



## STAFF REPORT ACTION REQUIRED

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

<b>Date:</b>	May 14, 2008
<b>To:</b>	Executive Committee
<b>From:</b>	City Manager
<b>Wards:</b>	All
<b>Reference Number:</b>	

#### SUMMARY

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This report recommends the actions necessary to comply with the requirements of the *Business Corporations Act* (Ontario) for holding an annual general meeting of the shareholder of Toronto Hydro Corporation including receipt of the audited financial statements and appointment of the auditor.

#### RECOMMENDATIONS

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**The City Manager recommends that City Council:**

1. consider the Council meeting to be the Annual General Meeting of the Shareholder for Toronto Hydro Corporation by:
  - a. adopting the recommendations embodied in the Toronto Hydro Corporation report, dated April 30, 2008, forming Attachment 1 to this report, that appoints Ernst and Young as the auditor for Toronto Hydro Corporation and receives the report from the Chair of the Board of Directors; and
  - b. receiving the information report of the Deputy City Manager and Chief Financial Officer, dated May 1, 2008, "Toronto Hydro Corporation – Financial Statements", forming Attachment 2 to this report and receiving the financial statements forming Appendix A to that report; and
2. refer Toronto Hydro Corporation's Consolidated 2007 Annual Financial Statements in Attachment 2 to the Audit Committee for review.

## **FINANCIAL IMPACT**

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There are no financial implications that would result from the adoption of this report

## **EQUITY IMPACT STATEMENT (Not Applicable)**

## **DECISION HISTORY**

Strategic Policies and Priorities Committee Report No. 10, Clause 1 as amended by City Council, adopted on June 9, 10 and 11, 1999, authorized the incorporation of Toronto Hydro Corporation.

## **ISSUE BACKGROUND**

In order to comply with the requirements of the OBCA, an annual meeting of the shareholders must be held within fifteen (15) months from the last preceding annual meeting. The last annual shareholder meeting for Toronto Hydro Corporation was held by City Council at its meeting of July 16, 17, 18 and 19, 2007 as Executive Committee Item EX10.12.

## **COMMENTS**

The report from Toronto Hydro Corporation requests that City Council consider the audited financial statements for the 2007 completed financial year and the auditor's report for that period.

Toronto Hydro Corporation also requests that City Council reappoint the incumbent auditors for the 2008 financial year and authorize the Board of Directors of Toronto Hydro Corporation to fix the auditor's remuneration.

The shareholder review of Toronto Hydro Corporation's 2007 Annual Audited Financial Statements is set out in the information report of the Deputy City Manager and Chief Financial Officer, which is attached to this report as Attachment 2 and which should be considered as part of the Annual General Meeting agenda.

## **CONTACT**

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## **SIGNATURE**

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Shirley Hoy, City Manager

## **ATTACHMENTS**

Attachment 1: Toronto Hydro Corporation Report April 30, 2008

- Appendix A Resolution of the City of Toronto (“Sole Shareholder”) To Appoint the Auditor of Toronto Hydro Corporation (the "Corporation")
- Appendix B Report from Clare Copeland – Chairman of the Toronto Hydro Board of Directors dated April 30, 2008

Attachment 2: Report of Deputy City Manager and Chief Financial Officer dated May 1, 2008 entitled “Toronto Hydro Corporation – Financial Statements”

- Appendix A 2007 Audited Consolidated Annual Financial Statements of Toronto Hydro Corporation

Attachment 1

## **Toronto Hydro Corporation Report April 30, 2008**

Addressed to the Executive Committee  
from Lawrence D. Wilde, Vice President General Counsel and Corporate Secretary  
Toronto Hydro Corporation

## **2007 Annual General Meeting – Toronto Hydro Corporation**

### Purpose

To comply with the requirements of subsection 94(1) of the *Business Corporations Act* (Ontario), R.S.O., c.B.16 (the "OBCA"), the directors of Toronto Hydro Corporation ("THC") are required to call an annual meeting of its shareholders (i.e. the City of Toronto) by no later than fifteen (15) months after holding the last preceding annual meeting. The last annual shareholder meeting for THC was held on July 16, 17, 18 and 19, 2007.

The directors of THC therefore hereby submit and recommend that this report and attached shareholder resolutions be reviewed by the Executive Committee and approved by the City Council at its next meeting.

### Recommendations

It is recommended that:

- (1) City Council, as the sole shareholder of THC, hold an annual shareholder meeting;
- (2) approve and adopt the shareholder resolutions attached in Appendix A to this report;
- (3) authorize and direct appropriate City officials to take the necessary action to give effect thereto; and
- (4) receive any additional reports attached hereto, for informational purposes.

### Background

City Council, by the amendment and adoption of Clause 1 of Report No. 10 of the Strategic Policies and Priorities Committee, at its meeting of June 9, 10 and 11, 1999, authorized the incorporation of THC. The City of Toronto is the sole shareholder of THC.

