CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2009

Consolidated Financial Statements
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Contents | **Page**

Auditors' Report	**1**
Consolidated Balance Sheets	**2**
Consolidated Statements of Income	**3**
Consolidated Statements of Retained Earnings	**3**
Consolidated Statements of Cash Flows	**4**
Notes to Consolidated Financial Statements	**5**

AUDITORS' REPORT

To the Shareholder of
Toronto Hydro Corporation

We have audited the consolidated balance sheets of **Toronto Hydro Corporation** [the "Corporation"] as at December 31, 2009 and 2008 and the consolidated statements of income, retained earnings and cash flows for the years then ended. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Corporation as at December 31, 2009 and 2008 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Ernst & Young LLP

Chartered Accountants
Licensed Public Accountants

Toronto, Canada,
February 26, 2010 [except as to note 30[d], which is as of March 5, 2010].

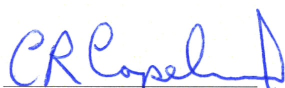
toronto hydro corporation

CONSOLIDATED BALANCE SHEETS

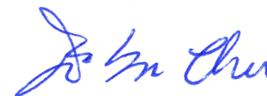
[in thousands of dollars]

As at December 31	2009 $	2008 $
ASSETS		
Current		
Cash and cash equivalents	**211,370**	340,492
Accounts receivable, net of allowance for doubtful accounts *[note 19[b]]*	**150,281**	131,582
Unbilled revenue *[note 19[b]]*	**295,647**	266,061
Payments in lieu of corporate taxes receivable	**15,932**	24,006
Inventories *[note 5]*	**6,224**	5,069
Prepaid expenses	**3,331**	2,503
Assets from discontinued operations *[note 27]*	**514**	-
Total current assets	**683,299**	769,713
Property, plant and equipment, net *[note 6]*	**1,919,954**	1,853,606
Intangible assets, net *[note 7]*	**73,829**	66,701
Investments *[note 8]*	**47,930**	52,908
Regulatory assets *[note 9]*	**68,193**	26,213
Other assets *[note 10]*	**7,615**	7,862
Future income tax assets *[note 21]*	**253,149**	2,809
Assets held for sale *[note 11]*	**5,258**	-
Total assets	**3,059,227**	2,779,812
LIABILITIES AND SHAREHOLDER'S EQUITY		
Current		
Accounts payable and accrued liabilities *[note 19[b]]*	**316,768**	294,839
Current portion of other liabilities *[note 13]*	**18,001**	17,382
Deferred revenue	**421**	3,274
Current portion of promissory note payable *[note 14]*	**-**	245,058
Liabilities from discontinued operations *[note 27]*	**1,549**	890
Total current liabilities	**336,739**	561,443
Long-term liabilities		
Debentures *[note 14]*	**720,475**	471,521
Promissory note payable *[note 14]*	**490,115**	490,115
Post-employment benefits *[note 15]*	**161,348**	152,771
Regulatory liabilities *[note 9]*	**308,575**	83,516
Other liabilities *[note 16]*	**1,473**	2,230
Asset retirement obligations *[note 17]*	**7,552**	6,528
Customers' advance deposits	**34,696**	30,283
Future income tax liabilities *[note 21]*	**-**	114
Total long-term liabilities	**1,724,234**	1,237,078
Total liabilities	**2,060,973**	1,798,521
Commitments and contingencies *[notes 24, 25 and 30]*		
Shareholder's equity		
Share capital *[note 22]*	**567,817**	567,817
Retained earnings	**430,437**	413,474
Total shareholder's equity	**998,254**	981,291
Total liabilities and shareholder's equity	**3,059,227**	2,779,812

ON BEHALF OF THE BOARD:



Clare R. Copeland, Director



Brian Chu, Director

The accompanying notes are an integral part of the consolidated financial statements.

toronto hydro corporation

CONSOLIDATED STATEMENTS OF INCOME

[in thousands of dollars, except for per share amounts]

Year ended December 31	**2009** **$**	**2008** **$**
Revenues	**2,461,671**	2,380,084
Costs		
Purchased power and other	**1,953,657**	1,884,296
Operating expenses	**210,889**	203,429
Depreciation and amortization	**162,970**	156,159
	2,327,516	2,243,884
Income before interest, change in fair value of investments and provision for payments in lieu of corporate taxes	**134,155**	136,200
Interest income	**3,207**	12,328
Interest expense		
Long-term debt	**(73,061)**	(71,542)
Other interest	**(697)**	(3,212)
Change in fair value of investments *[note 8]*	**(1,049)**	(22,033)
Income before provision for payments in lieu of corporate taxes	**62,555**	51,741
Provision for payments in lieu of corporate taxes *[note 21]*	**19,742**	5,745
Income from continuing operations	**42,813**	45,996
Income (loss) from discontinued operations - net of tax *[note 27]*	**(680)**	123,016
Net income	**42,133**	169,012
Basic and fully diluted net income per share from continuing operations *[note 26]*	**42,813**	45,996
Basic and fully diluted net income (loss) per share from discontinued operations *[note 26]*	**(680)**	123,016
Basic and fully diluted net income per share	**42,133**	169,012

CONSOLIDATED STATEMENTS OF RETAINED EARNINGS

[in thousands of dollars]

Year ended December 31	**2009** **$**	**2008** **$**
Retained earnings, beginning of year	**413,474**	360,878
Net income	**42,133**	169,012
Dividends *[note 22]*	**(25,170)**	(116,416)
Retained earnings, end of year	**430,437**	413,474

The accompanying notes are an integral part of the consolidated financial statements.

toronto hydro corporation

CONSOLIDATED STATEMENTS OF CASH FLOWS

[in thousands of dollars]

Year ended December 31	**2009** **$**	**2008** $
OPERATING ACTIVITIES		
Income from continuing operations	**42,813**	45,996
Adjustments for non-cash items		
Depreciation and amortization	**162,970**	156,159
Change in fair value of investments *[note 8]*	**1,049**	22,033
Net change in other assets and liabilities	**(972)**	(225)
Payments in lieu of corporate taxes	**8,074**	(1,826)
Post-employment benefits	**8,577**	8,719
Future income taxes *[note 21]*	**416**	1,864
Changes in non-cash working capital balances		
Decrease (increase) in accounts receivable	**(19,061)**	18,514
Decrease (increase) in unbilled revenue	**(29,586)**	10,290
Increase in inventories	**(1,155)**	(523)
Increase in prepaid expenses	**(904)**	(1,047)
Increase in accounts payable and accrued liabilities	**23,016**	7,941
Decrease in deferred revenue	**(2,786)**	(1,429)
Net cash provided by operating activities	**192,451**	266,466
INVESTING ACTIVITIES		
Purchase of property, plant and equipment	**(218,149)**	(188,792)
Purchase of intangible assets	**(31,156)**	(25,789)
Accumulated cash received from conduit trusts *[note 8]*	**3,929**	-
Net change in regulatory assets and liabilities	**(58,743)**	16,717
Net cash used in investing activities	**(304,119)**	(197,864)
FINANCING ACTIVITIES		
Decrease in promissory note payable	**(245,058)**	-
Dividends paid *[note 22]*	**(25,170)**	(116,416)
Proceeds from debentures	**248,399**	-
Increase in customers' advance deposits	**5,013**	3,694
Net cash used in financing activities	**(16,816)**	(112,722)
Net cash used in continuing operations	**(128,484)**	(44,120)
Net cash provided by (used in) discontinued operations *[note 27]*	**(638)**	168,610
Net increase (decrease) in cash and cash equivalents during the year	**(129,122)**	124,490
Cash and cash equivalents, beginning of year	**340,492**	216,002
Cash and cash equivalents, end of year	**211,370**	340,492
Supplementary cash flow information		
Total interest paid	**72,714**	72,606
Payments in lieu of corporate taxes	**14,803**	33,751

The accompanying notes are an integral part of the consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
[all tabular amounts in thousands of dollars]

December 31, 2009

1. INCORPORATION

On June 23, 1999, Toronto Hydro Corporation [the "Corporation"] was incorporated under the Business Corporations Act (Ontario) [the "BCA"] along with two wholly-owned subsidiary companies, Toronto Hydro-Electric System Limited ["LDC"] and Toronto Hydro Energy Services Inc. ["TH Energy"]. The incorporation was required in accordance with the provincial government's *Electricity Act, 1998*.

Under the terms of By-law No. 374-1999 of the City of Toronto ["Transfer By-law"] made under section 145 of the *Electricity Act, 1998* and in accordance with continuity of interest accounting, the former Toronto Hydro-Electric Commission and the City of Toronto [the "City"] transferred, at book value, their assets and liabilities (effective July 1, 1999) associated with:

[a] electricity distribution to LDC in consideration for the issuance of equity securities of LDC and long-term notes payable to the City; and

[b] electricity generation, co-generation and energy services to TH Energy in consideration for the issuance of equity securities of TH Energy.

The equity securities of LDC and TH Energy were subsequently transferred by the City to the Corporation in consideration for the issuance of equity securities of the Corporation to the City.

The book value of the assets transferred at July 1, 1999 was $1,548,048,000. The principal amount of the long-term notes payable to the City was $980,231,000 and the value of the common shares of the Corporation received by the City was $567,817,000.

The Corporation supervises the operations of, and provides corporate and management services and strategic direction to two principal subsidiaries (each of which is listed below, incorporated under the BCA and wholly-owned, directly or indirectly, by the Corporation):

[a] LDC (incorporated June 23, 1999) – which distributes electricity to customers located in the City and is subjected to rate regulation. LDC is also engaged in the delivery of Conservation and Demand Management ["CDM"] activities; and

[b] TH Energy (incorporated June 23, 1999) – which owns and operates street lighting and expressway lighting assets located in the City.

The principal business of the Corporation is the regulated distribution of electricity by LDC.

2. REGULATION

In April 1999, the government of Ontario initiated a restructuring of Ontario's electricity industry. The restructuring was intended, among other things, to facilitate competition in the generation and sale of electricity, to protect the interests of consumers with respect to prices and the reliability and quality of electricity service and to promote economic efficiency in the generation, transmission and distribution of electricity.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
[all tabular amounts in thousands of dollars]

December 31, 2009

The Ontario Energy Board [the "OEB"] has regulatory oversight of electricity matters in the Province of Ontario. The *Ontario Energy Board Act, 1998* sets out the OEB's authority to issue a distribution licence which must be obtained by owners or operators of a distribution system in Ontario. The OEB prescribes licence requirements and conditions including, among other things, specified accounting records, regulatory accounting principles, separation of accounts for separate businesses and filing process requirements for rate-setting purposes.

The OEB's authority and responsibilities include the power to approve and fix rates for the transmission and distribution of electricity, the power to provide continued rate protection for rural and remote electricity customers and the responsibility for ensuring that electricity distribution companies fulfill obligations to connect and service customers.

The continuing restructuring of Ontario's electricity industry and other regulatory developments, including current and possible future consultations between the OEB and interested stakeholders, may affect the distribution rates and other permitted recoveries in the future.

LDC is required to charge its customers for the following amounts (all of which, other than the distribution rate, represent a pass through of amounts payable to third parties):

[i] *Distribution Rate*. The distribution rate is designed to recover the costs incurred by LDC in delivering electricity to customers and the OEB-allowed rate of return. Distribution rates are regulated by the OEB and typically comprise a fixed charge and a usage-based (consumption) charge.

The volume of electricity consumed by LDC's customers during any period is governed by events largely outside LDC's control (principally sustained periods of hot or cold weather which increase the consumption of electricity and sustained periods of moderate weather which decrease the consumption of electricity).

[ii] *Electricity Price and Related Regulated Adjustments*. The electricity price and related regulated adjustments represent a pass through of the commodity cost of electricity.

[iii] *Retail Transmission Rate*. The retail transmission rate represents a pass through of wholesale costs incurred by distributors in respect of the transmission of electricity from generating stations to local areas. Retail transmission rates are regulated by the OEB.

