REPORT FOR ACTION WITH
CONFIDENTIAL ATTACHMENT

Toronto Hydro Corporation - Annual General Meeting
and 2016 Audited Financial Statements

Date: June 1, 2017
To: Executive Committee
From: City Manager and Deputy City Manager & Chief Financial Officer
Wards: All Wards

REASON FOR CONFIDENTIAL INFORMATION

This report involves the security of property belonging to the City or one of its agencies or corporations.

This report deals with personal matters about an identifiable person.

SUMMARY

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 2016 and appointment of the auditor for THC for 2017.

This report also contains recommendations for receipt at the Annual General Meeting of the Shareholder of THC, 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, 9 and 10 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 11(b) being confidential as it includes personal information about identifiable individuals.

**RECOMMENDATIONS**

The City Manager and Deputy City Manager & Chief Financial Officer recommend that:

1. City Council treat that 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. adopt the recommendations of the "Toronto Hydro Corporation Report" dated May 18, 2017 and approve the Shareholder Resolution in Appendix A of Attachment 1 to this Report in order to re-appoint KPMG LLP, Chartered Accountants, as the auditor for THC for 2017 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 2016 Annual Report – Powering Toronto's Future", the "Toronto Hydro Corporation 2016 Financial Report for the year ended December 31, 2016" including the Consolidated Financial Statements of Toronto Hydro Corporation for the years ended December 31, 2016 and 2015 and the Auditors' Report thereon, the "Toronto Hydro Corporation Annual Information Form for the year ended December 31, 2016", the "Toronto Hydro 2016 Environmental Performance Report", the "Toronto Hydro Corporation CEO and CFO Certification of Annual Filings", and the "Toronto Hydro Corporation First Quarter Financial Report dated March 31, 2017", including unaudited Consolidated Financial Statements of Toronto Hydro Corporation for the three months ended March 31, 2017, forming Attachments 2, 3, 4, 5, 6 and 12 respectively to this Report;

   c. receive the "Toronto Hydro Corporation Report to the Shareholder for the year ended December 31, 2016", the "Non-Consolidated Financial Statements of Toronto Hydro Corporation for the years ended December 31, 2016 and 2015", the "Financial Statements of Toronto Hydro-Electric System Limited for the years ended December 31, 2016 and 2015" and the Auditors' Report thereon, the "Financial Statements of Toronto Hydro Energy Services Inc. for the years ended December 31, 2016 and 2015" and the Auditors’ Report thereon, forming Confidential Attachments 7, 8, 9 and 10 respectively to this Report; and

   d. receive the two-part report "Executive Compensation Disclosure Toronto Hydro Corporation 2016", forming Attachment 11(a) and Confidential Attachment 11(b) to this Report.

2. City Council direct that Confidential Attachments 7, 8, 9 and 10 remain confidential in their entirety due to the security of the property of the City and securities

3. City Council direct that Confidential Attachment 11(b) 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, 2016 and 2015", included as part of Attachment 3 to this Report, to the Audit Committee for information.

FINANCIAL IMPACT

THC paid the City $63.35 million in dividends in 2016, in accordance with the City’s Shareholder Direction to THC. The 2017 City Council-Approved Operating Budget included receipt of dividends in 2017 from THC totalling $75 million, which includes THC dividends already received by the City of $6.25 million on March 31, 2017.

The Deputy City Manager & Chief Financial Officer has reviewed this Report and agrees with the financial impact information.

DECISION HISTORY


That portion of the City Council meeting of June 10-12, 2015, where Item EX6.4 was approved by City Council with amendments, was considered the previous Annual General Meeting and 2014 Annual Report and 2015 Annual Audited Financial Statements of the Shareholder for Toronto Hydro Corporation: http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2015.EX6.4

At its meeting of May 7-10, 2013, City Council in EX31.7 approved the Amended and Restated Shareholder Direction Relating to THC: http://www1.toronto.ca/City%20Of%20Toronto/City%20Manager's%20Office/Agencies%20and%20Corporations/Files/THC%20Amended%20Restated%20Shareholder%20Direction_Final%20May%202013.pdf
ISSUE BACKGROUND

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. Subsection 94 (1) 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 12, 13, 14 and 15, 2016.

