nevertheless, in 2003, the *real* appreciated significantly against the U.S. dollar due to the adoption of new monetary and fiscal policies by the new Federal Government. In 2004 and the first four months of 2005, the *real* continued to appreciate against the U.S. dollar, mostly due to the worldwide U.S. dollar depreciation and the tightening of the domestic monetary policy. In the past, the Central Bank has intervened occasionally to control unstable movements in foreign exchange rates. We cannot predict whether the Central Bank or the Brazilian government will continue to let the *real* float freely or will intervene in the exchange rate market through a currency band system or otherwise, or that the exchange market will not be volatile as a result of political instability or other factors. The *real* may depreciate or appreciate against the

U.S. dollar and other currencies substantially in the future. Any exchange rate fluctuations may also affect our financial condition.

The table below sets forth, for the periods indicated, the low, high, average and period-end noon buying rates for *reais*, expressed in *reais* per US\$1.00.

Month	Reais per US\$ 1.00			Period-end
	Low	High	Average	
November 2004	2.7277	2.8630	2.7877	2.7310
December 2004	2.6510	2.7800	2.7150	2.6550
January 2005	2.6115	2.7227	2.6895	2.6115
February 2005	2.5640	2.6310	2.5971	2.5846
March 2005	2.6103	2.7755	2.7061	2.6660
April 2005	2.5135	2.6572	2.5760	2.5330
May 2005 (through May 18, 2005)	2.4528	2.5147	2.4752	2.4625

Year Ended December 31,	Reais per US\$ 1.00			Period-end
	Low	High	Average	
2000	1.7230	1.9840	1.8301	1.9510
2001	1.9380	2.7880	2.3527	2.3120
2002	2.2730	3.9450	2.9213	3.5400
2003	2.8230	3.6640	3.0757	2.8950
2004	2.6510	3.2085	2.9262	2.6550

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Source: Federal Reserve Bank of New York

Exchange rate fluctuations may affect the U.S. dollar amounts received by the holders of ADSs. We will make any distributions with respect to our preferred shares in *reais* and the depositary will convert these distributions into U.S. dollars for payment to the holders of ADSs. Exchange rate fluctuations may also affect the U.S. dollar equivalent of the *real* price of the preferred shares on the Brazilian stock exchange where they are traded. Exchange rate fluctuations may also affect our results of operations. See Risk Factors Risks Relating to Brazil Exchange rate instability may adversely affect our results of operations and financial condition.

## Risk Factors





*You should consider the following risks as well as the other information in this annual report in evaluating an investment in our company.*



**Risks Relating to CEMIG**



*We are controlled by the State Government which may have interests that are different from yours.*



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As our controlling shareholder, the government of the State of Minas Gerais exercises substantial influence on the management and orientation of the business of CEMIG. Further, the present Governor of the State of Minas Gerais is a member of a party which is in opposition to the present Federal Government. It is not possible to analyze the impact and effects this may have on us or our results of operations.

The government of the State of Minas Gerais currently holds 51% of our common shares and, consequently, has the right to the majority of votes in decisions of the General Meetings of our Shareholders, and can (i) elect the majority of the members of the Board of Directors of CEMIG, and (ii) decide matters requiring approval by a specific majority of our shareholders, including transactions with related parties, shareholding reorganizations and the date and payment of any dividends.

The operations of CEMIG have had and will continue to have an important impact on the commercial and industrial development of the State of Minas Gerais, and on its social conditions. In the past, the State Government



has used, and may use in the future, its status as our controlling shareholder to decide that we should engage in certain activities and make certain investments aimed, principally, to promote its political, economic or social objectives and not necessarily to meet the objective of improving our business and/or operational results.

*We may not be able to collect a significant receivable from the State Government.*



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We have a significant receivable from the State Government under the CRC Account Agreement, which totaled R\$1,097 million as of December 31, 2004. Historically we have been facing difficulties in collecting such receivable. We are currently offsetting amounts that are due from the State under the CRC Account Agreement against payments of dividends and interest on capital that we are required to pay to the State Government as our shareholder, as allowed under the third amendment to the CRC Account Agreement. On November 19, 2004, our Board of Directors unanimously approved the main terms of a fourth amendment to the CRC Account Agreement, which includes an increase from 25% to 50% to the amount of dividends and interest on capital due to the State that we are entitled to offset against amounts due under the CRC Account Agreement. This amendment is still subject to approval by the State Government, and execution of such amendment depends on the approval of ANEEL, our shareholders and the state congress of the State of Minas Gerais. No assurance can be given that all such approvals will be obtained or, if obtained, that any of the installment payments under this amendment will be paid when due or at all. Furthermore, no assurance can be given that additional loss provisions with respect to receivable will not be recorded in future periods. See Item 10. Additional Information Material Contracts CRC Account Agreement .

*We are subject to extensive governmental legislation and regulation.*



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The Brazilian Federal Government has been implementing policies that have a far-reaching impact on the Brazilian power industry, in particular, the electricity industry. As part of the restructuring of the industry, Federal Law No. 10,848 of March 15, 2004, ( Law No. 10,848/04 or the New Industry Model Law ) introduced a new regulatory framework for the Brazilian electricity industry.

Law No. 10,848/04 remains subject to the implementation of resolutions by ANEEL. Moreover, the constitutionality of Law No. 10,848/04 is currently being challenged before the Brazilian Supreme Court. The Brazilian Supreme Court has not yet reached a final decision and, therefore, Law No. 10,848/04 is currently in force. If all or a portion of Law No. 10,848/04 is considered to be unconstitutional by the Brazilian Supreme Court, all or a portion of the regulatory scheme introduced by Law No. 10,848/04 may not come into effect, generating uncertainty as to how and when the Federal Government will be able to introduce changes to the electricity industry. Accordingly, we cannot now evaluate the impact of the new regulation to be issued by ANEEL or the adverse impact of a decision on the constitutionality of Law No. 10,848/04 would have on our future activities, results of operations and financial condition.

*Companies holding concessions for distribution of electricity are required to purchase all of their electricity demand by means of public auctions. We may not be able to pass on through our distribution rates a portion of the costs of our electricity purchases.*



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Under the New Industry Model Law, an electricity distributor must contract in advance, through public auctions conducted by the Electric Energy Trading Chamber (CCEE *Câmara de Comercialização de Energia Elétrica*), in accordance with laws determined by the Ministry of Mines and Energy, or MME, at least 100% of its forecasted electricity needs for the following five years. The New Industry Model Law establishes the conditions for passing through energy purchase volumes and prices. If the energy we purchase in the public auctions is less than 100% of our total captive consumption (which excludes Free Consumers, as defined in this annual report), we may be subject to fines which have not yet been determined by ANEEL and we may not be able to pass on the full costs of our additional energy purchases, which may be at higher prices, to our customers. If the energy we purchase in the public auction is more than 103% of our total captive consumption, we have to assume the price risk of buying in the public auctions and selling in the spot market.

The New Industry Model Law limits our ability to pass through the cost of electricity purchases to our customers if our costs exceed the Annual Reference Value (*Valor Anual de Referência*) established by ANEEL,

which is based on the weighted average price paid by all distribution companies in the public auctions for electricity from new generation undertakings to be delivered three and five years from the date of any such auction.

Considering the numerous factors that affect our electricity demand forecasts, including economic and population growth, and our required purchase of energy from Itaipu in an amount determined by the Federal Government, we cannot assure you that our forecasted electricity demand will be accurate and this may have an adverse effect on our business, results of operations and financial condition.

*New rules for the sale of electric energy and market conditions may affect our generation sale prices.*

The contracts by which we had initially contracted all of our generation capacity with regulated prices (the Initial Contracts ) began to phase out at the end of 2002 at the rate of 25% each year and we expect they will be completely phased out in 2005. Even if we are able to contract all generation capacity liberated from such contracts, we are not able to predict the price at which we will be able to contract such energy.

Additionally, we still have capacity from undertakings yet to be operational that we are planning to sell under the auctions for new undertakings to be held under the Regulated Contracting Environment (as defined in this annual report). Legislation allows distributors that contract with our generation company under the Regulated Contracting Environment to reduce the quantity contracted under these contracts until a certain limit, exposing the generation company to the risk of failing to contract this reduced energy with adequate prices.

Contracts with consumers allowed to purchase energy directly from generating companies or energy traders (generally consumers with demand equal to or greater than 3 MW, and referred to as Free Consumers ) will also give such consumers the flexibility to purchase less energy from us than was originally contracted for by such consumers, which may adversely impact our business, results of operations and financial condition.

If we are unable to contract our remaining capacity of energy liberated from existing contracts and energy from new undertakings at adequate prices, our revenues and our results of operations may be adversely affected.

*ANEEL has substantial discretion to establish the rates we charge. Such rates are determined pursuant to concession contracts entered with ANEEL and in accordance with ANEEL's regulatory decision-making authority.*

Concession agreements and Brazilian law establish a price cap mechanism that permits three types of rate adjustments: (1) the annual adjustment; (2) the periodic revision; and (3) the extraordinary revision. We are entitled to apply each year for the annual adjustment, which is designed to offset some of the effects of inflation on rates and pass through to customers certain changes in our cost structure that are beyond our control, such as the cost of electricity we purchase from certain sources and certain other regulatory charges, including charges for the use of transmission and distribution facilities. In addition, ANEEL carries out a periodic revision every five years that is aimed at identifying variations in our costs as well as setting a factor based on our operational efficiency that will be applied against the index of our ongoing annual rate adjustments, the intended effect of which is to reward the good management of our costs while sharing any related gains with customers. We are also entitled to request an extraordinary revision of our rates if unpredictable events significantly alter our cost structure. The periodic revision and extraordinary revision are subject to a certain degree of ANEEL's discretion.



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We cannot assure you that ANEEL will establish rates that will adequately compensate us and that our revenues and results of operations will not be adversely affected. In addition, to the extent any of these adjustments are not granted by ANEEL in a timely manner, our business, results of operations and financial condition may be adversely affected.

*We are strictly liable for any damages resulting from inadequate rendering of electricity services, and our contracted insurance policies may not fully cover such damages.*

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Under Brazilian law, we are strictly liable for direct and indirect damages resulting from the inadequate rendering of electricity services. In addition, the damages caused to end consumers as a result of interruptions or

disturbances arising from the generation, transmission or distribution systems, whenever these interruptions or disturbances are not attributed to an identifiable member of the Operador Nacional do Sistema (National System Operator, or ONS ) or the ONS itself, shall be shared among generation, distribution and transmission companies. Until a final criteria is defined, the liability for such damages shall be shared in the proportion of 60% to distribution agents, 20% to transmission agents and 20% to generation agents.

*We are subject to rules and limits applied to levels of public sector borrowing and to restrictions on the use of certain funds we raise, which could prevent us from obtaining financing.*



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As a state controlled company, we are subject to rules and limits on the level of credit applicable to the public sector issued by the National Monetary Council and by the Brazilian Central Bank. These rules set certain parameters and conditions for financial institutions to be able to offer credit to public sector entities. Thus, if we do not meet these conditions, we may have difficulty in obtaining financing from Brazilian financial institutions, which could create difficulties in the implementation of our investment plan or in refinancing our financial obligations. Brazilian legislation also establishes that a state-controlled company, in general, may only use proceeds of external or local transactions (debt, including bonds) to refinance financial obligations for which there is no other source of repayment. As a result of these regulations, our capacity to incur debt is again limited, and this could negatively affect the implementation of our investment plan or the refinancing of our obligations.

*There are contractual restrictions on our capacity to incur debt.*



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We are subject to certain restrictions on our ability to incur debt due to covenants set forth in our loan agreements. In the event of our non-compliance with any such covenants in our loan agreements, the total principal, future interest and any penalties due under these agreements may become immediately due and payable. Early maturity of our obligations could adversely affect our financial condition especially in light of cross default provisions in several of our loan and financing contracts. The existence of limitations on our indebtedness could prevent us from borrowing to finance our operations or to refinance our existing obligations which could adversely affect on business, results of operations and financial condition.

*We could be penalized by ANEEL for failing to comply with the terms of our concession agreements, which could result in fines, other penalties and, depending on the severity of non-compliance, expropriation of the concession agreements.*

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We conduct our generation, transmission and distribution activities pursuant to concession agreements entered into with the Brazilian government through ANEEL. ANEEL may impose penalties on us if we fail to comply with any provision of the concession agreements, including compliance with the established quality standards. Depending on the severity of the non-compliance, these penalties could include:

finer per breach of up to 2.0% of the concessionaire's revenues in the year ended immediately prior to the date of the relevant breach;

injunctive relief related to the construction of new facilities and equipment;

restrictions on the operation of existing facilities and equipment;

temporary suspension from participating in bidding processes for new concessions;

intervention by ANEEL in the management of the concessionaire in breach; and

termination of the concession.

In addition, the Brazilian government has the power to terminate any of our concessions prior to the end of the concession term in the case of bankruptcy or dissolution, or by means of expropriation for reasons related to the public interest.

We cannot assure you that ANEEL will not impose penalties or terminate our concessions in the event of a breach. Any compensation we may receive upon the termination of the concession contract may not be sufficient to compensate us for the full value of certain investments. If any of our concession agreements are terminated and we are at fault, the effective amount of compensation could be reduced through fines or other penalties. Termination or imposition of penalties could adversely affect our business, results of operations and financial condition.

*We are uncertain as to the renewal of our concessions.*



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We carry out our generation, transmission and distribution activities pursuant to concession agreements entered into with the Federal Government. The Brazilian Constitution requires that all concessions relating to public services be awarded through a bidding process. In 1995, in an effort to implement these constitutional provisions, the Federal Government adopted certain laws and regulations, known collectively as the Concessions Law, governing bidding procedures in the electricity industry. In accordance with the Concessions Law, as modified by the New Industry Model Law, upon application by the concessionaire, existing concessions may be renewed by the Federal Government for additional periods of up to 20 years without being subject to the bidding process, provided that the concessionaire has met minimum performance standards and that the proposal is otherwise acceptable to the Federal Government.

In light of the degree of discretion granted to the Federal Government by the Concessions Law and the concession contracts with respect to renewal of existing concessions, and given the lack of long-standing precedents with respect to the Federal Government's exercise of such discretion and interpretation and application of the Concessions Law, we cannot assure you that new concessions will be obtained or that concessions will be renewed on terms as favorable as those currently in effect. See Item 4. Information on the Company Competition Concessions and The Brazilian Power Industry Concessions in Annex A. In addition, it is possible that our large industrial clients could be authorized by ANEEL to generate electric energy for self consumption or sale to third parties, in which case they may obtain an authorization or concession for the generation of electric power in a given area, which could adversely affect our results of operations.

Non-renewal of our concessions could adversely affect our business, results operations and financial condition.

***The present structure of the Brazilian electricity sector is highly concentrated in hydroelectric generation, which makes it subject to certain risks.***

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The Brazilian electricity industry, highly concentrated in hydroelectric generation, faces a natural limitation to its generation capacity. Hydroelectric power plants cannot generate more electricity than is made possible by the country's water resources. Natural factors could affect our generating capacity, by increasing or reducing the level of reservoirs. Control of the level of reservoirs by the ONS seeks to optimize the level of water available for hydroelectric generation in each of the power plants associated with the respective reservoirs. In this context, the ONS could, for example, prevent a generating plant located at the beginning of a river from increasing its throughput of water, if this were to negatively affect the other plants further down the same river. In the same way, the ONS may decide to increase thermal generation and reduce hydro generation in order to conserve water in the reservoirs.

Periods of drought could lead to a reduction of the hydro generating capacity, thus obliging us to buy energy in the wholesale market to meet the selling contracts we have made. Shortages and/or rationing due to bad hydrological conditions could result in a reduction of revenue and reduced cash flow. Any limitation on our electricity generation capacity could adversely affect our business, results of operations and financial condition.

*Delays in the expansion of our facilities may significantly increase our costs.*





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We are currently engaged in the construction of additional hydroelectric plants and the evaluation of other potential expansion projects. Our ability to complete an expansion project on time, within a determined budget and without adverse economic effects, is subject to a number of risks. For instance:

we may experience problems in the construction phase of an expansion project;

we may face regulatory or legal challenges that delay the initial operation date of an expansion project;

our new or modified facilities may not operate at designated capacity or may cost more to operate than we expect;

we may not be able to obtain adequate working capital to finance our expansion projects; and

we may encounter environmental issues and claims by the local population during power plant construction.

If we experience these or other problems relating to the expansion of our electricity generation, transmission or distribution capacity, our ability to sell electric energy in amounts in line with our projections may be harmed and we may be exposed to increased costs. Consequently, we may fail to produce the revenues we anticipate in connection with such expansion projects.

*Impositions and restrictions by the environmental agencies could cause additional costs for us.*



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Our operations related to the generation, transmission and distribution of electricity as well as to the distribution of natural gas, are subject to various federal, state and municipal laws and regulations, and also to numerous requirements relating to the protection of health and the environment.

Non-compliance with environmental laws and regulations could, independently of the obligation to redress any damages that may be caused, result in criminal and administrative sanctions being applied. Based on Brazilian legislation, criminal penalties such as restricting rights, and even imprisonment, may be applied to individuals (including managers of legal entities), and penalties such as fines, restriction of rights or community service may be applied to legal entities. With respect to administrative sanctions, depending on the circumstances, the environmental authorities may impose warnings and fines, require partial or total suspension of activities; suspend or restrict tax benefits or cancel or suspend financing lines from governmental lending establishments as well as prohibit the entity from contracting with governmental agencies, companies and authorities. Any of these events could adversely affect our business, results of operations or financial condition.

*Our level of consumer default could adversely affect our business, results of operations and financial condition.*



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As of December 31, 2004, our total past due receivables from final consumers were approximately R\$596 million, corresponding to 7.7% of our net revenue for 2004. Approximately 13.4% of the past due receivables were owed by entities in the public sector. We may be unable to recover debts from several municipalities and other defaulting clients which are being renegotiated. If these debts are not totally or partially recovered, we will experience an adverse impact on our business, results of operations and financial condition.

*We may not be able to complete our proposed capital expenditure program.*



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We plan to spend approximately R\$6.4 billion during the period from 2005 through 2009 on the construction of new power installations and the refurbishment and maintenance of existing power plants and transmission and distribution systems. Our ability to carry out this capital expenditure program is dependent upon a number of factors, including our ability to charge adequate rates for our services, our access to domestic and international capital markets and a variety of operating and other factors. In addition, our plans to expand our generation and transmission capacity are subject to the competitive bidding process governed by the Concessions Law. We cannot give you any assurance that we will have the financial resources to complete this program.

*Our ability to distribute dividends is subject to limitations.*



Whether or not you receive a dividend depends on the amount of the mandatory distribution required under our bylaws, whether our financial condition permits us to distribute dividends under Brazilian law, and whether our shareholders, on the recommendation of our Board of Directors acting in its discretion, determine that our financial condition warrants a suspension of the distribution of dividends.

Because we are a holding company with no revenue-producing operations other than those of our subsidiaries, we will be able to distribute dividends to shareholders only if we receive dividends or other cash distributions from our subsidiaries.

*Our investment in the telecommunications sector may not have the return we expect.*



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Empresa de Infovias S.A., our telecommunications subsidiary, began operations in January 2001 and its subsidiary, WAY TV Belo Horizonte S.A., or WAY TV, began operations in 2002. We consider these businesses to be a strategic use of our existing infrastructure. The telecommunications business will require additional investments to be considered complete and competitive. We perform periodic evaluations of Empresa de Infovias S.A. and WAY TV, in order to determine their ability to run their businesses on a stand-alone and profitable basis, as well as to determine the need for an impairment reserve for this investment. Although currently available projections do not indicate a need for an impairment reserve, we can not assure that such an impairment reserve will not be required or that our investment in the telecommunications sector will not have an adverse impact on our financial condition.

*We operate without general third party liability and catastrophe insurance policies.*



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We do not have general third party liability insurance covering accidents and have not asked for bids relating to this type of insurance. However, we may contract for this type of insurance in the future. In addition, we have not asked for bids for, nor do we carry, insurance coverage for major catastrophes affecting our facilities such as earthquakes and floods, for business interruption risk or for operating system failures. Accidents or catastrophic events may adversely affect our business, results of operations or financial condition. See Item 10. Additional Information Insurance.

*We will need short-term funds to pay and refinance our obligations.*



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On December 31, 2004, our total debt was R\$4,167 million, of which R\$1,417 million matures in 2005.

We will need funds in the short term to pay and refinance these obligations. For this reason, we intend to refinance our debt profile in 2005 to lengthen maturities. We plan to raise approximately R\$1.5 billion in 2005.

We cannot assure you that we will be able to raise these funds prior to the maturities of our current debt obligations, in the amounts necessary or at competitive rates. If the refinancing does not successfully take place, we may not be able to pay our debt. On the other hand, if we simply pay our debt without refinancing, our investment program could suffer significant delays, which could adversely affect our business, results of operations or financial condition.

*We are exposed to foreign exchange rate risk.*

As of December 31, 2004, approximately 26.9% of our total indebtedness was denominated in currencies other than the *real* (76.6% in U.S. dollars). If the U.S. dollar/*real* exchange rate appreciates, our financing expenses will increase and our results of operations and financial condition could be adversely affected. While 37.0% of our debt denominated in foreign currencies is subject to currency swaps that convert our foreign currency obligations into *reais* in order mitigate this risk, we cannot assure you that these hedging arrangements will be sufficient to avoid an adverse effect on our business, results of operations and financial condition in case of unfavorable exchange rate fluctuations.

*We may incur losses in connection with pending litigation and arbitration.*





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We are currently defending several legal proceedings relating to civil, administrative, environmental, tax and other claims. These claims involve a wide range of issues and seek substantial amounts of money. Several individual disputes account for a significant part of the total amount of claims against us. Our consolidated financial statements include reserves relating to litigation and arbitration claims totaling R\$303 million as of December 31, 2004 (excluding labor-related matters) for probable and reasonably estimable losses and expenses we may incur in connection with pending litigation. In the event that our reserves for litigation and arbitration claims prove to be insufficient, the payment of litigation claims in an amount in excess of the reserved amounts could have an adverse effect on our business, results of operations or financial condition.

*Labor-related legal claims, strikes and/or work stoppages could have an adverse impact on our business.*



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Substantially all of our employees are covered by Brazilian labor legislation applicable to private sector employees. We have entered into a collective bargaining agreement with the labor unions representing most of these employees.

We are currently defending a number of labor-related claims brought by our employees that generally relate to overtime and hazardous occupation compensation. As of December 31, 2004, these employees were seeking, in the aggregate, approximately R\$138.5 million in compensation, and at that date we had accrued a liability of approximately R\$110.8 million for losses we expect from these claims. For a more detailed discussion of labor-related proceedings, see Item 8. Financial Information Legal Proceedings Labor and Pension Fund Obligations.

We have not experienced any material labor unrest during the last four years. Nevertheless, our operations might be interrupted by a labor disturbance in the future. We do not carry insurance for losses incurred as a result of business interruptions caused by labor action. In the event of a strike, we might face an immediate loss of revenue.

Contract disputes, strikes, legal claims or other types of conflicts relating to our employees or the labor unions that represent them may have an adverse effect on our business, results of operations or financial condition and our ability to maintain ordinary service levels or otherwise operate our business in the manner that our customers expect.

*Foreign shareholders may not be able to enforce judgments against our directors or officers.*



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All of our directors and officers named in this annual report reside in Brazil. Substantially all of our assets, as well as the assets of these persons, are located in Brazil. As a result, it may not be possible for foreign shareholders to effect service of process within the United States or other jurisdictions outside Brazil upon these persons, attach their assets, or enforce against them or us in United States courts, or the courts of other jurisdictions outside Brazil, judgments predicated upon the civil liability provisions of the securities laws of the United States or the laws of such other jurisdictions. See Item 10. Additional Information Difficulties of Enforcing Civil Liabilities Against Non-U.S. Persons.

*Effective control of CEMIG is subject to judicial challenge.*





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In connection with the purchase in 1997 of approximately 33% of our common shares by Southern Electric Brasil Participações Ltda., or Southern, the State Government entered into a shareholders' agreement with Southern, granting Southern control over certain significant corporate decisions. In 1999, the State Government filed a lawsuit seeking to nullify the shareholders' agreement on constitutional grounds. In August 2001, after several rulings and appeals, the Minas Gerais State Court of Appeals ruled that the shareholders' agreement is null and void. In December 2003, this ruling was appealed to the Superior Tribunal de Justiça (Superior Court of Justice), which upheld the Minas Gerais State Court of Appeals ruling. The decision of the Superior Court of Justice is subject to request for amendment and therefore the effective control of CEMIG remains subject to further judicial challenge in the Supreme Court (Supremo Tribunal Federal). As a result, Southern could retroactively challenge the legitimacy of certain decisions taken by our Board of Directors while these legal proceedings are pending. See Item 8. Financial Information Legal Proceedings Shareholders' Agreement and Item 10. Additional Information Material Contracts Shareholders' Agreement, dated June 18, 1997, between the State Government and Southern.

### **Risks Relating to Brazil**



*The Brazilian government exercises a significant influence on the Brazilian economy. Political and economic conditions can have a direct impact on our business.*



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The Brazilian government intervenes frequently in the country's economy, in monetary, fiscal and regulatory policy. Our business, results of operations or financial condition may be adversely affected by changes in government policies, and also by:

fluctuations in the exchange rate;

inflation;

instability of prices;

changes in interest rates;

fiscal policy;

other political, diplomatic, social and economic developments which may affect Brazil or the international markets;

control on capital flow; and

limits on foreign trade.