[iv] *Wholesale Market Service Charge*. The wholesale market service charge represents a pass through of various wholesale market support costs. Retail rates for the recovery of wholesale market service charges are regulated by the OEB.

3. ELECTRICITY DISTRIBUTION RATES

On May 15, 2008, the OEB issued its decision regarding LDC's electricity distribution rates application for 2008 and 2009. In its decision, the OEB approved LDC's 2008 base distribution revenue requirement and rate base of $473,000,000 and $1,968,900,000, respectively. As part of the decision, the deemed debt to equity structure of LDC was modified to 62.5% debt and 37.5% equity for 2008 and to 60.0% debt and 40.0% equity for 2009 and thereafter.

In its decision on LDC's electricity distribution rates for 2008 and 2009, the OEB ordered that 100% of the net after-tax gains on the sale of certain LDC properties should be deducted from the revenue requirement recovered through

distribution rates. The OEB deemed this amount to be $10,300,000 [the "deemed amount"]. On June 16, 2008, LDC filed an appeal with the Divisional Court of Ontario [the "Divisional Court"] seeking to overturn the gain on sale aspects of the OEB decision and also sought and obtained a stay order with respect to the deduction of the deemed amount from the revenue requirement recovered through rates. On April 30, 2009, the Divisional Court denied the appeal by LDC. LDC filed a motion with the Court of Appeal for leave to appeal that decision of the Divisional Court. The requested leave was denied on September 14, 2009.

LDC filed a notice of clarification with the OEB with respect to the timing and the quantum of the expected reduction in distribution revenue. LDC's position is that the reduction in distribution revenue should be done after the deemed properties are sold and for the related actual net after-tax gain. In the event the OEB does not concur with LDC's position and orders an immediate reduction in distribution revenue, the Corporation would have to reduce its distribution revenue by the deemed amount less the net after-tax gain of the deemed properties already sold. At December 31, 2009, the reduction in distribution revenue would be approximately $8,100,000. Further to the notice of clarification filed by LDC in the fourth quarter of 2009, the OEB indicated that it intends to provide a final ruling on this issue as part of LDC's electricity distribution rates decision for 2010.

On February 24, 2009, the OEB issued the allowed return on equity ["ROE"] for LDC for the 2009 rate year. The percentage was set at 8.01%. In addition to the ROE, the OEB also set LDC's 2009 distribution revenue requirement and rate base at $482,500,000 and $2,035,000,000, respectively.

On August 28, 2009, LDC filed a rate application with the OEB seeking approval of the distribution revenue requirement and corresponding rates for the rate year May 1, 2010.

On December 11, 2009, the OEB issued revised cost of capital guidelines which would set the initial allowed ROE for LDC for 2010 at 9.75%. The ROE formula will be adjusted to reflect the forecast long Canada Bond Yield and A-rated Canadian Utility bonds spreads when this data is released by the OEB on or about the beginning of March 2010. LDC will adjust its distribution rates to reflect the new guidelines as part of its rate finalization process for 2010 distribution rates.

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements of the Corporation have been prepared in accordance with Canadian generally accepted accounting principles ["GAAP"], including accounting principles prescribed by the OEB in the handbook "Accounting Procedures Handbook for Electric Distribution Utilities" ["AP Handbook"], and reflect the significant accounting policies summarized below:

a) Basis of consolidation

The consolidated financial statements include the accounts of the Corporation and its wholly-owned subsidiaries. All significant intercompany balances and transactions have been eliminated.

b) Regulation

The following regulatory treatments have resulted in accounting treatments which differ from Canadian GAAP for enterprises operating in an unregulated environment:

Regulatory Assets and Liabilities

Effective January 1, 2009, the Corporation adopted amended Canadian Institute of Chartered Accountants ["CICA"] Handbook Section 1100 – "Generally Accepted Accounting Principles" ["Handbook Section 1100"], Handbook Section 3465 – "Income Taxes" ["Handbook Section 3465"], and Accounting Guideline 19 "Disclosures by Entities Subject to Rate Regulation". These amended sections and guidance established new standards and removed a temporary exemption in Handbook Section 1100 pertaining to the application of that section to the recognition and measurement of assets and liabilities arising from rate regulation. The new standards require the recognition of future income tax liabilities and assets in accordance with Handbook Section 3465 as well as a separate regulatory asset or liability balance for the amount of future income taxes expected to be included in future rates and recovered from or paid to customers, and retain existing requirements to disclose the effects of rate regulation. The revised standards are effective for interim and annual financial statements for the fiscal years beginning on or after January 1, 2009.

Following the removal of the temporary exemption for rate-regulated operations included in Handbook Section 1100, the Corporation developed accounting policies for its assets and liabilities arising from rate regulation using professional judgment and other sources issued by bodies authorized to issue accounting standards in other jurisdictions. Upon final assessment and in accordance with Handbook Section 1100, the Corporation has determined that its assets and liabilities arising from rate-regulated activities qualify for recognition under Canadian GAAP and this recognition is consistent with U.S. Financial Accounting Standards Board Accounting Standards Codification 980 – "Regulated Operations". Accordingly, the removal of the temporary exemption had no effect on the Corporation's results of operations as of December 31, 2009.

Handbook Section 3465 as amended requires the recognition of future income tax assets and liabilities and related regulatory liabilities and assets for the amount of future income taxes expected to be refunded to, or recovered from, customers in future electricity rates, applied on a retrospective basis without prior period restatement. The implementation of these standards did not impact the Corporation's earnings or cash flows. As at December 31, 2009, LDC has recorded a future income tax asset of $250,948,000, and a corresponding regulatory liability of $250,948,000 *[note 9]*.

Payments in lieu of corporate taxes ["PILs"]

The Corporation and its subsidiaries are exempt from tax under the *Income Tax Act* (Canada) ["ITA"], the *Corporations Tax Act* (Ontario) and the *Taxation Act, 2007* (Ontario), if not less than 90% of the capital of the Corporation is owned by the City and not more than 10% of the income of the Corporation and each of its subsidiaries is derived from activities carried on outside the municipal geographical boundaries of the City.

The Corporation and each of its subsidiaries is a Municipal Electricity Utility ["MEU"] for purposes of the PILs regime contained in the *Electricity Act, 1998*. The *Electricity Act, 1998* provides that a MEU that is exempt from tax under the ITA, the *Corporations Tax Act* (Ontario) and the *Taxation Act, 2007* (Ontario) is required to make, for each taxation year, a PILs to the Ontario Electricity Financial Corporation in an amount equal to the tax that it would be liable to pay under the ITA and the *Taxation Act, 2007* (Ontario) (for years ending after 2008) or the *Corporations Tax Act* (Ontario) (for years ending prior to 2009) if it were not exempt from tax.

The PILs regime came into effect on October 1, 2001, at which time the Corporation and each of its subsidiaries were deemed to have commenced a new taxation year for purposes of determining the respective liabilities for PILs.

The differences between the financial statement carrying value and tax basis of assets and liabilities were accounted for by the Corporation as follows:

[a] in the case of the Corporation's unregulated businesses, the liability method of accounting was applied in accordance with recommendations of the CICA; and

[b] in the case of the Corporation's regulated electricity distribution business, until December 31, 2008, the taxes payable method of accounting was applied. Effective January 1, 2009, the Corporation's regulated business began using the liability method of accounting following the new recommendations from the CICA and the OEB.

Under the liability method, current income taxes payable are recorded based on taxable income. Future income taxes arise from temporary differences in the accounting and tax basis of assets and liabilities. Future tax assets and liabilities are provided based on substantively enacted tax rates that will be in effect when the differences are expected to reverse.

Under the taxes payable method, no provisions were made for future income taxes as a result of temporary differences between the tax basis of assets and liabilities and their carrying amounts for accounting purposes. When unrecorded future income taxes became payable, it was expected that they would be included in the rates approved by the OEB and recovered from the customers of the regulated business at that time.

Contributions in aid of construction

Capital contributions received from outside sources are used to finance additions to property, plant and equipment of LDC. According to the AP Handbook, capital contributions received are treated as a "credit" to property, plant and equipment. The amount is subsequently depreciated by a charge to accumulated depreciation and a credit to depreciation expense at an equivalent rate to that used for the depreciation of the related property, plant and equipment.

Allowance for funds used during construction

The AP Handbook provides for the inclusion of an Allowance for Funds Used During Construction ["AFUDC"] when capitalizing construction-in-progress assets, until such time as the asset is substantially complete. A concurrent credit of the same amount is made to the interest expense account when the allowance is capitalized. The interest rate for capitalization is prescribed by the OEB and modified on a periodic basis and is applied to the balance of the construction-in-progress assets on a simple interest basis. AFUDC is included in property, plant and equipment and construction-in-progress for financial reporting purposes, charged to operations through depreciation expense over the service life of the related assets and recovered through future revenue.

c) Cash and cash equivalents

Cash and cash equivalents include cash in bank accounts and short-term investments with terms to maturity of 90 days or less from their date of acquisition.

d) Inventories

Effective January 1, 2008, the Corporation adopted CICA Handbook Section 3031 – "Inventories" ["Handbook Section 3031"] which is based on the International Accounting Standards Board's International Accounting

Standard 2 and replaced existing CICA Handbook Section 3030. Under this new standard, inventories are required to be measured at the lower of cost and net realizable value and any items considered to be major future components of property, plant and equipment are to be transferred to property, plant and equipment. The new standard also provides updated guidance on the appropriate methods of determining cost and the impact of any write-downs to net realizable value. The implementation of this standard did not have any impact on the Corporation's results of operations.

Inventories consist primarily of maintenance and construction materials. The Corporation has retrospectively reclassified all major future components of its electricity distribution system infrastructure from inventory to property, plant and equipment. Once capitalized, these items are not depreciated until they are put into service. Inventories are carried at the lower of cost and net realizable value, with cost determined on an average cost basis net of a provision for obsolescence.

e) Investments

Investments include the replacement notes received on January 21, 2009 in connection with the restructuring of the Asset Backed Commercial Paper ["ABCP"] notes impacted by the liquidity issues that arose in August 2007. These investments are classified as long-term investments on the consolidated balance sheet. Following the receipt of the replacement notes, the Corporation changed the classification of its investments from "Investments Held to Maturity" to "Investments Held for Trading". This change was related to the underlying nature of the replacement notes and follows the guidance issued by the Accounting Standards Board of Canada ["AcSB"]. The investments are measured at fair value at each period end with changes in fair value included in the consolidated statements of income in the period in which they arise *[note 8]*.

f) Property, plant and equipment and depreciation

Property, plant and equipment are stated at cost and are removed from the accounts at the end of their estimated average service lives, except in those instances where specific identification allows their removal at retirement or disposition. Gains or losses at retirement or disposition of such assets are credited or charged to "Other" in the consolidated statements of income.

In the event that facts and circumstances indicate that property, plant and equipment may be impaired, an evaluation of recoverability is performed. For purposes of such an evaluation, the estimated future undiscounted cash flows associated with the asset are compared to the carrying amount of the asset to determine if a write-down is required. The impairment loss is measured as the amount by which the carrying amount of the asset exceeds its fair value.

Depreciation is provided on a straight-line basis over the estimated service lives at the following annual rates:

Buildings	2.0%
Stations	2.5% to 6.7%
Distribution lines	2.5% to 25.0%
Transformers	3.3% to 4.0%
Meters	2.9% to 6.7%
Other capital assets	4.0% to 20.0%
Communications	10.0% to 20.0%
Computer hardware	20.0% to 25.0%
Rolling stock	12.5% to 33.3%
Equipment and tools	10.0%

Construction in progress includes assets not currently in use which are not depreciated.

g) Intangible assets

Effective January 1, 2009, the Corporation retrospectively adopted CICA Handbook Section 3064 - "Goodwill and Intangible Assets" ["Handbook Section 3064"]. Handbook Section 3064 replaces Handbook Section 3062 – "Goodwill and Other Intangible Assets" ["Handbook Section 3062"] and provides extensive guidance on recognition, measurement and disclosure of intangible assets.

