



## REPORT FOR ACTION WITH CONFIDENTIAL ATTACHMENT

### Toronto Hydro Corporation - Annual General Meeting and 2018 Audited Financial Statements

**Date:** June 19, 2019

**To:** Executive Committee

**From:** City Manager and Chief Financial Officer and Treasurer

**Wards:** All Wards

#### **REASON FOR CONFIDENTIAL INFORMATION**

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The attachments to this report involves the security of property belonging to the City of Toronto or Toronto Hydro Corporation.

This report deals with personal matters about an identifiable person.

#### **SUMMARY**

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This report transmits materials submitted by the Board of Directors of Toronto Hydro Corporation to the City. No independent review or analysis has been performed by City staff.

This report contains recommendations for actions necessary to comply with the requirements of the Business Corporations Act, (Ontario) R.S.O. 1990, c.B.16 (OBCA) for holding the Annual General Meeting of the Shareholder of Toronto Hydro Corporation (THC) including receipt of THC's audited annual consolidated financial statements for 2018 and appointment of the auditor for THC for 2019.

This report also contains recommendations for receipt at the Annual General Meeting of the Shareholder of THC of other reports provided by THC as required by the Amended and Restated Shareholder Direction Relating to THC (Shareholder Direction) which, in addition to the OBCA requirements, include:

- THC's annual report, environmental performance report and annual information form;
- THC's report to the Shareholder, consolidated and non-consolidated financial statements and financial statements for its subsidiary companies. Note that THC has advised the City that Attachments 7, 8, and 9 are confidential due to: the security of

the property of the City, and securities requirements arising from THC's status as an offering corporation under the OBCA, THC's status as a reporting issuer under the Securities Act (Ontario), R.S.O. 1990, c.S.5, and the application by the Ontario Securities Commission of National Instrument 51-102; and

- THC's disclosure of executive compensation in two parts, with the part in Attachment 6b being confidential as it includes personal information about identifiable individuals.

THC's Shareholder Direction can be found at <https://www.toronto.ca/wp-content/uploads/2018/12/8cdc-THC-Shareholder-Direction-Executed-2013-Amended-2017.pdf>

Subsection 94 (1) of the OBCA requires that the directors of THC call an annual meeting of its Shareholder by no later than fifteen months after holding the last preceding annual meeting, which was held by City Council at its meeting of July 23, 24, 25, 26, 27 and 30, 2018.

## **RECOMMENDATIONS**

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The City Manager and Chief Financial Officer and Treasurer recommend that:

1. City Council treat the portion of the City Council meeting at which this Report is being considered as the Annual General Meeting of the Shareholder for Toronto Hydro Corporation, and:

- a. approve the "Resolution of the Sole Shareholder Re-appointing Auditor" in Attachment 1 Appendix A in order to re-appoint KPMG LLP, Chartered Accountants, as the auditor for THC for 2019 until the close of the next annual meeting of the Shareholder, or until a successor is appointed, at such remuneration as may be fixed by the Corporation's Board;
- b. receive the "Toronto Hydro Corporation 2018 Annual Report, Financial Report, and Consolidated Financial Statements," the "Toronto Hydro Corporation Annual Information Form 2018," the "Toronto Hydro Corporation Environmental Performance Report 2018," the "Toronto Hydro Corporation CEO and CFO Certifications of Annual Filings 2018," the "Toronto Hydro Corporation First Quarter Financial Report 2019," and the "Toronto Hydro Corporation Statement of Board Remuneration and Expenses 2018," forming Attachments 2, 3, 4, 5, 10, and 11 respectively to this Report;
- c. receive the "Toronto Hydro Corporation Shareholder Report 2018, including Non-Consolidated Financial Statements," the "Toronto Hydro-Electric System Limited Financial Statements 2018 and 2017," and the "Toronto Hydro Energy Services Inc. Financial Statements 2018 and 2017," forming Confidential Attachments 7, 8 and 9 respectively to this Report; and

d. receive the two-part report "Toronto Hydro Corporation Executive Compensation Disclosure 2018" forming Attachment 6a and Confidential Attachment 6b to this Report.