Measures by the Brazilian government to maintain economic stability, and also speculation on any future acts of the government, can generate uncertainties in the Brazilian economy and increased volatility in the domestic capital markets, adversely affecting our business, results of operations or financial condition. If the political and economic situations deteriorate, we may face increased costs.

*Inflation and certain governmental measures to curb inflation may contribute significantly to economic uncertainty in Brazil and could harm our business and the market value of the ADSs and our preferred shares.*

Brazil has in the past experienced extremely high rates of inflation. Inflation, and some of the Brazilian government's measures taken in an attempt to curb inflation, have had significant negative effects on the Brazilian economy. Since the introduction of the *real* in 1994, Brazil's inflation rate has been substantially lower than in previous periods. However, inflationary pressures persist, and action taken in an effort to curb inflation, coupled with speculation about possible future governmental actions, have contributed to economic uncertainty in Brazil and



heightened volatility in the Brazilian securities market. According to the *Índice Nacional de Preços ao Consumidor Amplo*, or IPCA, a consumer price index, the Brazilian annual inflation rates were 12.5%, 9.3% and 7.6% in 2002, 2003 and 2004, respectively. No assurance can be given that inflation will remain at these levels.

Future measures taken by the Brazilian government, including interest rate increases, intervention in the foreign exchange market and actions to adjust or fix the value of the *real* may trigger increases in inflation, and consequently, have adverse economic impacts on our business, results of operations and financial condition. If Brazil experiences high inflation in the future, we may not be able to adjust the rates we charge our customers to offset the effects of inflation on our cost structure.

Substantially all of our cash operating expenses are denominated in *reais* and tend to increase with Brazilian inflation. Inflationary pressures may also hinder our ability to access foreign financial markets or may lead to further government intervention in the economy, including the introduction of government policies that could harm our business, results of operations and financial condition or adversely affect the market value of our preferred shares and as a result, our ADSs.

*Exchange rate instability may adversely affect our business, results of operations and financial condition and the market price of the ADSs and our preferred shares.*

The Brazilian currency has been devalued periodically during the last four decades. Throughout this period, the Brazilian government has implemented various economic plans and utilized a number of exchange rate policies, including sudden devaluations, periodic mini-devaluations during which the frequency of adjustments has ranged from daily to monthly, floating exchange rate systems, exchange controls and dual exchange rate markets. Although over long periods depreciation of the Brazilian currency generally has correlated with the rate of inflation in Brazil, devaluation over shorter periods has resulted in significant fluctuations in the exchange rate between the Brazilian currency and the U.S. dollar and currencies of other countries.

The *real* depreciated against the noon buying U.S. dollar by 9.3% in 2000 and by 18.7% in 2001. In 2002, the *real* depreciated 52.3% against the U.S. dollar, due in part to political uncertainty surrounding the Brazilian presidential elections and the global economic slowdown. Although the *real* appreciated 18.25% against the U.S. dollar in 2003 and a further 8.1% in 2004, no assurance can be given that the *real* will not depreciate against the U.S. dollar again. On May 18, 2005, the noon buying U.S. dollar/*real* exchange rate was R\$2.4625 per U.S.\$1.00. See Exchange Rates .

There are no guarantees that the exchange rate between the *real* and the U.S. dollar will stabilize at current levels. Although we have managed our existing U.S. dollar debt obligations in order to protect against fluctuations in the dollar/*real* exchange rate, we could in the future experience monetary losses relating to these fluctuations. See Item 11. Quantitative and Qualitative Disclosures about Market Risk Exchange Rate Risk for information about our foreign exchange risk hedging policy.

Depreciations of the *real* relative to the U.S. dollar also create additional inflationary pressures in Brazil that may negatively affect us. Currency depreciations generally curtail access to foreign financial markets and may prompt government intervention, including recessionary governmental policies. Currency depreciations also reduce the U.S. dollar value of distributions and dividends on the ADSs and the U.S. dollar equivalent of the market price of preferred shares and, as a result, the ADSs. On the other hand, appreciation of the *real* against the U.S. dollar may lead to deterioration of the country's current account and the balance of payments, as well as to a dampening of export-driven growth.

*Changes in economic and market conditions in other countries, especially Latin American and emerging market countries, may adversely affect our business, results of operations and financial condition, as well as the market price of our preferred shares and ADSs.*

The market value of securities of Brazilian companies is affected to varying degrees by economic and markets conditions in other countries, including other Latin American and emerging market countries. Although economic conditions in such countries may differ significantly from economic conditions in Brazil, investors



reactions to developments in these other countries may have an adverse effect on the market value of securities of Brazilian issuers. Crises in other emerging market countries may diminish investor interest in securities of Brazilian issuers, including us. This could also make it more difficult for us access the capital markets and finance our operations in the future on acceptable terms or at all. Due to the characteristics of the Brazilian electricity industry (which requires significant investments in operating assets) and due to our financing needs, if access to the capital and credit markets is limited, we could face difficulties in completing our investment plan and refinancing our obligations which could adversely affect our business, results of operations and financial condition.

**Risks Relating to the Preferred Shares and ADSs**



*The preferred shares and ADSs generally do not have voting rights.*



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In accordance with the Brazilian Corporate Law and our by-laws, holders of the preferred shares, and, by extension, holders of the ADSs, are not entitled to vote at our shareholders' meetings, except in very limited circumstances. Holders of ADSs may also encounter difficulties in the exercise of certain rights, including limited voting rights. Under some circumstances, such as failure to provide the depositary with voting materials on a timely basis, holders of ADSs may not be able to vote by instructing the depositary.

*Exchange controls and restrictions on remittances abroad may adversely affect holders of ADSs.*



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You may be adversely affected by the imposition of restrictions on the remittance to foreign investors of the proceeds of their investments in Brazil and the conversion of *reais* into foreign currencies. The Federal Government imposed remittance restrictions for approximately three months in late 1989 and early 1990. Restrictions like these would hinder or prevent the conversion of dividends, distributions or the proceeds from any sale of preferred shares, as the case may be, from reais into U.S. dollars and the remittance of U.S. dollars abroad. We cannot assure you that the Federal Government will not take similar measures in the future. See Item 3. Key Information Exchange Rates.

*Exchanging ADSs for the underlying preferred shares may have unfavorable consequences.*





The Brazilian custodian for the preferred shares must obtain an electronic certificate of registration from the Central Bank to remit U.S. dollars abroad for payments of dividends, any other cash distributions, or upon the disposition of the shares and sales proceeds related thereto. If you decide to exchange your ADSs for the underlying preferred shares, you will be entitled to continue to rely, for five business days from the date of the exchange, on the depositary bank's electronic certificate of registration. Thereafter, you may not be able to obtain and remit U.S. dollars abroad upon the disposition of the preferred shares, or distributions relating to the preferred shares, unless you obtain your own certificate of registration under Resolution No. 2,689 of January 26, 2000, of the Brazilian *Conselho Monetário Nacional*, or National Monetary Council, which entitles foreign investors to buy and sell on the Brazilian stock exchanges. If you do not obtain this certificate, you will be subject to less favorable tax treatment on gains with respect to the preferred shares. If you attempt to obtain your own certificate of registration, you may incur expenses or suffer significant delays in the application process. Obtaining a certificate of registration involves generating significant documentation, including completing and filing various electronic forms with the Central Bank and the *Comissão de Valores Mobiliários* (the Brazilian securities regulatory body), or the CVM. In order to complete this process, the investor will usually need to have a consultant or attorney who has expertise in Central Bank and CVM regulations. Any delay in obtaining this certificate could adversely impact your ability to receive dividends or distributions relating to the preferred shares abroad or the return of your capital in a timely manner. If you decide to exchange your preferred shares back into ADSs once you have registered your investment in the preferred shares, you may deposit your preferred shares with the custodian and rely on the depositary bank's certificate of registration, subject to certain conditions. See Item 10. Additional Information Taxation Brazilian Tax Considerations.

We cannot assure you that the depositary bank's certificate of registration or any certificate of foreign capital registration obtained by you may not be affected by future legislative or other regulatory changes, or that additional Brazilian restrictions applicable to you, the disposition of the underlying preferred shares or the repatriation of the proceeds from disposition could not be imposed in the future.

***The relative volatility and illiquidity of the Brazilian securities market may adversely affect our shareholders.***



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Investing in Latin American securities, such as the preferred shares or the ADSs, involves a higher degree of risk than investing in securities of issuers from countries with more stable political and economic environments and such investments are generally considered speculative in nature. These investments are subject to certain economic and political risks, such as, among others:

changes to the regulatory, tax, economic and political environment that may affect the ability of investors to receive payment, in whole or in part, with respect to their investments; and

restrictions on foreign investment and on repatriation of capital invested.

The Brazilian securities market is substantially smaller, less liquid, more concentrated and more volatile than major securities markets in the United States. This may substantially limit your ability to sell the preferred shares underlying your ADSs at a price and time at which you wish to do so. The *Bolsa de Valores de São Paulo* – *BOVESPA*, or São Paulo Stock Exchange, the only stock exchange in Brazil upon which shares are traded, had a market capitalization of approximately US\$241.8 billion as of December 31, 2004 and an average monthly trading volume of approximately US\$9.5 billion for 2004. In comparison, the New York Stock Exchange, Inc., or the NYSE, had a market capitalization of US\$19.8 trillion as of December 31, 2004 and an average monthly trading volume of approximately US\$968.2 billion for 2004.

There is also significantly greater concentration in the Brazilian securities market than in major securities markets in the United States. The ten largest companies in terms of market capitalization represented approximately 66.9% of the aggregate market capitalization of the São Paulo Stock Exchange as of December 31, 2004. The top ten stocks in terms of trading volume accounted for approximately 49.5% of all shares traded on the São Paulo Stock Exchange in 2004. See Item 9. The Offer and Listing Trading Market.

*Shareholders may receive reduced dividend payments if our net income does not reach certain levels.*



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Under the Brazilian Corporate Law and our by-laws, we must pay our shareholders a mandatory distribution equal to at least 50% of our adjusted net income for the preceding fiscal year, based on our financial statements prepared in accordance with the accounting practices adopted in Brazil, with holders of preferred shares having priority of payment. In addition, our by-laws require us to pay holders of our preferred shares annual dividends equal to the greater of 10% of the par value of our shares or 3% of the book value of our shares. If we do not have net income or our net income is insufficient in a fiscal year, our management may recommend at the annual shareholders' meeting in respect of that year that the payment of the mandatory dividend should not be made. However, under the guarantee of the State Government, our controlling shareholder, a minimum annual dividend of 6% of par value would in any event be payable to all holders of common shares and preferred shares issued up to August 5, 2004 (other than public and governmental holders) in the event that mandatory distributions were not made for a fiscal year. See Item 8. Financial Information - Dividend Policy and Payments for a more detailed discussion.

*Holders of the ADSs and holders of preferred shares have less well-defined shareholders' rights than holders of shares in U.S. companies.*



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Our corporate governance, disclosure requirements and accounting standards applicable to Brazilian companies are governed by our by-laws and by the Brazilian Corporate Law, which may differ from the legal principles that would apply if we were incorporated in a jurisdiction in the United States, such as Delaware or New York, or in other jurisdictions outside Brazil. Your rights to protect your interests relative to actions taken by our Board of Directors or by our controlling shareholder may be less well defined and less well supported by established rules and judicial precedents than under the laws of certain jurisdictions outside Brazil.

Although Brazilian law imposes restrictions on insider trading and price manipulation, the Brazilian securities market is not as highly regulated and supervised as the U.S. securities market or markets in certain other



jurisdictions. In addition, rules and policies against self-dealing and regarding the preservation of shareholder interests are less developed and enforced in Brazil than in the United States, potentially disadvantaging holders of the preferred shares and ADSs.

*Shares eligible for future sale may adversely affect the market price of the preferred shares and the ADSs.*



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Sales of a substantial number of shares or the perception that such sales could take place could adversely affect the prevailing market price of the preferred shares and ADSs. As a consequence of the issuance of new shares or sales by existing shareholders, the market price of the preferred shares and, by extension, the ADSs, may decrease significantly.

*You may not be able to exercise preemptive rights with respect to the preferred shares.*



You may not be able to exercise the preemptive rights relating to the preferred shares underlying your ADSs unless a registration statement under the United States Securities Act of 1933, as amended, or the Securities Act, is effective with respect to those rights or an exemption from the registration requirements of the Securities Act is available. We are not obligated to file a registration statement with respect to the shares relating to these preemptive rights, and we cannot assure you that we will file any such registration statement. Unless we file a registration statement or an exemption from registration applies, you may receive only the net proceeds from the sale of your preemptive rights by the depositary or, if the preemptive rights cannot be sold, they will be allowed to lapse.

Item 4. **Information on the Company**



**Organization and Historical Background**





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We were organized in Minas Gerais, Brazil on May 22, 1952 as a *sociedade de economia mista* (a state-controlled mixed capital company) with limited liability and indefinite duration, pursuant to Minas Gerais State Law No. 828 of December 14, 1951 and its implementing regulation, Minas Gerais State Decree 3,710 of February 20, 1952. Our full legal name is Companhia Energética de Minas Gerais CEMIG, but we are also known as CEMIG. Our headquarters are located at Avenida Barbacena, 1200, Belo Horizonte, Minas Gerais, Brazil. Our main telephone number is (55-31) 3299 3711.

In order to comply with legal and regulatory provisions pursuant to which we were required to unbundle our vertically integrated businesses, we have incorporated two wholly-owned subsidiaries of CEMIG Cemig Geração e Transmissão S.A., referred to as Cemig Generation and Transmission, and Cemig Distribuição S.A., referred to as Cemig Distribution. Cemig Generation and Transmission and Cemig Distribution were created to carry out the activities of generation and transmission, and distribution, respectively.

On August 4, 2004 the State of Minas Gerais issued Law 15,290 governing the corporate restructuring of CEMIG. Subsequently, ANEEL, by Resolution 407/2004 dated December 23, 2004, approved our proposal for transfer of the concessions, assets and liabilities to the two new companies created, with CEMIG being maintained as a holding company. On December 30, 2004, an extraordinary general shareholders meeting of CEMIG authorized the transfer of assets and liabilities of CEMIG to the two wholly-owned subsidiaries Cemig Generation and Transmission and Cemig Distribution. On the same date, extraordinary general shareholders meetings of Cemig Generation and Transmission and of Cemig Distribution were held and approved capital increases of such subsidiaries. Pursuant to such shareholders meetings, CEMIG subscribed newly issued shares of each such subsidiaries, which shares were paid in with assets of CEMIG. As a consequence of this process, the assets and liabilities of the generation and transmission assets and distribution assets, were transferred to Cemig Generation and Transmission and Cemig Distribution, respectively. Cemig Generation and Transmission and Cemig Distribution began their operations on January 1, 2005.

The following chart shows our corporate structure as of May 18, 2005:

Through our subsidiaries, we are the largest integrated concessionaire of electric power generation, transmission and distribution in Brazil. We operate our generation, transmission and distribution businesses pursuant to concession agreements with the Federal Government. Until 1997, we had individual concessions for each of our generation facilities and for various regions within our distribution area. On July 10, 1997, we entered into new concession agreements with ANEEL that consolidated our various generation concessions into one agreement and our several distribution concessions into four distribution concessions covering the northern, southern, eastern and western regions of Minas Gerais. On the same date, we also entered into a new concession agreement with ANEEL with respect to our transmission operations. In connection with the unbundling, our concessions will be transferred to Cemig Generation and Transmission and Cemig Distribution, although we cannot assure you of the timing of that transfer as it will be determined by ANEEL.

At December 31, 2004, we generated electricity at 47 hydroelectric plants, four thermoelectric plants and one wind farm, and had a total installed capacity of 5,949 MW. At the same date, we owned and operated 3,017 miles of transmission lines and 238,309 miles of distribution lines. We hold concessions to distribute electricity in 96.7% of the territory of Minas Gerais.

The Brazilian electricity industry has undergone extensive regulatory restructuring as a result of which our electric generation, transmission and distribution businesses have been and will continue to be subjected to increased competition. For a more detailed description of regulatory changes that affect our business, see "The Brazilian Power Industry" in Annex A.

Pursuant to Minas Gerais state legislation, our by-laws were amended in 1984 to allow us to participate in an expanded range of activities relating to the energy sector through separate companies. In 1986, we created *Companhia de Gás de Minas Gerais* GASMIG, or Gasmig, as a subsidiary to undertake the distribution of natural gas through pipelines located in Minas Gerais. In December 2004 we sold a 40% stake in Gasmig to Petrobras Gás S.A. Gaspetro, or Gaspetro, and TSS Participações S.A, or TSS, both of which are wholly-owned subsidiaries of Petrobras S.A, for approximately R\$154 million. See Item 10. Additional

Information Material Contracts Gasmig Shareholders Agreement and Association Agreement.

Additional Minas Gerais state legislative changes enacted in 1997 authorized us to participate in non-energy activities that can be carried out using our operating assets. In January 1999, we incorporated *Empresa de Infovias S.A.*, a telecommunication service provider, as a joint venture with *AES Força Empreendimentos Ltda.*, part of the AES Corporation Group. In 2002, we purchased *AES Força Empreendimentos Ltda.*'s interest in *Empresa de*

Infovias S.A. We also provide consulting services and have entered into consulting agreements with electricity companies in several countries.

**Brazil's Energy Market**



*General*



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Traditionally, in the Brazilian electricity sector, generation, transmission and distribution activities are separated, but conducted by a small number of companies that had always been the property of either the Federal Government, or of governments of Brazil's individual states. In the last ten years, several companies controlled by the state were privatized, in an effort to increase efficiency and competition. The previous administration stated its objective to privatize the state-controlled part of the electricity sector, but the present administration has stopped this process, and moved in a new direction toward implanting a New Model for the Brazilian electricity sector as set forth in Law No. 10,848, of March 15, 2004.

### *The New Model*





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The main objectives of the new model are to guarantee: (i) security of supply; and (ii) reasonableness of rates. To guarantee supply, the new model creates the requirements (a) that distributors must contract their entire load, and will be responsible for making realistic projections of demand requirements and (b) that building new hydroelectric and thermal plants will be determined in ways that best balance security of supply and reasonableness of rates. The means of achieving reasonableness of rates are to be the following: (a) all purchases of electricity by distributors are to be by auction, on the lowest-rate criterion; (b) contracting is to be through the Pool system, as described below; and (c) contracting of load will be separated into two types of transactions, both of which will always be by auction: (i) contracting of the electricity of the new plants, which will target expansion; and (ii) contracting of the electricity of the existing plants, which will target the existing electricity demand.

The new model also creates two environments for the contracting of electricity supply: (i) the Regulated Contracting Environment (ACR), for contracting of electricity to meet the demands of distributors supplying captive consumers under regulated rates; and (ii) the free contracting environment (ACL), for contracting of energy to supply Free Consumers, through freely negotiated contracts. Distributors will be allowed to operate only in the regulated environment, while generators may operate in both, maintaining their competitive characteristic.

Expansion of the sector will be executed by the concession-granting power. Two new institutional agents have been created: (i) the Energy Research Company (EPE), a state-controlled company responsible for execution of the planning of expansion of generation and transmission; and (ii) the Electricity Trading Chamber (CCEE), a private company, which is the successor of the Wholesale Energy Market, and is responsible for management of the joint contracting of electricity to meet the needs of regulated consumers (the Pool system).

### *Regulation under the new model*



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The Brazilian electricity industry is regulated by ANEEL. After the enactment of Law No. 10,848, ANEEL's primary responsibility is to regulate and supervise the power industry in line with the policy to be dictated by the MME and to respond to matters which are delegated to it by the Brazilian government and by the MME. ANEEL's current responsibilities include, among others, (i) administering concessions for electricity generation, transmission and distribution activities, including the approval of electricity rates, (ii) enacting regulations for the electricity industry, (iii) implementing and regulating the exploitation of hydroelectric resources, (iv) promoting the public bidding process for new concessions, (v) settling administrative disputes among electricity generation entities and electricity purchasers and (vi) defining the criteria and methodology for the determination of transmission rates.

### *Rates*



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Electric energy rates in Brazil are set by ANEEL, which has the authority to readjust and review rates in accordance with the provisions under the relevant concession contracts. Each distribution company's concession contract provides for an annual rate adjustment (*reajuste anual*). In general, Parcel A costs are fully passed through

to consumers. Parcel A costs are the portion of the regular rate calculation formula, which provides for the recovery of certain costs that are not within the control of the distribution company. Parcel B costs, which are costs that are under the control of the distributors, are restated for inflation in accordance with the General Market Price Index (Índice Geral de Preços do Mercado), or IGP-M index.

As part of our annual rate adjustment ANEEL, through Resolution No. 83 dated as of April 7, 2004, provided for an average increase in the rates that we can charge end users from April 2004 until April 2005. In May 2004, ANEEL re-issued Resolution No. 83 and revised the basis for such average increase which resulted in lower rates. On April 6, 2005, through Resolution No. 87 ANEEL established an average rate adjustment of 23.88%. This adjustment includes a component of 1.67% representing an increase to recoup revenue we did not achieve in 2004 due to the lower rates under Resolution No. 83 as re-issued.

Concessionaires of electricity distribution are also entitled to periodic revisions (*revisão periódica*) every few years. These revisions are aimed at (i) assuring necessary revenues to cover efficient Parcel B operational costs and adequate compensation for investments deemed essential for the services within the scope of each such company's concession and (ii) determining the X factor, which is calculated based on expected productivity gains from increases in scale, evaluations by consumers (verified by ANEEL) and labor costs.

On April 8, 2003, we went through our first periodic rate revision and ANEEL established a 31.53% temporary average increase to be applied to our rates. On April 4, 2005, through Resolution No. 71, ANEEL reconsidered such decision and established a 44.41% average increase to be applied to our rates. In order to guarantee low rates to our end consumers, ANEEL only allowed us to reposition our rates up to 31.53% retroactive to April 8, 2003. ANEEL has also indicated that the rate adjustments expected for the years from 2004 to 2007 will be adjusted to recover the difference between the average rate increase of 44.41% we were entitled to and the 31.53% rate adjustment that was authorized. On April 8, 2005 our rate adjustment increase included a portion of the difference related to the difference between the average rate increase we were entitled to in 2004 and the rate adjustment authorized for that year.

In addition, concessionaires of electricity distribution are entitled to extraordinary review of rates (*revisão extraordinária*), on a case by case basis, to ensure their financial equilibrium and compensate them for unpredictable costs, including taxes, that significantly change their cost structure.

ANEEL has also issued regulations that govern the access to the distribution and transmission facilities and establish the rate for use of the local distribution grid, or Distribution Usage Rates ( TUSD ), and the rate for the use of the interconnected transmission grid, or Transmission Usage Rates ( TUST ). The rates to be paid by distribution companies, generators and independent customers for use of the interconnected power system are reviewed annually. The review of the TUST takes into account the revenues that are permitted of transmission concessionaires pursuant to their concession contracts. For more detailed information regarding the rate-setting structure in Brazil, see The Brazilian Power Industry Rates for the Use of the Distribution and Transmission Systems in Annex A.

### ***Concessions***





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Under the Brazilian Constitution, companies seeking to construct or operate a generation, transmission or distribution facility in Brazil are required to apply for an authorization or a concession from the Federal Government which is generally granted through a public bidding process conducted by ANEEL. Concessions grant exclusive rights to generate electricity in a particular plant, and to transmit or distribute electricity in a particular area for a specified period of time, generally 35 years for new generation concessions, 30 years for new transmission and distribution concessions, and 20 years for the renewal of existing concessions. For more detailed information regarding concessions, see *The Brazilian Power Industry Concessions* in Annex A.

### *Land Acquisition*



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The concessions granted to us by the Federal Government do not include a grant of the land upon which the plants are located. Electricity concessionaires in Brazil typically have to negotiate with the individual

landowners to obtain needed land. However, in the event that a concessionaire is unable to obtain needed land in this way, such land may be condemned for the concessionaire's use through specific legislation. In cases of governmental condemnation, the concessionaires may have to participate in negotiations relating to the amount of compensation with landowners and the resettlement of communities to other locations. Our resettlement policy has generally resulted in the settlement of condemnation disputes.

#### **Unbundling under the New Industry Model**

Law No. 10,848/04, which provides for the new industry model, prohibits holders of distribution concessions, permissions or authorizations that operate in the interconnected power system from: (i) performing activities related to generation, transmission and sale of energy to Free Consumers at freely negotiated prices; (ii) holding interest in other companies, directly or indirectly, other than (a) in companies whose corporate purpose is to manage financial resources necessary for rendering of services or (b) as provided in the concession contracts; or (iii) performing activities outside their corporate purpose, except as provided by law and the concession contracts. These restrictions do not apply to distributors: (i) supplying energy to isolated electricity systems; (ii) supplying their own market, provided such market has a demand of less than 500 GWh/year and the totality of energy produced is destined to such market; or (iii) when funding, investing or borrowing funds destined to the distributor itself or a company of the same economic group, subject to prior agreement by ANEEL. Similarly, holders of generation concessions or authorizations that operate in the interconnected system may not be affiliates or controlling shareholders of companies which are responsible for distribution activities.

Holders of concessions, permissions and authorizations for generation and distribution have 18 months in which to adapt to the rules for unbundling referred to above, from the date of publication of Law No. 10,848/04 that is, until September 2005. ANEEL may extend this period once, for 18 months, if the concessionaire is unable to comply with the requirements for reasons beyond its control.

