



**ANNUAL INFORMATION FORM
FOR THE YEAR ENDED DECEMBER 31, 2011**

March 29, 2012

TABLE OF CONTENTS

PART 1 - FORWARD-LOOKING INFORMATION.....	5
PART 2 - GLOSSARY OF DEFINED TERMS	5
PART 3 - CORPORATE STRUCTURE.....	10
3.1 Name, Address, Incorporation	10
3.2 Inter-corporate Relationships	10
PART 4 - BUSINESS OF TORONTO HYDRO.....	11
4.1 Industry Structure.....	11
4.2 Toronto Hydro Corporation	12
4.3 Toronto Hydro-Electric System Limited.....	12
(a) LDC's Electricity Distribution System	12
(i) Control Centre.....	12
(ii) Terminal Stations	12
(iii) Distribution Transformers and Municipal Substations.....	12
(iv) Wires	13
(v) Metering	13
(vi) Reliability of Distribution System.....	13
(b) LDC's Service Area and Customers	13
(c) LDC's Customer Care and Billing System	14
(d) LDC's Real Property	14
(e) Regulation of LDC.....	15
(i) Legislative Framework.....	15
(ii) Licences	16
(iii) Industry Codes	16
(f) Distribution Rates.....	18
(i) Rate Setting Mechanism.....	18
(ii) Other Regulated Charges	18
4.4 Toronto Hydro Energy Services Inc.....	18
4.5 Environmental Matters.....	19
(a) Environmental Protection Requirements.....	19
(b) Financial and Operational Effects of Environmental Protection Requirements.....	19
(c) Environmental Policy and Oversight	19
4.6 Additional Information Regarding Toronto Hydro	20
(a) Employees.....	20
(b) Specialized Skills and Knowledge	20
(c) Health and Safety	20
(d) Code of Business Conduct	21
(e) Insurance	21
(f) Lending and Investments	21
(g) Intangible Property.....	21
(h) Seasonal Effects	21
PART 5 - GENERAL DEVELOPMENT OF THE BUSINESS	22
5.1 Business Operations	22
5.2 Rate Applications	22
(a) 2009 Rate Year.....	22
(b) 2010 Rate Year.....	22
(c) 2011 Rate Year.....	22
(d) 2012-2014 Rate Application	23
5.3 Street Lighting Activities	24
5.4 Conservation and Demand Management	24
5.5 Contact Voltage.....	25
5.6 OEB PILs Proceeding	25
5.7 Accounting Standards	25

PART 6 - RELATIONSHIP WITH THE CITY	26
6.1 Shareholder Direction	26
(a) Shareholder Objectives	26
(b) Principles Governing Operations	26
(c) Shareholder Approval	27
(d) Financial Performance	27
(e) Credit Rating	27
(f) Dividends	28
6.2 Indebtedness to the City	28
6.3 Services Provided to the City	28
PART 7 - TAXATION	29
7.1 Tax Regime	29
7.2 PILs Recoveries through Rates	30
7.3 Tax Contingencies	30
PART 8 - RISK FACTORS	30
8.1 Condition of Distribution Assets	30
8.2 Regulatory Developments	30
8.3 Information Technology Infrastructure	31
8.4 Labour Relations	31
8.5 Natural and Other Unexpected Occurrences	31
8.6 Electricity Consumption	32
8.7 Market and Credit Risk	32
8.8 Additional Debt Financing	32
8.9 Work Force Renewal	32
8.10 Insurance	33
8.11 Credit Rating	33
8.12 Conflicts of Interest	33
8.13 Change of Ownership	33
8.14 Conversion to US GAAP	33
8.15 Real Property Rights	33
8.16 LDC Competition	33
PART 9 - CAPITAL STRUCTURE	34
9.1 Share Capital	34
9.2 Debentures	34
9.3 Credit Ratings	35
PART 10 - DIRECTORS AND OFFICERS	35
10.1 Nomination of Directors	35
10.2 Directors and Officers	36
10.3 Principal Occupations	37
10.4 Cease Trade Orders, Bankruptcies, Penalties or Sanctions	37
10.5 Independence	38
10.6 Committees of the Board of Directors	38
(a) Audit Committee	38
(b) Corporate Governance Committee	38
(c) Compensation Committee	39
(d) Health and Safety Committee	39
10.7 Board Orientation and Continuing Education	39
10.8 Board, Committee and Director Assessments	39
10.9 Board Oversight and Management of Risks	39
PART 11 - AUDIT COMMITTEE	40
11.1 Composition, Independence and Financial Literacy	40
11.2 Relevant Education and Experience	40
11.3 Audit Committee Charter	41
11.4 Policy on the Provision of Services by the External Auditors	41
11.5 External Auditors Service Fees	42

PART 12 - EXECUTIVE COMPENSATION	42
12.1 Compensation Governance	42
(a) Compensation Committee	42
(i) Composition and Independence	42
(ii) Relevant Education and Experience	42
(iii) Compensation Committee Charter	43
(b) Compensation Risk Oversight.....	43
12.2 Compensation Discussion and Analysis.....	44
(a) Named Executive Officers	44
(b) General Objectives of Compensation Program	44
(c) Process for Establishing Compensation	44
(i) Policies and Practices.....	44
(ii) Benchmarking	45
(iii) Compensation Consultants and Advisors	45
(d) Elements of Compensation.....	46
The principal components of compensation for NEOs are:	46
(i) Base Salary.....	46
(ii) Performance-Based Incentive Compensation.....	46
(iii) Personal Benefits and Perquisites	47
(iv) Pension Plan.....	47
(v) Retirement Benefits.....	47
(vi) Retirement Allowances	48
(vii) Termination Payments	48
12.3 Compensation of Named Executive Officers	48
(a) Summary Compensation Table	48
(b) Compensation of NEOs in 2011 – Narrative Discussion	49
(i) Base Salaries	49
(ii) Performance-Based Incentive Compensation.....	49
(iii) Personal Benefits and Perquisites	51
(iv) Pension Plan.....	51
(v) Retirement Benefits.....	51
(vi) Retirement Allowance.....	51
(vii) Termination Payments	51
12.4 Compensation of Directors.....	52
(a) Director Compensation Table	52
(b) Compensation of Directors – Narrative Discussion	52
PART 13 - LEGAL PROCEEDINGS	52
13.1 Christian Helm Class Action.....	53
13.2 2 Secord Avenue	53
13.3 2369 Lakeshore Boulevard West	53
13.4 Adamopoulos	54
13.5 Late Payment Charges Class Action	54
PART 14 - MATERIAL CONTRACTS	55
PART 15 - NAMED AND INTERESTS OF EXPERTS	55
PART 16 - TRANSFER AGENTS AND REGISTRARS.....	55
PART 17 - ADDITIONAL INFORMATION	55
ANNEX A - AUDIT COMMITTEE CHARTER	1

PART 1 - FORWARD-LOOKING INFORMATION

The Corporation includes forward-looking information in this Annual Information Form (the "AIF") within the meaning of applicable securities laws in Canada ("forward-looking information"). The purpose of the forward-looking information is to provide management's expectations regarding the Corporation's future results of operations, performance, business prospects and opportunities and may not be appropriate for other purposes. All forward-looking information is given pursuant to the "safe harbour" provisions of applicable Canadian securities legislation. The words "anticipates", "believes", "budgets", "could", "estimates", "expects", "forecasts", "intends", "may", "might", "plans", "projects", "schedule", "should", "will", "would" and similar expressions are often intended to identify forward-looking information, although not all forward-looking information contains these identifying words. The forward-looking information reflects management's current beliefs and is based on information currently available to the Corporation's management.

The forward-looking information in the AIF includes, but is not limited to, statements regarding the future financial and operational effects of LDC's environmental protection requirements, the outcome of outstanding rate applications and other proceedings before the OEB, LDC's CDM programs, the Corporation's conversion to US GAAP, the outcome of outstanding proceedings before the Ministry of Finance, the Corporation's plans to borrow funds to repay maturing Debentures and to finance the investment in LDC's infrastructure, the expected results of legal proceedings, market volatility on the Corporation's consolidated results of operations, performance, business prospects and opportunities, and the effect of changes in interest rates on future revenue requirements. The statements that make up the forward-looking information are based on assumptions that include, but are not limited to, the future course of the economy and financial markets, the receipt of applicable regulatory approvals and requested rate orders, the receipt of favourable judgments, the level of interest rates, the Corporation's ability to borrow, and the impact of the conversion to US GAAP on the Corporation's Consolidated Financial Statements.

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, market liquidity and the quality of the underlying assets and financial instruments, the timing and extent of changes in prevailing interest rates, inflation levels, legislative, judicial and regulatory developments that could affect revenues and the results of borrowing efforts.

Additional factors which could cause actual results or outcomes to differ materially from the results expressed or implied by forward-looking information include, among other things, the risk factors listed under Part 8 "Risk Factors" in this AIF. Please review this Part 8 – "Risk Factors" in detail. The Corporation cautions that the above list of risk factors is not exhaustive.

All forward-looking information in this AIF is qualified in its entirety by the above cautionary statements and, except as required by law, the Corporation undertakes no obligation to revise or update any forward-looking information as a result of new information, future events or otherwise after the date hereof.

PART 2 - GLOSSARY OF DEFINED TERMS

"2006 Rate Handbook" refers to the Electricity Distribution Rate Handbook issued by the OEB in May 2005 and containing filing requirements and guidelines and setting out how the OEB generally intends to address applications for 2006 electricity distribution rates, as amended.

"Affiliate Relationships Code" refers to the Affiliate Relationships Code for Electricity Distributors and Transmitters that was published by the OEB and became effective on April 1, 1999, as amended.

"AIF" refers to the Corporation's Annual Information Form for the year ended December 31, 2011.

"Amended and Restated City Note" refers to the Amended and Restated City Note dated May 1, 2006, in the principal amount of \$980,230,955, issued by the Corporation to the City. The Amended and Restated City Note has been cancelled. See section 6.2 under the heading "Indebtedness to the City".

"Board" refers to the board of directors of the Corporation.

"CAIDI" refers to the Customer Average Interruption Duration Index and is a measure (in hours) of the average duration of interruptions experienced by customers, not including MED. CAIDI represents the quotient obtained by dividing SAIDI by SAIFI.

"Canadian Environmental Protection Act" refers to the *Canadian Environmental Protection Act, 1999* (Canada), as amended.

"Capital Assets" refers to the sum of property, plant and equipment and intangible assets, in each case, net of accumulated amortization. See note 3(f), note 3(g), note 5, and note 6 to the Consolidated Financial Statements.

"Capital Expenditures" refers to expenditures relating to property, plant and equipment and intangible assets.

"CDM" refers to conservation and demand management.

"CEA" refers to the Canadian Electricity Association.

"CEO" refers to the President and Chief Executive Officer of the Corporation.

"CFO" refers to the Chief Financial Officer of the Corporation.

"City" refers to the city incorporated under the *City of Toronto Act, 1997* (Ontario) and comprised of the former municipalities of Metropolitan Toronto, Toronto, East York, Etobicoke, North York, Scarborough and York.

"Class Proceedings Act" refers to the *Class Proceedings Act, 1992* (Ontario), as amended.

"Consolidated Financial Statements" refers to the audited consolidated balance sheets of the Corporation as at December 31, 2011 and the audited consolidated statements of retained earnings, income and cash flows of the Corporation for the year ended December 31, 2011, together with the auditors' report thereon and the notes thereto, copies of which are available on the SEDAR website at www.sedar.com.

"Consumer Price Index" refers to the index measuring price movements published by Statistics Canada.

"Consumer Protection Act" refers to the *Consumer Protection Act, 2002* (Ontario), as amended.

"Corporation" refers to Toronto Hydro Corporation.

"Criminal Code" refers to the *Criminal Code* (Canada), as amended.

"CTA" refers to the *Corporations Tax Act* (Ontario), as amended.

"Dangerous Goods Transportation Act" refers to the *Dangerous Goods Transportation Act* (Ontario), as amended.

"DBRS" refers to DBRS Limited.

"Debentures" refers to the 6.11% Series 1 senior unsecured debentures issued by the Corporation on May 7, 2003, the 5.15% Series 2 senior unsecured debentures issued by the Corporation on November 14, 2007, the 4.49% Series 3 senior unsecured debentures issued by the Corporation on November 12, 2009, the 6.11% Series 4 senior unsecured debentures issued by the Corporation on April 1, 2010, the 6.11% Series 5 senior unsecured debentures issued by the Corporation on April 1, 2010, the 5.54% Series 6 senior unsecured debentures issued by the

Corporation on May 20, 2010, and the 3.54% Series 7 senior unsecured debentures issued by the Corporation on November 18, 2011. See note 11 to the Consolidated Financial Statements.

"Distribution System Code" refers to the Distribution System Code that was published by the OEB on July 14, 2000, as amended.

"Electricity Act" refers to the *Electricity Act, 1998* (Ontario), as amended.

"Electricity Property" refers to a municipal corporation's or an MEU's interest in real or personal property used in connection with generating, transmitting, distributing or retailing electricity.

"Electricity Restructuring Act" refers to the *Electricity Restructuring Act, 2004* (Ontario), as amended.

"Energy Competition Act" refers to the *Energy Competition Act, 1998* (Ontario), as amended.

"Energy Consumer Protection Act" refers to the *Energy Consumer Protection Act, 2010* (Ontario), as amended.

"Environmental Protection Act" refers to the *Environmental Protection Act, 1990* (Ontario), as amended.

"Fire Protection and Prevention Act" refers to the *Fire Protection and Prevention Act, 1997* (Ontario), as amended.

"GAAP" refers to Generally Acceptable Accounting Principles.

"Green Energy Act" refers to the *Green Energy and Green Economy Act, 2009* (Ontario), as amended.

"GWh" refers to a gigawatt-hour, a standard unit for measuring electrical energy produced or consumed over time. One GWh is the amount of electricity consumed by one million kWh.

"Hydro One" refers to Hydro One Inc.

"IEEE" refers to the Institute of Electrical and Electronic Engineers Inc.

"IESO" refers to the Independent Electricity System Operator.

"IFRS" refers to the International Financial Reporting Standards.

"Interest Act" refers to the *Interest Act* (Canada), as amended.

"ITA" refers to the *Income Tax Act* (Canada), as amended.

"kW" refers to a kilowatt, a common measure of electrical power equal to 1,000 Watts.

"kWh" refers to a kilowatt-hour, a standard unit for measuring electrical energy produced or consumed over time. One kWh is the amount of electricity consumed by ten 100 Watt light bulbs burning for one hour.

"LDC" refers to the Corporation's wholly-owned subsidiary, Toronto Hydro-Electric System Limited.

"Management's Discussion and Analysis" refers to Management's Discussion and Analysis of Financial Condition and Results of Operations of the Corporation for the year ended December 31, 2011, a copy of which is available on the SEDAR website at www.sedar.com.

"Market Participants" refers to persons authorized to participate in the wholesale market for electricity administered by the IESO, including generators, transmitters, electricity distributors, retailers and consumers.

"**MED**" refers to major event days as defined by IEEE specification 1366.

"**Mercer**" refers to Mercer (Canada) Limited.

"**MEU**" refers to a municipal electricity utility in the Province of Ontario.

"**Ministry of Finance**" refers to the Ministry of Finance of Ontario.

"**MTN Program**" refers to the medium term note program established by the Corporation under which the Corporation issues Debentures. See section 9.2 under the heading "Debentures".

"**MW**" refers to megawatt, a common measure of electrical power equal to one million watts.

"**Named Executive Officer**" or "**NEO**" means, collectively, the Corporation's CEO, the CFO, and the three most highly compensated executive officers of Toronto Hydro who were serving as executive officers as at December 31, 2011, and each individual who would be amongst the three most highly compensated executive officers for the Corporation, but for the fact that such individuals were not executive officers on December 31, 2011, if any.

"**OBCA**" refers to the *Business Corporations Act* (Ontario), as amended.