THC is the parent of the following subsidiaries:

- 1) Toronto Hydro-Electric System Limited, which distributes electricity;
- 2) Toronto Hydro Energy Services Inc., which provides street lighting and related ancillary services and is engaged in the development and sale of energy efficiency products and services;
- 3) Toronto Hydro Telecom Inc., which leases fibre optic cable capacity and provides managed data services;
- 4) 1455948 Ontario Inc., which was incorporated for the purpose of holding an equity interest in the EBT Express partnership, which holds an interest in SPi Group Inc., an organization providing electronic data management and transaction services through an electronic business transaction hub.

## **2007 Annual General Meeting**

City Council, as sole shareholder of THC, is to consider the following items at this annual general meeting:

- (1) audited financial statements for the 2007 completed financial year and the auditor's report for that period;
- (2) re-appointment of the incumbent auditors for the 2008 financial year and re-authorization of the THC board of directors to fix their remuneration for this period; and
- (3) receipt the additional report attached hereto as Appendix B, for information purposes.

### Comments

- (1) Audited Financial Statements and Auditor's Report

Audited financial statements for 2007 completed financial year, and related auditor's reports, have been delivered by THC and reviewed by the Deputy City Manager and Chief Financial Officer and his comments are presented in a separate report before this Committee. The financial statements of THC are on file with the City Clerk's office.

(2) Re-Appointment of Auditor and Authorization of THC Directors to Fix  
Remuneration

At the last preceding annual general meeting, the shareholder resolved to appoint the incumbent auditors, Ernst & Young LLP, Chartered Accountants ("E&Y") until the close

of the next annual meeting of the shareholder, or until a successor is appointed, and further resolved and authorized the directors of THC to fix the auditor's remuneration.

The Board of Directors of THC now recommends that the shareholder re-appoint E&Y as auditor for THC for the fiscal year 2008 or until the close of the next annual meeting of the shareholder, whichever is later. The directors of THC further recommend that City Council resolve and authorize the directors of THC to fix the auditor's remuneration for this period.

(3) Other Items

It is recommended that the shareholder receive the report attached as Appendix B hereto, for information purposes. The original is on file with the City Clerk.

Contact:

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List of Attachments:

Appendix A - Resolutions of the City of Toronto (“Sole Shareholder”)  
Appendix B - Report from Clare Copeland – Chairman of the THC Board of Directors dated April 30, 2008

Appendix A

Resolution of the City of Toronto (“the Shareholder”)  
To Appoint the Auditor of Toronto Hydro Corporation (the "Corporation")

RESOLVED THAT:

Ernst and Young LLP, Chartered Accountants, is hereby appointed the auditor of the Corporation to hold office until the close of the next annual meeting of the shareholder of the Corporation, or until a successor is appointed, at such remuneration as may be fixed by the directors and the directors are hereby authorized to fix such remuneration. The Corporation’s directors are authorized to pass the requisite resolutions giving effect to the foregoing, and any and all such resolutions passed by the directors of the Corporation regarding same are hereby confirmed and ratified.

\* \* \* \* \*

The foregoing resolutions are hereby consented to by sole shareholder of the Corporation pursuant to the *Business Corporation Act* (Ontario).

Dated as of this \_\_\_\_\_ day of \_\_\_\_\_, 2008

City of Toronto

\_\_\_\_\_  
per: Joseph Pennachetti  
Deputy City Manager and  
Chief Financial Officer

\_\_\_\_\_  
per: Ulli Watkiss  
City Clerk  
Approved as to Form per: \_\_\_\_  
Anna Kinastowski, City Solicitor

Authorized by Executive Committee Item No. \_\_\_\_ adopted by Council at its meeting of \_\_\_\_\_, 2008.

\_\_\_\_\_  
per: Ulli Watkiss  
City Clerk

## Appendix B

Clare R Copeland  
Chairman of the Board April 30, 2008

To: The Executive Committee

From: Clare R. Copeland  
Chairman of the Board

Subject: Toronto Hydro Corporation (“THC”)  
2007 Report to the Shareholder

### Recommendation:

It is recommended that this report be received for information purposes.

### Background:

THC was incorporated on July 1, 1999. THC was incorporated under the Ontario Business and Corporation Act (“OBCA”) and has a Board of Directors consisting of eight independent directors plus three City Councillors with accountability for the operational and financial management of THC.

Pursuant to its initial public offering of \$225 million in debentures on May 7, 2003, THC became a reporting issuer with the Ontario Securities Commission, and accordingly is subject to relevant reporting issuer rules and regulations.

THC operates three wholly-owned affiliates in the electricity distribution (“THESL”), energy management services (“TH Energy”) and telecommunications services (“THTI”). THESL, the electricity distribution business, holds 95% of the fixed assets and accounts for 97% of the gross revenue of the company. THESL serves 601,500 residential customers and 78,500 commercial and industrial customers, for a total of 680,000 customers in the City of Toronto. THESL owns and operates the electricity distribution grid within the City of Toronto. Power is delivered to the grid from generating stations located throughout the province through Hydro One’s transmission system to 35 terminal stations located throughout the City.

