FINANCIAL REPORT
DECEMBER 31, 2017

TORONTO HYDRO CORPORATION

TABLE OF CONTENTS

Glossary	3
Management's Discussion and Analysis	4
Executive Summary	5
Introduction	5
Business of Toronto Hydro Corporation	6
Electricity Distribution – Industry Overview	7
Results of Operations	8
Summary of Quarterly Results of Operations	15
Financial Position	16
Liquidity and Capital Resources	17
Corporate Developments	22
Legal Proceedings	24
Share Capital	24
Transactions with Related Parties	25
Controls and Procedures	25
Risk Management and Risk Factors	26
Critical Accounting Estimates	32
Significant Accounting Policies	32
Changes in Accounting Policies	32
Future Accounting Pronouncements	32
Forward-Looking Information	33
Selected Annual Information	36
Additional Information	36
Consolidated Financial Statements	37
Notes to the Consolidated Financial Statements	44

TORONTO HYDRO Corporation

GLOSSARY

CDM – Conservation and demand management

CGU – Cash generating unit

CIR – Custom Incentive Rate-setting

City – City of Toronto

Copeland Station – The Clare R. Copeland transformer station, formerly called "Bremner Station".

Corporation – Toronto Hydro Corporation

Electricity Act – *Electricity Act, 1998* (Ontario), as amended

ERM – Enterprise risk management

ERP – Enterprise resource planning

GAAP – Generally Accepted Accounting Principles

GWh – Gigawatt hour

HONI – Hydro One Networks Inc.

IAS – International Accounting Standard

IASB – International Accounting Standards Board

ICM – Incremental Capital Module

IESO – Independent Electricity System Operator. The IESO and the Ontario Power Authority were merged under the name Independent Electricity System Operator on January 1, 2015

IFRIC – International Financial Reporting Interpretations Committee

IFRS – International Financial Reporting Standards

IRM – Incentive Regulation Mechanism

ITA – *Income Tax Act* (Canada), as amended

kW – Kilowatt

LDC – Toronto Hydro-Electric System Limited

LRAM – Lost revenue adjustment mechanism

MD&A – Management's Discussion and Analysis

MEU – Municipal electricity utility

OCI – Other comprehensive income

OEB – Ontario Energy Board

OEB Act – *Ontario Energy Board Act, 1998* (Ontario), as amended

OFHP – Ontario's Fair Hydro Plan

OFHA – *Fair Hydro Act, 2017* (Ontario)

OMERS – Ontario Municipal Employees Retirement System

OPA – Ontario Power Authority. The IESO and the OPA were merged under the name Independent Electricity System Operator on January 1, 2015

OPEB – Other post-employment benefits

OREC – *Ontario Rebate for Electricity Consumers Act*, 2016 (Ontario).

PILs – Payments in lieu of corporate taxes

PP&E – Property, plant and equipment

TA – *Taxation Act, 2007* (Ontario), as amended

TH Energy – Toronto Hydro Energy Services Inc.

US GAAP – United States Generally Accepted Accounting Principles

WMS – Wholesale Market Service

MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEARS ENDED DECEMBER 31, 2017 AND 2016

Executive Summary

- Net income after net movements in regulatory balances for the three months and year ended December 31, 2017 was $35.1 million and $156.5 million, respectively, compared to $23.4 million and $151.4 million for the comparable periods in 2016;
- Capital expenditures were primarily related to the renewal of the electricity infrastructure of LDC and were $148.9 million and $552.9 million for the three months and year ended December 31, 2017, respectively, compared to $149.2 million and $551.7 million for the comparable periods in 2016;
- On June 28, 2017, the Corporation issued 200 common shares to the City for total proceeds of $250.0 million, net of share issue costs and expenses;
- On August 23, 2017, LDC 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 LDC's 2018 rates and the disposition of certain deferral and variance accounts;
- On November 14, 2017, the Corporation issued $200.0 million of 3.485% senior unsecured debentures due February 28, 2048;
- The Corporation's Series 2 debentures in the amount of $250.0 million, matured and were repaid on November 14, 2017; and
- Under the terms of the energy conservation agreement with the IESO for the delivery of CDM programs over the 2015 – 2020 period, the Corporation is entitled to a performance incentive if the verified mid-term electricity savings target is achieved by December 31, 2017. The Corporation exceeded the mid-term energy savings target and recognized a performance incentive of $12.2 million.

Introduction

This MD&A should be read in conjunction with the Corporation's audited consolidated financial statements and accompanying notes as at and for the years ended December 31, 2017 and 2016, which were prepared in accordance with IFRS (the "Consolidated Financial Statements").

Copies of these documents are available on the System for Electronic Document Analysis and Retrieval website at www.sedar.com.

Business of Toronto Hydro Corporation

The Corporation is a holding company which wholly owns two subsidiaries:

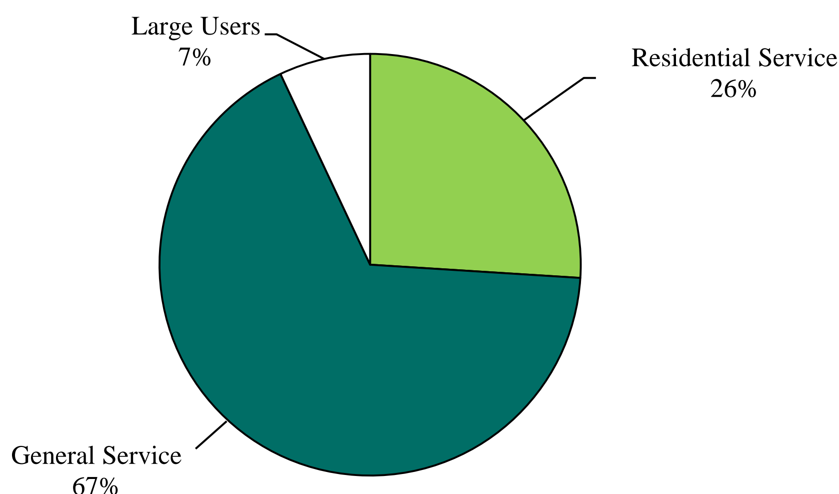
- LDC - distributes electricity and engages in CDM activities; and
- TH Energy - provides street lighting and expressway lighting services in the City.

The Corporation supervises the operations of, and provides corporate, management services and strategic direction to its subsidiaries.

The principal business of the Corporation and its subsidiaries is the distribution of electricity by LDC. LDC owns and operates an electricity distribution system, delivering electricity to approximately 768,000 customers located in the City. The City is the sole shareholder of the Corporation. LDC serves the largest city in Canada and distributes approximately 19% of the electricity consumed in Ontario. The business of LDC and other electricity distributors is regulated by the OEB, which has broad powers relating to licensing, standards of conduct and service, and the regulation of electricity distribution rates charged by LDC and other electricity distributors in Ontario. For the year ended December 31, 2017, LDC earned energy sales and distribution revenues of $3,742.0 million from general service users[1], residential service users[2] and large users[3].

LDC Energy Sales and Distribution Revenues by Class

Year ended December 31, 2017



[1] "general service" means a service supplied to premises other than those receiving "residential service" and "large users" and typically includes small businesses and bulk-metered multi-unit residential establishments. This service is provided to customers with a monthly peak demand of 5,000 kW or less averaged over a twelve-month period.

[2] "residential service" means a service that is for domestic or household purposes, including single family or individually metered multi-family units and seasonal occupancy.

[3] "large users" means a service provided to a customer with a monthly peak demand of more than 5,000 kW averaged over a twelve-month period.

Electricity Distribution – Industry Overview

In April 1999, the Government of Ontario began restructuring the province's electricity industry. Under regulations passed pursuant to the restructuring, LDC and other electricity distributors purchase electricity from the wholesale market administered by the IESO and recover the costs of electricity and certain other costs from customers in accordance with rate-setting procedures mandated by the OEB.

The OEB has regulatory oversight of electricity matters in Ontario. The OEB Act sets out the OEB's authority to issue a distribution licence that must be obtained by owners or operators of an electricity distribution system in Ontario. The OEB prescribes licence requirements and conditions including, among other things, specified accounting records, regulatory accounting principles, separation of accounts for distribution and other activities, and requirements for rate-setting and other legal filings.

The OEB's authority and responsibilities include the power to approve and fix rates for the transmission and distribution of electricity, the power to approve the amounts paid to non-contracted generators, the responsibility to provide rate protection for rural or remote electricity customers, and the responsibility for ensuring that electricity distribution companies fulfill their obligations to connect and service customers.

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

- *Commodity Charge* – The commodity charge represents the market price of electricity consumed by customers and is passed through the IESO back to operators of generating stations. It includes the global adjustment, which represents the difference between the market price of electricity and the rates paid to regulated and contracted generators.

- *Retail Transmission Rate* – The retail transmission rate represents the costs incurred in respect of the transmission of electricity from generating stations to local distribution networks. Retail transmission rates are passed through back to operators of transmission facilities.

- *WMS Charge* – The WMS charge represents various wholesale market support costs, such as the cost of the IESO to administer the wholesale electricity system, operate the electricity market, and maintain reliable operation of the provincial grid. Wholesale charges are passed through back to the IESO.

- *Distribution Rate* – The distribution rate is designed to recover the costs incurred by LDC in delivering electricity to customers, including the OEB-allowed cost of capital. Distribution rates are regulated by the OEB and include fixed and variable (usage-based) components, based on a forecast of LDC's customers and load.

LDC is required to satisfy and maintain prudential requirements with the IESO, which include credit support with respect to outstanding market obligations in the form of letters of credit, cash deposits or guarantees from third parties with prescribed credit ratings.

The Corporation is exempt from tax under the ITA if not less than 90% of the capital of the Corporation is owned by the City and not more than 10% of the income of the Corporation is derived from activities carried on outside the municipal geographical boundaries of the City. In addition, the Corporation's subsidiaries are also exempt from tax under the ITA provided that all of their capital is owned by the Corporation and not more than 10% of their respective income is from activities carried on outside the municipal geographical boundaries of the City. A corporation exempt from tax under the ITA is also exempt from tax under the TA.

The Corporation and each of its subsidiaries are MEUs for purposes of the PILs regime contained in the Electricity Act. The Electricity Act provides that a MEU that is exempt from tax under the ITA and the TA is required to make, for each taxation year, a PILs payment to the Ontario Electricity Financial Corporation in an amount equal to the tax that it would be liable to pay under the ITA and the TA if it were not exempt from tax. The PILs regime came into effect on October 1, 2001, at which time the Corporation and each of its subsidiaries were deemed to have commenced a new taxation year for purposes of determining their respective liabilities for PILs payments.

TORONTO HYDRO Corporation

Results of Operations

Net Income after Net Movements in Regulatory Balances

Interim Consolidated Statements of Income
Three months ended December 31
(in millions of Canadian dollars)

	2017 $	2016 $	Change $
Revenues			
Energy sales	728.9	813.3	(84.4)
Distribution revenue	181.7	159.0	22.7
Other	27.7	22.0	5.7
	938.3	994.3	(56.0)
Expenses			
Energy purchases	750.7	782.6	31.9
Operating expenses	77.8	78.6	0.8
Depreciation and amortization	62.0	59.6	(2.4)
	890.5	920.8	30.3
Finance costs	(18.9)	(19.5)	0.6
Gain on disposals of PP&E	0.2	2.1	(1.9)
Income before income taxes	29.1	56.1	(27.0)
Income tax expense	(11.1)	(28.0)	16.9
Net income	18.0	28.1	(10.1)
Net movements in regulatory balances	10.9	(30.6)	41.5
Net movements in regulatory balances arising from deferred tax assets	6.2	25.9	(19.7)
Net income after net movements in regulatory balances	35.1	23.4	11.7

The increase in net income after net movements in regulatory balances for the three months ended December 31, 2017 was primarily due to higher 2017 electricity distribution rates, higher electricity consumption, and higher other revenue related to the recognition of the CDM mid-term incentive and pole and duct rentals. These variances were partially offset by amounts being deferred into capital related regulatory accounts for future refunds to customers, higher income taxes (including regulatory balances arising from deferred tax assets), and higher depreciation and amortization related to new in-service asset additions.

TORONTO HYDRO Corporation

Consolidated Statements of Income
Year ended December 31
(in millions of Canadian dollars)

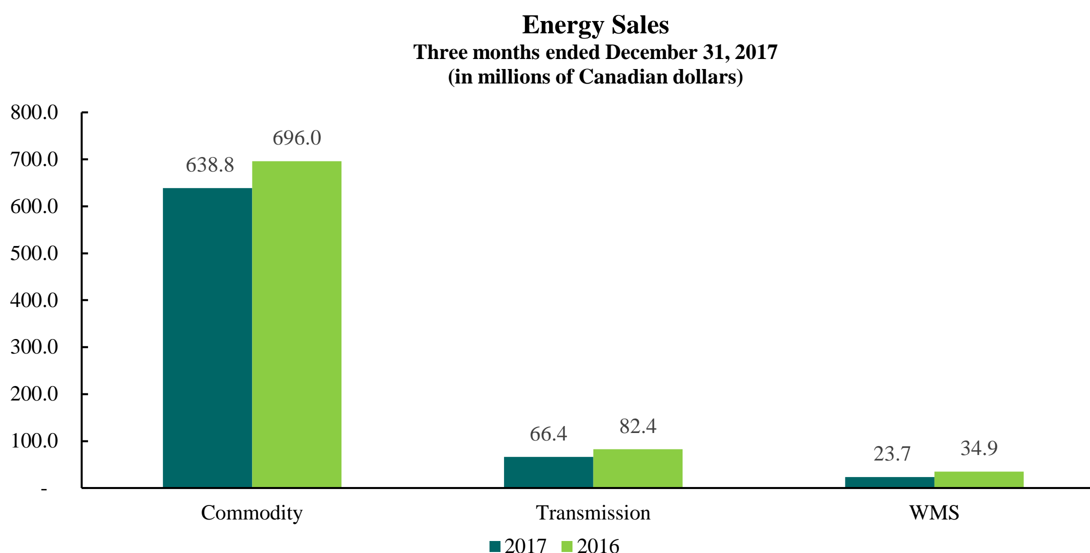
	2017 $	2016 $	Change $
Revenues			
Energy sales	3,017.8	3,306.2	(288.4)
Distribution revenue	724.2	647.9	76.3
Other	107.7	75.9	31.8
	3,849.7	4,030.0	(180.3)
Expenses			
Energy purchases	3,063.5	3,216.9	153.4
Operating expenses	293.0	277.1	(15.9)
Depreciation and amortization	224.2	212.2	(12.0)
	3,580.7	3,706.2	125.5
Finance costs	(77.7)	(74.2)	(3.5)
Gain on disposals of PP&E	9.8	2.1	7.7
Income before income taxes	201.1	251.7	(50.6)
Income tax expense	(44.7)	(67.1)	22.4
Net income	156.4	184.6	(28.2)
Net movements in regulatory balances	(13.1)	(77.2)	64.1
Net movements in regulatory balances arising from deferred tax assets	13.2	44.0	(30.8)
Net income after net movements in regulatory balances	156.5	151.4	5.1

The increase in net income after net movements in regulatory balances for the year ended December 31, 2017 was primarily due to higher 2017 electricity distribution rates and higher other revenue related to the recognition of the CDM mid-term incentive and pole and duct rentals. These variances were partially offset by lower electricity consumption, higher operating expenses in connection with system maintenance, higher depreciation and amortization related to new in-service asset additions, higher income taxes (including regulatory balances arising from deferred tax assets), amounts being deferred into capital related regulatory accounts for future refunds to customers, and a one-time residual ICM balance recorded as an increase in equity through net movements in regulatory balances in 2016. The 2016 first quarter implementation of the new electricity distribution rates also resulted in $19.2 million of foregone revenue being recorded in net movements in regulatory balances for the comparable period, instead of distribution revenue given IFRS 14 - *Regulatory Deferral Accounts* ("IFRS 14") treatment.

Energy Sales

LDC's energy sales arise from charges to customers for electricity consumed, based on regulated rates. Energy sales include amounts billed or billable to customers for commodity charges, retail transmission charges, and WMS charges at current rates. These charges are passed through to customers over time and are considered revenue by LDC. During the same period, energy sales should be equal to the cost of energy purchased. However, a difference between energy sales and energy purchases arises when there is a timing difference between the amounts charged by LDC to customers, based on regulated rates, and the electricity and non-competitive electricity service costs billed monthly by the IESO to LDC. This difference is recorded as a settlement variance, representing amounts to be recovered from or refunded to customers through future rates approved by the OEB. In accordance with IFRS 14, this settlement variance is presented within regulatory balances on the consolidated balance sheets ("Consolidated Balance Sheets")

and within net movements in regulatory balances on the consolidated statements of income and comprehensive income ("Consolidated Statements of Income").

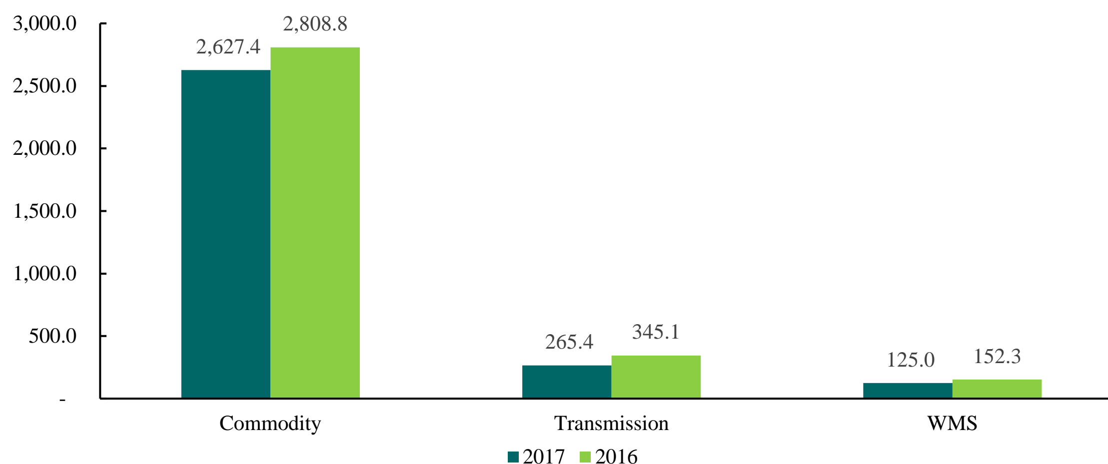


Energy sales for the three months ended December 31, 2017 were $728.9 million compared to $813.3 million for the comparable period in 2016. The decrease was primarily due to lower commodity charges ($57.2 million) and lower retail transmission charges ($16.0 million). The decrease in commodity and retail transmission charges was primarily due to lower pass-through electricity costs.

Energy Purchases , Energy Sales, and Settlement Variances
Three months ended December 31, 2017
(in millions of Canadian dollars)

	Energy Purchases $	Energy Sales $	Settlement Variances $
Commodity Charges	673.1	638.8	34.3
Retail Transmission Charges	65.2	66.4	(1.2)
WMS Charges	12.4	23.7	(11.3)
Total	750.7	728.9	21.8

For the three months ended December 31, 2017, LDC recognized $728.9 million in energy sales to customers and was billed $750.7 million for energy purchases from the IESO. The difference between energy sales and energy purchases represents a $21.8 million settlement variance for the period. The settlement variance was recorded as a decrease to the regulatory credit balance ($21.8 million including carrying charges on the accumulated settlement variance balance) on the Consolidated Balance Sheets, and presented within net movements in regulatory balances on the Consolidated Statements of Income.



Energy sales for the year ended December 31, 2017 were $3,017.8 million compared to $3,306.2 million for the comparable period in 2016. The decrease was primarily due to lower commodity charges ($181.4 million) and lower retail transmission charges ($79.7 million). The decrease in commodity and retail transmission charges was primarily due to lower electricity consumption and lower pass-through electricity costs.

Energy Purchases, Energy Sales, and Settlement Variances
Year ended December 31, 2017
(in millions of Canadian dollars)

	Energy Purchases $	Energy Sales $	Settlement Variances $
Commodity Charges	2,681.4	2,627.4	54.0
Retail Transmission Charges	281.8	265.4	16.4
WMS Charges	100.3	125.0	(24.7)
Total	3,063.5	3,017.8	45.7

For the year ended December 31, 2017, LDC recognized $3,017.8 million in energy sales to customers and was billed $3,063.5 million for energy purchases from the IESO. The difference between energy sales and energy purchases represents a $45.7 million settlement variance for the year. The settlement variance was recorded as a decrease to the regulatory credit balance ($45.2 million including carrying charges on the accumulated settlement variance balance, see the regulatory credit balance table in note 9 to the Consolidated Financial Statements) on the Consolidated Balance Sheets, and presented within net movements in regulatory balances on the Consolidated Statements of Income.

Distribution Revenue

Distribution revenue is recorded based on OEB-approved distribution rates to recover the costs incurred by LDC in delivering electricity to customers, and includes revenue collected through OEB-approved rate riders.

Distribution revenue for the three months and year ended December 31, 2017 was $181.7 million and $724.2 million, respectively, compared to $159.0 million and $647.9 million for the comparable periods in 2016.

The increase in distribution revenue for the three months ended December 31, 2017 was primarily due to higher electricity distribution rates ($11.7 million), higher electricity consumption ($5.6 million), and additional revenue collected through OEB-approved rate riders ($5.5 million).

The increase in distribution revenue for the year ended December 31, 2017 was primarily due to higher electricity distribution rates ($48.8 million) and additional revenue collected through OEB-approved rate riders ($22.6 million), partially offset by lower electricity consumption in 2017 ($14.9 million). The remaining increase was related to the recognition of 2016 foregone revenue ($19.2 million) from the implementation of the new electricity distribution rates effective March 1, 2016, which was recorded in net movements in regulatory balances for the year ended December 31, 2016 given the IFRS 14 treatment, instead of distribution revenue.

Other Revenue

Other revenue includes revenue from services ancillary to electricity distribution, delivery of street lighting services, pole and duct rentals, amortization of deferred revenue related to capital contributions from customers, and CDM cost efficiency incentives.

Other revenue for the three months and year ended December 31, 2017 was $27.7 million and $107.7 million, respectively, compared to $22.0 million and $75.9 million for the comparable periods in 2016.

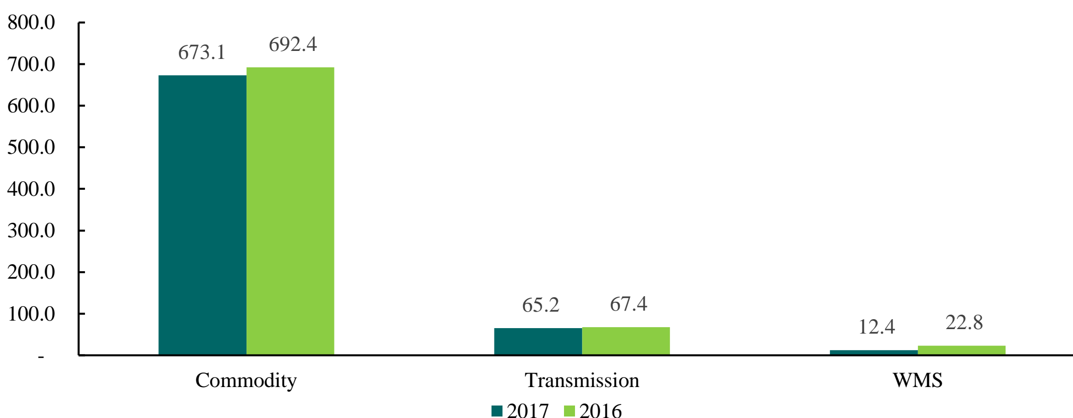
The increase was primarily due to higher revenue in connection with ancillary services, street lighting services, pole and duct rentals, recognition of the CDM mid-term incentive, and deferral of development charges. The development charges are excess expansion deposits retained by LDC where the requested number of connections or demand were not met by the connecting customer (see development charges in note 9(o) to the Consolidated Financial Statements).