"**OEB**" refers to the Ontario Energy Board.

"**OEB Act**" refers to the *Ontario Energy Board Act, 1998* (Ontario), as amended.

"**OEFC**" refers to the Ontario Electricity Financial Corporation.

"**OMERS**" refers to the Ontario Municipal Employees Retirement System, a multi-employer, contributory, defined benefit pension plan established in 1962 by the Province for employees of municipalities, local boards and school boards in Ontario.

"**OPA**" refers to the Ontario Power Authority.

"**Open Access**" refers to the opening of the Province's wholesale and retail electricity markets to competition pursuant to the requirement under the Electricity Act that transmitters and distributors of electricity in the Province provide generators, retailers and consumers with non-discriminatory access to their transmission and electricity distribution systems. Open Access commenced on May 1, 2002.

"**OPG**" refers to Ontario Power Generation Inc.

"**PCBs**" refers to polychlorinated biphenyls, a synthetic chemical compound consisting of chlorine, carbon and hydrogen. PCBs are used primarily as insulating and cooling elements in electrical equipment. Secondary uses include hydraulic and heat transfer fluids, flame proofing adhesives, paints, sealants and cable insulating paper.

"**PILs**" refers to the Payment In Lieu of Corporate Taxes regime contained in the Electricity Act pursuant to which MEUs that are exempt from tax under the ITA, the CTA and the TA are required to make, for each taxation year, payments in lieu of corporate taxes to the OEFC. See note 3(p) and note 18 to the Consolidated Financial Statements.

"**Province**" refers to the Province of Ontario.

"**Residential Tenancies Act**" refers to the *Residential Tenancies Act, 2006* (Ontario), as amended.

"**Retail Settlement Code**" refers to the Retail Settlement Code that was published by the OEB on December 13, 2000 and became effective on the commencement of Open Access (except with respect to "Service Agreements", as that term is defined in the Retail Settlement Code, which came into effect on March 1, 2001), as amended.

"ROE" refers to return on equity.

"RPP" refers to the Regulated Price Plan created as a result of the Electricity Restructuring Act, as amended. The OEB has developed an RPP for residential, small business and certain other customers, which came into effect on April 1, 2005.

"S&P" refers to Standard & Poor's.

"SAIDI" means System Average Interruption Duration Index and is a measure (in hours) of the annual system average interruption duration for customers served, not including MED. SAIDI represents the quotient obtained by dividing the total customer hours of interruptions longer than one minute by the number of customers served.

"SAIFI" means System Average Interruption Frequency Index and is a measure of the frequency of service interruptions for customers served, not including MED. SAIFI represents the quotient obtained by dividing the total number of customer interruptions longer than one minute by the number of customers served.

"SEDAR" refers to the Canadian Securities Administrators' System for Electronic Document Analysis and Retrieval. SEDAR's website is www.sedar.com.

"Shareholder Direction" refers to the Shareholder Direction adopted by the Council of the City with respect to the Corporation, as amended and restated from time to time, pursuant to which the City has set out certain corporate governance principles with respect to the Corporation.

"Smart Meter" refers to a metering device capable of recording and transmitting hourly consumption information of a residential or general service customer.

"Smart Sub-Metering Code" refers to the Smart Sub-Metering Code that was published by the OEB on July 24, 2008, as amended.

"Standard Supply Customers" refers to persons connected to an electricity distributor's distribution system who are not served by retailers or whose retailer is unable to sell them electricity or who request the distributor to sell electricity to them.

"Standard Supply Service" refers to an electricity distributor's obligation to sell electricity to Standard Supply Customers, or to give effect to such rates as determined by the OEB under section 79.16 of the OEB Act.

"Standard Supply Service Code" refers to the Standard Supply Service Code for Electricity Distributors that was published by the OEB on December 8, 1999 and became effective on the commencement of Open Access, as amended.

"TA" refers to the *Taxation Act, 2007* (Ontario), as amended.

"Technical Standards and Safety Act" refers to the *Technical Standards and Safety Act, 2000* (Ontario), as amended.

"TH Energy" refers to the Corporation's wholly-owned subsidiary, Toronto Hydro Energy Services Inc.

"Time-of-Use" refers to differential electricity rates charged on consumption depending on the time of day.

"Toronto Hydro" refers to the Corporation and its subsidiaries.

"Transfer By-law" refers to By-law No. 374-1999 of the City made under section 145 of the Electricity Act pursuant to which the Toronto Hydro-Electric Commission and the City transferred their assets and liabilities and employees in respect of the electricity distribution system to LDC and in respect of electricity generation, co-generation and energy services to TH Energy. See note 1 to the Consolidated Financial Statements. The Transfer By-law permits the Treasurer of the City to adjust the fair market value of the assets and the consideration paid in

respect of the electricity distribution assets transferred to LDC as a consequence of OEB rate orders and permitted rates of return for 2000 or any subsequent year.

"Transportation of Dangerous Goods Act" refers to the *Transportation of Dangerous Goods Act, 1992* (Canada), as amended.

"Unit Smart Meter" refers to a unit Smart Meter installed by LDC in a unit of a multi-unit complex where the multi-unit complex is not connected to a bulk meter, and includes such other meters as may be prescribed by the Energy Consumer Protection Act.

"US GAAP" refers to United States Generally Accepted Accounting Principles.

"Watt" or **"W"** refers to a common measure of electrical power. One Watt equals the power used when one ampere of current flows through an electrical circuit with a potential of one volt.

Unless otherwise specified, all references to statutes are to statutes of the Province and all references to dollars are to Canadian dollars.

PART 3 - CORPORATE STRUCTURE

3.1 Name, Address, Incorporation

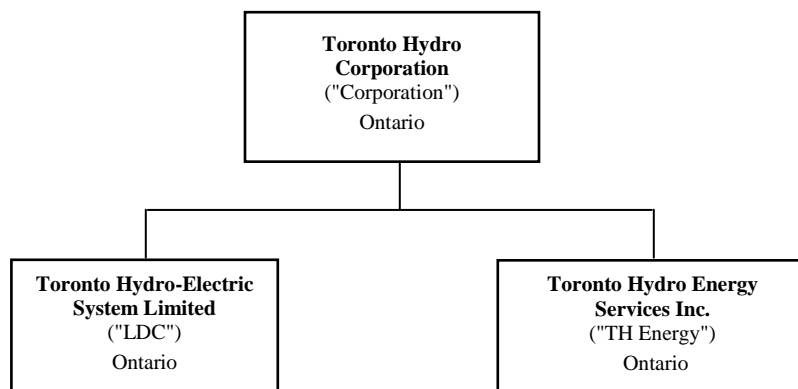
On January 1, 1998, the former municipalities of Metropolitan Toronto, Toronto, East York, Etobicoke, North York, Scarborough and York amalgamated to form the City. At the same time, the electric commissions of Toronto, East York, Etobicoke, North York, Scarborough and York were combined to form the Toronto Hydro-Electric Commission. Toronto Hydro is the successor to the Toronto Hydro-Electric Commission.

The Corporation, LDC and TH Energy were incorporated under the OBCA on June 23, 1999. Pursuant to the Transfer By-law, the Toronto Hydro-Electric Commission and the City transferred their assets and liabilities in respect of the electricity distribution system to LDC and electricity generation, co-generation and energy services to TH Energy. See note 1 to the Consolidated Financial Statements.

The registered and head office of the Corporation is located at 14 Carlton Street, Toronto, Ontario, M5B 1K5.

3.2 Inter-corporate Relationships

The sole shareholder of the Corporation is the City. The Corporation, in turn, owns 100% of the shares of the principal subsidiaries listed below, each of which was incorporated under the OBCA:



PART 4- BUSINESS OF TORONTO HYDRO

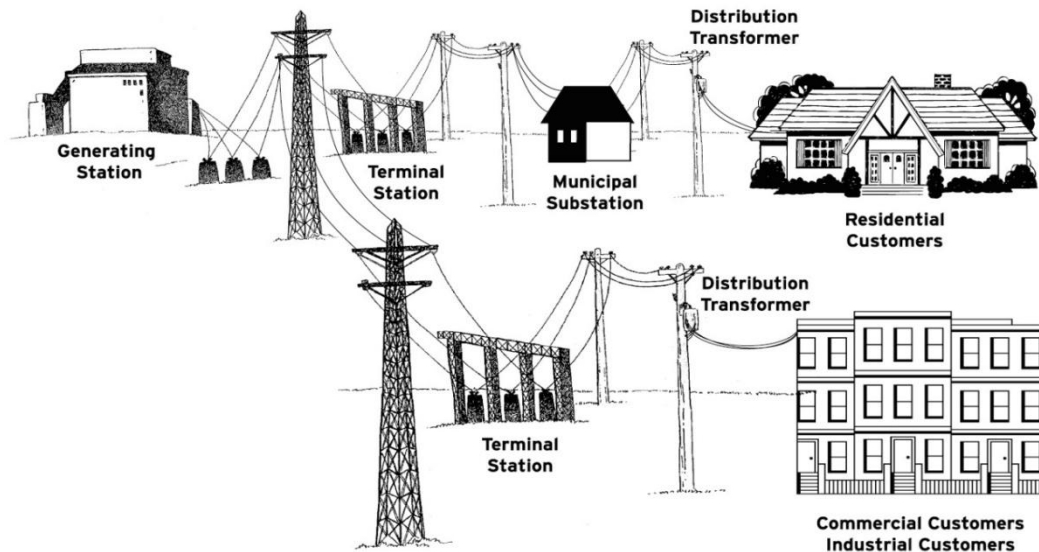
4.1 Industry Structure

The electricity industry in the Province is divided into four principal segments:

- Generation - the production of electricity at generating stations using nuclear, fossil, hydro or other sources of energy;
- Transmission - the transfer of electricity from generating stations to local areas using large, high-voltage power lines;
- Distribution - the delivery of electricity to homes and businesses within local areas using relatively low-voltage power lines; and
- Retailing - the purchase of electricity from generators and its sale to consumers together with a range of related services such as energy profiling and energy management.

Electricity produced at generating stations is boosted to high voltages by nearby transformers so that the electricity can be transmitted long distances over transmission lines with limited power loss. The voltage is then reduced (stepped down) at terminal stations for supply to electricity distributors or large customers. Electricity distributors carry the electricity to distribution transformers that further reduce the voltage for supply to local customers. Electricity is distributed in the Province through a network of local electricity distributors that includes approximately eighty municipal electricity distributors, a few privately owned electricity distributors, and Hydro One.

The following diagram illustrates the basic structure of an electricity infrastructure system:



4.2 Toronto Hydro Corporation

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

- LDC – which distributes electricity and engages in CDM activities; and
- TH Energy – which provides street lighting services.

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

4.3 Toronto Hydro-Electric System Limited

The principal business of Toronto Hydro is the distribution of electricity by LDC. LDC owns and operates \$2.4 billion of Capital Assets comprised primarily of an electricity distribution system that delivers electricity to approximately 709,000 customers located in the City. LDC is the largest municipal electricity distribution company in Canada and distributes approximately 18% of the electricity consumed in the Province.

(a) LDC's Electricity Distribution System

Electricity produced at generating stations is transmitted along transmission lines owned by Hydro One to terminal stations at which point the voltage is then reduced (or stepped down) to distribution-level voltages. Distribution-level voltages are then distributed across LDC's electricity distribution system to distribution class transformers at which point the voltage is further reduced (or stepped down) for supply to end use customers. Electricity typically passes through a meter before reaching a distribution board or service panel that directs the electricity to end use circuits.

LDC's electricity distribution system is serviced from 35 terminal stations and is comprised of approximately 19,800 primary switches, approximately 60,600 distribution transformers, 170 in-service municipal sub-stations, approximately 15,100 kilometres of overhead wires supported by approximately 140,600 poles and approximately 10,900 kilometres of underground wires.

(i) Control Centre

LDC has one control centre. The control centre co-ordinates and monitors the distribution of electricity throughout its electricity distribution assets, and provides isolation and work protection for LDC's construction and maintenance crews and external customers. LDC's control centre utilizes supervisory control and data acquisition (SCADA) systems to monitor, operate, sectionalize, and restore the electricity distribution system.

(ii) Terminal Stations

LDC receives electricity at 35 transmission system terminal stations at which the voltage is stepped down to distribution-level voltages. The terminal stations contain power transformers and high-voltage switching equipment that are owned by Hydro One, with the exception of Cavanagh station which is fully owned by LDC. Terminal stations also contain low-voltage equipment such as circuit breakers, switches and station busses that are typically owned by LDC.

(iii) Distribution Transformers and Municipal Substations

Distribution voltage electricity is distributed from the terminal stations to distribution transformers that are typically located in buildings or vaults or mounted on poles or surface pads and that are used to reduce or step down voltages to utilization levels for supply to customers. The electricity distribution system includes approximately 60,600 distribution transformers. The electricity distribution system also includes 170 in-service municipal sub-stations that are located in various parts of the City and are used to reduce or step down electricity voltage prior to delivery to

distribution transformers. LDC also delivers electricity at distribution voltages directly to certain commercial and industrial customers that own their own substations.

(iv) *Wires*

LDC distributes electricity through a network comprised of an overhead circuit of approximately 15,100 kilometres supported by approximately 140,600 poles and an underground circuit of approximately 10,900 kilometres.

(v) *Metering*

LDC provides its customers with meters through which electricity passes before reaching a distribution board or service panel that directs the electricity to end use circuits on the customer's premises. The meters are used to measure electricity consumption. LDC owns the meters and is responsible for their maintenance and accuracy.

In accordance with the decision by the Province's Ministry of Energy to install Smart Meters throughout the Province, LDC launched its Smart Meter project in 2006. The Smart Meter project's objective was to install Smart Meters and supporting infrastructure for all residential and commercial customers. LDC substantially completed its Smart Meter project in 2010.

As part of its metering services and Smart Meter project, LDC also installs Unit Smart Meters in multi-unit complexes. As at December 31, 2011, LDC had installed approximately 23,000 Unit Smart Meters in multi-unit complexes.

(vi) *Reliability of Distribution System*

The table below sets forth certain industry recognized measurements of system reliability with respect to LDC's electricity distribution system and the composite measures reported by LDC and the CEA for the twelve month periods ending December 31 in the years indicated below.

	<u>LDC</u> <u>2011</u>	<u>LDC</u> <u>2010</u>	<u>CEA</u> <u>2010⁽¹⁾</u>
SAIDI	1.43	1.29	4.34
SAIFI	1.62	1.77	2.11
CAIDI	0.88	0.73	2.06

Note:

(1) CEA 2010 Service Continuity Report on Distribution System Performance in Canadian Electrical Utilities, excluding significant events. At the date of this AIF, the CEA 2011 Service Continuity Report has not been published.

(b) LDC's Service Area and Customers

LDC is the sole provider of electricity distribution services in the City, and serves approximately 709,000 customers. The City is the largest city in Canada with a population of approximately 2.5 million. The City is a financial centre with large and diversified service and industrial sectors.

The table below sets out LDC's customer classes and certain operating data with respect to each class for each of the years in the two-year period ended December 31, 2011:

	<u>Year ended December 31</u>	
	<u>2011</u>	<u>2010</u>
Residential Service ⁽¹⁾		
Number of customers (as at December 31).....	629,049	620,501

	Year ended December 31	
	2011	2010
kWh	5,204,012,541	5,209,204,594
Revenue	\$703,765,567	\$657,418,209
% of total service revenue	25.4%	25.7%
General Service ⁽²⁾		
Number of customers (as at December 31)	80,222	79,836
kWh	17,148,430,298	17,317,547,986
Revenue	\$1,824,321,064	\$1,705,831,766
% of total service revenue	66.0%	66.6%
Large Users ⁽³⁾		
Number of customers (as at December 31)	52	50
kWh	2,355,143,073	2,219,247,453
Revenue	\$238,627,556	\$198,167,877
% of total service revenue	8.6%	7.7%
Total		
Number of customers (as at December 31)	709,323	700,387
kWh	24,707,585,912	24,746,000,033
Revenue	\$2,766,714,187	\$2,561,417,852

Notes:

- (1) "Residential Service" means a service that is for domestic or household purposes, including single family or individually metered multi-family units and seasonal occupancy.
- (2) "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.
- (3) "Large Users" means a service provided to a customer with a monthly peak demand of 5,000 kW or more averaged over a twelve-month period.