The Corporation evaluated existing intangible assets as at January 1, 2009 to determine whether the intangible assets recognized under previous Handbook Section 3062 met the definition, recognition, and measurement criteria of an intangible asset in accordance with Handbook Section 3064. The assets included land rights or easements, computer software, and capital contributions. As a result, the Corporation identified $1,985,000 of expenditures that no longer met the definition of intangible assets under Handbook Section 3064 and these expenditures were removed from intangible assets and transferred to a regulatory asset account for future recovery. The Corporation's decision to record these expenditures to regulatory assets is based on the fact that the expenditures have already been approved for recovery by the OEB in prior regulatory proceedings. In the absence of rate regulation, these expenditures would have been recorded to opening retained earnings.

Intangible assets are all externally acquired and are stated at cost. Amortization is provided on a straight-line basis over their estimated useful service lives at the following annual rates:

Computer software	20.0%
Capital contributions	4.0%

Software in development includes assets not currently in use which are not amortized.

h) Deferred debt issue costs

Debt issue costs arising from the Corporation's debenture offerings are recorded against the principal amount of the "Debentures". The debentures are accreted back to their face value using the effective interest rate method over the remaining period to maturity.

i) Workplace Safety and Insurance Act

The Corporation is a Schedule 1 employer for workers' compensation under the Workplace Safety and Insurance Act ["WSIA"]. As a Schedule 1 employer, the Corporation is required to pay annual premiums into an insurance fund established under the WSIA and recognizes expenses based on funding requirements.

j) Revenue recognition

LDC

Revenues from the sale of electricity are recorded on a basis of cyclical billings and also include unbilled revenues accrued in respect of electricity delivered but not yet billed.

In May 2007, LDC entered into CDM agreements with the Ontario Power Authority [“OPA”] for the period from 2007 to 2010. The revenues and costs associated with these programs are accounted for using the net basis of accounting, while any performance fees are recognized as the related CDM programs are delivered.

Revenues from Lost Revenue Adjustment Mechanism [“LRAM”] and Shared Savings Mechanism [“SSM”] are recognized as related programs are delivered and measurable.

Other revenues, which includes revenues from electricity distribution related services, are recognized as the services are rendered.

TH Energy

Revenues from the delivery of street lighting and expressway lighting services are recorded as services are rendered.

Other revenues, which includes energy efficiency products and services revenues are accounted for under the percentage of completion method, with revenues recognized proportionately with the degree of completion of the services under contract. Losses on contracts are fully recognized when they become evident.

k) Financial instruments

At inception, all financial instruments which meet the definition of a financial asset or financial liability are to be recorded at fair value, unless fair value cannot be reliably determined. Gains and losses related to the measurement of financial instruments are reported in the consolidated statements of income. Subsequent measurement of each financial instrument will depend on the balance sheet classification elected by the Corporation. The fair value of a financial instrument is the amount of consideration that would be agreed upon in an arm’s length transaction between willing parties.

The following summarizes the accounting classification the Corporation has elected to apply to each of its significant categories of financial instruments:

Cash equivalents and short-term investments	Investments Held-to-Maturity
Accounts receivable and unbilled revenue	Loans and Receivables
Investments	Investments Held-for-Trading
Accounts payable and accrued liabilities	Other Financial Liabilities
Customers’ advance deposits	Other Financial Liabilities
Debentures	Other Financial Liabilities
Promissory note payable to the City	Other Financial Liabilities

The Corporation uses the following methods and assumptions to estimate the fair value of each class of financial instruments for which carrying amounts are included in the consolidated balance sheet:

- Cash equivalents, comprising short-term investments, are classified as “Investments Held-to-Maturity” and are measured at amortized cost, which, upon initial recognition, is considered equivalent to fair value. The carrying amounts approximate fair value because of the short maturity of these instruments.
- Accounts receivable and unbilled revenue are classified as “Loans and Receivables” and are measured at amortized cost, which, upon initial recognition, are considered equivalent to fair value. Subsequent

measurements are recorded at amortized cost using the effective interest rate method. The carrying amounts approximate fair value because of the short maturity of these instruments.

- Investments, comprised of the replacement notes received on January 21, 2009 in connection with the restructuring of the ABCP notes, are classified as "Investments Held-for-Trading". Prior to receiving the replacement notes, the Investments were classified as "Investments Held-to-Maturity". The notes are measured at fair value at each period end with changes in fair value included in the consolidated statements of income in the period in which they arise. Estimated fair value has been determined using valuation techniques that incorporate discounted future cash flows reflecting market conditions and other factors that a market participant would consider *[note 8]*.
- Accounts payable and accrued liabilities are classified as "Other Financial Liabilities" and are initially measured at their fair value. Subsequent measurements are recorded at amortized cost using the effective interest rate method. The carrying amounts approximate fair value because of the short maturity of these instruments.
- Customers' advance deposits are classified as "Other Financial Liabilities" and are initially measured at their fair value. Subsequent measurements are recorded at amortized cost using the effective interest rate method. The carrying amounts approximate fair value because of the short maturity of the current portion, and the discounted long-term portion approximates the carrying value, taking into account interest accrued on the outstanding balance.
- The debentures and the promissory note payable to the City are classified as "Other Financial Liabilities" and are initially measured at their fair value. The carrying amounts of the debentures and the promissory note payable to the City are carried at amortized cost, based on an initial fair value as determined at the time using quoted market price for similar debt instruments. The fair value of the debentures and the promissory note payable to the City is calculated by discounting the related cash flows at the estimated yield to maturity of similar debt instruments *[note 19]*. While the Corporation has the option to redeem some or all of the debentures at their discretion, this option has no value and has not been recorded in the consolidated financial statements.

Effective January 1, 2008, the Corporation adopted CICA Handbook Sections 3862 – "Financial Instruments – Disclosures" ["Handbook Section 3862"] and 3863 – "Financial Instruments – Presentation", which establish the requirement of disclosure of risks associated with both recognized and unrecognized financial instruments and the management of those risks. The adoption of these standards did not have any impact on the Corporation's results of operations or financial position *[note 19]*.

In January 2009, the CICA issued Emerging Issues Committee Abstract 173, "Credit Risk and the Fair Value of Financial Assets and Financial Liabilities" ["EIC-173"], effective for interim and annual financial statements ending on or after January 2009. EIC-173 provides further information on the determination of the fair value of financial assets and financial liabilities under Handbook Section 3855 – "Financial Instruments – Recognition and Measurement" ["Handbook Section 3855"]. It states that an entity's own credit and the credit risk of the counterparty should be taken into account in determining the fair value of financial assets and financial liabilities, including derivative instruments. The adoption of this standard did not have any impact on the Corporation's results of operations or financial position.

In June 2009, the CICA amended Handbook Section 3862 to include additional disclosure requirements with respect to fair value measurements of financial instruments and to enhance liquidity risk disclosure requirements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

[all tabular amounts in thousands of dollars]

December 31, 2009

Handbook Section 3862 establishes a fair value hierarchy which includes three levels of inputs that may be used to measure fair value:

- Level 1 – Unadjusted quoted prices in active markets for identical assets or liabilities. An active market for the asset or liability is a market in which transactions for the asset or liability occur with sufficient frequency and volume to provide pricing information on an ongoing basis;
- Level 2 – Observable inputs other than level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities; and
- Level 3 – Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

The Corporation adopted these amendments effective for the fiscal year ended December 31, 2009. Comparative information is not required in the first year of application *[note 19]*.

In August 2009, the CICA amended Handbook Section 3855 to add guidance concerning the assessment of embedded derivatives upon reclassification of a financial asset out of the assets held-for-trading category. These amendments apply prospectively to reclassifications made on or after July 1, 2009. Earlier adoption is permitted. The application of these amendments did not have any impact on the Corporation's results of operations or financial position.

In August 2009, the CICA amended Handbook Section 3025 – "Impaired Loans" to include held-to-maturity investments and to conform the definition of a loan to that in amended Handbook Section 3855. These amendments apply to annual financial statements relating to fiscal years beginning on or after November 1, 2008. The Corporation adopted these amendments effective for the fiscal year ended December 31, 2009. The application of these amendments did not have any impact on the Corporation's results of operations or financial position.

l) Capital disclosures

Effective January 1, 2008, the Corporation adopted CICA Handbook Section 1535 – "Capital Disclosures" which requires disclosure of the Corporation's objectives, policies and processes for managing capital as well as its compliance with any external capital requirements *[note 18]*. The implementation of this standard did not have any impact on the Corporation's results of operations or financial position.

m) Employee future benefits

Pension plan

The Corporation provides a pension plan for its full-time employees through the Ontario Municipal Employees Retirement System ["OMERS"]. OMERS is a multi-employer, contributory, defined benefit pension plan established in 1962 by the Province of Ontario for employees of municipalities, local boards and school boards in Ontario. Both participating employers and employees are required to make plan contributions based on participating employees' contributory earnings. The Corporation recognizes the expense related to this plan as contributions are made.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Employee future benefits other than pension

Employee future benefits other than pension provided by the Corporation include medical, dental and life insurance benefits, and accumulated sick leave credits. These plans provide benefits to employees when they are no longer providing active service. Employee future benefit expense is recognized in the period in which the employees render services on an accrual basis.

The accrued benefit obligations and current service costs are calculated using the projected benefit method prorated on service and based on assumptions that reflect management's best estimate. The current service cost for a period is equal to the actuarial present value of benefits attributed to employees' services rendered in the period. Past service costs from plan amendments are amortized on a straight-line basis over the average remaining service period of employees active at the date of amendment. The excess of the net actuarial gains (losses) over 10% of the accrued benefit obligation is amortized into expense over the average remaining service period of active employees to full eligibility. The effects of a curtailment gain or loss are recognized in income in the year of the event giving rise to the curtailment. The effects of a settlement gain or loss are recognized in the period in which a settlement occurs.

n) Asset retirement obligations

The Corporation recognizes a liability for the future environmental remediation of certain properties and for future removal and handling costs for contamination in distribution equipment in service and in storage. Initially, the liability is measured at present value and the amount of the liability is added to the carrying amount of the related asset. In subsequent periods, the asset is depreciated and the liability is adjusted quarterly for the discount applied upon initial recognition of the liability ("accretion expense") and for changes in the underlying assumptions. The liability is recognized when the asset retirement obligation ["ARO"] is incurred and when the fair value is determined.

o) Customers' advance deposits

Customers' advance deposits are cash collections from customers to guarantee the payment of energy bills. The customers' advance deposits liability includes interest credited to the customers' deposit accounts, with the debit charged to interest expense. Deposits expected to be refunded to customers within the next fiscal year are classified as a current liability.

p) Use of estimates

The preparation of the Corporation's consolidated financial statements in accordance with Canadian GAAP requires management to make estimates and assumptions which affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses for the year. Actual results could differ from those estimates, including changes as a result of future decisions made by the OEB, the Minister of Energy, the Minister of Finance, or the Minister of Revenue.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
[all tabular amounts in thousands of dollars]

December 31, 2009

q) Future Accounting Pronouncements

International Financial Reporting Standards ["IFRS"]

On February 13, 2008, the AcSB confirmed that publicly accountable enterprises will be required to adopt IFRS in place of Canadian GAAP for interim and annual reporting purposes for fiscal years beginning on or after January 1, 2011. A limited number of converged or IFRS-based standards will be incorporated into Canadian GAAP prior to 2011, with the remaining standards to be adopted at the change over date. The Corporation has an internal initiative to govern the conversion process and is currently in the process of evaluating the potential impact of the conversion to IFRS on its consolidated financial statements. Although the impact of the adoption of IFRS on the Corporation's financial position and results of operations is not yet reasonably determinable or estimable, the Corporation does expect a significant increase in financial statement disclosure requirements resulting from the adoption of IFRS, and is designing the systems and related processes changes, which will be required in order to provide the additional information required to make these disclosures.