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.

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.

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 audited consolidated annual financial statements for 2016 are included as part of Attachment 3 to this Report and are filed with the City Clerk's office, posted on THC's website and posted on the SEDAR website for Canadian public securities documents.

The Annual Information Form ("AIF") is a public document published annually by THC as a public debt issuer in accordance with Ontario Securities Commission requirements. The 2016 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.

COMMENTS

1. Appointment Of Auditor

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 external auditor for the 2017 calendar year and for completion of the 2017 year-end audit in 2018. It is recommended that City Council, acting as Shareholder, approve the Shareholder Resolution in Appendix A to THC's Report forming Attachment 1 to this Report, which includes the Shareholder Resolution to appoint KPMG LLP, Chartered Accountants, as the auditor for THC for 2017 and to authorize the Board of Directors of THC to fix the auditor's remuneration.
2. Key Achievements In 2016

THC's 2016 Annual Report, Powering Toronto's Future, provides information on THC's corporate governance and contains highlights on THC's operational performance. Key achievements by THC in 2016 include the following:

- Served approximately 761,000 residential, commercial and industrial customers.
- For the year ended December 31, 2016, THC generated a net income of $151.4 million and paid $63.35 million in dividends to the City of Toronto.
- Invested $551.7 million to renew aging infrastructure, address reliability and safeguard the system against extreme weather events. As a result, since 2010 average service interruptions have improved by 21% and average duration of interruptions is down by 26%.
- On June 14, 2016, THC issued $200 million of 2.52% senior unsecured debentures at a price of $999.84 per $1,000 principal amount due August 25, 2026.
- Improved customer service through call centre and outage communications enabling a 16% increase in electronic engagement, and resolving 86% of customer issues during their first call.
- Continued focus on innovation to drive towards a smart city through leading edge initiatives including installing photovoltaic (PV) panels on municipal buildings, and moving towards electrification of the city.
- THC raised $800,000 through partners and sponsors at the annual golf tournament in support of the Ross Tilley Burn Centre at Sunnybrook Hospital, and raised more than $144,000 for United Way Toronto and York Region.
- In November 2016, THC was awarded the Canadian Electricity Association (CEA) 2016 Integrated Approach to Sustainability Award in recognition of the integration of sustainability into its corporate culture and business strategy.


The Consolidated Audited Financial Statements for THC for the fiscal year ended December 31, 2016 are provided in Attachment 3 to this Report. These financial results reflect the consolidated operations of THC, and its wholly-owned subsidiaries: Toronto Hydro-Electric System Limited, an electricity distribution company which makes up the majority of THC’s business; and Toronto Hydro Energy Services Inc., which provides street lighting services to the City of Toronto, and is the smaller subsidiary, having only a minor impact on THC’s financial results.

Attachment 6 to this Report provides the Ontario Security Commission forms which certify the THC filings. THC’s 2016 Report to the Shareholder and THC's confidential financial statements, including unconsolidated statements relating to its subsidiary companies and the holding company are provided in Confidential Attachments 7, 8, 9 and 10 to this Report.
A summary of public financial data for 2016 and 2015 is provided below.

### THC Audited Consolidated Key Financial Results

<table>
<thead>
<tr>
<th></th>
<th>2016</th>
<th>2015</th>
<th>Change Yr over Yr</th>
<th>% Change</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Balance Sheet Items as at Dec 31</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Capital Expenditures</td>
<td>551.7</td>
<td>537.2</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total Assets and Regulatory Balances*</td>
<td>4,954.4</td>
<td>4,686.9</td>
<td>267.5</td>
<td>5.7%</td>
</tr>
<tr>
<td>Long Term Debt- Debentures</td>
<td>1,834.8</td>
<td>1,885.1</td>
<td></td>
<td></td>
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<tr>
<td>Short Term Debt (including current portion of debentures)</td>
<td>517.9</td>
<td>338.2</td>
<td></td>
<td></td>
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<tr>
<td>Total Liabilities</td>
<td>3,356.1</td>
<td>3,174.4</td>
<td>181.7</td>
<td>5.7%</td>
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<tr>
<td>Shareholder's Equity</td>
<td>1,428.9</td>
<td>1,340.9</td>
<td>88.0</td>
<td>6.6%</td>
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<tr>
<td>Regulatory credit balances*</td>
<td>169.4</td>
<td>171.6</td>
<td></td>
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</tbody>
</table>