(c) LDC's Customer Care and Billing System

On July 6, 2011, LDC implemented a new customer care and billing system for its regulated electricity distribution business. The new system allows for more flexibility for its users and provides better information for the calculation of accounting estimates related to revenue recognition. The system provides an integrated billing platform leveraging the technology of the Smart Meters installed over the past few years.

(d) LDC's Real Property

The following table sets forth summary information with respect to the principal real property owned, leased or otherwise used by LDC:

Property	Total	Owned	Leased	Other⁽¹⁾
Terminal stations	35 sites	8	-	27
Municipal sub-stations	170 sites	157	4	9
Decommissioned municipal sub-stations.....	37 sites	37	-	-
Control centre ⁽²⁾	1 site	1	-	-
Operations centres ⁽³⁾	7 sites	3	4	-

Other ⁽⁴⁾	2 sites	2	-	-
----------------------------	---------	---	---	---

Notes:

- (1) Certain terminal stations and municipal substations are located on lands owned by the Province, the City and others. Where electricity distribution lines cross over and run parallel with lands owned by railway companies, appropriate access rights, generally referred to as crossing agreements, have been obtained from the railway companies.
- (2) LDC's control centre is located within one of its operations centres.
- (3) LDC's operation centres accommodate office, staff, crews, vehicles, equipment and material necessary to operate and monitor the electricity distribution systems.
- (4) Parcels of land for future use.

Under the OEB Act, electricity distributors are entitled to apply to the OEB for authority to expropriate land required in connection with new or expanded electricity distribution lines or interconnections. If, after a hearing, the OEB is of the opinion that the expropriation of land is in the public interest, the OEB may make an order authorizing expropriation upon payment of specified compensation. The Electricity Act grandfathered thousands of existing unregistered easements, principally for distribution over third-party lands. The Electricity Act also authorizes electricity distributors to locate assets on, over or under public streets and highways.

(e) Regulation of LDC

(i) Legislative Framework

The Electricity Act and the OEB Act provide the broad legislative framework for the Province's electricity market.

The Electricity Act restructured the Province's electricity industry. Under the Electricity Act, the former Ontario Hydro was reorganized into five separate corporations (listed below under their current names):

- OPG, the entity responsible for the former Ontario Hydro's generation business;
- Hydro One, the entity responsible for the former Ontario Hydro's electricity transmission, distribution and energy services businesses;
- OEFC, the entity responsible for managing and retiring the former Ontario Hydro's outstanding indebtedness and remaining liabilities;
- IESO, a non-profit corporation responsible for central market operations; and
- Electrical Safety Authority, a non-profit corporation responsible for the electric installation inspection function.

Additionally, the Electricity Act requires electricity distributors in the Province to keep their distribution businesses separate from their other businesses.

The OEB Act expanded the jurisdiction and mandate of the OEB to include regulation of the non-competitive electricity market in addition to the natural gas markets. 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, and transmission rates charged by Hydro One and other transmitters.

In 2004, the Electricity Restructuring Act established the OPA, as a non-profit, self-financed organization with the mandate to ensure long-term electricity supply adequacy in the Province. The OPA is authorized and has the responsibility to implement an integrated power system supply plan and to deliver CDM programs in the Province.

The Energy Consumer Protection Act came into force on January 1, 2011. The Energy Consumer Protection Act amends several statutes, including the OEB Act, the Electricity Act, the Consumer Protection Act and the

Residential Tenancies Act. The Energy Consumer Protection Act also enables and sets out the requirements relating to LDC's installation of Unit Smart Meters in multi-unit complexes and provides new rules regarding the manner in which energy consumers are to be billed for their electricity consumption.

(ii) *Licences*

Distribution Licence

The OEB has granted LDC a distribution licence. The term of the current licence is until October 16, 2023. The licence allows LDC to own and operate an electricity distribution system in the City. Among other things, the licence provides that LDC may not carry on any business activity, other than the distribution of electricity, except through affiliated companies, may not impose charges for the distribution of electricity except in accordance with distribution rate orders approved by the OEB and must comply with industry codes established by the OEB. In addition to the distribution of electricity, under the terms of the Electricity Restructuring Act and the Green Energy Act, electricity distributors are also permitted to provide additional services related to the promotion of CDM activities and alternative, clean and renewable sources of energy.

Electricity Retailer Licence

On March 7, 2000, the OEB issued an electricity retailer licence to TH Energy. This licence was most recently renewed on May 5, 2010 and terminates on May 4, 2015, although the term may be unilaterally extended by the OEB. The licence allows TH Energy to retail electricity subject to the terms and conditions contained in the licence. Apart from certain bill consolidation and settlement services provided under contract to the City, TH Energy does not currently engage in electricity retailing.

Electricity Generation Licence

On December 18, 2002, the OEB issued an electricity generation licence to TH Energy and TREC Windpower Co-operative (No.1) Incorporated (the co-venturers), in connection with a wind turbine located at Exhibition Place in the City. The licence allows the co-venturers to generate electricity or provide ancillary services for sale through the IESO-administered markets, or directly to another person, subject to certain terms and conditions. This licence terminates on December 17, 2022, although the term may be extended by the OEB.

Smart Sub-Metering Licence

On July 7, 2010, LDC applied to the OEB for a Smart Sub-Metering Licence, which would allow LDC to conduct smart sub-metering activities as defined under the OEB's Smart Sub-Metering Code. LDC's application for the Smart Sub-Metering Licence stems from various OEB code requirements that it may be subject to should it ever acquire the metering business of another licensed smart sub-metering provider. The application is currently being reviewed by the OEB.

(iii) *Industry Codes*

The OEB has established the Affiliate Relationships Code, the Distribution System Code, the Retail Settlement Code, the Standard Supply Service Code, and the Conservation and Demand Management Code. These codes prescribe minimum standards of conduct, as well as standards of service, for electricity distributors in the non-competitive electricity market, and have been assigned the following ranking in the event there is a conflict between them:

- (1) Affiliate Relationships Code;
- (2) Distribution System Code;
- (3) Retail Settlement Code;
- (4) Standard Supply Service Code; and
- (5) Conservation and Demand Management Code.

These codes are summarized below.

Affiliate Relationships Code

The Affiliate Relationships Code establishes standards and conditions for the interaction between electricity distributors and their affiliated companies. It is intended to minimize the potential for an electricity distributor to cross-subsidize competitive or non-monopoly activities, protect the confidentiality of consumer information collected by an electricity distributor, and ensure that there is no preferential access to regulated services. The Affiliate Relationships Code prescribes standards of conduct for an electricity distributor with respect to the following: the degree of separation from affiliates; sharing of services and resources; transfer pricing; financial transactions with affiliates; equal access to services; and confidentiality of customer information.

Distribution System Code

The Distribution System Code establishes the minimum conditions that an electricity distributor must meet in carrying out its obligations to distribute electricity under its licence and under the Energy Competition Act, and has been amended as the regulatory environment has evolved. Generally, the Distribution System Code prescribes the rights and responsibilities of electricity distributors and electricity distribution customers with respect to the following: connections; connection agreements and conditions of service; expansion projects; alternative bids (available to customers for work otherwise done by an electricity distributor); metering; operations; disconnection and security deposits; and other matters.

Retail Settlement Code

The Retail Settlement Code outlines the obligations of an electricity distributor with respect to its relationship with retail market participants and its role as a retail market settlements administrator. Under the terms of the Retail Settlement Code, an electricity distributor is required to do the following: unbundle the costs of competitive electricity services and non-competitive electricity services; record, in variance accounts, the difference between amounts billed by the IESO to the electricity distributor for competitive and non-competitive electricity services, and the aggregate amounts billed by the electricity distributor to consumers, retailers and others for the same services; and provide electricity billing and settlement services to retailers and customers.

Standard Supply Service Code

The Standard Supply Service Code requires an electricity distributor to act as a default supplier and provide Standard Supply Service to persons connected to the electricity distributor's distribution system. The Standard Supply Service Code also specifies the conditions and manner by which OEB approved Standard Supply Service rates are to be charged to customers. Under the Standard Supply Service Code, an electricity distributor's rates for Standard Supply Service must be approved by the OEB and must consist of the price of electricity and an administrative charge that will allow the electricity distributor to cover its costs of providing the service.

Conservation and Demand Management Code

The Conservation Demand Management Code sets out the obligations and requirements that licensed electricity distributors must comply with in relation to CDM targets as set out in their licences, as well as the operational framework for electricity distributor-operated CDM activities. The Conservation and Demand Management Code also sets out the conditions and rules that licensed electricity distributors are required to follow if they choose to use OEB approved CDM programs to meet their CDM targets.

(f) Distribution Rates

(i) Rate Setting Mechanism

Pursuant to Section 78 of the OEB Act, the OEB is mandated to regulate the electricity distribution rates charged by electricity distributors. Generally, an electricity distributor's rates are set by way of either a Cost of Service or Incentive Regulation Mechanism framework.

A Cost of Service application requires a detailed examination of evidence and an assessment of the costs incurred by an electricity distributor to provide service, including: capital costs and cost rates for equity and debt; PILs payments; amortization costs; operations, maintenance, and administrative costs; and cost of service offsets in the form of revenues from sources other than electricity distribution rates. The electricity distributor's rates are calculated to recover the total amount of all costs less revenue from other sources, as determined by the OEB, required to provide service to its customers.

The Incentive Regulation Mechanism framework provides for an annual adjustment to an electricity distributor's rates based on a formulaic calculation with no direct examination of evidence regarding the electricity distributor's actual costs and infrastructure needs. The Incentive Regulation Mechanism rate setting plan runs on a four year cycle, with a Cost of Service rate application known as a "rebasement application" serving as the starting point for three subsequent annual rate changes determined through the Incentive Regulation Mechanism adjustment process.

The OEB's current 3rd Generation version of Incentive Regulation Mechanism allows electricity distributors to adjust their rates by the difference between the inflation factor (as determined by Statistics Canada) and the sum of a deemed productivity factor of 0.72% (representing the expected annual electricity distributor productivity gain) and a stretch factor of 0.2%, 0.4% or 0.6% (representing an additional productivity target determined by benchmarked electricity distributor performance).

The Incremental Capital Module is a component of the Incentive Regulation Mechanism process which is designed to address incremental capital needs that electricity distributors may experience, in between rebasing years, during the Incentive Regulation Mechanism term. The OEB determines actual capital amounts that an electricity distributor can receive funding for under the Incremental Capital Module by applying a combination of criteria.

See section 5.2 under the heading "Rate Applications" for more information on LDC's rate applications.

(ii) Other Regulated Charges

The OEB's 2006 Rate Handbook provides standard rates and guidelines to electricity distributors with respect to other regulated charges that are non-competitive in nature, required under OEB codes and guidelines, governed by the market rules or are under the direction of the Province, including transmission charges and retail service charges relating to services provided by electricity distributors to electricity retailers in accordance with the Retail Settlement Code.

4.4 Toronto Hydro Energy Services Inc.

TH Energy is a professional energy services company with two employees (its President and Chief Financial Officer) and \$65.2 million of Capital Assets, as at December 31, 2011. Until January 1, 2012, TH Energy owned and operated all of the street lighting assets located in the City and had the sole right to provide maintenance and capital improvements to the street lighting systems throughout the City until 2035, which services were sub-contracted to LDC. Effective January 1, 2012, TH Energy transferred a portion of its street lighting assets to LDC. TH Energy continues to provide street lighting system maintenance and capital improvement services to the City, and such services continue to be sub-contracted to LDC. See section 5.3 under the heading "Street Lighting Activities" for more information on the transfer of street lighting assets from TH Energy to LDC.

TH Energy also provides consolidated billing services to the City, which services are sub-contracted to LDC, and operates a wind turbine located at the Better Living Centre (Exhibition Place) in a joint venture with TREC Windpower Cooperative (No.1) Incorporated.

4.5 Environmental Matters

(a) Environmental Protection Requirements

Toronto Hydro is subject to extensive federal, provincial and local regulation relating to the protection of the environment. The principal federal legislation is the Canadian Environmental Protection Act that regulates the use, import, export and storage of toxic substances, including PCBs and ozone-depleting substances. Toronto Hydro is also subject to the federal Transportation of Dangerous Goods Act which prescribes safety standards and requirements for the handling and transportation of hazardous goods including PCBs, and sets reporting, training and inspection requirements relating thereto.

The principal provincial legislation is the Environmental Protection Act, which regulates releases and spills of contaminants, including PCBs, ozone-depleting substances and other halocarbons, contaminated sites, waste management, and the monitoring and reporting of airborne contaminant discharge. The provincial Technical Standards and Safety Act also applies to Toronto Hydro's operations with respect to the handling of and training related to compressed gas, propane and liquid fuels. The provincial Fire Protection and Prevention Act requires Toronto Hydro to incorporate procedures and training for dealing with any spills of flammable or combustible liquids. The provincial Dangerous Goods Transportation Act prescribes safety standards and requirements for the transportation of dangerous goods on provincial highways and sets out inspection requirements related thereto.

Finally, municipal by-laws regulate discharges of industrial sewage and storm water run-off to the municipal sewer system and the reporting of the release of certain toxic substances into the atmosphere.

(b) Financial and Operational Effects of Environmental Protection Requirements

In 2011, LDC spent approximately \$0.5 million to meet environmental protection requirements. These costs are not anticipated to significantly increase for future years, and do not currently have a material impact on the Corporation's financial and operational results.

The Corporation recognizes a liability for the future environmental remediation of certain properties and for future removal and handling costs for contamination in electricity distribution equipment in service and in storage. The liability is recognized when the asset retirement obligation is incurred and when the fair value is determined. As at December 31, 2011, the Corporation's asset retirement obligations amounted to \$4.9 million. See note 3(n) and note 14 to the Consolidated Financial Statements.

(c) Environmental Policy and Oversight

Toronto Hydro's Environmental Policy establishes specific commitments to continuously monitor and improve Toronto Hydro's management of environmental protection requirements. The Environmental Policy is monitored and administered by LDC's Vice-President, Organizational Effectiveness, Environment, Health and Safety and its implementation is overseen by LDC's Environmental, Health and Safety department. The content and compliance with the Environmental Policy is reviewed annually by the Board. Pursuant to this annual review, the Board approved a revision to the Environmental Policy on November 22, 2011 in order to align the policy with the requirements of ISO 14001, an international environmental standard.

Under the direction of LDC's Vice-President, Organizational Effectiveness, Environment, Health and Safety, LDC has also established various programs designed to identify and manage environmental impacts associated with the distribution of electricity and to aid in the improvement of environmental performance. LDC's environmental programs include: Total Recycled Waste Program (i.e., copper, aluminum, sundry nonferrous, steel); PCB Cable Disposal Program; Spill Response; Waste Management Program (i.e., oils, gas etc.); and Recycling and Conservation at Work Program (i.e., paper, office blue bin). LDC's environmental programs are administered by

LDC's Environmental, Health and Safety department, and quarterly updates are presented to the Board regarding current environmental risks, mitigation strategies and other material environmental matters.

4.6 Additional Information Regarding Toronto Hydro

(a) Employees

At December 31, 2011, Toronto Hydro had approximately 1,800 employees, all of whom were employed by LDC except for two employees who were employed by the Corporation (its CEO and CFO) and two employees who were employed by TH Energy (its President and Chief Financial Officer). Included in Toronto Hydro's employees are 1,194 members of bargaining units represented by the Canadian Union of Public Employees, Local One ("CUPE One"), and 59 engineers represented by the Society of Energy Professionals. Following the implementation of the restructuring program referenced in section 5.2(d) under the heading "2012-2014 Rate Application", Toronto Hydro had approximately 1,600 employees as at March 29, 2012.