Consolidated Financial Statements and Non-controlling Interests

In January 2009, the CICA issued Handbook Section 1601 – "Consolidated Financial Statements" ["Handbook Section 1601"]. This section along with the new Handbook Section 1602 – "Non-controlling Interests" ["Handbook Section 1602"] replace Handbook Section 1600 – "Consolidated Financial Statements" and establish standards for the preparation of consolidated financial statements. These standards apply to interim and annual consolidated financial statements relating to fiscal years beginning on or after January 1, 2011. Earlier application is permitted as of the beginning of a fiscal year. The Corporation has determined that these standards will have no impact on the classification or valuation of its consolidated financial statements.

Financial Instruments – Recognition and Measurement

In June 2009, the CICA amended Handbook Section 3855 to clarify when an embedded prepayment option is separated from its host debt instrument for accounting purposes. This amendment applies to interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011. Earlier adoption is permitted. This section has also been amended to clarify the application of the effective interest method after a debt instrument has been impaired. This amendment applies retrospectively to financial statements for fiscal years beginning on or after January 1, 2010. The Corporation expects these amendments will have no impact on its results of operations and financial position.

Comprehensive Revaluation of Assets and Liabilities

In August 2009, the CICA amended Handbook Section 1625 – "Comprehensive Revaluation of Assets and Liabilities" to be consistent with Handbook Section 1582 – "Business Combinations", Handbook Section 1601 and Handbook Section 1602, which were issued in January 2009. The amendments apply prospectively to comprehensive revaluations of assets and liabilities occurring in fiscal years beginning on or after January 1, 2011. Earlier adoption is permitted as of the beginning of a fiscal year. The Corporation expects these amendments will have no impact on its results of operations and financial position.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
[all tabular amounts in thousands of dollars]

December 31, 2009

5. INVENTORIES

Inventories consist of the following:

	2009 $	2008 $
Consumables, tools and other maintenance items	**1,870**	1,478
Fuses	**1,783**	1,014
Vehicle parts and supplies	**407**	436
Other	**2,284**	2,235
Less: Allowance for provisions	**(120)**	(94)
	6,224	5,069

6. PROPERTY, PLANT AND EQUIPMENT, NET

Property, plant and equipment consist of the following:

	2009			2008		
	Cost $	Accumulated depreciation $	Net book value $	Cost $	Accumulated depreciation $	Net book value $
Land	**4,048**	**—**	**4,048**	4,073	—	4,073
Buildings	**146,163**	**53,476**	**92,687**	151,029	50,717	100,312
Stations	**253,659**	**120,201**	**133,458**	242,557	113,315	129,242
Distribution lines	**2,449,630**	**1,291,104**	**1,158,526**	2,324,813	1,197,962	1,126,851
Transformers	**567,573**	**321,140**	**246,433**	542,176	301,446	240,730
Meters	**204,425**	**105,829**	**98,596**	199,127	97,145	101,982
Other capital assets	**53,269**	**29,935**	**23,334**	65,612	38,413	27,199
Communications	**23,860**	**18,994**	**4,866**	29,351	23,381	5,970
Computer hardware	**33,136**	**27,380**	**5,756**	49,299	40,055	9,244
Rolling stock	**68,043**	**42,650**	**25,393**	59,209	41,749	17,460
Equipment and tools	**37,154**	**28,011**	**9,143**	35,827	26,579	9,248
Construction in progress	**117,714**	**—**	**117,714**	81,295	—	81,295
	3,958,674	**2,038,720**	**1,919,954**	3,784,368	1,930,762	1,853,606

For the year ended December 31, 2009, AFUDC in the amount of $2,752,000 [2008 - $2,016,000] was capitalized to property, plant and equipment and credited to interest expense.

At December 31, 2009, net book value of stranded meters related to the deployment of smart meters amounting to $25,347,000 [December 31, 2008 - $25,866,000] is included in property, plant and equipment. In the absence of rate regulation, property, plant and equipment would have been $25,347,000 lower at December 31, 2009 [December 31, 2008 - $25,866,000].

7. INTANGIBLE ASSETS, NET

Intangible assets consist of the following:

	2009			2008		
	Cost $	**Accumulated amortization $**	**Net book value $**	**Cost $**	**Accumulated amortization $**	**Net book value $**
Land rights	**—**	**—**	**—**	1,720	242	1,478
Computer software	**145,074**	**113,163**	**31,911**	151,804	111,895	39,909
Capital contributions	**2,043**	**443**	**1,600**	2,043	361	1,682
Software in development	**40,318**	**—**	**40,318**	23,632	—	23,632
	187,435	**113,606**	**73,829**	179,199	112,498	66,701

During the year ended December 31, 2009, the Corporation acquired $14,055,000 intangible assets subject to amortization [2008 - $20,889,000] and acquired $17,101,000 intangible assets not subject to amortization [2008 - $4,900,000].

8. INVESTMENTS

The Corporation held $88,000,000 of third-party ABCP notes impacted by the liquidity crisis that arose in the Canadian market in August 2007. At the time the Corporation purchased each of these notes, they were rated R1(High) by DBRS Limited ["DBRS"], the highest credit rating issued for commercial paper. Following the liquidity crisis, a group representing banks, asset providers and major investors [the "Montreal Committee"] was formed to oversee the restructuring of the impacted ABCP notes.

On January 12, 2009, the Ontario Superior Court approved the restructuring plan proposed by the Montreal Committee and supported by the noteholders of the Canadian third-party ABCP market. On January 21, 2009, the amended restructuring plan was completed and the Corporation received its replacement notes. The replacement notes received have an aggregate principal amount of $87,700,000.

The distribution by class is listed below:

Master Asset Vehicle II	Amount Received $	Percent of Total
Class A-1	36,900,000	42.1%
Class A-2	34,500,000	39.3%
Class B	6,300,000	7.2%
Class C	2,400,000	2.7%
Ineligible Asset Tracking notes	7,600,000	8.7%

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

[all tabular amounts in thousands of dollars]

December 31, 2009

Of the $87,700,000, $80,100,000 includes a combination of leveraged collateralized debt, synthetic assets and traditional securitized assets which is represented by senior Class A-1 and Class A-2 and subordinated Class B and Class C long-term restructured notes, and $7,600,000 is represented by assets that have an exposure to U.S. mortgages and sub-prime mortgages, which has been replaced by Ineligible Asset Tracking [“IAT”] notes.

At the time of issuance, DBRS assigned an “A” credit rating to the Class A-1 and A-2 notes; the Class B, C and IAT notes were unrated. On August 11, 2009, DBRS downgraded the rating of the Class A-2 notes from A to BBB (low).

According to the Eighteenth and Nineteenth Reports of the Monitor, the “legal final maturity” of the restructured notes is July 15, 2056. However, the expected repayment date for the restructured Class A-1 and Class A-2 notes is January 22, 2017. Based on the information contained in the above-mentioned reports, there is no obligation to pay interest on the notes before 2019 and no legal requirement to pay principal until 2056.

As part of the implementation of the restructuring plan, the Corporation re-measured its investments in ABCP notes prior to the exchange. This valuation considered new information available at that date and reflected current market conditions. As a result of this valuation, the Corporation increased the fair value of its investment in ABCP notes from $52,908,000 at December 31, 2008 to $56,524,000 at January 20, 2009. The increase in fair value reflected the expected payment to the Corporation of its share of cash accumulated in the conduit trusts from August 2007 to January 2009. The increase in fair value was recorded as income in the first quarter of 2009, under change in fair value of investments.

On January 23, 2009, the Corporation received $2,712,000 representing the first instalment of its share of the accumulated cash in the conduit trusts up to August 31, 2008. On May 15, 2009, the Corporation received a further $1,217,000 representing the second instalment of its share of accumulated cash in the conduit trusts from September 2008 through January 20, 2009. These balances reduced the value of the investments.

Following the receipt of the new notes, the Corporation changed the classification of these investments from “Investments Held-To-Maturity” to “Investments Held-For-Trading”. This change was mainly related to the underlying nature of the new notes and follows the guidance issued by the AcSB on February 2, 2009. The new notes are measured at fair value at each period end with changes in fair value included in the consolidated statements of income in the period in which they arise.

In the fourth quarter of 2009, the Corporation noticed evidence of the development of a market for these notes. However as at December 31, 2009, this market had not developed to a state that warranted a mark-to-market valuation process. Accordingly, the Corporation continued to use a mark-to-model valuation technique that incorporated available information and market data. The valuation technique used by the Corporation to estimate the fair value of its investments in the restructured notes as at December 31, 2009, incorporated a discounted cash flow model considering the best available public information regarding market conditions, including the ratings assigned by DBRS regarding the Class A-1 and Class A-2 notes, and other factors that a market participant would consider to evaluate such investments. The Corporation may change its valuation methodology to a mark-to-market valuation in the future as a more robust market for these notes develops.

A weighted average interest rate of 1.28% was used to determine the expected interest income on the restructured notes, except for the IAT notes, for which a weighted average interest rate of 1.98% was used. These rates were based on a forecast of 90-day Bankers’ Acceptance [“BA”] rates less 50 basis points from 2010 through 2017; except for the IAT notes for which a discount rate based on forecast 90-day BA rate plus 20 basis points was used.

To derive a net present value of the principal and future cash flows, the restructured notes were discounted using an interest rate spread over forecast BA rates ranging from 340 basis points to 1,600 basis points over a seven-year period. On a weighted average basis, the interest rates used to discount the notes ranged from 4.27% to 16.87%.

The discount rates vary by each of the different replacement long-term notes issued as each is expected to have a different risk profile. The discount rates used to value the notes include a risk premium factor that incorporates current indicative credit default swap spreads, an estimated liquidity premium, and a premium for credit losses.

Based on the assumptions described above, the discounted cash flows resulted in an estimated fair value of the Corporation's investment in the restructured notes of $47,930,000 as at December 31, 2009 as compared to $56,524,000 as at January 20, 2009. The variance was mainly related to the cash received in connection with the Corporation's share of cash accumulated in the conduit trusts and change in interest rates due to changing market conditions including the impact of the credit rating downgrade of the Class A-2 notes in August 2009.

A sensitivity analysis was also conducted to examine the impact of an increase or a decrease in the overall weighted average discount rate. Based on the Corporation's mark-to-model valuation, a variation of 1% (100 basis points) would reduce or increase the estimated fair value of the restructured notes by approximately $3,700,000.

The estimation by the Corporation of the fair value of the restructured notes, as at December 31, 2009, is subject to significant risks and uncertainties, including the timing and amount of future cash flows, market liquidity and the quality of the underlying assets and financial instruments. Accordingly, there can be no assurance that the Corporation's assessment of the estimated fair value of the restructured notes will not change materially in subsequent periods.

The on-going liquidity crisis regarding the investments described above has had no significant impact on the Corporation's operations. The Corporation has sufficient cash to fund all of its ongoing liquidity and capital expenditure requirements and is in compliance with the financial covenants under the terms of its outstanding indebtedness.

9. REGULATORY ASSETS AND LIABILITIES

Regulatory assets consist of the following:

	2009 **$**	**2008** **$**
Smart meters	**50,669**	25,830
Contact voltage	**9,050**	—
LRAM and SSM	**3,546**	—
Other	**4,928**	383
	68,193	26,213

Regulatory liabilities consist of the following:

	2009 $	2008 $
Future income taxes	**250,948**	—
Settlement variances	**36,615**	57,516
PILs variances	**15,197**	11,712
Regulatory assets recovery account	**3,598**	13,832
Other	**2,217**	456
	308,575	83,516

For the year ended December 31, 2009, LDC recovered approved regulatory assets amounts of $nil through permitted distribution rate adjustments [2008 – $15,381,000]. For the year ended December 31, 2009, LDC disposed of approved regulatory liability amounts of $13,747,000 through permitted distribution rate adjustments [2008 – $9,671,000].