The corporate relationship between THC and the City is set out in the Shareholder Direction approved by Council on July 1, 1999, and amended October 3, 2002, May 25, 2006 and June 29, 2006. The Shareholder Direction was further amended by Council on October 22, 2007 but a revised Shareholder Direction incorporating those amendments has not yet been received from the City. The Shareholder Direction sets out the City’s objectives and principles for THC. The Board of Directors is responsible



for determining and implementing the appropriate balance among the objectives and principles, and for causing the Corporation to conduct its affairs accordingly.

The Shareholder's objectives in connection with its relationship with THC are as follows:

- (a) the value of THC should be maintained or increased;
- (b) the Shareholder's income stream from THC be comparable to the Shareholder's estimated financial benefit if Toronto Hydro had been sold as a going concern;
- (c) THC's consumers should not be unduly impacted by the succession by THC of Toronto Hydro Electric Commission; and
- (d) environmental impacts related to THC should be improved.

The following key principles are excerpted from the Shareholder Direction that currently governs the operations of THC:

- (a) the Business is integral to the well-being and the infrastructure of the City of Toronto;
- (b) THC will provide a reliable, effective and efficient distribution system that meets changing demand utilizing emerging green technologies as appropriate;
- (c) THC will provide its services with an emphasis on customer orientation and satisfaction;
- (d) THC will operate in a safe and environmentally-responsible manner;
- (e) THC will promote energy conservation and environmental responsibility and work with the City of Toronto to achieve its climate change initiative;
- (f) THC will engage in recruitment practices designed to attract employees from the diverse community it serves;
- (g) THC's administrative strategies will support the City of Toronto priority objectives where consistent with THC's business objectives, including procurement practices that encourage participation of equity-seeking groups;
- (h) THC will keep its property and facilities clean and well maintained and free from graffiti; and
- (i) THC will operate in a manner that will protect and enhance the City's urban forest.

THC recognizes that it is in the best interests of THC and the community of stakeholders whom the business affects that THC conducts its affairs:

- (i) on a commercially prudent basis;
- (ii) in a manner consistent with the energy policies established by the Shareholder from time to time; and
- (iii) in accordance with the following financial performance objectives (and that the Board will use its best efforts to ensure compliance):
  - THC will maintain a credit rating of A- or higher;
  - THC will pay dividends based on the higher of: 50% of the consolidated annual net income or \$25 million; and
  - THC will employ the most effective cost structures, implement cost reduction programs and maximize return on the Shareholder's equity.

THC reports to the City Finance Department on a regular basis with its Board of Directors-approved quarterly reports on budget-to-actual results, five-year business plan and annual audited consolidated financial statements. Over the course of any given year, THC and City staff meet to review and discuss issues and progress as required.

The Board has incorporated the principles and objectives in the Shareholder Direction into its corporate strategy. Accordingly, THC's goals and objectives incorporate the key elements of the Shareholder Direction.

- Health and Safety of Employees
  - Ensure that employees are safe and healthy – *implementation of ZeroQuest program*
  - Engage, develop and empower employees
  - Renew our workforce
- Modernize our Utility:
  - Invest in the renewal of THESL's aging electricity infrastructure
  - Operate the businesses with the highest levels of integrity and fairness
  - Continue to be environmentally responsible
- Focus on customer Service:
  - Listen to the concerns of our customers
  - Ensure distribution system reliability
  - Lead in energy conservation and demand management initiatives
- Consistent Financial Performance:
  - Provide a consistent and fair return to our Shareholder
  - Minimize business risks
  - Selective growth of our unregulated businesses

As reflected further in this report, THC has and continues to meet the objectives and principles set out by the Shareholder Direction.

#### Purpose:

This report highlights THC's key achievements in 2007. We take pride that our core business, distribution of electricity, is a necessity of life. The Board of Directors of THC reports that 2007 was highly successful. Consistent with the priorities established in the Shareholder Direction, our strategy remained focused on customer service, reliability, workplace safety, customer satisfaction, energy conservation, environmental responsibility and sound financial management.

#### Highlights

In 2007, THC's contribution to the City through interest and dividends amounted to \$106.1 million. Interest payments on the outstanding City promissory note amounted to \$59.9 million. Dividend payments were made in accordance with the dividend policy as set out in the Shareholder Direction and amounted to \$46.2 million.

On December 31, 2007, THC paid to the City the first installment of \$245.1 million on the City promissory note in accordance with the repayment schedule approved in 2006. THC financed this repayment through a public debt offering of \$250.0 million on November 14, 2007. The debentures issued bear interest at a rate of 5.15% per annum, payable semi-annually in arrears in equal installments on May 14 and November 14 of each year. The debentures mature on November 14, 2017.