On December 22, 2008, CUPE One ratified collective agreements governing inside and outside employees for a five-year period expiring January 31, 2014. The collective agreements implemented a wage increase of 3.0% on December 22, 2008 and provide for general wage increases of 3.0%, effective on each of February 1, 2010, 2011, 2012 and 2013, respectively. The collective agreements also contain cost of living escalator clauses that provide for wage adjustments corresponding to the percentage change in the Consumer Price Index. The escalator clauses only become effective if certain prescribed thresholds are exceeded.

On July 1, 2007, the Society of Energy Professionals ratified a new collective agreement for a 4.5-year period expiring December 31, 2011. The collective agreement implemented wage increases of 1.75% retroactive to January 1, 2007, 2.50% effective January 1, 2008 and 2.75% effective January 1, 2009, January 1, 2010 and January 1, 2011, respectively. LDC is currently in negotiations with the Society of Energy Professionals to reach a new collective agreement.

Full time employees of Toronto Hydro participate in the OMERS pension plan. Plan benefits are determined on a formula based on the highest 5-year average contributory earnings and years of service with an offset for Canada Pension Plan benefits and are indexed to increases in the Consumer Price Index, subject to an annual maximum of 6%. Any increase in the Consumer Price Index above 6% per year is carried forward for later years. Both participating employers and participating employees are required to make plan contributions based on participating employees' contributory earnings. All obligations to make payments to retirees under the OMERS pension plan are the responsibility of OMERS.

In addition to OMERS, Toronto Hydro provides other retirement and post-employment benefits to employees, including medical, dental and life insurance benefits. See note 3(m) and note 12 to the Consolidated Financial Statements.

(b) Specialized Skills and Knowledge

Trades and technical jobs play a critical role in the safe and reliable design, construction and maintenance of LDC's electricity distribution system. These jobs include overhead and underground trades as well as designers and engineers. LDC hires experienced workers when available, along with apprentices to trades and technical positions. Trade apprentices require up to 54 months to become fully competent and capable of performing all aspects of their job. LDC provides internal trades related, legislative and compliance training through its apprenticeship program.

(c) Health and Safety

Toronto Hydro has established various health and safety programs including safe work practices, accident investigation and safety performance management. LDC has reduced lost time accident frequencies from 0.30 hours per 200,000 hours worked in 2009 to 0.16 hours per 200,000 hours worked in 2011. Toronto Hydro's safety programs are reviewed and updated periodically by the Health and Safety Committee of the Board.

(d) Code of Business Conduct

All employees, officers and directors of Toronto Hydro are required to comply with the principles set out in the Code of Business Conduct, which was implemented by Toronto Hydro in 2004. The Code provides for the appointment of an Ethics and Compliance Officer and establishes a direct hotline to the Ethics and Compliance Officer by which perceived violations of the principles set out in the Code may be reported, anonymously or otherwise. The Ethics and Compliance Officer reports quarterly to the Audit Committee of the Board on the nature of complaints received including those related to audit and accounting matters. Where the complaint involves the conduct of a director or officer of the Corporation, the Ethics and Compliance Officer is required to report it to the Chair of the Audit Committee, who oversees the investigation of that complaint. A copy of Toronto Hydro's Code of Business Conduct is available on the SEDAR website at www.sedar.com.

(e) Insurance

Toronto Hydro's current insurance policies provide coverage for a variety of losses and expenses which might arise from time to time, including comprehensive general liability, all risk property and boiler and machinery insurance, covering loss or damage on certain physical assets, liabilities of directors and officers and automobile liability. The Corporation believes that the coverage, amounts and terms of its insurance arrangements are consistent with prudent Canadian industry practice.

(f) Lending and Investments

Toronto Hydro's lending and investment activities are governed by the terms of the Shareholder Direction and by the terms of the Corporation's Treasury Policy. The Corporation's Treasury Policy was adopted by the Board, is administered by LDC's Treasury Department and overseen by the Corporation's CFO. The primary objective of the Treasury Policy is the implementation of appropriate and effective short-term cash management, investment and borrowing strategies required to manage all corporate funds and related financial risks. The Treasury Policy includes specific operational rules, procedures and benchmarks relating to cash management, liquidity, investments, foreign exchange hedging, borrowing of funds, interest rate risk management, investor relations and corporate debt financing.

(g) Intangible Property

The Corporation owns various intangible assets, such as computer software systems used in the course of business, and intellectual property, including the "Toronto Hydro" brand name and the trademark Toronto Hydro star logo. The Corporation also owns the trademarks peakSAVER[®], POWERSHIFT[®] and PEAKSAVER PLUS[™]. The trademarks peakSAVER[®] and PEAKSAVER PLUS[™] have been licensed by the Corporation to the OPA and sub-licensed to various electricity distributors in the Province for the promotion of a province-wide demand response CDM program.

(h) Seasonal Effects

The Corporation's financial results are impacted by changes in revenues resulting from variations in seasonal weather conditions, the fluctuations in electricity prices, and the timing and recognition of regulatory decisions. The Corporation's revenues tend to be higher in the first and third quarters of a year as a result of higher energy consumption for winter heating in the first quarter and air conditioning and cooling in the third quarter.

PART 5 - GENERAL DEVELOPMENT OF THE BUSINESS

5.1 Business Operations

Over the past three years, the Corporation continued to streamline its business operations to focus on LDC's core businesses of distributing electricity and engaging in CDM activities.

On January 1, 2011, the Corporation amalgamated with one of its wholly-owned subsidiaries, 1455948 Ontario Inc. ("14 Co."). At the time of the amalgamation, 14 Co. did not have any business operations. 14 Co. had been incorporated by the Corporation to operate an equal partnership with a wholly-owned subsidiary of OPG, OPG EBT Holdco Inc. (the "EBT Express Partnership"). The EBT Express Partnership owned an interest in The SPi Group Inc., an electronic clearing house for wholesale and retail electricity transactions. On April 30, 2009, the EBT Express Partnership sold its interest in The SPi Group Inc. to EARTH Corporation for cash consideration of approximately \$5.2 million. The Corporation's share of the sale proceeds from this transaction as it relates to 1455948 Ontario Inc. was approximately \$2.6 million.

5.2 Rate Applications

LDC's electricity distribution rates are typically effective from May 1 to April 30 of the following year. Accordingly, LDC's distribution revenue for the first four months of 2011 was based on the electricity distribution rates approved for the May 1, 2010 to April 30, 2011 rate year (the "2010 Rate Year"), and the distribution revenue for the remainder of 2011 and for the first four months of 2012 are and will be based on electricity distribution rates approved for the May 1, 2011 to April 30, 2012 rate year (the "2011 Rate Year").

The following is an overview of LDC's rate applications from 2009 to date.

(a) 2009 Rate Year

LDC's electricity distribution rates for the 2009 rate year commencing on May 1, 2009 and ending on April 30, 2010 (the "2009 Rate Year") were determined through an application under the Cost of Service framework. On February 24, 2009, the OEB issued its decision regarding LDC's electricity distribution rates for the 2009 Rate Year. The decision provided for a distribution revenue requirement and rate base of \$482.5 million and \$2,035.0 million, respectively. In addition, the decision provided for capital program spending levels and operating, maintenance and administration spending levels of \$240.1 million and \$190.2 million, respectively.

(b) 2010 Rate Year

LDC's electricity distribution rates for the 2010 Rate Year were determined through an application under the Cost of Service framework. On April 9, 2010, the OEB issued its decision regarding LDC's electricity distribution rates for the 2010 Rate Year. The decision provided for a distribution revenue requirement and rate base of \$518.7 million and \$2,140.7 million, respectively. In addition, the decision provided for capital program spending levels and operating, maintenance and administration spending levels of \$350.0 million and \$204.1 million, respectively.

(c) 2011 Rate Year

LDC's electricity distribution rates for the 2011 Rate Year were determined through an application filed under the Cost of Service framework. On July 7, 2011, the OEB issued its decision regarding LDC's electricity distribution rates for the 2011 Rate Year. The decision provided for a distribution revenue requirement and rate base of \$522.0 million and \$2,298.2 million, respectively. In addition, the decision provided for capital program spending levels and operating, maintenance and administration spending levels of \$378.8 million and \$238.0 million, respectively.

(d) 2012-2014 Rate Application

On August 26, 2011, LDC filed a rate application, following the Cost of Service framework, with the OEB seeking approval of separate and successive revenue requirements and corresponding electricity distribution rates for three rate years commencing on May 1, 2012, May 1, 2013 and May 1, 2014 (the "2012-2014 Rate Application"). The requested distribution revenue requirements for these rate years were \$571.4 million, \$639.5 million, and \$712.8 million, respectively, and the expected rate bases for these rate years were \$2,636.3 million, \$3,053.5 million, and \$3,503.2 million, respectively.

Pursuant to the Incentive Regulation Mechanism framework, the OEB established, as a preliminary issue in the 2012-2014 Rate Application, that it would consider the question of whether the application filed by LDC was acceptable or whether it should be dismissed (the "Preliminary Issue"). In particular, the OEB established that in order for it to find that LDC's 2012-2014 Rate Application was acceptable, LDC would be required to show why and how LDC cannot adequately manage its resources and financial needs under the Incentive Regulation Mechanism framework.

LDC filed evidence supporting its position for electricity distribution rates to be set under the Cost of Service framework as part of its 2012-2014 Rate Application. In particular, LDC provided evidence that it cannot adequately manage its resources and financial needs under the Incentive Regulation Mechanism framework. The OEB established a process by which a portion of LDC's evidence was tested during an oral hearing held in November 2011.

On January 5, 2012, the OEB rendered its decision on the Preliminary Issue and dismissed LDC's Cost of Service 2012-2014 Rate Application. In its decision, the OEB found that LDC was not permitted to deviate from the standard Incentive Regulation Mechanism framework cycle, and LDC will therefore be required to file its request for electricity distribution rates commencing on May 1, 2012 pursuant to the formulaic adjustment provided for under the Incentive Regulation Mechanism framework.

On January 25, 2012, LDC filed with the OEB a motion to review the OEB's January 5, 2012 decision.

On February 6, 2012, LDC filed a notice of appeal with the Ontario Divisional Court regarding the OEB's January 5, 2012 decision.

Pursuant to the OEB's decision of January 5, 2012, LDC is currently preparing an application for electricity distribution rates using the 3rd Generation Incentive Regulation Mechanism framework including the filing of an Incremental Capital Module. The quantum of this application is consistent with the capital program spending levels previously approved by the OEB for the 2011 Rate Year.

Under the 3rd Generation Incentive Regulation Mechanism framework, LDC has to significantly reduce its costs structure, and in particular its operating expenses, in order to meet its financial obligations. Accordingly, in the first quarter of 2012, LDC began implementing a restructuring program aimed at reducing its operating costs in the future. The main component of this restructuring program is a workforce reduction plan targeting both union and management employees. As at the date of this AIF, the costs incurred as a result of the restructuring program amounted to approximately \$19.3 million, which were mainly related to employee severance and buy-out payments.

The Corporation continues to assess all of the impacts related to the imposition by the OEB of the 3rd Generation Incentive Regulation Mechanism framework, which impacts may include additional restructuring costs. The incremental restructuring costs could have a material impact on the Corporation's consolidated financial statements in the future.

5.3 Street Lighting Activities

On June 15, 2009, the Corporation filed an application with the OEB seeking an electricity distribution licence for a new wholly-owned legal entity to which the Corporation intended to transfer the street lighting assets of TH Energy. Concurrently, the Corporation filed another application with the OEB seeking approval for the merger of LDC and the new legal entity. The main objective of these applications was to transfer the street lighting assets to the regulated electricity distribution activities of LDC to increase the overall safety of the related infrastructure.

On February 11, 2010, the OEB issued its decision in regard to these applications. In its decision, the OEB agreed that, under certain conditions, the treatment of certain types of street lighting assets as regulated assets is justified. The OEB ordered the Corporation to provide a detailed valuation of the street lighting assets and to perform an operational review to determine which street lighting assets could become regulated assets.

The Corporation performed a detailed asset operational review and financial valuation of the street lighting assets, which was submitted to the OEB on January 31, 2011.

On August 3, 2011, the OEB issued its final decision allowing the transfer of a portion of the street lighting assets to the new wholly-owned legal entity, and for LDC to amalgamate with the new legal entity.

On January 1, 2012, the Corporation completed the transfer of street lighting assets to LDC for a purchase price of \$28.5 million, subject to post closing adjustment and transaction costs.

5.4 Conservation and Demand Management

On March 31, 2010, the Minister of Energy and Infrastructure of Ontario, under the guidance of sections 27.1 and 27.2 of the OEB Act, directed the OEB to establish CDM targets to be met by electricity distributors. Accordingly, on November 12, 2010, the OEB amended LDC's distribution licence to require LDC, as a condition of its licence, to achieve 1,304 GWh of energy savings and 286 MW of summer peak demand savings, over the period beginning January 1, 2011 through December 31, 2014.

Effective January 1, 2011, LDC entered into an agreement with the OPA to deliver CDM programs in the amount of approximately \$50.0 million extending from January 1, 2011 to December 31, 2014 (the "Master CDM Program Agreement"). As at December 31, 2011, LDC received approximately \$19.9 million from the OPA for the delivery of CDM programs under the Master CDM Program Agreement. All programs to be delivered under the Master CDM Program Agreement are fully funded and paid in advance by the OPA. These programs are expected to support the achievement of the mandatory CDM targets described above.

On January 10, 2011, LDC filed an application with the OEB seeking an order granting approval of funding for CDM programs specific to its customer base. LDC requested funding for eight specific CDM programs amounting to \$50.7 million. On July 12, 2011, the OEB issued its decision regarding the CDM programs of LDC. In its decision, the OEB approved with modifications two of the eight programs for a total funding of \$5.3 million. The modifications directed by the OEB included changes to the term and nature of those two programs. The OEB did not approve the other six programs as it considered them to be duplicative of existing CDM programs already funded by the OPA.

On August 3, 2011, LDC filed a letter with the OEB informing it that, due to the modified terms and nature of the two approved programs, LDC's revised economic assessment showed these two programs to be uneconomic and that they would not be implemented. Accordingly, LDC expects to continue to work with the OPA to expand the roster of current CDM programs in order to achieve its mandated CDM targets.

5.5 Contact Voltage

On June 30, 2009, LDC filed an application with the OEB seeking recovery of costs incurred in 2009 for the remediation of safety issues related to contact voltage. LDC sought recovery of \$14.4 million by way of fixed term rate riders of 3 years for the street lighting and unmetered scattered load rate classes, and one year for all other classes.

On December 10, 2009, the OEB issued an initial decision in this proceeding which provided for the recovery of allowable actual expenditures incurred above the amount deemed as controllable expenses in LDC's 2009 approved electricity distribution rates. At the time of the decision, the Corporation estimated the allowable recovery of costs at \$9.1 million.

On October 29, 2010, the OEB issued a second decision in the matter, following further review of costs incurred by LDC. In this decision, the OEB deemed the balance allowable for recovery at \$5.3 million. The variance from the Corporation's original estimate is mainly due to the OEB's interpretation of the definition of controllable expenses used to determine the final allowable recovery. In connection with this decision from the OEB, the Corporation revised its recovery estimate for contact voltage costs, resulting in an increase in operating expenses of \$3.8 million in 2010. On November 18, 2010, LDC filed a motion to review the decision with the OEB seeking an amendment to allow for recovery in accordance with the initial decision rendered on December 10, 2009. On March 25, 2011, the OEB issued its decision on the LDC motion, denying the requested additional recovery.