The regulatory assets and liabilities balances of the Corporation are as follows:

[a] Smart Meters

The smart meters regulatory asset account relates to the Province of Ontario's decision to install smart meters throughout Ontario by 2010. LDC launched its project shortly following the Province of Ontario's announcement in 2006. As at December 31, 2009, LDC had installed approximately 631,000 smart meters. In 2008, in connection with this initiative, the OEB approved the disposition of the balances incurred in 2006 and 2007. The OEB also approved the transfer from regulatory assets to property plant and equipment of all capital expenditures incurred in 2006 and 2007. In a separate decision regarding LDC's electricity distribution rates for 2008, the OEB ordered LDC to record all future expenditures and revenues related to smart meters to a regulatory asset account and allowed LDC to keep the net book value of the stranded meters related to the deployment of smart meters in its rate base.

In connection with its smart meter initiatives, the Corporation has incurred costs amounting to $22,833,000 for the year ended December 31, 2009 [2008 - $34,125,000]. As at December 31, 2009, smart meter capital expenditures, net of accumulated depreciation, totalling $51,501,000 have been recorded to regulatory assets [December 31, 2008 - $27,559,000]. These expenditures would otherwise have been recorded as property, plant and equipment and intangible assets under Canadian GAAP for unregulated businesses. In the absence of rate regulation, property, plant and equipment and intangible assets would have been $45,606,000 and $5,895,000 higher as at December 31, 2009 [December 31, 2008 - $27,559,000 and $nil, respectively].

For the year ended December 31, 2009, smart meter operating expenses of $3,048,000 [2008 - $863,000], and smart meter depreciation expense of $3,447,000 [2008 - $1,128,000] were deferred which would have been expensed under Canadian GAAP for unregulated businesses. In the absence of rate regulation, for the year ended December 31, 2009, operating expenses would have been $3,048,000 higher [2008 - $863,000 higher], and depreciation expense would have been $3,447,000 higher [2008 - $1,128,000 higher].

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

[all tabular amounts in thousands of dollars]

For the year ended December 31, 2009, smart meter customer revenues of $5,741,000 were deferred [2008 - $3,796,000]. In the absence of rate regulation, for the year ended December 31, 2009, revenue would have been $5,741,000 higher [2008 - $3,796,000 higher].

[b] Contact Voltage

On June 30, 2009, LDC filed an application with the OEB seeking recovery of costs incurred for the unexpected impact of the remediation of safety issues on its electricity distribution infrastructure. LDC sought recovery of $14,350,000 by way of fixed term rate riders of three years for the street lighting and unmetered scattered load rate classes, and one year for all other classes. On December 10, 2009, the OEB issued its decision, which provides for the future recovery of $9,050,000 of related expenditures. Accordingly, the Corporation has increased its regulatory assets and reduced its operating expenditures by $9,050,000 for 2009. In the absence of rate regulation, for the year ended December 31, 2009, operating expenses would have been $9,050,000 higher.

[c] Lost Revenue Adjustment Mechanism and Shared Savings Mechanism

Under certain specific rules, the OEB has allowed LDC to receive compensation for the lost revenue and the benefits associated to CDM programs delivered. The LRAM represents the lost revenue from CDM programs and the SSM represents LDC's share of provincial savings related to these programs.

On December 15, 2008, LDC applied to the OEB to recover LRAM and SSM amounts related to CDM programs undertaken in 2007. On September 22, 2009, the OEB approved the recovery by LDC of $2,904,000 for LRAM and $586,000 for SSM programs through rate riders commencing on May 1, 2010 and ending April 30, 2011.

[d] Future income taxes

This regulatory liability account relates to the expected future electricity distribution rate reduction for customers arising from timing differences in the recognition of future tax assets.

On January 1, 2009, LDC began to account for the differences between its financial statement carrying value and tax basis of assets and liabilities following the liability method in accordance with CICA Handbook Section 3465 *[note 4[b]]*. As at December 31, 2009, LDC has recorded a future income tax asset of $250,948,000, and a corresponding regulatory liability of $250,948,000.

[e] Settlement variances

This account is comprised of the variances between amounts charged by LDC to customers (based on regulated rates) and the corresponding cost of non-competitive electricity service incurred by LDC after May 1, 2002. The settlement variances relate primarily to service charges, non-competitive electricity charges, imported power charges and the global adjustment. Accordingly, LDC has deferred these recoveries in accordance with the criteria set out in the AP Handbook.

The balance for settlement variances continues to be calculated and attract carrying charges in accordance with the OEB's direction. For the year ended December 31, 2009, settlement variances of $6,628,000 were disposed through rate adjustments.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

[all tabular amounts in thousands of dollars]

December 31, 2009

[f] PILs variances

As at December 31, 2009, LDC has accumulated a PILs variance amount representing differences that have resulted from a legislative or regulatory change to the tax rates or rules assumed in the rate adjustment model totalling an over-recovery of $15,197,000 [December 31, 2008 - $11,712,000].

[g] Regulatory assets recovery account ["RARA"]

The RARA consists of balances of regulatory assets or regulatory liabilities approved for disposition by the OEB through rate riders. The RARA is subject to carrying charges following the OEB prescribed methodology and related rates.

In its decision regarding the electricity distribution rates of LDC issued on May 15, 2008, the OEB approved the disposition of regulatory liabilities of $18,622,000, consisting of settlement variances of $14,590,000 and pre-market opening line loss variance of $4,032,000, which were transferred to the 2008 RARA in June 2008.

On April 16, 2009, the OEB approved disposition of regulatory liability of $7,582,000, for amounts arising from the extended effectiveness of certain rate riders into the 2008 rate year, which was transferred to the 2009 RARA in April 2009.

10. OTHER ASSETS

Other assets consist of the following:

	2009 **$**	**2008** **$**
Prepaid leases	**7,456**	7,544
Other	**159**	318
	7,615	7,862

11. ASSETS HELD FOR SALE

In November 2009, the Corporation committed to a plan to sell a building and related land owned by TH Energy. An active program to locate a buyer and other actions required to complete the sale plan have been initiated and the property has been actively marketed for sale. Accordingly, an amount of $5,258,000 has been transferred from property, plant and equipment to assets held for sale as at December 31, 2009. The balance is measured at the lower of the carrying amount or fair value less cost to sell. The Corporation does not record depreciation on assets classified as held for sale.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
[all tabular amounts in thousands of dollars]

December 31, 2009

12. BANK INDEBTEDNESS AND LETTERS OF CREDIT

The Corporation has a Revolving Credit Facility with a syndicate of Canadian banks [the "Revolving Credit Facility"] expiring on May 3, 2010. Under the terms of the Revolving Credit Facility, the Corporation may borrow up to $500,000,000, of which:

[a] $500,000,000 less the amount utilized under [b] is available for working capital and LDC capital expenditure purposes in the form of prime rate loans in Canadian dollars and BAs; and

[b] up to $175,000,000 is available in the form of letters of credit to support the prudential requirements of LDC and TH Energy and general credit requirements of the Corporation and its subsidiaries.

The Revolving Credit Facility contains a negative pledge, customary covenants and events of default.

At December 31, 2009, $45,176,000 [December 31, 2008 - $45,078,000] had been utilized under the Revolving Credit Facility in the form of letters of credit primarily to support the prudential requirements of LDC with the Independent Electricity System Operator. At December 31, 2009, no amounts had been drawn for working capital purposes [December 31, 2008 - $nil].

The Corporation also has a bilateral demand line of credit for $20,000,000 with a Canadian chartered bank. The line of credit bears interest at the bank's prime rate. At December 31, 2009, no amounts had been drawn on the line of credit [December 31, 2008 - $nil].

13. CURRENT PORTION OF OTHER LIABILITIES

Current portion of other liabilities consists of the following:

	2009 $	2008 $
Current portion of obligations under capital leases *[note 24]*	**218**	199
Customers' advance deposits	**17,002**	16,402
Other	**781**	781
	18,001	17,382

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
[all tabular amounts in thousands of dollars]

December 31, 2009

14. LONG-TERM DEBT

Long-term debt consists of the following:

	2009 $	2008 $
Senior unsecured debentures		
Series 1 - 6.11% due May 7, 2013	**223,406**	223,001
Series 2 - 5.15% due November 14, 2017	**248,653**	248,520
Series 3 - 4.49% due November 12, 2019	**248,416**	—
Promissory note payable to the City	**490,115**	735,173
	1,210,590	1,206,694
Less: Current portion of promissory note payable to the City	—	245,058
Long-term debt	**1,210,590**	961,636
Comprising:		
Debentures	**720,475**	471,521
Promissory note payable to the City	**490,115**	490,115

All long-term debt of the Corporation ranks equally.

a) Senior unsecured debentures

On May 7, 2003, the Corporation issued $225,000,000 10-year senior unsecured debentures [“Series 1”]. The Series 1 debentures bear interest at the rate of 6.11% per annum, payable semi-annually in arrears in equal instalments on May 7 and November 7 of each year. The Series 1 debentures mature on May 7, 2013.

On November 14, 2007, the Corporation issued $250,000,000 10-year senior unsecured debentures [“Series 2”]. The Series 2 debentures bear interest at the rate of 5.15% per annum, payable semi-annually in arrears in equal instalments on May 14 and November 14 of each year. The Series 2 debentures mature on November 14, 2017.

On November 12, 2009, the Corporation issued $250,000,000 10-year senior unsecured debentures [“Series 3”]. The Series 3 debentures bear interest at the rate of 4.49% per annum, payable semi-annually in arrears in equal instalments on May 12 and November 12 of each year. The Series 3 debentures mature on November 12, 2019.

The Corporation may redeem some or all of the debentures at any time prior to maturity at a price equal to the greater of the Canada Yield Price (determined in accordance with the terms of the debentures) and par, plus accrued and unpaid interest up to but excluding the date fixed for redemption. Also, the Corporation may, at any time and from time to time, purchase debentures for cancellation, in the open market, by tender or by private contract, at any price. The debentures have the benefit of certain covenants which, subject to certain exceptions, restrict the ability of the Corporation and LDC to create security interests, incur additional indebtedness not ranking *pari passu* or dispose of all or substantially all of their assets.

b) Promissory note payable to the City

On July 1, 1999, LDC issued a promissory note to the City ["Initial Note"] in the principal amount of $947,000,000 in partial consideration for the assets in respect of the electricity distribution system transferred by the Toronto Hydro-Electric Commission and the City to LDC effective July 1, 1999. The Initial Note was non-interest bearing until December 31, 1999 and interest bearing thereafter at the rate of 6% per annum. Pursuant to the Transfer By-law, the principal amount of the Initial Note was adjusted effective January 1, 2000 to $980,231,000 to reflect the deemed debt to equity structure of LDC permitted by the OEB. At the same time, the Initial Note was replaced by a promissory note ["Replacement Note"] issued by LDC, which was interest bearing at the rate of 6.8% per annum. At December 31, 2002, the Replacement Note was payable on the earlier of demand and December 31, 2003.

Concurrent with the closing of the Series 1 unsecured debentures on May 7, 2003, the City transferred the Replacement Note to the Corporation in consideration for the issuance by the Corporation to the City of a new promissory note in the principal amount of $980,231,000 [the "City Note"].

On September 5, 2006, the Corporation announced that it and the City had amended and restated the City Note effective May 1, 2006 by fixing the interest rate at 6.11% and establishing an agreed repayment schedule. The Corporation is required to pay the principal amount of the note as follows: $245,058,000 on the last business day before each of December 31, 2007, December 31, 2009, December 31, 2011 and on May 6, 2013. On December 31, 2007, the Corporation made the first scheduled payment of $245,058,000 to the City in accordance with the terms of the City Note. On December 31, 2009, the Corporation made the second scheduled payment of $245,058,000 to the City in accordance with the terms of the City Note. Accordingly, the remainder of the principal amount outstanding under the City Note is classified as a long-term liability. Interest is calculated and payable quarterly in arrears on the last business day of March, June, September and December of each year.

15. EMPLOYEE FUTURE BENEFITS

Pension

For the year ended December 31, 2009, the Corporation's OMERS current service pension costs were $11,348,000 [2008 - $11,116,000].