2007 was a busy year for THESL from a regulatory perspective. Regulatory certainty was obtained regarding the recovery of costs associated with the Provincial Smart Meter initiative and the recovery of costs and benefits arising from conservation initiatives delivered under the Ontario Energy Board ("OEB") governance framework. In August, THESL filed its electricity distribution rates application for 2008, 2009 and 2010. An oral hearing was conducted by the OEB in December in connection with this application and a final decision is expected in May 2008.

Throughout the year, we showed our commitment to excellence and customer service as we continued to meet or exceed most OEB service standards.

In 2007, THC continued to be a leader in the provincial energy conservation efforts. Once again, THESL led all utilities and provincial agencies in the delivery of Conservation and Demand Management ("CDM") initiatives to help customers conserve energy, save money, and help the environment. In 2007, THESL received numerous awards for its efforts regarding the environment and energy conservation. Among others, THESL received the 2007 Platts Global Energy Award for its PeakSaver

program and the 2007 Environment Achievement Award from the City of Toronto for its Summer Challenge program.

Properly investing in maintenance and capital work in the distribution system is a vital role that THESL carries out for its customers. In 2007, THESL increased its capital spending significantly in order to meet the goals of its 10 year infrastructure modernization plan filed with the OEB. Accordingly, \$275.6 million was spent, including \$183.4 million on electricity distribution plant and \$35.1 million on smart meters.

In February 2007, TH Energy sold its electric water heater business to The Consumers' Waterheater Income Fund for cash consideration of \$40.8 million. This transaction provided for a net gain of \$24.2 million in 2007.

For the third year in row THC was selected as one of Canada's Top 100 Employers as featured by MacLean's magazine. Furthermore, for 2007, THC was also selected as one of the Top 50 Employers in the GTA as featured by the Toronto Star, and one of Canada's Top 10 Family-Friendly Employers as featured by Canadian Family Magazine. To obtain this recognition, THC went through a rigorous selection process whereby several areas such as physical workplace, work atmosphere, compensation and benefits, employee communications, performance management and employee training were evaluated.

#### Electricity Business Environment

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.

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's authority and responsibilities include the power to approve and fix rates for the distribution of electricity and the responsibility to ensure that electricity distribution companies fulfill their obligations to connect and service customers.

THESL 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] *Electricity Price and Related Rebates.* The electricity price and related rebates represent a pass through of the commodity cost of electricity.

[ii] *Distribution Rates.* The distribution rates are designed to recover the costs incurred by THESL for delivering electricity to customers and the OEB-allowed rate of return. Distribution rates comprise a fixed charge and a usage-based (consumption) charge.

The volume of electricity consumed by customers during any period is governed by events largely outside of THESL'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).

[iii] *Retail Transmission Rates.* The retail transmission rates represent 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 Charges.* The wholesale market service charges represent a pass through of various wholesale market support costs. Retail rates for the recovery of wholesale market service charges are regulated by the OEB.

In late 2002, Bill 210 dramatically changed the operation of the electricity market effectively shutting down the active retail electricity market. Bill 210 also required municipal councils to confirm the original decision to commercialize the distribution company. City Council passed the required Council resolutions in February 2003.

In December 2003 the government passed the *Ontario Energy Board Amendment Act (Electricity Pricing)*, which was intended to remove subsidies in electricity commodity pricing and restored much of the OEB's role in approving distribution rates.

In December 2004, the Province initiated a further restructuring of Ontario's electricity industry with the passage of the *Electricity Restructuring Act, 2004*. The restructuring was intended, among other things, to ensure efficient and effective management of electricity, promote the expansion of new electricity supply and capacity, encourage electricity conservation and renewable energy and regulate prices in parts of the electricity sector.

In 2006, the OEB ordered that the Board of Directors of each of the electricity distribution utilities in the Province include one third of independent Directors. For THESL this meant that one-third of the Directors should be unrelated to the City, the THC Board of Directors or the management of THC and its affiliates. Accordingly, the City agreed to modify the Shareholder Direction to allow the THC Board of Directors to appoint independent Directors to the THESL Board of Directors in order to meet the requirement of the OEB.

#### Electricity Distribution Rates

In April 2006, the OEB approved a decrease in the distribution rates of THESL for the period May 1, 2006 to April 30, 2007 representing a revenue reduction of approximately \$58.0 million. The decrease in electricity distribution rates was mainly related to the benefits derived from the amalgamation of the former six utilities. The methodology used by the OEB to establish distribution rates was based on, among other things, a rate base of \$1.861 billion, a deemed debt to equity structure of 65:35 and an allowed return on deemed equity of 9%. As part of its decision, the OEB reduced the allowable interest rate recoverable on related party debt including the outstanding City promissory note from 6.8% to 5% per annum.