5.6 OEB PILs Proceeding

The OEB conducted a review of the PILs variances accumulated in regulatory variance accounts for the period from October 1, 2001 to April 30, 2006 for certain MEUs. On June 24, 2011, the OEB issued its decision for these MEUs and provided guidelines for the calculation and further disposition of the balances accumulated in the PILs regulatory variance accounts.

LDC has reviewed the balances of its PILs regulatory variance accounts and applied the guidelines provided by the OEB. As at December 31, 2011, LDC estimated its liability at approximately \$2.8 million. This balance has been recorded in the Corporation's Consolidated Financial Statements. LDC intends to apply for disposition of this balance in 2012. The amount to be approved by the OEB will be based on the OEB's interpretation and application of its guidelines and the final balance which is yet to be approved by the OEB could differ materially from LDC's estimation of its liability. See note 22(b) to the Consolidated Financial Statements.

5.7 Accounting Standards

Publicly accountable enterprises in Canada were required to adopt IFRS in place of Canadian GAAP for interim and annual reporting purposes for fiscal years beginning on or after January 1, 2011. On September 10, 2010, the Canadian Accounting Standards Board granted an optional one-year deferral for IFRS adoption for entities subject to rate regulation.

The Corporation elected to take the optional one-year deferral of its adoption of IFRS. The Corporation therefore continued to prepare its consolidated financial statements in accordance with Canadian GAAP accounting standards in Part V of the Canadian Institute of Chartered Accountants Handbook in 2011.

In 2011, the Corporation decided to evaluate the option of adopting US GAAP effective January 1, 2012 as an alternative to IFRS. On July 8, 2011, the Corporation filed an application with the applicable Canadian securities regulatory authorities to permit the Corporation to prepare its consolidated financial statements in accordance with US GAAP without qualifying as a US Securities and Exchange Commission issuer.

On July 21, 2011, the Canadian securities regulatory authorities issued a decision which gave the Corporation the option to prepare its consolidated financial statements in accordance with US GAAP for its fiscal years beginning

on or after January 1, 2012 but before January 1, 2015. The decision is similar to that obtained by other Canadian rate-regulated utilities.

On August 19, 2011, LDC filed a letter with the OEB stating its intention to adopt US GAAP as the basis for the calculation of electricity distribution rates starting in 2012 in accordance with the guidelines provided by the OEB. In the OEB guidelines, the OEB indicated to the Province's electricity distributors that it would permit the use of US GAAP for the calculation of electricity distribution rates if such electricity distributors receive approval from the Ontario Securities Commission and if it benefits electricity distribution consumers.

On August 26, 2011, the Board approved the adoption of US GAAP for financial reporting purposes for the year beginning on January 1, 2012. The Corporation plans to commence reporting under US GAAP in its first quarterly consolidated financial statements in 2012.

The Corporation does not believe that the adoption of US GAAP will have a material impact on its consolidated financial statements. See section 8.14 under the heading "Conversion to US GAAP" for more information.

PART 6 - RELATIONSHIP WITH THE CITY

6.1 Shareholder Direction

As sole shareholder of the Corporation, the City has adopted the Shareholder Direction that sets out the following corporate governance principles with respect to Toronto Hydro:

- the objectives of the City in connection with its relationship with Toronto Hydro;
- the principles that govern the operations of Toronto Hydro;
- the matters in addition to those set out in the OBCA that require the approval of the City as the sole shareholder of Toronto Hydro; and
- certain financial and administrative arrangements between the Corporation and the City.

(a) Shareholder Objectives

The City's objectives in connection with its relationship with Toronto Hydro are as follows:

- the value of Toronto Hydro should be maintained or increased;
- the City's income stream from Toronto Hydro should be comparable to the City's estimated financial benefit if Toronto Hydro had been sold as a going concern;
- Toronto Hydro's consumers should not be unduly impacted by the transfer of assets from the City and the Toronto Hydro-Electric Commission to Toronto Hydro; and
- the environmental impacts related to Toronto Hydro should be improved.

(b) Principles Governing Operations

The Shareholder Direction states that the business of Toronto Hydro is integral to the well being and the infrastructure of the City and provides, among other things, that it is in the best interests of Toronto Hydro and the stakeholders affected by its business that Toronto Hydro conducts its affairs:

- on a commercially prudent basis, while engaging in recruitment practices designed to attract employees from the diverse community it serves and supporting the City's objectives where consistent with Toronto Hydro's business objectives, including procurement practices that encourage participation of equity-seeking groups, in a manner consistent with the energy policies

established by the City from time to time, in a socially responsible manner that supports priority objectives of the City that are consistent with Toronto Hydro's business objectives and in accordance with the financial performance objectives of the City;

- to provide a reliable and efficient electricity distribution system that meets changing demand utilizing emerging green technologies as appropriate with an emphasis on customer satisfaction;
- in a safe and environmentally responsible manner while working with the City to achieve its climate change objectives; and
- in a manner that promotes energy conservation and environmental responsibility, works with the City to achieve its climate change objectives, keeps its property and facilities clean and well maintained and free from graffiti and protects and enhances the City's urban forest.

The Shareholder Direction provides that the Board is responsible for determining and implementing the appropriate balance among these principles.

(c) Shareholder Approval

In addition to those matters set out in the OBCA, the following matters, among others, require the approval of the City as the sole shareholder of the Corporation:

- subject to certain exceptions in the case of LDC, creating any security over the assets of the Corporation or LDC;
- in the case of LDC, providing any financial assistance to any person other than in accordance with the Shareholder Direction;
- in the case of the Corporation and LDC, making any investment in or providing any financial assistance to any subsidiary of the Corporation (other than LDC), other than trade payables incurred in the ordinary course of business on customary terms and an investment in or financial assistance to a subsidiary that originally was an investment in or financial assistance to LDC, in excess of 12% of the shareholder's equity of LDC as shown in its most recent financial statements; and
- acquiring any interest in the electricity distribution system, undertaking or securities of a distributor operating outside the City unless, among other things, the acquisition does not adversely affect the dividend payable to the City and there is no dilution of the City's shareholding in the Corporation.

The City has authorized the Corporation to provide up to \$500.0 million in financial support with respect to prudential requirements and as security for obligations under third-party contracts. See note 17 to the Consolidated Financial Statements.

(d) Financial Performance

The Shareholder Direction provides that the Board will use its best efforts to ensure that Toronto Hydro meets certain financial performance standards, including those relating to credit rating and dividends.

(e) Credit Rating

The Shareholder Direction provides that the Corporation will obtain and maintain a rating of A minus or higher as defined by S&P on its senior debt securities.

(f) Dividends

Subject to applicable law, the Shareholder Direction provides that the Corporation will pay dividends to the City each year equal to the greater of \$25.0 million or 50% of the Corporation's consolidated net income for the year. The dividends are not cumulative and are payable as follows:

- \$6.0 million on the last day of each of the first three fiscal quarters during the year;
- \$7.0 million on the last day of the fiscal year; and
- the amount (if any) by which 50% of Corporation's annual consolidated net income for the year exceeds \$25.0 million, within ten days after the Board approves the Corporation's consolidated financial statements for the year.

The Corporation declared and paid dividends to the City totalling \$25.2 million in 2009, \$25.0 million in 2010, and \$33.1 million in 2011. See note 19 and note 25(d) to the Consolidated Financial Statements.

On March 2, 2012, the Corporation declared dividends in the amount of \$29.0 million. The dividends are comprised of \$23.0 million with respect to net income for the year ended December 31, 2011, payable to the City on March 12, 2012 and \$6.0 million with respect to the first quarter of 2012, payable to the City on March 30, 2012.

LDC declared and paid dividends to the Corporation amounting to, \$nil in 2009, \$nil in 2010, and \$nil in 2011.

TH Energy declared and paid dividends to the Corporation amounting to \$nil in 2009, \$19.6 million in 2010 and \$nil in 2011.

6.2 Indebtedness to the City

On April 1, 2010, the City monetized its interest in the Amended and Restated City Note under which the Corporation had \$490.1 million of indebtedness outstanding to the City. The Amended and Restated City Note represented the Corporation's remaining indebtedness to the City in consideration for the transfer of \$980.2 million of electricity distribution system assets by the Toronto Hydro-Electric Commission and the City to LDC upon initial formation of Toronto Hydro on July 1, 1999.

The Amended and Restated City Note was converted, in accordance with its terms, into two series of debentures of the Corporation ("Series 4" and "Series 5") on April 1, 2010. The Corporation did not receive any proceeds from the offering of the Series 4 and Series 5 debentures. Following the completion of the offering of the Series 4 and Series 5 debentures, the Amended and Restated City Note has been cancelled and the Corporation has no further indebtedness outstanding to the City under the terms of the Amended and Restated City Note.

As at the date of this AIF, the Corporation has no further indebtedness outstanding to the City.

6.3 Services Provided to the City

Toronto Hydro provides certain services to the City at commercial and regulated rates, including consolidated electricity billing services and street lighting maintenance services provided by TH Energy and sub-contracted to LDC. See section 4.4 under the heading "Toronto Hydro Energy Services Inc." for more information. See note 20 to the Consolidated Financial Statements.

PART 7 - TAXATION

7.1 Tax Regime

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 and the CTA.

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 an MEU that is exempt from tax under the ITA, the CTA and the TA is required to make, for each taxation year, a PILs payment to the OEFC in an amount equal to the tax that it would be liable to pay under the ITA and the TA (for years ending after 2008) or the CTA (for years ending prior to 2009) 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.

If the Corporation or a subsidiary ceases to be exempt from tax under the ITA, the TA and the CTA, it will become subject to tax under those statutes, will no longer be required to make PILs payments to the OEFC, and will be deemed to have disposed of its assets for proceeds of disposition equal to their fair market value at that time and to have reacquired its assets at the same amount with the result that:

- such corporation would become liable to make a PILs payment in respect of any income or gains arising as a result of these deemed dispositions; and
- the amount of annual taxes payable by the corporation under the ITA, the TA and the CTA may be different from the PILs payment that would be payable without a loss of tax-exempt status to reflect, among other things, the consequences of these deemed dispositions and acquisitions.

The Electricity Act also provides that a municipal corporation or an MEU is required to pay a transfer tax when it transfers Electricity Property. An interest in Electricity Property includes any interest in a corporation, partnership or other entity that derives its value in whole or in part from Electricity Property. The transfer tax is the prescribed percentage (currently 33%) of the fair market value of the interest transferred. The amount of transfer tax payable where the interest that is transferred is an interest in a corporation, partnership or other entity, is calculated in accordance with a special rule. The amount of transfer tax payable by an MEU on a transfer of Electricity Property may be reduced by:

- any PILs payment made by the MEU in respect of the part of the taxation year up to and including the date that the transfer takes place or a previous taxation year;
- any amount that the MEU has paid as tax under Parts II, II.1 or III of the CTA or Part III of the TA in respect of the part of the taxation year up to and including the date of the transfer or a previous taxation year; and
- any amount that the MEU would be liable to pay under Part I of the ITA in respect of the taxation year if that tax were calculated on the basis that the MEU had no income during the taxation year other than the capital gain, or income under paragraph 14(1)(b) of the ITA in respect of the disposition of eligible capital property, arising on the transfer of the property subject to the transfer tax.

Transfers of Electricity Property made to a municipal corporation, an MEU, Hydro One or OPG will generally be an excluded transfer and thereby exempt from the transfer tax.

In addition, a refund of transfer tax will generally be made where such tax had been paid on the sale or transfer of Electricity Property and where the proceeds of that transfer were reinvested in certain other capital or depreciable assets used in electricity activity and, subject to certain deeming rules, before the end of the second taxation year following the taxation year in which the liability to pay the transfer tax arose.

PILs payments are deductible in computing the transfer tax only to the extent that they have not been previously applied to reduce transfer tax payable by a municipal corporation or an MEU.

7.2 PILs Recoveries through Rates

The 2006 Rate Handbook provides for electricity distribution rate adjustments to permit recoveries relating to PILs payments. These recoveries are recalculated and submitted for recovery by LDC in each Cost of Service or rebasing distribution rate application. LDC is also generally at risk for variances between forecasted and actual PILs paid, excluding variances arising from changes in tax rates not assumed in the setting of rates for the period in question, which variances are disposed of through deferral accounts under both a Cost of Service or Incentive Regulation Mechanism. See note 7(h) and 22(b) to the Consolidated Financial Statements.

7.3 Tax Contingencies

The Ministry of Finance has issued assessments in respect of payments in lieu of additional municipal and school taxes under section 92 of the Electricity Act that are in excess of the amounts LDC believes are payable. The dispute arose as a result of inaccurate information incorporated into Ontario Regulation 224/00. The Corporation has worked with the Ministry of Finance to resolve this issue, and as a result the Ministry of Finance issued Ontario Regulation 423/11 on August 31, 2011. The new regulation revoked Ontario Regulation 224/00 and corrected inaccurate information retroactively to 1999.

The balance assessed by the Ministry of Finance on its most recent statement of account amounts to approximately \$10.0 million above the balance accrued by the Corporation. While the Corporation expects that reassessments will be issued as a consequence of the change in regulation, there can be no assurance that the Corporation will not have to pay the full assessed balance in the future.

PART 8 - RISK FACTORS

Toronto Hydro's business is subject to a variety of risks including those described below:

8.1 Condition of Distribution Assets

LDC estimates that approximately one-third of its electricity distribution assets are past their expected useful life. 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 OEB allowing recovery of costs in respect of LDC's maintenance program and capital expenditure requirements for distribution plant refurbishment and replacement.

8.2 Regulatory Developments

Ontario's electricity industry regulatory developments and policy changes 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 in its ability to provide reliable service to its customers. In particular, there can be no assurance that:

- the OEB will approve LDC's electricity distribution rates under the Incentive Regulation Mechanism framework, including the Incremental Capital Module, at levels that will permit LDC to carry out its planned capital work programs required to maintain reliable service to its customers and earn the allowed rate of return on the investment in the business;
- 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 licenced 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.

Changes to any of the laws, rules, regulations and policies applicable to the businesses carried on by Toronto Hydro could also have a significant impact on Toronto Hydro. There can be no assurance that Toronto Hydro will be able to comply with applicable future laws, rules, regulations and policies. Failure by Toronto Hydro to comply with applicable laws, rules, regulations and policies may subject Toronto Hydro to civil or regulatory proceedings that may have a material adverse effect on Toronto Hydro.

8.3 Information Technology Infrastructure

LDC'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, financial and billing systems and business systems to capture data and to produce timely and accurate information. Failures of LDC's financial, business and operating systems could have a material adverse effect on Toronto Hydro's business, operating results, financial condition and prospects.

LDC's electricity distribution infrastructure and technology systems are also potentially vulnerable to damage or interruption from cyber attacks, which could have an adverse impact on Toronto Hydro's operations, financial conditions, brand and reputation. While LDC has implemented protective measures to monitor the risk of a cyber attack and mitigate its effects, there can be no assurance that such protective measures will be completely effective in protecting LDC's electricity distribution infrastructure or assets from a cyber attack or the effects thereof.

8.4 Labour Relations

Toronto Hydro's ability to operate successfully in the electricity industry in the Province will continue to depend in part on its ability to make changes to existing work processes and conditions to adapt to changing circumstances. Toronto Hydro's ability to make such changes, in turn, will continue to depend in part on its relationship with its labour unions and its ability to develop plans and approaches that are acceptable to its labour unions. There can be no assurance that Toronto Hydro will be able to secure the support of its labour unions.

8.5 Natural and Other Unexpected Occurrences

LDC's operations are exposed to the effects of natural and other unexpected occurrences such as severe or unexpected weather conditions, terrorism and pandemics. Although LDC'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 LDC's facilities or interruption of LDC's operations arising from these occurrences could result in lost revenues and repair costs that can be substantial. Although the Corporation has insurance, if it sustained a large uninsured loss caused by natural or other unexpected occurrences, LDC would apply to the OEB for the recovery of the loss. There can be no assurance that the OEB would approve, in whole or in part, such an application.