2. City Council direct that Confidential Attachments 7, 8, and 9 remain confidential in their entirety due to the security of the property of the City and securities requirements arising from Toronto Hydro Corporation's status as an offering corporation under the Business Corporations Act, (Ontario) R.S.O. 1990, c.B.16, Toronto Hydro Corporation's status as a reporting issuer under the Securities Act, (Ontario) R.S.O. 1990, c.S.5, and the application by the Ontario Securities Commission of National Instrument 51-102.

3. City Council direct that Confidential Attachment 6b remain confidential in its entirety as it deals with personal information about identifiable individuals.

4. City Council direct the City Clerk to forward a copy of the "Toronto Hydro Corporation Consolidated Financial Statements December 31, 2018 and 2017", included as part of Attachment 2 to this Report, to the Audit Committee for information.

## **FINANCIAL IMPACT**

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THC paid the City \$93.9 million in dividends in 2018, based on 60% of the prior year's net income after net movements in regulatory balances, in accordance with the City's Shareholder Direction to THC. The 2019 City Council-Approved Operating Budget included receipt of dividends in 2019 from THC totalling \$97.8 million. Based on THC actual financial results for the year ended December 31, 2018, the City anticipates receiving dividends totaling \$100.38 million in 2019, including dividends already received on March 29, 2019 of \$25.095 million.

The Chief Financial Officer and Treasurer has reviewed this Report and agrees with the financial impact information.

## **DECISION HISTORY**

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At the Annual Meeting of the Shareholder on July 23, 24, 25, 26, 27 and 30, 2018, City Council adopted with amendments item EX35.14 Toronto Hydro Corporation Annual General Meeting and 2017 Annual Audited Financial Statements.

<http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2018.EX35.14>

## COMMENTS

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### **Appointment of Auditor**

Section 149 (2) of the OBCA requires that THC's Shareholder at each annual meeting appoint one or more auditors to hold office until the close of the next annual meeting, and allows the Shareholder to authorize the directors to fix the auditor's remuneration.

The auditor is selected by THC based on a competitive process, subject to Shareholder approval. KPMG LLP, Chartered Accountants, has been selected by THC as the external auditor for the 2019 calendar year and for completion of the 2019 year-end audit in 2020. It is recommended that City Council, acting as Shareholder, approve the Shareholder Resolution in Attachment 1 Appendix A to this Report, which includes the Shareholder Resolution to appoint KPMG LLP, Chartered Accountants, as the auditor for THC for 2019 and to authorize the Board of Directors of THC to fix the auditor's remuneration.

### **Achievements and Performance in 2018**

Section 9.8 of the THC Shareholder Direction requires THC to deliver an annual report detailing THC's accomplishments, Business Plan status, environmental performance data, executive compensation information, and the financial statements noted above.

THC's 2018 Annual Report, Attachment 2, provides information on THC's operational performance and achievements in 2018, as well as its corporate governance. THC's Environmental Performance Report, Attachment 4, provides details on the Corporation's environmental performance.

### **Summary – 2018 Audited Consolidated Financial Statements**

Subsection 154 (1) of the OBCA requires that the Shareholder receive THC's audited annual financial statements and the report of the auditor at the annual meeting of the Shareholder. Section 9.7 of the THC Shareholder Direction requires THC to deliver its audited consolidated annual financial statements for THC and its active subsidiary companies to the Shareholder within three months after the end of each fiscal year.

THC's audited consolidated annual financial statements for 2018 are included as part of Attachment 2 to this Report and are filed with the City Clerk's office, posted on THC's website and posted on the SEDAR (System for Electronic Document Analysis and Retrieval) website for Canadian public securities documents.