Employee future benefits other than pension

The Corporation has a number of unfunded benefit plans providing retirement and post-employment benefits (excluding pension) to most of its employees. The Corporation pays certain medical, dental and life insurance benefits under unfunded defined benefit plans on behalf of its retired employees. The Corporation pays accumulated sick leave credits, up to certain established limits based on service, in the event of retirement, termination or death of certain employees.

The Corporation measures its accrued benefits obligation for accounting purposes as at December 31 of each year. The latest actuarial valuation was performed as at January 1, 2007.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

[all tabular amounts in thousands of dollars]

December 31, 2009

[a] Accrued benefit obligation

	2009 $	2008 $
Balance, beginning of year	**128,804**	165,661
Experience loss at beginning of year	**6,393**	—
Current service cost	**4,793**	3,613
Interest cost	**10,240**	9,155
Benefits paid	**(6,891)**	(5,055)
Actuarial (gains) losses	**33,805**	(44,276)
Sale of Toronto Hydro Telecom Inc [“Telecom “]	—	(294)
Balance, end of year	**177,144**	128,804

[b] Reconciliation of the accrued benefit obligation to the balance sheet accrued benefits liability

	2009 $	2008 $
Accrued benefit obligation	**177,144**	128,804
Unamortized net actuarial gains (losses)	**(12,654)**	28,073
Unamortized past service costs	**(3,142)**	(4,106)
Post-employment benefits liability	**161,348**	152,771

[c] Components for net periodic defined benefit costs

	2009 $	2008 $
Current service cost	**4,793**	3,613
Interest cost	**10,240**	9,155
Actuarial (gains) losses	**33,805**	(44,276)
Cost incurred (recovered) in the year	**48,838**	(31,508)
Differences between costs incurred and costs recognized in the year in respect of:		
Actuarial (gain) loss	**(34,334)**	44,318
Past service costs	**964**	964
	(33,370)	45,282
Defined benefit costs recognized	**15,468**	13,774
Capitalized as part of property, plant and equipment	**7,043**	6,093
Charged to operations	**8,425**	7,681

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
[all tabular amounts in thousands of dollars]

December 31, 2009

[d] Significant assumptions

	2009 %	2008 %
Accrued benefit obligation as of December 31:		
Discount rate	**6.0**	7.5
Rate of compensation increase	**4.0**	4.0
Benefit costs for years ended December 31:		
Discount rate	**7.5**	5.5
Rate of compensation increase	**4.0**	4.0
Assumed health care cost trend rates at December 31:		
Rate of increase in dental costs	**4.0**	4.0

For December 31, 2009, medical costs are assumed to increase at 7.5% [2008 - 8.5%] graded down by 0.5% [2008 - 0.5%] annual decrements to 5.0% [2008 - 5.0%] in 2016 and thereafter.

[e] Sensitivity analysis

Assumed health and dental care cost trend rates have a significant effect on the amounts reported for health and dental care plans. A one-percentage-point change in assumed health and dental care cost trend rates have the following effects for 2009:

	Increase $	Decrease $
Total of current service and interest cost (at 7.5%)	**1,938**	**(1,492)**
Accrued benefit obligation at December 31, 2009 (at 6.0%)	**28,160**	**(21,574)**

Assumed interest rates have a significant effect on the amounts reported for the total accrued benefit obligation and expense. A one-percentage-point change in assumed interest rates would have the following effects for 2009:

	Increase $	Decrease $
Accrued benefit obligation as at December 31, 2009	**(20,024)**	**28,547**
Estimated expense for fiscal 2010	**(314)**	**2,474**

16. OTHER LIABILITIES

Other long-term liabilities consist of the following:

	2009 $	2008 $
Obligations under capital leases *[note 24]*	**447**	397
Other	**1,026**	1,833
	1,473	2,230

17. ASSET RETIREMENT OBLIGATIONS

Reconciliation between the opening and closing ARO liability balances is as follows:

	2009 $	2008 $
Balance, beginning of year	**6,528**	7,523
ARO liabilities settled in the year	**(87)**	(463)
Accretion expense	**291**	405
Revision in estimated cash flows	**820**	(937)
Balance, end of year	**7,552**	6,528

At December 31, 2009, the Corporation estimates the undiscounted amount of cash flows required over the next one to fifty years to settle the ARO is $9,274,000 [December 31, 2008 - $9,244,000]. Discount rates ranging from 1.39% to 6.60% were used to calculate the carrying value of the ARO liabilities. No assets have been legally restricted for settlement of the liability.

18. CAPITAL DISCLOSURES

The Corporation's main objectives when managing capital are to:

- ensure ongoing access to funding to maintain and improve the electricity distribution system of LDC, and to meet any capital needs of its other subsidiary companies should such needs arise;
- ensure compliance with covenants related to its credit facilities, senior unsecured debentures and the City Note;
- maintain an A- credit rating as required under its shareholder direction; and
- align its capital structure for regulated activities of LDC with the debt to equity structure deemed by the OEB.

As at December 31, 2009, the Corporation's definition of capital includes shareholder's equity and long-term debt which includes the current portion of the promissory note payable to the City, and has remained unchanged from December 31, 2008. As at December 31, 2009, shareholder's equity amounts to $998,254,000 [December 31, 2008 – $981,291,000] and long-term debt, including the current portion of the promissory note payable to the City,

amounts to $1,210,590,000 [December 31, 2008 – $1,206,694,000]. The Corporation's capital structure as at December 31, 2009 is 55% debt and 45% equity [December 31, 2008 - 55% debt and 45% equity]. There have been no changes in the Corporation's approach to capital management during the year.

As at December 31, 2009, the Corporation is subject to debt agreements that contain various covenants. The Corporation's unsecured debentures and the City Note limit consolidated funded indebtedness to a maximum of 75% of total consolidated capitalization. As at December 31, 2009, consolidated funded indebtedness to consolidated capitalization was 55% [December 31, 2008 – 56%].

The Corporation's Revolving Credit Facility limits the debt to capitalization ratio to a maximum of 75%. As at December 31, 2009, the debt to capitalization ratio was 56% [December 31, 2008 – 56%].

The Corporation's long-term debt agreements also include negative covenants such as limitations on funded indebtedness, limitations on designated subsidiary indebtedness, restrictions on mergers and dispositions of designated subsidiaries, and amendments to the City Note. As at December 31, 2009 and as at December 31, 2008, the Corporation was in compliance with all covenants included in its long-term debt agreements, City Note and short-term Revolving Credit Facility.

19. FINANCIAL INSTRUMENTS

a) Recognition and measurement

The Corporation's carrying value and fair value of financial instruments consist of the following:

	2009 $		2008 $	
	Carrying value	**Fair value**	**Carrying value**	**Fair value**
Cash and cash equivalents	**211,370**	**211,370**	340,492	340,492
Accounts receivable, net of allowance for doubtful accounts	**150,281**	**150,281**	131,582	131,582
Unbilled revenue	**295,647**	**295,647**	266,061	266,061
Investments	**47,930**	**47,930**	52,908	52,908
Accounts payable and accrued liabilities	**316,768**	**316,768**	294,839	294,839
Customers' advance deposits	**51,698**	**51,698**	46,685	46,685
Senior unsecured debentures				
Series 1 – 6.11% due May 7, 2013	**223,406**	**247,967**	223,001	242,522
Series 2 – 5.15% due November 14, 2017	**248,653**	**265,874**	248,520	247,872
Series 3 – 4.49% due November 12, 2019	**248,416**	**249,581**	—	—
Promissory note payable to the City	**490,115**	**529,886**	735,173	770,224

The Corporation's fair value measurements of financial instruments within the fair value hierarchy, as at December 31, 2009 consists of $47,930,000 of investments in Level 3.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
[all tabular amounts in thousands of dollars]

December 31, 2009

The following table reconciles the Corporation's Level 3 fair value measurements, which includes its investments from January 1 to December 31, 2009:

Fair value measurements using Level 3 inputs	2009 $
Balance, beginning of year	**52,908**
Loss included in net income	**(1,049)**
Settlements[1]	**(3,929)**
Balance, end of year	**47,930**

[1] Settlements relate to share of accumulated cash received from the conduit trusts on the investments.

b) Risk Factors

The following is a discussion of risks and related mitigation strategies that have been identified by the Corporation for financial instruments. This is not an exhaustive list of all risks, nor will the mitigation strategies eliminate all risks listed. Risks related to the Corporation's investments are discussed in more detail in Investments *[note 8]*.

The Corporation's activities provide for a variety of financial risks, particularly credit risk, interest rate risk and liquidity risk.

Credit risk

Financial instruments are exposed to credit risk as a result of the risk of the counter-party defaulting on its obligations. The Corporation monitors and limits its exposure to credit risk on a continuous basis. The Corporation provides reserves for credit risks based on the financial condition and short and long-term exposures to counter-parties.

The Corporation's credit risk associated with accounts receivable is primarily related to payments from LDC customers. LDC has approximately 690,000 customers, the majority of which are residential. LDC collects security deposits from customers in accordance with directions provided by the OEB. As at December 31, 2009, LDC held security deposits in the amount of $51,698,000 [December 31, 2008 - $46,685,000].

The carrying amount of accounts receivable is reduced through the use of an allowance for doubtful accounts and the amount of the related impairment loss is recognized in the consolidated statements of income. Subsequent recoveries of receivables previously provisioned are credited to the consolidated statements of income.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
[all tabular amounts in thousands of dollars]

December 31, 2009

Credit risk associated with accounts receivable is as follows:

	2009 $	2008 $
Total accounts receivable	**162,861**	141,692
Less: Allowance for doubtful accounts	**(12,580)**	(10,110)
Total accounts receivable, net	**150,281**	131,582
Of which:		
Outstanding for not more than 30 days	**128,729**	104,869
Outstanding for more than 30 days but not more than 120 days	**20,796**	21,668
Outstanding for more than 120 days	**13,336**	15,155
Less: Allowance for doubtful accounts	**(12,580)**	(10,110)
Total accounts receivable, net	**150,281**	131,582

Unbilled revenue represents amounts to which the Corporation has a contractual right to receive cash through future billings but are unbilled at period-end. As at December 31, 2009, total unbilled revenue was $295,647,000 [December 31, 2008 - $266,061,000]. Unbilled revenue outstanding is considered current.

At December 31, 2009, there were no significant concentrations of credit risk with respect to any class of financial assets or counterparties with the exception of investments *[note 8]*. The Corporation's maximum exposure to credit risk is equal to the carrying value of its financial assets.

Interest rate risk

The Corporation is exposed to interest rate risk in holding certain financial instruments. The Corporation's objective is to minimize net interest expense. The Corporation attempts to minimize interest rate risk by issuing long-term fixed rate debt, and by extending or shortening the term of its short-term money market investments by assessing the monetary policy stance of the Bank of Canada, while ensuring that all payment obligations are met on an on-going basis.

Under the Corporation's Revolving Credit Facility *[note 12]*, the Corporation may obtain short-term borrowings for working capital purposes. These borrowings may expose the Corporation to fluctuations in short-term interest rates (borrowings in the form of prime rate loans in Canadian dollars and BAs and letters of credit). The fee payable for BAs and letters of credit is based on a margin determined by reference to the Corporation's credit rating.