In August 2007, THESL filed a rate application with the OEB seeking approval of separate and successive revenue requirements and corresponding rates for the rate years commencing May 1, 2008, 2009 and 2010. The requested base distribution revenue requirements for these rate years are \$490.5 million, \$532.5 million and \$564.3 million respectively. If approved by the OEB, this application would provide for an increase in rates of approximately 4% over the next three years for an average residential customer. The OEB conducted an oral hearing regarding THESL's application in December 2007. A final decision from the OEB is expected in May 2008.

Also in August 2007, the OEB issued its decision approving the recovery of costs associated with smart metering activities incurred by THESL. In its decision, the OEB approved the recovery of expenditures for smart metering activities conducted in 2006. The remaining amounts related to expenditures incurred in 2007 will be subject to regulatory review in 2008 using the same methodology used to review and approve the 2006 expenditures.

In September 2007, THESL received approval from the OEB to recover \$2.9 million of loss revenue and \$4.3 million representing its share of Provincial savings related to the CDM programs delivered in 2005 and 2006.

### 2007 Performance Review

In accordance with the Shareholder Direction and through its corporate strategy, THC and its subsidiary companies performed well in 2007 in the key areas of people, operations, customers and financials.

#### 1. People

- In May 2007, THESL was formally recognized by the Electrical & Utilities Safety Association ("EUSA") for its completion of the "Committed" level of the ZeroQuest program. The ZeroQuest program is sponsored by EUSA and is widely recognized as encompassing best practices for safety policies and initiatives. Full installation of the ZeroQuest management system will result in THC being firmly embedded in a network of utilities utilizing the same system and practices.

- THC was selected as one of Canada's Top 100 Employers as featured by MacLean's magazine. Furthermore, in 2007, THC was also selected as one of the Top 50 Employers in the GTA as featured by the Toronto Star, and one of Canada's Top 10 Family-Friendly Employers as featured by Canadian Family Magazine.
- In 2007, THC, through its employees, was once again very active in the United Way Greater Toronto campaign with a record-breaking contribution of approximately \$194,000.
- The Society of Energy Professionals ratified a 4.5 year collective agreement in 2007. This multi-year contract provides for long-term stability in this area. The Society of Energy Professionals represents approximately 30 employees in THESL.
- At the end of 2007, THESL had 67 apprentices in trade training, including 35 newly hired Certified Power Line Persons apprentices. These apprentices were hired in connection with our strategy to renew our workforce as several employees will be eligible for retirement in the near future. In order to meet its future needs, THESL is running its own certified electrical trade program out of its 500 Commissioners facility.

## 2. Operations

- In 2006, THESL performed a detailed study of its electricity distribution infrastructure. Not unexpectedly, given the age of much of the infrastructure, the analysis showed that 35% of the distribution system infrastructure is past its useful life and that, in order to maintain the current level of service to customers, large portions of the system will need to be replaced over the next 5 to 10 years. Accordingly, an investment plan designed to improve the condition of THESL's assets was developed and approved by the Board of Directors.
- In 2007, THESL filed this investment plan with the OEB in connection with its electricity distribution rates application for 2008, 2009 and 2010. Under this plan, \$1.2 billion will be invested in THESL's core electricity distribution assets over the next 10 years.
- As part of its investment plan in 2007, THESL increased investing in its infrastructure. Total capital expenditures for 2007 amounted to \$275.6 million compared to \$167.7 million in 2006. This amount includes an increase in spending for core electrical distribution plan of \$51.8 million.
- THESL installed 213,000 smart meters to residential and commercial customers in 2007. At the end of 2007, THESL had installed a total of 416,000 smart meters since the issuance of the Minister of Energy directive in 2005. THESL leads all utilities in the deployment of smart meters in Ontario.

- In 2007, THC continued its long-standing support of the City's of Toronto Urban Forest campaign, Ontario Forestry Association and Local Enhancement and Appreciation of Forest (LEAF) through tree planting initiatives and forest education programs. Furthermore, through its internal team of certified arborists THESL worked closely with the City to develop sustainable urban forestry practices to manage the urban forest that is in proximity to its distribution lines.
- Through its management of the street lighting and expressway lighting assets acquired from the City at the end of 2005 TH Energy provided City residents with excellent service. Throughout the year, TH Energy's street lighting crews performed maintenance and capital work in accordance with the service agreement and exceeded all service level targets.
- In 2007, THTI delivered several operational initiatives. It implemented a new customer order and billing management system to reduce order provisioning time and to improve billing accuracy. It completed to deployment of a new core backbone system which provided for 100% reliability and it completed phase one of its new collocation facility in the west end.
- THC continued its environmental efforts in areas such as energy efficiency, use of alternate energy and recycling. Total waste diversion at THC reached 81.5%.