The audited financial statements reflect the consolidated operations of THC, and of its wholly-owned subsidiaries:

- Toronto Hydro-Electric System Limited (THESL), an electricity distribution company to approximately 772,000 customers, which makes up the majority of THC's business; and

- Toronto Hydro Energy Services Inc. (THESI), a smaller subsidiary having only a minor impact on THC's financial results. The business of this subsidiary includes the provision of street lighting services to the City of Toronto.

Attachment 5 to this Report provides the Ontario Security Commission forms that certify THC's filings. THC's 2018 Report to the Shareholder and its confidential financial statements, including the unconsolidated statements of THC and its subsidiary companies, are provided in Confidential Attachments 7, 8, and 9. A summary of public financial data for 2018 and 2017 is provided below.

*Table 1 - THC Audited Consolidated Key Financial Results (\$millions)*

	2018	2017	Year over Year Change
<b>Income Statement for the year ended December 31</b>			
Energy Sales	2,704.1	2,810.2	(106.1)
Distribution Revenue	674.2	724.2	(50.0)
Other Revenue	94.4	107.7	(13.3)
<b>Total Revenue</b>	<b>3,472.7</b>	<b>3,642.1</b>	<b>(169.4)</b>
<i>Less:</i>			
Energy Purchases	2,646.3	2,855.9	(209.6)
Operating Expenses	307.5	293.0	14.5
Depreciation & Amortization	238.3	224.2	14.1
<b>Operating Income</b>	<b>280.6</b>	<b>269.0</b>	<b>11.6</b>
Finance Costs	74.6	77.7	(3.1)
Income Taxes	82.4	44.7	37.7
Gain on disposal of Property, Plant & Equipment	108.6	9.8	98.8
Change in Regulatory Balances*	(64.9)	0.1	(65)
<b>Net Income after Net Movements in Regulatory Balances</b>	<b>167.3</b>	<b>156.5</b>	<b>10.8</b>
<b>Balance Sheet Items as of December 31</b>			
Capital Expenditures	511.3	552.9	(41.6)
<b>Total Assets and Regulatory Balances*</b>	<b>5,360.1</b>	<b>5,226.2</b>	<b>133.9</b>
Debentures	2,034.9	2,034.0	

	2018	2017	Year over Year Change
Short Term Debt (not including current portion of debentures)	125.6	170.7	
Total Liabilities	3,348.4	3,305.8	42.6
Shareholder's Equity	1,833.5	1,760.4	73.1
Total Debt/Total Capitalization	54.1%	55.6%	

\* Regulatory balances are cash flows to be recovered from, or refunded to customers, in accordance with OEB orders

## Income Statement

THC consolidated net income after movements in regulatory balances for fiscal 2018, at \$167.3 million, demonstrated an increase of 6.9% over fiscal 2017. In 2018, THC had total revenues of \$3.5 billion, a decrease over 2017 (\$3.6 billion). Total revenues include the following:

- Energy revenues, at \$2.7 billion in 2018, were less than 2017 (\$2.6 billion). However, the cost of energy is a pass-through for THC.
- While consumption and electricity distribution rates were both slightly higher in 2018, they were offset by lower OEB rate-riders (or surcharges), resulting in lower overall distribution revenues. In 2018, electricity distribution revenues were \$674.2 million, as compared with 2017 (\$724.2 million).
- Other revenue includes revenue from services ancillary to electricity distribution, delivery of street lighting services, pole and duct rentals, other regulatory service charges, capital contributions and CDM programs. Other revenues decreased in 2018 revenue, to \$94.4 million (vs 2017: \$107.7 million), due primarily to the recognition of a Conservation and Demand Management mid-term incentive in 2017.
- In 2018, operating expenditures (\$307.5 million) were greater than in 2017 (\$293 million) primarily as a result of higher distribution maintenance programs driven by storm events, and a higher demand for ancillary services, offset in part by lower administrative and other costs.

## Balance Sheet

As at December 31, 2018, THC had total assets and regulatory balances of \$5.36 billion, a slight increase over 2017 (\$5.23 billion). Total Liabilities and Shareholder's Equity also increased slightly over 2018. However, THC's total debt to total capitalization ratio decreased to 54.1% as at 2018 fiscal year end.