The development charges were recorded as a regulatory balance on the Consolidated Balance Sheets, with a corresponding offset in net movements in regulatory balances on the Consolidated Statements of Income. This regulatory balance is expected to offset future electricity distribution rates for customers, although application has yet to be made to dispose of the balance.

Energy Purchases

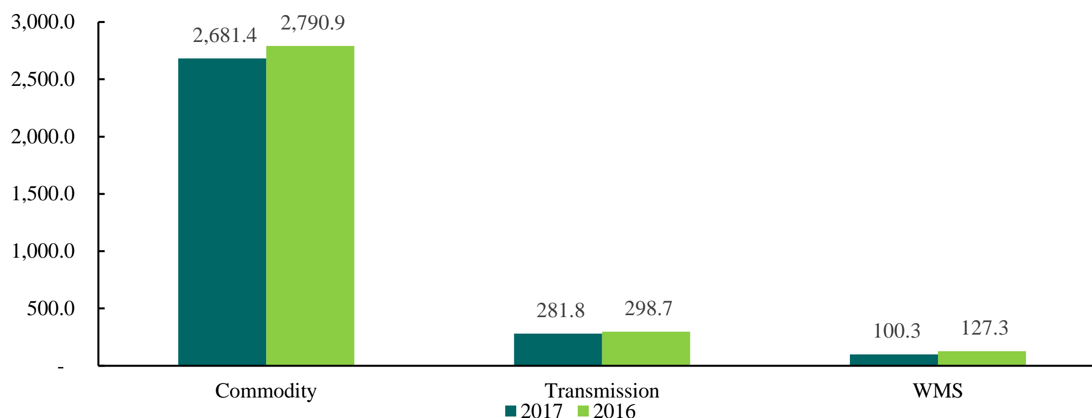
LDC's energy purchases consist of actual charges for electricity generated by third parties, which are passed through to customers over time in the form of energy sales. Energy purchases are billed monthly by the IESO and include commodity charges, retail transmission charges and WMS charges.

LDC Energy Purchases
Three months ended December 31, 2017
(in millions of Canadian dollars)



Energy purchases for the three months ended December 31, 2017 were $750.7 million compared to $782.6 million for the comparable period in 2016. The decrease was primarily due to lower commodity charges ($19.3 million) and lower WMS charges ($10.4 million). The decrease in commodity and WMS charges was primarily due to lower rates.

LDC Energy Purchases
Year ended December 31, 2017
(in millions of Canadian dollars)



Energy purchases for the year ended December 31, 2017 were $3,063.5 million compared to $3,216.9 million for the comparable period in 2016. The decrease was primarily due to lower commodity charges ($109.5 million) and lower WMS charges ($27.0 million). The decrease in commodity and WMS charges was primarily due to lower electricity consumption and lower rates.

Operating Expenses

Operating expenses for the three months and year ended December 31, 2017 were $77.8 million and $293.0 million, respectively, compared to $78.6 million and $277.1 million for the comparable periods in 2016.

The decrease in operating expenses for the three months ended December 31, 2017 was primarily due to lower street lighting maintenance costs, lower rental expenses due to expiration of rental agreements, and lower service fees for third party warehouse costs, partially offset by higher ancillary service costs.

The increase in operating expenses for the year ended December 31, 2017 was primarily due to higher costs in connection with ancillary services and system maintenance programs, partially offset by lower rental expenses due to expiration of rental agreements and lower street lighting maintenance costs.

Depreciation and Amortization

Depreciation and amortization expense for the three months and year ended December 31, 2017 was $62.0 million and $224.2 million, respectively, compared to $59.6 million and $212.2 million for the comparable periods in 2016.

The increase in depreciation and amortization expense for the three months and year ended December 31, 2017 was primarily due to new in-service asset additions in 2017, partially offset by certain assets being fully depreciated, and lower derecognition of assets removed from service.

Finance Costs

Finance costs for the three months and year ended December 31, 2017 were $18.9 million and $77.7 million, respectively, compared to $19.5 million and $74.2 million for the comparable periods in 2016.

The decrease in finance costs for the three months ended December 31, 2017 was primarily due to a lower average amount of outstanding long-term debt ($2,058.6 million) in the fourth quarter of 2017 compared with the same period in 2016 ($2,084.6 million) (see "Liquidity and Capital Resources" below).

The increase in finance costs for the year ended December 31, 2017 was primarily due to a higher average amount of outstanding long-term debt ($2,078.4 million) during 2017 compared with the same period in 2016 ($2,001.4 million) and lower capitalized borrowing costs (see "Liquidity and Capital Resources" below).

Gain on Disposals of PP&E

Gain on disposals of PP&E for the three months and year ended December 31, 2017 were $0.2 million and $9.8 million, respectively, compared to $2.1 million for the comparable periods in 2016. The increase in gain on disposals of PP&E for the year ended December 31, 2017 was primarily due to the gain realized on disposal of a surplus property in the second quarter of 2017 ($9.3 million), offset by lower gain realized on other disposals. The gain on disposal of a surplus property, net of tax of $8.0 million was recorded as a regulatory balance on the Consolidated Balance Sheets to reduce future electricity distribution rates for customers, with a corresponding offset in net movements in regulatory balances on the Consolidated Statements of Income.

Income Tax Expense and Income Tax Recorded in Net Movements in Regulatory Balances

Income tax expense and income tax recorded in net movements in regulatory balances for the three months and year ended December 31, 2017 were $4.9 million and $31.5 million, respectively, compared to $2.1 million and $23.1 million for the comparable periods in 2016.

The unfavourable variance in income tax expense and income tax recorded in net movements in regulatory balances for the three months ended December 31, 2017 was primarily due to higher income before taxes (including net movements in regulatory balances), offset by higher net deductions for permanent and temporary differences between accounting and tax treatments.

The unfavourable variance in income tax expense and income tax recorded in net movements in regulatory balances for the year ended December 31, 2017 was primarily due to higher income before taxes (including net movements in regulatory balances) and lower net deductions for permanent and temporary differences between accounting and tax treatments.

Net Movements in Regulatory Balances

In accordance with IFRS 14, the Corporation separately presents regulatory balances and related net movements on the Consolidated Balance Sheets and Consolidated Statements of Income.

The increase in the regulatory debit ($9.1 million) and the decrease in the regulatory credit ($9.4 million) balances for the year ended December 31, 2017 equals the sum ($18.5 million) of net movements in regulatory balances, net movements in regulatory balances arising from deferred tax assets, and net movements in regulatory balances related to OCI, net of tax for the relevant period (see "Financial Position" below).

Energy purchases record the actual cost of power purchased which varies from month to month. Since the selling price of power within energy sales is fixed for set periods of time, a gain or loss usually results, and is part of the calculation of net income. However, per OEB regulations, such gains or losses on energy sales are deferred within balance sheet regulatory variance accounts for later disposition to or from rate payers via rate riders after approval by the OEB. Deferrals of gains or losses on energy sales (see discussion on "settlement variance" under "Results of Operations" above), or disposition of past deferrals in electricity rates will usually represent the largest single element of the net movements in regulatory balances for a period.

Net movements in regulatory balances for the three months ended December 31, 2017 were a recovery of $10.9 million compared to a charge of $30.6 million for the comparable period in 2016. The recovery of $10.9 million for the three months ended December 31, 2017 was primarily due to the timing difference between the electricity costs billed monthly by the IESO and LDC's billing to customers, partially offset by amounts disposed through OEB approved rate riders and amounts being deferred into capital-related regulatory accounts for future refunds to customers. The charge of $30.6 million for the three months ended December 31, 2016 was primarily due to the timing difference between the electricity costs billed monthly by the IESO and LDC's billing to customers.

Net movements in regulatory balances for the year ended December 31, 2017 were a charge of $13.1 million compared to a charge of $77.2 million for the comparable period in 2016. The charge of $13.1 million for the year ended December 31, 2017 was primarily due to the timing difference between the electricity costs billed monthly by the IESO and LDC's billing to customers, partially offset by amounts disposed through OEB approved rate riders and amounts being deferred into capital-related regulatory accounts for future refunds to customers. The charge of $77.2 million for the year ended December 31, 2016 was primarily due to the timing difference between the electricity costs billed monthly by the IESO and LDC's billing to customers, partially offset by the recognition of the 2016 approved foregone revenue per the OEB's CIR decision and rate order.

Net movements in regulatory balances related to OCI, net of tax for the three months and year ended December 31, 2017 were a recovery of $18.4 million, compared to a charge of $15.5 million for the comparable periods in 2016. The recovery of $18.4 million for the three months and year ended December 31, 2017 was due to the actuarial loss recognized for post-employment benefits. The charge of $15.5 million for the three months and year ended December 31, 2016 was due to the actuarial gain recognized for post-employment benefits.

Summary of Quarterly Results of Operations

The table below presents a summary of the Corporation's results of operations for eight quarters including and immediately preceding December 31, 2017.

Summary of Quarterly Results of Operations
(in millions of Canadian dollars)

	December 31 2017 $	September 30 2017 $	June 30 2017 $	March 31 2017 $
Energy sales	728.9	817.9	721.8	749.2
Distribution revenue	181.7	186.1	178.2	178.2
Other	27.7	36.6	23.0	20.4
Revenues	938.3	1,040.6	923.0	947.8
Net income after net movements in regulatory balances	35.1	46.8	35.0	39.6
	December 31 2016 $	**September 30 2016 $**	**June 30 2016 $**	**March 31 2016 $**
Energy sales	813.3	899.9	801.1	791.9
Distribution revenue	159.0	183.3	158.8	146.8
Other	22.0	21.2	16.8	15.9
Revenues	994.3	1,104.4	976.7	954.6
Net income after net movements in regulatory balances	23.4	52.5	31.2	44.3

The Corporation's revenues, all other things being equal, are impacted by temperature fluctuations and unexpected weather conditions. Revenues would tend to be higher in the first quarter as a result of higher energy consumption for winter heating, and in the third quarter due to air conditioning/cooling. The Corporation's revenues are also impacted by fluctuations in electricity prices and the timing and recognition of regulatory decisions and rate orders.

Financial Position

The following table outlines the significant changes in the consolidated balance sheets as at December 31, 2017 as compared to the consolidated balance sheets as at December 31, 2016.

Consolidated Balance Sheet Data
(in millions of Canadian dollars)

Balance Sheet Account	Increase (Decrease) $	Explanation of Significant Change
Assets		
Accounts receivable and unbilled revenue	(54.3)	The decrease was primarily due to lower pass-through electricity costs, partially offset by the recognition of the CDM mid-term incentive receivable.
Assets held for sale	8.7	In 2017, LDC commenced the process to sell a property to a third party and subsequently entered into a sales agreement. Accordingly, the carrying amount of the property of $8.7 million was reclassified from PP&E to Assets held for sale.
PP&E and intangible assets	314.6	The increase was primarily due to capital expenditures, partially offset by depreciation and derecognition, and reclassification of assets held for sale during the year.
Deferred tax assets	(6.8)	The decrease was primarily due to lower net deductible temporary differences between tax and accounting values of PP&E and intangible assets.
Liabilities and Equity		
Commercial paper	(102.0)	The decrease was primarily due to repayment using the proceeds from the equity investment received from the City in June 2017 ($250.0 million), offset by issuances required for general corporate purposes (see "Liquidity and Capital Resources" below).
Debentures	(50.6)	The decrease was primarily due to the repayment of the Series 2 debentures ($250.0 million), partially offset by the issuance of Series 13 debentures ($200.0 million) in the fourth quarter of 2017 (see "Liquidity and Capital Resources" below).
Accounts payable and accrued liabilities	11.9	The increase was primarily due to timing differences in payments, partially offset by lower electricity costs payable to the IESO.
Deferred revenue	44.5	The increase was primarily due to capital contributions received in 2017.

Consolidated Balance Sheet Data
(in millions of Canadian dollars)

Balance Sheet Account	Increase (Decrease) $	Explanation of Significant Change
Post-employment benefits	32.5	The increase was primarily due to the recognized actuarial loss driven by the annually updated actuarial assumptions.
Retained earnings	81.5	The increase was due to net income after net movements in regulatory balances ($156.5 million) offset by dividends paid ($75.0 million).
Regulatory Balances		
Regulatory debit balances	9.1	The increase was primarily due to the OPEB actuarial loss recorded as regulatory debit balance, partially offset by amounts disposed through OEB-approved rate riders primarily related to foregone revenue.
Regulatory credit balances	(9.4)	The decrease was primarily due to balances arising in the period related to settlement variances, partially offset by amounts being deferred into capital related regulatory accounts for future refunds to customers and amounts disposed through OEB-approved rate riders.

Liquidity and Capital Resources

The Corporation's current assets and current liabilities amounted to $526.7 million and $770.5 million, respectively, as at December 31, 2017, resulting in a working capital deficit of $243.8 million. The deficit is attributable to the Corporation's preference for utilizing its Commercial Paper Program and Working Capital Facility (both defined below) before issuing additional debentures to fulfill the Corporation's ongoing liquidity requirements, including funding of significant capital spending in the current year. The Corporation seeks to maintain an optimal mix of short-term and long-term debt in order to lower overall financing costs and to enhance borrowing flexibility.

The Corporation's primary sources of liquidity and capital resources are cash provided by operating activities, issuances of commercial paper, amounts available to be drawn against its credit facilities, and borrowings from debt capital markets. The Corporation's liquidity and capital resource requirements are mainly for capital expenditures to maintain and improve the electricity distribution system of LDC, for energy purchases and to meet financing obligations. See "Liquidity Risk" under note 16 to the Consolidated Financial Statements.

The amount available under the Revolving Credit Facility and the outstanding borrowings under the Revolving Credit Facility and Commercial Paper Program are as follows:

(in millions of Canadian dollars)	Revolving Credit Facility Limit $	Revolving Credit Facility Borrowings $	Commercial Paper Outstanding $	Revolving Credit Facility Availability $
December 31, 2017	800.0	-	159.0	641.0
December 31, 2016	800.0	-	261.0	539.0

The Corporation is a party to a $20.0 million demand facility with a Canadian chartered bank for the purpose of working capital management ("Working Capital Facility"). As at December 31, 2017, $11.7 million had been drawn under the Working Capital Facility compared to $7.1 million as at December 31, 2016.

Consolidated Statements of Cash Flow Data
(in millions of Canadian dollars)

	Three months ended December 31		Year ended December 31	
	2017 $	2016 $	2017 $	2016 $
Working capital facility beginning of period	(10.1)	(9.1)	(7.1)	(14.2)
Net cash provided by operating activities	211.4	191.7	584.7	571.3
Net cash used in investing activities	(132.3)	(138.2)	(520.9)	(549.4)
Net cash used in financing activities	(80.7)	(51.5)	(68.4)	(14.8)
Working capital facility, end of period	(11.7)	(7.1)	(11.7)	(7.1)

Operating Activities

Net cash provided by operating activities for the three months and year ended December 31, 2017 was $211.4 million and $584.7 million, respectively, compared to $191.7 million and $571.3 million for the comparable periods in 2016.

The increase in net cash provided by operating activities for the three months and year ended December 31, 2017 was primarily due to improved working capital mainly related to timing differences in the settlement of receivable and payables (see note 22 to the Consolidated Financial Statements), and lower net movements in regulatory balances arising from deferred tax assets, partially offset by lower collection from energy sales in excess of energy purchases, which were deferred as a settlement variance and timing of income tax instalments paid.

Investing Activities

Net cash used in investing activities for the three months and year ended December 31, 2017 was $132.3 million and $520.9 million, respectively, compared to $138.2 million and $549.4 million for the comparable periods in 2016.

The decrease in net cash used in investing activities for the three months ended December 31, 2017 was due to lower cash spending on capital projects, partially offset by lower proceeds on disposals of PP&E in the fourth quarter of 2017.

The decrease in net cash used in investing activities for the year ended December 31, 2017 was due to lower cash spending on capital projects and higher proceeds on disposals.

Electricity distribution is a capital-intensive business. As the municipal electricity distribution company serving the largest city in Canada, LDC continues to invest in the renewal of existing aging infrastructure to address safety, reliability and customer service requirements.

TORONTO HYDRO Corporation

The following table summarizes the Corporation's capital expenditures, both PP&E and intangible assets, which are inclusive of capital accruals, for the periods indicated.

Capital Expenditures
(in millions of Canadian dollars)

	Three months ended December 31		Year ended December 31	
	2017 $	**2016 $**	**2017 $**	**2016 $**
Regulated LDC				
Distribution system				
Planned [1]	103.1	85.1	373.0	365.3
Reactive	12.8	16.9	48.1	47.6
Copeland Station	4.9	7.8	23.2	22.6
Facilities consolidation	-	16.1	35.2	50.6
Technology assets	20.3	17.0	54.9	49.1
Other [2]	5.3	3.8	10.5	10.8
Regulated capital expenditures	146.4	146.7	544.9	546.0
Unregulated capital expenditures [3]	2.5	2.5	8.0	5.7
Total capital expenditures	148.9	149.2	552.9	551.7

[1] Includes, among other initiatives, the replacement of underground and overhead infrastructures, station programs, and the delivery of customer connections.

[2] Includes fleet capital and buildings.

[3] Primarily relates to street lighting and generation equipment.

The total regulated capital expenditures for the three months and year ended December 31, 2017 were $146.4 million and $544.9 million, respectively, compared to $146.7 million and $546.0 million for the comparable periods in 2016.

For the three months ended December 31, 2017, spending on regulated capital expenditure year over year was relatively consistent. Changes were primarily related to lower spending on the facilities consolidation program ($16.1 million), partially offset by higher spending on the implementation of an SAP ERP project ($8.1 million), station programs related to the renewal of aging station infrastructure ($4.7 million), network infrastructure ($1.8 million), and metering ($1.7 million).

For the year ended December 31, 2017, the decrease in regulated capital expenditures was primarily related to lower spending on overhead infrastructure ($19.1 million), the radio project ($16.0 million), and the facilities consolidation program ($15.4 million). These variances were partially offset by higher spending on station programs related to the renewal of aging station infrastructure ($26.2 million), the implementation of an SAP ERP project ($19.9 million), and metering ($7.3 million).

The largest capital initiatives in 2017 include the replacement of underground and overhead infrastructures, station programs, delivery of customer connections, the facilities consolidation program, and the construction of Copeland Station in response to the growing need for distribution options in the downtown core of the City.

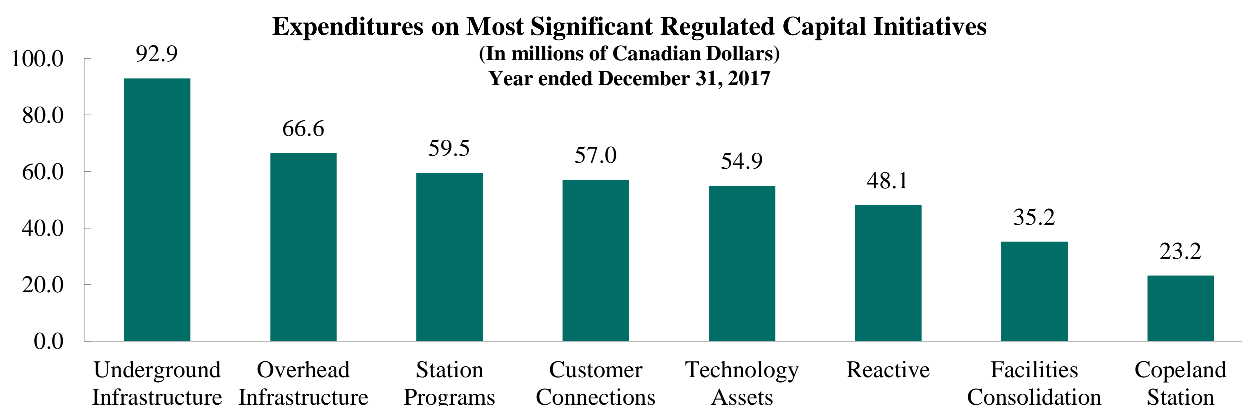
The replacement of underground infrastructure includes replacing direct buried cables, transformer switches, handwells and other aging underground infrastructure. The replacement of overhead infrastructure includes replacing poles, overhead transformers, conductors, overhead switches and other aging overhead infrastructure and equipment. Both initiatives will allow LDC to continue to provide ongoing safe and reliable service to its customers. For the year ended December 31, 2017, capital expenditures for the underground and overhead infrastructures were $92.9 million and $66.6 million, respectively.

The station programs relate to the lifecycle management of electrical equipment installed at each of the Corporation's active Municipal and transformer stations, while ensuring that adequate capacity is available to serve customers. For the year ended December 31, 2017, capital expenditures for the station programs were $59.5 million.

The delivery of customer connections includes spending related to new services and upgrades to existing services for specific commercial customers. For the year ended December 31, 2017, capital expenditures for the delivery of customer connections were $57.0 million.

The facilities consolidation program relates to the consolidation of operating centres to lower operating centre costs and simplify long-term planning. In the year ended December 31, 2017, the Corporation continued relocating staff, equipment and operations as well as performing the required capital investment on specific properties and incurred costs of $35.2 million.

Copeland Station will be the first transformer station built in downtown Toronto since the 1960's and will be the second underground transformer station in Canada. When in service, it will provide electricity to buildings and neighbourhoods in the central-southwest area of Toronto. During 2017, major electrical equipment including power transformers and high and medium voltage switchgear, medium voltage cable, control wiring and DC systems was installed, tested and commissioned, and the high voltage cable was completed. The electric station service equipment was installed and energized. Protection and control equipment was installed and testing and commissioning commenced. In addition, the machine shop installation and landscaping were completed and sidewalks and roadway were paved. HONI, the electricity transmission provider, commenced the installation of their transmission equipment, including high voltage switchgear and protection and control equipment. As at December 31, 2017, the cumulative capital expenditures on the Copeland Station project amounted to $195.1 million, plus capitalized borrowing costs. All capital expenditures related to Copeland Station are recorded to PP&E. Copeland Station is one of the most complex projects ever undertaken by the Corporation and the expected completion date is 2018. The total capital expenditure required to complete the project is approximately $200.0 million, plus capitalized borrowing costs. There may be additional unforeseen delays and expenditures prior to completion of the project. See "Risk Management and Risk Factors" below for further information on the Copeland Station project.



Financing Activities

Net cash used in financing activities for the three months and year ended December 31, 2017 was $80.7 million and $68.4 million, respectively, compared to $51.5 million and $14.8 million for the comparable periods in 2016. The change for the year was primarily due to the repayment of the Corporation's Series 2 debentures and commercial paper and an increase in dividends paid, partially offset by the equity investment received from the City in June 2017.

The Corporation is a party to a credit agreement with a syndicate of Canadian chartered banks which established a revolving credit facility expiring on October 10, 2022 ("Revolving Credit Facility"), pursuant to which it may borrow up to $800.0 million, of which up to $210.0 million is available in the form of letters of credit. On August 1, 2017, the maturity date of the Revolving Credit Facility was extended by one year from October 10, 2021 to October 10, 2022. As at December 31, 2017, the Corporation was in compliance with all covenants included in its Revolving Credit Facility agreement.

The Corporation has a commercial paper program allowing up to $600.0 million of unsecured short-term promissory notes ("Commercial Paper Program") to be issued in various maturities of no more than one year. The Commercial Paper Program is supported by liquidity facilities available under the Revolving Credit Facility; hence, available borrowing under the Revolving Credit Facility is reduced by the amount of commercial paper outstanding at any point in time. Proceeds from the Commercial Paper Program are used for general corporate purposes.

For the three months and year ended December 31, 2017, the average aggregate outstanding borrowings under the Corporation's Revolving Credit Facility, Working Capital Facility and Commercial Paper Program were $140.2 million and $210.3 million respectively, with a weighted average interest rate of 1.21% and 0.93% (compared to $253.2 million and $348.7 million with a weighted average interest rate of 0.83% and 0.89% for the three months and year ended December 31, 2016).