In order to comply with regulatory provisions pursuant to which we were required to unbundle our vertically integrated businesses, we have incorporated two wholly-owned subsidiaries of CEMIG – Cemig Generation and Transmission, and Cemig Distribution – created to carry out the activities of electricity generation and transmission, and distribution, respectively. For more detailed information regarding these entities and the corporate restructuring of CEMIG, see Organization and Historical Background.

#### **Unbundling in the Concession Contracts**



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The obligation to implement the unbundling of the generation, transmission and distribution activities in separate operational companies was already provided for in several concession contracts. According to such contracts, the corporate reorganization should have been concluded by December 31, 2000, but we failed to comply with this deadline.

As a result of such non-compliance, ANEEL imposed a fine of R\$3.7 million on us at the beginning of 2001, which we contested, achieving not only its cancellation by ANEEL, but also a new deadline for completing the corporate reorganization, namely September 21, 2002. Since we also failed to complete the process by the new deadline, ANEEL imposed another fine on us, of R\$5.5 million, on November 11, 2002. On April 3, 2003 we appealed this fine, applying for its suspension. On February 23, 2005, ANEEL issued a ruling reducing the fine to R\$2.7 million. We continue to contest this fine. No reserve has been recorded for this potential claim since we believe we have a meritorious defense against this and any other possible penalties that may be imposed regarding this matter. We believe ANEEL is likely to analyze these proceedings taking into consideration the new regulations of the electricity industry, so that in practice, it is unlikely that there is going to be an outcome before September 2005.

### **Capital Expenditures**



Capital expenditures for the years ended December 31, 2004, 2003 and 2002, in millions of *reais*, are as follows:



	2004	Year ended December 31, 2003	2002
Empresa de Infovias S.A. equity acquisition			87
Others	10	4	16
Total capital expenditures under affiliates	10	4	103
Generation power projects under Property, plant and equipment	679	594	413
Transmission network expansion	59	97	59
Distribution network expansion	245	263	278
Others	78	75	119
Total capital expenditures under property, plant and equipment	1,061	1,029	869
Total Capital expenditures	1,071	1,033	972

We currently project total capital expenditures of approximately R\$2,068 million in 2005. The principal uses of these expenditures are expected to be for expansion of our distribution infrastructure and increases in our generation capacity.

### Business Overview

*General*

During 2004, we generated at our own plants approximately 64.5% of the aggregate amount of energy sold by us to end users or lost due to technical and non-technical reasons, and we purchased the balance from third parties. We are required, like other Brazilian electric utilities, to purchase electricity from Itaipu in an amount determined by the Federal Government based on our electricity sales. See Generation and Purchase of Electric Power Purchase of Electric Power Itaipu. In addition, we purchase energy from other concessionaires and the interconnected power system. See Generation and Purchase of Electric Power Purchase of Electric Power Interconnected Power System. We also purchase energy generated by self power producers, or SPPs, and independent power producers, or IPPs, that are located within our concession area.

The following table sets forth certain information, in GWh, pertaining to the electricity that we generated, purchased from other sources and delivered during the periods specified:

## ELECTRIC ENERGY BALANCE (CEMIG MARKET)

(GWh)	Year ended December 31,		
	2004	2003	2002
<b>RESOURCES (1)</b>	45,117	51,927	49,372
Electricity generated by CEMIG (2)	26,922	27,025	21,608
Electricity generated by auto-producers	1,581	1,650	1,234
Electricity generated by Ipatinga	237	351	348
Electricity generated by Barreiro	72		
Electricity generated by Sá Carvalho (3)	468	305	425
Electricity generated by Horizontes (3) (4)	105	59	
Electricity bought from Itaipu	11,936	12,220	12,735
Electricity bought from the national grid and other companies (5)		10,317	13,022
Electricity bought from CCEE and other companies (6)	3,796		
<b>REQUIREMENTS</b>	45,117	51,927	49,372
Electricity delivered to final consumers (7)	36,669	35,248	34,862
Electricity delivered to auto-producers	1,472	1,323	1,323
Electricity delivered by Ipatinga	237	351	348
Electricity delivered by Barreiro	72		
Electricity delivered by Sá Carvalho (3)	474	305	425
Electricity delivered by Horizontes (3)	80	59	
Electricity delivered to the national grid and other companies (5)		9,720	7,863
Electricity delivered to the CCEE and other companies (6) (8)	1,798		
Losses	4,315	4,921	4,551

(1) In 2004 there was a change in the method of calculating and recording transactions in the wholesale market and with other companies, as stated in Notes 5 and 6. This change is responsible for the variation in the figures for sources and demand from 2003 to 2004.

(2) Discounting the losses attributed to generation (637 GWh) and the internal consumption of the generating plants (22GWh).

(3) Up to 2003, these portions referred to the total amounts of energy available and demand. Beginning in 2004, the short-term transactions on the CCEE and with other companies are included in the items Electricity bought from the CCEE and other companies and Electricity delivered to the CCEE and other companies .

(4) Includes the generation by the Pai Joaquim small hydro plant.

(5) In previous years, this portion represented contracts and the physical interchanges between CEMIG's network and the national grid, and also optimization supply.

(6) Beginning in 2004, this amount refers to contracts, purchases and sales of electricity under the CCEE, including the Energy Reallocation Mechanism (*Mecanismo de Realocação de Energia*).

(7) Includes electricity delivered to consumers outside the concession area.

(8) Includes 270 GWh of Initial Contracts and bilateral contracts with other agents of the CCEE.

*Generation*

According to ANEEL, at December 31, 2004, we were the seventh largest electric power generation concessionaire in Brazil as measured by total installed capacity. At December 31, 2004, we generated electricity at 47 hydroelectric plants, four thermoelectric plants and one wind farm and had a total installed generation capacity of 5,949 MW, of which hydroelectric plants accounted for 5,764 MW, thermoelectric plants accounted for 184 MW and our wind farm accounted for 1 MW. Seven of our hydroelectric plants accounted for approximately 84% of our installed electric generation capacity in 2004. We supplied approximately 93% of the electricity consumed in Minas Gerais during 2004. During the year ended December 31, 2004, we generated approximately 64.5% of the aggregate amount of electricity we delivered to end users or lost due to technical and non-technical reasons. See Energy Losses.

*Transmission*



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We are engaged in the electric power transmission business, which consists of transporting electric power from the facilities where it is generated to the distribution networks for delivery to end users. We transport energy produced at our own generation facilities as well as energy that we purchase from Itaipu, the interconnected power system and other concessionaires. Our transmission network is comprised of power transmission lines with a voltage capacity equal to or greater than 230 kV and is part of the national transmission grid regulated by the ONS. See The Brazilian Power Industry in Annex A. As of December 31, 2004, our transmission network in Minas Gerais consisted of 1,344 miles of 500 kV lines, 1,206 miles of 345 kV lines and 467 miles of 230 kV lines, as well as 32 substations with a total of 94 transformers and an aggregate transformation capacity of 15,393 MVA.

### *Distribution*





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We have a distribution concession in Minas Gerais that grants us rights to supply electric energy to consumers within our concession area except for consumers that may be eligible, in accordance with the legislation, to become Free Consumers (currently consumers with demand equal to or greater than 3 MW). Our concession area covers approximately 219,103 square miles, or 96.7% of the territory of the state. As of December 31, 2004, we owned and operated 238,309 miles of distribution lines, through which we supplied electricity to nearly 5.9 million customers. At December 31, 2004, we were the largest electricity distribution concessionaire in Brazil in terms of GWh sold to end users. Of the electricity we supplied to final customers as of December 31, 2004, 61.5% was to industrial customers, 17.4% was to residential customers, 9.4% was to commercial customers and 11.7% was to rural and other customers. These figures include the energy sold by Barreiro and Pai Joaquim of 73 GWh and 29 GWh, respectively, which were not consolidated in our financial statements.

### *Other Businesses*



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While our main business consists of the generation, transmission and distribution of electric power, we also engage in the business of distributing natural gas in Minas Gerais through our majority-owned subsidiary Gasmig. We also engage in the telecommunications business through our consolidated subsidiary Empresa de Infovias S.A., a company created for the purpose of providing a fiber-optic and coaxial cable network installed along our transmission and distribution lines through which telecommunication services can be provided. We are also engaged in the national and international consulting business through our subsidiary Efficientia S.A.

### **Revenue Sources**



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The following table shows the revenues attributable to each of our principal revenue sources, for the periods indicated:

	Year ended December 31,		
	2004	2003	2002
Electricity sales to final customers	8,561	7,179	5,458
Regulatory extraordinary rate adjustment	89	63	281
Deferred rate adjustment	640	199	
Electricity sales to the interconnected power system	36	56	161
Use of basic transmission network	245	257	185
Natural gas sales	420	367	200
Services rendered	29	31	23
Telecommunication and other	87	70	37
<b>Total</b>	<b>10,107</b>	<b>8,222</b>	<b>6,345</b>

**Generation**

*Generation*



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The following table sets forth certain operating information concerning our electric power generation plants as of December 31, 2004:

Facility	Installed Capacity (MW)	Assured Energy(1) (average MW)	Year Commenced Operations	Installed Capacity % of Total	Date Concession Expires
<b>Major Hydroelectric Plants</b>					
São Simão	1,710	1,281.00	1978	28.7	January 2015
Emborcação	1,192	497.00	1982	20.0	July 2005 (7)
Nova Ponte	510	276.00	1994	8.6	July 2005 (7)
Jaguara	424	336.00	1971	7.1	August 2013
Miranda	408	202.00	1998	6.9	December 2016
Três Marias	396	239.00	1962	6.7	July 2015
Volta Grande	380	229.00	1974	6.4	February 2017
Salto Grande	102	75.00	1956	1.7	July 2015
Sá Carvalho	78	58.00	2000 (2)	1.3	December 2024
Rosal	55	30.00	2004 (2)	0.9	May 2032
Itutinga	52	28.00	1955	0.9	July 2015
Camargos	46	21.00	1960	0.8	July 2015
Porto Estrela	37 (3)	18.60 (3)	2001	0.6	July 2032
Igarapava	30.5 (4)	19.72 (4)	1999	0.5	December 2028
Funil	88 (5)	43.61 (5)	2002	1.5	December 2035
Queimado	86.6 (6)	47.85 (6)	2004	1.5	January 2033
Pai Joaquim	23	13.91	2004	0.4	April 2032
Piau	18	8.00	1955 (2)	0.3	July 2015
Gafanhoto	14	6.68	1946	0.2	July 2015
<b>Smaller Hydroelectric Plants</b>	<b>114</b>	<b>61.88</b>		<b>1.9</b>	
<b>Thermoelectric Plants</b>					
Igarapé	131	93.00	1978	2.2	August 2024
Ipatinga	40		2000 (2)	0.7	December 2014
Barreiro	12.90	11.45	2004	0.2	April 2023
Formoso	0.4	0.22	1992	0.0	Indefinite
Wind Farm	1	0.30	1994	0.0	Indefinite
<b>Total</b>	<b>5,949.4</b>	<b>3,597.22</b>		<b>100.0%</b>	

(1) Assured Energy is the plant's long-term average output, as established by ANEEL in accordance with studies conducted by the ONS. Calculation of Assured Energy considers such factors as reservoir capacity and connection to other power plants. Contracts with final customers and other concessionaires do not provide for amounts in excess of a plant's Assured Energy.

(2) Indicates our acquisition date.

(3) Represents our interest in the Porto Estrela plant (33.3%).

(4) Represents our interest in the Igarapava plant (14.5%).

(5) Represents our interest in the Funil plant (49.0%).

(6) Represents our interest in the Queimado plant (82.50%).

(7) A renewal request for 20 more years was made to ANEEL in September 2004. See Concessions Competition .

The following tables set forth certain additional operating information pertaining to our electricity generation operations as of the dates indicated:

	Circuit Length of Generation Lines in Miles (from power plants to generation substations)			
	As of December 31,			
	2004		2003	2002
<b>Voltage of Connection Lines</b>				
500 kV	4		6	6
345 to 230 kV	7		10	10
161 to 138 kV	42		6	6
69 to 13.8 kV	102	(1)	53	53
<b>Total</b>	<b>155</b>		<b>75</b>	<b>75</b>

	Step-Down Transformation Capacity(2) of Generation Substations			
	As of December 31,			
	2004		2003	2002
<b>Number of step-down substations</b>	<b>52</b>		<b>48</b>	<b>48</b>
<b>MVA</b>	<b>6,433</b>		<b>6,240</b>	<b>6,240</b>

(1) We increased the circuit length of our 69 kV connection lines in 2004, because we bought the Rosal Facility and the Queimado Facility began operations.

(2) Step-down transformation capacity refers to the ability of a transformer to receive energy at a certain voltage and release it at a reduced voltage for further distribution.

#### *Generation Assets*



We have formed in Minas Gerais and other states of Brazil, the following wholly-owned subsidiaries to operate certain of our generation facilities and to hold the related concessions:

*Usina Térmica Ipatinga S.A.* We operate the Ipatinga thermoelectric plant through our subsidiary Usina Térmica Ipatinga S.A. This plant is an SPP installed and operated within the premises of Usinas Siderúrgicas de Minas Gerais S.A. USIMINAS, or Usiminas, a large Brazilian steel manufacturer. The plant supplies power to a large steel mill owned by Usiminas located in eastern Minas Gerais. We acquired the Ipatinga plant in 2000 for R\$90 million from Usiminas as payment for outstanding power supply debts. We have signed a power purchase agreement with Usiminas for power produced at Ipatinga. The plant currently has an installed capacity of 40 MW, generated by two units that began operating in 1984 and that use blast furnace gas as fuel.

*Sá Carvalho S.A.* We operate the Sá Carvalho hydroelectric power plant, located on the Piracicaba River in the municipality of Antônio Dias in the State of Minas Gerais, through our subsidiary Sá Carvalho S.A., which we acquired in 2000 for R\$87 million from Acesita S.A., or Acesita, a steel company. This acquisition was funded by an issuance of debentures by a special trust, UHESC S.A., which we are obligated to repay. On June 5, 2003, we renegotiated the interest rate applicable to 46.67% of the aggregate principal amount of these debentures for the following two year period and the remaining 53.33% was redeemed for R\$64 million.

*Rosal Energia S.A.* In November 2004 we bought the *Rosal* hydroelectric plant, which has installed capacity of 55 MW, from Caiuá Serviços de Eletricidade S.A., or Caiuá, for a payment of R\$134 million. The Rosal plant, the sole asset of Rosal Energia S.A., is located on the Itabapoana River, which runs along the border between the states of Espírito Santo (Municipality of Guaçuí) and Rio de Janeiro (Municipality of Bom Jesus de Itabapoana). It operates in integrated connection with the *Alegre* and *Mimoso do Sul* electricity systems, which are owned by the electricity utility of the State of Espírito Santo, Escelsa (Espírito Santo Centrais Elétricas S.A.). The plant's first and second rotors started operating in December 1999 and January 2000, respectively. It has a concession contract for 35 years, maturing in 2032. ANEEL approved the transfer of control on December 20, 2004.

*Cemig Capim Branco Energia S.A.* We incorporated Cemig Capim Branco Energia S.A. to develop the Capim Branco Power Facility in partnership with Companhia Vale do Rio Doce CVRD, or CVRD, a mining company, Comercial e Agrícola Paineiras, an agricultural company, and Companhia Mineira de Metais, a metallurgic company. The project consists of the Capim Branco I and Capim Branco II hydroelectric power plants, with installed capacity of 240 MW and 210 MW, respectively. See Capim Branco Power Facility, under

Expansion of Generation Capacity below. As of December 31, 2004, we had invested R\$24.2 million in this project. We have entered into a purchase contract with Cemig Capim Branco Energia S.A. under which we will purchase the energy produced by Capim Branco I and Capim Branco II for 20 years from the date of the start of each plant's commercial operations. This contract was submitted to ANEEL in 2002 ANEEL and was approved in December 2004. See Item 8. Financial Information Legal Proceedings Legal Proceedings Related to Environmental Matters.

*Horizontes Energia S.A.* We formed Horizontes Energia S.A., or Horizontes Energia, to generate and trade electricity as an IPP through the commercial operation of the following of our smaller hydroelectric plants: the Machado Mineiro Power Plant (located on the Pardo River in the municipality of Ninheira in the State of Minas Gerais with an installed capacity of 1.72 MW); the Salto do Paraopeba Power Plant (located on the Paraopeba River in the town of Jeceaba in the State of Minas Gerais with an installed capacity of 2.37 MW); the Salto Voltão Power Plant (located on the Chapecozinho River in the town of Xanxerê in the State of Santa Catarina with an installed capacity of 6.76 MW); and the Salto do Passo Velho Power Plant (located on the Chapecozinho River in the town of Xanxerê in the State of Santa Catarina with an installed capacity of 1.66 MW), as well as other generating projects to be acquired or built with our participation. The concession relating to the Machado Mineiro Power Plant expires on July 7, 2025 and the concessions relating to the other plants expire on October 4, 2030. Horizontes Energia S.A. currently has an agreement with clients to provide electricity from 2004 to 2005. We entered into an agreement with Horizontes Energia S.A. under which it is obligated to purchase the energy generated by the power plants held by Horizontes Energia S.A. from January 2007 through December 2016, but the approval of this contract is pending. We have requested that MME approve the volume of Assured Energy of Salto Voltão, which we expect to be 7.36 MW on average. This approval is also still pending.

*Usina Termelétrica Barreiro S.A.* We formed Usina Termelétrica Barreiro S.A. to participate, in partnership with Vallourec & Mannesmann V&M do Brasil S.A., or Vallourec & Mannesmann, a metallurgic company, in the construction and operation of the 12.9 MW Barreiro thermoelectric power plant, located on Vallourec & Mannesmann's premises in the Barreiro section of the city of Belo Horizonte in Minas Gerais. See Barreiro Thermoelectric Power Plant, under Expansion of Generation Capacity, below. As of December 31, 2004 we had invested R\$24.4 million in this project. ANEEL requested that we transfer our interest in Usina Termelétrica Barreiro S.A. to a company which we do not control. To fulfill this request, a new company called Central Termelétrica de Cogeração S.A. was formed in 2003 in partnership with Companhia de Saneamento de Minas Gerais COPASA, or COPASA, the Minas Gerais state-controlled water and sewage company, as described below. ANEEL has authorized Central Termelétrica de Cogeração S.A. to trade energy. Usina Termelétrica Barreiro S.A. still holds the assets of Barreiro thermoelectric power plant.

*CEMIG PCH S.A.* We formed CEMIG PCH S.A. to generate and trade electric energy as an IPP. ANEEL requested that we transfer our interest in CEMIG PCH S.A. to a company which we do not control. To fulfill this request, a new company called Central Hidrelétrica Pai Joaquim S.A. was formed in 2003 in partnership with COPASA, as described below. ANEEL has already authorized Central Hidrelétrica Pai Joaquim S.A. to be an IPP. CEMIG PCH S.A. still holds the assets of Pai Joaquim Small Hydroelectric Power Plant which amount to R\$49 million as of December 31, 2004.

We also have a minority interest in the following companies:

*Central Hidrelétrica Pai Joaquim S.A.* We formed Central Hidrelétrica Pai Joaquim S.A. in partnership with COPASA to satisfy ANEEL's request to transfer the concession of Pai Joaquim to a company which we do not control. Central Hidrelétrica Pai Joaquim S.A.'s main activity is the production and sale of electric energy through a small hydroelectric power plant, as an IPP of 23 MW. These assets are still held by Cemig PCH S.A. We have a 49% interest in Central Hidrelétrica Pai Joaquim S.A. We and COPASA are now negotiating an increase of our interest in this company, which has to be approved by ANEEL. We intend to sell this energy to some Free Consumers which are expected to pay higher prices than distribution companies.

*Central Termelétrica de Cogeração S.A.* We formed Central Termelétrica de Cogeração S.A. in partnership with COPASA to satisfy ANEEL's request to transfer our interest in Usina Termelétrica Barreiro S.A. to a company which we do not control. Central Termelétrica de Cogeração S.A.'s main activity is the production and sale of electric energy through a thermoelectric power plant, as an IPP of 12.9 MW. These assets are still held by

Usina Termelétrica Barreiro S.A. Commercial generation began in February 2004. We have a 49% interest in Central Termelétrica de Cogeração S.A. We and COPASA are now negotiating an increase of our interest in this company, which has to be approved by ANEEL.

*Expansion of Generation Capacity*





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Our capital investment plan submitted to ANEEL currently contemplates increasing the installed generation capacity of our hydroelectric facilities by 617 MW during the next three years through the construction of new power plants and the expansion of existing plants. New generation projects have concession periods of 35 years, beginning on the date of the concession agreement. The construction of the Capim Branco I and Capim Branco II hydroelectric power plants, the Pai Joaquim hydroelectric plant and the Barreiro thermoelectric power plant, discussed under *Generation Assets* above, constitute a part of our capital investment plan. The following is a brief description of our other projects, the completion of which are subject to various contingencies, certain of which are beyond our control:

*Queimado Hydroelectric Power Plant.* Our partner in this project is Companhia Energética de Brasília, or CEB, a state-controlled electricity company. CEB has a 17.5% interest and we have the remaining 82.5%. The plant, with an installed capacity of 105 MW, is located on the Preto River, encompassing areas in the states of Minas Gerais and Goiás and in Brazil's Federal District. Construction on this project began on August 10, 2000. The power plant began its commercial generation on April 9, 2004 with the operation of its first unit. The commercial operation of the second and third units began on June 16, 2004 and July 8, 2004, respectively. As of December 31, 2004, we had invested R\$207.3 million in the project. The concession relating to this plant expires on December 18, 2032.

*Funil Hydroelectric Power Plant.* The Funil power plant, with an installed capacity of 180 MW, was built in the upper course of Grande River, in southern Minas Gerais. Construction began on September 1, 2000 and commercial generation of the first unit began in January 2003. Commercial generation of the second and third units began in June and July 2003 respectively. We have a 49% interest in this project and our partner, CVRD, has a 51% stake. As of December 31, 2004, we had invested R\$155.5 million in this project. The concession relating to this plant expires on December 20, 2035.

*Aimorés Hydroelectric Power Plant.* The Aimorés power plant, that is under construction on the Doce River, will have an installed capacity of 330 MW. We have a 49% interest in this enterprise and our partner, CVRD, has a 51% interest. Construction began in May 2001 and commercial generation is scheduled to begin in June 2005. As of December 31, 2004, we had invested R\$495.8 million in this project. The concession relating to this plant expires on December 20, 2035. We and CVRD are defending a lawsuit related to licensing for this plant. See *Item 8. Financial Information - Legal Proceedings - Legal Proceedings Related to Environmental Matters*.

*Irapé Hydroelectric Power Plant.* The Irapé power plant, which will have an installed capacity of 360 MW, is located on the Jequitinhonha River, in northern Minas Gerais. Construction began in April 2002 and commercial generation is expected to begin in August 2005. As of December 31, 2004, we had invested R\$802.0 million in this project, including R\$67.5 million debentures bought by the State of Minas Gerais, using the dividends that were due to the State Government pursuant to an agreement between us and the State Government. The concession relating to this plant expires on February 28, 2035.

*Pai Joaquim Small Hydroelectric Power Plant.* This project, with an installed capacity of 23 MW, consists of the construction of a new hydroelectric power plant and the reassembly of the existing Pai Joaquim powerhouse. It is located on the Araguari River in the western part of Minas Gerais. Construction started in April 2002 and the commercial generation began on March 31, 2004. As of December 31, 2004 we had invested R\$49.1 million in this project. The concession relating to this plant expires on April 4, 2032.

*Capim Branco Power Facility.* This project consists of the Capim Branco I and Capim Branco II hydroelectric power plants, with installed capacity of 240 MW and 210 MW, respectively. These power plants will be built on the Araguari River in the western part of Minas Gerais. Construction of Capim Branco I began in September 2003 and Capim Branco II in March 2004. Commercial generation at Capim Branco I is expected to begin in January 2006. Commercial generation at Capim Branco II is expected to begin in December 2006. As of

December 31, 2004 we had invested R\$24.2 million in this project. The concessions relating to these plants expire on August 29, 2036.

*Barreiro Thermoelectric Power Plant.* This project consists of the construction and operation of the 12.9 MW Barreiro thermoelectric power plant, which utilizes blast furnace gas and charcoal tar as fuel. The construction of the plant, located on Vallourec & Mannesmann's premises in the Barreiro section of the city of Belo Horizonte in Minas Gerais, began in April 2002. We were the manager of the engineering, procurement and construction contract for this project, and we are also responsible for the operation and maintenance of the plant. Vallourec & Mannesmann provides the facilities, supplies the fuel and signed a power purchase agreement to assure a guaranteed return on investment to us. Commercial generation began on February 21, 2004. As of December 31, 2004 we had invested R\$9.3 million in this project.

*Co-generation Joint Ventures with Customers*



We intend to enter into joint ventures with industrial customers to develop co-generation facilities. These facilities would be built on customers premises and would generate electricity using fuel supplied by the customers industrial processes. Each co-generation project would be funded in part through an agreement with the particular customer to purchase the electricity generated in that customer s facility. We would assume the responsibility for operating and maintaining the co-generation facility.

*Wind Farm*



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Morro do Camelinho, our wind farm, began operating in 1994. It is located in Gouveia, a municipality in northern Minas Gerais. This project is the first wind farm in Brazil to be connected to the national electricity transmission grid and it is connected to CEMIG's distribution system. It has a total generation capacity of 1 MW, powered by four turbines with a capacity of 250 kW each. Morro do Camelinho was built through a technical and scientific cooperation arrangement with the government of Germany. The cost of the project was US\$1.5 million, with 51% of the cost provided by us and the remaining 49% provided by the government of Germany.

