



REPORT FOR ACTION WITH CONFIDENTIAL ATTACHMENT

Toronto Hydro Corporation - Annual General Meeting and 2019 Audited Financial Statements

Date: September 9, 2020

To: Executive Committee

From: City Manager and Chief Financial Officer and Treasurer

Wards: All Wards

REASON FOR CONFIDENTIAL INFORMATION

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

This report deals with personal matters about an identifiable person.

SUMMARY

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 including receipt of Toronto Hydro Corporation's audited annual consolidated financial statements for 2019 and appointment of the auditor for Toronto Hydro Corporation for 2020.

In light of the state of emergency that was declared in Ontario in response to the COVID-19 pandemic, the deadline to hold annual meetings of shareholders for OBCA corporations was temporarily extended through the addition of Part XIX to the OBCA. With the Ontario declaration of emergency having come to an end on July 24, 2020, the extended meeting deadlines for OBCA incorporated companies that were required to hold annual meetings on or before July 24, 2020 now have until October 22, 2020 to hold their annual meetings.

This report also contains recommendations for receipt at the Annual General Meeting of the Shareholder of information disclosing the individual compensation of executive officers employed by Toronto Hydro Corporation in 2019.

RECOMMENDATIONS

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 Toronto Hydro Corporation for 2020 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 2019 Annual Report," "Toronto Hydro Corporation 2019 Annual Financial Report, and Consolidated Financial Statements," "Toronto Hydro Corporation Annual Information Form 2019," "Toronto Hydro Corporation Environmental Performance Report 2019," "Toronto Hydro Corporation CEO and CFO Certifications of Annual Filings 2019," the "Toronto Hydro Corporation First Quarter Financial Report 2020," and the "Toronto Hydro Corporation Statement of Board Remuneration and Expenses 2019," forming Attachments 2a, 2b, 3, 4, 5, 10, and 11 respectively to this Report;

c. receive the "Toronto Hydro Corporation Shareholder Report 2019, including Non-Consolidated Financial Statements," "Toronto Hydro-Electric System Limited Financial Statements 2019 and 2018," and "Toronto Hydro Energy Services Inc. Financial Statements 2019 and 2018," forming Confidential Attachments 7, 8 and 9 respectively to this Report; and

d. receive the two-part report "Toronto Hydro Corporation Executive Compensation Disclosure 2019" 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, 2019 and 2018", included as part of Attachment 2b to this Report, to the Audit Committee for information.

5. City Council, as Shareholder, direct the Board of Toronto Hydro Corporation, in consultation with the City of Toronto's Chief Financial Officer and Treasurer, to bring forward a report on the impacts of COVID-19 on Corporation operating and capitals budgets and operations, detailing any modifications to their programs and initiatives to address COVID-19, to City Council through Executive Committee, by Q1 of 2021.

FINANCIAL IMPACT

There are no financial implications resulting from the implementation of the recommendations in this report.

Toronto Hydro Corporation pays the City dividends, calculated 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 Toronto Hydro Corporation. Toronto Hydro Corporation paid the City \$100.38 million in dividends in 2019. The City anticipates receiving dividends totaling \$92.64 million in 2020. For the first two quarters of 2020, the City has received dividends of \$46.32 million.

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

DECISION HISTORY

At the Annual Meeting of the Shareholder on July 16, 17 and 18, 2019, City Council adopted with amendments item EX7.10 Toronto Hydro Corporation Annual General Meeting and 2018 Annual Audited Financial Statements.

<http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2019.EX7.10>

On July 11, 2012, City Council approved a requirement that Shareholder Directions for all wholly-owned City corporations be amended to require public disclosure to the extent permitted by law of individual executive compensation as part of the annual reporting to the Shareholder and where required obtain consent from executives.

<http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2012.EX21.19>

ISSUE BACKGROUND

City Council authorized the establishment of Toronto Hydro Corporation, on June 11, 1999 pursuant to subsection 142(1) of the Electricity Act, 1998. Toronto Hydro Corporation was incorporated under the Business Corporations Act (Ontario) (OBCA) on June 23, 1999. The City is the sole shareholder.

Subsection 94(1) of the OBCA requires that the directors of a corporation call an annual meeting of shareholders not later than fifteen months after holding the last preceding annual meeting. Section 149(2) requires shareholders at each annual meeting to appoint one or more auditors to hold office until the close of the next annual meeting. Subsection 154(1) requires the directors of an offering corporation to place before each annual meeting of shareholders the financial statements required to be filed under the Securities Act and the regulations thereunder relating separately to the period that began immediately after the end of the last completed financial year and ended not more than six months before the annual meeting, and the immediately preceding financial year, if any, together with the report of the auditor to the shareholders and any further information respecting the financial position of the corporation and the results of its operations required by the articles, the by-laws or any unanimous shareholder agreement.

In light of the state of emergency that was declared in Ontario in response to the COVID-19 pandemic, the deadline to hold annual meetings of shareholders for OBCA corporations was temporarily extended through the addition of Part XIX to the OBCA. With the Ontario declaration of emergency having come to an end on July 24, 2020, the extended meeting deadlines for OBCA incorporated companies that were required to hold annual meetings on or before July 24, 2020 now have until October 22, 2020 to hold their annual meetings.