THC's credit ratings remain at the same levels as the previous fiscal year, and are provided in the table below.

*Table 2 – THC Credit Ratings, December 31, 2018*

	<b>Issuer Rating</b>	<b>Senior Unsecured Debentures</b>
DBRS	A stable	A stable
S&P	A stable	A

### **Subsequent to Year End**

THC first quarterly financial report for 2019 is Attachment 10 to this report. For the first quarter ended March 31, 2019, THC reported net income after net movements in regulatory balances of \$42.6 million, at the same level as in the first fiscal quarter of 2018 (\$42.5 million).

Total assets increased slightly to \$5.4 billion as at March 31, 2019, compared to \$5.36 billion as at 2018 fiscal year end. This was primarily the result of an increased book value of property, plant and equipment as THC continued to make capital expenditures for the purpose of replacing its aging electricity distribution infrastructure.

### **2018 Annual Information Form**

The Annual Information Form (AIF), Attachment 3, is a public document published annually by THC as a public debt issuer in accordance with Ontario Securities Commission requirements. The 2018 AIF is filed with the City Clerk's office, posted on THC's website and posted on the SEDAR website for Canadian public securities documents.

### **Executive Compensation**

The compensation of Named Executive Officers (NEOs) is set out in the AIF in Attachment 3. In addition to the executive compensation reported through the AIF, City Council as the Shareholder has also directed that executive compensation, including compensation for executives other than NEOs, be disclosed annually to City Council as permitted by law.

This information is provided in two parts. The compensation disclosure for NEOs, which is already public information through the AIF, forms Attachment 6a to this Report. Reporting of additional executive compensation information includes personal information about identifiable individuals and this information is contained in Confidential Attachment 6b to this Report.

### **Rate Application**

In August 2018, THESL filed a rate application to the OEB for the period of 2020 to 2024. The application seeks approval of Toronto Hydro's 2020 test-year revenue requirement on a cost of service basis and subsequent annual rate adjustments based on a custom index specific to Toronto Hydro for the period commencing on January 1, 2021 and ending on December 31, 2024. The rate application requests approvals to fund capital expenditures of approximately \$2.8 billion over the 2020-2024 period.

THESL submitted a rate application in 2014 to the OEB for the period of 2015-2019. On August 23, 2017, THESL filed its 2018 rate application seeking OEB's approval to finalize distribution rates and other charges for the period commencing on January 1, 2018 and ending on December 31, 2018. On December 14, 2017, the OEB issued a decision and rate order approving THESL's 2018 rates, with an effective date of January 1, 2018, and the disposition of certain deferral and variance accounts.

## **CONTACT**

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## **SIGNATURE**

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Heather Taylor  
Chief Financial Officer and Treasurer

Chris Murray  
City Manager

## **ATTACHMENTS**

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Attachment 1 - THC Report on the 2019 Annual Shareholder Meeting

Attachment 1 Appendix A - Resolution of the Shareholder Re-appointing Auditor

Attachment 2 - THC 2018 Annual Report, Financial Report, and Consolidated Financial Statements

Attachment 3 - THC Annual Information Form 2018

Attachment 4 - THC Environmental Performance Report 2018

Attachment 5 - THC CEO and CFO Certification of Annual Filings 2018



Attachment 6a - THC Executive Compensation Disclosure 2018 (Part 1, NEOs)

Confidential Attachment 6b - THC Executive Compensation Disclosure 2018 (Part 2, All Executives)

Confidential Attachment 7 - THC Shareholder Report 2018, including Non-Consolidated Financial Statements

Confidential Attachment 8 - THESL Financial Statements 2018 and 2017

Confidential Attachment 9 - THESI Financial Statements 2018 and 2017

Attachment 10 - THC First Quarter Financial Report 2019

Attachment 11 - THC Statement of Board Remuneration and Expenses 2018