Additionally, the Corporation is a party to a $75.0 million demand facility with a Canadian chartered bank for the purpose of issuing letters of credit mainly to support LDC's prudential requirements with the IESO ("Prudential Facility"). As at December 31, 2017, $38.4 million of letters of credit were issued against the Prudential Facility.

The Corporation filed a base shelf prospectus dated May 8, 2017 with the securities commissions or similar regulatory authorities in each of the provinces of Canada. These filings allow the Corporation to make offerings of unsecured debt securities of up to $1.0 billion during the 25-month period following the date of the prospectus.

On November 14, 2017, the Corporation issued $200.0 million senior unsecured debentures at a rate of 3.485% ("Series 13"). The Series 13 debentures due on February 28, 2048 were priced at $999.29 per $1,000 principal amount and bear interest payable semi-annually in arrears. The net proceeds were used to repay certain existing indebtedness and for general corporate purposes. Debt issuance costs of $1.4 million relating to the Series 13 debentures were recorded against the carrying amount of the debentures in the fourth quarter of 2017 and are amortized to finance costs using the effective interest method.

The Corporation's Series 2 debentures matured and were repaid on November 14, 2017.

As at December 31, 2017, the Corporation had debentures outstanding in the principal amount of $2.0 billion. These debentures will mature between 2019 and 2063. As at December 31, 2017, the Corporation was in compliance with all covenants included in its trust indenture and supplemental trust indentures.

The following table sets out the current credit ratings of the Corporation:

Credit Ratings
As at December 31, 2017

	DBRS		**Standard & Poor's**	
	Credit Rating	Trend	Credit Rating	Outlook
Issuer rating	A	Stable	A	Stable
Senior unsecured debentures	A	Stable	A	-
Commercial paper	R-1 (low)	Stable	-	-

The Corporation believes that it has sufficient available sources of liquidity and capital to satisfy working capital requirements for the next twelve months.

On March 2, 2017, the Board of Directors of the Corporation declared dividends in the amount of $6.25 million with respect to the first quarter of 2017 (March 31, 2016 – $44.6 million), which was paid to the City on March 31, 2017.

On May 11, 2017, the Board of Directors of the Corporation declared dividends in the amount of $6.25 million with respect to the second quarter of 2017 (June 30, 2016 – $6.25 million), which was paid to the City on June 30, 2017.

In connection with receipt of the equity investment from the City, the Board of Directors of the Corporation declared dividends payable to the City and approved amendments to the Corporation's Dividend Policy, as follows:

- In respect of fiscal 2017, an aggregate amount of $75.0 million shall be paid to the City, consisting of the two previously declared and paid instalments of $6.25 million each and a further $62.5 million. The $62.5 million was paid to the City on July 7, 2017.

- In respect of fiscal 2018 and subsequent fiscal years, 60% of the Corporation's consolidated net income after net movements in regulatory balances for the prior fiscal year shall be declared separately in four equal quarterly instalments, with each instalment payable to the City on the last business day of each fiscal quarter.

On March 7, 2018, the Board of Directors of the Corporation declared a quarterly dividend in the amount of $23.5 million, payable to the City by March 31, 2018.

Summary of Contractual Obligations and Other Commitments

The following table presents a summary of the Corporation's debentures, major contractual obligations and other commitments.

Summary of Contractual Obligations and Other Commitments
As at December 31, 2017
(in millions of Canadian dollars)

	Total $	2018 $	2019/2020 $	2021/2022 $	After 2022 $
Working Capital Facility	11.7	11.7	-	-	-
Commercial paper [1]	159.0	159.0	-	-	-
Debentures – principal repayment	2,045.0	-	250.0	300.0	1,495.0
Debentures – interest payments	1,471.3	75.7	143.1	121.3	1,131.2
Operating leases	1.4	0.3	0.6	0.5	-
Capital projects [2] and other	46.0	17.5	27.5	1.0	-
Finances leases	1.5	1.5	-	-	-
Total contractual obligations and other commitments	3,735.9	265.7	421.2	422.8	2,626.2

[1] The notes under the Commercial Paper Program were issued at a discount and are repaid at their principal amount.
[2] Primarily commitments for construction services and estimated capital contributions.

Corporate Developments

Changes to the Corporation's Board of Directors and Audit Committee

Effective January 1, 2017, the City, as the sole shareholder of the Corporation, re-appointed Councillor Paul Ainslie, Deputy Mayor Stephen Holyday (as the Mayor's designate), and Deputy Mayor Denzil Minnan-Wong to the Board of Directors for a term ending November 30, 2018, or until their successors are appointed.

On March 2, 2017, the Board of Directors of the Corporation confirmed the Chair of the Corporation, David McFadden, as an ex officio member of each of its Audit, Corporate Governance and Nominating, and Human Resources and Environment Committees, with all the responsibilities and privileges of the regular members of each committee.

Effective April 26, 2017, the City appointed Juliana Lam to the Board of Directors. The appointment is effective for a term ending April 26, 2019, or until her successor is appointed. Juliana Lam was appointed by the Board of Directors to the Audit Committee to replace Brian Chu who retired from the Audit Committee, effective May 11, 2017.

Effective December 10, 2017, the City re-appointed David McFadden, Brian Chu, Heather Zordel, the Honourable Howard Weston, Senator, Mary Ellen Richardson, Michael Nobrega and Tamara Kronis to the Board of Directors for a term ending December 10, 2019, or until their successors are appointed.

TORONTO HYDRO Corporation

Electricity Distribution Rates

The OEB's regulatory framework for electricity distributors is designed to support the cost-effective planning and operation of the electricity distribution network and to provide an appropriate alignment between a sustainable, financially viable electricity sector and the expectations of customers for reliable service at a reasonable price.

The OEB typically regulates the electricity rates for distributors using a combination of detailed cost of service reviews and IRM adjustments. Under the OEB's rate-setting methods, actual operating conditions may vary from forecasts such that actual returns achieved can differ from approved returns. Approved electricity rates are generally not adjusted as a result of actual costs or revenues being different from forecasted amounts, other than for certain prescribed costs that are eligible for deferral for future collection from, or refund to, customers.

On March 1, 2016 pursuant to LDC's 2015 – 2019 CIR application, the OEB set 2018 distribution rates on an interim basis. On August 23, 2017, LDC 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 LDC's 2018 rates, with an effective date of January 1, 2018, and the disposition of certain deferral and variance accounts.

Ontario's Fair Hydro Plan

On March 2, 2017, the Government of Ontario announced the OFHP, which includes a number of initiatives, some of which affect LDC or its customers.

OFHP includes the OREC, which came into effect on January 1, 2017. The OREC provides eligible customers with financial assistance in the form of an 8% rebate of the pre-tax cost of their electricity. The OREC rebates are administered by LDC and paid by the IESO in the month following customer billing. Current accounts receivable and unbilled revenue include the amount owing by the IESO to LDC. No effect on revenue or expense is recognized by LDC in respect of the OREC rebates.

OFHP also includes the OFHA, which enacted the Ontario Fair Hydro Plan Act, 2017 and amended the Electricity Act, 1998 and the Ontario Energy Board Act, 1998. The OFHA came into effect on June 1, 2017 and its impact is reflected in the Consolidated Financial Statements. The OFHA provides eligible customers with financial assistance through various changes to commodity pricing, new or amended programs, and eliminating or reducing certain provincial charges on the electricity bill. The OFHP reduces electricity bills by 25% on average for eligible customers, which includes the 8% OREC rebate. The OFHA reduces the total electricity bill for eligible customers and, accordingly, reduces current accounts receivable, unbilled revenue, accounts payable and accrued liabilities for LDC. No effect on distribution revenue or expense is recognized by LDC in respect of the OFHA.

CDM Activities

On March 26, 2014, the Minister of Energy of Ontario, under the guidance of sections 27.1 and 27.2 of the OEB Act, directed the OEB to amend the licence of each licensed electricity distributor to require the electricity distributor, as a condition of its licence, to make CDM programs available to its customers and to do so in relation to each customer segment in its service area, over the period beginning January 1, 2015 through December 31, 2020. On March 31, 2014, the Minister of Energy of Ontario issued a direction to require the OPA to coordinate, support and fund the delivery of CDM programs through electricity distributors. The objective of the CDM efforts is to reduce electricity consumption in the Province of Ontario by a total of 7 terawatt hours between January 1, 2015 and December 31, 2020, of which LDC's share is approximately 1,576 GWh of energy savings.

On November 13, 2014, LDC entered into an energy conservation agreement with the OPA for the delivery of CDM programs over the 2015-2020 period. The IESO and the OPA were merged under the name IESO starting on January 1, 2015.

Under the energy conservation agreement with the IESO, LDC has a joint CDM plan with Oakville Hydro Electricity Distribution Inc. ("Oakville Hydro") for the delivery of CDM programs over the 2015-2020 period. LDC can choose between full cost recovery funding, pay-for-performance funding, or a combination of both, on a CDM program by program basis. Under the full cost recovery funding method, the IESO reimburses LDC for all adequately documented incurred costs, with an option to receive a portion of its funding in advance. Cost efficiency incentives may be awarded

if LDC's electricity savings meet or exceed certain CDM plan targets for programs under the full cost recovery funding method, with a mid-term review to be performed by the IESO for the 2015-2017 period. Under the pay-for-performance funding method, LDC receives payment in arrears based on verified electricity savings achieved with various options for frequency of payment. The programs under the joint CDM plan with Oakville Hydro are only being offered under the full cost recovery funding method.

The joint CDM plan provides combined funding of approximately $425.0 million, including participant incentives and program administration costs to achieve an aggregate energy savings target of approximately 1,668 GWh. Oakville Hydro's programs under the joint CDM plan started on January 1, 2016. LDC received $44.9 million as at December 31, 2016 and $57.4 million in the year ended December 31, 2017 from the IESO for the delivery of CDM programs. Amounts received but not yet spent are presented on the consolidated balance sheets under current liabilities as deferred conservation credit. As at December 31, 2017, LDC estimated that approximately $12.9 million qualified as a joint mid-term incentive, of which $12.2 million represents LDC's portion and is included within accounts receivable.

Effective October 16, 2017, LDC entered into an agreement to transfer $4.0 million of funding and a corresponding 20 GWh of its energy savings target to another local distribution company. This agreement will decrease the joint CDM plan funding with Oakville Hydro to $421.0 million, with a revised energy savings target of 1,648 GWh. The revised CDM plan was approved by the IESO on December 14, 2017.

Legal Proceedings

In the ordinary course of business, the Corporation is subject to various legal actions and claims from customers, suppliers, former employees and other parties. On an ongoing basis, the Corporation assesses the likelihood of any adverse judgments or outcomes as well as potential ranges of probable costs and losses. A determination of the provision required, if any, for these contingencies is made after an analysis of each individual issue. The provision may change in the future due to new developments in each matter or changes in approach, such as a change in settlement strategy. If damages were awarded under these actions, the Corporation and its subsidiaries would make a claim under any applicable liability insurance policies which the Corporation believes would cover any damages which may become payable by the Corporation and its subsidiaries in connection with these actions, subject to such claim not being disputed by the insurers. There have been no material changes in legal proceedings as disclosed in note 25 to the Consolidated Financial Statements.

Share Capital

Share capital consists of the following:

	Number of Shares	$
Authorized The authorized share capital of the Corporation consists of an unlimited number of common shares without par value. All shares issued were fully paid.		
Issued and outstanding		
Common shares, beginning of the year	1,000	567.8
Common shares issued [1]	200	250.0
Common shares issued and outstanding, end of the year	1,200	817.8

[1] On June 28, 2017, the Corporation issued 200 common shares to the City for total proceeds of $250.0 million, net of share issue costs and expenses.

Transactions with Related Parties

As the City is the sole shareholder of the Corporation, the Corporation and the City are considered related parties. The Corporation provides electricity, street lighting and ancillary services to the City. All transactions with the City are conducted on terms similar to those offered to unrelated parties.

Summary of Transactions with Related Parties
(in millions of Canadian dollars)

	Year ended December 31	
	2017 **$**	**2016** **$**
Revenues	**283.3**	275.3
Operating expenses and capital expenditures	**22.2**	26.9
Dividends	**75.0**	63.4

Summary of Amounts Due to/from Related Parties
(in millions of Canadian dollars)

	As at December 31	
	2017 **$**	**2016** **$**
Accounts receivable	**13.8**	12.7
Unbilled revenue	**26.3**	23.2
Accounts payable and accrued liabilities	**40.1**	41.0
Customer deposits	**15.7**	14.1
Deferred revenue	**1.9**	3.5

Revenues represent amounts charged to the City primarily for electricity, street lighting and ancillary services. Operating expenses and capital expenditures represent amounts charged by the City for purchased road cut repairs, property taxes and other services. Dividends are paid to the City.

Accounts receivable represents receivables from the City primarily for electricity, street lighting and ancillary services. Unbilled revenue represents receivables from the City mainly related to electricity provided and not yet billed. Accounts payable and accrued liabilities represent amounts payable to the City related to road cut repairs and other services. Customer deposits represent amounts received from the City for future expansion projects. Deferred revenue represents amounts received from the City primarily for the construction of electricity distribution assets.

Controls and Procedures

For purposes of certain Canadian securities regulations, the Corporation is a "Venture Issuer". As such, it is exempt from certain requirements of National Instrument 52-109 Certification of Disclosure in Issuers' Annual and Interim Filings. Accordingly, the Chief Executive Officer and Chief Financial Officer have reviewed the Consolidated Financial Statements and the MD&A for the year ended December 31, 2017 and 2016. Based on their knowledge and exercise of reasonable diligence, they have concluded that these documents fairly present in all material respects the financial condition, financial performance and cash flows of the Corporation as at the date of and for the period presented.

Risk Management and Risk Factors

The Corporation faces various risks that could impact the achievement of its strategic objectives. It adopts an enterprise wide approach to risk management, achieved through a process of consolidating and aligning the various views of risk across the enterprise via a risk governance structure. The Corporation executes its ERM activities via an ERM framework that is aligned to industry best practices and international guidelines. The Corporation views ERM as a management activity undertaken to add value and improve overall operations. It helps the Corporation by enabling the attainment of its strategic goals and objectives through a systematic, disciplined approach towards identifying, evaluating, treating, monitoring and reporting of risks. Accordingly, ERM is an integral part of the strategic management of the Corporation and is routinely considered in forecasting, planning and executing all aspects of the business.

The ERM framework is operationalized by a consistent, disciplined methodology that clearly defines the risk management process which incorporates subjective elements, risk quantification and risk interdependencies.

While the Corporation's philosophy is that ERM is the responsibility of all business units, at all levels, in strategic and operational matters, the ERM governance structure is comprised of three key levels.

At the top level is the Board, which works to maintain a general understanding of the Corporation's risk profile, the risk categories, the types of risks to which the Corporation may be exposed and the practices used to identify, assess, measure and manage those risks. The risk profile is a list of key risks that represent the greatest threats to achieving the Corporation's strategic objectives.

The second level is the executive team, the lead body to ensure systems are in place to identify, manage, and monitor risks. Through its review of reports from the business and other areas, the executive team assesses the appropriateness and consistent application of systems to manage risks within the Corporation. The executive team also ensures that key risks are brought forward to the attention of the Board for discussion and action, as required.

Finally, the third level is the senior leadership team. The senior leadership team supports the executive team and is a collection of subject matter experts from across the Corporation who actively engage in the day-to-day management of risks. Working with the executive team, this group oversees the Corporation's risk profile, its performance against the defined risk appetite and determines appropriate risk responses. They also work to ensure effective, efficient, complete and transparent risk reporting to the executive team.

The Corporation's business is subject to a variety of risks including those described in the following sections. There can be no assurance that any steps the Corporation may take to manage risks will avoid future loss resulting from the occurrence of such risks.

Risks from External Influences

Ownership by the City and Inconsistent Policy Risk

The Corporation is subject to the risk that its shareholder can potentially limit the Corporation's ability to meet its business objectives as laid out in the Shareholder Direction principles. Under the Shareholder Direction, the City also has the power to direct the Corporation and its subsidiaries to conduct their affairs and govern their operations in accordance with such rules, policies, directives or objectives as are directed by City Council from time to time. These council approved directions can be inconsistent and/or divergent with the Shareholder Direction principles and could materially adversely affect the Corporation's business, operations, financial condition or prospects if the Corporation is required to comply with such directions.

Regulatory Risk

The Corporation is subject to the risk that its business activities may be impeded by the OEB (includes both traditional regulated Cost of Service work and non-traditional new ancillary service model work). There is a risk that future changes to Ontario's regulatory model, manner of regulation and/or broader government policy framework does not align with the Corporation's business direction and could materially adversely affect the Corporation's strategic goals and financial results.

Ontario's electricity industry regulatory developments may affect the electricity distribution rates charged by LDC and the costs LDC is permitted to recover. This may in turn have a material adverse effect on the financial performance of the Corporation and/or LDC's ability to deliver effective and efficient operations and reliable service to its customers, and as well as create barriers to LDC achieving its strategic objectives. Among other things, there can be no assurance that:

- the OEB will approve LDC's electricity distribution rates, at levels that will permit LDC to carry out its planned capital expenditures required to maintain safe and reliable service to its customers and earn the allowed rate of return on the investment in the business;
- all capital expenditures incurred by LDC will be approved by the OEB. In particular, capital cost overruns due to project delays or increased costs may not be recoverable in distribution rates;
- the regulatory instruments that are made available to LDC will be sufficient to address LDC's operations, needs and circumstances in respect of future applications for electricity distribution rates;
- the OEB will not set a lower recovery for LDC's cost of capital;
- the full cost of providing service to distribution customers will be permitted to be recovered through LDC's electricity distribution rates;
- the OEB will not permit competitors to provide distribution services in LDC's licensed area, or permit loads within LDC's service area to become electrically served by a means other than through LDC's electricity distribution system;
- the OEB will allow recovery for revenue lost as a consequence of unanticipated effects of CDM;
- parts of LDC's services will not be separated from LDC and opened to competition; or
- regulatory or other changes will not be made to the PILs regime.

Any future regulatory decision to disallow or limit the recovery of costs could lead to potential asset impairment and charges to results from operations, which could have a material adverse effect on the Corporation.

Political and Legislative Risk

The Corporation is subject to the risk that government bodies and policy priorities of government may impact the Corporation's ability to deliver effective and efficient operations and meet business objectives. Changes to any of the laws, rules, regulations and policies applicable to the businesses carried on by the Corporation could materially adversely affect the Corporation. There can be no assurance that the Corporation will be able to comply with applicable future laws, rules, regulations and policies. Failure by the Corporation to comply with applicable laws, rules, regulations and policies may subject the Corporation to civil or regulatory proceedings that could have a material adverse effect on the Corporation. The OEB may not allow recovery for the costs of coming into or maintaining compliance with these laws, rules, regulations and policies.

Risks to Maintaining Operations

Human Capital Risk

The Corporation is subject to the risk that human resources may not be available with the necessary knowledge, skills and education to support the Corporation's future talent requirements. All retirements pose risks for knowledge management and business continuity, both at the Corporation and the industry. Development and retention of talent to meet the evolving needs of the business requires LDC to focus on a series of proactive activities and programs to mitigate these risks, such as strategic workforce planning, promotion of apprenticeship programs, investments in colleges and universities, succession planning, knowledge transfer and a robust training program.

The Corporation's ability to operate successfully in the electricity industry in Ontario will continue to depend in part on its ability to make changes to existing work processes and conditions in order to adapt to changing circumstances. The Corporation's ability to make such changes, in turn, will continue to depend in part on its relationship with its

labour unions including reaching a new collective bargaining agreement with Power Workers' Union. There can be no assurance that the Corporation will be able to secure the support of its labour unions.

Strategy and Business Model Risk

The Corporation is subject to the risk that it may fail to monitor the external environment and or develop and pursue strategies through appropriate business models, thus failing to gain a strategic advantage, which could materially adversely affect the Corporation. The OEB distribution licence issued to LDC stipulates a service area that reflects the territory within the City. By law, only the OEB can grant such a licence for a service area and only an entity with such a licence can provide licenced services to the public-at-large within a service area. The OEB has not granted any other distribution licence that permits distribution within LDC's service area. In addition to this regulatory barrier to entry, there are other barriers to entry, including the cost of constructing an electricity distribution system, physical space limitations within and legal access to the right-of-way, the specialized skills associated with the distribution business, the level of expertise required to achieve operational and regulatory compliance, and LDC's relationships with its customers. There can be no assurance that these barriers will continue to be sufficient to prevent this type of competition. Other regulated and unregulated entities have always competed with LDC and its predecessors to provide customers with other sources of energy, including electricity. The pervasiveness of this competition and its effects on LDC's distribution business have varied over time and continue to vary based on many factors, including the relative price of energy source (e.g., natural gas, grid-supplied electricity, behind-the-meter generation) and technology advancements (e.g., multi-unit building sub-metering, micro-grids, electricity storage).

There can be no assurance that the future nature, prevalence, or effects of these forms of competition will be comparable to current or historic experience. Failure to effectively scan our external and internal environment could lead to missed business opportunities and loss of competitive advantage (see "Customer Risk" section for additional details).

Asset Integrity Risk

The Corporation is subject to the risk that it may be unable to maintain continuous supply due to failure of the existing distribution infrastructure and assets which could materially adversely affect the Corporation. Electricity distribution is a capital-intensive business. As the municipal electricity distribution company serving the largest city in Canada, LDC continues to invest in the renewal of existing aging infrastructure and in the development of new infrastructure (such as the Copeland Station project) to address safety, reliability and customer service requirements.

LDC estimates that approximately one-third of its electricity distribution assets have already exceeded or will reach the end of their expected useful lives within the next 5-year period. At the same time, Toronto is a growing city, and LDC must make system upgrades to expand its capacity to keep pace with urban intensification and electrification. In addition, as the City, Ontario and the Government of Canada implement policies and programs to respond to climate change, the pressures on the Corporation's system will only increase. Widespread adoption of electric vehicles, fuel switching and changing emissions standards make electricity the comparatively clean energy choice. This drives the need for significant capital expenditures for system upgrades so that the grid can handle such increased load. LDC's ability to continue to provide a safe work environment for its employees and a reliable and safe distribution service to its customers and the general public will depend on, among other things, the ability of the Corporation to fund additional infrastructure, and the OEB allowing recovery of costs in respect of LDC's maintenance program and capital expenditure requirements for distribution plant refurbishment and replacement.

One of LDC's largest capital initiatives currently in progress is the construction of Copeland Station, which is also one of the most complex projects ever undertaken by the Corporation. Due to unforeseen delays, the expected completion date for the Copeland Station project has been extended to 2018 and it is currently anticipated that the total expenditure required to complete the project will increase from $195.0 million to approximately $200.0 million, plus capitalized borrowing costs as applicable. There may be additional unforeseen delays and expenditures prior to the completion of the project. On January 25, 2017, the Corporation was informed that Carillion Construction Inc., the general contractor for the Copeland Station Project, filed for creditor protection under the Companies' Creditors Arrangement Act after its affiliate, Carillion plc, went into compulsory liquidation in the United Kingdom.

All capital projects for new and replacement infrastructure have risks related to delays or increased costs due to many factors, including: necessary modifications to project plans; the availability, scheduling and cost of materials,

equipment and qualified personnel; LDC's ability to obtain necessary environmental and other regulatory and governmental approvals; and the impact of weather conditions, site conditions and contractor performance.

LDC is focused on overcoming the above challenges and executing its capital and maintenance programs. However, if LDC is unable to carry out these plans in a timely and optimal manner or becomes subject to significant unforeseen equipment failures, equipment performance will degrade. Such degradation may compromise the reliability of distribution assets, the ability to deliver sufficient electricity and/or customer supply security and increase the costs of operating and maintaining these assets.