### **Transmission**





*Overview*



Our transmission business consists of the bulk transfer of electricity from the power plants where it is generated to the distribution system, which carries the electricity to final customers. Our transmission system is comprised of transmission lines and step-down substations with voltages ranging from 230 kV to 500 kV.

In 1998, ANEEL created the ONS, a non-profit private entity comprised of Free Consumers and energy utilities engaged in the generation, transmission and distribution of electricity, in addition to other private participants such as importers and exporters. The ONS's primary role is to coordinate and control the generation and transmission operations in the interconnected power system, subject to ANEEL's regulation and supervision. Until the enactment of Law No. 10,848, the ONS was a self-regulated entity and its management was not subject to interference from the Federal Government. Law No. 10,848 granted the Brazilian government the power to nominate the main directors of the ONS. One of the main objectives of the ONS is to guarantee that all parties in the industry have access to the transmission network in a non-discriminatory manner. Under ANEEL regulations, owners of different parts of the basic transmission network, Brazil's nationwide electric power transmission network, must transfer operating control of their transmission facilities to the ONS. We complied with this requirement by entering into a transmission service agreement on December 10, 1999. Pursuant to this agreement, the ONS could represent us in contracts with generation companies, distribution companies and Free Consumers for use of the basic transmission network. Pursuant to the contracts between the ONS, acting on our behalf, and users of the basic transmission network, the users pay us a portion of the revenues we are permitted to receive (as determined by ANEEL) pursuant to our concession contract. During the year ended December 31, 2004, we recorded income totaling R\$245 million as a result of this arrangement. In turn, because we are also a distribution company and because we purchase electricity from Itaipu and others, our use of the basic transmission network requires us to pay scheduled rates to the ONS and owners of different parts of the basic transmission network. During the year ended

December 31, 2004, we recorded expenses totaling R\$586 million relating to payments made to the ONS and owners of different portions of the basic transmission network. See Item 5. Operating and Financial Review and Prospects and The Brazilian Power Industry in Annex A.

We transmit both the energy that we generate and the energy that we purchase from Itaipu, the interconnected power system and other sources. At December 31, 2004, we also had 9 industrial customers whom we supplied directly with high voltage (equal to or greater than 230 kV per industrial customer) energy through their connections to our transmission lines. These industrial customers accounted for approximately 11.5% of the total volume of electricity we sold in the year ended December 31, 2004. We also transmit energy to distribution systems through the South/Southeast division of the interconnected power system.

The following tables set forth certain operating information pertaining to our transmission capacity for the dates indicated:

	Circuit Length of Transmission Lines in Miles (from generation substations to distribution substations)			
	As of December 31,			
	2004		2003	2002
<b>Voltage of Transmission Lines</b>				
500 kV	1,344		1,344	1,351
345 kV	1,206		1,193	1,195
230 kV	467		463	466 (1)
Total	3,017		3,000	3,012

(1) We reduced the circuit length of our 230 kV transmission lines in 2002 because Escelsa Espírito Santo Centrais Elétricas S.A. connected its own 230 kV transmission line from its Mascarenhas Power Plant to our Valadares distribution substation.

	Step-Down Transformation Capacity(1) of Transmission Substations			
	As of December 31,			
	2004		2003	2002
Number of step-down substations	32		31	30
MVA	15,393		15,169 (2)	14,563

(1) Step-down transformation capacity refers to the ability of a transformer to receive energy at a certain voltage and release it at a reduced voltage for further distribution.

(2) Increment due to Itajubá 3 and Vespasiano 2.

#### *Expansion of Transmission Capacity*



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In accordance with the new regulatory framework in the Brazilian electricity sector, concessions for the expansion of the electricity transmission infrastructure in Brazil are awarded according to a public bidding system or are authorized by ANEEL.

*Bom Despacho 3.* ANEEL awarded us the concession to build and operate the Bom Despacho 3 Substation in February 2002. This substation, located in the town of Bom Despacho, 93.2 miles from Belo Horizonte, started its operation on May 3, 2004. The goal of this project is to increase the reliability of the basic transmission network in the Southeast Region of Brazil. This substation improves the operation of our system and supplies 100 MVA of reactive energy to the system, which improves the quality of the electricity in our system and in the basic transmission network. As of December 31, 2004, we had invested R\$83.4 million in this project.

*Montes Claros - Irapé.* In September 2003, a consortium formed by us, Companhia Técnica de Engenharia Elétrica ALUSA, or ALUSA, Furnas Centrais Elétricas S.A., or Furnas, and Orteng Equipamentos e Sistemas Ltda., or Orteng, won the concession auctioned by ANEEL to the Montes Claros Irapé transmission line. As required in the bidding process, the partners formed the Companhia Transleste de Transmissão, which will be responsible for building and operating the transmission line. This 345 kV transmission line will connect a substation

located in Montes Claros, a city in northern Minas Gerais, and the substation of the Irapé Hydroelectric Power Plant, with a length of approximately 93.2 miles. The project began in May 2004 and construction began in January 2005 and is expected to be completed in October 2005. The concession expires on February 18, 2034. As of December 31, 2004, we had invested R\$8.3 million in this project.

*Furnas - Pimenta.* In September 2004, a consortium formed by us and Furnas, with interests of 49%, and 51%, respectively, won the concession auctioned by ANEEL to the Furnas Pimenta transmission line. As required in the bidding process, the partners formed the Companhia de Transmissão Centroeste de Minas, which will be responsible for building and operating this transmission line. This 345 kV transmission line, with a length of approximately 46.6 miles, will connect the substation of the Furnas Hydroelectric Power Plant and a substation located in Pimenta, a city in the Center West Region of Minas Gerais. We began the project in March 2005 and expect it to be complete in approximately 18 months. As of December 31, 2004, we had invested R\$0.3 million in this project.

*Itutinga Juiz de Fora.* In September 2004, a consortium formed by us, Alusa, Furnas, and Orteng, with interests of 24%, 41%, 25% and 10%, respectively, won the concession auctioned by ANEEL to the Itutinga Juiz de Fora transmission line. As required in the bidding process, the partners formed the Companhia Transudeste de Transmissão, which will be responsible for building and operating this transmission line. This 345 kV transmission line, with a length of approximately 87.0 miles, will connect the substation of the Itutinga Hydroelectric Power Plant and a substation located in Juiz de Fora, a city in the southeastern Minas Gerais. We began the project in March 2005 and expect it to be complete in approximately 20 months. As of December 31, 2004, we had invested R\$0.7 million in this project.

*Irapé - Araçuaí.* In November 2004, a consortium formed by us, Alusa, Furnas, and Orteng, with interests of 24.5%, 41%, 24.5% and 10%, respectively, won the concession auctioned by ANEEL to the Irapé - Araçuaí transmission line. As required in the bidding process, the partners formed the Companhia Transirapé de Transmissão, which will be responsible for building and operating this transmission line. This 230 kV transmission line, with a length of approximately 40.4 miles, will connect the substation of the Irapé Hydroelectric Power Plant and a substation to be built in Araçuaí, a city located in the northeastern Minas Gerais. We began the project in March 2005 and expect it to be complete in approximately 18 months. As of December 31, 2004, we had not started to invest in this project.

We believe that our transmission system will need to be reinforced and expanded through the construction of new substations and transmission lines within the next five years. See Item 5. Operating and Financial Review and Prospects Liquidity and Capital Resources.

#### **Distribution and Purchase of Electric Power**





*Overview*



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Our distribution operations consist of the transfer of electricity from distribution substations to final customers. Our distribution network is comprised of a widespread network of overhead and underground lines and substations with voltages of less than 230 kV. We supply electricity to smaller industrial customers at the higher end of the voltage range and residential and commercial customers at the lower end of the range.

From January 1, 2000 through December 31, 2004, we invested approximately R\$1,755 million in the construction and acquisition of property, plant and equipment used to expand our distribution system.

The following tables provide certain operating information pertaining to our distribution system, as of the dates presented:

	Circuit Length of Distribution Lines in Miles (from distribution substations to final customers)			
	As of December 31,			
	2004		2003	2002
<b>Voltage of Distribution Lines</b>				
161 kV	34.2		34.2	34.2
138 kV	6,526.9		6,524.4	6,521.3
69 kV	2,823.5 (1)		2,887.5	2,886.3
34.5 kV + Others	610.8		610.8	594.7 (2)
<b>Total</b>	<b>9,995.4 (1)</b>		<b>10,056.9</b>	<b>10,036.5</b>

	Circuit Length of Distribution Lines in Miles (from distribution substations to final customers)			
	As of December 31,			
	2004		2003	2002
<b>Type of Distribution Lines</b>				
Overhead urban distribution lines	51,461.2		51,051.7	34,426.3
Underground urban distribution lines	439.9		439.3	195.1
Overhead rural distribution lines	176,412.8		171,769.3	170,777.6
<b>Total</b>	<b>228,313.9</b>		<b>223,260.3 (3)</b>	<b>205,399.0</b>

	Step-Down Transformation Capacity(4) of Distribution Substations			
	As of December 31,			
	2004		2003	2002
Number of substations	350		348	346
MVA	8,050		7,987	7,953

- (1) The decrease in the circuit length of these lines from 2003 was due to the decommissioning of certain lines.
- (2) The decrease in the circuit length of these lines from 2001 was due to the decommissioning of certain lines in eastern Minas Gerais as a result of the conversion of 34.5 kV lines to 69 kV lines.
- (3) In April 2003 PROOBRA was replaced by SIGEM in the management of the distribution company's logistics management program.
- (4) Step-down transformation capacity refers to the ability of a transformer to receive energy at a certain voltage and release it at a reduced voltage for further distribution.

Physical data for the Control and Management Investment Program, or PROOBRA, were calculated by projection from the existing network. In 2003, we began to calculate this as the sum of the linear extension of the medium-voltage network and the low-voltage network available in the GEMINI system, double counting (in relation to the previous criterion) where joint medium and low voltage networks are in existence.

The GEMINI system is the manager of CEMIG's distribution network. With the inclusion and startup of the Operation, Projects, Client Registry and Planning modules, all the distributor's assets are now being managed by the GEMINI system and are now the source of information for ANEEL in assembling the data on assets for the rate reviews.

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As a result, the statistics on extent of networks, number of transformers, public illumination and quantity of transmission posts are now supplied by the GEMINI system on a geo-referenced basis. We believe this has resulted in more precise data, reduction of errors in valuing fixed assets, and increased reliability.

### *Expansion of Distribution Capacity*



Our distribution expansion plan for the next five years is based on projections of market growth. We anticipate that this growth will be fueled by new customer connections, increased electricity usage among our



existing customers and additional electricity distribution needs from new IPP projects. According to applicable law, IPPs have the right to use our distribution network upon payment of certain fees. During the next five years, we anticipate connecting approximately 882,000 new urban customers and 182,000 rural customers. In order to accommodate this growth, we expect that we will need to add 885,000 medium-voltage poles, 202.6 miles of transmission lines and 12 step-down substations to our distribution network, increasing the network's installed capacity to 510 MVA. Over the next five years, we expect to invest approximately R\$3.45 billion to expand our distribution system. See Item 5. Operating and Financial Review and Prospects Liquidity and Capital Resources.

We have adopted a rural electricity development program, with the participation of the Federal Government and the State Government, called *Luz Para Todos*. Our plan is to use the *Luz Para Todos* program to meet our target for supply of electricity to 100% of rural consumers in Minas Gerais by 2006 - this is a total of approximately 176,000 clients. To meet this objective, we will need funding in the amount of approximately R\$1,641 million. The *Luz Para Todos* program includes the *Luz Solar* sub-program, which uses solar energy to light schools, community centers and rural homes in remote locations not yet reached by the distribution network. We expect that this sub-program will connect 7,000 new consumers by 2006. Additionally, the *Luz no Saber* sub-program connected 479 state and municipal schools in 2004, and aims to connect 646 state and municipal schools in 2005, thereby completing the connection of electricity services to all the schools in the State of Minas Gerais.

***Purchase of Electric Power***



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During the year ended December 31, 2004, we purchased 11,936 GWh of electricity from Itaipu, which represented approximately 32.6% of the electricity we sold to end users. In addition, during the same period, we purchased 3,796 GWh of electricity from the interconnected power system and other concessionaires, which represented approximately 10.4% of the electricity we sold to end users.

*Itaipu.* Itaipu is one of the largest operating hydroelectric plants in the world, with an installed capacity of 12,600 MW. *Centrais Elétricas Brasileiras S.A.*, or Eletrobrás, a holding company controlled by the Federal Government, owns a 50% interest in Itaipu, while the remaining 50% is owned by the government of Paraguay. Brazil, pursuant to its 1973 treaty with Paraguay, has the option to purchase all of the electricity generated by Itaipu that is not consumed by Paraguay. In practice, Brazil generally purchases more than 95% of the electricity generated by Itaipu.

We are one of the 19 electric power distribution companies operating in the South, Southeast and Center West Regions of Brazil that are jointly required to purchase all of Brazil's portion of the electricity generated by Itaipu. The Federal Government allocates Brazil's portion of Itaipu's power among these electric companies in amounts proportionate to their respective historical market share of total electricity sales. We are currently required to purchase approximately 17% of the total amount of electricity purchased by Brazil from Itaipu at rates fixed to defray Itaipu's operating expenses and payments of principal and interest on Itaipu's dollar-denominated borrowings and the cost in *reais* of transmitting such power to the interconnected power system. These rates have been above the national average for bulk supply of power and are calculated in U.S. dollars. Therefore, fluctuations in the U.S. dollar/*real* exchange rate affect the cost, in real terms, of electricity we are required to purchase from Itaipu. Historically, we have been able to recover the cost of such electricity by charging supply rates to consumers. According to our concession agreement, increases in the supply rate may be transferred to the final customer upon approval by ANEEL.

*Interconnected Power System.* We also purchase electricity from the interconnected power system, a national interconnected power grid designed to optimize electricity generation in Brazil. Electric power generation companies in Brazil, including us, are required to transfer excess energy into the interconnected power system, where it then becomes available for purchase by other power companies.

## Energy Losses

The rules under the New Industry Model for the electricity sector have led to a change in our method of calculating losses resulting from the energy that passes through our system. Under the New Industry Model for the electricity sector, as an incentive for competition, there is now free access to the transmission and distribution networks, enabling certain customers to buy their electricity freely from other suppliers. Customers who opt for this free-negotiation mode of supply now have two contracts: one with the owner of the distribution or transmission network for the use of the networks, and the other with the selling agent or generator for the electricity. Also, under the new regulations, (i) our transmission assets with voltage of greater than or equal to 230 kV became part of the national basic grid which is operated by the ONS, referred to as the Basic Grid; and (ii) energy losses occurring in this Basic Grid are divided equally so that 50% is allocated among generation agents in proportion to each of their levels of energy generation and the other 50% is allocated among consumption agents (distributors and Free Consumers) in proportion to each of their energy loads. As a result, the losses in the Basic Grid attributed to a given agent now have no direct relationship with its Basic Grid assets, nor can the agents have control over them. Therefore, these losses take on the status of an electricity transmission service charge for the agents of the sector, and become part of the cost structure covered by the distributors' retail rate, substantially reducing the risk of financial losses.

In 2004, our level of total energy losses was 4,315 GWh. Part of this loss (915 GWh) is related to operations in the Basic Grid, and the remainder (3,400 GWh) reflects losses in our distribution systems and represents 8.6% of the total energy that passed through our distribution systems (39,375 GWh).

We divide our energy losses into two basic categories: technical losses and non-technical losses. Technical losses account for approximately 92% of our energy losses. These losses are the inevitable result of the step-down transformation process and the transportation of electric energy through the 3,017 miles of transmission lines and 238,309 miles of distribution lines that we operate.

We attempt to minimize technical losses by performing rigorous and regular evaluations of the quality of our electricity supply. We routinely upgrade and expand our transmission and distribution systems in order to maintain quality and reliability standards, and consequently, reduce technical losses. In addition, we operate our transmission and distribution systems at certain specified voltage levels in order to minimize losses.

Non-technical losses account for the remaining 8% of our energy losses and result from fraud, illegal connections (which increased during the Electricity Rationing Plan), metering errors and meter defects. These losses accounted for 0.8% of the electricity that we sold during 2004. In order to minimize non-technical losses, we regularly take preventative actions, including:

inspection of customers' meters and connections;

modernization of metering systems;

training of meter-reading personnel;

standardization of meter installation procedures;

installation of meters with quality control warranties;

customer database updating; and

development of a theft-protected distribution network.

Additionally, we have developed an integrated system designed to help detect and measure controllable losses in all parts of our distribution system.

**Customers and Billing**



*Customer Base*





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Our distribution business customers, all of whom are located within our concession area in Minas Gerais, are divided into five principal categories: industrial (including mining, manufacturing and processing activities); residential; commercial (including service-oriented businesses, universities and hospitals); rural; and other (including governmental and public entities). During the year ended December 31, 2004, we sold 37,533 GWh of energy. This does not include sales to the interconnected power system and other concessionaires, but does include energy sold by Barreiro and Pai Joaquim of 73 GWh and 29 GWh, respectively, which were not consolidated in our financial statements.

For 2004, as compared to 2003, the volume of electric power sold by us to industrial, commercial and rural customers increased by 6.2%, 4.0%, 3.5%, respectively. The other consumer category grew 0.8% (this excludes wholesale supply). The residential consumption remained roughly unchanged from 2003 to 2004. In 2004, Sá Carvalho, Ipatinga, Barreiro, Pai Joaquim and Horizontes Energia S.A. were included considered in the industrial category. The following table provides information regarding the number of our customers as of December 31, 2004 and consumption by customer category for the years ended December 31, 2004, 2003 and 2002:

Customer Category	Number of customers at December 31,	Consumption (GWh)			
		Years ended December 31,			
		2004	2003	2002	
Industrial	68,265	23,071 <sup>(3)</sup>	21,715 <sup>(2)</sup>	21,906 <sup>(1)</sup>	
Residential	4,830,935	6,526	6,529	6,360	
Commercial	530,158	3,537	3,402	3,283	
Rural	388,445	1,846	1,783	1,705	
Own consumption	1,324 <sup>(5)</sup>	55	55	50	
Other (4)	55,780	2,498	2,478	2,330	
<b>Total</b>	<b>5,874,907</b>	<b>37,533</b>	<b>35,962</b>	<b>35,634</b>	

(1) Includes consumption by *Sá Carvalho S.A.* and *Usina Térmica Ipatinga S.A.*, which consume all of the energy that they produce.

(2) ANEEL includes consumption by *Sá Carvalho S.A.*, *Usina Térmica Ipatinga S.A.* and *Horizontes Energia S.A.*

(3) In 2004, in addition to the projects noted in footnote 2, the consumption by *Central Hidrelétrica Pai Joaquim* and *Usina Termelétrica Barreiro S.A.* were also included.

(4) Does not include consumption through supply to other concessionaires.

(5) Refers to the number of our plants, facilities and offices that use our energy, each of which is considered a customer pursuant to ANEEL regulations.

In 2004, we added and billed 130,708 new final customers, representing growth of 2.3% compared to 2003, through the expansion of our transmission and distribution systems.

The largest portion of the energy we sell is purchased by large industrial customers. At December 31, 2004, nine of our industrial customers had high voltage electrical energy supplied through direct connections to our transmission lines. These customers constituted 11.5% of our total volume of electrical power sales during 2004, and approximately 6.6% of our revenues. In the same period, our ten largest industrial customers accounted for nearly 17.9% of energy consumed. None of our ten largest customers is owned by the State Government or by the Federal

Government.

As of December 31, 2004, we had entered into standard power purchase agreements with 3,840 of our industrial customers, of which 580 customers had demand above 500 kW. Our standard power purchase agreement with industrial customers has a duration of three, five or ten years and contains a minimum demand clause that requires the customer to pay for the contracted demand, which represents the system capacity reserved for that

customer, as well as the customer's actual consumption. We believe that this billing method provides us with a relatively stable source of revenue.

The following table shows our industrial energy sales volumes by type of industrial customer as of December 31, 2004 :

Industrial Customers	Energy Sales Volume in GWh	Consumption as a Percentage of Total Industrial Energy Sales Volume
Steel industry	5,238 (1)	22.70
Ferroalloy industry	4,575	19.83
Non-ferrous metal industry	1,749	7.58
Mining industry	2,355	10.21
Cement industry	780	3.38
Automotive industry	618	2.68
Others	7,756 (2)	33.62
Total	23,071	100.00

(1) Includes consumption by Sá Carvalho, Barreiro and Ipatinga.

(2) Includes Pai Joaquim and Horizontes Energia S.A.

The following table sets forth the names and related industries of our ten largest customers in 2004:

**Ten Largest Customers**

(listed in order of total GWh of electricity purchased from us in 2004)

	Industry
Usinas Siderúrgicas de Minas Gerais S.A. USIMINAS	Steel
White Martins Gases Industriais S.A.	Chemical
Rima Eletrometalurgia S.A	Ferroalloys
Companhia Siderúrgica Belgo Mineira	Steel
Companhia Mineira de Metais.	Non-ferrous
Ligas de Alumínio S.A.	Ferroalloys
Companhia Brasileira de Carbureto de Cálcio - CBCC.	Ferroalloys
Companhia Ferro Ligas Minas Gerais	Ferroalloys
Ligas de Alumínio S.A. Italmagnésio Nordeste S.A.	Ferroalloys
Saint Gobain Materiais Cerâmicos Ltda.	Chemical

We have entered into contracts with other large Free Consumers both within and outside of Minas Gerais involving electricity volume of 8,760 GWh as a result of a strategy to capture a larger market share. As a result of the unbundling, these contracts were assigned to Cemig Generation and Transmission in 2005.

Some of our customers may elect to become Free Consumers and purchase electricity directly from other generators or traders of electricity instead of purchasing from us. Most of our large clients have already bought electricity from Cemig Generation and Transmission for the next

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several years, representing almost 47.3% of our annual sales revenue. Consumers that opt to become Free Consumers are primarily industrial customers whose demand generally exceeds 3 MW. Consumers that consume between 500 kW and 3 MW may opt to purchase energy from other sources, if such source is a renewable energy source, such as small hydroelectric facilities or biomass. A total of 762 of our clients which currently purchase electricity at regulated rates ( captive consumers ) representing annual sales revenue of R\$683 million (or 7.2% of our annual sales revenue), may elect to become Free Consumers or opt to purchase energy from alternative sources.

### ***Billing***



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Our monthly billing and payment procedures for electricity supply vary by customer category. Our large customers with direct connections to our transmission network are billed on the same day their meters are read.

Payment is required within five days after delivery of the bill. Other customers receiving high and medium voltage electricity (approximately 8,000 consumers supplied at a voltage level equal to or greater than 2.3 kV or connected by underground distribution lines, with the exception of public sector entities) are billed within one (70%) or two (30%) days of their meter reading and payment is required within five days after delivery of the bill. Our remaining customers are billed within seven days of their meter reading and payment is required within 10 days after delivery of the bill or 15 days after delivery of the bill in the case of public sector entities. Bills are prepared from meter readings or on the basis of estimated consumption.

*Seasonality*





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Our sales are affected by market seasonality. Usually, an increase in consumption by industrial and commercial customers occurs in the third quarter due to increases in industrial and commercial activity. In addition, there is generally an increase in usage across all customer categories during the summer due to the increase in temperatures. Certain figures representing quarterly consumption by final customers from 2002 through 2004, in GWh, are set forth below:

Year	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
2002(1) (4)	8,306	9,087	9,127	9,114
2003(2) (4)	8,831	8,932	8,964	9,235
2004(3) (4)	9,067	9,353	9,496	9,617

- 
- (1) Includes consumption by *Sá Carvalho S.A* and *Usina Térmica Ipatinga S.A.*
  - (2) Includes consumption by *Sá Carvalho S.A.*, *Usina Térmica Ipatinga S.A.* and *Horizontes Energia S.A.*
  - (3) Includes consumption by *Sá Carvalho S.A.*, *Usina Térmica Ipatinga S.A.*, *Usina Térmica Barreiro S.A.*, *Usina Hidrelétrica Pai Joaquim S.A.* and *Horizontes Energia S.A.*
  - (4) Does not include supply to other concessionaires.

Consumption by residential customers remains sluggish and has not returned to pre-rationing levels. However, the total sales in the fourth quarter of 2003 returned to levels similar to those prerationing. In 2004, consumption by residential customers remained at almost the same level as 2003.

### Competition



*Impacts of the New Model for the Electricity Sector*

The implementation of the new model for the electricity sector has allowed consumers with a demand of three MW or more to become Free Consumers. This might adversely affect the results of operations of our distribution company, considering that 48.9% of the volume of its annual sales was to potentially Free Consumers, which were the target of our competitors. Considering the current situation of excess capacity in Brazil and the obligation of distributors to buy through regulated auctions, our generation and transmission subsidiary undertook a strategy of maintaining and even seeking to enlarge its market share, and also of minimizing its need for sales in the regulated auctions for existing capacity.

The management of our portfolio through a major commercial effort in relation to our client base, resulted in our successfully obtaining signatures to 129 contracts with Free Consumers by December 31, 2004. Eleven of these contracts are with companies located outside of our distribution company's concession area. These contracts have an average duration of three to ten years, and represent a volume of 18,000 GWh/year.

Of the previous base of our captive consumers, only four did not sign contracts with us and instead opted to become Free Consumers. These four formerly captive consumers represented an annual volume of 367 GWh. Another seven consumers, representing approximately 963 GWh, elected to opt out of the Regulated Contracting

Environment (ACR) and choose their own generation subsidiary as a supplier.