### 3. Customers

- For 2007, the electricity distribution business met or exceed most of the customer services requirements from the OEB:
  - o Average time per outage of 48 minutes (OEB target is 48 minutes).
  - o Performed 96% of low voltage connections within 5 days (OEB target is 90%).
  - o Performed 99% of high voltage connections within 10 days (OEB target is 90%).
  - o Performed 98% of locates within 5 days (OEB target is 90%).
  - o Kept 99% of customer appointments on time (OEB target: 90%).
  - o Answered 78% of calls within 30 seconds (OEB target is 65%).
  - o Responded to 90% of emergency calls within 60 minutes (OEB target is 80%).
  - o Responded to written inquiries within 5 days 88% of the time (OEB target is 80%).

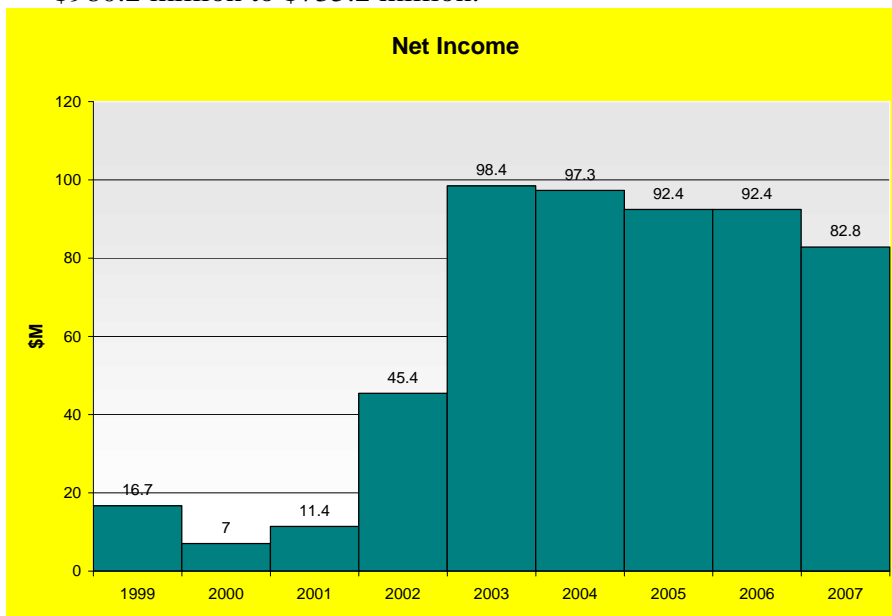


- Average outage duration per customer of 105 minutes (OEB target is 82 minutes). This target was not achieved in 2007 due to several incidences of unfavourable weather conditions and the aging electricity infrastructure causing longer outages.
- Average number of outages per customer of 2.2 (OEB target is 2.1). This target was not achieved in 2007 due to several incidences of unfavourable weather conditions and the aging electricity infrastructure causing higher number of outages.
- In 2007, THESL completed the delivery of the CDM programs approved by the OEB in 2005. These programs entailed a budget of \$39.8 million in the areas of customer energy conservation, demand response, power distribution system loss reduction, load displacement and stand-by generators.
- Following the completion of the OEB-approved conservation programs, THESL applied to and received approval, from the Ontario Power Authority (“OPA”), for the funding of future CDM programs under the Minister of Energy initiative for the City of Toronto and under the Provincial Standard Programs. In connection with these approved initiatives, THESL spent \$20.7 million in 2007 for the delivery of CDM programs. The highlights of the programs were as follows:
  - Under the 2007 business Summer Challenge program and the residential Summer Savings program, THESL provided 156,000 customers with a rebate on their electricity bill after they reduced their consumption by 10%. Both of these programs were originally developed by Toronto Hydro and were the first of their kind in Canada.
  - THESL participated in several mass market programs which resulted in the distribution of efficient CFL bulbs, energy-efficient LED festive light strings; and the collection of old, inefficient refrigerators and window air conditioning units.
  - THESL enrolled 36 ,000 customers in the PeakSaver program, aimed at reducing air conditioning load during summer heat wave high consumption periods.
- Over the past two years, THESL supported the saving of 483,000 MWh through its conservation programs.
- Over the past three years, TH Energy has delivered numerous energy efficiency projects that contributed to our energy conservation goals and objectives. These projects include the energy retrofit of several civic centers and community recreation facilities in Toronto.

- Again in 2007, THTI continued to meet the standards set forth in its service level agreements for customer commitments related to network availability, provisioning time and mean time for repair.