Occupational Health and Safety Risk

The Corporation is subject to the risk that employees may be exposed to serious or fatal injuries or illness as a result of the work environment in which they operate. Due to the nature of the Corporation's business and business activities, occupational safety is an integral part of our corporate culture. Employees could be exposed to hazards when performing their work duties. This includes hazards such as electrical contact, working in confined spaces, fires and explosions, slips, trips and falls and motor vehicle accidents. The Corporation is subject to compliance with provincial Health and Safety legislation. The Corporation's management approach to occupational safety is to meet or excel on legal compliance and eliminate or safeguard known occupational hazards and risks. There are processes in place to develop and nurture good leadership practices through recruitment, education, training and performance management practices that encourage the application of our corporate values, including safety. LDC received OHSAS 18001 certification in 2013 and conducts annual third party audits to maintain certification, in addition occupational health and safety legal compliance audits are conducted every two years.

Customer Risk

The Corporation is subject to the risk that it may fail to identify and meet its customers' needs and expectations, within approved OEB funding levels, and consequently customers leave the Corporation's distribution area or opt for alternative sources of electricity. This includes all customer classes, but is primarily related to general service and large users. This may lead to erosion of the Corporation's revenue base and monopoly position. It is important that the Corporation maintains its relationship with its customers to better understand the specific needs and expectations of each class. The political environment and government policy regarding the energy sector may impact customer satisfaction and perception of value, especially with concerns around hydro costs. The Corporation is taking steps to help its customers through cost saving CDM programs. Service interruptions due to increasing weather events, or unexpected events could further impact customer satisfaction and service quality (see "Business Interruption Risk" section for additional details).

Advances in technology may compete with the Corporation by affecting energy consumption levels and, as a result, customer demand for the Corporation's services could be negatively impacted in a material way. As customers increasingly prioritize energy efficiency and awareness of energy costs, and governments increasingly provide subsidies to encourage energy efficiency, primarily in response to climate change concerns, there will be a corresponding increase in the demand for technologies that enable customers to better monitor and minimize their energy consumption and otherwise exercise greater control over their electricity supply and demand. For example, distributed generation technologies draw on renewable sources of energy, such as solar power and wind, allowing customers to generate their own supply of electricity. The effect of such technologies may be reduced reliance on larger-scale utilities such as the Corporation. Likewise, energy-efficient homes and improvements to energy storage technologies like batteries may further affect consumption levels and the demand for the Corporation's services. Although OEB's current policy is moving residential customers to fixed delivery charges as opposed to consumption-based delivery charges, as technologies continue to advance and become more widely adopted, the Corporation may be required to make changes to its business and operations, which may present additional risks and challenges for the Corporation.

The Corporation is affected by energy demand which may change as a result of technology change, available customer choice and CDM programs, as well as general economic conditions, energy prices, disposable income and population growth, among other things. Reduced or increased energy demand could have a material adverse effect on the Corporation's business, operations, financial condition or prospects, as well as on the Corporation's need for, and ability to, fund future capital expenditures.

Information Technology and Cybersecurity Risk

The Corporation is subject to the risk that it may be unable to preserve the confidentiality, integrity, authenticity, availability, accountability and non-repudiation of information assets. The Corporation's ability to operate effectively is in part dependent on the development, maintenance and management of complex information technology systems. Computer systems are employed to operate LDC's electricity distribution system, and the Corporation's financial, billing and business systems to capture data and to produce timely and accurate information. Failures of any one of the financial, business and operating systems could have a material adverse effect on the Corporation's business, operations, financial condition or prospects. The Corporation mitigates this risk through various methods including the implementation of high availability and redundancy in its core infrastructure and application components. Operational technology systems are isolated from business systems and operate independently.

LDC's electricity distribution infrastructure and technology systems are also potentially vulnerable to damage or interruption from cyber-attacks, breaches or other compromises, which could result in business interruption, service disruptions, theft of intellectual property and confidential information (about customers, suppliers, counterparties and employees), additional regulatory scrutiny, litigation and reputational damage. The Corporation has implemented security controls aligned with industry best practices and standards including the National Institute of Standards and Technology Cybersecurity Framework, and maintains cyber insurance. Cyber-attacks, breaches or other compromises of electricity distribution infrastructure and technology systems could result in service disruptions and system failures, including as a result of a failure to provide electricity to customers, property damage, corruption or unavailability of critical data or confidential employee or customer information. A significant breach could materially adversely affect the financial performance of the Corporation or its reputation and standing with customers, regulators and in the financial markets. It could also expose the Corporation to third-party claims.

LDC must also comply with legislative and licence requirements relating to the collection, use and disclosure of personal information (including the personal information of customers), as well as information provided by suppliers, contractors, employees, counterparties, and others. Such information could be exposed in the event of a cybersecurity incident or other unauthorized access, which could materially adversely affect the Corporation and also result in third-party claims against the Corporation.

Preventative controls are employed to protect information and technology assets against cyber-attacks and mitigate their effects. Detective controls are employed to continuously monitor information systems so that the Corporation can respond appropriately to minimize the damage in the event of a cyber-attack. Even with these measures in place, since the techniques used to obtain unauthorized access, disable or degrade service, or sabotage systems change frequently and often are not recognized until launched against a target, the Corporation may be unable to anticipate these techniques or to implement adequate preventative measures. As such, there can be no assurance that such measures will be effective in protecting LDC's electricity distribution infrastructure or assets, or the personal information of its customers, from a cyber-attack or the effects therefrom.

Brand and Reputation Risk

The Corporation is subject to the risk that an action or inaction by it or its representatives will impair the Corporation's image in the community, public confidence or brand. The Corporation is committed to delivering safe and reliable electricity to its customers in an environmentally responsible manner at optimal costs. Failure to deliver on our commitment could impact the public's perception of the Corporation. In addition, events and/or external factors that draw negative media attention to the Corporation could cause reputational damages and impact the Corporation's business and relationship with its stakeholders.

Business Interruption Risk

The Corporation is subject to the risk that it may be unable to maintain continuing and sustainable business operations, or recover from business interruption, in an effective manner. The Corporation's operations are exposed to the effects of natural and other unexpected occurrences such as extreme storm and other weather conditions and natural disasters, as well as terrorism and pandemics. Although the Corporation's facilities and operations are constructed, operated and maintained to withstand such occurrences, there can be no assurance that they will successfully do so in all circumstances. Any major damage to the Corporation's facilities or interruption of the Corporation's operations arising from these occurrences could result in lost revenues and repair costs that can be substantial. Although the Corporation has insurance which it considers to be consistent with industry practice, if it sustained a large uninsured loss caused

by natural or other unexpected occurrences, LDC may apply to the OEB for the recovery of the loss related to the electricity distribution system. There can be no assurance that the OEB would approve, in whole or in part, such an application.

Risks to Maintaining Financial Condition

Capital Structure Risk

The Corporation is subject to the risk that it may not be able to optimize its debt to equity ratio or access capital markets at effective rates. There can be no assurance that debt or equity financing will be available or sufficient to meet the Corporation’s requirements, objectives, or strategic opportunities. If and when financing is available, there can be no assurance that it will be on acceptable terms to the Corporation.

The Corporation relies on debt financing through its MTN Program, CP Program or existing credit facilities to finance the Corporation's daily operations, repay existing indebtedness, and fund capital expenditures. The Corporation's ability to arrange sufficient and cost-effective debt financing could be materially adversely affected by a number of factors, including financial market conditions and activity in the global capital markets, the regulatory environment in Ontario, the Corporation's business, operations, financial condition or prospects, compliance with covenants, the ratings assigned to the Corporation or the debentures issued under the Corporation's MTN Program by credit rating agencies, the rating assigned to short-term borrowings under the CP Program by a credit rating agency, and the availability of the commercial paper market.

In the event the Corporation is unable to maintain an R-1 (low) credit rating for its CP Program, the Corporation has sufficient liquidity through its Revolving Credit Facility to repay its commercial paper obligations as they become due.

Market and Credit Risk

The Corporation is directly and indirectly subject to various market and credit fluctuations which could materially adversely affect the Corporation. For example, LDC is exposed to credit risk with respect to customer non-payment of electricity bills. LDC is permitted, at certain times of the year, to mitigate the risk of customer non-payment using any means permitted by law, including security deposits (i.e. letters of credit, surety bonds, cash deposits or lock-box arrangements, under terms prescribed by the OEB), late payment penalties, pre-payment, pre-authorized payment, load limiters or disconnection. While LDC would be liable for the full amount of the default, there can be no assurance that the OEB would allow recovery of the bad debt expense. Established practice in such cases is that the OEB would examine any electricity distributor's application for recovery of extraordinary bad debt expenses on a case-by-case basis. LDC’s security interest or other measures, if any, may also not provide sufficient protection. Additionally, security interests and other measures taken by, or in favour of, LDC, if any, may not provide sufficient protection.

The Corporation is exposed to fluctuations in interest rates for the valuation of its post-employment benefit obligations. The Corporation estimates that a 1% (100 basis point) increase in the discount rate used to value these obligations would decrease the accrued benefit obligation of the Corporation, as at December 31, 2017, by $46.8 million, and a 1% (100 basis point) decrease in the discount rate would increase the accrued benefit obligation, as at December 31, 2017, by $60.2 million.

The Corporation is exposed to short-term interest rate risk on the short-term borrowings under its CP Program and Working Capital Facility, and customer deposits, while most of its remaining obligations were either non-interest bearing or bear fixed interest rates, and its financial assets were predominately short-term in nature and mostly non-interest bearing. The Corporation manages interest rate risk by monitoring its mix of fixed and floating rate instruments, and taking action as necessary to maintain an appropriate balance. The Corporation estimates that a 100 basis point increase (decrease) in short-term interest rates, with all other variables held constant, would result in an increase (decrease) of approximately $2.3 million to annual finance costs.

The Corporation had limited exposure to the changing values of foreign currencies. While the Corporation purchases goods and services which are payable in US dollars, and purchases US currency to meet the related commitments when required, the impact of these transactions as at December 31, 2017 was not material.

TORONTO HYDRO Corporation

Critical Accounting Estimates

The preparation of the Corporation's Consolidated Financial Statements in accordance with IFRS requires management to make judgments, estimates and assumptions which affect the application of accounting policies, reported assets, liabilities and regulatory balances, and the disclosure of contingent assets and liabilities at the date of the Consolidated Financial Statements, and the reported revenues and expenses for the year. The estimates are based on historical experience, current conditions and various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities as well as for identifying and assessing the accounting treatment with respect to commitments and contingencies. Actual results could differ from those estimates, including changes as a result of future decisions made by the OEB, the IESO, the Ontario Ministry of Energy or the Ontario Ministry of Finance.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to estimates are recognized prospectively. Assumptions and estimates with a significant risk of resulting in a material adjustment within the next financial year are used in the following:

- Note 26(b) – Recognition and measurement of regulatory balances;
- Note 26(j) – Revenue recognition – measurement of unbilled revenue, determination of the CDM incentive;
- Notes 26(f) and 26(g) – Determination of useful lives of depreciable assets;
- Notes 26(m) and 14 – Measurement of post-employment benefits – key actuarial assumptions;
- Notes 26(o) and 21 – Recognition of deferred tax assets – availability of future taxable income against which deductible temporary differences and tax loss carryforwards can be used; and
- Note 25 – Recognition and measurement of provisions and contingencies.

Significant Accounting Policies

The Corporation's Consolidated Financial Statements have been prepared in accordance with IFRS with respect to the preparation of financial information. The Consolidated Financial Statements are presented in Canadian dollars, which is the Corporation's functional currency. The significant accounting policies of the Corporation are summarized in notes 2 and 26 to the Consolidated Financial Statements.

Changes in Accounting Policies

In January 2016, the IASB issued amendments to IAS 7 *Statement of Cash Flows* as part of the IASB's Disclosure Initiative. These amendments require entities to provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including changes from cash flows and non-cash changes. These amendments are effective for annual periods beginning on or after January 1, 2017. The additional disclosures relating to changes in liabilities arising from financing activities are included in note 22 to the Consolidated Financial Statements and have no impact to the Corporation's financial position or results of operations.

Future Accounting Pronouncements

A number of new standards, amendments and interpretations are not yet effective for the year ended December 31, 2017, and have not yet been applied in preparing the Consolidated Financial Statements.

Revenue from Contracts with Customers

In May 2014, the IASB issued IFRS 15 *Revenue from Contracts with Customers* ("IFRS 15"), which replaces existing revenue recognition guidance, including IAS 18 *Revenue* and IFRIC 18 *Transfers of Assets from Customers*. IFRS 15 contains a single model that applies to contracts with customers with two methods for recognizing revenue: at a point in time or over time. IFRS 15 is effective for annual periods beginning on or after January 1, 2018.

The Corporation will adopt IFRS 15 on January 1, 2018 using the modified retrospective approach. The Corporation has completed its assessment of the key revenue streams. The majority of the Corporation's revenue (energy sales and distribution revenue) is generated from electricity distribution at regulated prices. The Corporation concluded that IFRS 15 will not have a material impact on the accounting for these revenue streams. Upon adoption of IFRS 15, there will be a $167.6 million income statement reclassification between Energy Sales and Energy Purchases for the comparative year ended December 31, 2017 and no impact to opening retained earnings as at January 1, 2018. The

Corporation is currently finalizing its assessment on capital contributions. The Corporation has determined that IFRS 15 will also increase its required disclosure on revenue streams.

Financial Instruments

In July 2014, the IASB issued the final version of IFRS 9 *Financial Instruments* ("IFRS 9"), which replaces IAS 39 *Financial Instruments: Recognition and Measurement* ("IAS 39"). IFRS 9 includes revised guidance on the classification and measurement of financial instruments, including a new expected credit loss model for measuring impairment on financial assets, and new general hedge accounting requirements. It also carries forward the guidance on recognition and derecognition of financial instruments from IAS 39. The standard is effective for annual periods beginning on or after January 1, 2018, and will be applied retrospectively with some exceptions. The Corporation has assessed the impact of adopting IFRS 9, and concluded that the new classification under IFRS 9 will not have a material impact on the consolidated financial statements. Management is currently evaluating the impact of adopting the new expected credit loss model for measuring impairment.

Leases

In January 2016, the IASB issued IFRS 16 *Leases* ("IFRS 16"), which replaces IAS 17 *Leases* ("IAS 17") and related interpretations. IFRS 16 introduces a single lessee accounting model eliminating the current distinction between finance and operating leases. It requires the recognition of lease-related assets and liabilities on the balance sheet, except for short-term leases and leases of low value underlying assets. In addition, the nature and timing of expenses related to leases will change, as IFRS 16 replaces the straight-line operating leases expense with the depreciation expense for the assets and interest expense on the lease liabilities. Lessor accounting remains substantially unchanged. The standard is effective for annual periods beginning on or after January 1, 2019, and may be applied either retrospectively or using a modified retrospective approach. Early adoption is permitted if IFRS 15 is also adopted.

The Corporation intends to early adopt IFRS 16 on January 1, 2018. The Corporation has completed its assessment of existing operating leases. IFRS 16 will not have a significant impact on the Corporation's consolidated financial statements and the Corporation has assessed the quantitative impact of adopting IFRS 16 to be $nil in opening retained earnings, and an increase of $1.6 million in total assets and total liabilities for the right-of-use assets and the lease liabilities, respectively, as at January 1, 2018.

Forward-Looking Information

Certain information included in this MD&A constitutes "forward-looking information" within the meaning of applicable securities legislation. The purpose of the forward-looking information is to provide the Corporation's current expectations regarding future results of operations, performance, business prospects and opportunities and may not be appropriate for other purposes. All information, other than statements of historical fact, which address activities, events or developments that we expect or anticipate may or will occur in the future, are forward-looking information. The words "anticipates", "believes", "budgets", "committed", "can", "could", "estimates", "expects", "focus", "forecasts", "future", "intends", "may", "might", "plans", "propose", "projects", "schedule", "seek", "should", "trend", "will", "would", "objective", "outlook" or the negative or other variations of these words or other comparable words or phrases, are intended to identify forward-looking information, although not all forward-looking information contains these identifying words. The forward-looking information reflects the Corporation's current beliefs and is based on information currently available to the Corporation.

Specific forward-looking information in the MD&A includes, but is not limited to, the statements regarding the settlement variance and other regulatory balance variances as described in the section entitled "Results of Operations"; the effect of changes in energy consumption on future revenue as described in the sections entitled "Summary of Quarterly Results of Operations" and "Risk Management and Risk Factors"; the Corporation's plans to finance the investment in LDC's infrastructure and, the Corporation's available sources of liquidity and capital resources and the sufficiency thereof to satisfy working capital requirements for the next twelve months as described in the section entitled "Liquidity and Capital Resources"; the planned and proposed capital initiatives and the expected results of such initiatives as described in the section entitled "Liquidity and Capital Resources"; the expected capital expenditures required to complete Copeland Station and the anticipated completion date for Copeland Station as described in the section entitled "Liquidity and Capital Resources" and "Risk Management and Risk Factors"; the anticipated contractual obligations and other commitments of the Corporation over the next five years as set out in the section entitled "Liquidity and Capital Resources"; the payment of dividends as described in the section entitled

"Liquidity and Capital Resources"; plans to meet CDM targets as described in the section entitled "Corporate Developments"; the Corporation's expectation that cash generated from operations, after the payment of dividends, is not expected to be sufficient to repay existing indebtedness, fund capital expenditures and meet other liquidity requirements over the next 12 months as described in the section entitled "Risk Management and Risk Factors"; the ability to claim under applicable liability insurance policies and/or pay any damages with respect to legal actions and claims as described in the section entitled "Legal Proceedings"; the Corporation's reliance on debt financing through its medium-term note program, Commercial Paper Program or existing credit facilities to finance the Corporation's daily operations, repay existing indebtedness, and fund capital expenditures as described in the section entitled "Risk Management and Risk Factors"; the effect of changes in interest rates and discount rates on future revenue requirements and future post-employment benefit obligations, respectively, as described in the section entitled "Risk Management and Risk Factors"; the Corporation's plans to attract, train and retain skilled employees and mitigate risks from retiring employees as described in the section entitled "Risk Management and Risk Factors"; the possibility that advances in technology may compete with the Corporation by affecting energy consumption levels and, as a result, customer demand for the Corporation's services as described in the section entitled "Risk Management and Risk Factors"; the expectation that one-third of the Corporation's electricity distribution assets have already exceeded or will reach the end of their expected useful lives within the next 5-year period as described in the section entitled "Risk Management and Risk Factors";; and the adoption and impact of new standards, amendments and interpretations on the Corporation's consolidated financial statements in the section entitled "Future Accounting Pronouncements".

The forward-looking information is based on estimates and assumptions made by the Corporation's management in light of past experience and perception of historical trends, current conditions and expected future developments, as well as other factors that management believes to be reasonable in the circumstances, including, but not limited to, the amount of indebtedness of the Corporation, changes in funding requirements, the future course of the economy and financial markets, no unforeseen delays and costs in the Corporation's capital projects (including Copeland Station), no unforeseen changes in the legislative and operating framework for Ontario's electricity market, the receipt of applicable regulatory approvals and requested rate orders, no unexpected delays in obtaining required approvals, the receipt of applicable IESO approvals for mid-term CDM incentives, the ability of the Corporation to obtain and retain qualified staff, equipment and services in a timely and cost efficient manner, the receipt of favourable judgments, no unforeseen changes in rate orders or rate setting methodologies, no unfavourable changes in environmental regulation, the level of interest rates and the Corporation's ability to borrow, and assumptions regarding general business and economic conditions.

The forward-looking information is subject to risks, uncertainties and other factors that could cause actual results to differ materially from historical results or results anticipated by the forward-looking information. The factors which could cause results or events to differ from current expectations include, but are not limited to, risks associated with the execution of the Corporation's capital and maintenance programs necessary to maintain the performance of our aging distribution assets and make required infrastructure improvements; risks associated with capital projects, including Copeland Station; risks associated with electricity industry regulatory developments and other governmental policy changes; risks associated with the timing and results of regulatory decisions regarding the Corporation's revenue requirements, cost recovery and rates; risks associated with information system security and with maintaining complex information technology systems; risk to the Corporation's facilities and operations posed by unexpected weather conditions caused by climate change and other factors, terrorism and pandemics and the Corporation's limited insurance coverage for losses resulting from these events; risks associated with being controlled by the City, including the risk that the City could introduce rules, policies or directives that can potentially limit the Corporation's ability to meet its business objectives as laid out in the Shareholder Direction principles; risks related to the Corporation's work force demographic and its potential inability to attract, train and retain skilled employees; risks associated with possible labour disputes and the Corporation's ability to negotiate appropriate collective agreements; risk that the Corporation may fail to monitor the external environment and or develop and pursue strategies through appropriate business models, thus failing to gain a strategic advantage; risk that the Corporation is not able to arrange sufficient and cost-effective debt financing to repay maturing debt and to fund capital expenditures and other obligations; risk of downgrades to the Corporation's credit rating; risks related to the timing and extent of changes in prevailing interest rates and discounts rates and their effect on future revenue requirements and future post-employment benefit obligations; risk of substantial and currently undetermined or underestimated environmental costs and liabilities; risk that assumptions that form the basis of the Corporation's recorded environmental liabilities and related regulatory balances may change; risk that the presence or release of hazardous or harmful substances could lead to claims by third parties and/or governmental orders and other factors which are discussed in more detail under the section entitled "Risk Management and Risk Factors" in this MD&A. Please review this section – "Risk Management and Risk Factors" in detail. All of the forward-looking information included in this MD&A is qualified by the cautionary

statements in this "Forward-Looking Information" section and the "Risk Management and Risk Factors" section of this MD&A. These factors are not intended to represent a complete list of the factors that could affect the Corporation; however, these factors should be considered carefully and readers should not place undue reliance on forward-looking information made herein. Furthermore, the forward-looking information contained herein is dated as of the date of this MD&A or as of the date specified in this MD&A, as the case may be, and the Corporation has no intention and undertakes no obligation to update or revise any forward-looking information, whether as a result of new information, future events or otherwise, except as required by law.

TORONTO HYDRO Corporation

Selected Annual Information

The following table sets forth selected annual financial information of the Corporation for the three years ended December 31, 2017, 2016 and 2015. This information has been derived from the Corporation's consolidated financial statements.

Selected Annual Consolidated Financial Information
(in millions of Canadian dollars)

	2017 $	2016 $	2015 $
Year Ended December 31			
Total Revenues [1]	3,849.7	4,030.0	3,539.9
Net income after net movements in regulatory balances [1]	156.5	151.4	126.7
As at December 31			
Total assets and regulatory balances [2]	5,226.2	4,954.4	4,686.9
Total debentures [2,3]	2,034.0	2,084.6	1,885.1
Other non-current financial liabilities [4]	9.1	17.3	16.6
Total equity [2]	1,760.4	1,428.9	1,340.9
Dividends [5]	75.0	63.4	56.3

[1] See "Results of Operations" for further details on distribution revenue, other revenue, and net income after net movements in regulatory balances.

[2] See "Financial Position" for further details of significant changes in assets, debentures and shareholder's equity.

[3] Total debentures include current and long-term debentures.

[4] Other non-current financial liabilities include primarily non-current obligations under capital lease and non-current customer deposits. Under IFRS, deposits that are due or will be due on demand within one year from the end of the reporting period have been reclassified to other current financial liabilities.

[5] See "Liquidity and Capital Resources" for further details on dividends.

Additional Information

Additional information with respect to the Corporation (including its annual information form) is available on the System for Electronic Document Analysis and Retrieval website at www.sedar.com.

Toronto, Canada

March 7, 2018

CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2017 AND 2016

See Financial Report for abbreviations and defined terms
used in the audited consolidated financial statements.

MANAGEMENT'S REPORT

The accompanying Consolidated Financial Statements have been prepared by management of Toronto Hydro Corporation (the "Corporation"), who are responsible for the integrity, consistency and reliability of the information presented. The Consolidated Financial Statements have been prepared in accordance with International Financial Reporting Standards and applicable securities legislation.