In addition to our sales effort in the Free Contracting Environment (ACL), we were successful in obtaining contracts in the Regulated Contracting Environment (ACR) that represent a volume of 8,120 GWh/year. The term of these contracts begins in 2006 and they have a duration of eight years. In addition, in April 2005 we obtained new contracts in the ACR that represented a volume of 920 GWh/year with terms beginning on January 1, 2008 and which have a duration of eight years. We still have an opportunity to obtain contracts on the remaining 25% of the Initial Contracts, in the approximate amount of 7,600 GWh, which we expect will terminate in 2005.

Through implementation of this strategy, we were successful in selling most of the existing generation capacity, largely through contracts for which renewals will begin only after five years. By that point, a balance is expected between the supply and demand of electricity in Brazil, which should result in better price conditions.

*Concessions*



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Each concession that we currently hold is subject to a competitive bidding process upon its expiration. However, in accordance with the Concessions Law, existing concessions may be renewed without a bidding process by the Federal Government for additional periods of up to 20 years upon application by the concessionaire, provided the concessionaire has met minimum performance standards and the proposal is otherwise acceptable to the Federal Government. On September 22, 2004, we applied to ANEEL for a 20-year renewal of the concessions of the Emborcação and Nova Ponte Hydroelectric Plants.

In addition, it is possible that a number of our large industrial clients may become SPPs pursuant to the Concessions Law in order to obtain the right to generate electricity for their own use. The granting of certain concessions to our large industrial clients could adversely affect our results of operations.

### **Raw Materials**

Our principal raw materials expense is the purchase of fuel oil, which is consumed by our three thermoelectric plants in the electricity generation process. Fuel oil consumption for the year ended December 31, 2004 represented an expense of R\$19.1 million of which R\$18.3 million was reimbursed to us by the Conta de Consumo de Combustível (Fuel Usage Quota Account), or CCC Account. The CCC Account was created by the Federal Government to offset the higher marginal operating costs of thermoelectric plants, and we and other electricity concessionaires must make contributions to this account. See Item 5. Operating and Financial Review and Prospects and The Brazilian Power Industry Regulatory Charges in Annex A. We believe that supplies of fuel oil are readily available. Although the price of fuel oil may fluctuate, we have generally been able to offset all or a portion of our increased fuel oil costs through adjustments to our rates.

**Other Businesses**





*Natural Gas Distribution*



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Our subsidiary Gasmig was established in Minas Gerais, Brazil in 1986 for the purpose of developing and implementing the distribution of natural gas in Minas Gerais. We own approximately 55% of Gasmig. The remaining shares are owned by TSS Participações S.A., Gaspetro Petrobras Gas S.A., Minas Gerais Participações Ltda., or MGI, the investing body of the State Government, and by the city of Belo Horizonte.

In January 1993, the State Government granted to Gasmig an exclusive 30-year distribution concession covering all of Minas Gerais and all types of consumers. Gasmig's marketing efforts focus on its ability to provide a more economically efficient and environmentally friendly alternative to oil, liquefied petroleum gas (LPG) and wood. In 2004, Gasmig supplied approximately 1.1 million cubic meters of gas per day to 140 customers. At December 31, 2004, Gasmig also supplied natural gas to 63 automotive natural gas stations and to two power plants. During 2004, Gasmig distributed approximately 5% of all natural gas distributed in Brazil.

Minas Gerais accounts for approximately 17% of the total energy consumption in Brazil. Many energy-intensive industries such as the cement, steel, ferroalloys and metallurgy industries have significant operations in the state. We estimate that total demand for natural gas in Minas Gerais will amount to nearly 13 million cubic meters of gas per day by 2009, which exceeds the projected available supply. In addition, the recent completion of a natural gas pipeline between Brazil and Bolivia provides a significant source of natural gas, enabling Gasmig to better meet demand. Gasmig's key strategy is to expand its distribution network in order to serve the unsatisfied portion of the demand. Gasmig is engaged in the development of new projects to extend its distribution systems to reach customers in other areas of Minas Gerais, principally in heavily industrialized areas.

For 2004, Gasmig had gross revenues of R\$435 million and net income after taxes of R\$39 million.

In 2004, Gasmig invested approximately R\$30 million in the expansion of its gas pipeline network to serve more clients in the State of Minas Gerais. The funds to finance the expansion came primarily from its own cash flow and dividend reinvestment. Currently, the natural gas pipeline which brings natural gas from the Campos oil basin (State of Rio de Janeiro, Brazil) operates at full capacity and further investment by the Federal Government will be necessary to expand the capacity or in the construction of a new pipeline to supply the growing natural gas demand in the State of Minas Gerais.

On August 25, 2004, CEMIG, Gasmig, Gaspetro and Petrobras entered into an Association Agreement, pursuant to which CEMIG agreed to sell a 40% equity interest in Gasmig to Gaspetro, a subsidiary of Petrobras. Under the terms of the Association Agreement, Petrobras agreed to make investments to expand the capacity of the current pipelines connected to the Gasmig distribution network as well in the construction of new pipelines, and CEMIG and Gaspetro agreed to fund Gasmig's capital expenditure plan to expand its distribution network.

The transaction was implemented on December 15, 2004 when Petrobras, through its subsidiaries Gaspetro and TSS, concluded the acquisition of a 40% equity interest in Gasmig. As a condition to such investment, Petrobras and CEMIG entered into a Shareholders Agreement in which CEMIG agreed to with Petrobras and its subsidiaries to share in the management of Gasmig. See Item 10- Additional Information - Material Contracts - Gasmig Shareholders Agreement and Association Agreement .

We expect that the association with Petrobras will expand Gasmig's distribution capacity, as our ability to offer natural gas to our customers will increase significantly with the implementation of Petrobras's investments in pipelines. We expect that Gasmig's capital expenditure for 2005 will be mostly used for the expansion of our distribution network in highly industrialized areas of Minas Gerais.

Gasmig is not a consolidated subsidiary in our financial statements as of December 31, 2004, in accordance with Emerging Issues Task Force ( EITF ) Issue No. 96-16, Investor's Accounting for an Investee When the Investor Has a Majority of the Voting Interest but the Minority Shareholder or Shareholders Have Certain Approval or Veto Rights. We consolidated Gasmig's revenues and expenses for the period from January 1, 2004 to December 15, 2004, the date of our sale of a 40.00% equity interest in Gasmig to Petrobras.

#### ***Telecommunications, Internet and Cable Television***



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On January 13, 1999, we incorporated Empresa de Infovias S.A. in Minas Gerais, Brazil, as a joint venture with AES Força Empreendimentos Ltda., an affiliate of AES Corporation Group. Currently, we own 99.94% of the common shares of Empresa de Infovias S.A. Empresa de Infovias S.A. has an optical fiber-based long-distance communications backbone installed along our power grid using optical ground wire cables. This communications backbone is connected to an access network that is based on hybrid fiber-coaxial cable technology and is deployed along our power grid. We lease our network infrastructure to Empresa de Infovias S.A. pursuant to a 15-year operating lease agreement entered into on March 31, 2000. Pursuant to Brazilian telecommunications law, we also make our network infrastructure available to other telecommunications providers interested in leasing it.

Empresa de Infovias S.A. started its business operations in January 2001. The main telecommunication services provided by Empresa de Infovias S.A. through its network are signal transportation and access, both for point-to-point and point-to-multipoint applications, delivered mainly to telecommunications operators and Internet

service providers on a clear channel basis. Empresa de Infovias S.A. is also extending its broadband Internet services, currently available in the cities of Belo Horizonte, Poços de Caldas and Barbacena, to other cities in Minas Gerais.

Empresa de Infovias S.A. provides the network for cable television service in 12 cities in Minas Gerais pursuant to a 15-year service agreement with WAY TV Belo Horizonte S.A., or WAY TV, and Brasil Telecomunicações S.A., each a holder of concessions to provide cable television and Internet service in certain cities in Minas Gerais, under which Empresa de Infovias S.A. allows these companies to use its network infrastructure. In return, WAY TV and Brasil Telecomunicações are obligated to deliver to Empresa de Infovias S.A. a percentage of the revenues derived from their cable television and Internet subscribers. At December 31, 2004, these two companies had approximately 43,990 cable television subscribers and 20,333 Internet service subscribers.

Empresa de Infovias S.A. holds a 69.25% equity interest in WAY TV, including 49.9% of its common shares. The control of WAY TV is exercised by Empresa de Infovias S.A. and CLIC Clube de Investimentos dos Empregados da Cemig, or CLIC, which owns 1.1% of WAY TV's common shares, through a shareholders' agreement. Under this agreement, CLIC has agreed to vote in accordance with Empresa de Infovias S.A.'s interests at the WAY TV shareholders' meetings and board of directors. To date, Empresa de Infovias S.A. has invested approximately R\$62.6 million in WAY TV.

Empresa de Infovias S.A. also provides intracompany data transmission services to us pursuant to a five-year agreement signed in 2001. We use this service for internal communications as well as for certain communications with our customers.

In September 2002, Empresa de Infovias S.A. signed an agreement with us pursuant to which we are to provide geo-referenced information and related services to Empresa de Infovias S.A.

During 2004, Empresa de Infovias S.A. had operating revenues of R\$71.0 million, of which R\$30.9 million related to the provision of telecommunication services and R\$40.1 million related to the provision of cable television and Internet services.

Empresa de Infovias S.A.'s capital expenditures for the past four years were R\$196.3 million. Empresa de Infovias S.A.'s capital expenditures for 2005 will be mostly used for expansion of its telecommunications network.

### *Consulting and Other Services*





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We provide consulting services to governments and public utility companies in the electricity industry in order to derive additional revenues from the technology and expertise we have developed through our operations. During the past eight years, we have provided such services to government agencies and utilities in ten countries, including Canada, Paraguay, Honduras and El Salvador and to the government of Panama.

On January 9, 2002 we created Efficientia S.A., referred to as Efficientia, in Minas Gerais, to provide project efficiency optimization solutions and operation and management services to energy supply facilities. We have a 100% interest in Efficientia, which began operating in 2003. In 2004, although the Brazilian economic context was favorable to productive activities in general, Efficientia posted a loss of R\$1.4 million, largely caused by factors other than its business management, as described below.

In its second year of operations, Efficientia still depended, for a large part of its sales revenue, on CEMIG's Energy Efficiency Program. This program is subject to numerous requirements by ANEEL, including a timetable for approval of the projects presented, with a view to their being executed in the immediately subsequent year. The portfolio of projects presented for approval in November 2003, with a view to implementation and invoicing for sales revenue in 2004, was not converted into revenues in 2004. This was due to the significant delay in the analysis and approval by ANEEL which, instead of complying with its requirement to approve the project within a maximum period of two months, did not approve the program until October 2004.

**Environmental Matters**



*Overview*



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Our generation, transmission and distribution activities are subject to comprehensive federal and state legislation relating to the preservation of the environment. See The Brazilian Power Industry Environmental Regulations in Annex A. The primary environmental authorities in the State of Minas Gerais are *Fundação Estadual do Meio Ambiente* (State of Minas Gerais Environmental Foundation), or FEAM, Instituto Mineiro de Gestão das Águas (State of Minas Gerais Water Management Institute), or IGAM, *Secretaria de Meio Ambiente e Desenvolvimento Sustentável* (State Secretariat for the Environmental and Sustainable Development), or SEMAD, and *Conselho Estadual de Política Ambiental* (State of Minas Gerais Environmental Policy Council), or COPAM. At the Federal level, the main authorities are *Conselho Nacional de Meio Ambiente* (National Environment Council), or CONAMA, *Instituto Brasileiro do Meio Ambiente e dos Recursos Naturais Renováveis* (the Brazilian Institute of the Environment and Natural Renewable Resources), or IBAMA, and *Agência Nacional de Águas* (National Water Agency), or ANA.

We believe that we are in compliance in all material respects with the relevant laws and regulations.

In 2003, we received the ISO 14001:1996 Certification from Det Norske Veritas, or DNV, related to the Environmental Management System of Hydroelectric Facility of Nova Ponte, concerning all activities related to Hydroelectric Energy Generation, Reservoir Operation and Management of a Natural Private Reserve. In addition, DNV also issued certifications for some of our distribution systems, including their respective administrative offices, covering the municipalities of Alfenas, Divinópolis, Varginha, Montes Claros and Pouso Alegre, among others. Such certifications attest to the compliance of such facilities with the Environmental Management System - Level 1, which is CEMIG's internal environmental regulation. In 2004, for the fifth consecutive year CEMIG was selected to be a component of Dow Jones Sustainability Index (DJSI World Index).

In accordance with our environmental policy, we have established various programs for prevention and control of damage aiming at limiting our risks related to environmental issues.

In 2004 we invested approximately R\$123 million in environmental compliance projects for plant and equipment and the vehicle fleet, and in the implementation of new projects, and also spent R\$19 million on operational and maintenance expenses for our current activities, such as final disposal of waste, putting environmental management systems in place, audits, planting of riverside forests, fish cultivation, putting in place tree pruning and oil policies, environmental education programs, maintenance of conservation units, training and other activities. These amounts also include R\$3 million corresponding to environmental research and development projects developed with universities and research institutes.

### ***Licensing***





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Applicable law in Brazil requires that licenses be obtained in connection with the construction, installation, expansion and operation of any facility that utilizes environmental resources, causes environmental degradation, pollutes or has the potential to cause environmental degradation or pollution or harm archaeological wealth. Generally, state governments manage the environmental licensing process for facilities that are to be built within their territories. However, the Federal Government manages the environmental licensing process for facilities that are expected to have an environmental impact on more than one state and/or are located between two or more states.

COPAM Regulatory Ordinances No. 17, dated December 17, 1996, and No. 23, dated October 21, 1997, provide that operational licenses shall be renewed from time to time for periods of four to eight years depending on the size and pollution potential of the facility. Aimed at surveying and rescuing archaeological wealth that has not been previously considered, the provisions of Ordinance No. 28, dated January 31, 2003, of *Instituto do Patrimônio Histórico e Artístico Nacional* (National Historical and Artistic Heritage Institute), or IPHAN, set forth that the renewal of operational licenses for hydroelectric power plants shall be conditioned on a favorable opinion of IPHAN concerning archaeological studies on the depletion area of the reservoir. These studies are to be sponsored by the plant operator.

Gasmig's distribution of natural gas through pipelines in Minas Gerais is also subject to environmental control. We believe that all licenses for the regular operation of Gasmig's activities have been obtained.

*Corrective Environmental Operation Licensing*

Pursuant to Resolution No. 6, dated September 16, 1987, of the *Conselho Nacional de Meio Ambiente* (the Brazilian Environmental Council), or CONAMA, environmental impact assessment studies must be undertaken, and a corresponding environmental impact assessment report must be prepared, for all major electric generation facilities built in Brazil after February 1, 1986. While studies are not required for facilities built prior to February 1, 1986, such facilities must obtain corrective environmental operation licenses, which may be acquired by filing a form containing certain information regarding the facility in question.

Federal Law No. 9,605, dated February 12, 1998, sets forth penalties for facilities that operate without environmental licenses. In 1998, the Federal Government issued Provisional Measure No. 1,710 (currently Provisional Measure No. 2,163/41), which establishes the potential for project operators to enter into agreements with relevant environmental regulators for the purpose of coming into compliance with Federal Law No. 9,605/98. Accordingly, we have been negotiating with the *Instituto Brasileiro do Meio Ambiente e dos Recursos Naturais Renováveis* (the Brazilian Institute of the Environment and Natural Renewable Resources), or IBAMA, and FEAM to obtain the corrective environmental operation licensing for all our plants that began operating prior to February 1986. Generation facilities located within the State of Minas Gerais fall within the jurisdiction of FEAM for purposes of corrective licensing. We have agreed with FEAM to bring our facilities located in Minas Gerais into compliance on a gradual basis. We do not currently anticipate any costs and commitments in connection with any recommendations that may be made by IBAMA and FEAM. We currently have operating licenses for the following facilities: (i) hydroelectric plants: Miranda, Nova Ponte, Igarapava, Porto Estrela, Sá Carvalho, Funil and Queimado, (ii) small hydroelectric plants: Pai Joaquim, Rio de Pedras, Santa Luzia, Salto dos Moraes, Poquim and Piçarrão, (iii) thermoelectric plants: Barreiro and Formoso, and (iv) the wind farm: Morro do Camelinho.

Our Emborcação, São Simão, Jaguara and Volta Grande hydroelectric power plants need to obtain corrective environmental operation licenses, since they all began operating prior to February 1986. In 2004, after a technical inspection by IBAMA of the facilities and areas of influence of the Jaguara and Volta Grande hydroelectric power plants, a reference report was issued for the preparation of environmental impact studies for the obtaining of corrective environmental licensing for the Emborcação, Jaguara, São Simão and Volta Grande plants and the transmission systems associated with them. At present we are preparing these studies for submission to IBAMA.

The environmental licenses, either issued by state or federal bodies, are subject to several conditions imposed in light of the foreseen environmental impacts. In extreme circumstances, the failure to comply with such conditions may result in the revocation of the license. We believe we are in compliance with the requirements mentioned in our licenses.

*Compensation measures*



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According to Federal Law No. 9,985, dated July 18, 2000, and corresponding Decree No. 4,340, dated August 22, 2002, the companies whose activities are deemed to cause high environmental impacts are required to invest in protected areas in order to offset those impacts. These companies are required to invest at least 0.5% of total amounts invested in implementation of its corresponding project in activities and areas defined by environmental agents.

During the licensing procedure, in light of the environmental impacts identified by the environmental assessment studies presented by the operator, environmental bodies may determine the amount to be invested and which protected areas shall be benefited.

The criteria for environmental and social compensation have not been defined, and there is a possibility that requests from environmental agencies, the Public Attorneys Office, NGOs or affected populations may be added to those traditionally proposed. Due to these uncertainties, licensing (including corrective licensing), timing

and budgets of new projects, and even their feasibility, may be affected. Discussions are currently in progress with official environmental bodies (at both the federal and state level) for the purpose of establishing criteria to govern environmental compensations.

A work group that has been created in the Brazilian Federal Government is developing a resolution concerning environmental compensation measures which, if implemented, could have an effect on us.

*Fishways*



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The dams at each of our hydroelectric generation facilities can put fish that inhabit the adjoining reservoirs in danger. In order to reduce the impact of these facilities on nearby fish populations, the State Government enacted State Law No. 12,488, dated April 9, 1997, which imposes measures assuring that migratory fish that pass through dams will be redirected to fishways, through which they can pass safely. As of December 31, 2004, we had fishway projects installed at our Igarapé, Salto de Moraes, Funil and Igarapava facilities. In April 2002 we sent COPAM a study relating to our dams. In July 2002 we received a response from SEMAD that requires us to provide additional studies relating to the feasibility of installing fishways in our dams located in Minas Gerais. We executed an agreement with a non-governmental organization, named SMC (*Sociedade Mineira de Cultura*) and the university PUCMinas (Pontificia Universidade Católica de Minas Gerais) in order to proceed with the studies for SEMAD in connection with the Gafanhoto, Cajuru and Volta Grande hydroelectric facilities. We are also evaluating the options for the construction of fishways at Miranda and Nova Ponte hydroelectric plants. The studies that are in progress are not yet conclusive as to the need for the provision of fishways. In addition, there has been no decision by the environmental authorities regarding the building of fishway projects at CEMIG's hydroelectric generation facilities. However, there is a possibility that future decisions by the environmental authorities, or changes in the environmental legislation, or even new information obtained from the studies which are in progress, may lead to a need for the construction of fishways at our hydroelectric generation facilities.

### **Urban occupation of rights of way**





Our piped natural gas distribution networks are underground, crossing through inhabited areas, and using public rights of way in common with underground piping utilities operated by other public concession holders and public agencies. This increases the potential for risk of undue work without prior communication and consultation of our gas distribution network registers, and there is a possibility of this causing accidents, with potentially significant personal, property and environmental damage. However, all our gas networks are explicitly, and intensively, marked and signaled. Gasmig, through its Dig Safely ( *Escave com Segurança* ) program, has been building partnerships with the community, mainly with public authorities and holders of concessions, in addition to the companies which carry out digging in public rights of way, to ensure that before digging close to the natural gas network, they telephone Gasmig's 24-hour helpline and request support for safe execution of their work.

*Transmission lines:* Several of the safety bands under our transmission lines have been occupied by unauthorized facilities (buildings, etc.) and dwellings. These occupations generate risks of electric shock and accidents involving people living at the location, and constitute an obstacle to maintenance of our electricity system. It is thus necessary to solve this situation over the coming years, either removing some of the occupants, or introducing improvements to make it possible to live with these invasions. Faced with the risks associated with this situation, we planned two lines of action for the coming years. The first is preparation of a document entitled Diagnosis of areas invaded and under risk of invasion, for strengthening of inspection activities, including installation of improvements in locations classified as having high invasion risk . In 2004 studies were begun for the contracting of a company specialized in geo-referenced mapping, which will identify the areas with potential for invasion, making possible decisions on measures and procedures in relation to control, monitoring and inspection of the transmission line paths where there is a high risk of invasion. The second line of action involves the evacuation of areas already invaded. The withdrawal of people from these areas involves payment of indemnities, regularization of electricity connections and the opening of bands for the construction of squares and streets. In conformity with CEMIG's risk management, we draw attention to the multi-year planning of allocation of funds to achieve withdrawal of some of the occupants and the execution of local improvements to ensure the safety conditions of these areas.

**Environmental regulations**



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Environmental issues can significantly impact the operations of our company. For example, large hydroelectric power plants can require flooding of considerable areas and as a result relocation of a considerable population. The Brazilian Constitution gives the Federal Government, states and municipalities powers to enact laws designed to protect the environment and issue enabling regulations under these laws. While the Federal Government has the power to promulgate general environmental regulation, state governments have the power to enact more stringent environmental regulation.

The Brazilian National Environment System (SISNAMA *Sistema Nacional do Meio Ambiente*) was created for the purpose of protecting the Brazilian environment. It consists of: an administrative body, the Governing Council (*Conselho Governamental*); a consultative and decision-making body, the National Environment Council, or CONAMA (*Conselho Nacional de Meio Ambiente*); a central body, the Environment Ministry, or MMA (*Ministério do Meio Ambiente*); an executive body, the Brazilian Environment and Renewable Natural Resources Institute, or IBAMA (*Instituto Brasileiro do Meio Ambiente e dos Recursos Naturais Renováveis*); and various local and sectorial bodies. The agencies that merit special attention are CONAMA and IBAMA. CONAMA carries out or approves studies and assists and advises the Government Council on the official orders for government policy on environmental and natural resources, and on decisions, within its attributed scope, on regulations and other legislative rules applicable to the Brazilian environment. IBAMA enforces the national environment policy and inspects, preserves and supports the use of natural resources.

Law No. 6,938/81, of August 31, 1981, is known as the Environmental Policy Law, and regulates civil liability for damage to the environment. In legal terms, this responsibility has an objective nature, and is not only strict but also expands the list of liable parties adopting the principle of joint and several responsibilities. Irrespective of the nature of the offending act, demonstration of a cause-and-effect relationship between the damage caused and an action or omission is enough to create a legal obligation, on the party responsible for the contamination, to redress the environmental damage. Also, compliance with environmental licenses does not eliminate environmental liability.

Activities which cause damage to the environment may also lead to administrative and criminal fines, under Law No. 9,605, of February 12, 1998 (the Environmental Crimes Law). The effects of the aforementioned law apply to any person, individual or legal entity, who by any means contributes to damage caused to the environment to the extent of his/her fault, in the amount of the damage caused. This law provides that a legal entity may be held liable for conduct deemed harmful to the environment, provided that the infraction was committed in its interest or benefit, upon the decision of its legal or contractual representatives or of its plenary board. Management and members of the board who are aware of any criminal conduct of another and are thus able to prevent it but do not do so, are, by their omission, also considered participants in the crime.

The Federal Decree No. 3,179, issued in September 1999, established administrative fines applicable to conduct or activities damaging to the environment and to the regulations governed by the Environmental Crimes Law. This Decree sets forth penalties, such as fines of up to R\$50 million, and authorizes facilities to be closed down.

In relation to water resources, Law No. 9,433 of January 8, 1997 created the National Water Resources Policy, which was organized in accordance with the various river basins of Brazil. This policy is implemented by the governmental and non-governmental agencies, and classifies water as a public asset. Thus, no individual or company may appropriate the use of water, and any use of water does not result in absolute exclusion of all potential users.

Also, public authorities must supply a justification for the concession of rights to use water.

The right to use federal water is given by the National Waters Agency, or ANA (*Agência Nacional de Águas*), created by Law No. 9,984 of July 17, 2000, and regulated by Decree No. 3,692 of December 19, 2000, in collaboration with ANEEL. As well as granting these rights, ANA also regulates and supervises the use of federal water resources and implements the collection of charges for the use of water, at a ratio of 0.75% of the value of the energy generated. Permission for use of non-federal water resources must be obtained from the respective state-level

environmental/water resource agency.

The National Water Resources Policy also created the need for the grant of permission for the use of water in the production of electricity. At the phase of planning of the plant, application must be made by ANEEL to the water resources authorities for reservation of water availability, which will be transformed into permission to use water resources and granted together with the grant of concession for commercial operation of hydroelectric energy. The plants which already are in operation, and have the concession grant, automatically also have the grant of the water resources right. However, when application is made for renewal of the concession for commercial use of hydroelectric energy, grant of the right to use the water resources must also be applied for.