8.6 Electricity Consumption

LDC's electricity distribution rates are comprised of a fixed charge and a usage-based (consumption) charge. The volume of electricity consumed by LDC's customers during any period is governed by events largely outside LDC's control (e.g., principally sustained periods of hot or cold weather could increase the consumption of electricity, sustained periods of mild weather could decrease the consumption of electricity, and general economic conditions could affect overall electricity consumption). Accordingly, there can be no assurance that LDC will earn the revenue requirement approved by the OEB. Economic conditions could also lead to lower overall electricity consumption, particularly in the commercial customer segment, which is estimated to be the most sensitive to economic changes. Lower electricity consumption from commercial customers could negatively impact LDC's revenue.

8.7 Market and Credit Risk

LDC is subject to credit risk with respect to customer non-payment of electricity bills. LDC is permitted to mitigate the risk of customer non-payment using any means permitted by law, including security deposits (including 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. In the event of an actual payment default and a corresponding bad debt expense incurred by LDC, roughly 80% of the expense would be related to commodity and transmission costs and the remainder to LDC's distribution revenue. 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 from remaining customers. 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 is also exposed to fluctuations in interest rates as its regulated rate of return is derived using a formulaic approach, which is based in part on a forecast of long-term Government of Canada bond yields and A-rated Canadian utility bond spreads. LDC estimates that a 1% (100 basis point) reduction in long-term Government of Canada bond yields used to determine its regulated rate of return would reduce LDC's net income, as at December 31, 2011, by approximately \$4.6 million.

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, as at December 31, 2011, by approximately \$33.1 million, and a 1% (100 basis point) decrease in the discount rate would increase the accrued benefit obligation, as at December 31, 2011, by approximately \$42.9 million.

8.8 Additional Debt Financing

Cash generated from operations, after the payment of expected dividends, will not be sufficient to repay Toronto Hydro's existing indebtedness, fund Capital Expenditures and meet other obligations. The Corporation relies on debt financing through its MTN Program or existing credit facilities to repay existing indebtedness and fund Capital Expenditures. The Corporation's ability to arrange sufficient and cost-effective debt financing could be adversely affected by a number of factors, including financial market conditions, the regulatory environment in the Province, the Corporation's results of operations and financial condition, the ratings assigned to the Corporation and its Debentures by credit rating agencies, the current timing of the Corporation's Debentures and general economic conditions. See note 11 to the Consolidated Financial Statements.

8.9 Work Force Renewal

Over the next decade, a significant portion of LDC's employees will become eligible for retirement, including potential retirements occurring in supervisory, trades and technical positions. Accordingly, LDC will be required to attract, train and retain skilled employees. There can be no assurance that LDC will be able to attract and retain the required workforce.

8.10 Insurance

Although Toronto Hydro maintains insurance as described under section 4.6(e) under the heading "Insurance" above, there can be no assurance that Toronto Hydro will be able to obtain or maintain adequate insurance in the future at rates it considers reasonable or that insurance will continue to be available. Further, there can be no assurance that available insurance will cover all losses or liabilities that might arise in the conduct of Toronto Hydro's business. Toronto Hydro self-insures against certain risks (e.g., business interruption and physical damage to certain automobiles). The occurrence of a significant uninsured claim or a claim in excess of the insurance coverage limits maintained by Toronto Hydro could have a material adverse effect on the Corporation's results of operations and financial position.

8.11 Credit Rating

Should the Corporation's credit rating from both credit rating agencies fall below "A (minus)" (S&P) and "A (low)" (DBRS), the Corporation and its subsidiaries may be required to post additional collateral with the IESO.

8.12 Conflicts of Interest

The City owns all of the outstanding shares of the Corporation and has the power to determine the composition of the Board and influence the Corporation's major business and corporate decisions, including its financing programs and dividend payments. A conflict may arise between the City's role as the sole shareholder of the Corporation and its role as the administrator of the City's budget and other matters for the residents of the City.

8.13 Change of Ownership

The City may decide to sell all or part of the Corporation. In the case of such event, depending on the nature of the transaction, the Corporation's credit ratings could be negatively affected.

8.14 Conversion to US GAAP

As noted in section 5.7 under the heading "Accounting Standards", the Corporation plans to commence reporting under US GAAP in its first quarterly consolidated financial statements in 2012. The Corporation does not believe that the adoption of US GAAP will have a material impact on its consolidated financial statements. However, given that the decision granted by the Canadian securities regulatory authorities only allows for the option to prepare consolidated financial statements in accordance with US GAAP for fiscal years beginning before January 1, 2015, and the continued uncertainty around the timing, scope and eventual adoption of a rate regulated accounting ("RRA") standard under IFRS and the potential material impact of RRA on the Corporation's financial statements, if the Corporation were to adopt the use of IFRS for fiscal years beginning on or after January 1, 2015, it may have an impact on the Corporation's future financial position and results of operations, which cannot be reasonably quantified at this time.

8.15 Real Property Rights

Certain terminal stations and municipal sub-stations of LDC are located on lands owned by the Province, the City and others. In some cases, LDC does not have and may not be able to obtain formal access agreements with respect to such facilities. Failure to obtain or maintain access agreements could adversely affect LDC's operations.

8.16 LDC Competition

In the past, there had been one electricity distributor in each region of the Province. Under the current regulatory regime, a person must obtain a licence from the OEB in order to own and operate an electricity distribution system. LDC has the right to distribute electricity in the City. Although the distribution licence specifies the area in which

the electricity distributor is authorized to distribute electricity, unless otherwise provided, the licence does not provide exclusive distribution rights for such area.

The Corporation believes that the complexities and potential inefficiencies that would be created by having multiple electricity distributors authorized to serve a single area are likely to result in the continuation of the practice of having a single electricity distributor authorized to serve a single area. In addition, the Corporation believes that there are significant barriers to entry with respect to the business of electricity distribution in the Province, including the cost of maintaining an electricity distribution system, OEB regulation of electricity distribution rates and the level of regulatory compliance required to operate an electricity distribution system. However, the Corporation recognizes that more than one distribution licence could be issued for the same area and there is a possibility that in the future some business functions or activities could be separated from LDC and made open to competition from non-regulated business entities, or that defined geographical areas within LDC's service area may be electrically supplied by a means other than through LDC's electricity distribution system.

PART 9 - CAPITAL STRUCTURE

9.1 Share Capital

The authorized capital of the Corporation consists of an unlimited number of common shares of which 1,000 common shares are issued and outstanding as at the date of this AIF. The City is the sole shareholder of the Corporation. See note 19 to the Consolidated Financial Statements.

9.2 Debentures

On May 7, 2003, the Corporation issued \$225.0 million 6.11% senior unsecured debentures due May 7, 2013 ("Series 1"). On November 14, 2007, the Corporation issued \$250.0 million 5.15% senior unsecured debentures due November 14, 2017 ("Series 2").

On December 12, 2008, the Corporation filed under its MTN Program a shelf prospectus providing for the issuance of up to \$1.0 billion of debentures during the 25 month period following the date of the shelf prospectus (the "First Shelf Prospectus"). On November 12, 2009, the Corporation issued \$250.0 million 4.49% senior unsecured debentures under the First Shelf Prospectus, due November 12, 2019 ("Series 3").

The net proceeds from the sale of the Series 1, Series 2 and Series 3 debentures were used by the Corporation for general corporate purposes including the repayment of then-existing indebtedness to the City under the terms of the Amended and Restated City Note.

On April 1, 2010, the Amended and Restated City Note was converted, in accordance with its terms, into \$245.0 million 6.11% senior unsecured debentures due December 31, 2011 ("Series 4") and \$245.0 million 6.11% senior unsecured debentures due May 6, 2013 ("Series 5"). The Corporation did not receive any proceeds from the offering of the Series 4 and Series 5 debentures. See section 6.2 under the heading "Indebtedness to the City" for further information.

On May 20, 2010, the Corporation issued \$200.0 million 5.54% senior unsecured debentures due May 21, 2040 ("Series 6"). The net proceeds from the sale of the Series 6 debentures were used principally to finance regulated Capital Expenditures of LDC.

On December 9, 2010, the Corporation filed under its MTN Program a new shelf prospectus providing for the issuance of up to \$1.0 billion of debentures during the 25 month period following the date of the prospectus (the "Second Shelf Prospectus").

On November 18, 2011, the Corporation issued \$300.0 million 3.54% senior unsecured debentures under the Second Shelf Prospectus, due November 18, 2021 ("Series 7"). The net proceeds from the sale of the Series 7 debentures were used to repay the Corporation's Series 4 debentures which matured on December 30, 2011 and the balance is expected to be used for general corporate purposes. See note 11 to the Consolidated Financial Statements.

9.3 Credit Ratings

The Debentures issued under the Corporation's MTN Program are rated "A (high)" by DBRS as at January 20, 2012 and "A" by S&P as at August 30, 2011.

DBRS rates long-term debt instruments by rating categories ranging from a high of "AAA" to a low of "D". A DBRS rating may be modified by the addition of "high" or "low" to indicate relative standing within the major rating categories. The "A" category is characterized as "good credit quality".

S&P rates long-term debt instruments by rating categories ranging from a high of "AAA" to a low of "D". An S&P rating may be modified by the addition of a plus or minus to indicate relative standing within the major rating categories. The "A" category is characterized as somewhat more susceptible to the adverse changes in circumstances and economic conditions as obligations in higher-rated categories. However, the obligor's capacity to meet its financial commitment on the obligation is still strong.

Credit ratings are intended to provide investors with an independent measure of the credit quality of an issue of securities. A rating is not a recommendation to buy, sell or hold securities and may be subject to revision or withdrawal at any time by the rating agency.

The Debentures are not listed, posted for trading or quoted on any stock exchange or quotation system.

The Debentures have been issued under the CDSX book entry system administered by CDS Clearing and Depository Services Inc. ("CDS") with CIBC Mellon Trust Company as trustee. Accordingly, a nominee of CDS is the registered holder of the Debentures and beneficial ownership of the Debentures is evidenced through book entry credits to securities accounts of CDS participants (e.g., banks, trust companies and securities dealers), who act as agents on behalf of beneficial owners who are their customers, rather than by physical certificates representing the Debentures.

PART 10 - DIRECTORS AND OFFICERS

10.1 Nomination of Directors

The Board consists of ten directors, all of whom are appointed by the sole shareholder of the Corporation, the City.

Pursuant to the Shareholder Direction, in electing directors to the Board, the City gives due regard to the qualifications of a candidate, including: experience or knowledge; commercial sensitivity and acumen; independence of judgment; and personal integrity. The City seeks candidates with experience and knowledge in: public utility commissions or boards of major corporations or other commercial enterprises; corporate finance; corporate governance; market development; large system operation and management; urban energy industries; and public policy issues and laws relating to Toronto Hydro, the electricity industry, environmental matters, labour relations and occupational health and safety issues.

10.2 Directors and Officers

The following table sets forth, for each of the directors and officers of the Corporation, the name, province and country of residence, office, principal occupation and, if a director, the date on which the person became a director and when his or her current term as a director is set to expire.

<u>Name ⁽¹⁾ and Residence</u>	<u>Office</u>	<u>Principal Occupation</u>	<u>Director Since</u>	<u>Expiry of Current Term</u>
Clare R. Copeland Ontario, Canada	Director and Chair of the Board of Directors	Chief Executive Officer, Falls Management Company ⁽²⁾	June 23, 1999	November 30, 2012
Patricia Callon Ontario, Canada	Director and Chair- Designate	Director, Stakeholder Outreach & Communications, Canadian Securities Transition Office ⁽³⁾	August 1, 2005	November 30, 2012
Brian Chu Ontario, Canada	Director	Partner, Bogart Robertson & Chu ⁽⁴⁾	August 1, 2005	November 30, 2012
Derek Cowbourne Ontario, Canada	Director	Corporate Director	December 1, 2008	November 30, 2012
Paulette Kennedy Ontario, Canada	Director	Commissioner, Ontario Securities Commission ⁽⁵⁾	December 1, 2008	November 30, 2012
Shoba Khetrupal Ontario, Canada	Director	Corporate Director	December 1, 2008	November 30, 2012
David Williams Ontario, Canada	Director	Corporate Director	March 31, 2010 ⁽⁶⁾	November 30, 2012
Shelley Carroll Ontario, Canada	Director	Councillor, City of Toronto	December 7, 2010	November 30, 2012
Josh Colle Ontario, Canada	Director	Councillor, City of Toronto	December 7, 2010	November 30, 2012
Ron Moeser Ontario, Canada	Director	Councillor, City of Toronto	December 7, 2010 ⁽⁷⁾	November 30, 2012
Anthony Haines Ontario, Canada	President and Chief Executive Officer	President and Chief Executive Officer, Toronto Hydro Corporation	N/A	N/A
Jean-Sebastien Couillard Ontario, Canada	Chief Financial Officer	Chief Financial Officer, Toronto Hydro Corporation	N/A	N/A

Notes:

- (1) No director serves as a director of another reporting issuer except for: (a) Mr. Copeland, who serves as a director of RioCan Real Estate Investment Trust, Danier Leather Inc., Chesswood Income Trust (formerly called Cars4U), Entertainment One Ltd., M.D.C. Holdings, Inc., and Telesat Canada; and (b) Mr. Williams, who serves as director of Shoppers Drug Mart Corporation, lead director of Aastra Technologies Inc., and director of Canadian Apartment Properties Real Estate Investment Trust.
- (2) Falls Management Company is the developer and operator of Casino Niagara and Niagara Fallsview Casino Resort.
- (3) The Canadian Securities Transition Office was established by the Government of Canada in 2009 to lead the transition to a single Canadian securities regulator.
- (4) Bogart, Robertson & Chu is a law firm.
- (5) The Ontario Securities Commission is a regulatory agency which administers and enforces securities legislation in the Province.
- (6) Mr. Williams also served as a director of the Corporation from June 23, 1999 to August 1, 2005.
- (7) Mr. Moeser also served as a director of the Corporation from June 21, 2002 to December 4, 2003.

10.3 Principal Occupations

All of the directors and senior officers of the Corporation have held the principal occupations identified in section 10.2 above with the same or associated companies or organizations for 5 years or more, except for:

- (a) Ms. Callon, who was a Consultant with the Ontario Securities Commission between September 2005 and August 2009;
- (b) Mr. Cowbourne, who held various executive positions with the IESO prior to April 1, 2008;
- (c) Ms. Kennedy, who was the Chief Financial Officer and Chief Auditor of AEGON Canada Inc. prior to January 2008;
- (d) Mr. Colle, who was Manager, Government Relations of Greater Toronto Airports Authority from March 2004 to August 2008, and Associate Vice-President of Bridgepoint Group Ltd. from August 2008 to November 2010; and
- (e) Mr. Haines who was the President of LDC from September 2006 until his appointment as CEO effective October 1, 2009.

10.4 Cease Trade Orders, Bankruptcies, Penalties or Sanctions

Mr. Copeland was a director of White Rose Crafts and Nursery Sales Inc. that filed a voluntary assignment into bankruptcy in June 2002. Mr Copeland resigned from this position in June 2002. Mr. Copeland also sat on the board of directors of Playdium Entertainment Corporation, which filed an application under the Companies' Creditors Arrangement Act (Canada) in February 2001. Mr. Copeland resigned from this position in May 2001. In each instance, Mr Copeland had been asked to join the board when the company was already in difficulty due to his corporate restructuring experience.