The preparation of the Consolidated Financial Statements necessarily involves the use of estimates and assumptions based on management's judgments, particularly when transactions affecting the current accounting period cannot be finalized with certainty until future periods. Estimates and assumptions are based on historical experience, current conditions and various other assumptions believed to be reasonable in the circumstances, with critical analysis of the significant accounting policies followed by the Corporation as described in Note 26 to the Consolidated Financial Statements. The preparation of the Consolidated Financial Statements includes information regarding the estimated impact of future events and transactions. Actual results in the future may differ materially from the present assessment of this information because future events and circumstances may not occur as expected. The Consolidated Financial Statements have been prepared within reasonable limits of materiality in light of information available up to March 7, 2018.

In meeting its responsibility for the reliability of financial information, management maintains and relies on a comprehensive system of internal controls and internal audit, which is designed to provide reasonable assurance that the financial information is relevant, reliable and accurate, and that the Corporation's assets are safeguarded and transactions are properly authorized and executed. The system includes formal policies and procedures and appropriate delegation of authority and segregation of responsibilities within the organization. An internal audit function evaluates the effectiveness of these internal controls and reports its findings to management and the Audit Committee of the Corporation, as required.

The Board of Directors, through its Audit Committee, is responsible for overseeing management in the performance of its financial reporting and internal controls. The Audit Committee is composed of independent directors and meets periodically with management, the internal auditors and the external auditors to discuss internal controls over the financial reporting process, auditing matters and financial reporting issues, to satisfy itself that each group has properly discharged its respective responsibility and to review the Consolidated Financial Statements before recommending approval by the Board of Directors. The Audit Committee also considers, for review by the Board of Directors and approval by the shareholder, the appointment of the external auditors. The external auditors have direct and full access to the Audit Committee, with and without the presence of management, to discuss their audit and their findings as to the integrity of the financial reporting and the effectiveness of the system of internal controls.

The Consolidated Financial Statements were reviewed by the Audit Committee, and on their recommendation, were approved by the Board of Directors. The Consolidated Financial Statements have been examined by KPMG LLP, independent external auditors appointed by the Corporation's shareholder. The external auditors' responsibility is to express their opinion on whether the Consolidated Financial Statements are fairly presented in accordance with International Financial Reporting Standards. The attached Independent Auditors' Report outlines the scope of their examination and their opinion.

On behalf of Toronto Hydro Corporation's management:

"Anthony Haines"	*"Sean Bovingdon"*
Anthony Haines	Sean Bovingdon
President and Chief Executive Officer	Executive Vice-President and Chief Financial Officer

KPMG LLP
Chartered Professional Accountants
Bay and Adelaide Centre
Suite 4600
333 Bay Street
Toronto, ON M5H 2S5

Telephone (416) 777-8500
Fax (416) 777-8818
www.kpmg.ca

INDEPENDENT AUDITORS' REPORT

To the Shareholder of Toronto Hydro Corporation

We have audited the accompanying consolidated financial statements of Toronto Hydro Corporation, which comprise the consolidated balance sheets as at December 31, 2017 and December 31, 2016, the consolidated statements of income, comprehensive income, changes in equity and cash flows for the years ended December 31, 2017 and December 31, 2016, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of Toronto Hydro Corporation as at December 31, 2017 and December 31, 2016, and its consolidated financial performance and its consolidated cash flows for the years ended December 31, 2017 and December 31, 2016 in accordance with International Financial Reporting Standards.

KPMG LLP

Chartered Professional Accountants, Licensed Public Accountants
March 7, 2018
Toronto, Canada

KPMG LLP is a Canadian limited liability partnership and a member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. KPMG Canada provides services to KPMG LLP.

TORONTO HYDRO Corporation

CONSOLIDATED BALANCE SHEETS

[in millions of Canadian dollars]

As at December 31	2017 $	2016 $
ASSETS		
Current		
Accounts receivable *[notes 4 and 16[b]]*	**217.7**	229.8
Unbilled revenue *[note 16[b]]*	**278.3**	320.5
Materials and supplies	**9.3**	9.7
Other assets *[note 5]*	**12.7**	13.5
Assets held for sale *[note 8]*	**8.7**	-
Total current assets	**526.7**	573.5
Property, plant and equipment *[note 6]*	**4,143.4**	3,907.2
Intangible assets *[note 7]*	**296.2**	217.8
Deferred tax assets *[note 21]*	**57.0**	63.8
Other assets *[note 5]*	**3.0**	1.3
Total assets	**5,026.3**	4,763.6
Regulatory balances *[note 9]*	**199.9**	190.8
Total assets and regulatory balances	**5,226.2**	4,954.4
LIABILITIES AND EQUITY		
Current		
Working capital facility *[note 10]*	**11.7**	7.1
Commercial paper *[note 10]*	**159.0**	261.0
Accounts payable and accrued liabilities *[note 11]*	**516.3**	504.4
Income tax payable	**12.8**	8.1
Customer deposits	**49.2**	39.1
Deferred revenue *[note 12]*	**10.7**	5.1
Deferred conservation credit *[note 3[c]]*	**9.3**	5.5
Debentures *[note 13]*	**-**	249.8
Other liabilities *[note 24]*	**1.5**	3.1
Total current liabilities	**770.5**	1,083.2
Debentures *[note 13]*	**2,034.0**	1,834.8
Customer deposits	**8.9**	15.0
Deferred revenue *[note 12]*	**179.2**	140.3
Post-employment benefits *[note 14]*	**313.0**	280.5
Other liabilities *[note 24]*	**0.2**	2.3
Total liabilities	**3,305.8**	3,356.1
Commitments, contingencies and subsequent events *[notes 2, 24 and 25]*		
Equity		
Share capital *[note 17]*	**817.8**	567.8
Retained earnings	**942.6**	861.1
Total equity	**1,760.4**	1,428.9
Total liabilities and equity	**5,066.2**	4,785.0
Regulatory balances *[note 9]*	**160.0**	169.4
Total liabilities, equity and regulatory balances	**5,226.2**	4,954.4

ON BEHALF OF THE BOARD:

"David McFadden"
David McFadden, Director

"Michael Nobrega"
Michael Nobrega, Director

See accompanying notes to the consolidated financial statements.

TORONTO HYDRO Corporation

CONSOLIDATED STATEMENTS OF INCOME

[in millions of Canadian dollars]

Year ended December 31	**2017** **$**	**2016** **$**
Revenues		
Energy sales	**3,017.8**	3,306.2
Distribution revenue	**724.2**	647.9
Other *[note 18]*	**107.7**	75.9
	3,849.7	4,030.0
Expenses		
Energy purchases	**3,063.5**	3,216.9
Operating expenses *[note 19]*	**293.0**	277.1
Depreciation and amortization *[notes 6 and 7]*	**224.2**	212.2
	3,580.7	3,706.2
Finance costs *[note 20]*	**(77.7)**	(74.2)
Gain on disposals of property, plant and equipment	**9.8**	2.1
Income before income taxes	**201.1**	251.7
Income tax expense *[note 21]*	**(44.7)**	(67.1)
Net income	**156.4**	184.6
Net movements in regulatory balances *[note 9]*	**(13.1)**	(77.2)
Net movements in regulatory balances arising from deferred tax assets *[note 9]*	**13.2**	44.0
Net income after net movements in regulatory balances	**156.5**	151.4

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

[in millions of Canadian dollars]

Year ended December 31	**2017** **$**	**2016** **$**
Net income after net movements in regulatory balances	**156.5**	151.4
Other comprehensive income		
Items that will not be reclassified to income or loss		
Remeasurements of post-employment benefits, net of tax (2017 - $6.7, 2016 - $5.5) *[note 14]*	(18.4)	15.5
Net movements in regulatory balances related to OCI, net of tax (2017 - $6.7, 2016 - $5.5) *[note 14]*	18.4	(15.5)
Other comprehensive income, net of tax	**-**	-
Total comprehensive income	**156.5**	151.4

See accompanying notes to the consolidated financial statements.

TORONTO HYDRO Corporation

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

[in millions of Canadian dollars]

Year ended December 31	**2017** **$**	**2016** **$**
Share capital *[note 17]*	**817.8**	567.8
Retained earnings, beginning of year	**861.1**	773.1
Net income after net movements in regulatory balances	**156.5**	151.4
Dividends *[notes 17 and 23]*	**(75.0)**	(63.4)
Retained earnings, end of year	**942.6**	861.1
Total equity	**1,760.4**	1,428.9

See accompanying notes to the consolidated financial statements.

TORONTO HYDRO Corporation

CONSOLIDATED STATEMENTS OF CASH FLOWS

[in millions of Canadian dollars]

Year ended December 31	**2017** **$**	**2016** $
OPERATING ACTIVITIES		
Net income after net movements in regulatory balances	**156.5**	151.4
Net movements in regulatory balances *[note 9]*	**13.1**	77.2
Net movements in regulatory balances arising from deferred tax assets *[note 9]*	**(13.2)**	(44.0)
Adjustments		
Depreciation and amortization *[notes 6 and 7]*	**224.2**	212.2
Amortization of deferred revenue *[note 12]*	**(4.7)**	(3.8)
Finance costs	**77.7**	74.2
Income tax expense	**44.7**	67.1
Post-employment benefits	**7.4**	5.0
Gain on disposals of property, plant and equipment	**(9.8)**	(2.1)
Other	**1.0**	0.7
Capital contributions received *[note 12]*	**50.8**	44.7
Net change in other non-current assets and liabilities	**(6.9)**	(1.8)
Increase in customers deposits	**4.0**	6.7
Changes in non-cash working capital balances *[note 22]*	**62.0**	(15.3)
Income tax paid	**(22.1)**	(0.9)
Net cash provided by operating activities	**584.7**	571.3
INVESTING ACTIVITIES		
Purchase of property, plant and equipment *[note 22]*	**(440.0)**	(511.7)
Purchase of intangible assets *[note 22]*	**(93.4)**	(39.9)
Proceeds on disposals of property, plant and equipment	**12.5**	2.2
Net cash used in investing activities	**(520.9)**	(549.4)
FINANCING ACTIVITIES		
Decrease in commercial paper, net of issuances *[note 10]*	**(102.0)**	(63.0)
Common shares issued *[note 17]*	**250.0**	-
Dividends paid *[note 17]*	**(75.0)**	(63.4)
Proceeds from issuance of debentures *[note 13]*	**199.9**	200.0
Debt issuance costs paid *[note 13]*	**(1.4)**	(1.3)
Repayment of debentures *[note 13]*	**(250.0)**	-
Repayment of finance lease liability	**(3.0)**	(3.1)
Interest paid	**(86.9)**	(84.0)
Net cash used in financing activities	**(68.4)**	(14.8)
Net decrease (increase) in working capital facility during the year	**(4.6)**	7.1
Working capital facility, beginning of year	**(7.1)**	(14.2)
Working capital facility, end of year	**(11.7)**	(7.1)

See accompanying notes to the consolidated financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the years ended December 31, 2017 and 2016
[All tabular amounts in millions of Canadian dollars]

1. NATURE OF BUSINESS

The Corporation was incorporated on June 23, 1999 under the *Business Corporations Act* (Ontario) in accordance with the Electricity Act. The Corporation is wholly owned by the City and is domiciled in Canada, with its registered office located at 14 Carlton Street, Toronto, Ontario, M5B 1K5. The Corporation and its subsidiaries distribute electricity to customers and provide street lighting and expressway lighting services in the City.

2. BASIS OF PRESENTATION

The Corporation's audited consolidated financial statements for the years ended December 31, 2017 and 2016 ["Consolidated Financial Statements"] have been prepared in accordance with IFRS with respect to the preparation of annual financial information.

These Consolidated Financial Statements are presented in Canadian dollars, the Corporation's functional currency, and have been prepared on the historical cost basis, except for post-employment benefits which are recorded at actuarial value.

The Corporation has evaluated the events and transactions occurring after the consolidated balance sheet date through March 7, 2018 when the Corporation's Consolidated Financial Statements were authorized for issue by the Corporation's Board of Directors, and identified the events and transactions which required recognition in the Consolidated Financial Statements and/or disclosure in these notes to the Consolidated Financial Statements *[notes 8 and 17]*.

The summary of significant accounting policies has been disclosed in note 26.

3. REGULATION

The OEB has regulatory oversight of electricity matters in Ontario. The OEB's authority and responsibilities include the power to approve and fix rates for the transmission and distribution of electricity, the power to approve the amounts paid to non-contracted generators, the responsibility to provide rate protection for rural or remote electricity customers, and the responsibility for ensuring that electricity distribution companies fulfill their obligations to connect and service customers.

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

- *Commodity Charge* – The commodity charge represents the market price of electricity consumed by customers and is passed through the IESO back to operators of generating stations. It includes the global adjustment, which represents the difference between the market price of electricity and the rates paid to regulated and contracted generators.

- *Retail Transmission Rate* – The retail transmission rate represents the costs incurred in respect of the transmission of electricity from generating stations to local distribution networks. Retail transmission rates are passed through back to operators of transmission facilities.

- *WMS Charge* – The WMS charge represents various wholesale market support costs, such as the cost of the IESO to administer the wholesale electricity system, operate the electricity market, and maintain reliable operation of the provincial grid. Wholesale charges are passed through back to the IESO.

- *Distribution Rate* – The distribution rate is designed to recover the costs incurred by LDC in delivering electricity to customers, including the OEB-allowed cost of capital. Distribution rates are regulated by the OEB and include fixed and variable (usage-based) components, based on a forecast of LDC's customers and load.

a) Electricity Distribution Rates

The OEB's regulatory framework for electricity distributors is designed to support the cost-effective planning and operation of the electricity distribution network and to provide an appropriate alignment between a sustainable, financially viable electricity sector and the expectations of customers for reliable service at a reasonable price.

The OEB typically regulates the electricity rates for distributors using a combination of detailed cost of service reviews and IRM adjustments. Under the OEB's rate-setting methods, actual operating conditions may vary from forecasts such that actual returns achieved can differ from approved returns. Approved electricity rates are generally not adjusted as a result of actual costs or revenues being different from forecasted amounts, other than for certain prescribed costs that are eligible for deferral for future collection from, or refund to, customers.

On March 1, 2016 pursuant to LDC's 2015 – 2019 CIR application, the OEB set 2018 distribution rates on an interim basis. On August 23, 2017, LDC 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 LDC's 2018 rates, with an effective date of January 1, 2018, and the disposition of certain deferral and variance accounts.

b) Ontario's Fair Hydro Plan

On March 2, 2017, the Government of Ontario announced the OFHP, which includes a number of initiatives, some of which affect LDC or its customers.

OFHP includes the OREC, which came into effect on January 1, 2017. The OREC provides eligible customers with financial assistance in the form of an 8% rebate of the pre-tax cost of their electricity. The OREC rebates are administered by LDC and paid by the IESO in the month following customer billing. Current accounts receivable and unbilled revenue include the amount owing by the IESO to LDC. No effect on revenue or expense is recognized by LDC in respect of the OREC rebates.

OFHP also includes the OFHA, which enacted the Ontario Fair Hydro Plan Act, 2017 and amended the Electricity Act, 1998 and the Ontario Energy Board Act, 1998. The OFHA came into effect on June 1, 2017 and its impact is reflected in the Consolidated Financial Statements. The OFHA provides eligible customers with financial assistance through various changes to commodity pricing, new or amended programs, and eliminating or reducing certain provincial charges on the electricity bill. The OFHA reduces the total electricity bill for eligible customers and, accordingly, reduces current accounts receivable, unbilled revenue, accounts payable and accrued liabilities for LDC. No effect on distribution revenue or expense is recognized by LDC in respect of the OFHA.

c) CDM Activities

On March 26, 2014, the Minister of Energy of Ontario, under the guidance of sections 27.1 and 27.2 of the OEB Act, directed the OEB to amend the licence of each licensed electricity distributor to require the electricity distributor, as a condition of its licence, to make CDM programs available to its customers and to do so in relation to each customer segment in its service area, over the period beginning January 1, 2015 through December 31, 2020. On March 31, 2014, the Minister of Energy of Ontario issued a direction to require the OPA to coordinate, support and fund the delivery of CDM programs through electricity distributors. The objective of the CDM efforts is to reduce electricity consumption in the Province of Ontario by a total of 7 terawatt hours between January 1, 2015 and December 31, 2020, of which LDC's share is approximately 1,576 GWh of energy savings.

On November 13, 2014, LDC entered into an energy conservation agreement with the OPA for the delivery of CDM programs over the 2015-2020 period. The IESO and the OPA were merged under the name IESO starting on January 1, 2015.

Under the energy conservation agreement with the IESO, LDC has a joint CDM plan with Oakville Hydro Electricity Distribution Inc. [“Oakville Hydro”] for the delivery of CDM programs over the 2015-2020 period. LDC can choose between full cost recovery funding, pay-for-performance funding, or a combination of both, on a CDM program by program basis. Under the full cost recovery funding method, the IESO reimburses LDC for all adequately documented incurred costs, with an option to receive a portion of its funding in advance. Cost efficiency incentives may be awarded if LDC’s electricity savings meet or exceed certain CDM plan targets for programs under the full cost recovery funding method, with a mid-term review to be performed by the IESO for the 2015-2017 period. Under the pay-for-performance funding method, LDC receives payment in arrears based on verified electricity savings achieved with various options for frequency of payment. The programs under the joint CDM plan with Oakville Hydro are only being offered under the full cost recovery funding method.

The joint CDM plan provides combined funding of approximately $425.0 million, including participant incentives and program administration costs to achieve an aggregate energy savings target of approximately 1,668 GWh. Oakville Hydro’s programs under the joint CDM plan started on January 1, 2016. LDC received $44.9 million as at December 31, 2016 and $57.4 million in the year ended December 31, 2017 from the IESO for the delivery of CDM programs. Amounts received but not yet spent are presented on the consolidated balance sheets under current liabilities as deferred conservation credit. As at December 31, 2017, LDC estimated that approximately $12.9 million qualified as a joint mid-term incentive, of which $12.2 million represents LDC’s portion and is included within accounts receivable.

Effective October 16, 2017, LDC entered into an agreement to transfer $4.0 million of funding and a corresponding 20 GWh of its energy savings target to another local distribution company. This agreement will decrease the joint CDM plan funding with Oakville Hydro to $421.0 million, with a revised energy savings target of 1,648 GWh. The revised CDM plan was approved by the IESO on December 14, 2017.

4. ACCOUNTS RECEIVABLE

Accounts receivable consists of the following:

	2017 $	2016 $
Trade receivables	**189.9**	215.4
Due from related parties *[note 23]*	**13.8**	12.7
CDM mid-term incentive *[note 3[c]]*	**12.2**	—
Other	**1.8**	1.7
	217.7	229.8

5. OTHER ASSETS

Other assets consist of the following:

	2017 $	2016 $
Prepaid expenses	**11.3**	12.3
Deferred financing costs	**1.6**	1.6
Other	**2.8**	0.9
Total other assets	**15.7**	14.8
Less: Current portion of other assets relating to:		
Prepaid expenses	**11.3**	12.3
Deferred financing costs	**0.4**	0.4
Other	**1.0**	0.8
Current portion of other assets	**12.7**	13.5
Non-current portion of other assets	**3.0**	1.3

6. PROPERTY, PLANT AND EQUIPMENT

PP&E consist of the following:

	Distribution assets $	Land and buildings $	Equipment and other $	Construction in progress $	Total $
Cost					
Balance as at January 1, 2016	3,027.2	203.1	175.7	498.7	3,904.7
Additions/(Transfers)	381.2	111.3	67.0	(47.7)	511.8
Disposals and retirements	(32.1)	(0.1)	(0.3)	—	(32.5)
Balance as at December 31, 2016	3,376.3	314.3	242.4	451.0	4,384.0
Additions/(Transfers)	**404.4**	**84.8**	**38.4**	**(76.1)**	**451.5**
Assets held for sale *[note 8]*	—	**(21.2)**	—	—	**(21.2)**
Disposals and retirements	**(31.5)**	**(3.2)**	**(0.4)**	—	**(35.1)**
Balance as at December 31, 2017	**3,749.2**	**374.7**	**280.4**	**374.9**	**4,779.2**
Accumulated depreciation					
Balance as at January 1, 2016	222.6	15.7	77.7	—	316.0
Depreciation	129.3	10.3	25.9	—	165.5
Disposals and retirements	(4.6)	—	(0.1)	—	(4.7)
Balance as at December 31, 2016	347.3	26.0	103.5	—	476.8
Depreciation	**138.1**	**13.5**	**26.7**	—	**178.3**
Assets held for sale *[note 8]*	—	**(12.5)**	—	—	**(12.5)**
Disposals and retirements	**(5.9)**	**(0.5)**	**(0.4)**	—	**(6.8)**
Balance as at December 31, 2017	**479.5**	**26.5**	**129.8**	—	**635.8**
Carrying amount					
Balance as at December 31, 2016	3,029.0	288.3	138.9	451.0	3,907.2
Balance as at December 31, 2017	**3,269.7**	**348.2**	**150.6**	**374.9**	**4,143.4**

As at December 31, 2017, "Equipment and other" included assets under finance lease with cost of $18.2 million [December 31, 2016 - $18.2 million] and accumulated depreciation of $10.4 million [December 31, 2016 - $8.3 million]. For the year ended December 31, 2017, the Corporation recorded depreciation expense of $2.1 million [2016 - $2.3 million] related to assets under finance lease.

For the year ended December 31, 2017, borrowing costs in the amount of $6.2 million [2016 - $9.5 million] were capitalized to PP&E and credited to finance costs, with an average capitalization rate of 3.73% [2016 - 3.61%].

"Construction in progress" additions are net of transfers to the other PP&E categories.

7. INTANGIBLE ASSETS

Intangible assets consist of the following:

	Computer software $	Contributions $	Software in development $	Contributions for work in progress $	Total $
Cost					
Balance as at January 1, 2016	101.6	21.7	11.8	104.3	239.4
Additions/(Transfers)	11.9	53.8	8.4	(34.2)	39.9
Balance as at December 31, 2016	113.5	75.5	20.2	70.1	279.3
Additions/(Transfers)	**23.4**	**—**	**34.0**	**44.0**	**101.4**
Balance as at December 31, 2017	**136.9**	**75.5**	**54.2**	**114.1**	**380.7**
Accumulated amortization					
Balance as at January 1, 2016	38.1	2.0	—	—	40.1
Amortization	19.3	2.1	—	—	21.4
Balance as at December 31, 2016	57.4	4.1	—	—	61.5
Amortization	**20.0**	**3.0**	—	—	**23.0**
Balance as at December 31, 2017	**77.4**	**7.1**	—	—	**84.5**
Carrying amount					
Balance as at December 31, 2016	56.1	71.4	20.2	70.1	217.8
Balance as at December 31, 2017	**59.5**	**68.4**	**54.2**	**114.1**	**296.2**

For the year ended December 31, 2017, borrowing costs in the amount of $3.6 million [2016 - $3.0 million] were capitalized to intangible assets and credited to finance costs, with an average capitalization rate of 3.73% [2016 - 3.61%].

"Software in development" and "Contributions for work in progress" additions are net of transfers to the other intangible asset categories.

"Computer software" is externally acquired. The remaining amortization periods for computer software and contributions range from less than one year to 5 years, and from 11 to 25 years, respectively.

8. ASSETS HELD FOR SALE

In 2017, LDC commenced the process to sell a property including land and buildings to a third party. Accordingly, the carrying amount of the identified assets of $8.7 million was transferred from PP&E to assets held for sale as at December 31, 2017. Upon reclassification as assets held for sale, no further depreciation was recorded by LDC on the related assets. On January 16, 2018, LDC entered into an agreement to sell the property, which is expected to close on April 16, 2018. Upon completion of the sale, the net gain including the future tax savings will be deferred as a regulatory credit balance *[note 9[c]]*.