For the construction of the hydroelectric power plant, Brazilian electricity companies have to comply with several environmental protection measures. First, an environmental impact study must be prepared by external experts, who should make recommendations on how to minimize the impact of the plant on the environment. The study, in conjunction with an environmental impact assessment report on the project prepared by the company, is then submitted to the state or federal-level governmental authorities for analysis and approval. The project undergoes a process of licensing in three stages, which includes a Prior License which indicates the viability of the project, an Installation License for the beginning of construction, and an Operation License for startup of the plant. Environmental licenses also have to be obtained for expansion of the plant or installation of new equipment. It should be mentioned that on basis of the environmental impact studies conclusions, the issued license is subject to several conditions or requirements that must be observed; otherwise the licenses may be revoked.

Installations that are considered to represent a considerable environmental impact are obliged by law to allocate a minimum of 0.5% of their total investment costs to the creation of environmental preservation areas.

Under the Brazilian Forest Code (*Código Florestal Brasileiro* - Law No. 4,771 of September 15, 1965), the land area surrounding water reservoirs, whether it is natural or artificial, is considered to be a permanent preservation area, which represents restriction on use. The amendments to the Brazilian Forest Code introduced by Provisional Measure 2,166-67 of August 24, 2001 provide that the operator of a reservoir is obliged to acquire such surrounding areas. This requirement can impact the economic viability of new hydroelectric undertakings, but has so far not been enforced.

The Forest Policy of the State of Minas Gerais (Law No. 14,309 of June 19, 2002) and Decree No. 43,710 of January 8, 2004 does not oblige the operator to acquire the land area surrounding the reservoir, but it does demand indemnity for the restriction on use, in forms provided for by law.

These rules, when applicable, will result in additional costs in connection with in the installation of new hydroelectric power plants.

Any corporate entity involved in activities which cause pollutant effects, or the potential for pollutant effects, or which involve products which are considered dangerous to the environment, is obliged to register with IBAMA. This registry involves quarterly payments of an environmental control and inspection charge TCFA, which for CEMIG's activities is equal to an amount of approximately R\$10 thousand per year.

## **Carbon Market**



The Kyoto Protocol became effective on February 16, 2005. According to the Kyoto Protocol, the reduction of greenhouse gas emissions through projects designed under the Clean Development Mechanism, or CDM, may be converted into Carbon Credits, which may be negotiated worldwide. **Legislation that would govern the carbon market in Brazil and tax incentives in connection therewith is currently before Congress in Brazil. Brazil has great potential to generate Carbon Credits arising from clean energy projects that comply with the CDM.**





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CEMIG s has implemented a strategy to study CDM project development opportunities in the carbon market. In order to undertake CDM projects, we are training our professionals, including through courses administered by USAID and the World Bank. Last year, CEMIG sponsored a course promoted by USAID and the World Bank at the State of Minas Gerais Industry Federation to discuss CDM projects in the State of Minas Gerais. We intend to create a multidisciplinary task force to mobilize our wholly-owned subsidiaries and affiliated companies to identify projects that would allow us to obtain certificates of reduction of greenhouse gases.

**Operational Technologies**



We continue to invest in automated monitoring and control equipment in connection with our strategy of increasing efficiency and further modernizing and automating our generation, distribution and transmission systems.

*Load Dispatch Center*



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The *Centro de Operação de Sistema da Cemig* (System Operation Center), or COS, located at our headquarters in Belo Horizonte, is the nerve center of our operations. The COS is a data clearing house and control center that uses fiber optic and coaxial cables, microwaves and other communication technologies to monitor and coordinate our generation and transmission systems in real time, helping to guarantee the security, continuity, and quality of our energy supply. With the restructuring of the Brazilian utility sector, the COS has begun operating through the ONS, controlling and supervising 39 substations, 22 large plants and 3,017 miles of transmission lines.

### *Regional Distribution Operation Centers*





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Our distribution network is managed through seven *Centros de Operações Regionais de Distribuição* (Regional Distribution Operation Centers), or CODs. The CODs monitor and coordinate our distribution network operations in real time. The CODs are responsible for the supervision and control of 350 distribution substations, 228,314 miles of medium voltage distribution lines, 9,995 miles of sub-transmission lines and 5.9 million customers in our concession area.

There are various systems in use to automate and support the CODs processes including trouble call, field crew management, distribution substation supervision and control, restoration of power, emergency switching, network disconnection and inspection. Technologies like geographic information system and radio/satellite data communication help to reduce the customer restoration time and to provide better customer attendance.

### *Geospatial Information & Technology*



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We are intensively using the geospatial and technical document management technology to support and improve engineering processes. Geo-referenced information of the electrical network, satellite and aerial photographs of the concession area, diagrams and technical document images are stored in geospatial databases and can be easily retrieved by computers connected to our Corporate Network, helping technicians to plan, design, construct, operate and maintain the generation, transmission and distribution network. We are using mobile technology in service dispatch for distribution network maintenance and medium and high-voltage network data acquisition.

### *Internal Telecommunications Network*



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Our private telecommunications network is one of the largest in Brazil. It is comprised of high-performance microwave links with 130 communication stations and total range of 1,380 miles, a telephone system with 188 telephone exchanges and a mobile communication system with 700 trunking radios and 1,105 radio sets. We have also developed several projects in association with Empresa de Infovias S.A. based on fiber-optic networks that uses our distribution infrastructure of poles and transmission towers, aimed at integrating our internal voice, data and image services in order to reduce operational costs and increase the reliability of the electrical system.

### *Corporate Data Network*



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Our corporate network integrates enterprise servers (one 350 MIPS Mainframe processing the Billing System and 10 Risc machines for the ERP System), 7,015 Intel microcomputers, 306 servers and 877 units of connectivity equipment, serving 164 sites in 90 cities of Minas Gerais State. The centralized infrastructure uses modern servers and devices with service level agreements for hardware maintenance and software support. The reception of meter reading data, digital calculation of electricity bills, and issuance of electricity bills to consumers in CEMIG's secondary network were recommended for the ISO-9001:2000 certification.

*Call Centers*





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We have one call center located in Belo Horizonte. Our final customers can use a toll-free number to contact a call center to obtain information about their accounts and to report service problems. Our call center is integrated with the technologies available in the CODs, allowing us to provide up-to-the-minute information to customers about service issues.

### *Maintenance and Repair Systems*



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We use several maintenance and repair systems to minimize unscheduled interruptions in electrical service to our customers. More than 90% of our service interruptions have resulted from factors such as lightning, fire, vandalism, wind and corrosion on our transmission and distribution networks, which are composed largely of steel towers, although we also have wood and concrete overhead lines.

We inspect our transmission lines on average twice a year. The lines are patrolled by helicopter, car and motorcycle. We also use a Gimbal Camera in the aerial inspections. Our linemen climb most of the towers at least once a year, depending on the age and the importance of each line for the whole system. We have continually introduced new predictive techniques into our maintenance program, as for example corona and infrared inspections.

To support emergencies involving fallen towers, we have used modern modular aluminum structures. Most of our intervention on transmission lines is done using live line methods. Being the first company in Brazil to use bare hand live line techniques in the maintenance of transmission lines, we have accumulated, through the last almost thirty years, significant experience in this area. We have trained our staff in this area and have special vehicles and other necessary tools to support live and dead line maintenance.

We also have crews strategically located throughout the State of Minas Gerais in order to promptly attend to our transmission and distribution system needs.

### *Information Security Management*



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In August 2004 we put in place the Corporate Information Security Plan. The principal objective of this plan is to prepare an action plan to reduce the risk of loss of information confidentiality, integrity and availability. The project also aims to adapt the company to the new legal and regulatory requirements which call for implementation of various security controls. A specialized consulting company was contracted, for a period of 11 months, and has been assisting the Information Security Management team in developing the actions and projects.

In 2004 we installed software for information security management, completed the Corporate Network security specification, and began the security assessment and implementation for critical information technology assets.

### **Management Tools**



*Enterprise Resource Planning*





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During the end of 2004, we underwent a complex process of improvements on our current Enterprise Resource Planning, or ERP package (SAP R/3). The process involved an upgrade from version 4.0 into the newer version 4.7 with improvements on internal processes and controls and the implementation of new functionalities. The new system has new and revised functionalities covering accounting, cost and funds control, budgeting, investment management, treasury, cash flow management, quality control, project management, inventory management, maintenance, asset control, human resources management (including payroll, time management and personnel development), travel management, sales management and a new workflow functionality covering the finance and supply chains.

The new solution includes, beyond process review, modernization and legacy systems integration, with new and improved hardware, software and processes on its first phase that went live on January 10, 2005 and supported our unbundling project, approved by ANEEL on December 20, 2004.

The next project phase (expected to be live in July 2005) will pilot improvements on our strategic management functionalities, including balanced scorecard, new data warehouse functionality, long-term cash flow monitoring and financial consolidation.

*Quality Management Systems*



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In 1991, we instituted a company-wide quality control program called Total Quality. As part of the Total Quality Program, we adopted the International Standardization Organization Project in 1999, through which we certify different parts of our operations and management as being of superior quality according to international standards known as ISO 9000 and ISO 14000. We also certify parts of our operations according to internally created criteria.

In addition to the continued expansion in the implementation of the Quality and Environment Management systems in our activities and processes, we also have in progress the implementation of the Health and Safety Management System, providing control in accordance with the standards for this type of system.

Based on experience gained in the last few years, we have prepared the Cemig Management System Manual, which integrates the Quality, Environment and Health and Safety Management Systems. The integration of the management systems, to be carried out in the areas of interest to the Company, will ensure functionality in the activities executed and greater efficiency in the results.

We have received ISO 9001/2000 certification for our business, including certain customer service offices, call centers, laboratories, repair shops, engineering teams and the São Simão hydroelectric power plant, which represented 29% of our installed capacity as of December 31, 2004.

In February 2000, the Nova Ponte hydroelectric power plant, with an installed capacity of 510 MW, received ISO 14001 certification from Det Norske Veritas - DNV. The certification includes the 500 square kilometer (193 square mile) reservoir as well as the 2,850 hectare (11 square mile) Galheiro nature reserve. Nova Ponte is the first large power plant in Latin America to receive this certification.

**In 2004, one transmission and three distribution units, covering 161 municipalities, 54 substations, more than 93 miles of distribution lines, and more than 5 miles of transmission lines were certified under the internally created criteria that we refer to as the CEMIG EMS (Environmental Management System). A materials storage and logistics warehouse also received this certification. Products and services certified include: new customer connections; billing; collection; product sales and services; network expansion and improvement; network operation; public lighting maintenance and restoration; overhead lines and network maintenance and inspection; electric system planning; and substation and equipment maintenance and inspection.**

### *Risk Management*



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With the assistance of a leading consulting firm chosen through a formal selection process, we began establishment of a Corporate Risk Management System in 2003, and consolidated it in 2004 in connection with our restructuring. As holder of a concession in the Brazilian electricity sector, we operate in environments where factors such as corporate restructurings, regulations issued by government agencies, technological development, globalizations and changes in the consumer market generate uncertainties and threats.

The implementation of a coherent risk vision and strategy at the corporate level is a new management trend, encouraged not only by the requirements of the Sarbanes-Oxley Act and the methods recommended by the Committee of Sponsoring Organizations (COSO II), but also by the perception that management of risk is an essential part of a sustainable development philosophy which aims to create value for shareholders.

Our Corporate Risk Management Program aims to achieve the following: operate as an auxiliary in achievement of the objectives set by the strategic plan; create awareness among shareholders of the possible events that could constitute a risk of loss of value; structure the company to be able to take proactive stances in relation to its risk environment; provide the company's executives with a methodology and tools for effective management of risk; and provide other areas of strategic management with input concepts and procedures, and factors that strengthen the company's organizational control infrastructure.

In 2004, the structure of corporate risks that was prepared in 2003 was revised and updated, to adapt it to the profound regulatory changes to which the whole Brazilian electricity sector was subjected – most importantly Law 10,848, regulated by Decree 5,163. We also put in place the functional structure of the risk management system, with the creation of CEMIG's Corporate Risk Management Committee, finalizing an approved version of the Corporate Risks Management Policy, the Corporate Risk Management Procedures Manual, and licensing of the information technology tool which supports this activity.

In 2003, CEMIG's Electricity Risks Management Committee, or CGRE, was created to propose policies and procedures for approval by the executive officers to minimize risks in the contracting (purchase and sale) of energy. The committee has members from numerous areas of the Company, including generation, distribution, sales, legal and financial.

The CGRE was very active in 2004, analyzing the recent changes in the Brazilian electricity sector and their impact on CEMIG. Based on its analyses of market, price, regulatory and legal risks, the committee proposed guidelines for the structure of contracts for the sale of electricity to Free Consumers, through the auction procedures held by the Company. It also gave support to the decisions of the executive officers in relation to the Company's participation in the first Existing Energy Supply Auction, held on December 7, 2004 by the CCEE. Based on risk analyses, it proposed the maximum volumes that could be sold and the amounts purchased by the distributor in that auction.

### *Management of Financial Risks*





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In 2004, we continued putting in place the *Risk Control* software for management of financial risks, to monitor the risks associated with the carrying out of transactions in the financial markets. Use of this software, associated with implementation of the risk management methodology, is designed to give our managers capacity to recognize the existing and potential risks and to control them, and to operate proactively in relation to their environment of financial risks when implementing plans of action. The delay in fully implementing the software was due to the mobilization of the task force in the upgrading of SAP R/3.

### **Property, Plant and Equipment**



Our principal properties consist of the power generation plants and transmission and distribution facilities described in this Item 4. Our net book value of total property, plant and equipment, including our investment in certain consortia that operate electricity generation projects, was R\$11,191 million at December 31, 2004 (including ongoing construction projects). Generation facilities represented 52.4% of this net book value, transmission and distribution facilities represented 43.8% and other miscellaneous property and equipment, including natural gas and telecommunication facilities, represented 3.8%. The average annual depreciation rate applied to these facilities was 2.5% for hydroelectric generation facilities, 3.4% for transmission facilities, 4.9% for distribution facilities, 7.7% for administration facilities, 6.0% for natural gas facilities and 7.9% for telecommunication facilities. Our facilities are generally adequate for our present needs and suitable for their intended purposes.

Item 5. **Operating and Financial Review and Prospects**



*You should read the information contained in this section together with our financial statements contained elsewhere in this annual report. The following discussion is based on our financial statements, which have been prepared in accordance with U.S. GAAP and presented in reais.*

*General*





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We are a state-controlled energy company engaged, through our subsidiaries, primarily in the generation, transmission and distribution of electricity in Minas Gerais. According to ANEEL, at December 31, 2004, we were the seventh largest electric power generation concessionaire in Brazil as measured by total installed capacity, and for the year ended December 31, 2004, we were the largest electric power distribution concessionaire in Brazil, as measured by GWh of energy sold to final customers. We supplied approximately 97% of the electricity consumed in Minas Gerais during the year ended December 31, 2004. See Item 4. Information on the Company Customers and Billing. At December 31, 2004, we generated electricity at 47 hydroelectric plants, four thermoelectric plants and one wind farm and had a total installed generation capacity of 5,949 MW, of which the hydroelectric plants accounted for 5,764 MW. See Item 4. Information on the Company Generation and Purchase of Electric Power. The State Government as our controlling shareholder establishes our operating and long-term strategy.

The following are our subsidiaries as of December 31, 2004:

Cemig Geração e Transmissão S.A. (100% interest). Cemig Generation and Transmission, which as of January 1, 2005 is engaged in the generation and transmission of energy.

Cemig Distribuição S.A. (100% interest): Cemig Distribution, which as of January 1, 2005 is engaged in the distribution of energy.

Sá Carvalho S.A. (100% interest). Sá Carvalho S.A. is engaged in the production and sale of electric energy and holds the concession to operate the Sá Carvalho hydroelectric power plant.

Rosal S.A. (100% interest). Rosal S.A. is engaged in the production and sale of electric energy and holds the concession to operate Rosal hydroelectric power plant. See Note 10 to our consolidated financial statements.

Usina Térmica Ipatinga S.A. (100% interest). Usina Térmica Ipatinga S.A. is an SPP engaged in the production and sale of electric energy at the Ipatinga thermoelectric and steam power plant.

Companhia de Gás de Minas Gerais GASMIG (55% interest). Gasmig is engaged in the acquisition, transportation and distribution of natural gas. In December 2004, CEMIG sold 40% of its interest in Gasmig. See note 10 to our consolidated financial statements.

Empresa de Infovias S.A. (99.94% interest). The principal activities of Empresa de Infovias S.A. are rendering telecommunications services and developing activities related thereto, through multiservice networks using optical fiber cable, coaxial cable and other electronic equipment. Empresa de Infovias S.A. owns 69.25% of the

capital stock of Way TV Belo Horizonte S.A., a cable TV and internet services provider in certain cities of the State of Minas Gerais.

Efficientia S.A. (100% interest). Efficientia is engaged in rendering efficiency, optimization and energy solutions services, as well as providing operating and maintenance services, to energy supply facilities. Efficientia initiated operations in the first quarter of 2003.

Horizontes Energia S.A. (100% interest). Horizontes Energia is engaged in the production and sale of electric energy, as an independent power producer, at the Machado Mineiro and Salto do Paraopeba hydroelectric power plants, located in the State of Minas Gerais, and the Salto Voltão and Salto do Passo Velho hydroelectric power plants, located in the State of Santa Catarina. Horizontes Energia initiated operations in the first quarter of 2003.

Companhia de Transmissão Centroeste de Minas (51% interest). Companhia de Transmissão Centroeste de Minas will be responsible for building, implementing, operating and maintaining the 345 kV transmission line from the substation of the Furnas Hydroelectric Power Plant and a substation located in Pimenta.

We also have a 100% interest in each of the following companies: Usina Termelétrica Barreiro S.A.; CEMIG PCH S.A.; CEMIG Trading S.A.; and Cemig Capim Branco Energia S.A. These companies were organized to conduct specific projects in the electric energy sector and have not yet commenced operations.

Our consolidated financial statements as of and for the years ended December 31, 2004 and 2003 include the financial results of CEMIG and all of our subsidiaries (operational and pre-operational) described above. In 2004, we entered into a Shareholders' Agreement with Petrobras and Gaspetro in connection with the sale of 40% of our equity interest in Gasmig. Gasmig's revenues and expenses were included in our consolidated Statement of Income up to December 15, 2004. Gasmig's assets and liabilities are not included in our consolidated financial statements as of December 31, 2004. See Notes 2 and 10 to our consolidated financial statements. Additionally, we have a minority interest in the following companies:

Central Hidrelétrica Pai Joaquim S.A. (48.5% interest). Central Hidrelétrica Pai Joaquim S.A. is engaged in the production and sale of Electric Energy as an independent power producer.

Central Termelétrica de Cogeração S.A. (48.5% interest). Central Termelétrica de Cogeração S.A. is engaged in the production and sale of thermoelectric energy, as an independent power producer, through the Barreiro thermoelectric plant, located on Vallourec & Mannesmann's premises in the State of Minas Gerais.

Companhia Transleste de Transmissão (25.0% interest). Companhia Transleste de Transmissão will be responsible for building and operating the 345 kV transmission line connecting a substation located in Montes Claros and the substation of the Irapé Hydroelectric Power Plant.

Companhia Transudeste de Transmissão (24.0% interest). Companhia Transudeste de Transmissão will be responsible for building, implementing, operating and maintaining the 345 kV transmission line from Itutinga to Juiz de Fora.

Companhia Transirapé de Transmissão (24.4% interest). Companhia Transirapé de Transmissão will be responsible for constructing, implanting, operating and maintaining the 230 kV transmission line LT Irapé Araçuaí.

#### **Critical Accounting Estimates**



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The preparation of our consolidated financial statements in conformity with U.S. GAAP requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements, as well as the reported amounts of revenues and expenses during the reporting periods. We evaluate our estimates on an ongoing basis and base them on a combination of historical experiences and various other assumptions that we believe to be reasonable under the circumstances. Actual results could differ materially from those estimates. Our critical accounting policies that affect our more significant judgments used in the preparation of our consolidated financial statements are set forth below.

### *Regulatory assets*



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Due to changes in the electric utilities sector in Brazil in 2001 and 2002 and related acts by regulatory bodies of the Federal Government, we have concluded that because the rate-setting structure in Brazil was designed to recover certain allowable costs, we are subject to the provisions of Statement of Financial Accounting Standards No. 71 Accounting for the Effects of Certain Types of Regulation, or SFAS No. 71.

SFAS No. 71 requires rate-regulated public utilities such as CEMIG to record certain costs and credits allowed in the rate-setting process in different periods than for non-regulated entities. These costs and credits are deferred as regulatory assets and are recognized in the consolidated statement of operations at the time they are reflected in rates. Accordingly, we capitalize allowable incurred costs as deferred regulatory assets when there is a probable expectation that future revenue equal to the costs incurred will be billed and collected as a direct result of

the inclusion of the costs in an increased rate set by the regulator. The deferred regulatory asset is realized when we collect the related costs through billings to customers. ANEEL performs a rate review on an annual basis. If ANEEL excludes all or part of a cost from recovery, that portion of the deferred regulatory asset is impaired and is accordingly reduced to the extent of the excluded cost. We evaluate and revise the accounting for our regulatory assets on an ongoing basis as new regulatory orders are properly issued and account for our activities under SFAS No. 71. As we recognize regulatory assets in accordance with rulings of the regulatory authorities of the Federal Government, future regulatory rulings may impact the carrying value and accounting treatment of our regulatory assets.

During 2001, the electricity markets in significant portions of Brazil experienced rationing, or reduced availability of electricity to customers, due to low rainfall, reduced reservoir levels and Brazil's significant dependence on electricity generated from hydrological resources. These factors resulted in lower sales. In December 2001, electricity concessionaires in Brazil, including us, reached an industry-wide agreement with the Federal Government that provided resolution to rationing related issues as well as certain electricity rate-related issues. This agreement, known as the General Agreement of the Electricity Sector, generally allows for increased rates to be charged to electric power consumers until the amounts lost by the power generation and distribution concessionaires as a result of the rationing are recovered. The rate increases set forth in the General Agreement of the Electricity Sector intended to reimburse rationing-related losses are expected to remain in effect from January 2002 for an average of 72 months. However, no assurance can be given that the full amount of the rationing-related losses we incurred will be recovered over this period.

In addition, we are subject to the provisions of Emerging Issues Task Force Issue No. 92-07 Accounting by Rate-Regulated Utilities for the Effects of Certain Alternative Revenue Programs, or EITF 92-07, which establishes a 24-month limit for collection of regulatory assets related to billing losses. Accordingly, we were required to estimate this asset recovery based on assumptions of future billings.

We perform periodic valuations of the recoverability of our deferred regulatory assets in order to determine whether impairment provisions are necessary based on applicable ANEEL regulations. We recorded a loss provision accordingly. This provision is based on projections prepared by us, which projections may change in response to regulatory changes and other developments. See Notes 2(q) and 4 to our consolidated financial statements. If ANEEL disallows a material amount of capitalized costs to be included in future rates, the write-off of the regulatory assets may have a material adverse impact on our operating results.

#### *Valuation of assets*

We have long-lived assets, including power generation plants. Many of these assets are the result of recent capital investments and have not yet reached a mature life cycle in construction. We assess the carrying amount and potential impairment of these long-lived assets whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Factors we consider in determining whether an impairment review is necessary include a significant underperformance of the assets relative to projected future operating results and significant negative industry or economic trends. We determine when an impairment review is necessary through a comparison between the expected undiscounted future cash flows and the carrying amount of the asset. If the carrying amount of the asset is the larger of the two amounts, an impairment loss is recognized by the amount that the carrying amount of the asset exceeds the fair value of the asset. The fair value is determined by quoted market prices, appraisals or the use of valuation techniques such as expected discounted future cash flows. We must make assumptions regarding these estimated future cash flows and other factors to determine the fair value of the respective assets. In determining estimated future cash flows, we consider historical experience as well as future expectations and estimated future cash flows are based on expected future rates and expected future customer demand. A significant reduction in actual cash flows and estimated cash flows may have a material adverse impact on our operating results and financial condition.

#### *Accrual for contingencies*



We are party to certain legal proceedings in Brazil arising in the normal course of business regarding tax, labor, civil and other issues.

We account for contingencies in accordance with SFAS No. 5 Accounting for Contingencies. Such accruals are estimated based on historical experience, the nature of the claims, as well as the current status of the claims. Accounting for contingencies requires significant judgment by management concerning the estimated probabilities and ranges of exposure to potential liability. Management's assessment of our exposure to contingencies could change as new developments occur or more information becomes available. The outcome of the contingencies could vary significantly and could materially impact our consolidated results of operations, cash flows and financial position. Management has applied its best judgment in applying SFAS No. 5 to these matters.

#### *Employee post-retirement benefits*

We sponsor a defined-benefit pension plan and defined-contribution pension plan covering substantially all of our employees. We have also established post-retirement health care plans and pay life insurance premiums. We account for these benefits in accordance with SFAS No. 87 Employers Accounting for Pensions and SFAS No. 106 Employers Accounting for Post-retirement Benefits other than Pensions. We have applied SFAS 132(R) Employers Disclosures about Pensions and Other Post-retirement Benefits to disclose information about pension plans and other post-retirement benefit plans.