<table>
<thead>
<tr>
<th></th>
<th>2016</th>
<th>2015</th>
<th>Change Yr over Yr</th>
<th>% Change</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Income Statement for the year ended Dec 31</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Energy Sales</td>
<td>3,306.2</td>
<td>2,925.6</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Distribution Revenue</td>
<td>647.9</td>
<td>555.4</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Other</td>
<td>75.9</td>
<td>58.9</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Total Revenues</strong></td>
<td>4,030.0</td>
<td>3,539.9</td>
<td>490.1</td>
<td>13.8%</td>
</tr>
<tr>
<td>Less:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Energy purchases</td>
<td>3,216.9</td>
<td>2,898.5</td>
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<td></td>
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<tr>
<td>Operating Expenses</td>
<td>277.1</td>
<td>274.6</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Depreciation &amp; Amortization</td>
<td>212.2</td>
<td>194.3</td>
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<td></td>
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<tr>
<td><strong>Total Operating Expenses</strong></td>
<td>3,706.2</td>
<td>3,367.4</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Net Operating Income</strong></td>
<td>323.8</td>
<td>172.5</td>
<td></td>
<td></td>
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<tr>
<td>Net Financing Charges</td>
<td>74.2</td>
<td>70.4</td>
<td></td>
<td></td>
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<tr>
<td>Income tax expense</td>
<td>67.1</td>
<td>31.5</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Gain)/Loss on Disposal of Assets</td>
<td>(2.1)</td>
<td>(10.1)</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Net movements in Regulatory Balances</strong></td>
<td>(33.2)</td>
<td>46.0</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Net Income after net movements in regulatory balances</strong></td>
<td>151.4</td>
<td>126.7</td>
<td>24.7</td>
<td>19.5%</td>
</tr>
<tr>
<td>Dividends Paid</td>
<td>63.4</td>
<td>56.3</td>
<td></td>
<td></td>
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</tbody>
</table>

*regulatory balances are recovered over time in accordance with OEB orders.

THC consolidated net income for the year ended December 31, 2016, of $151.4 million, demonstrated a 19.5% increase over the prior year's net income of $126.7 million.
Gross revenues include the following:

- **Energy Sales** ($3,306.2 million in 2016, vs $2,925.6 million in 2015). Energy sales include charges to customers for electricity consumed, transmission charges, and other non-distribution charges. While energy sales should equal the cost of energy purchased, a difference between the two relates to timing differences between amounts paid, and amounts charged to customers.

- **Electricity distribution revenue** ($647.9 million in 2016, as compared to $555.4 million in 2015). The increase was primarily due to implementation of electricity distribution rates per the OEB’s rate decision and order covering this period.

- **Other revenues** ($75.9 million in 2016 vs $58.9 million in 2015), include revenue from services ancillary to electricity distribution, delivery of street lighting services, pole and duct rentals, amortization of deferred revenues, and "Conservation and Demand Management" cost efficiency incentives. The increase was primarily due to higher revenue in connection with ancillary services.

Capital expenditures related primarily to the renewal of the electricity infrastructure. For the year ended December 31, 2016, THC had capital expenditures on property, plant, and equipment, and intangible assets of $551.7 million, of which $546.0 million were regulated capital expenditures. This was slightly greater than 2015 total capital expenditures of $537.2 million.

During 2016, regulated capital expenditures included the Copeland Station, at $22.6 million, for a total of $176.1 million on this project to date, with project completion anticipated in 2018. Other capital expenditures in 2016 included $365.3 million mainly for underground and overhead infrastructure and delivery of customer connections, $47.6 million in reactive spending, $50.6 million for facilities consolidation, and $59.9 million for other capital initiatives.