The date on which an OBCA corporation is required to hold its annual meeting of shareholders is based upon both the meeting date described in section 94 of the OBCA (within 15 months from the corporation's last annual meeting) and the financial statements required to be placed before the meeting (i.e., for the period that began immediately after the end of the last completed financial year and ending not more than six months before the annual meeting). For OBCA corporations with a December 31 year-end, this generally requires that a meeting be held by no later than June 30. Part XIX, temporarily extends this deadline to October 22, 2020.

Under the temporary provisions of Part XIX of the OBCA, the directors of corporations must place before annual meetings the financial statements relating to the most recently completed annual period. The requirement that the financial information placed before an annual meeting pertain to a period ended not more than six months before the meeting is suspended. This clarifies that OBCA corporations holding their annual meetings by the extended deadline will be able to place their annual financial statements for the 2019 fiscal year before their shareholders at their 2020 annual general meeting.

COMMENTS

1. Appointment of Auditor

The auditor is selected by Toronto Hydro Corporation based on a competitive process, subject to Shareholder approval. KPMG LLP, Chartered Accountants, has been selected by Toronto Hydro Corporation as the external auditor for the 2020 calendar year and for completion of the 2020 year-end audit in 2021. It is recommended that City

Council, in its capacity 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 Toronto Hydro Corporation for 2020, and to authorize the Board of Directors of Toronto Hydro Corporation to fix the auditor's remuneration.

2. Key Toronto Hydro Corporation Achievements in 2019

Toronto Hydro Corporation's 2019 Annual Report (Attachment 2a) highlights key achievements in 2019. Toronto Hydro Corporation's Environmental Performance Report (Attachment 4), provides details on the Corporation's environmental performance.

3. Summary – Toronto Hydro Corporation 2019 Audited Financial Statements

The audited consolidated financial statements of THC for the fiscal year ended December 31, 2019 are provided in Attachment 2b to this Report, reflecting the consolidated operations of THC and of its wholly-owned subsidiaries, as required under Section 9.7 of the Shareholder Direction and Subsection 154(1) of the OBCA.

THC's principal business is electricity distribution to approximately 778,000 customers in Toronto, through its distribution subsidiary (Toronto Hydro Electric System Limited, or "THESL"). THESL is regulated by the Ontario Energy Board, which in December 2019, approved its distribution rates for 2020-2024. Toronto Hydro Energy Services Inc. ("THESI") is a smaller THC subsidiary having only a minor impact on the THC consolidated financial results. The business of this subsidiary includes the provision of street lighting services to the City of Toronto.

THC's 2019 Shareholder Report and its confidential financial statements, including the unconsolidated statements of THC and its subsidiary companies, are provided in Confidential Attachments 7, 8 and 9.

THC is also a "market issuer" under Ontario Securities Commission rules, as a result of its issuance of debentures in the public marketplace. Attachment 5 to this Report provides the Ontario Security Commission forms that certify THC's filings.

Table 1 - THC Audited Consolidated Key Financial Results for the Years 2019 and 2018

	2019	2018	Year over Year Change
Income Statement for the year ended December 31 (\$millions)			
Energy Sales	2,779.7	2,704.1	
Distribution Revenue	799.2	674.2	
Other Revenue	94.4	94.4	
Total Revenue	3,673.3	3,472.7	200.6

	2019	2018	Year over Year Change
Less:			
Energy Purchases	2,779.6	2,646.3	
Operating Expenses	308.9	307.5	
Depreciation & Amortization	255.6	238.3	
Financing Costs	80.1	74.6	
Income Taxes	67.9	82.4	
Total Expenses	3,492.1	3,349.1	143.0
Operating Income	181.2	123.6	57.6
Gain on Disposal of Property, Plant & Equipment	2.2	108.6	
Change in Regulatory Balances*	(29.0)	(64.9)	
Net Income	154.4	167.3	(12.9)
Balance Sheet Items as of December 31 (\$millions)			
Capital Expenditures	587.1	511.3	
Total Assets and Regulatory Balances*	5,778.7	5,360.1	418.6
Debentures	2,183.0	2,034.9	
Short Term Debt (not including current portion of debentures)	137.0	125.6	
Total Liabilities	3,673.0	3,348.4	324.6
Shareholder's Equity	1,887.5	1,833.5	54.0
Regulatory Balances*	218.2	178.2	40.0
Total Debt/Total Capitalization	55.1%	54.1%	

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

Highlights of 2019 Financial Results

THC financial results can be summarized as follows:

- Net income decreased to \$154.4 million in 2019 as compared to \$167.3 million in 2018.

- Capital expenditures were \$587.1 million for the year compared to \$511.3 million for 2018 and were primarily related to the renewal of the electricity infrastructure of LDC.
- Debentures increased by \$148.1 million due to issuance of senior unsecured debentures of \$400.0 million, which were offset by repayments of \$250.0 million.