The determination of the amount of our obligations for pension and other post-retirement benefits depends on certain actuarial assumptions. These assumptions are described in note 17 to our consolidated financial statements and include, among others, the expected long-term rate of return on plan assets and increases in salaries and healthcare costs. In accordance with U.S. GAAP, actual results that differ from our assumptions are accumulated and amortized over future periods and generally affect our recognized expenses and recorded obligations in such future periods. While we believe that our assumptions are appropriate, significant differences in actual results or significant changes in our assumptions may materially affect our pension and other post-retirement obligations.

#### *Deferred taxes*

We account for income taxes in accordance with SFAS No. 109 Accounting for Income Taxes, which requires an asset and liability approach to recording current and deferred taxes. Accordingly, the effects of differences between the tax basis of assets and liabilities and the amounts recognized in our consolidated financial statements have been treated as temporary differences for the purpose of recording deferred income tax.

We regularly review our deferred tax assets for recoverability and establish a valuation allowance based on historical taxable income, projected future taxable income, and the expected timing of the reversals of existing temporary differences. If we are unable to generate sufficient future taxable income, or if there is a material change in the actual effective tax rates or time period within which the underlying temporary differences become taxable or deductible, we could be required to establish a valuation allowance against all or a significant portion of our deferred tax assets resulting in a substantial increase in our effective tax rate and a material adverse impact on our operating results.

#### *Depreciation*

Depreciation is computed using the straight-line method, at annual rates based on the estimated useful lives of the assets, in accordance with ANEEL regulations and industry practice in Brazil. To the extent that the actual lives differ from these estimates, there would be an impact on the amount of depreciation accrued in our consolidated financial statements. A significant decrease in the estimated useful life of a material

amount of property, plant and equipment, or in the assets of the electricity generation project consortium in which we are a partner, could have a material adverse impact on our operating results in the period in which the estimate is revised and in subsequent periods.

*Allowance for doubtful accounts*

We record an allowance for doubtful accounts in an amount that we estimate to be sufficient to cover presently foreseeable losses.

We continuously monitor collections and payments from customers and review and refine our estimation process.

**Recently Issued U.S. GAAP Pronouncements**



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In July 2003, the Emerging Issues Task Force stated in EITF Issue No. 03-11, or EITF 03-11, that the determination as to whether realized gains and losses on derivative contracts not held for trading purposes should be reported on a net or gross basis is a matter of judgment that depends on the relevant facts and circumstances and the economic substance of the transaction. In analyzing the facts and circumstances, EITF Issue No. 99-19 and Opinion No. 29, Accounting for Non-monetary Transactions, should be considered. EITF 03-11 is effective for transactions or arrangements entered into after September 30, 2003. The adoption of EITF 03-11 did not have a material effect on the Company's financial statements.

In December 2004, the Financial Accounting Standards Board (the FASB) issued Statement of Financial Accounting Standards No. 153, Exchanges of Non-monetary Assets - an amendment of APB Opinion No. 29 (SFAS 153), which amends Accounting Principles Board Opinion No. 29, Accounting for Non-monetary Transactions to eliminate the exception for non-monetary exchanges of similar productive assets and replaces it with a general exception for exchanges of non-monetary assets that do not have commercial substance. SFAS 153 is effective for non-monetary asset exchanges occurring in fiscal periods beginning after June 15, 2005. The Company will apply SFAS 153 in the event that exchanges of non-monetary assets occur in fiscal periods beginning after June 15, 2005.

### **Analysis of Electricity Sales and Cost of Electricity Purchased**



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Electricity rates in Brazil are set by ANEEL, which has the authority to readjust and review rates in accordance with the applicable provisions of the concession contracts. See Annex A The Brazilian Power Industry Rates for the Use of the Distribution and Transmission Systems .

We charge captive customers for their actual electricity consumption during each 30-day billing period at specified rates. Certain large industrial consumers are charged according to the electricity capacity contractually made available to them by us, with adjustments to those rates according to consumption during peak demand time as well as capacity requirements that exceed the contracted amount.

In general, rates on electricity that we purchase are determined by reference to the capacity contracted for as well as the volumes actually used. In the case of Itaipu, we are committed to purchase 17.3% of the amount of its capacity that Brazil is required to purchase at a fixed price denominated in dollars paid three times a month at exchange rates determined at the time of each payment.

The following table sets forth the average rate (in *reais* per MWh) and volume (by GWh) components of electricity sales and purchases for the periods indicated. The term average rate refers to revenues for the relevant class of customers divided by the MWh used by such class and does not necessarily reflect actual rates and usage by a specific class of end-users during any particular period. The figures included in the table include the energy sold by Barreiro and Pai Joaquim, which were not consolidated in our financial statements.



	Year ended December 31,			
	2004		2003	2002
<b>Electricity Sales:</b>				
Average rate to final customers (R\$/MWh)				
Industrial rate	154.86		132.35	100.06
Residential rate	406.07		356.87	281.60
Commercial rate	355.95		306.00	240.94
Rural rate	214.52		186.76	147.80
Public services rate and others	236.99		201.78	158.80
Total sales to final customers (GWh)				
Industrial customers	22,969		21,715	21,906
Residential customers	6,526		6,529	6,360
Commercial customers	3,537		3,402	3,283
Rural customers	1,846		1,783	1,705
Public services and other customers	2,498		2,478	2,330
Average rate (R\$/MWh)	226.19		197.12	151.64
Total revenues (millions of R\$)	8,560		7,179	5,458
Sales to distributors:				
Volume (GWh)	364		621	313
Average rate (R\$/MWh)	68.68		51.53	67.09
Total revenues (millions of R\$)(1)	25		32	21
<b>Electricity Purchases from Itaipu:</b>				
Volume (GWh)	11,936		12,220	12,735
Average cost (R\$/MWh)	95.93		96.15	76.87
Total cost (millions of R\$)	1,145		1,175	979

(1) Does not include R\$12 million, R\$24 million and R\$140 million relating to energy transactions on the CCEE during 2004, 2003 and 2002, respectively.

## Rates

Our results of operations in the past have been significantly affected by fluctuations in the levels of rates that we are permitted to charge for the generation and distribution of electricity. The rate-setting process in Brazil has historically been influenced by government attempts to control inflation. With the restructuring of the electric power sector in Brazil that commenced in 1995 and under the terms of the renewal of the concession agreement that we signed with ANEEL in 1997, the process by which rates are set has changed to a significant degree. Electricity that we distribute to captive customers (those customers with no alternative means of energy supply, including residential, commercial and most industrial customers) is provided at rates that are adjusted and revised by ANEEL in accordance with the provisions of our concession contract. We have entered into electricity supply contracts at freely negotiated rates with our Free Consumers (those customers that have a demand of 3 MW or more of electricity at voltage levels of 69 kV or more) that elected not to be subject to ANEEL's rate-setting structure. Under Law No. 10,848, distribution companies are no longer allowed to enter in new contracts for sale of electricity to Free Consumers at non-regulated prices. See "The Brazilian Power Industry Rates for the Use of the Distribution and Transmission Systems" in Annex A.

ANEEL has approved extraordinary rate increases designed to compensate generation and distribution companies for losses incurred as a result of the Electricity Rationing Plan. See "Power Rationing and Government Measures to Compensate Electric Utilities."

ANEEL, through Resolution No. 71, dated as of April 4, 2005, established our first periodic rate revision, allowing for recovery of operating costs and an appropriate return on investments.

The average rate adjustment applied to our rates on April 8, 2003 as part of our periodic rate review was 31.53%. However, according to Resolution No. 71, such rate adjustment was entitled to be 44.41%. ANEEL has

indicated that the rate adjustments expected for the years from 2004 to 2007 will be adjusted in order to recover the differences between the 44.41% rate adjustment we were entitled to and the 31.53% rate adjustment that was authorized. For more information see Item 8. Financial Information Legal Proceedings Regulatory Matters.

The difference between the revenue under the 31.53% rate adjustment and the revenue that would have been earned based on the 44.41% rate adjustment was recorded by CEMIG as a deferred regulatory asset of R\$1,013 million, including monetary variation and accrued interest at a rate of 11.3%, to be recovered through the annual readjustments until 2007. See Note 4 to our consolidated financial statements.

ANEEL issued Resolution No. 87 on April 6, 2005, which established our average annual rate adjustment of 23.88%. The components of this increase are (i) 6.68% due to the Rate Adjustment Index (*Índice de Reajuste Tarifário*), or IRT; (ii) 5.72% due to deferred regulatory asset; (iii) 7.35% due to intra-annual variation of fixed costs, or CVA; (iv) 2.46% due to increases in the *Programa de Formação do Patrimônio do Servidor* (a fund for the benefit of public employees), or PASEP, and the *Contribuição para Seguridade Social* (a federal social security contribution), or COFINS, taxes and (v) 1.67% due to revenue we did not achieve in 2004 as a result of the re-issuing of Resolution No. 83 on May 24, 2004, which reduced our rates.

#### **Power Rationing and Government Measures to Compensate Electric Utilities**

Low amounts of rainfall in 2000 and early 2001, vigorous growth in demand for energy and Brazil's significant dependence on electricity generated from hydrological resources resulted in abnormally low water levels in many reservoirs that are used to power Brazil's major hydroelectric generation facilities. In May 2001, the Federal Government announced several measures in response to these conditions. First, the President of Brazil passed Provisional Measure No. 2,147 on May 15, 2001 (as updated by Provisional Measure No. 2,152-2 on June 1, 2001), creating the *Câmara de Gestão da Crise de Energia Elétrica*, or Energy Crisis Committee. The Energy Crisis Committee resolved on May 16, 2001 to require certain electricity distributors, including us, to suspend distribution of electricity to new customers (except residential and rural customers) and for certain non-essential purposes such as nighttime sporting events and advertising use, and to reduce distribution for the illumination of public areas by 35%. Second, the President passed Decree No. 3,818, on May 15, 2001, requiring the Federal Government to reduce its electricity consumption by 35% beginning July 1, 2001. Third, on May 18, 2001, the Federal Government announced additional power rationing measures to be imposed on industrial, commercial and residential customers in the most industrialized and heavily populated areas of Brazil beginning on June 1, 2001. These measures required most residential consumers to reduce their electricity consumption by 20% of the average consumption in May, June and July 2000. Industrial and commercial consumers also had to reduce their consumption by 15% to 25% of the average consumption during the same period. Further measures provided that bonuses would be paid to residential consumers whose energy consumption was lower than the requisite target and that power cuts and surcharges would be imposed on consumers whose energy consumption exceeded the requisite target. ANEEL established specific accounts and controls to record the effect of the rationing measures relating to the bonus, surcharge and other related costs. The power rationing measures ultimately ceased on February 28, 2002.

On October 17, 2001, the Federal Government, through Provisional Measure No. 4, approved by Law No. 10,310 of November 22, 2001, stated that electric utilities, including us, would be reimbursed for expenses associated with payment of bonuses to consumers and other related costs that exceeded the aforementioned surcharges. In 2002, we received approximately R\$132 million as reimbursement for a portion of the expenses we incurred in connection with payment of bonuses to consumers. In addition, we are currently negotiating with ANEEL our reimbursement of approximately R\$23 million relating to surcharges that were not paid by certain customers because their surcharges are under dispute. There is no assurance that ANEEL will reimburse us, and therefore the total estimated exposure to the Company for this matter is fully reserved. In accordance with ANEEL Resolution No. 600, dated October 31, 2002, we have been reimbursed for operating costs of approximately R\$28 million that relate to the adoption of the Electricity Rationing Plan and that exceed amounts received from surcharges on consumer rates. Reimbursement of these operating costs was made through rate increases in force since April 8, 2003, April 8, 2004 and April 8, 2005.

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On December 12, 2001, through Provisional Measure No. 14, approved on April 26, 2002 by Law No. 10,438, the Federal Government authorized the creation of the General Agreement of the Electricity Sector. The General Agreement of the Electricity Sector provides that electric power distribution and generation companies in

Brazil, such as us, will be compensated for revenue losses caused by the reduction in amounts of energy sold and the purchase of energy on the CCEE, as applicable, due to the Federal Government-mandated rationing measures. Compensation is made by means of an extraordinary increase in the energy rate applicable to future power sales and companies are entitled to use this increased rate for an average period of 72 months, beginning January 2002. See Note 4 to our consolidated financial statements.

#### **Impact of Our Account Receivable from the State Government**

Our liquidity, as well as net income, is affected by payments made in connection with the CRC Account, the account receivable we have from the State Government. The State Government did not make any payments to us under the CRC Account Agreement in 2001 or 2002. In 2003 and 2004, we offset a portion of these overdue amounts against payments of interest on capital that we are required to make to the State Government as our shareholder. In order to address the settlement of these outstanding amounts, we signed three amendments to the CRC Account Agreement with State Government, each of which is described below.

The First Amendment to the CRC Account Agreement was signed on January 24, 2001 and its purpose was to change the monetary restatement index from UFIR (Tax Reference Unit Index) to IGPD-DI (*Índice Geral de Preços* - General Market Price Index), since the UFIR was extinguished in October 2000.

The Second Amendment to the CRC Account Agreement, signed on October 14, 2002, refers to 149 monthly installment payments, with maturities from January 1, 2003 through May 1, 2015, representing the total amount of R\$1,845 million at December 31, 2004, bearing interest at 6% per year, with restatement based on IGP-DI. We entered into this Second Amendment with the State Government in order to preserve the terms and conditions of the original CRC Account Agreement with respect to the above-referenced installments. We did not receive any scheduled payments from the State Government in respect of this Second Amendment. We recorded a full provision for loss for this asset as of December 31, 2001. See Note 3 to our consolidated financial statements.

The Third Amendment to the CRC Account Agreement, signed on October 24, 2002, refers to outstanding installments originally due under the CRC Account Agreement from April 1, 1999 through December 31, 1999 and from March 1, 2000 through December 1, 2002. These installments, which totaled R\$1,097 million as of December 31, 2004, bear interest at an annual rate of 12%, with restatement based on IGP-DI. We did not receive any scheduled payments in respect of this Third Amendment in 2002. In 2003 and 2004, we offset a portion of overdue amounts in the value of R\$28 million and R\$49 million, respectively, against payments of interest on capital that we are required to make to the State Government as our shareholder. We are permitted to retain payments of dividends and interest on capital due to the State Government as our shareholder as a set-off against amounts that the State Government owes us under this Third Amendment. For this reason, we have not recorded a loss provision in respect of amounts due thereunder. See Note 3 to our consolidated financial statements.

On November 19, 2004 our Board of Directors unanimously approved the main terms of a Fourth Amendment to the CRC Account Agreement. If we execute this amendment with the State Government, we will be entitled to retain 50% of the payments of dividends and interest on capital due to the State Government, as our shareholder, and to set off such amounts against amounts that the State Government owes us under the CRC Account Agreement. Under the terms approved by our Board of Directors, the outstanding amount will bear interest at an annual rate of 10%, with restatement based on the IGP-DI. The execution of the Fourth Amendment depends on the prior approval by our shareholders, ANEEL and the legislative assembly of the State of Minas Gerais. See **Item 10. Additional Information - Material Contracts - CRC Account Agreement.**

**Exchange Rates**

Substantially all of our revenues and operating expenses are denominated in *reais*. Although our electricity purchases from Itaipu are denominated in U.S. dollars, the related foreign exchange risk is no longer reflected in our operating revenues and operating expenses due to rate legislation changes in 2001 which allow electricity utilities such as us to record exchange rate losses related to Itaipu purchases as deferred regulatory assets. However, we have significant levels of foreign currency-denominated debt and other liabilities. As a result, in reporting periods when the *real* declines against the dollar or other foreign currencies in which our debt is denominated, our operating

results and financial position are adversely affected. Foreign exchange gain or loss and monetary variation gain or loss may significantly impact our results of operations in periods in which there are wide swings in the value of the *real* relative to the dollar or high inflation. We have a number of financial and other contracts under which we owe, or are entitled to, amounts in respect of monetary variation as measured by an index of price inflation in Brazil. In 2004, we have used financial instruments such as interest rate swaps in order to reduce the risk from exchange rate fluctuations. As of December 31, 2004, we had entered into swap agreements in the notional amount of US\$88.2 million and, with respect to the Japanese yen, in the amount of ¥6,937 million (equivalent to US\$67.8 million), in order to change the original interest rate of certain financing from an interest rate calculated based on the U.S. dollar and Japanese yen variations to an interest rate calculated based on the *Certificado de Depósito Interbancário* CDI (Interbank Certificates of Deposit) rate. See Notes 2(d), 14, 21, 23 and 24 to our consolidated financial statements.

### **Unbundling**

We undertook a reorganization of our corporate structure to comply with Law 10,848/04, which establishes that a distribution company may not exercise other activities such as the generation and transmission of electric energy. Two wholly-owned subsidiaries were created, Cemig Generation and Transmission and Cemig Distribution, which will carry out the activities of electricity generation and transmission, and distribution respectively. This process will be finalized with the signature of amendments to the existing concession contracts, after convocation by ANEEL.

### *Financial Reporting and Tax Considerations*

We do not believe that the unbundling will result in material differences in the presentation of our reporting for financial purposes in accordance with U.S. GAAP or Brazilian GAAP since the financial results of the new generation, transmission and distribution subsidiaries would be consolidated with ours. We also do not believe that our marginal tax rate, on a consolidated basis, will change as a result of the unbundling. We do, however, anticipate that our operating results will be adversely affected as a consequence of the application of certain Brazilian revenue taxes. The revenue taxes which would cause the adverse effect on operating results comprise the *Contribuição para Seguridade Social* (a federal social security contribution), or COFINS, and the *Programa de Formação do Patrimônio do Servidor* (a fund for the benefit of public employees), or PASEP, and were assessed against our consolidated revenues at a combined rate of approximately 4.65% from December 2002 to December 2003 and 3.65% from January through November 2002. Since February 2004, the combined tax rate for these contributions is 9.25% of a tax base equal to the gross revenue less certain deductions. Following the unbundling, we anticipate that the revenue taxes would be assessed at the subsidiary level with respect to revenues of the generation subsidiary and, separately, revenues of the distribution subsidiary.

### **Year Ended December 31, 2004 Compared to Year Ended December 31, 2003**

#### *Net operating revenues*

Net operating revenues increased 26.9% to R\$7,654 million in 2004 from R\$6,032 million in 2003 due primarily to higher electricity sales to final customers.





	2004	% of net operating revenues	2003	% of net operating revenues	2004 versus 2003 - %
Electricity sales to final customers	8,561	111.8	7,179	119.0	19.3
Regulatory extraordinary rate adjustment	89	1.2	63	1.0	41.3
Deferred rate adjustment	640	8.3	199	3.3	221.6
Electricity sales to the interconnected power system	36	0.5	56	0.9	(35.7)
Use of basic transmission network	245	3.2	257	4.3	(4.7)
Other operating revenues	536	7.0	468	7.8	14.5
Tax on revenues	(2,453)	(32.0)	(2,190)	(36.3)	12.0
Total net operating revenues	7,654	100.00	6,032	100.00	26.9

The increase in revenues from electricity sales to final customers is primarily due to increases in the average rate and in the volume of electricity sales to final customers. There was a 14.8% increase in the average energy rate in 2004 to R\$226.21 per MWh compared to R\$197.12 per MWh in 2003 as a result of rate increases of 31.5% in April 2003 (full effect in 2004) and 14.0% in April 2004. In addition, there was a 4.1% increase in the volume of our electricity sales to final customers. In 2004, we recorded R\$89 million in revenue relating to the regulatory extraordinary rate adjustment, a 41.3% increase compared to the R\$63 million that we recorded in 2003. We recorded revenue relating to the regulatory extraordinary rate adjustment in accordance with the terms of the General Agreement of the Electricity Sector, which provides for reimbursement of revenue losses incurred during the period of the Electricity Rationing Plan and related spot market transactions through special rate increases to be billed to final customers, and in accordance with consensus described in EITF Issue No. 92-07, Accounting by Rate-Regulated Utilities for the Effects of Certain Alternative Revenue Programs, which establishes a 24-month limit for the recovery of revenue losses incurred during the Energy Rationing Plan. See Note 4 to our consolidated financial statements.

Revenues related to the deferred rate adjustment were R\$640 and R\$199 million in 2004 and 2003, respectively. The ANEEL Resolution No. 71, dated April 4, 2004, disclosed the results of CEMIG's periodic rate review. According to this resolution, the rate adjustment that would have to be applied on CEMIG's rates starting April 8, 2003 was 44.4%, instead of the 31.5% applied. The difference will be included by ANEEL in future rate adjustments. See Note 4 to our consolidated financial statements.

Electricity sales to the interconnected power system were R\$36 million in 2004, a 35.7% decrease compared to R\$56 million in 2003. This decrease resulted primarily from lower sales of energy on the spot market in 2004.

Other operating revenues increased 14.5% to R\$536 million in 2004 from R\$468 million in 2003. The variation in our other operating revenues in 2004 is mainly due to R\$53 million increase in revenues from Gasmig, our subsidiary. We consolidated Gasmig's revenues and expenses for the period from January 1, 2004 to December 15, 2004, the date of our sale of a 40.00% equity interest in Gasmig to Petrobras. See Note 10 and 19 to our consolidated financial statements.

Taxes on revenues increased 12.0% to R\$2,453 million in 2004 from R\$2,190 million in 2003 as a result of the increase in our electricity sales to final customers in 2004 as compared to 2003 and as a result of the VAT billed to customers in connection with the extraordinary rate adjustment. Taxes on revenues consist of: (i) VAT, assessed at an average rate of 21% on electricity sales to final customers, and VAT billed to customers related to the deferred regulatory assets; (ii) COFINS, assessed at a rate of 7.6%; (iii) PASEP, assessed at a rate of 1.65%; and (iv) the *Encargo de Capacidade Emergencial* (Emergency Capacity Charge), a charge established in 2002 that is prorated among final consumers of electric energy and relates to the *Comercializadora Brasileira de Energia Elétrica* CBEE, or CBEE, a Federal Government agency set up to supply energy to utilities in the event of future shortages. See Notes 4 and 19 to our consolidated financial statements.



*Operating costs and expenses*

Operating costs and expenses increased 17.7% to R\$5,536 million in 2004 from R\$4,703 million in 2003, principally as a result of an increase in 2004 of regulatory charges, use of basic transmission network, electricity purchased for resale and higher personnel costs.

	2004	% of net operating revenues	2003	% of net operating revenues	2004 versus 2003 - %
Electricity purchased for resale	(1,477)	(19.3)	(1,396)	(23.1)	5.8
Natural gas purchased for resale	(268)	(3.5)	(246)	(4.1)	8.9
Use of basic transmission network	(586)	(7.7)	(310)	(5.1)	89.0
Depreciation and amortization	(677)	(8.8)	(686)	(11.4)	(1.3)
Personnel	(788)	(10.3)	(710)	(11.8)	11.0
Regulatory charges	(861)	(11.2)	(585)	(9.7)	47.2
Third-party services	(329)	(4.3)	(325)	(5.4)	1.2
Employee post-retirement benefits	(153)	(2.0)	(109)	(1.8)	40.4
Materials and supplies	(83)	(1.1)	(88)	(1.5)	(5.7)
Gain on Gasmig Sale	102	1.3			
Other	(407)	(5.3)	(422)	(7.0)	(3.6)
Reversal (Provision) for loss on deferred regulatory assets	(9)	(0.1)	174	2.9	
Total operating costs and expenses	(5,536)	(72.3)	(4,703)	(78.0)	17.7

Electricity purchased for resale consists primarily of purchases from Itaipu through *Centrais Elétricas Brasileiras S.A. - Eletrobrás*. We are required under applicable regulations to purchase 17.0% of Itaipu's capacity at U.S. dollar-denominated prices. We also purchase electricity from the CCEE and Furnas. Electricity purchased for resale increased 5.8% to R\$1,477 million in 2004 from R\$1,396 million in 2003 due primarily to the system services charges recorded in 2004, in the amount of R\$95 million, that are fixed costs which were passed through our rates. See Note 20 to our consolidated financial statements.

Natural gas purchased for resale increased 8.9% to R\$268 million in 2004 compared to R\$246 million in 2003 and consists of purchases made by our subsidiary, Gasmig.

Charges for use of the basic transmission network mainly correspond to the cost of transporting electricity in the Brazilian basic transmission network that are prorated among the Brazilian distribution companies. Charges for use of the basic transmission network are fixed costs that represented a 89.0% increase to R\$586 million in 2004 compared to R\$310 million in 2003 primarily due to increases in the operating costs of new transmission lines of the Brazilian electric system.

Depreciation and amortization expense did not vary significantly, decreasing 1.3% to R\$677 million in 2004 compared to R\$686 million in 2003.

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Personnel expense increased to R\$788 million in 2004 compared to R\$710 million in 2003 primarily as a result of wage increases of 7.0% and 16.2% in November 2004 and 2003, respectively, and the implementation of our Careers and Remuneration Plan in 2004. Additionally, there were provisions related to our Termination Resignation Program in the amount of R\$25 and R\$78 million in 2004 and 2003, respectively.

Regulatory charges increased 47.2% to R\$861 million in 2004 from R\$585 million in 2003 due primarily to the increases of R\$120 and R\$118 million in the Energy Development Account (*Conta de Desenvolvimento Energético*), or CDE, a new charge created to foster energy development in the states and to promote competition regarding energy produced through wind farms, small hydroelectric power plants, biomass, natural gas and coal, and charges for use of water resources, respectively. These expenses are fixed costs. See Note 4 to our consolidated financial statements.

Third-party services expense was R\$329 million in 2004 compared to R\$325 million in 2003. Third-party services expenses consists primarily of contracts related to meter reading, delivery of bills to consumers, collection services and maintenance of distribution and transmission lines.