Cash balances, which are not required to meet day-to-day obligations of the Corporation, are either held in account or invested in Canadian money market instruments, with terms of one day to 90 days, exposing the Corporation to fluctuations in short-term interest rates. These fluctuations could impact the level of interest income earned by the Corporation.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

[all tabular amounts in thousands of dollars]

December 31, 2009

Liquidity risk

The Corporation monitors and manages its liquidity risk to ensure access to sufficient funds to meet operational and investing requirements. The Corporation's objective is to ensure that sufficient liquidity is on hand to meet obligations as they fall due while minimizing interest expense. The Corporation has access to credit facilities and monitors cash balances daily to ensure that sufficient levels of liquidity are on hand to meet financial commitments as they come due. Liquidity risks associated with financial commitments are as follows:

December 31, 2009			
	Due within 1 year $	**Due between 1 year and 5 years $**	**Due after 5 years $**
Financial liabilities			
Accounts payable and accrued liabilities	**316,768**	**—**	**—**
Promissory note payable to the City	**—**	**490,115**	**—**
Senior unsecured debentures			
Series 1 – 6.11% due May 7, 2013	**—**	**225,000**	**—**
Series 2 – 5.15% due November 14, 2017	**—**	**—**	**250,000**
Series 3 – 4.49% due November 12, 2019			**250,000**
	316,768	**715,115**	**500,000**

Hedging and Derivative risk

As at December 31, 2009, and as at December 31, 2008, the Corporation has not entered into hedging and derivative financial instruments.

Foreign exchange risk

As at December 31, 2009, the Corporation has limited exposure to the changing values of foreign currencies. While the Corporation purchases goods and services which are payable in U.S. dollars, and purchases U.S. currency to meet the related payables commitments when required, the impact of these transactions is not material to the consolidated financial statements.

20. FINANCIAL GUARANTEES

The City has authorized the Corporation to provide financial assistance to its subsidiaries, and LDC to provide financial assistance to other subsidiaries of the Corporation, in the form of letters of credit and guarantees, for the purpose of enabling them to carry on their businesses up to an aggregate amount of $500,000,000.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
[all tabular amounts in thousands of dollars]

December 31, 2009

21. PAYMENTS IN LIEU OF CORPORATE TAXES

The provision for PILs differs from the amount that would have been recorded using the combined Canadian federal and Ontario statutory income tax rate. Reconciliation between the statutory and effective tax rates is set out below:

Consolidated Statements of income

	2009 $	2008 $
Rate reconciliation		
Income before PILs	**62,555**	51,741
Consolidated Statutory Canadian federal and provincial income tax rate	**33.00%**	33.50%
Expected provision for PILs	**20,643**	17,333
Temporary differences not benefited	**(1,097)**	3,658
Valuation allowance	**1,105**	5,333
Decrease in future tax rates	**374**	—
Change in income tax positions	**(1,256)**	(28,503)
Other	**(27)**	7,924
Provision for PILs	**19,742**	5,745
Effective tax rate	**31.56%**	11.10%
Components of provision for PILs		
Current tax provision	**19,326**	3,881
Future income tax provision related to the origination and reversal of temporary differences	**416**	1,864
Provision for PILs	**19,742**	5,745

Consolidated Balance sheets

Significant components of the Corporation's future income tax assets and liabilities are as follows:

	2009 $	2008 $
Property, plant and equipment and intangible assets	**154,515**	9,910
Regulatory adjustments	**62,737**	—
Post-employment benefits liability	**40,337**	1,921
Other taxable temporary differences	**5,641**	6,886
Non-capital loss carryforwards	**479**	643
Valuation allowance	**(10,560)**	(16,665)
	253,149	2,695

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

[all tabular amounts in thousands of dollars]

December 31, 2009

Presented on the consolidated balance sheets as follows:

	2009 $	2008 $
Future income tax assets, long-term	**253,149**	2,809
Future income tax liabilities, long-term	—	(114)
	253,149	2,695

On January 1, 2009, LDC began to account for the differences between its financial statement carrying value and tax basis of assets and liabilities following the liability method in accordance with CICA Handbook Section 3465 *[note 4[b]]*. As at December 31, 2009, LDC has recorded a future income tax asset of $250,948,000 and a corresponding regulatory liability of $250,948,000.

As at December 31, 2009, the Corporation has accumulated tax losses for PILs purposes of approximately $1,916,000 [December 31, 2008 - $2,218,000], which are available to reduce taxable income in future years.

22. SHARE CAPITAL

Share capital consists of the following:

	2009 $	2008 $
Authorized		
The authorized share capital of the Corporation consists of an unlimited number of common shares		
Issued and outstanding		
1,000 common shares	**567,817**	567,817

Dividends

The shareholder direction adopted by the City with respect to the Corporation provided that the Corporation's board of directors would use its best efforts to ensure that the Corporation met certain financial performance standards, including those relating to credit rating and dividends.

Subject to applicable law, the shareholder direction provides that the Corporation will pay dividends to the City each year amounting to the greater of $25,000,000 or 50% of the Corporation's consolidated net income. The dividends are not cumulative and are payable as follows:

[a] $6,000,000 on the last day of each of the first three fiscal quarters in each year;

[b] $7,000,000 on the last day of the fiscal year; and

[c] the amount, if any, by which 50% of the Corporation's annual consolidated net income for the year exceeds $25,000,000 within ten days after the board of directors of the Corporation approves the Corporation's audited consolidated financial statements for the year.

During 2009, the board of directors of the Corporation declared and paid dividends totalling $25,170,000 [2008 – $116,416,000 to the City, including a $75,000,000 special dividend payment in relation to the sale of all the shares of Telecom in 2008].

23. RELATED PARTIES

For the Corporation, transactions with related parties include transactions with the City. All transactions with the City are conducted at prevailing market prices and normal trade terms.

For the year ended December 31, 2009, LDC provided electricity to the City in the amount of $109,678,000 [2008 - $107,093,000]. As at December 31, 2009, included in "unbilled revenue" is a balance amounting to $9,679,000 [December 31, 2008 - $9,090,000] receivable from the City related to the provision of electricity for the previous months.

For the year ended December 31, 2009, LDC provided relocation services related to the City in the amount of $886,000 [2008 - $991,000]. As at December 31, 2009, included in LDC's "Accounts receivable, net of allowance for doubtful accounts" is $1,183,000 [December 31, 2008 - $4,098,000] receivable from the City related to relocation services and other construction activities.

For the year ended December 31, 2009, TH Energy provided energy management services, street lighting services and consolidated billing services to the City amounting to $20,964,000 [2008 - $19,853,000]. As at December 31, 2009, included in TH Energy's "Accounts receivable, net of allowance for doubtful accounts" is $5,045,000 [December 31, 2008 - $4,884,000] receivable from the City related to these services.

For the year ended December 31, 2009, LDC purchased road cut and other services of $6,873,000 [2008 - $4,877,000] from the City. As at December 31, 2009, included in "Accounts payable and accrued liabilities" is $5,492,000 [December 31, 2008 - $4,514,000] payable to the City related to services received from the City.

For the year ended December 31, 2009, LDC and TH Energy paid property tax expenses to the City of $6,279,000 [2008 - $6,533,000].

On December 31, 2009, the Corporation made the second scheduled payment of $245,058,000 to the City in accordance with the terms of the City Note. As at December 31, 2009, the outstanding principal amount in respect of the City Note was $490,115,000 [December 31, 2008 - $735,173,000] *[note 14]*. For the year ended December 31, 2009, interest of $44,919,000 [2008 - $44,919,000], on the City Note was paid to the City.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
[all tabular amounts in thousands of dollars]

December 31, 2009

24. LEASE COMMITMENTS

Operating lease obligations

As at December 31, 2009, the future minimum annual lease payments under property operating leases with remaining lease terms from one to five years and thereafter are as follows:

	$
2010	**4,506**
2011	**3,952**
2012	**983**
2013	**74**
2014	**80**
Thereafter	**1,574**
Total minimum lease payments	**11,169**

Capital lease obligations

As at December 31, 2009, the future minimum annual lease payments under capital leases with remaining lease terms from one to five years and thereafter are as follows:

	$
2010	**240**
2011	**217**
2012	**135**
2013	**87**
2014 and thereafter	**43**
Total amount of future minimum lease payments	**722**
Less interest	**57**
	665
Current portion *[note 13]*	**218**
Long-term portion *[note 16]*	**447**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

[all tabular amounts in thousands of dollars]

December 31, 2009

25. CONTINGENCIES

a) Legal Proceedings

Late Payment Charges Class Action

On April 22, 2004, in a decision in a class action commenced against The Consumers' Gas Company Limited [now Enbridge Gas Distribution Inc., hereinafter referred to as "Enbridge"], the Supreme Court of Canada [the "Supreme Court"] ruled that Enbridge was required to repay the portion of certain late payment charges collected by it from its customers that were in excess of the interest limit stipulated in section 347 of the *Criminal Code*. Although the claim related to charges collected by Enbridge after the enactment of section 347 of the *Criminal Code* in 1981, the Supreme Court limited recovery to charges collected after the action was initiated in 1994. The Supreme Court remitted the matter back to the Ontario Superior Court of Justice for a determination of the plaintiffs' damages. The parties reached a settlement of this class action. The Ontario Superior Court of Justice has approved this settlement.

On February 4, 2008, the OEB, in response to an application filed by Enbridge, ruled that all of Enbridge's costs related to settlement of the class action lawsuit, including legal costs, settlement costs and interest, are recoverable from ratepayers. The representative plaintiff in the class action lawsuit has made a petition to the Lieutenant Governor in Council ["Cabinet"] under subsection 34(1) of the *Ontario Energy Board Act, 1998*, Schedule B for an order that the matter be submitted back to the OEB for reconsideration. The Cabinet dismissed the petition.

LDC was not a party to the Enbridge class action. It is, however, subject to the two class actions described below in which the issues are analogous.

The first is an action commenced in April 1994 against a predecessor of LDC and other Ontario MEUs under the *Class Proceedings Act, 1992* (Ontario) seeking $500,000,000 in restitution for late payment charges collected by them from their customers that were in excess of the interest limit stipulated in section 347 of the *Criminal Code*. This action is at a preliminary stage. Pleadings have closed but examinations for discovery have not been conducted and the classes have not been certified. After the release by the Supreme Court of its 2004 decision in the Enbridge case, the plaintiffs in this proposed class action indicated their intention to proceed with the litigation.

The second is an action commenced in November 1998 against a predecessor of LDC under the *Class Proceedings Act, 1992* (Ontario) seeking $64,000,000 in restitution for late payment charges collected by it from its customers that were in excess of the interest limit stipulated in section 347 of the *Criminal Code*. This action is also at a preliminary stage. Pleadings have closed and examinations for discovery have been conducted but, as in the first action, the classes have not been certified.

The claims made against LDC and the definitions of the plaintiff classes are identical in both actions. As a result, any damages payable by LDC in the first action would reduce the damages payable by LDC in the second action, and vice versa.

The determination of whether the late payment charges collected by LDC from its customers were in excess of the interest limit stipulated in section 347 of the *Criminal Code* is fact specific in each circumstance. Also, decisions of the OEB are fact specific in each circumstance and the decision of the OEB in respect of Enbridge's application for recovery of costs related to the settlement is not necessarily determinative of the outcome of any similar application which LDC may make to the OEB in the future.

2 Secord Avenue

An action was commenced against LDC in September 2008 in the Ontario Superior Court of Justice under the *Class Proceedings Act, 1992* (Ontario) seeking damages in the amount of $30,000,000 as compensation for damages allegedly suffered as a result of a fire and explosion in an underground vault at 2 Secord Avenue on July 20, 2008. This action is at a preliminary stage. The statement of claim has been served on LDC, a statement of defence has been filed, and a certification order issued. Affidavits of Documents have been produced by LDC to the other parties and examinations for discovery have commenced and are continuing. Given the preliminary status of this action, it is not possible to reasonably quantify the effect, if any, of this action on the financial performance of the Corporation. If damages were awarded, LDC would make a claim under its liability insurance which the Corporation believes would cover any damages which may become payable by LDC in connection with the action.

Another action was commenced against LDC in February 2009 in the Ontario Superior Court of Justice seeking damages in the amount of $20,000,000 as compensation for damages allegedly suffered as a result of a fire and explosion in an underground vault at 2 Secord Avenue on July 20, 2008. This action is at a preliminary stage. The statement of claim has been served on LDC, a statement of defence has been filed, and a certification order issued. Affidavits of Documents have been produced by LDC to the other parties and examinations for discovery have commenced and are continuing. Given the preliminary status of this action, it is not possible to reasonably quantify the effect, if any, of this action on the financial performance of the Corporation. If damages were awarded, LDC would make a claim under its liability insurance which the Corporation believes would cover any damages which may become payable by LDC in connection with the action.