9. REGULATORY BALANCES

Debit balances consist of the following:

	January 1, 2017 $	Balances arising in the period $	Recovery/ reversal $	Other movements $	December 31, 2017 $	Remaining recovery/ reversal period (months)	Carrying charges applicable
OPEB actuarial net loss	**60.2**	**25.1**	**—**	**—**	**85.3**	note 9[a]	—
Foregone revenue	**64.3**	**—**	**(20.3)**	**—**	**44.0**	24	—
Gain on disposal	**8.6**	**(8.1)**	**18.6**	**—**	**19.1**	note 9[c]	*
LRAM	**10.5**	**11.0**	**(4.8)**	**—**	**16.7**	note 9[d]	*
IFRS transitional adjustments	**22.8**	**—**	**(7.8)**	**—**	**15.0**	24	—
Stranded meters	**11.4**	**—**	**(3.9)**	**—**	**7.5**	24	*
OPEB cash versus accrual	**2.9**	**1.3**	**—**	**—**	**4.2**	note 9[g]	—
Named properties	**4.6**	**—**	**(1.5)**	**—**	**3.1**	24	—
Capital contributions	**1.5**	**—**	**(0.5)**	**—**	**1.0**	24	—
Smart meters	**2.1**	**—**	**(3.1)**	**1.0**	**—**	—	—
Other	**1.9**	**2.1**	**—**	**—**	**4.0**	—	*
	190.8	**31.4**	**(23.3)**	**1.0**	**199.9**		

	January 1, 2016 $	Balances arising in the period $	Recovery/ reversal $	Other movements $	December 31, 2016 $	Remaining recovery/ reversal period (months)	Carrying charges applicable
OPEB actuarial net loss	81.2	(21.0)	—	—	60.2	note 9[a]	—
Foregone revenue	61.1	19.2	(16.0)	—	64.3	36	—
Gain on disposal	—	—	14.5	(5.9)	8.6	note 9[c]	*
LRAM	9.1	4.7	(3.3)	—	10.5	note 9[d]	*
IFRS transitional adjustments	28.9	—	(6.1)	—	22.8	36	—
Stranded meters	14.4	—	(3.0)	—	11.4	36	*
OPEB cash versus accrual	1.8	1.1	—	—	2.9	note 9[g]	—
Named properties	5.8	—	(1.2)	—	4.6	36	—
Capital contributions	1.9	—	(0.4)	—	1.5	36	—
Smart meters	10.0	—	(7.9)	—	2.1	4	—
Settlement variances	25.3	—	—	(25.3)	—	—	*
Other	2.2	1.6	—	(1.9)	1.9	—	*
	241.7	5.6	(23.4)	(33.1)	190.8		

* In accordance with the OEB's direction, carrying charges were accrued to certain regulatory balances at a rate of 1.10% for January 1, 2017 to September 30, 2017 and 1.50% for October 1, 2017 to December 31, 2017 [2016 - 1.10%].

Credit balances consist of the following:

	January 1, 2017 $	Balances arising in the period $	Recovery/ reversal $	Other movements $	December 31, 2017 $	Remaining recovery/ reversal period (months)	Carrying charges applicable
Deferred taxes	**65.3**	**(6.5)**	**—**	**—**	**58.8**	note 9[j]	—
Settlement variances	**62.8**	**(45.2)**	**23.4**	**—**	**41.0**	note 9[k]	*
Capital-related revenue requirement	**8.8**	**16.2**	**—**	**—**	**25.0**	note 9[l]	*
Derecognition	**12.8**	**3.1**	**—**	**—**	**15.9**	note 9[m]	*
Tax-related variances	**17.5**	**—**	**(8.2)**	**—**	**9.3**	12	*
Development charges	**—**	**5.3**	**—**	**—**	**5.3**	note 9[o]	*
Smart meters	**—**	**—**	**(0.7)**	**1.0**	**0.3**	—	—
Other	**2.2**	**2.7**	**(0.5)**	**—**	**4.4**	—	*
	169.4	**(24.4)**	**14.0**	**1.0**	**160.0**		

	January 1, 2016 $	Balances arising in the period $	Recovery/ reversal $	Other movements $	December 31, 2016 $	Remaining recovery/ reversal period (months)	Carrying charges applicable
Deferred taxes	114.8	(49.5)	—	—	65.3	note 9[j]	—
Settlement variances	—	89.3	1.2	(27.7)	62.8	note 9[k]	*
Capital-related revenue requirement	2.8	6.0	—	—	8.8	note 9[l]	*
Derecognition	9.9	2.9	—	—	12.8	note 9[m]	*
Tax-related variances	26.5	—	(8.5)	(0.5)	17.5	24	*
ICM	9.7	0.1	(9.8)	—	—	—	*
Gain on disposal	5.9	—	—	(5.9)	—	—	*
Other	2.0	1.2	(2.0)	1.0	2.2	—	*
	171.6	50.0	(19.1)	(33.1)	169.4		

* In accordance with the OEB's direction, carrying charges were accrued to certain regulatory balances at a rate of 1.10% for January 1, 2017 to September 30, 2017 and 1.50% for October 1, 2017 to December 31, 2017 [2016 - 1.10%].

The "Balances arising in the period" column consists of new additions to regulatory balances (for both debits and credits). The "Recovery/reversal" column consists of amounts disposed through OEB-approved rate riders or transactions reversing an existing regulatory balance. The "Other movements" column consists of impairment and reclassification between the regulatory debit and credit balances. In addition, the "Other movements" column includes reclassification of regulatory deferral accounts considered to be insignificant into the "Other" categories. During 2016, residual regulatory balances approved by the OEB for disposition over a 10-month period commencing on March 1, 2016 were reclassified from "Other" regulatory debit balance, settlement variances and tax-related variances into "Other" regulatory credit balance. There was no impairment recorded for the year ended December 31, 2017.

Reconciliation between the net movements in regulatory balances shown above and the net movements presented on the consolidated statements of income and the consolidated statements of comprehensive income is as follows:

	2017 $	2016 $
Total movements per regulatory debit balances table	**9.1**	(50.9)
Total movements per regulatory credit balances table	**9.4**	2.2
Total net movements	**18.5**	(48.7)
Net movements per financial statements:		
Net movements in regulatory balances	**(13.1)**	(77.2)
Net movements in regulatory balances arising from deferred tax assets	**13.2**	44.0
Net movements in regulatory balances related to OCI, net of tax	**18.4**	(15.5)
Total net movements per financial statements	**18.5**	(48.7)

Regulatory developments in Ontario's electricity industry and other governmental policy changes may affect the electricity distribution rates charged by LDC and the costs LDC is permitted to recover. There is a risk that the OEB may disallow the recovery of a portion of certain costs incurred in the current period through future rates or disagree with the proposed recovery period. In the event that the disposition of these balances is assessed to no longer be probable based on management's judgment, any impairment will be recorded in the period when the assessment is made.

The regulatory balances of the Corporation consist of the following:

a) OPEB Actuarial Net Loss

This regulatory balance accumulates the actuarial gains and losses arising from changes in actuarial assumptions and experience adjustments recognized in OCI. The balance arising during the year ended December 31, 2017 of $25.1 million is related to the actuarial loss recorded for the year [2016 - $21.0 million actuarial gain] *[note 14[a]]*. The net position is an actuarial loss that is recoverable in future rates. LDC has not sought recovery to date from the OEB as changes in underlying assumptions may reduce the balance in the account. LDC expects to recover this regulatory balance as per OEB direction, in a future rate application.

b) Foregone Revenue

This regulatory balance relates to the revenue that LDC would have recovered in 2015 and 2016 if new OEB-approved rates were implemented as of May 1, 2015 and January 1, 2016, respectively. In the CIR decision and rate order, the OEB approved foregone revenue rate riders over 46 months commencing on March 1, 2016 for May 1, 2015 to December 31, 2015 based on approved 2015 rates and for January 1, 2016 to February 29, 2016 based on approved 2016 rates.

c) Gain on Disposal

This regulatory balance consists of the net of amounts disposed through the OEB-approved rate riders offset by the related tax savings (debits), and the after-tax gain realized on two significant LDC properties (credits). As part of the CIR decision and rate order, LDC agreed to a rate rider that would pass the total forecasted net gains along with future tax savings on both properties back to ratepayers, effective from March 1, 2016 to December 31, 2018. During 2015, the gain on one of the properties was realized by LDC resulting in a net credit balance at December 31, 2015. As at December 31, 2016, the amount disposed through the rate riders exceeded the gain realized on the first property as the second property was still not sold, resulting in a net debit balance. Upon the sale of the second property, the account

would revert to a credit balance if actual net gains and tax savings exceed the total amount of the approved rate riders *[note 8]*. In the second quarter of 2017, LDC realized a gain in connection with the disposal of a third property. LDC expects to seek disposition for any residual balance in a future rate application.

d) Lost Revenue Adjustment Mechanism

This regulatory balance relates to the difference between the level of CDM program activities included in LDC's load forecast used to set approved rates and the actual impact of CDM activities achieved. New variances are accrued based on current CDM activities. Approved variances up to 2014 were disposed through OEB-approved rate riders over 12 months commencing on January 1, 2017 and approved variances for 2015 and 2016 will be disposed through OEB-approved rate riders over 12 months commencing on January 1, 2018. Variances pertaining to years subsequent to 2016 have yet to be applied for disposition.

e) IFRS Transitional Adjustments

This regulatory balance relates to the differences arising from accounting policy changes for PP&E and intangible assets due to the transition from US GAAP to IFRS in 2014, primarily related to derecognition of certain assets and additional capitalized borrowing costs. In the CIR decision and rate order, the OEB approved disposition of the balance over 46 months commencing on March 1, 2016.

f) Stranded Meters and Smart Meters

These regulatory balances relate to the provincial government's decision to install smart meters throughout Ontario.

The net book value of stranded meters related to the deployment of smart meters was reclassified from PP&E to a new regulatory balance as at December 31, 2013. In the CIR decision and rate order, the OEB approved LDC's request for recovery of the forecasted net book value of the stranded meters as at December 31, 2014 over 46 months commencing on March 1, 2016.

On January 16, 2014, the OEB approved LDC's request for incremental revenue and disposition of the smart meter regulatory balances to be recovered through rates over 36 months commencing on May 1, 2014. The OEB ruling on smart meters also permitted the recovery in principle of LDC's allowed cost of capital on smart meters since 2008, with a rate order issued to this effect. This allows LDC to recover the incremental revenue requirement associated with these assets for the period during which they remained outside of rate base.

g) OPEB Cash versus Accrual

This regulatory balance relates to the difference between LDC's forecasted OPEB costs determined on an accrual basis and the cash payments made under the OPEB plans. The OEB directed LDC to track the difference as a temporary arrangement, pending the OEB's conclusion on the sector-wide policy consultation it initiated on the regulatory treatment of pension and OPEB costs. On September 14, 2017, the OEB issued its final report on the consultation and established the use of the accrual accounting method as the default method on which to set rates for OPEB costs. LDC will continue to track the cash versus accrual difference until its next rate application when the disposition of this regulatory balance will be considered. The timing of disposition of the balance is currently unknown.

h) Named Properties

As part of 2010 rates, LDC had forecasted net gains on certain properties which were planned for sale between 2007 and 2011. This regulatory balance relates to the excess of those forecasted net gains over the actual net gains realized

upon the sale of the named properties. In the CIR decision and rate order, the OEB approved disposition of this variance over 46 months commencing on March 1, 2016.

i) Capital Contributions

This regulatory balance relates to the difference between amounts included in rates for HONI capital contributions and actual contributions made in 2010 and 2011. In the CIR decision and rate order, the OEB approved disposition of this variance over 46 months commencing on March 1, 2016.

j) Deferred Taxes

This regulatory credit balance relates to both deferred tax amounts reclassified under IFRS 14 *[note 26[b]]* and the expected future electricity distribution rate reduction for customers arising from timing differences in the recognition of deferred tax assets. LDC did not apply for disposition of the balance since it is reversed through timing differences in the recognition of deferred tax assets.

The amounts reclassified under IFRS 14 include the deferred tax liability related to regulatory balances of $34.9 million as at December 31, 2017 [December 31, 2016 - $36.4 million], offset by the recognition of a regulatory balance in respect of additional temporary differences for which a deferred tax amount was recognized of $8.5 million as at December 31, 2017 [December 31, 2016 - $10.4 million].

The deferred tax amount related to the expected future electricity distribution rate reduction for customers was $32.4 million as at December 31, 2017 [December 31, 2016 - $39.3 million].

k) Settlement Variances

This account includes the variances between amounts charged by LDC to customers, based on regulated rates, and the corresponding cost of electricity and non-competitive electricity service costs incurred by LDC. LDC has deferred the variances between the costs incurred and the related recoveries in accordance with the criteria set out in the accounting principles prescribed by the OEB. New variances are accrued based on current charges while approved variances up to 2016, including carrying charges forecasted to the end of 2017, will be disposed through OEB-approved rate riders over 12 months commencing on January 1, 2018. Settlement variances pertaining to years subsequent to 2016 have yet to be applied for disposition.

l) Capital-related Revenue Requirement

This regulatory balance relates to the asymmetrical variance between the cumulative 2015 to 2019 capital-related revenue requirement included in rates and the actual capital-related revenue requirement over the same period. If the cumulative 2015 to 2019 capital-related revenue requirement included in rates exceeds the actual capital-related revenue requirement over the same rate period, LDC must apply for disposition of this account in order to clear the balance to ratepayers through a rate rider. This account was approved by the OEB in the CIR decision and rate order. The timing of disposition of the balance is currently unknown.

m) Derecognition

This regulatory balance relates to the difference between the revenue requirement on derecognition of PP&E and intangible assets included in the OEB-approved rates and the actual amounts of derecognition. This account was approved by the OEB in the CIR decision and rate order. The timing of disposition of the balance is currently unknown.

n) Tax-related Variance Accounts

This regulatory credit balance arose from favourable income tax reassessments on certain prior year tax positions received, which differed from those assumed in previous applications for electricity distribution rates. In the CIR decision and rate order, the OEB approved disposition of the balance over 10-34 months commencing on March 1, 2016.

o) Development charges

This regulatory balance relates to excess expansion deposits retained by LDC where the requested number of connections or electricity demand were not met by the connecting customer. Pursuant to the OEB's Distribution System Code, LDC may collect expansion deposits on offers to connect from specific customers to guarantee the payment of additional costs relating to expansion projects. During the customer connection horizon, LDC has an obligation to annually return the expansion deposit to the connecting customer in proportion to the actual connections or electricity demand that occurred in that year. If the number of connections or electricity demand requested by the customer do not materialize by the end of the specified customer connection horizon, LDC retained the excess expansion deposit not otherwise returned to the connecting customer.

The excess expansion deposits were recorded as a regulatory balance on the Consolidated Balance Sheets, with a corresponding offset in net movements in regulatory balances. This regulatory balance is expected to offset future electricity distribution rates for customers, although application has yet to be made to dispose of the balance.

p) Incremental Capital Module

This regulatory balance related to the ICM application approved by the OEB and the associated rate riders, which became effective June 1, 2013. The balance of $9.8 million represented the net of amounts collected through the ICM rate riders from 2013 to 2014 and amounts recognized in profit or loss in relation to the eligible in-service capital expenditures. Further to the OEB's decision on July 28, 2016, the entire balance of $9.8 million was recorded as an increase in equity through net movements in regulatory balances in 2016.

10. SHORT-TERM BORROWINGS

The Corporation is a party to a credit agreement with a syndicate of Canadian chartered banks which established a revolving credit facility [“Revolving Credit Facility”], pursuant to which it may borrow up to $800.0 million, of which up to $210.0 million is available in the form of letters of credit. On August 1, 2017, the maturity date of the Revolving Credit Facility was extended by one year from October 10, 2021 to October 10, 2022. Borrowings under the Revolving Credit Facility bear interest at short-term floating rates plus a fixed spread, which varies in accordance with the Corporation's credit rating.

The Corporation has a commercial paper program allowing up to $600.0 million of unsecured short-term promissory notes [“Commercial Paper Program”] to be issued in various maturities of no more than one year. The Commercial Paper Program is supported by liquidity facilities available under the Revolving Credit Facility; hence, available borrowing under the Revolving Credit Facility is reduced by the amount of commercial paper outstanding at any point in time. Proceeds from the Commercial Paper Program are used for general corporate purposes. Borrowings under the Commercial Paper Program bear interest based on the prevailing market conditions at the time of issuance.

Additionally, the Corporation is a party to:

- a $75.0 million demand facility with a Canadian chartered bank for the purpose of issuing letters of credit mainly to support LDC's prudential requirements with the IESO ["Prudential Facility"]; and
- a $20.0 million demand facility with a second Canadian chartered bank for the purpose of working capital management ["Working Capital Facility"].

The available amount under the Revolving Credit Facility as well as outstanding borrowings under the Revolving Credit Facility and Commercial Paper Program are as follows:

	Revolving Credit Facility Limit $	Revolving Credit Facility Borrowings $	Commercial Paper Outstanding $	Revolving Credit Facility Availability $
December 31, 2017	800.0	—	159.0	641.0
December 31, 2016	800.0	—	261.0	539.0

For the year ended December 31, 2017, the average aggregate outstanding borrowings under the Corporation's Revolving Credit Facility, Working Capital Facility and Commercial Paper Program were $210.3 million [2016 - $348.7 million] with a weighted average interest rate of 0.93% [2016 - 0.89%].

As at December 31, 2017, $11.7 million had been drawn under the Working Capital Facility [December 31, 2016 - $7.1 million] and $38.4 million of letters of credit had been issued against the Prudential Facility [December 31, 2016 - $33.4 million].

11. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities consist of the following:

	2017 $	2016 $
Trade payables	**325.1**	328.6
Accrued liabilities	**133.2**	116.3
Due to related parties *[note 23]*	**40.1**	41.0
Accrued interest	**15.9**	16.6
Other	**2.0**	1.9
	516.3	504.4

12. DEFERRED REVENUE

Deferred revenue consists of capital contributions received from electricity customers to construct or acquire PP&E which have not yet been recognized into other revenue, and revenue not yet recognized from ancillary services *[note 26[j]]*.

	2017 $	2016 $
Capital contributions, beginning of year	**143.6**	103.0
Capital contributions received	**50.8**	44.7
Amortization	**(4.7)**	(3.8)
Other	**(1.5)**	(0.3)
Capital contributions, end of year	**188.2**	143.6
Other	**1.7**	1.8
Total deferred revenue	**189.9**	145.4
Less: Current portion of deferred revenue relating to:		
Capital contributions	**9.0**	3.3
Other	**1.7**	1.8
Current portion of deferred revenue	**10.7**	5.1
Non-current portion of deferred revenue	**179.2**	140.3

13. DEBENTURES

Debentures consist of the following:

	2017 $	2016 $
Senior unsecured debentures		
Series 2 – 5.15% due November 14, 2017	—	250.0
Series 3 – 4.49% due November 12, 2019	**250.0**	250.0
Series 6 – 5.54% due May 21, 2040	**200.0**	200.0
Series 7 – 3.54% due November 18, 2021	**300.0**	300.0
Series 8 – 2.91% due April 10, 2023	**250.0**	250.0
Series 9 – 3.96% due April 9, 2063	**245.0**	245.0
Series 10 – 4.08% due September 16, 2044	**200.0**	200.0
Series 11 – 3.55% due July 28, 2045	**200.0**	200.0
Series 12 – 2.52% due August 25, 2026	**200.0**	200.0
Series 13 – 3.485% due February 28, 2048	**200.0**	—
Total debentures	**2,045.0**	2,095.0
Less: Unamortized debt issuance costs	**10.2**	9.7
Unamortized discount/premium	**0.8**	0.7
Current portion of debentures	—	249.8
Long-term portion of debentures	**2,034.0**	1,834.8

All debentures of the Corporation rank equally.

The Corporation filed a base shelf prospectus dated May 8, 2017 with the securities commissions or similar regulatory authorities in each of the provinces of Canada. These filings allow the Corporation to make offerings of unsecured debt securities of up to $1.0 billion during the 25-month period following the date of the prospectus.

On June 14, 2016, the Corporation issued $200.0 million senior unsecured debentures at a rate of 2.52% [“Series 12”]. The Series 12 debentures due on August 25, 2026 were priced at $999.84 per $1,000 principal amount and bear interest payable semi-annually in arrears. The net proceeds were used to repay certain existing indebtedness and for general corporate purposes. Debt issuance costs of $1.3 million relating to the Series 12 debentures were recorded against the carrying amount of the debentures in the second quarter of 2016 and are amortized to finance costs using the effective interest method.

On November 14, 2017, the Corporation issued $200.0 million senior unsecured debentures at a rate of 3.485% [“Series 13”]. The Series 13 debentures due on February 28, 2048 were priced at $999.29 per $1,000 principal amount and bear interest payable semi-annually in arrears. The net proceeds were used to repay certain existing indebtedness and for general corporate purposes. Debt issuance costs of $1.4 million relating to the Series 13 debentures were recorded against the carrying amount of the debentures in the fourth quarter of 2017 and are amortized to finance costs using the effective interest method.

The Corporation’s Series 2 debentures matured and were repaid on November 14, 2017.

The Corporation may redeem all or part of its outstanding debentures at any time prior to maturity at a price equal to the greater of the Canada Yield Price (determined in accordance with the terms of the debentures) and par, plus accrued and unpaid interest up to and excluding the date fixed for redemption. Also, the Corporation may, at any time and from time to time, purchase debentures for cancellation, in the open market, by tender or by private contract, at any

price agreed upon with the holder of the debentures being purchased. The debentures contain certain covenants which, subject to certain exceptions, restrict the ability of the Corporation and LDC to create security interests, incur additional indebtedness or dispose of all or substantially all of their assets.

14. EMPLOYEE FUTURE BENEFITS

Pension

The Corporation's eligible employees participate in a defined benefit pension plan through OMERS. As at December 31, 2017, the OMERS plan was 94.0% funded [December 31, 2016 - 93.4%]. OMERS has a strategy to return the plan to a fully funded position. The Corporation is not able to assess the implications, if any, of this strategy or of the withdrawal of other participating entities from the OMERS plan on its future contributions. For the year ended December 31, 2017, the Corporation's contributions were $17.6 million [2016 - $17.6 million], representing less than five percent of total contributions to the OMERS plan. The Corporation expects to contribute approximately $19.0 million to the OMERS plan in 2018.

Post-employment benefits other than pension

a) Benefit obligation

	2017 $	2016 $
Balance, beginning of year	**280.5**	296.5
Current service cost	**4.1**	6.2
Interest cost	**11.2**	12.0
Benefits paid	**(11.0)**	(10.9)
Experience loss (gain) (1)	**1.9**	(4.2)
Actuarial gain arising from changes in demographic assumptions (1)	**—**	(17.5)
Actuarial loss (gain) arising from changes in financial assumptions (1)	**26.3**	(1.6)
Balance, end of year	**313.0**	280.5

(1) Actuarial loss (gain) on accumulated sick leave credits of $3.1 million [2016 - ($2.3) million] is recognized in benefit cost *[note 14[c]]* and actuarial loss (gain) on medical, dental and life insurance benefits of $25.1 million [2016 - ($21.0) million] is recognized in OCI *[note 14[d]]*.