Except as noted above, no director or executive officer of the Corporation is, as at the date of this AIF, or has within ten years prior to the date of this AIF:

- (a) been a director, chief executive officer or chief financial officer of any company (including the Corporation) that was the subject of a cease trade or similar order or an order that denied the company access to any exemption under securities legislation for a period of more than 30 consecutive days, where such order was issued while the director or executive officer was acting in the capacity as director, chief executive officer or chief financial officer;
- (b) been a director, chief executive officer or chief financial officer of any company (including the Corporation) that was the subject of a cease trade or similar order or an order that denied the company

access to any exemption under securities legislation for a period of more than 30 consecutive days, where such order was issued after the director or executive officer ceased to be a director, chief executive officer or chief financial officer and which resulted from an event that occurred while that person was acting in the capacity as director, chief executive officer or chief financial officer;

- (c) been a director, chief executive officer or chief financial officer of any company (including the Corporation) that, while that person was acting in that capacity or within a year of that person ceasing to act in that capacity, became bankrupt, made a proposal under any legislation relating to bankruptcy or insolvency or was subject to or instituted any proceedings, arrangement or compromise with creditors or had a receiver, receiver manager or trustee appointed to hold its assets; or
- (d) become bankrupt, made a proposal under any legislation relating to bankruptcy or insolvency or was subject to or instituted any proceedings, arrangement or compromise with creditors or had a receiver, receiver manager or trustee appointed to hold the assets of such director or executive officer.

10.5 Independence

The Board consists of ten directors, all of whom are appointed by the City in its capacity as sole shareholder of the Corporation. Three of the directors are Councillors of the City of Toronto and are not considered independent because of their positions. None of the other directors have a direct or indirect material relationship with the Corporation and are independent within the meaning of applicable Canadian securities law.

No members of management sit on the Board. The Board meets regularly in the absence of management to discuss the management of the Corporation. Under its mandate, the Board is authorized to retain independent legal counsel and other advisors if it considers this appropriate. The mandate also provides that the Board shall have unrestricted access to the officers of the Corporation and is authorized to invite officers and employees of the Corporation and others to attend or participate in its meetings and proceedings if it considers this appropriate.

10.6 Committees of the Board of Directors

The Board has established four standing committees:

(a) Audit Committee

The Audit Committee is responsible for overseeing the adequacy and effectiveness of financial reporting, accounting systems and internal controls. The Audit Committee reviews the Corporation's quarterly and annual financial statements as well as financial statements prepared in connection with securities offerings or required by applicable regulatory authorities, reviews the audit plans of the external auditors, oversees the internal audit of the Corporation, reviews officers' personal expenses on an annual basis and recommends the external auditor for appointment by the Corporation's sole shareholder. Members of the Audit Committee are Mr. Chu, Ms. Kennedy Ms. Khetrpal and Mr. Bastable. Mr. Chu is the Chair of the Audit Committee. Mr. Bastable is a member of the Board of Directors of LDC. See Part 11 under the heading "Audit Committee" below for further information on the Audit Committee.

(b) Corporate Governance Committee

The Corporate Governance Committee is responsible for considering and making recommendations to the Board with respect to matters relating to the corporate governance of Toronto Hydro, including board and committee composition and mandates, and guidelines for assessing the effectiveness of the Board and its committees and procedures to ensure that the Board functions independently from management. Management undertakes orientation and education programs for new directors. Members of the Corporate Governance Committee are Mr. Cowbourne, Mr. Chu and Ms. Kennedy. Mr. Cowbourne is the Chair of the Corporate Governance Committee.

(c) Compensation Committee

The Compensation Committee is responsible for reviewing and assisting the Board in overseeing Toronto Hydro's compensation program. Members of the Compensation Committee are: Ms. Callon, Mr. Copeland, Mr. Bastable and Ms. Beed. Ms. Callon is the Chair of the Compensation Committee. Mr. Bastable and Ms. Beed are members of the Board of Directors of the LDC. See section 12.1(a) under the heading "Compensation Committee" for further information on the Compensation Committee.

(d) Health and Safety Committee

The Health and Safety Committee is responsible for considering and making recommendations to the Board with respect to matters of health and safety. Members of the Health and Safety Committee are Mr. Williams, Ms. Callon and Ms. Khetrapal. Mr. Williams is the Chair of the Health and Safety Committee.

10.7 Board Orientation and Continuing Education

Each new director, upon joining the Board, is given a comprehensive set of materials designed to provide him/her with a summary of the key organizational, financial, regulatory, and operational aspects of Toronto Hydro. These materials also contain information on the various Toronto Hydro boards and their committees.

On an on-going basis, as part of regular and special board meetings, directors receive presentations and reports on topics related to Toronto Hydro's businesses and the obligations and responsibilities of directors. Topics covered are either suggested by management or requested by the directors. As well, directors receive information from management in response to any actions arising at a board meeting or otherwise. Directors are also periodically provided with orientation sessions with senior management and facility tours to assist them in understanding Toronto Hydro's businesses.

10.8 Board, Committee and Director Assessments

The Corporate Governance Committee oversees a process used to evaluate the effectiveness of the Board and its committees. The process consists of a written questionnaire evaluating the Board, its committees and the individual directors that is completed periodically by each director. The directors' responses to the questionnaire related to the operation of the Board and its committees are compiled into a summary report that is reviewed by the Corporate Governance Committee. This report and recommended remedial actions are presented by the Chair of the Corporate Governance Committee to the Board for review, consideration and implementation. The directors' responses related to the individual directors are provided directly to the Chair of the Board for review, consideration and application.

10.9 Board Oversight and Management of Risks

In 2010, the Corporation adopted an Enterprise Risk Management Program to provide a consistent and disciplined methodology for the identification, assessment, mitigation, monitoring and reporting of risks applicable to Toronto Hydro. The Enterprise Risk Management Program follows industry best practices and adopts a rigorous top-down and bottom-up approach to integrate risk management into the Corporation's strategic plan and to manage strategic, operational, financial, employee, health and safety, environmental, and external risks.

To ensure strong oversight over the risk management process, a formal risk governance structure is in place. The Corporation's Enterprise Risk Management Program is administered under the supervision of LDC's Vice-President, Strategic Management and Information Technology, who reports and makes recommendations to an executive Risk Oversight Committee consisting of all executive officers of the Corporation and LDC. The executive Risk Oversight Committee provides quarterly reports to the Board regarding material risks. The Board is ultimately responsible for the oversight and management of the Corporation's risks.

PART 11- AUDIT COMMITTEE

11.1 Composition, Independence and Financial Literacy

The Audit Committee is comprised of Mr. Chu (Chair), Ms. Kennedy, Ms. Khetrpal and Mr. Bastable, each of whom is independent and financially literate within the meaning of applicable Canadian securities laws. Mr. Bastable is a member of the Board of Directors of LDC.

11.2 Relevant Education and Experience

In addition to each member's general business experience, the education and experience of each Audit Committee member that is relevant to the performance of his or her responsibilities as an Audit Committee member is described below.

Mr. Chu holds a Juris Doctor from the University of Toronto and is a member of the Law Society of Upper Canada. Mr. Chu is a founding partner of the law firm of Bogart Robertson and Chu, practicing corporate and commercial real estate law. Mr. Chu served as Chair of the Audit Committee of Centennial College and as a member of the Finance Committee of the Ontario College of Art and Design. Mr. Chu served as the Chair of the Finance and Audit Committee of the Laidlaw Foundation. Mr. Chu serves on the Finance and Operations Committee of the Centennial Centre of Science and Technology (Ontario Science Centre). Mr. Chu has been a member of the Canadian Tax Foundation since 1986.

Ms. Kennedy is a chartered accountant and holds a Bachelor of Commerce degree from McMaster University. Ms. Kennedy has held a variety of senior financial management and accounting positions including Chief Financial Officer and Chief Auditor, AEGON Canada Inc., Senior Vice-President and Chief Internal Auditor, Sobeys Inc., Chief Auditor, Sun Life Financial Inc. and Vice-President Finance and Actuarial Sun Life Financial Inc. Ms. Kennedy is currently a Commissioner of the Ontario Securities Commission, a member of the Financial Consumer Agency of Canada External Stakeholder Advisory Committee, a member of the Business Board of the University of Toronto and Chair of the University of Toronto Audit Committee.

Ms. Khetrpal holds a Masters degree in Economics, is a certified director of the Institute of Corporate Directors and a member of the Toronto Chartered Financial Analysts Society. She is a member of the Board of Directors of St. Joseph's Health Centre and Chair of its Audit Committee. She is also a member of the Board of Directors of Cancer Care Ontario and Vice Chair of its Audit Committee. She is also a member of the Board of Directors of The Public Accountants Council, and a member for its Audit Committee. In addition, she is a member of the Canada Pension Plan Review Tribunal. Previous positions held include Vice President and Chief Financial Officer of Weekenders International Holding Corporation, Vice President and Treasurer, Moore Corporation Limited, Director, Economics & Planning Canadian Pacific Enterprises Limited and member of the Board of Directors of Moore Group Services BVBA-Belgium, Peak Technologies Canada Ltd., Moore Holdings Ltd. - Australia and the Ontario Casino Corporation.

Mr. Bastable is a Fellow of the Institute of Chartered Accountants in Ireland. He is currently Chairman of Cushman & Wakefield Ltd. His past business experience includes positions as Chief Financial Officer, and Chief Executive Officer of Royal LePage Ltd. He is a past director and member of the Audit Committee of Decision Dynamics Technology Ltd. He currently serves as a Trustee of Brookfield Office Properties Canada Real Estate Investment Trust and is a member of its Audit Committee, and Chair of its Governance and Nominating Committee. He is also a member of the Independent Review Committee of Brandes Investment Partners & Co. He has significant board and committee experience with not-for-profit organizations including as Chair of the Board of Governors of McMaster University in Hamilton, Ontario.

11.3 Audit Committee Charter

Under the terms of its charter, the Audit Committee is responsible for: managing the relationship between the Corporation and its external auditors; overseeing the external audit; overseeing the internal audit; reviewing, approving and recommending to the Board for approval the financial statements, management's discussion and analysis and interim reports of the Corporation, the annual information form and other public disclosure of financial information extracted from the Financial Statements of the Corporation; overseeing internal financial control structure and financial risk management systems; and establishing and reviewing certain procedures.

The full text of Corporation's Audit Committee Charter is attached as Annex A.

11.4 Policy on the Provision of Services by the External Auditors

The Audit Committee has developed a Policy on the Provision of Services by the External Auditors. Under the terms of the Policy:

- the external auditors may not provide services to Toronto Hydro that impair or have the potential to impair the independence and objectivity of the external auditors in relation to the external audit function (generally, prohibited services include services where the external auditors participate in activities that are normally undertaken by management of Toronto Hydro, are remunerated through a "success fee" structure, act in an advocacy role for Toronto Hydro or may be required to audit their own work);
- the Audit Committee has pre-approved certain audit and permitted non-audit services as services that the auditors may provide to Toronto Hydro, including: services that constitute the agreed scope of the external audit or interim reviews of Toronto Hydro; services that are outside the agreed scope of, but are consistent with, the external audit or interim reviews of Toronto Hydro; tax services that do not compromise the independence and objectivity of the external auditors in relation to the external audit; and other services of an advisory nature that do not compromise the independence and objectivity of the external auditors in relation to the external audit work; and
- an authorization process has been established which provides, among other things: the Chief Financial Officer may authorize in advance all engagements of the external auditors to provide pre-approved services (other than audit services) to Toronto Hydro up to a maximum of \$25,000 for any engagement and up to a maximum of \$100,000 for all engagements in any fiscal quarter (the Chief Financial Officer must report all such authorized engagements to the Audit Committee at its next meeting); the Chair of the Audit Committee may authorize in advance all engagements of the external auditors to provide pre-approved services (other than audit services) to Toronto Hydro up to a maximum of \$50,000 for any engagement and up to a maximum of \$100,000 for all engagements in any fiscal quarter (the Chair must report all such authorized engagements to the Audit Committee at its next meeting); and the Audit Committee must authorize in advance all engagements of the external auditors to provide pre-approved services to Toronto Hydro above the prescribed thresholds and all engagements to provide services that are not pre-approved services regardless of the dollar value of the services.

Exceptions can be made to this Policy where the exceptions are in the interests of Toronto Hydro and appropriate arrangements are established to ensure the independence and objectivity of the external auditors in relation to the external audit. Any exception must be authorized by the Audit Committee and must be reported to the Board.

11.5 External Auditors Service Fees

On April 12, 2011, KPMG LLP was appointed as the external auditor of the Corporation, replacing the former external audit firm of Ernst & Young LLP.

The table below sets out the fees billed by the Corporation's auditors for each of last two fiscal years in respect of the services noted below.

	Year ended December 31,		
	2011	2010	
	KPMG	E&Y	E&Y
Audit fees ⁽¹⁾	\$279,158	\$455,248	\$800,385
Audit-related fees ⁽²⁾	\$105,930	\$-	\$159,557
Tax fees ⁽³⁾	\$-	\$-	\$-
All other fees	\$654,533 ⁽⁴⁾	\$61,772 ⁽⁵⁾	\$583,035 ⁽⁶⁾

Notes:

- (1) Fees for audit services.
- (2) Fees for assurance and related services that are reasonably related to the performance of the audit or review of the Corporation's financial statements and are not reported under (1) above. These fees represent fees for interim reviews.
- (3) Fees for professional services rendered for tax compliance, tax advice and tax planning.
- (4) Fees related to consultations in respect of the transition to IFRS and US GAAP, implementation of a new billing system, the annual Canadian Public Accountability Board levy and other miscellaneous fees.
- (5) Fees related to translations, the annual Canadian Public Accountability Board levy and other miscellaneous fees.
- (6) Fees related to consultations in respect of the transition to IFRS, the MTN Program, the annual Canadian Public Accountability Board levy and other miscellaneous fees.

PART 12- EXECUTIVE COMPENSATION

12.1 Compensation Governance

(a) Compensation Committee

(i) *Composition and Independence*

The Corporation's executive compensation program is supervised by the Compensation Committee under the direction of the Board. The Compensation Committee is comprised of Ms. Callon (Chair), Mr. Copeland, Mr. Bastable and Ms. Beed, each of whom is independent within the meaning of applicable Canadian securities laws. Mr. Bastable and Ms. Beed are members of the Board of Directors of LDC.

(ii) *Relevant Education and Experience*

The general business experience, education, skills and expertise of each Compensation Committee member, together with the education, experience, skills and expertise of the other members of the Compensation Committee, enable the Compensation Committee to make decisions on the suitability of Toronto Hydro's compensation policies and practices. The relevant experience, education, skills and expertise of each Compensation Committee member is described below.

Ms. Callon holds a law degree from the University of Western Ontario and is a member of the Law Society of Upper Canada. She is currently a member of the senior management team of the Canadian Securities Transition Office. Ms. Callon has held a variety of senior positions, including Vice-President & Associate General Counsel, Canadian Imperial Bank of Commerce and advisor to the Ontario Securities Commission. In 2005, she graduated from the Directors Education Program sponsored by the Institute of Corporate Directors Corporate Governance

College and the Rotman School of Management which included specific training on the board's role in enhancing human performance, including the appointment, evaluation, compensation and renewal of an organization's executive team. She is a member of the Board of Directors of Community MicroSkills Development Centre and Chair of its corporate governance committee which is responsible for, among other things, succession planning and performance evaluation of the Community MicroSkills Development Centre's executive director.

Mr. Copeland has a wide range of experience in Executive Compensation. He has held the position of Chairman of the Compensation Committee on several companies including Toronto Hydro Corporation, RioCan Real Estate Investment Trust, Danier Leather Inc., Chesswood Income Trust, The Pioneer Group Inc., M.D.C. Holdings, Inc. and Entertainment One Ltd. Mr. Copeland is well versed and up-to-date with compensation systems and benefit programs at all levels. Mr. Copeland has also been the Chief Executive Officer of several organizations and in that role has the business experience of being the ultimate decision maker, together with the organizations' boards of directors and compensation committees, as applicable, regarding compensation issues.

Mr. Bastable has considerable experience in executive compensation matters from his years as the Chief Executive Officer of a publicly traded company, and as a member of the compensation committees of several boards on which he serves or has served as a director, including the compensation committees of Royal LePage Ltd. and McMaster University. He is familiar with the structure of compensation systems and related benefit programs, and is experienced in executive performance evaluation. See section 11.2 under the heading "Relevant Education and Experience" for more information on Mr. Bastable's education and experience.