By order of the court, these two actions, together with a third smaller non-class action commenced in April 2009 involving the same incident, will be tried at the same time or consecutively. Consequently, documentary discovery and examinations for discovery will be joined for all three actions.

3650 Kingston Road

An action was commenced against LDC in March 2009 in the Ontario Superior Court of Justice under the *Class Proceedings Act, 1992* (Ontario) seeking damages in the amount of $30,000,000 as compensation for damages allegedly suffered as a result of a fire and explosion in the electrical room at 3650 Kingston Road on March 19, 2009. This action is at a preliminary stage. A statement of claim has been served on LDC but a statement of defence has not been filed. The proceedings of other parties to the action have revealed that the damages are likely to have been caused by a party other than LDC and LDC is making a motion to have LDC dismissed from the action. While it is not possible at this time to state conclusively, it is unlikely that LDC will be found liable for damages. If damages were awarded against LDC, LDC would make a claim under its liability insurance which LDC believes would cover such damages. Accordingly, this action is not likely to have a material effect on the financial performance of the Corporation.

2369 Lakeshore Boulevard West

A third party action was commenced against LDC in October 2009 in the Ontario Superior Court of Justice under the *Class Proceedings Act, 1992* (Ontario) seeking damages in the amount of $30,000,000 as compensation for damages allegedly suffered as a result of a fire in the electrical room at 2369 Lakeshore Boulevard West on March 19, 2009. This action is at a preliminary stage. A third party claim has been served on LDC but a statement of defence to the third party claim has not been filed. Accordingly, given the preliminary status of this action, it is not possible at this time to reasonably quantify the effect, if any, of this action on the financial performance of the

Corporation. If damages were awarded, LDC would make a claim under its liability insurance which the Corporation believes would cover any damages which may become payable by LDC in connection with the action.

Another third party action was commenced against LDC in October 2009 in the Ontario Superior Court of Justice seeking damages in the amount of $30,000,000 as compensation for damages allegedly suffered as a result of a fire in the electrical room at 2369 Lakeshore Boulevard West on March 19, 2009. This action is at a preliminary stage. A third party claim has been served on LDC and a statement of defence to the third party claim has not been filed. Accordingly, given the preliminary status of this action, it is not possible at this time to reasonably quantify the effect, if any, of this action on the financial performance of the Corporation. If damages were awarded, LDC would make a claim under its liability insurance which the Corporation believes would cover any damages which may become payable by LDC in connection with the action.

b) OEB PILs Proceeding

In 2009, the OEB commenced its review of the PILs variances accumulated in regulatory variance accounts for the period from October 1, 2001 to April 30, 2006 for all MEUs. The current proceeding is expected to provide direction regarding the interpretation of the rules issued by the OEB. The outcome of this proceeding could have a material impact on the financial position of the Corporation.

c) Payments in Lieu of Additional Municipal and School Taxes

The Ministry of Revenue has issued assessments in respect of payments in lieu of additional municipal and school taxes under s.92 of the *Electricity Act, 1998* that are in excess of the amounts LDC believes are payable. The dispute arose as a result of inaccurate information incorporated into Ontario Regulation 224/00, correction of which has been requested by LDC.

The balance assessed by the Ministry of Revenue above the balance accrued by the Corporation amounts to $8,660,000 as at December 31, 2009. The Corporation has been proactive with the Ministry of Revenue and the Ministry of Finance to resolve this issue. However, there can be no assurance that the Corporation will not have to pay the full assessed balance in the future.

26. NET INCOME PER SHARE

The weighted daily average number of shares outstanding was 1,000 as at December 31, 2009 and 2008, for the purpose of determining basic and fully diluted net income per share from continuing and discontinued operations. Basic and fully diluted net income per share from continuing and discontinued operations were determined by dividing the net income for the year by the weighted daily average number of shares outstanding.

27. DISCONTINUED OPERATIONS

On July 31, 2008, the Corporation sold all the shares of Telecom to Cogeco Cable Canada Inc. for cash consideration of $200,000,000. In connection with this transaction, the Corporation recorded a net gain of $118,673,000 in the third quarter of 2008, and recorded an unfavourable post-closing adjustment of $1,905,000 for the year ended December 31, 2009. The results of operations and financial position of Telecom have been segregated and presented as discontinued operations in the consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

[all tabular amounts in thousands of dollars]

On April 30, 2009, EBT Express, an equal partnership between the Corporation's wholly owned subsidiary 1455948 Ontario Inc. and OPG EBT Holdco Inc., sold its interest in The SPi Group ["SPi"] to ERTH Corporation for cash consideration of approximately $5,200,000 subject to post-closing adjustments and transaction costs. The Corporation's share of the sale proceeds from this transaction as it relates to 1455948 Ontario Inc. was approximately $2,600,000. In connection with this transaction and other activities related to this business, the Corporation recorded a net gain of $1,220,000 in the second quarter of 2009. The results of operations and financial position of SPi have been segregated and presented as discontinued operations in the consolidated financial statements.

Current assets from discontinued operations relate to SPi and amount to $514,000 as at December 31, 2009 [December 31, 2008 - $nil]. Current liabilities from discontinued operations relate to Telecom and amounts to $1,549,000, as at December 31, 2009 [December 31, 2008 - $890,000].

For the years ended December 31, 2009 and December 31, 2008, the following revenues and expenses of SPi and Telecom have been reclassified from continuing operations to discontinued operations:

	2009 $	2008 $
Revenues	**850**	2,606
Costs		
Operating expenses	**971**	2,043
Depreciation and amortization	**101**	188
Other	**(2)**	(22)
	(220)	397
Provision for (recovery of) PILs	**13**	(48)
Minority interest	**(78)**	148
Income (loss) from discontinued operations - SPi	**(155)**	297
Income (loss) from discontinued operations - Telecom	**(1,905)**	4,046
Gain on sale of SPi – net of tax	**1,380**	—
Gain on sale of Telecom – net of tax	—	118,673
Income (loss) from discontinued operations - net of tax	**(680)**	123,016

28. SEGMENT REPORTING

The designation of the segments has been based on a combination of the regulatory status and the nature of products and services provided. The Corporation has two reportable segments:

[a] **Electricity Distribution**
The regulated business which consists of the electricity distribution business and conservation activities including OPA contracts of LDC; and

[b] **Non-regulated**
The non-regulated business of TH Energy consists primarily of the delivery of street lighting and expressway lighting services and energy efficiency products and services.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

[all tabular amounts in thousands of dollars]

December 31, 2009

Segment information is as follows:

	2009 $	2008 $
Electricity distribution		
Revenues	**2,438,907**	2,349,547
Purchased power and other	**1,946,812**	1,869,557
Operating expenses	**195,460**	182,363
Depreciation and amortization	**155,468**	149,019
Income before interest and provision for PILs	**141,167**	148,608
Interest income	**1,257**	8,897
Interest expense	**70,181**	72,402
Provision for PILs	**21,242**	8,969
Income from continuing operations	**51,001**	76,134
Non-regulated		
Revenues	**22,827**	32,135
Purchased power and other	**6,845**	14,761
Operating expenses	**15,492**	21,154
Depreciation and amortization	**7,502**	7,140
Loss before interest, change in fair value of investments and recovery of PILs	**(7,012)**	(10,920)
Interest income	**1,950**	3,431
Interest expense	**3,577**	2,352
Change in fair value of investments	**(1,049)**	(22,033)
Recovery of PILs	**(1,500)**	(3,224)
Loss from continuing operations	**(8,188)**	(28,650)
Intersegment eliminations		
Revenues	**(63)**	(1,598)
Purchased power and other	—	(22)
Operating expenses	**(63)**	(88)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

[all tabular amounts in thousands of dollars]

December 31, 2009

	2009 $	2008 $
Total		
Revenues	**2,461,671**	2,380,084
Purchased power and other	**1,953,657**	1,884,296
Operating expenses	**210,889**	203,429
Depreciation and amortization	**162,970**	156,159
Income before interest, change in fair value of investments and provision for PILs	**134,155**	136,200
Interest income	**3,207**	12,328
Interest expense	**73,758**	74,754
Change in fair value of investments	**(1,049)**	(22,033)
Provision for PILs	**19,742**	5,745
Income from continuing operations	**42,813**	45,996

	2009 $	2008 $
Expenditures on property, plant and equipment and intangible assets		
Electricity distribution	**241,686**	205,712
Non-regulated	**7,619**	8,869
Total	**249,305**	214,581

	2009 $	2008 $
Assets		
Electricity distribution	**2,819,230**	2,506,141
Non-regulated	**268,781**	300,071
Intersegment eliminations	**(29,298)**	(26,400)
Discontinued operations	**514**	—
Total	**3,059,227**	2,779,812

All revenues, costs and assets, as the case may be, are earned, incurred or held in Canada.

29. COMPARATIVE CONSOLIDATED FINANCIAL STATEMENTS

The comparative consolidated financial statements have been reclassified from statements previously presented to conform to the presentation of the 2009 consolidated financial statements.

30. SUBSEQUENT EVENTS

a) Late Payment Charges Class Action

On January 15, 2010, a conditional settlement was reached for both actions pursuant to which the defendants would pay the amount of $17,000,000 plus costs and taxes in settlement of all claims. The amount paid by each MEU will be its proportionate share of the settlement amount based on its percentage of distribution service revenue over the period for which it has exposure for repayment of late payment penalties exceeding the interest rate limit in the *Criminal Code*. While the amounts have not yet been determined, it is anticipated that LDC's share of the settlement amount will be in the range of $7,500,000 to $9,500,000. The settlement is conditional upon a sufficient number of MEUs participating so as to collect the full amount of the settlement funds payable to the plaintiffs. It is also conditional upon court approval. All the MEUs involved in the settlement, including LDC, will request an order from the OEB allowing for the future recovery from customers of all costs related to the proposed settlement. LDC has not accrued any liabilities in relation to this proposed settlement. There is no guarantee that the OEB will allow for total or partial recovery of such costs in the future. The outcome of the OEB decision in this regard could have an adverse material impact on the consolidated results of operations and financial position of the Corporation in the future.

b) 2010 Electricity Distribution Rates

On February 4, 2010, the OEB tentatively accepted a settlement proposal agreed to by LDC and various intervening parties. The settlement proposal captured a majority of issues, and provides for a 2010 capital budget of $350,000,000 with a variance account to capture up to an additional $27,800,000 of capital expenditures and operations, maintenance and administration expenditures of $204,100,000. The settlement proposal did not settle issues relating to cost of capital (including applicability of new ROE guidelines to LDC), suite metering, and distributed generation, which are subject to a decision by the OEB in the first quarter of 2010. The final disposition of these matters could have a material impact on the final settlement.

c) Street Lighting Activities

On June 15, 2009, the Corporation filed an application with the OEB seeking an electricity distribution license for a new wholly-owned legal entity to which the Corporation intends to transfer the street lighting assets of TH Energy. Concurrently, the Corporation filed another application with the OEB seeking approval for the merger of LDC and the new legal entity. The main objective of these applications is to transfer the street lighting assets to the regulated electricity distribution activities of LDC to increase the overall safety of the related infrastructure.

On February 11, 2010, the OEB issued its decision in regards to these applications. In its decision, the OEB agreed, that under certain conditions, the treatment of certain types of street lighting assets as regulated assets is justified. The OEB ordered the Corporation to provide a detailed valuation of the street lighting assets and to perform an operational review to determine which assets could become regulated assets. The Corporation is currently evaluating the impact of this decision on its regulated and unregulated businesses and whether to transfer the street lighting assets to LDC.

d) Dividends

On March 5, 2010, the board of directors of the Corporation declared dividends in the amount of $6,000,000 with respect to the first quarter of 2010, payable to the City on March 31, 2010.