The weighted average duration of the benefit obligation as at December 31, 2017 is 16.7 years [2016 - 16.7 years].

b) Amounts recognized in regulatory balances

As at December 31, 2017, the amount recognized in regulatory balances related to net actuarial loss was $85.3 million [December 31, 2016 - $60.2 million] *[note 9[a]]*.

c) *Benefit cost recognized*

	2017 $	2016 $
Current service cost	**4.1**	6.2
Interest cost	**11.2**	12.0
Actuarial loss (gain) on other employee benefits *[note 14[a]]*	**3.1**	(2.3)
Benefit cost	**18.4**	15.9
Capitalized to PP&E and intangible assets	**8.1**	6.4
Charged to operating expenses	**10.3**	9.5

d) *Amounts recognized in OCI*

	2017 $	2016 $
Actuarial loss (gain) *[note 14[a]]*	**25.1**	(21.0)
Income tax expense (recovery) in OCI *[note 21]*	**(6.7)**	5.5
Remeasurements of post-employment benefits, net of tax	**18.4**	(15.5)
Net movements in regulatory balances related to OCI, net of tax	**(18.4)**	15.5
OCI, net of tax	**—**	—

e) *Significant assumptions*

	2017	2016
Discount rate (%) used in the calculation of:		
Benefit obligation as at December 31	**3.50**	4.00
Assumed medical and dental cost trend rates (%) as at December 31:		
Rate of increase in dental costs assumed for next year	**4.00**	4.00
Rate of increase in medical costs assumed for next year		
For pre July 2000 retirements	**5.00**	5.00
For other retirements	**5.50**	5.50
Rate that medical cost trend rate gradually declines to		
For pre July 2000 retirements	**5.00**	5.00
For other retirements	**5.00**	5.00
Year that the medical cost trend rate reaches the ultimate trend rate		
For pre July 2000 retirements	**2015**	2015
For other retirements	**2018**	2018

f) Sensitivity analysis

Significant actuarial assumptions for benefit obligation measurement purposes are discount rate and assumed medical and dental cost trend rates. The sensitivity analysis below has been determined based on reasonably possible changes of the assumptions, in isolation of one another, occurring at the end of the reporting period. This analysis may not be representative of the actual change since it is unlikely that changes in the assumptions would occur in isolation of one another as some of the assumptions may be correlated.

Changes in key assumptions would have had the following effect on the benefit obligation:

	Change in assumption	2017 $	2016 $
Benefit obligation		**313.0**	280.5
Discount rate	1% -	**(46.8)**	(42.0)
	1% ¯	**60.2**	54.0
Medical and dental cost trend rate	1% -	**40.2**	36.1
	1% ¯	**(36.0)**	(32.3)

15. CAPITAL MANAGEMENT

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

- ensure ongoing access to funding to maintain, refurbish and expand the electricity distribution system of LDC;
- ensure sufficient liquidity is available (either through cash and cash equivalents, investments or committed credit facilities) to meet the needs of the business;
- ensure compliance with covenants related to its credit facilities and senior unsecured debentures; and
- minimize finance costs while taking into consideration current and future industry, market and economic risks and conditions.

The Corporation monitors forecasted cash flows, capital expenditures, debt repayment and key credit ratios similar to those used by key rating agencies. The Corporation manages capital by preparing short-term and long-term cash flow forecasts. In addition, the Corporation accesses capital debt markets as required to help fund some of the periodic net cash outflows and to maintain available liquidity. There have been no changes in the Corporation's approach to capital management during the year. As at December 31, 2017, the Corporation's definition of capital included equity, borrowings under its Working Capital Facility, Commercial Paper Program and Revolving Credit Facility, long-term debt and obligations under finance leases, including the current portion thereof, and had remained unchanged from the definition as at December 31, 2016. As at December 31, 2017, equity amounted to $1,760.4 million [December 31, 2016 - $1,428.9 million], and borrowings under its Working Capital Facility, Commercial Paper Program and Revolving Credit Facility, long-term debt and obligations under finance leases, including the current portion thereof, amounted to $2,206.2 million [December 31, 2016 - $2,357.8 million].

The Corporation is subject to debt agreements that contain various covenants. The Corporation's unsecured debentures limit consolidated funded indebtedness to a maximum of 75% of total consolidated capitalization as defined in the agreements. The Corporation's Revolving Credit Facility limits the debt to capitalization ratio to a maximum of 75%.

The Corporation's debt agreements also include restrictive covenants such as limitations on designated subsidiary indebtedness, and restrictions on mergers and dispositions of designated subsidiaries. As at December 31, 2017 and December 31, 2016, the Corporation was in compliance with all covenants included in its trust indenture, supplemental trust indentures and Revolving Credit Facility agreement.

16. FINANCIAL INSTRUMENTS

a) *Recognition and measurement*

As at December 31, 2017 and December 31, 2016, the fair values of accounts receivable, unbilled revenue, Working Capital Facility, commercial paper, and accounts payable and accrued liabilities approximated their carrying amounts due to the short maturity of these instruments *[note 26[k]]*. The fair value of customer deposits approximates their carrying amounts taking into account interest accrued on the outstanding balance. Obligations under finance leases are measured based on a discounted cash flow analysis and approximate the carrying amounts as management believes that the fixed interest rates are representative of current market rates.

The carrying amounts and fair values of the Corporation's debentures consist of the following:

	2017 $		2016 $	
	Carrying amount	**Fair value (1)**	**Carrying amount**	**Fair value (1)**
Senior unsecured debentures				
Series 2 – 5.15% due November 14, 2017	—	—	249.8	258.7
Series 3 – 4.49% due November 12, 2019	**249.6**	**260.6**	249.5	270.8
Series 6 – 5.54% due May 21, 2040	**198.7**	**264.2**	198.7	253.5
Series 7 – 3.54% due November 18, 2021	**299.1**	**313.9**	298.9	322.8
Series 8 – 2.91% due April 10, 2023	**249.2**	**255.5**	249.0	259.3
Series 9 – 3.96% due April 9, 2063	**243.3**	**266.4**	243.3	246.4
Series 10 – 4.08% due September 16, 2044	**198.4**	**221.0**	198.3	209.4
Series 11 – 3.55% due July 28, 2045	**198.3**	**202.9**	198.3	191.3
Series 12 – 2.52% due August 25, 2026	**198.9**	**196.2**	198.8	195.5
Series 13 – 3.485% due February 28, 2048	**198.5**	**200.7**	—	—
	2,034.0	**2,181.4**	2,084.6	2,207.7

(1) The fair value measurement of financial instruments for which the fair value has been disclosed is included in Level 2 of the fair value hierarchy *[note 26[k]]*.

b) *Financial risks*

The following is a discussion of financial risks and related mitigation strategies that have been identified by the Corporation for financial instruments. This is not an exhaustive list of all risks, nor will the mitigation strategies eliminate all risks listed.

Credit risk

The Corporation is exposed to credit risk as a result of the risk of counterparties defaulting on their obligations. The Corporation's exposure to credit risk primarily relates to accounts receivable and unbilled revenue. The Corporation monitors and limits its exposure to credit risk on a continuous basis.

The Corporation is subject to credit risk with respect to customer non-payment of electricity bills. LDC obtains security instruments from certain customers in accordance with direction provided by the OEB. As at December 31, 2017, LDC held security deposits in the amount of $58.2 million [December 31, 2016 - $54.1 million], of which $29.8 million [December 31, 2016 - $30.0 million] was related to security deposits on offers to connect to guarantee the payment of additional costs related to expansion projects. The Corporation's security instruments may not provide sufficient protection from counterparties defaulting on their obligations. As at December 31, 2017, there were no significant concentrations of credit risk with respect to any customer. The credit risk and mitigation strategies with respect to unbilled revenue are the same as those for accounts receivable. The credit risk related to cash, cash equivalents and investments is mitigated by the Corporation's treasury policies on assessing and monitoring the credit exposures of counterparties.

The Corporation did not have any single customer that generated more than 10% of total consolidated revenue for the years ended December 31, 2017 and December 31, 2016.

Credit risk associated with accounts receivable and unbilled revenue is as follows:

	2017 $	2016 $
Accounts receivable (net of allowance for doubtful accounts)		
Outstanding for not more than 30 days	**178.6**	197.9
Outstanding for more than 30 days and not more than 120 days	**33.8**	27.3
Outstanding for more than 120 days	**5.3**	4.6
Total accounts receivable	**217.7**	229.8
Unbilled revenue	**278.3**	320.5
Total accounts receivable and unbilled revenue	**496.0**	550.3

The Corporation has a broad base of customers. As at December 31, 2017 and December 31, 2016, the Corporation's accounts receivable and unbilled revenue which were not past due or impaired were assessed by management to have no significant collection risk and no additional allowance for doubtful accounts was required for these balances.

Reconciliation between the opening and closing allowance for doubtful accounts balances is as follows:

	2017 $	2016 $
Balance, beginning of year	**(9.8)**	(11.5)
Provision for doubtful accounts	**(6.2)**	(4.0)
Write-offs	**6.0**	6.0
Recoveries	**(0.2)**	(0.3)
Balance, end of year	**(10.2)**	(9.8)

Unbilled revenue represents amounts for which the Corporation has a contractual right to receive cash through future billings and are unbilled at period-end. Unbilled revenue is considered current and no allowance for doubtful accounts was provided as at December 31, 2017 and December 31, 2016.

Interest rate risk

The Corporation is exposed to fluctuations in interest rates for the valuation of its post-employment benefit obligations *[note 14[f]]*. The Corporation is also exposed to short-term interest rate risk on the net of cash and cash equivalents, short-term borrowings under its Revolving Credit Facility, Working Capital Facility and Commercial Paper Program *[note 10]* and customer deposits. The Corporation manages interest rate risk by monitoring its mix of fixed and floating rate instruments, and taking action as necessary to maintain an appropriate balance.

As at December 31, 2017, aside from the valuation of its post-employment benefit obligations, the Corporation was exposed to interest rate risk predominately from short-term borrowings under its Commercial Paper Program and customer deposits, while most of its remaining obligations were either non-interest bearing or bear fixed interest rates, and its financial assets were predominately short-term in nature and mostly non-interest bearing. The Corporation estimates that a 100 basis point increase (decrease) in short-term interest rates, with all other variables held constant, would result in an increase (decrease) of approximately $2.3 million to annual finance costs.

Liquidity risk

The Corporation is exposed to liquidity risk related to its ability to fund its obligations as they become due. The Corporation monitors and manages its liquidity risk to ensure access to sufficient funds to meet operational and financial requirements. The Corporation has access to credit facilities and debt capital markets and monitors cash balances daily. The Corporation's objective is to ensure that sufficient liquidity is on hand to meet obligations as they fall due while minimizing finance costs.

Liquidity risks associated with financial commitments are as follows:

2017						
	Due within 1 year $	**Due within 2 years $**	**Due within 3 years $**	**Due within 4 years $**	**Due within 5 years $**	**Due after 5 years $**
Working Capital Facility	**11.7**	—	—	—	—	—
Commercial paper [(1)]	**159.0**	—	—	—	—	—
Accounts payable and accrued liabilities [(2)]	**500.4**	—	—	—	—	—
Obligations under finance leases	**1.5**	—	—	—	—	—
Senior unsecured debentures						
Series 3 – 4.49% due November 12, 2019	—	**250.0**	—	—	—	—
Series 6 – 5.54% due May 21, 2040	—	—	—	—	—	**200.0**
Series 7 – 3.54% due November 18, 2021	—	—	—	**300.0**	—	—
Series 8 – 2.91% due April 10, 2023	—	—	—	—	—	**250.0**
Series 9 – 3.96% due April 9, 2063	—	—	—	—	—	**245.0**
Series 10 – 4.08% due September 16, 2044	—	—	—	—	—	**200.0**
Series 11 – 3.55% due July 28, 2045	—	—	—	—	—	**200.0**
Series 12 – 2.52% due August 25, 2026	—	—	—	—	—	**200.0**
Series 13 – 3.485% due February 28, 2048	—	—	—	—	—	**200.0**
Interest payments on debentures	**75.7**	**77.1**	**66.0**	**66.0**	**55.3**	**1,131.2**
	748.3	**327.1**	**66.0**	**366.0**	**55.3**	**2,626.2**

[(1)] The notes under the Commercial Paper Program were issued at a discount and are repaid at their principal amount.
[(2)] Accounts payable and accrued liabilities exclude $15.9 million of accrued interest on debentures included within "Interest payments on debentures".

Foreign exchange risk

As at December 31, 2017, the Corporation had limited exposure to the changing values of foreign currencies. While the Corporation purchases goods and services which are payable in US dollars, and purchases US currency to meet the related commitments when required, the impact of these transactions is not material to the Consolidated Financial Statements.

17. SHARE CAPITAL

Share capital consists of the following:

	Number of Shares	$
Authorized		
The authorized share capital of the Corporation consists of an unlimited number of common shares without par value. All shares issued were fully paid.		
Issued and outstanding		
Common shares, beginning of the year	1,000	567.8
Common shares issued [(1)]	200	250.0
Common shares issued and outstanding, end of the year	**1,200**	**817.8**

[(1)] On June 28, 2017, the Corporation issued 200 common shares to the City for total proceeds of $250.0 million, net of share issue costs and expenses.

Dividends

The Shareholder Direction adopted by the City with respect to the Corporation provides that the Board of Directors of the Corporation will use its best efforts to ensure that the Corporation meets certain financial performance standards, including those relating to credit rating and dividends.

On March 2, 2017, the Board of Directors of the Corporation declared dividends in the amount of $6.25 million with respect to the first quarter of 2017 [March 31, 2016 – $44.6 million], which was paid to the City on March 31, 2017.

On May 11, 2017, the Board of Directors of the Corporation declared dividends in the amount of $6.25 million with respect to the second quarter of 2017 [June 30, 2016 – $6.25 million], which was paid to the City on June 30, 2017. In connection with receipt of the equity investment from the City, the Board of Directors of the Corporation declared dividends payable to the City and approved amendments to the Corporation's Dividend Policy, as follows:

[i] In respect of fiscal 2017, an aggregate amount of $75.0 million shall be paid to the City, consisting of the two previously declared and paid instalments of $6.25 million each and a further $62.5 million. The $62.5 million was paid to the City on July 7, 2017.

[ii] In respect of fiscal 2018 and subsequent fiscal years, 60% of the Corporation's consolidated net income after net movements in regulatory balances for the prior fiscal year shall be declared separately in four equal quarterly instalments, with each instalment payable to the City on the last business day of each fiscal quarter.

On March 7, 2018, the Board of Directors of the Corporation declared a quarterly dividend in the amount of $23.5 million, payable to the City by March 31, 2018.

18. OTHER REVENUE

Other revenue consists of the following:

	2017 $	2016 $
Ancillary services	**22.3**	16.4
Street lighting service fee	**18.9**	16.6
Pole and duct rentals	**15.8**	12.0
Other regulatory service charges	**13.3**	16.7
CDM mid-term incentive *[note 3[c]]*	**12.2**	—
Development charges *[note 9[o]]*	**5.1**	—
Amortization of deferred revenue *[note 12]*	**4.7**	3.8
Miscellaneous	**15.4**	10.4
	107.7	75.9

19. OPERATING EXPENSES

Operating expenses consist of the following:

	2017 $	2016 $
Salaries and benefits	**226.5**	223.6
External services	**138.6**	112.9
Other support costs [(1)]	**22.3**	32.7
Materials and supplies	**21.6**	16.7
Less: Capitalized costs	**(116.0)**	(108.8)
	293.0	277.1

[(1)] Includes taxes other than income taxes, utilities, rental, communication, insurance, and other general and administrative expenses.

For the year ended December 31, 2017, the Corporation recognized operating expenses of $13.0 million related to materials and supplies used to service electricity distribution assets [2016 - $7.6 million].

TORONTO HYDRO Corporation

20. FINANCE COSTS

Finance costs consist of the following:

	2017 $	2016 $
Interest income	**(0.2)**	(0.2)
Interest expense		
Interest on long-term debt [1]	**83.2**	81.6
Interest on short-term debt	**3.7**	4.9
Other interest	**0.8**	0.5
Capitalized borrowing costs	**(9.8)**	(12.6)
	77.7	74.2

[1] Includes amortization of debt issuance costs, discounts and premiums.

21. INCOME TAXES

Income tax expense differs from the amount that would have been recorded using the combined statutory Canadian federal and provincial income tax rate. Reconciliation of income tax expense computed at the statutory income tax rate to the income tax provision is set out below:

	2017 $	2016 $
Rate reconciliation before net movements in regulatory balances		
Income before income taxes	**201.1**	251.7
Statutory Canadian federal and provincial income tax rate	**26.5%**	26.5%
Expected income tax expense	**53.3**	66.7
Non-taxable amounts	**(8.7)**	0.4
Other	**0.1**	—
Income tax expense	**44.7**	67.1
Effective tax rate	**22.2%**	26.7%
Rate reconciliation after net movements in regulatory balances		
Net income after net movements in regulatory balances, before income tax [1]	**188.0**	174.5
Statutory Canadian federal and provincial income tax rate	**26.5%**	26.5%
Expected income tax expense	**49.8**	46.2
Temporary differences recoverable in future rates	**(15.5)**	(22.7)
Other	**(2.8)**	(0.4)
Income tax expense and income tax recorded in net movements in regulatory balances	**31.5**	23.1
Effective tax rate	**16.8%**	13.2%

[1] Income tax includes income tax expense and income tax recorded in net movements in regulatory balances.

Income tax expense as presented in the consolidated statements of income and OCI are as follows:

	2017 $	2016 $
Income tax expense	**44.7**	67.1
Income tax recorded in net movements in regulatory balances	**(13.2)**	(44.0)
Income tax expense and income tax recorded in net movements in regulatory balances	**31.5**	23.1
Income tax expense (recovery) in OCI *[note 14[d]]*	**(6.7)**	5.5
Income tax expense (recovery) in OCI recorded in net movements in regulatory balances	**6.7**	(5.5)
Income tax expense in OCI	**—**	—

Components of income tax expense and income tax recorded in net movements in regulatory balances are as follows:

	2017 $	2016 $
Current tax expense		
Current year	**32.5**	24.3
Adjustment for tax positions taken in prior periods	**(1.1)**	(2.2)
	31.4	22.1
Deferred tax expense		
Origination and reversal of temporary differences	**0.1**	1.0
Income tax expense and income tax recorded in net movements in regulatory balances	**31.5**	23.1

Deferred tax assets consist of the following:

	Net balance, January 1 2017 $	Recognized in net income $	Recognized in OCI $	Net balance, December 31 2017 $
PP&E and intangible assets	**11.7**	**(26.6)**	**—**	**(14.9)**
Post-employment benefits	**74.3**	**1.9**	**6.7**	**82.9**
Other taxable temporary differences	**(22.2)**	**11.2**	**—**	**(11.0)**
	63.8	**(13.5)**	**6.7**	**57.0**

	Net balance, January 1 2016 $	Recognized in net income $	Recognized in OCI $	Net balance, December 31 2016 $
PP&E and intangible assets	34.5	(22.8)	—	11.7
Post-employment benefits	78.6	1.2	(5.5)	74.3
Other taxable temporary differences	1.2	(23.4)	—	(22.2)
	114.3	(45.0)	(5.5)	63.8

As at December 31, 2017, the Corporation had accumulated net capital losses of $18.7 million [December 31, 2016 - $18.7 million], which are available to offset capital gains in future years. As at December 31, 2017, the Corporation had $1.7 million accumulated non-capital losses for income tax purposes [December 31, 2016 - $2.6 million], which are available to offset net income in future years before expiring [$1.4 million expires in 2035 and $0.3 million expires in 2036].

Deferred tax assets have not been recognized in respect of the following items because it is not probable that future taxable income will be available against which the Corporation can utilize the benefits therefrom.

	2017 $	2016 $
Deductible temporary differences	**7.4**	7.7
Net capital losses	**5.0**	5.0
Non-capital losses	**0.4**	0.7
	12.8	13.4

22. CONSOLIDATED STATEMENTS OF CASH FLOWS

Changes in non-cash working capital provided/(used) cash as follows:

	2017 $	2016 $
Accounts receivable	**12.1**	(38.1)
Unbilled revenue	**42.2**	(0.1)
Income tax receivable	**—**	9.9
Materials and supplies	**0.4**	0.1
Other current assets	**0.8**	(3.6)
Accounts payable and accrued liabilities	**(6.0)**	20.6
Income tax payable	**4.7**	8.1
Deferred revenue	**5.6**	0.3
Deferred conservation credit	**3.8**	(12.4)
Other current liabilities	**(1.6)**	(0.1)
	62.0	(15.3)

Reconciliation between the amount presented on the consolidated statements of cash flows and total additions to PP&E and intangible assets is as follows:

	2017 $	2016 $
Purchase of PP&E, cash basis	**440.0**	511.7
Net change in accruals related to PP&E	**9.9**	(1.7)
Other	**1.6**	1.8
Total additions to PP&E	**451.5**	511.8
Purchase of intangible assets, cash basis	**93.4**	39.9
Net change in accruals related to intangible assets	**8.0**	—
Total additions to intangible assets	**101.4**	39.9

Summary of changes in liabilities arising from financing activities:

	2016 $	Cash flows [1] $	Non-cash changes $ Foreign exchange	 Other	2017 $
Year ended December 31					
Commercial paper	**261.0**	**(102.0)**	—	—	**159.0**
Dividends payable	—	**(75.0)**	—	**75.0**	—
Debentures *[note 13]*	**2,084.6**	**(51.5)**	—	**0.9**	**2,034.0**
Accrued interest [2]	**16.6**	**(86.9)**	—	**86.2**	**15.9**
Lease liability [3]	**4.6**	**(3.0)**	**(0.1)**	—	**1.5**
	2,366.8	**(318.4)**	**(0.1)**	**162.1**	**2,210.4**

	2015 $	Cash flows [1] $	Non-cash changes $ Foreign exchange	 Other	2016 $
Year ended December 31					
Commercial paper	324.0	(63.0)	—	—	261.0
Dividends payable	—	(63.4)	—	63.4	—
Debentures *[note 13]*	1,885.0	198.7	—	0.9	2,084.6
Accrued interest [2]	14.9	(84.0)	—	85.7	16.6
Lease liability [3]	8.0	(3.1)	(0.3)	—	4.6
	2,231.9	(14.8)	(0.3)	150.0	2,366.8

[1] Cash inflows and cash outflows arising from commercial paper borrowings and debentures are presented on a net basis
[2] Included within accounts payable and accrued liabilities *[note 16[b]]*
[3] Included within other liabilities

23. RELATED PARTY TRANSACTIONS

As the City is the sole shareholder of the Corporation, the Corporation and the City are considered related parties.

Summary of Transactions with Related Parties	2017 $	2016 $
Revenues	**283.3**	275.3
Operating expenses and capital expenditures	**22.2**	26.9
Dividends	**75.0**	63.4

Summary of Amounts Due to/from Related Parties	2017 $	2016 $
Accounts receivable	**13.8**	12.7
Unbilled revenue	**26.3**	23.2
Accounts payable and accrued liabilities	**40.1**	41.0
Customer deposits	**15.7**	14.1
Deferred revenue	**1.9**	3.5

Revenues represent amounts charged to the City primarily for electricity, street lighting and ancillary services. Operating expenses and capital expenditures represent amounts charged by the City for purchased road cut repairs, property taxes and other services. Dividends are paid to the City *[note 17]*.

Accounts receivable represents receivables from the City primarily for electricity, street lighting and ancillary services. Unbilled revenue represents receivables from the City mainly related to electricity provided and not yet billed. Accounts payable and accrued liabilities represent amounts payable to the City related to road cut repairs and other services. Customer deposits represent amounts received from the City for future expansion projects. Deferred revenue represents amounts received from the City primarily for the construction of electricity distribution assets.

Key management personnel include the Corporation's senior executive officers and members of the Board of Directors. The compensation costs associated with the key management personnel are as follows:

	2017 $	2016 $
Short-term employee benefits	**4.6**	4.1
Post-employment benefits	**1.1**	1.0
	5.7	5.1

24. COMMITMENTS

Operating leases and capital projects

As at December 31, 2017, the future minimum payments under property operating leases, capital projects and other commitments were as follows:

	Operating leases $	Capital projects [1] and other $
Less than one year	**0.3**	**17.5**
Between one and five years	**1.1**	**28.5**
Total amount of future minimum payments [2]	**1.4**	**46.0**

[1] Mainly commitments for construction services and estimated capital contributions.
[2] Refer to note 16 for financial commitments excluded from the table above.