As at December 31, 2016, THC's debentures were rated "A" by Standard & Poor's (S&P) with a "Negative Outlook"; and "A" by DBRS with a "Stable" trend. S&P had changed its outlook from "Stable" to "Negative" in 2016, but on April 25, 2017, S&P restored its THC credit outlook to "Stable" as a result of City Council's decision to offer its financial support by way of a $250 million equity contribution.

### 4. Highlights – 2016 Annual Information Form

THC's Annual Information Form for the year ended December 31, 2016, forms Attachment 4 to this Report. The AIF is published annually by THC as a public debt issuer according to Ontario Securities Commission requirements.

#### Employees

At December 31, 2016, THC had approximately 1,490 employees. Included in THC's employees are 850 members of bargaining units represented by the Power Workers' Union ("PWU"), and 61 engineers represented by the Society of Energy Professionals. THC employees currently represented by PWU were formerly represented by Canadian
Union of Public Employees, Local One ("CUPE One"), which merged with PWU on October 6, 2016.

In 2016, THC achieved five million hours without a lost-time injury and total recordable injuries were 74% lower than its benchmarked peers. Within the same year, THC recorded lowest absenteeism rate in its history, 66% lower than the Canadian utilities benchmark. Comparisons are based on benchmark data for Canadian electrical utilities from 2015 as 2016 data was not available at the time of release of the 2016 AIF.

Executive Compensation

At its meeting of July 12-15, 2016, City Council as Shareholder adopted a motion to require the Board of THC, to review its senior executive compensation policy and forward it to the City Manager for inclusion in a report to City Council, through Executive Committee in 2017. THC continues to move forward on City Council's direction.

5. 2016 Environmental Performance

Attachment 5 to this Report contains THC's 2016 Environmental Performance Report. Highlights for 2016 include:

- THC operates in an integrated Environment, Health and Safety (EHS) Management System. In 2016, THC continued to work with residential, small business, industrial and commercial customers to implement energy-efficiency projects. THC's 2016 Conservation and Demand Management (CDM) programs led to an estimated energy savings of 273.2 GWh (equivalent of taking 36,720 homes off the grid). These initiatives also helped reduce greenhouse gas (GHG) emissions in the city by 11,200 tCO₂e.

- THC's total GHG emissions were 40,318 tCO₂e, a decrease of 37% relative to 2015. The make-up of the carbon footprint is similar to 2015 with 78% of emissions attributed to line losses.

- As a result of downsizing its fleet by 17 vehicles and introducing anti-idling technologies, THC realized 2016 cumulative savings, relative to 2013, of 30% reduction in total fuel consumed; 28% reduction in GHG emissions; 26% reduction in kilometres travelled; and 29% reduction in total non-Power Take Off idling hours.

- Overall, THC has enabled over 1,572 renewable generation interconnections totalling approximately 81.9MW between 2009 and 2016, representing 15% of the City's 2020 renewable energy generation goal.
CONTACT

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Robert Hatton, Director, Strategic Initiatives & Intergovernmental Finance, 416.392.9149, robert.hatton@toronto.ca

Lorraine Searles-Kelly, Solicitor, Legal Services, 416.392.7240, lorraine.searles-kelly@toronto.ca

SIGNATURE

_____________________________________
Roberto Rossini
Deputy City Manager & Chief Financial Officer

_____________________________________
Peter Wallace
City Manager

ATTACHMENTS

Attachment 1 - Toronto Hydro Corporation Report 2016 Annual Shareholder Meeting, Resolution of the Sole Shareholder – City of Toronto: 1a) Re-appointing Auditor

Attachment 2 - Toronto Hydro Corporation 2016 Annual Report, Powering Toronto's Future

Attachment 3 - Toronto Hydro Corporation Financial Report for the year ended December 31, 2016 including Consolidated Financial Statements of Toronto Hydro Corporation for the years ended December 31, 2016 and 2015 and the Auditors' Report thereon

Attachment 4 - Toronto Hydro Corporation Annual Information Form for the year ended December 31, 2016

Attachment 5 - Toronto Hydro 2016 Environmental Performance Report