#### 4. Financial

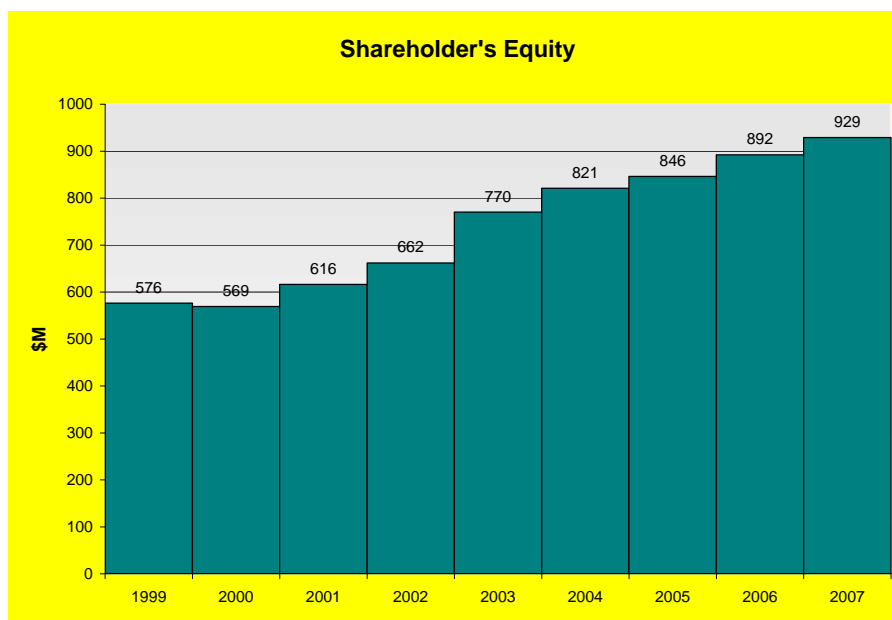
- In 2007, THC continued to contribute to the cash flow of the City with a total contribution of \$106.1 million. The balance paid in 2007 includes dividend payments of \$46.2 million (paid in accordance with Shareholder Direction) and interest payments of \$59.9 million on the City promissory note.
- In November 2007, THC issued senior unsecured debentures in the amount of \$250.0 million. The debentures bear interest at a rate of 5.15% per annum, payable semi-annually in arrears in equal installments in May and November of each year. The debentures mature on November 14, 2017. The issuance of the public debentures increased the outstanding balance of public debt from \$225.0 million to \$475.0 million.
- The majority of the proceeds from the issuance were used to pay the first installment of \$245.1 million on the City Promissory Note on December 31, 2007. The payment was made in accordance with the repayment schedule provided by the City in 2006. Following this payment, the City promissory note was reduced from \$980.2 million to \$735.2 million.



- Net income of \$82.8 million for 2007 exceeded the budget of \$64.3 million. The favourable variance of \$18.5 million was mainly due to the higher than expected gain on the sale of the water heater business in TH Energy, effective management of operating costs and the unexpected contribution of energy conservation incentives in connection with OEB and OPA programs. THC was able

to exceed its business plan financial objectives despite recording an impairment provision of \$13.1 million in connection with its investments in asset back commercial paper (“ABCP”).

- At December 31, 2007, THC and its subsidiary TH Energy held ABCP notes issued by a number of trusts with an aggregate principal amount of \$88.0 million. On the dates THC purchased these notes they were rated R1-High by DBRS Limited, the highest credit rating issued for commercial paper. The purchase of these notes was made in compliance with THC investment policy and the Shareholder Direction. These notes matured in the third quarter of 2007 but remained unpaid due to liquidity issues in the ABCP market. These market issues are impacting over \$33.0 billion in the Canadian ABCP investment market. A restructuring process for these notes is currently under negotiation in order to minimize the potential exposure of all market participants. THC is monitoring the restructuring process and evaluating the potential impacts it could have in its investments. At the end of 2007, Management decided to record an impairment provision of \$13.1 million on these investments based on the information available at that time. It is expected that the restructuring will be completed in the second quarter of 2008. Despite the ABCP issues, THC has sufficient cash to fund all its ongoing liquidity and capital expenditure requirements and is in compliance with the financial covenants under the terms of its outstanding indebtedness.
- THC has modified its investment policy to eliminate investing in ABCP in the future.
- Shareholder equity continued to increase in 2007 with a growth of \$37.0 million or 4% from 2006 and by \$353.0 million or 61 % since incorporation in 1999.



- Throughout the year, THC maintained strong credit ratings with an A from DBRS Limited and an A- from Standard & Poors. Note that the Shareholder Direction requires that THC to maintain a minimum rating of A- with Standard & Poor's.
- THC maintained a strong cash position at the end of 2007 with a balance of \$216.0 million. This balance is not consistent but fluctuates throughout each month as cash is received and paid out over the course of the month. For example, this cash position at December 31, 2007 does not reflect the \$167.0 million required to provide payment to the IESO for electricity consumed in December and accordingly overstates the total excess cash available to THC. The current available cash will mainly be used to fund investments in the electricity distribution infrastructure over the next few years. According to the current long-term asset plan, capital spending will increase significantly in the future to maintain the current level of reliability.
- In February 2007, TH Energy sold its water heater business for cash consideration of \$40.8 million. The cash received in connection with this transaction was higher than initial valuation received of \$20 million. The gain associated with this transaction amounted to \$24.2 million (budgeted gain was \$7.7 million). All employees affected by this transaction have been redeployed within THC and its affiliates.
- In 2007, THTI grew its business through active sales management and prudent capital investment. Revenue from our telecom activities increased by 27% from \$29.6 million in 2006 to \$37.5 million in 2007.
- For 2007, Ernst & Young provided THC with an unqualified audit opinion.
- In August 2006, the Board of Directors of THC approved the establishment of an internal audit function. This new function is under the leadership of the Director of Internal Audit who has direct access to the Audit Committee of THC. In 2007, the internal audit function focused its activities on financial internal controls in connection with THC compliance with Bill-198.
- For 2007, THC met all internal control requirements from the Ontario Securities Commission (Bill-198) in connection with disclosure controls and internal controls over financial reporting.