Operating lease expense for the year ended December 31, 2017 was $0.8 million [2016 - $2.8 million].

Finance leases

As at December 31, 2017 and December 31, 2016, reconciliation between the future minimum lease payments and their present value was as follows:

	2017 $			2016 $		
	Future minimum lease payments	Interest	Present value of minimum lease payments	Future minimum lease payments	Interest	Present value of minimum lease payments
Less than one year	**1.5**	—	**1.5**	3.2	0.2	3.0
Between one and five years	—	—	—	1.6	—	1.6
More than five years	—	—	—	—	—	—
	1.5	—	**1.5**	4.8	0.2	4.6
Current portion included within Other liabilities			**1.5**			3.0
Non-current portion included within Other liabilities			—			1.6

25. CONTINGENCIES

Legal Proceedings

In the ordinary course of business, the Corporation is subject to various legal actions and claims from customers, suppliers, former employees and other parties. On an ongoing basis, the Corporation assesses the likelihood of any adverse judgments or outcomes as well as potential ranges of probable costs and losses. A determination of the provision required, if any, for these contingencies is made after an analysis of each individual issue. The provision may change in the future due to new developments in each matter or changes in approach, such as a change in settlement strategy. If damages were awarded under these actions, the Corporation and its subsidiaries would make a claim under any applicable liability insurance policies which the Corporation believes would cover any damages which may become payable by the Corporation and its subsidiaries in connection with these actions, subject to such claim not being disputed by the insurers.

26. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

a) Basis of consolidation

The Consolidated Financial Statements include the accounts of the Corporation and its wholly-owned subsidiaries. All intercompany balances and transactions have been eliminated.

b) Regulation

The following regulatory treatments have resulted in accounting treatments which differ from those prescribed by IFRS for enterprises operating in an unregulated environment and regulated entities that did not adopt IFRS 14 *Regulatory Deferral Accounts* [“IFRS 14”]:

Regulatory Balances

In January 2014, the IASB issued IFRS 14 as an interim standard giving entities conducting rate-regulated activities the option of continuing to recognize regulatory balances according to their previous GAAP. Regulatory balances provide useful information about the Corporation’s financial position, financial performance and cash flows. IFRS 14 is restricted to first-time adopters of IFRS and remains in force until either repealed or replaced by permanent guidance on rate-regulated accounting from the IASB.

The Corporation has determined that certain debit and credit balances arising from rate-regulated activities qualify for the application of regulatory accounting treatment in accordance with IFRS 14 and the accounting principles prescribed by the OEB in the “Accounting Procedures Handbook for Electricity Distributors”. Under rate-regulated accounting, the timing and recognition of certain expenses and revenues may differ from those otherwise expected under other IFRS in order to appropriately reflect the economic impact of regulatory decisions regarding the Corporation’s regulated revenues and expenditures. These amounts arising from timing differences are recorded as regulatory debit and credit balances on the Corporation’s consolidated balance sheets, and represent existing rights and obligations regarding cash flows expected to be recovered from or refunded to customers, based on decisions and approvals by the OEB. Regulatory balances can be recognized for rate-setting and financial reporting purposes only if the OEB directs the relevant regulatory treatment or if future OEB direction is determined by management to be probable. In the event that the disposition of these balances is assessed to no longer be probable based on management’s judgment, the balances are recorded in the Corporation’s consolidated statements of income in the period when the assessment is made. Regulatory balances, which do not meet the definition of an asset or liability under any other IFRS, are segregated on the consolidated balance sheets and are presented on the consolidated statements of income and the consolidated statements of comprehensive income as net movements in regulatory balances and net movements in regulatory balances related to OCI, net of tax. The netting of regulatory debit and

credit balances is not permitted. The measurement of regulatory balances is subject to certain estimates and assumptions, including assumptions made in the interpretation of the OEB's regulations and decisions.

c) Cash and cash equivalents

Cash and cash equivalents include cash in bank accounts and short-term investments with terms to maturity of 90 days or less from their date of acquisition. On the consolidated statements of cash flows, cash and cash equivalents (working capital facility) include bank overdrafts that are repayable on demand and form an integral part of the Corporation's cash management.

d) Accounts receivable and unbilled revenue

Accounts receivable is recorded at the invoiced amount and overdue amounts bear interest at OEB-approved rates. Unbilled revenue is recorded based on an estimated amount for electricity delivered and for other services provided and not yet billed. The estimate is primarily based on the customers' previous billings with adjustments mainly for assumptions related to seasonality and weighted average price. The carrying amount of accounts receivable and unbilled revenue is reduced through an allowance for doubtful accounts, if applicable, and the amount of the related impairment loss is recognized in the consolidated statements of income. The impairment loss is the difference between an asset's carrying amount and the estimated future cash flows. When the Corporation considers that there are no realistic prospects of recovery of the financial assets, the relevant amounts are written off. If the amount of impairment loss subsequently decreases due to an event occurring after the impairment was recognized, then the previously recognized impairment loss is reversed through net income.

Accounts receivable and unbilled revenue are assessed at each reporting date to determine whether there is objective evidence of impairment, which includes default or delinquency by a debtor, indications that a debtor or issuer will enter bankruptcy, and adverse changes in the payment status of borrowers or issuers. Accounts receivable and unbilled revenue that are not individually assessed for impairment are collectively assessed for impairment by grouping together receivables with similar risk characteristics, and the Corporation considers historical trends on the timing of recoveries and the amount of loss incurred, as well as current economic and credit conditions.

e) Materials and supplies

Materials and supplies consist primarily of small consumable materials mainly related to the maintenance of the electricity distribution infrastructure. The Corporation classifies all major construction related components of its electricity distribution infrastructure to PP&E. Materials and supplies are carried at the lower of cost and net realizable value, with cost determined on a weighted average cost basis net of a provision for obsolescence.

f) Property, plant and equipment

PP&E are measured at cost less accumulated depreciation and any accumulated impairment losses, if applicable. The cost of PP&E represents the original cost, consisting of direct materials and labour, contracted services, borrowing costs, and directly attributable overhead. Subsequent costs are capitalized only if it is probable that the future economic benefits associated with the expenditure will flow to the Corporation and the costs can be measured reliably. If significant parts of an item of PP&E have different useful lives, then they are accounted for as separate major components of PP&E. The carrying amount of an item of PP&E is derecognized on disposal of the asset or when no future economic benefits are expected to accrue to the Corporation from its continued use. Any gain or loss arising on derecognition is recorded in the consolidated statements of income in the period in which the asset is derecognized. The gain or loss on disposal of an item of PP&E is determined as the sale proceeds less the carrying amount of the asset and costs of removal and is recognized in the consolidated statements of income.

Depreciation begins when an asset becomes available for use. Depreciation is provided on a straight-line basis over the estimated useful lives at the following annual rates:

Distribution assets:	
Distribution lines	1.7% to 5.0%
Transformers	3.3% to 5.0%
Meters	2.5% to 6.7%
Stations	2.0% to 10.0%
Buildings	1.3% to 5.0%
Equipment and other:	
Street lighting assets	1.7% to 5.0%
Assets under finance lease	1.0% to 14.3%
Other capital assets	4.0% to 25.0%

Leased assets are depreciated over the shorter of the lease term and their useful lives unless it is reasonably certain that the Corporation will obtain ownership by the end of the lease term. Assets under finance lease included a 99-year land lease. Construction in progress relates to assets not currently available for use and therefore is not depreciated. The depreciation method and useful lives are reviewed at each financial year-end and adjusted if appropriate. There are no residual values for items of PP&E.

g) Intangible assets

Intangible assets are measured at cost less accumulated amortization and any accumulated impairment losses, if applicable.

Amortization begins when an asset becomes available for use. Amortization is provided on a straight-line basis over the estimated useful lives at the following annual rates:

Computer software	10.0% to 25.0%
Contributions	4.0%

Software in development and contributions for work in progress relate to assets not currently available for use and therefore are not amortized. Contributions represent payments made to HONI for dedicated infrastructure in order to receive connections to transmission facilities. The amortization method and useful lives are reviewed at each financial year-end and adjusted if appropriate.

h) Impairment of non-financial assets

The Corporation reviews the carrying amounts of its non-financial assets other than materials and supplies and deferred tax assets at each reporting date to determine whether there is any indication of impairment, in which case the assets' recoverable amounts are estimated. For impairment testing, assets are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent on the cash inflows of other assets or CGUs. The Corporation has determined that its CGUs are at the individual entity level due to interdependencies of each entity's group of assets to generate cash flows. An impairment loss is recognized if the carrying amount of an asset or CGU exceeds its recoverable amount. Impairment losses are recognized in the consolidated statements of income, and are allocated to reduce the carrying amounts of assets in the CGU on a pro rata basis. An impairment loss recognized in prior periods is reversed when an asset's recoverable amount has increased, but not exceeding the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognized for the asset in prior years.

i) Capitalized borrowing costs

Borrowing costs directly attributable to the acquisition, construction or development of qualifying assets that necessarily take a substantial period of time to get ready for their intended use are capitalized, until such time as the assets are substantially ready for their intended use. The interest rate for capitalization is the Corporation's weighted average cost of borrowing, and is applied to the carrying amount of the construction-in-progress assets or assets under development including borrowing costs previously capitalized, net of capital contributions received. Capitalization commences immediately as the expenditure on a qualifying asset is incurred. Borrowing costs are included in PP&E and intangible assets for financial reporting purposes, and charged to operations through depreciation and amortization expense over the useful lives of the related assets.

j) Revenue recognition

Revenues from energy sales and electricity distribution are recorded on the basis of cyclical billings and include an estimated amount for electricity delivered and not yet billed. These revenues are impacted by energy demand primarily driven by outside temperature, and customer class usage patterns and composition.

Energy sales arise from charges to customers for electricity consumed, based on regulated rates. Energy sales include amounts billed or billable to customers for commodity charges, retail transmission charges, and WMS charges at current rates. These charges are passed through to customers over time and are considered revenue by LDC due to the collection risk of the related balances. The Corporation applies judgment to determine whether revenues are recorded on a gross or net basis. The Corporation has primary responsibility for the delivery of electricity to the customer. During the same period, energy sales should be equal to the cost of energy purchased. However, a difference between energy sales and energy purchases arises when there is a timing difference between the amounts charged by LDC to customers, based on regulated rates, and the electricity and non-competitive electricity service costs billed monthly by the IESO to LDC. This difference is recorded as a settlement variance, representing future amounts to be recovered from or refunded to customers through future billing rates approved by the OEB. In accordance with IFRS 14, this settlement variance is presented within regulatory balances on the consolidated balance sheets and within net movements in regulatory balances on the consolidated statements of income.

Distribution revenue is recorded based on OEB-approved distribution rates to recover the costs incurred by LDC in delivering electricity to customers. Distribution revenue also includes revenue related to the collection of OEB-approved rate riders.

Other revenue, which includes revenue from services ancillary to the electricity distribution, delivery of street lighting services, and pole and duct rentals, is recognized as the services are rendered. When services are made up of different components which are not separately identifiable, the related other revenues are recognized on a straight-line basis over the term of the contract. Capital contributions received from electricity customers to construct or acquire PP&E for the purpose of connecting a customer to a network are recorded as deferred revenue and amortized into other revenue at an equivalent rate to that used for the depreciation of the related PP&E. Revenue from ancillary services not yet recognized is also included within deferred revenue.

Revenues and costs associated with CDM programs are presented using the net basis of accounting. Cost efficiency incentives related to the CDM programs, included as part of other revenue, are recognized when it is probable that future economic benefits will flow to the entity and the amount can be reasonably measured.

k) Financial instruments

All financial assets are classified as "Loans and Receivables" and all financial liabilities are classified as "Other Financial Liabilities". These financial instruments are recognized initially at fair value adjusted for any directly attributable transaction costs. Subsequently, they are measured at amortized cost using the effective interest method less any impairment for the financial assets. The fair value of a financial instrument is the amount of consideration that would be agreed upon in an arm's length transaction between willing parties.

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

- Cash, cash equivalents and short-term investments are classified as "Loans and Receivables" and are measured at fair value. The carrying amounts approximate fair value due to the short maturity of these instruments.

- Accounts receivable and unbilled revenue are classified as "Loans and Receivables" and are measured at amortized cost, which, upon initial recognition, is considered equivalent to fair value. Subsequent measurements are recorded at amortized cost using the effective interest rate method. The carrying amounts approximate fair value due to the short maturity of these instruments.

- Working capital facility, revolving credit facility and commercial paper are classified as "Other Financial Liabilities" and are initially measured at fair value. Subsequent measurements are recorded at amortized cost using the effective interest rate method. The carrying amounts approximate fair value due to the short maturity of these instruments. Transaction costs incurred in connection with the Corporation's revolving credit facility are capitalized within other assets on the consolidated balance sheets and are amortized on a straight-line basis over the term of the facility, and are included in finance costs.

- Accounts payable and accrued liabilities are classified as "Other Financial Liabilities" and are initially measured at fair value. Subsequent measurements are recorded at amortized cost using the effective interest rate method. The carrying amounts approximate fair value because of the short maturity of these instruments.

- Customer deposits are classified as "Other Financial Liabilities" and are initially measured at fair value. Subsequent measurements are recorded at cost plus accrued interest. The carrying amounts approximate fair value taking into account interest accrued on the outstanding balance.

- Obligations under finance leases are classified as "Other Financial Liabilities" and are initially measured at fair value, or the present value of the minimum lease payments if lower. Subsequent measurements are based on a discounted cash flow analysis and approximate the carrying amount as management believes that the fixed interest rates are representative of current market rates.

- Debentures are classified as "Other Financial Liabilities" and are initially measured at fair value. The carrying amounts of the debentures are carried at amortized cost, based on the fair value of the debentures at issuance, which was the fair value of the consideration received adjusted for transaction costs. The fair values of the debentures are based on the present value of contractual cash flows, discounted at the Corporation's current borrowing rate for similar debt instruments *[note 16[a]]*. Debt issuance costs incurred in connection with the Corporation's debenture offerings are capitalized as part of the carrying amount of the debentures and amortized over the term of the related debentures, using the effective interest method, and the amortization is included in finance costs.

l) Fair value measurements

The Corporation utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. A fair value hierarchy exists that prioritizes observable and unobservable inputs used to measure fair value. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Corporation's assumptions with respect to how market participants would price an asset or liability. The fair value hierarchy includes three levels of inputs that may be used to measure fair value:

- Level 1: Unadjusted quoted prices in active markets for identical assets or liabilities. An active market for the asset or liability is a market in which transactions for the asset or liability occur with sufficient frequency and volume to provide pricing information on an ongoing basis;
- Level 2: Other than quoted prices included within Level 1 that are observable for the assets or liabilities, either directly or indirectly; and
- Level 3: Unobservable inputs, supported by little or no market activity, used to measure the fair value of the assets or liabilities to the extent that observable inputs are not available.

m) Employee benefits

(i) Short-term employee benefits

Short-term employee benefit obligations that are due to be settled wholly within twelve months after the end of the annual reporting period in which the employees render the related service are measured on an undiscounted basis and are expensed as the related service is provided. A liability is recognized for the amount expected to be paid if the Corporation has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

(ii) Multi-employer pension plan

The Corporation's full-time employees participate in a pension plan through OMERS. The OMERS plan is a jointly sponsored, multi-employer defined benefit pension plan established in 1962 by the province of Ontario for employees of municipalities, local boards and school boards. Both participating employers and employees are required to make plan contributions equally based on participating employees' contributory earnings, and share equally in funding gains or losses. The plan assets and pension obligations are not segregated in separate accounts for each member entity. The OMERS plan is accounted for as a defined contribution plan and the contribution payable is recognized as an employee benefit expense in the consolidated statements of income in the period when the service is rendered by the employee, since it is not practicable to determine the Corporation's portion of pension obligations or of the fair value of plan assets.

(iii) Post-employment benefits other than pension

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

The cost of providing benefits under the benefit plans is actuarially determined using the projected unit credit method, which incorporates management's best estimate of future salary levels, retirement ages of employees, health care costs, and other actuarial factors. Changes in actuarial assumptions and experience adjustments give rise to actuarial gains and losses. Actuarial gains and losses on medical, dental and life insurance benefits are recognized in OCI as

they arise. Actuarial gains and losses related to rate-regulated activities are subsequently reclassified from OCI to a regulatory balance on the consolidated balance sheets. Actuarial gains and losses on accumulated sick leave credits are recognized in the consolidated statements of income in the period in which they arise.

The measurement date used to determine the present value of the benefit obligation is December 31 of the applicable year. The latest actuarial valuation was performed as at January 1, 2016.

n) Customer deposits

Security deposits from electricity customers are cash collections to guarantee the payment of electricity bills. This liability includes related interest amounts owed to the customers with a corresponding amount charged to finance costs. Deposits that are refundable upon demand are classified as a current liability.

Security deposits on offers to connect are cash collections from specific customers to guarantee the payment of additional costs relating to expansion projects. This liability includes related interest amounts owed to the customers with a corresponding amount charged to finance costs. Deposits are classified as a current liability when the Corporation no longer has an unconditional right to defer payment of the liability for at least 12 months after the reporting period.

o) Income taxes

Under the Electricity Act, the Corporation is required to make PILs to the Ontario Electricity Financial Corporation. These payments are calculated in accordance with the ITA and the TA as modified by regulations made under the Electricity Act and related regulations. This effectively results in the Corporation paying income taxes equivalent to what would be imposed under the Federal and Ontario Tax Acts.

The Corporation uses the liability method of accounting for income taxes. Under the liability method, current income taxes payable are recorded based on taxable income. The Corporation recognizes deferred tax assets and liabilities for the future tax consequences of events that have been included in the Consolidated Financial Statements or income tax returns. Deferred tax assets and liabilities are determined based on the difference between the carrying value of assets and liabilities on the consolidated balance sheets and their respective tax basis, using the tax rates enacted or substantively enacted by the consolidated balance sheet date that are in effect for the year in which the differences are expected to reverse. Tax benefits associated with income tax positions taken, or expected to be taken, in a tax return are recorded only when it is probable that they will be realized, and are measured at the best estimate of the tax amount expected to be paid to or recovered from the taxation authorities. Deferred tax assets are reviewed at each reporting date and reduced to the extent that it is no longer probable that the related tax benefits will be realized. The calculation of current and deferred taxes requires management to make certain judgments with respect to changes in tax interpretations, regulations and legislation, and to estimate probable outcomes on the timing and reversal of temporary differences and tax authority audits of income tax.

Rate-regulated accounting requires the recognition of regulatory balances and related deferred tax assets and liabilities for the amount of deferred taxes expected to be refunded to or recovered from customers through future electricity distribution rates. A gross up to reflect the income tax benefits associated with reduced revenues resulting from the realization of deferred tax assets is recorded within regulatory credit balances. Deferred taxes that are not included in the rate-setting process are charged or credited to the consolidated statements of income.

The benefits of the refundable and non-refundable apprenticeship and other ITCs are credited against the related expense in the consolidated statements of income.

p) Use of judgments and estimates

The preparation of the Corporation's Consolidated Financial Statements in accordance with IFRS requires management to make judgments, estimates and assumptions which affect the application of accounting policies, reported assets, liabilities and regulatory balances, and the disclosure of contingent assets and liabilities at the date of the Consolidated Financial Statements, and the reported revenues and expenses for the year. The estimates are based on historical experience, current conditions and various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities as well as for identifying and assessing the accounting treatment with respect to commitments and contingencies. Actual results could differ from those estimates, including changes as a result of future decisions made by the OEB, the IESO, the Ontario Ministry of Energy or the Ontario Ministry of Finance.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to estimates are recognized prospectively. Assumptions and estimates with a significant risk of resulting in a material adjustment within the next financial year are used in the following:

- Note 26[b] – Recognition and measurement of regulatory balances;
- Note 26[j] – Revenue recognition – measurement of unbilled revenue, determination of the CDM incentive;
- Notes 26[f] and 26[g] – Determination of useful lives of depreciable assets;
- Notes 26[m] and 14 – Measurement of post-employment benefits – key actuarial assumptions;
- Notes 26[o] and 21 – Recognition of deferred tax assets – availability of future taxable income against which deductible temporary differences and tax loss carryforwards can be used; and
- Note 25 – Recognition and measurement of provisions and contingencies.

q) Changes in accounting policies

In January 2016, the IASB issued amendments to IAS 7 *Statement of Cash Flows* as part of the IASB's Disclosure Initiative. These amendments require entities to provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including changes from cash flows and non-cash changes. These amendments are effective for annual periods beginning on or after January 1, 2017. The additional disclosures relating to changes in liabilities arising from financing activities are included in note 22 and have no impact to the Corporation's financial position or results of operations.

r) Future accounting pronouncements

A number of new standards, amendments and interpretations are not yet effective for the year ended December 31, 2017, and have not yet been applied in preparing these Consolidated Financial Statements.

Revenue from Contracts with Customers

In May 2014, the IASB issued IFRS 15 *Revenue from Contracts with Customers* ["IFRS 15"], which replaces existing revenue recognition guidance, including IAS 18 *Revenue* and IFRIC 18 *Transfers of Assets from Customers*. IFRS 15 contains a single model that applies to contracts with customers with two methods for recognizing revenue: at a point in time or over time. IFRS 15 is effective for annual periods beginning on or after January 1, 2018.

The Corporation will adopt IFRS 15 on January 1, 2018 using the modified retrospective approach. The Corporation has completed its assessment of the key revenue streams. The majority of the Corporation's revenue (energy sales and

distribution revenue) is generated from electricity distribution at regulated prices. The Corporation concluded that IFRS 15 will not have a material impact on the accounting for these revenue streams. Upon adoption of IFRS 15, there will be a $167.6 million income statement reclassification between Energy Sales and Energy Purchases for the comparative year ended December 31, 2017 and no impact to opening retained earnings as at January 1, 2018. The Corporation is currently finalizing its assessment on capital contributions. The Corporation has determined that IFRS 15 will also increase its required disclosure on revenue streams.

Financial Instruments

In July 2014, the IASB issued the final version of IFRS 9 *Financial Instruments* [“IFRS 9”], which replaces IAS 39 *Financial Instruments: Recognition and Measurement* [“IAS 39”]. IFRS 9 includes revised guidance on the classification and measurement of financial instruments, including a new expected credit loss model for measuring impairment on financial assets, and new general hedge accounting requirements. It also carries forward the guidance on recognition and derecognition of financial instruments from IAS 39. The standard is effective for annual periods beginning on or after January 1, 2018, and will be applied retrospectively with some exceptions. The Corporation has assessed the impact of adopting IFRS 9, and concluded that the new classification under IFRS 9 will not have a material impact on the consolidated financial statements. Management is currently evaluating the impact of adopting the new expected credit loss model for measuring impairment.

Leases

In January 2016, the IASB issued IFRS 16 *Leases* [“IFRS 16”], which replaces IAS 17 *Leases* [“IAS 17”] and related interpretations. IFRS 16 introduces a single lessee accounting model eliminating the current distinction between finance and operating leases. It requires the recognition of lease-related assets and liabilities on the balance sheet, except for short-term leases and leases of low value underlying assets. In addition, the nature and timing of expenses related to leases will change, as IFRS 16 replaces the straight-line operating leases expense with the depreciation expense for the assets and interest expense on the lease liabilities. Lessor accounting remains substantially unchanged. The standard is effective for annual periods beginning on or after January 1, 2019, and may be applied either retrospectively or using a modified retrospective approach. Early adoption is permitted if IFRS 15 is also adopted.

The Corporation intends to early adopt IFRS 16 on January 1, 2018. The Corporation has completed its assessment of existing operating leases. IFRS 16 will not have a significant impact on the Corporation’s consolidated financial statements and the Corporation has assessed the quantitative impact of adopting IFRS 16 to be $nil in opening retained earnings, and an increase of $1.6 million in total assets and total liabilities for the right-of-use assets and the lease liabilities, respectively, as at January 1, 2018.