Employee post-retirement benefits increased 40.4% to R\$153 million in 2004 compared to R\$109 million in 2003 due to a higher projected net periodic cost for 2004 as a result of a higher expected interest expense compared to the expected return on plan assets. See Note 16 to our consolidated financial statements.

We recorded a provision for losses of R\$9 million in 2004 compared to a reversion provision for loss on deferred regulatory assets of R\$174 million in 2003 to reflect our estimation of the recoverability of our deferred regulatory assets. The extraordinary rate adjustment regulatory asset had an initial maximum recovery period of 82 months, which was reduced to 74 months, from January 2002 to February 2008, pursuant to ANEEL's Resolution No. 1 dated January 12, 2004. We made studies to verify if the 74-month recovery period would be sufficient to recover the amounts approved by ANEEL. Based on those studies, we recorded an allowance for losses in the amount of R\$13 million as of December 31, 2004. Therefore, there was an additional allowance, in the amount of R\$9 million, since the original amount recorded, as of December 31, 2003, was R\$4 million. See Notes 2(q) and 4 to our consolidated financial statements.

Other expenses decreased 3.6% to R\$407 million in 2004 from R\$422 million in 2003. The main variations in other expenses in 2004 compared to 2003 were a decrease of R\$25 million in losses on disposal of fixed assets and a decrease of R\$50 million in other provisions for contingencies and doubtful accounts, offset by a provision in 2004 of R\$24 million related to bonuses paid during the rationing period which were not reimbursed from the Federal Government, an increase of R\$9 million in rental expenses and a increase of R\$17 million in employee profit sharing. See Note 20 to our consolidated financial statements.

#### *Operating income*

As a result of the foregoing, we had operating income of R\$2,118 million in 2004 compared to operating income of R\$1,329 million in 2003.

#### *Financial income, net*

Financial income, net, includes (i) financial income, which is mainly comprised of interest and monetary restatement of our account receivable from the State Government, investment income earned, late charges on overdue electricity bills, foreign exchange gains, monetary restatement on deferred regulatory assets, and (ii) financial expense, which is mainly comprised of interest expense on loans and financing, the *Contribuição Provisória sobre a Movimentação ou Transmissão de Valores e de Créditos e Direitos de Natureza Financeira* (a financial transaction tax), or CPMF, foreign exchange losses, monetary restatement losses, monetary restatement of deferred regulatory liabilities and other expenses. We had financial income, net of R\$350 million in 2004 compared to financial income, net of R\$674 million in 2003, principally due to a R\$242 million decrease in foreign exchange revenues resulting from the 8.7% appreciation of the *real* against the U.S. dollar in 2004 compared to an 18.2% appreciation of the *real* against the U.S. dollar in 2003. Additionally, there was a R\$122 million increase in losses from financial instruments due to the swap operations made in 2004 to reduce our exchange rate risk See Notes 3, 4, 14, 21, 23 and 24 to our consolidated financial statements.

#### *Income taxes*

Income taxes were an expense of R\$731 million on pre-tax income of R\$2,468 million in 2004 compared to expenses of R\$607 million on pre-tax income of R\$2,003 million in 2003. Deductions of R\$173 million and R\$85 million in 2004 and 2003, respectively, with respect to interest on capital reduced the amount provisioned for income taxes in 2004 and 2003. See Note 5 to our consolidated financial statements.

*Minority interests*

We had income from minority interests of R\$2 million in 2004, related to our interest in Gasmig.

*Net income*

As a result of the foregoing, we had net income of R\$1,739 million in 2004 compared to net income of R\$1,396 million in 2003.

*Other comprehensive loss*

Other comprehensive loss was R\$474 million in 2004 compared to other comprehensive loss of R\$64 million in 2003 as a result of the higher additional minimum liability recorded in 2004. In 2004, CEMIG made a change in some actuarial assumptions in the annual discount rate and in the mortality rate. The effect of these changes was an increase in our retirement benefit obligation, which was recorded as an other comprehensive loss in 2004.

*Comprehensive income*

As a result of the factors stated above, comprehensive income was R\$1,265 million in 2004 compared to R\$1,332 million in 2003.

**Year Ended December 31, 2003 Compared to Year Ended December 31, 2002***Net operating revenues*

Net operating revenues increased 23.8% to R\$6,032 million in 2003 from R\$4,872 million in 2002 due primarily to higher electricity sales to final customers, deferred rate adjustment and use of basic transmission network, partially offset by a decrease in regulatory extraordinary rate adjustment intended to reimburse us for revenue losses incurred as a result of the Electricity Rationing Plan and a decrease in electricity sales to the interconnected power system.

	2003	% of net operating revenues	2002	% of net operating revenues	2003 versus 2002 - %
Electricity sales to final customers	7,179	119.0	5,458	112.0	31.5
Regulatory extraordinary rate adjustment	63	1.0	281	5.8	(77.6)
Deferred rate adjustment	199	3.3			
Electricity sales to the interconnected power system	56	0.9	161	3.3	(65.2)
Use of basic transmission network	257	4.3	185	3.8	38.9
Other operating revenues	468	7.8	260	5.3	80.0
Tax on revenues	(2,190)	(36.3)	(1,473)	(30.2)	48.7

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Total net operating revenues	6,032	100.00	4,872	100.00	23.8
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Electricity sales to final customers were R\$7,179 million in 2003, representing a 31.5% increase compared to R\$5,458 million in 2002. This resulted primarily from an increase in the average rate and an increase in the volume of electricity sales to final customers. There was a 30.0% increase in the average energy rate in 2003 to R\$197.12 per MWh compared to R\$151.64 per MWh in 2002 as a result of rate increases of 10.5% in April 2002 (full effect in 2003) and 31.5% in April 2003. In addition, there was a 0.9% increase in the volume of our electricity sales to final customers. For 2003 compared to 2002, the volume of electric power sold by us to residential, commercial, rural and other customers increased by 2.7%, 3.6%, 4.6% and 6.3%, respectively, while sales to industrial customers decreased by 0.9%.

In 2003, we recorded R\$63 million in revenue relating to the regulatory extraordinary rate adjustment, a 77.6% decrease compared to the R\$281 million that we recorded in 2002. We recorded revenue relating to the regulatory extraordinary rate adjustment in 2003 and 2002 in accordance with the terms of the General Agreement of the Electricity Sector, which provides for reimbursement of revenue losses incurred during the period of the



Electricity Rationing Plan and related spot market transactions through special rate increases to be billed to final customers, and in accordance with consensus described in Emerging Issues Task Force Issue No. 92-07, Accounting by Rate-Regulated Utilities for the Effects of Certain Alternative Revenue Programs, which establishes a 24-month limit for the recovery of revenue losses incurred during the Energy Rationing Plan. See Note 4 to our consolidated financial statements.

In 2003, we recorded R\$199 million in revenue relating to the deferred rate adjustment. ANEEL Resolution No. 71, dated April 4, 2004, disclosed the results of CEMIG's periodic rate review. According to this resolution, the rate adjustment that would have to be applied on CEMIG's rates starting April 8, 2003 was 37.9%, instead of the 31.5% applied. The difference will be included by ANEEL in future rate adjustments.

Electricity sales to the interconnected power system were R\$56 million in 2003, a 65.2% decrease compared to R\$161 million in 2002. This decrease resulted primarily from higher spot market rates associated with energy transactions on the CCEE in the prior year.

Revenues from use of the basic transmission network by other concessionaires increased 38.9% to R\$257 million in 2003 from R\$185 million in 2002 due to rate increases in July 2002 (full effect in 2003) and July 2003.

Other operating revenues increased 80.0% to R\$468 million in 2003 from R\$260 million in 2002 due primarily to an R\$167 million increase in revenues from Gasmig, our subsidiary, reflecting 83.5% period-over-period growth, and an increase of R\$28 million in revenue from Empresa de Infovias S.A. as a result of telecommunication services rendered in 2003.

Taxes on revenues increased 48.7% to R\$2,190 million in 2003 from R\$1,473 million in 2002 as a result of the 31.5% increase in our electricity sales to final customers in 2003 as compared to 2002 and as a result of the VAT billed to customers in connection with the extraordinary rate adjustment. Taxes on revenues consist of: (i) VAT, assessed at an average rate of 21% on electricity sales to final customers, and VAT billed to customers related to the deferred regulatory assets; (ii) COFINS, assessed at a rate of 3%; (iii) PASEP, assessed at a rate of 1.65%; and (iv) the *Encargo de Capacidade Emergencial* (Emergency Capacity Charge), a charge established in 2002 that is prorated among final consumers of electric energy and relates to the *Comercializadora Brasileira de Energia Elétrica* CBEE, or CBEE, a Federal Government agency set up to supply energy to utilities in the event of future shortages. See Notes 4 and 19 to our consolidated financial statements.

#### *Operating costs and expenses*

Operating costs and expenses increased 8.2% to R\$4,703 million in 2003 from R\$4,345 million in 2002, principally as a result of an increase in 2003 of electricity purchased for resale and higher personnel costs, partially offset by a reversion provision recognized in 2002 related to loss on deferred regulatory assets.

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	2003	% of net operating revenues	2002	% of net operating revenues	2003 versus 2002 - %
Electricity purchased for resale	(1,396)	(23.1)	(1,333)	(27.4)	4.7
Natural gas purchased for resale	(246)	(4.1)	(152)	(3.1)	61.8
Use of basic transmission network	(310)	(5.1)	(298)	(6.1)	4.0
Depreciation and amortization	(686)	(11.4)	(666)	(13.7)	3.0
Personnel	(710)	(11.8)	(532)	(10.9)	33.5
Regulatory charges	(585)	(9.7)	(548)	(11.2)	6.8
Third-party services	(325)	(5.4)	(265)	(5.4)	22.6
Employee post-retirement benefits	(109)	(1.8)	(207)	(4.3)	(47.3)
Materials and supplies	(88)	(1.5)	(78)	(1.6)	12.8
Other	(422)	(7.0)	(238)	(4.9)	77.3
Reversal (Provision) for loss on deferred regulatory assets	174	2.9	(28)	(0.6)	
Total operating costs and expenses	(4,703)	(78.0)	(4,345)	(89.2)	8.2

Electricity purchased for resale consists primarily of purchases from Itaipu through *Centrais Elétricas Brasileiras S.A. - Eletrobrás*. We are required under applicable regulations to purchase 17.0% of Itaipu's capacity at U.S. dollar-denominated prices. We also purchase electricity from the CCEE and Furnas. Electricity purchased for resale increased 4.7% to R\$1,396 million in 2003 from R\$1,333 million in 2002 due mainly to a 20.0% increase in purchases from Itaipu to R\$1,175 million in 2003 compared to R\$979 million in 2002, partially offset by a 73.2% decrease in energy purchased from the CCEE, considering the higher spot market rates associated with energy transactions on the CCEE in the prior year. See Note 20 to our consolidated financial statements.

Natural gas purchased for resale increased 61.8% to R\$246 million in 2003 compared to R\$152 million in 2002 and consists of purchases made by our subsidiary, Gasmig. The increase in natural gas purchased for resale is the result of increases in the natural gas price, and a 12.2% increase in the volume of gas sold by Gasmig in 2003.

Charges for use of the basic transmission network mainly correspond to the cost of transporting electricity purchased from Itaipu and other concessionaires. Charges for use of the basic transmission network represented a 4.0% increase to R\$310 million in 2003 compared to R\$298 million in 2002 principally as a result of rate increases in July of 2002 and 2003.

Depreciation and amortization increased 3.0% to R\$686 million in 2003 from R\$666 million in 2002 as a result primarily of the entry into service of additional distribution and transmission networks and lines.

Personnel expense increased to R\$710 million in 2003 compared to R\$532 million in 2002 primarily as a result of wage increases of 16.2% and 11.5% in November 2003 and 2002, respectively, and a provision relating to our Termination Resignation Program in the amount of R\$78 million.

Regulatory charges increased 6.8% to R\$585 million in 2003 from R\$548 million in 2002 due primarily to R\$118 million related to the CDE, partially offset by a R\$63 million decrease in Fuel Usage Quota Account charges in 2003 to R\$282 million from R\$345 million in 2002 as a result of decreased operations of thermal generation plants in 2003. See Note 20 to our consolidated financial statements.

Third-party services expense increased 22.6% to R\$325 million in 2003 compared to R\$265 million in 2002. This increase resulted mainly from an increase in the prices for service contracts relating to meter reading, delivery of bills to consumers and collection services.

Employee post-retirement benefits decreased 47.3% to R\$109 million in 2003 compared to R\$207 million in 2002 due to a lower projected net periodic cost for 2003 as a result of a higher expected return on plan assets. See Note 16 to our consolidated financial statements.

We recorded a reversion provision for loss on deferred regulatory assets of R\$174 million in 2003 compared to a provision of R\$28 million in 2002 to reflect our estimation of the recoverability of our deferred regulatory assets. The extraordinary rate adjustment regulatory asset had an initial maximum recovery period of 82 months, which was reduced to 74 months, from January 2002 to February 2008, pursuant to ANEEL's Resolution No. 1 dated January 12, 2004. We made studies to verify if the 74-month recovery period would be sufficient to recover the amounts approved by ANEEL. Based on those studies, we recorded an allowance for losses in the amount of R\$4 million as of December 31, 2003. Therefore, there was a reversal of the allowance, in the amount of R\$174 million, since the original amount recorded, as of December 31, 2002, was R\$178 million. See Notes 2(q) and 4 to our consolidated financial statements.

Other expenses increased 77.3% to R\$422 million in 2003 from R\$238 million in 2002 due principally to an increase of R\$55 million in employees profit sharing, considering our better financial performance in 2003, and an increase of R\$44 million in provision for doubtful accounts to R\$57 million in 2003 compared to R\$13 million in 2002, and, to a lesser extent, to increases in our losses on disposal of fixed assets and expenses related to other taxes and rentals. See Note 20 to our consolidated financial statements.

#### *Operating income*

As a result of the foregoing, we had operating income of R\$1,329 million in 2003 compared to operating income of R\$527 million in 2002.

#### *Financial income (expense), net*

Financial income (expense), net, includes (i) financial income, which is mainly comprised of interest and monetary restatement of our account receivable from the State Government, investment income earned, late charges on overdue electricity bills, foreign exchange gains, monetary restatement on deferred regulatory assets, and (ii) financial expense, which is mainly comprised of interest expense on loans and financing, the *Contribuição Provisória sobre a Movimentação ou Transmissão de Valores e de Créditos e Direitos de Natureza Financeira* (a financial transaction tax), or CPMF, foreign exchange losses, monetary restatement losses, monetary restatement of deferred regulatory liabilities and other expenses. We had financial revenues, net of R\$674 million in 2003 compared to financial expenses, net of R\$525 million in 2002, principally due to a R\$321 million increase in foreign exchange revenues and a decrease of R\$800 million in foreign exchange losses, resulting from the 18.2% appreciation of the *real* against the U.S. dollar in 2003 compared to an 52.3% devaluation of the *real* against the U.S. dollar in 2002. Additionally, there was a R\$330 million increase in monetary restatement on deferred regulatory assets and reclassification adjustment on marketable securities gains of R\$76 million from the sale of *Notas do Tesouro Nacional* (Brazilian National Treasury Notes) offset by a R\$158 million decrease in income from temporary cash investments due to lower cash and cash equivalents and restricted investments in 2003 and income from cash investments denominated in U.S. dollars, losses on financial instruments, net of R\$44 million and a R\$139 million decrease in interest and monetary restatement of an account receivable from the State Government due to lower variation of IGP-DI, index of the contract. See Notes 3, 4, 14, 21, 23 and 24 to our consolidated financial statements.

#### *Income taxes*

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Income taxes were an expense of R\$607 million on pre-tax income of R\$2,003 million in 2003 compared to expenses of R\$26 million on pre-tax income of R\$2 million in 2002. Deductions of R\$85 million and R\$73 million in 2003 and 2002, respectively, with respect to interest on capital reduced the amount provisioned for income taxes in 2003. See Note 5 to our consolidated financial statements.

*Minority interests*

Minority interests were income of R\$12 million in 2002, related to the operation of Empresa de Infovias S.A.

*Net income (loss)*

As a result of the foregoing, we had net income of R\$1,396 million in 2003 compared to net loss of R\$12 million in 2002.

*Other comprehensive income (loss)*

Other comprehensive loss was R\$64 million in 2003 compared to other comprehensive income of R\$242 million in 2002 as a result of the additional minimum liability recorded and the reclassification adjustment resulting from the sale of the available for sale securities.

*Comprehensive income*

As a result of the factors stated above, comprehensive income was R\$1,332 million in 2003 compared to R\$230 million in 2002.

**Liquidity and Capital Resources**

Our business is capital intensive. Historically, we have required capital to finance the construction of new generation facilities and the expansion and modernization of existing generation, transmission and distribution facilities. Our liquidity requirements are also affected by our dividend policy. See Item 8. Financial Information Dividend Policy and Payments. We have funded our liquidity and capital requirements primarily with cash provided by operations and, to a lesser extent, with proceeds of financings. We believe that our current cash reserves, cash provided by operations and anticipated proceeds from financings will be sufficient during the next 12 months to meet our liquidity requirements.

*Cash and cash equivalents*

Cash and cash equivalents as of December 31, 2004 were R\$874 million compared to R\$440 million as of December 31, 2003 and R\$123 million as of December 31, 2002. None of our cash or cash equivalents was held in currencies other than *reais* as of December 31, 2004.

*Cash flow from operating activities*

Net cash provided by operating activities in 2004, 2003 and 2002 totaled R\$1,538 million, R\$658 million and R\$732 million, respectively. The increase in cash provided by operating activities in 2004 compared to 2003 was due primarily to financial settlement of the CCEE transactions in 2003. The same reason justified the decrease in cash provided by operating activities in 2003 compared to 2002. Significant non-cash items affecting earnings included increased depreciation and amortization expense as a result of our on-going capital improvements projects, recognition of deferred regulatory assets, the effects of monetary variation and exchange rate variations and the provision for loss on the receivable under the CRC Account Agreement.

*Cash flow from investing activities*

Net cash used in investing activities during 2004, 2003 and 2002 amounted to R\$917 million, R\$852 million and R\$546 million, respectively, principally relating to the acquisition of property, plant and equipment and the modernization of existing generation, transmission and distribution facilities. Capital expenditures from the acquisition of property, plant and equipment amounted to R\$1,061 million, R\$1,029 million and R\$869 million in 2004, 2003 and 2002, respectively. New investments in other affiliates also impacted net cash use in investing activities. Such investments amounted to R\$10 million, R\$4 million and R\$103 million in 2004, 2003 and 2002,

respectively. See Item 4. Information on the Company Capital Expenditures for more detail regarding how these capital expenditures were applied by us.

*Cash flow from financing activities*

Net cash used in financing activities during 2004 was R\$187 million, comprised of R\$1,230 million and R\$316 million in proceeds from long-term financing and short-term loans, respectively, offset by the repayment of R\$1,424 million of real- and foreign currency-denominated long-term financing and the payment of R\$309 million in dividends and interest on capital.

Net cash provided by financing activities during 2003 was R\$511 million, comprised of R\$717 million and R\$820 million in proceeds from long-term financing and short-term loans, respectively, offset by the repayment of R\$826 million of real- and foreign currency-denominated long-term financing and the payment of R\$200 million in dividends and interest on capital.

Net cash used in financing activities during 2002 was R\$281 million, comprised of the repayment of R\$597 million of real- and foreign currency-denominated long-term financing and the payment of R\$214 million in dividends and interest on capital, offset by R\$518 million in proceeds from long-term financing, including U.S. dollar-denominated long-term loans, and an advance for future capital increase made by minority shareholders of R\$12 million.

Our indebtedness as of December 31, 2004 was R\$4,167 million, composed of R\$2,750 million of long-term debt and R\$1,417 million of the current portion of long-term debt. This compares with indebtedness as of December 31, 2003 of R\$ 3,991 million, composed of R\$2,331 million of long-term debt and R\$1,660 million current portion of long-term debt. Of our long-term debt (including the current portion) at December 31, 2004, R\$1,119 million was denominated in foreign currencies (R\$857 million of which was U.S. dollar-denominated) and R\$3,048 million was denominated in *reais*. Of our total indebtedness of R\$4,167 million as of December 31, 2004, R\$3,369 million is subject to variable interest rates. See Notes 14 and 23 to our consolidated financial statements.

We are subject to financial covenants contained in some of our debt agreements that require us to maintain certain financial ratios. These ratios are computed based on our financial statements prepared in accordance with accounting practices adopted in Brazil. These and other covenants could limit our ability to support our liquidity and capital requirements.

We are currently not in compliance with certain financial covenants of a debt agreement between Empresa de Infovias S.A. and MBK Furukawa Sistemas S.A./Unibanco in the total principal amount of R\$58.0 million as of December 31, 2004, of which R\$40.8 million is classified as long-term liabilities in our consolidated financial statements. These covenants are based on the financial statements prepared in accordance with the accounting practices adopted in Brazil. However, Empresa de Infovias S.A. has obtained a waiver from the creditors party to the contract for non-compliance with those covenants. The waiver affirms that such creditors will not exercise their rights to demand either accelerated or immediate payment of the total amount due until December 31, 2005. We cannot assure you that we will be able to renew this waiver in which case the relevant creditors would be able to accelerate payment. This would result in the cross-acceleration of other indebtedness of CEMIG due to cross-default provisions in its other debt agreements. See Note 14 to our consolidated financial statements and Item 13. Defaults, Dividend Arrearages and Delinquencies.



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On December 31, 2004, our total debt was R\$4,167 million, of which R\$1,417 million matures in 2005. Of our total debt, R\$1,119 million was contracted in foreign currency, of which R\$342 million matures in 2005. Due to these maturities in 2005, we need funds in the short term to pay and refinance these obligations. For this reason, we are refinancing our debt in 2005 to lengthen maturities. We plan to raise approximately R\$1.5 billion in 2005, which will be used to repay debt. We cannot assure you that we will successfully consummate this refinancing.

In addition to the financings described in our financial statements, we have credit lines with financial institutions as of December 31, 2004 in the amount of R\$94 million which we have not yet used.

On July 19, 2004, we set up a Local Note Program, or the Program, according to Instrução CVM No. 400, dated December 29, 2003. The Program is expected to last two years from the date of the filing with the Comissão de Valores Mobiliários - CVM. Initially, under the Program we were permitted to issue debentures in an amount of up to R\$1.5 billion. We currently have R\$230.4 million outstanding under the Program. Because of the unbundling, we cannot issue additional debentures under the Program. We may in the future establish other local note programs directly or through our subsidiaries.

As a state-controlled company, we are subject to restrictions under current financing laws and regulations in Brazil on our ability to obtain financing in certain situations. For example, we must obtain approval from the Brazilian Ministry of Finance and the Central Bank prior to certain international financial transactions and such approval is typically granted only if the purpose of the transaction is to finance the import of goods or to roll over our external debt. In addition, financial institutions in Brazil are subject to risk exposure restrictions with regard to state governments, governmental agencies and state-controlled companies such as us. The restrictions mentioned in this paragraph have not prevented us from obtaining financing, although there is no assurance that our ability to obtain financing will not be hindered in the future. See Item 3. Key Information Risk Factors Risks Relating to Brazil We currently face limitations on our ability to obtain financing.

We currently plan to make capital expenditures aggregating approximately R\$1,988 million in 2005. The principal uses of these expenditures are expected to be for expansion of our distribution infrastructure and increases in our generation capacity. In 2004, we funded our capital expenditures and met our liquidity requirements through a combination of cash flow from operations and financings. We expect that we will fund our proposed capital expenditures and meet our other liquidity requirements in 2005 through a combination of cash flow from operations and financings. Because we rely primarily on cash generated from operations to fund our liquidity and capital requirements, factors that cause our revenues and net income to increase or decrease could have a corresponding effect on our access to sources of liquidity.

Over the long term, we anticipate that it will be necessary to make significant capital expenditures in connection with the maintenance and upgrading of our generation, transmission and distribution facilities, and we expect to employ a variety of liquidity sources, such as cash flow from operations and financings, in connection with such requirements. See Item 3. Key Information Risk Factors for a discussion of certain matters that might adversely affect our liquidity position.

#### **Off-Balance Sheet Arrangements**

We do not have any off-balance sheet arrangements.

#### **Tabular Disclosure of Contractual Obligations**

We have outstanding contractual obligations and commitments which include principal debt payment provisions, the obligation to purchase electricity for resale from Itaipu, the obligation to transfer and transport electric power from Itaipu as well as construction commitments. The following table provides information, as of December 31, 2004, about our contractual obligations and commitments in millions of *reais*.



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	Total	Less than 1 year	1-3 years	3-5 years	More than 5 years
Total debt(1)	4,167	1,417	1,322	873	555
Purchase obligations					
Purchase of electricity from Itaipu for resale(2)	8,619	1,024	2,048	2,048	3,499
Energy auction on CCEE	6,478	267	1,618	1,621	2,972
Transfer and transport electric power from Itaipu(2)	505	60	120	120	205
Investments					
Aimorés hydroelectric power plant(3)	66	66			
Irapé hydroelectric power plant(3)	287	271	16		
Funil hydroelectric power plant(3)	11	11			
Queimado hydroelectric power plant(3)	20	20			
Pai Joaquim hydroelectric power plant(3)	10	10			
Cemig Capim Branco Energia(3)	39	22	17		
Transmission Lines(3)	46	35	11		
Gasmig	75	5	64	6	
Empresa de Infovias S.A.	48	48			
Other long-term obligations					
Pension plan contributions	1,555	112	237	186	1,020