Conclusion:

The Board of Directors of THC is pleased to report that, in 2007, THC operated within the Shareholder Direction in a balanced manner by making financial contributions to the

City of \$106.1 million, and continuing to focus on safety, operational effectiveness, customer service, energy conservation and environmental issues.

As forecasted last year, the net income of THC from continuing operations was lower in 2006 than 2007 due to the successful windup of THC's unregulated electricity retail business. Over the next few years, THC expects net income to steadily increase as it is investing in the electricity distribution infrastructure of its regulated electricity business.

The upcoming year will provide for significant challenges for the Board of Directors. The modernization of our electricity distribution infrastructure, the continued focus on electricity conservation and demand management, the completion of our smart meter deployment strategy, the implementation of our OEB distribution rate decision for 2008-2010 and the review of our strategies for our unregulated businesses will be the cornerstones of our activities for 2008.

Clare R. Copeland  
Chairman,  
Toronto Hydro Corporation

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## Toronto Hydro Corporation – Financial Statements

<b>Date:</b>	May 14, 2008
<b>To:</b>	Executive Committee
<b>From:</b>	Deputy City Manager and Chief Financial Officer

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### Disclosure of Financial Results:

Section 6.6 of the Shareholder Direction requires the Corporation to deliver its audited consolidated annual financial statements to the Shareholder within 120 days of its fiscal year end. These documents are filed with the City Clerk's office and are posted on the internet on the Toronto Hydro Corporation website ([www.torontohydro.com](http://www.torontohydro.com)) and via the SEDAR website for Canadian public securities documents.

The consolidated statements are public documents upon their release. The corporation's unconsolidated statements (relating to its subsidiary companies and the holding company) remain confidential.

The *Business Corporations Act*, Ontario ("OBCA") (s.94) requires that an annual meeting of shareholders be called no later than 15 months after the last preceding annual meeting. The last annual general meeting of the Corporation was held at the Council meeting of July 16, 17, 18 and 19, 2007 (Executive Committee Report No. 10, Clause 12).

### Financial Results

For the fiscal year ended December 31, 2007, the Corporation generated a consolidated net income of \$82.8 million, compared with \$92.4 million for 2006.

Contributing to the \$9.6 million lower net income were:

- Lower net revenues (\$12.5 million) stemming from the completion of the energy services subsidiary in 2006;
- Higher operating expenses (\$12.4 million) and depreciation and amortization (\$14.3 million) due to the distribution subsidiaries infrastructure and workforce renewal initiatives;
- Impairment of investments (\$13.1 million) held to maturity recorded in 2007 due to the Corporation's exposure to third-party asset-backed commercial paper;
- A one-time gain on sale of TH Energy's water heater assets of \$22.0 million;
- A lower provision for PILS of \$17.4 million.

During fiscal 2007, the City received interest payments of \$59.9 million on Toronto Hydro Corporation debt of \$980 million, and Shareholder dividend payments totalling \$46.2 million. Debt principal of \$245 million was repaid to the City at year-end.

Key consolidated results of Toronto Hydro Corporation (“the Corporation”) are as follows:

<b>Consolidated Financial Results of Toronto Hydro Corporation</b>		
(\$ millions)		
	Year ended Dec 31, 2007	Year ended Dec 31, 2006
	Actual	Actual
Net Income	\$82.8	\$92.4
Shareholder's Equity	\$928.7	\$892.1
Total Assets	\$2,672.5	\$2,591.7
Cash at end of period	\$216.0	\$327.5
Dividends Paid to City	\$46.2	\$46.2
Interest Paid	\$59.9	\$62.1

#### Subsequent Events

On March 5, 2008, the Corporation declared dividends totalling \$22.4 million, comprised of:

3. a \$6 million first quarterly dividend instalment as required under the Shareholder Direction, payable to the City of Toronto March 31, 2008;
4. a \$16.4 million payment related to earnings in fiscal 2007, March 14 2008.

In addition, the City received a scheduled interest payment on the Promissory Note of \$11.2 million on March 31, 2008.

#### **CONTACT**

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#### **SIGNATURE**

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Joseph P. Pennachetti  
Deputy City Manager and Chief Financial Officer