Income Statement

During fiscal 2019, total revenues were \$3,673.3 million, an increase of \$200.6 million from 2018, resulting from:

- An increase of \$75.6 million in energy sales due to higher commodity charges (\$67.9 million) and higher retail transmission charges (\$11.1 million).
- An increase of \$125.0 million in distribution revenue due to higher revenue collected through OEB-approved rate riders (\$107.4 million) and higher 2019 electricity distribution rates (\$30.7 million).

Although its principal business is electricity distribution, most of the THC revenues relate to energy billings on behalf of other energy-related entities. Any difference between energy purchase (payments) and sales (receipts) are deferred and treated as "regulatory balances", to be recovered or transferred in future periods.

Total expenses were \$3,492.1 million, an increase of \$143.0 million from 2018, primarily due to an increase of \$133.3 million in energy purchases resulting from higher commodity charges (\$151.4 million) that were partially offset by lower retail transmission charges (\$12.6 million).

During fiscal 2019, total THC operating income was \$181.2 million, an increase over the previous fiscal year (\$123.6 million). Gain on disposal of property, plant and equipment (PP&E) decreased by \$106.4 million as the entity was not required to provide similar levels of refunds to customers on significant disposals of PP&E that occurred in 2018. 2019's net income of \$154.4 million represented a \$12.9 million reduction over 2018 (\$167.3 million), due to higher depreciation related to new in-service asset additions (\$17.3 million), lower electricity consumption (\$13.7 million), higher finance costs (\$5.5 million), and amounts deferred for future refund to customers (\$5.1 million), which were offset by higher electricity distribution rates (\$30.7 million).

Balance Sheet

As at December 31, 2019, THC had total assets and regulatory balances of \$5.78 billion, an increase over 2018 (\$5.46 billion) primarily due to capital expenditures relating to customer-initiated plant relocations and expansions, customer connections, and overhead infrastructure capitalized in 2019.

Total liabilities were \$3,673.0 million, an increase of \$324.6 million compared with the previous year, resulting from:

- An increase of \$148.1 million in debentures from issuance of senior unsecured debentures (\$400.0 million) net of debentures that matured and were repaid (\$250.0 million).

- An increase of \$120.9 million in deferred revenue due to additional capital contributions received in 2019.
- An increase of \$59.0 million in post-employment benefits due to recognized actuarial loss as a result of lower discount rate and past service costs recorded in 2019.

THC's total debt to total capitalization ratio increased to 55.1% over 2018 fiscal year end (54.1%). 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, 2019

	Issuer Rating	Senior Unsecured Debentures
DBRS	A stable	A stable
S&P	A stable	A

Subsequent to Year End

In December 2019, Ontario Energy Board (OEB) issued its rate decision for Toronto Hydro's Electricity Distribution Rates from 2020 to 2024. Subsequent to the 2019 fiscal year end, THC reported its first quarterly results for 2020. The entity reported a net income (after net movements in regulatory balances) of \$35.4 million, which was slightly lower than the figure reported in the first quarter of 2019 (\$42.6 million). 2020's net income was lower than in 2019 partially due to lower overall demand for electricity. Electricity distribution revenues for the first quarter of 2020 were \$187 million, which was slightly less than the revenues reported in the first quarter of 2019 (\$192.9 million).

4. 2019 Executive Compensation

The compensation of Toronto Hydro Corporation Named Executive Officers (NEOs) is set out in the Annual Information Form in Attachment 3. The Annual Information Form is a public document published annually by Toronto Hydro Corporation as a public debt issuer in accordance with Ontario Securities Commission requirements.

In addition to the executive compensation reported through the Annual Information Form, 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 Annual Information Form, 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. The protection of individual privacy is required by the Municipal Freedom of Information and Protection of Privacy Act (MFIPPA). Specific compensation data of individual employees is private information under MFIPPA.

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SIGNATURE

Heather Taylor
Chief Financial Officer and Treasurer

Chris Murray
City Manager

ATTACHMENTS

Attachment 1 - THC Report on the 2019 Annual Shareholder Meeting
Attachment 1 Appendix A - Resolution of the Shareholder Re-appointing Auditor
Attachment 2a - THC 2019 Annual Report
Attachment 2b - THC 2019 Financial Report and Consolidated Financial Statements
Attachment 3 - THC Annual Information Form 2019
Attachment 4 - THC Environmental Performance Report 2019
Attachment 5 - THC CEO and CFO Certification of Annual Filings 2019
Attachment 6a - THC Executive Compensation Disclosure 2019 (Part 1, NEOs)
Confidential Attachment 6b - THC Executive Compensation Disclosure 2019 (Part 2, All Executives)
Confidential Attachment 7 - THC Shareholder Report 2019, including Non-Consolidated Financial Statements
Confidential Attachment 8 - THESL Financial Statements 2019 and 2018
Confidential Attachment 9 - THESI Financial Statements 2019 and 2018
Attachment 10 - THC First Quarter Financial Report 2020
Attachment 11 - THC Statement of Board Remuneration and Expenses 2019