Ms. Beed holds a Master's of Science degree in Nursing from the University of Toronto and has held many senior positions in the health care field including at the Hospital for Sick Children, the Princess Margaret Hospital / Ontario Cancer Institute (Vice-President, Organizational Development), the University Health Network (Chief Operating Officer) and Markham Stouffville Hospital (Chief Executive Officer). Ms. Beed has also been a Global Partner with Deloitte Consulting Inc., where her focus was Change Management and Strategic Business Development in both the Energy and Consumer industry groups. Ms. Beed currently sits on several not-for-profit boards including, ventureLAB Inc., Character Community Foundation of York Region, and the Dean's Advisory Council of the Faculty of Health at York University.

(iii) *Compensation Committee Charter*

The Compensation Committee operates under a written charter adopted by the Board. The primary function of the Compensation Committee is to advise and assist the Board in overseeing Toronto Hydro's compensation program and assessing the performance and compensation of the CEO. Specifically, under the terms of its charter, the Compensation Committee is responsible for assisting the Board in fulfilling its responsibilities with respect to: the recruitment and assessment of the performance of the CEO; the approval of the compensation of the CEO and review of the compensation of the other executive officers of Toronto Hydro; the review and approval of executive compensation disclosure; and the general oversight of the compensation structure and benefit plans and programs for Toronto Hydro.

(b) Compensation Risk Oversight

Toronto Hydro has a rigorous risk management and governance structure in place to assist the Board with its oversight and management of all of the Corporation's risks, including risks related to Toronto Hydro's compensation policies and practices. While the Board and Compensation Committee have not conducted a formal assessment of the implications of risks specifically associated with the Corporation's compensation policies and practices, the Compensation Committee has and continues to consider the Corporation's strategic objectives, plans and risk strategy in its review and recommendations regarding Toronto Hydro's compensation program. In addition to the Corporation's Enterprise Risk Management Program, the practices, processes and systems in place to identify and mitigate compensation policies and practices that could encourage an executive officer to take inappropriate or excessive risks include: the periodic review and audit of the Corporation's executive compensation program by the Corporation's internal auditor; the development and application of a management control reporting system providing transparency and control to compensation measures; the use of a balanced scorecard of corporate, divisional and individual performance objectives; the periodic benchmarking of the Corporation's compensation program; the

review of the Corporation's compensation program by an independent compensation consultant and, from time to time, the OEB; and the application of maximum payout amounts for achievement of individual performance goals. See section 10.9 under the heading "Board Oversight and Management of Risks" for more information on the Corporation's Enterprise Risk Management Program, section 12.2(c)(ii) under the heading "Benchmarking" for more information on the Corporation's benchmarking of its compensation program, section 12.2(c)(iii) under the heading "Compensation Consultants and Advisors" for more information on the Corporation's compensation consultant and section 12.2(d)(ii) under the heading "Performance-Based Incentive Compensation" for more information on the Corporation's performance-based incentive compensation program.

12.2 Compensation Discussion and Analysis

(a) Named Executive Officers

This Compensation Discussion and Analysis describes and explains all significant elements of compensation awarded to, earned by, paid to, or payable to the NEOs for the financial year ended December 31, 2011. The NEOs are:

- (i) **Anthony Haines**
President and CEO, Toronto Hydro Corporation
- (ii) **Jean-Sebastien Couillard**
CFO, Toronto Hydro Corporation
- (iii) **Dino Priore**
Vice-President, Distribution Services, Toronto Hydro-Electric System Limited
- (iv) **Ben La Pianta**
Vice-President, Distribution Grid Management, Toronto Hydro-Electric System Limited
- (v) **Ivano Labricciosa**
Vice-President, Asset Management, Toronto Hydro-Electric System Limited

(b) General Objectives of Compensation Program

The Corporation's executive compensation program is designed to attract and retain executives who have the skills and experience to help the Corporation achieve its strategic goals, to motivate executives to achieve such corporate goals and to reward executives for superior performance and achievement of corporate, divisional and individual objectives.

(c) Process for Establishing Compensation

(i) Policies and Practices

The Corporation's overall executive compensation structure and program is developed and supervised by the Compensation Committee with the assistance of a compensation consultant, and approved by the Board. See section 12.2(c)(iii) under the heading "Compensation Consultants and Advisors" for more information on the compensation consultant.

Pursuant to the terms of its charter, the Compensation Committee has the responsibility to annually, and more frequently if appropriate, review and approve the individual performance-based incentive compensation goals and objectives related to the compensation of the CEO and to assess the CEO's performance against those goals and objectives. The Compensation Committee also makes recommendations to the Board with respect to the overall compensation and benefits of the CEO. The Board ultimately sets and approves the CEO's compensation.

The CEO has the responsibility to annually, and more frequently if appropriate, review and approve the individual performance-based incentive compensation goals and objectives related to the compensation of the other executive officers, including the NEOs, and assess the other executive officers' performance against those goals and objectives. The CEO approves the other executive officers' performance-based incentive compensation and overall compensation, subject to the Compensation Committee's review.

(ii) *Benchmarking*

The Corporation periodically benchmarks the compensation it provides to the NEOs to ensure reasonableness, competitiveness and effectiveness of the Corporation's compensation program, including the level and type of compensation provided. The Compensation Committee engages Mercer to provide executive compensation benchmarking consulting services. See section 12.2(c)(iii) under the heading "Compensation Consultants and Advisors" for more information on services provided by Mercer.

NEO compensation is generally benchmarked against the executive compensation provided by other electricity distributors and other organizations that are selected and deemed relevant due to the fact that they are similar to the Corporation in scope, complexity and revenue. In particular, when benchmarking the NEOs' compensation with respect to the Corporation's revenue as compared to the revenue of other companies in the benchmarking group, Mercer has taken a conservative approach and excluded the Corporation's flow through revenue for electricity transmission and generation. The benchmark group's compensation data is derived from the Mercer Benchmark Database, which includes data from industrial organizations located in the Greater Toronto Area, industrial organizations located across Canada, and organizations from the national public sector. Publicly-disclosed compensation information for executive officers is also considered.

For the purposes of benchmarking the CEO's compensation specifically, the Compensation Committee has benchmarked against the executive compensation provided by the following companies: AltaGas Ltd., ATCO Ltd., British Columbia Hydro and Power Authority (operates as BC Hydro), Capital Power Corporation, Emera Inc., Enbridge Inc., ENMAX Corporation, Epcor Utilities Inc., Hydro One, IESO, OEB, Ontario Power Authority, OPG, SaskPower, TransAlta Corporation and Union Gas Limited.

The executive compensation information derived from the benchmarking analysis is designed to assist the Compensation Committee in establishing, over a reasonable period of time, total compensation for NEOs in the range of the median total compensation of those companies within the benchmark group. Total compensation to NEOs may exceed the median of the marketplace when corporate, divisional and individual performance significantly exceeds objectives.

(iii) *Compensation Consultants and Advisors*

The Corporation began engaging the services of Mercer for executive compensation consulting services in 2005. In 2007, Mercer was retained directly by the Compensation Committee for executive compensation consulting services. The services provided to the Compensation Committee by Mercer include providing advice on the competitiveness and appropriateness of the Corporation's executive and director compensation program, compensation benchmarking services, and other compensation related matters that may arise from time to time.

The table below sets out the fees billed by Mercer for each of last two fiscal years in respect of the services noted below.

	Year ended December 31,	
	2011	2010
Executive Compensation – Related Fees ⁽¹⁾	\$148,405	\$113,814
All Other Fees ⁽²⁾	\$19,414	\$-

Notes:

- (1) Aggregate fees billed by Mercer, or any of its affiliates, for services related to determining compensation for any of the Corporation's directors and executive officers.
- (2) Aggregate fees for all other services provided by Mercer, or any of its affiliates, that are not reported under (1) above. These fees relate to workforce diversity consultation services performed at the request of the management, and pursuant to a Board request. There is no formal requirement for the Board or the Compensation Committee to pre-approve other services provided by Mercer or its affiliates to the Corporation at the request of management.

(d) Elements of Compensation

The principal components of compensation for NEOs are:

- base salary;
- performance-based incentive compensation;
- personal benefits and perquisites;
- pension plan;
- retirement benefits;
- retirement allowances; and
- termination payments.

As the Corporation has a single shareholder that is the registered and beneficial owner of all of its issued and outstanding shares, the Corporation is not able to offer an equity incentive plan or other stock-based compensation to its NEOs. The lack of an equity incentive is an underlying consideration of the Corporation in determining the NEOs overall compensation package from the above-noted components.

(i) Base Salary

In accordance with the general objectives and process for establishing compensation noted above, the Corporation provides NEOs with a base salary to compensate them for services rendered during the fiscal year. The Corporation provides reasonably competitive market-based base salaries to help attract, motivate, and retain NEOs who are critical to the Corporation's success.

Annually, adjustments to base salaries for NEOs are driven by market benchmarking data and the NEO's individual performance rating. The performance rating is determined, in the case of the CEO, by the Compensation Committee and, in the case of the other NEOs, by the CEO, based on the achievement of performance-based incentive compensation objectives, knowledge, skills, and competencies related to day-to-day performance, as well as demonstration of desired corporate behaviours, subject to the Compensation Committee's review.

(ii) Performance-Based Incentive Compensation

All NEOs receive a portion of their annual compensation in the form of performance-based cash payments. The performance-based incentive compensation is designed to retain, motivate and reward NEOs for reaching corporate, divisional and individual performance objectives established at the beginning of each calendar year.

The annual performance-based incentive compensation is calculated as a percentage of the NEO's base salary for the year and, if earned, paid in one lump sum in the next fiscal year.

In order for an NEO to earn and receive the performance-based incentive compensation, the Corporation and the NEO must each achieve certain pre-determined performance objectives. Each NEO's performance-based incentive compensation is based on a weighting of corporate, divisional and individual performance objectives, which weightings and objectives are determined at the start of each year and vary by role to reflect the performance focus of the role. The weighting and objectives are reviewed and set each year in order to reflect the Corporation's overall strategy and objectives.

Corporate and divisional performance objectives are based on financial and other industry specific measures. Each NEO's individual objectives are based on areas of strategic and operational emphasis related to their respective responsibilities and portfolios.

The CEO's individual objectives are reviewed and approved by the Compensation Committee. The individual objectives of the other NEOs are reviewed and approved by the CEO.

The NEO's individual objectives are intended to be reasonably difficult to attain and to encourage success in the NEO's performance. Individual objectives are often but not always achieved by an NEO in any given year. NEOs review their objectives and measurements throughout the year, with one formal mid-year review with the Chair of the Board (in the case of the CEO), and with the CEO (in the case of the other NEOs), to track achievement to-date and revise performance goals as may be necessary to reflect any change in corporate strategy or priorities.

In the case of the CEO, an annual performance evaluation in respect of his individual performance goals is conducted by the Chair of the Board who provides a recommendation to the Compensation Committee regarding the performance-based incentive compensation to be paid to the CEO. The amount paid to the CEO is approved by the Board after review of the recommendation of the Compensation Committee.

In the case of each of the other NEOs, an annual performance evaluation in respect of the individual objectives for each individual is conducted by the CEO, who determines the amount of performance-based incentive compensation to be paid to each other NEO. The Compensation Committee also reviews the amounts of performance-based incentive compensation to be paid to each of the other NEOs.

In the case of the CEO, the Compensation Committee, and, in the case of the other NEOs, the CEO, may exercise their discretion to increase or reduce the performance-based incentive compensation paid to the CEO or NEO, as applicable, including in certain circumstances absent attainment of a relevant performance goal or similar condition.

(iii) *Personal Benefits and Perquisites*

The Corporation provides NEOs with other personal benefits and perquisites that the Corporation believes are reasonable and consistent with its overall compensation program to better enable the Corporation to attract and retain superior employees for key positions. Benefits include group health, dental, group life insurance, short-term and long-term disability, accidental death & dismemberment, a fitness subsidy, and educational reimbursements, all of which are generally available to all salaried employees and do not discriminate in scope, terms or operation between employees of the same classification. In 2011, the Corporation also provided NEOs with vehicles as part of the NEOs' personal benefits and perquisites, which benefit has been eliminated effective February 28, 2012.

(iv) *Pension Plan*

All full-time employees of the Corporation, including the NEOs, are required to participate in the OMERS pension plan. Pursuant to the terms of the OMERS pension plan, NEOs are required to make plan contributions based on their pensionable earnings. In 2011, each NEO was required to contribute 7.40% of the first \$48,300 of pensionable earnings and thereafter 10.70% on all earnings over \$48,300 and up to \$143,163. Beyond the \$143,163 maximum, contributions of 10.70% continue towards a Retirement Compensation Arrangement (RCA), which is governed separately under the Canadian Income Tax Act. The OMERS pension plan is generally available to all other salaried employees and does not discriminate in scope, terms or operation between employees of the same classification. See 4.6(a) under the heading "Employees" for more information on the OMERS pension plan.

(v) *Retirement Benefits*

NEOs are eligible to receive post-retirement health, dental and life insurance after a minimum of five years of service with the Corporation if they retire from the Corporation and begin collecting under the OMERS pension plan upon retirement. The post-retirement benefits provided to eligible NEOs are the same as are generally available to all other salaried employees and do not discriminate in scope, terms or operation between employees of the same classification. Post-retirement benefits aid in attracting and retaining key executives to ensure the long-term success of the Corporation.

(vi) *Retirement Allowances*

From time to time, in certain circumstances, the Corporation enters into retirement allowance agreements with its NEOs. The retirement allowance agreements are designed in recognition of service and to promote retention, stability and continuity of the NEOs. These agreements are made on a case-by-case basis based on an NEO's years of service and position. Any retirement allowance provided to the CEO is approved by the Board after review of the recommendation of the Compensation Committee. In the case of each of the other NEOs, any retirement allowance agreement is approved by the CEO and reviewed by the Compensation Committee. Retirement allowance payments are typically paid in one or two lump sum instalments following termination or retirement of the NEO.

(vii) *Termination Payments*

From time to time, the Corporation enters into agreements with NEOs which provide for payments upon termination. These agreements are made on a case-by-case basis based on the NEO's age, years of service and position. Any such agreement for the CEO is approved by the Board after review of the recommendation of the Compensation Committee. In the case of each of the other NEOs, any such agreement is approved by the CEO and reviewed by the Compensation Committee. Typically, termination payments are paid either as a lump sum or as salary continuation for an agreed period following termination.

12.3 Compensation of Named Executive Officers

(a) Summary Compensation Table

The following table provides a summary of the compensation earned during the years ended December 31, 2009, 2010 and 2011, by the NEOs:

Summary Compensation Table⁽¹⁾

NEO Name and Principal Position	Year	Salary ⁽²⁾ (\$)	Non-Equity Incentive Plan Compensation ⁽³⁾ (\$)	All Other Compensation ⁽⁴⁾ (\$)	Total Compensation (\$)
Anthony Haines ⁽⁵⁾ President and Chief Executive Officer, Toronto Hydro Corporation	2011	\$421,702	\$371,378	\$58,903 ⁽⁶⁾	\$851,983
	2010	\$372,807	\$340,018	\$44,905	\$757,730
	2009	\$325,744	\$224,166	\$129,161	\$679,071
Jean-Sebastien Couillard Chief Financial Officer, Toronto Hydro Corporation	2011	\$257,934	\$141,152	\$30,337 ⁽⁷⁾	\$429,423
	2010	\$238,462	\$129,860	\$24,220	\$392,542
	2009	\$231,542	\$111,796	\$57,913	\$401,251
Dino Priore Vice-President, Distribution Services Toronto Hydro –Electric System Limited	2011	\$244,104	\$134,121	\$20,140 ⁽⁸⁾	\$398,365
	2010	\$219,583	\$126,763	\$19,272 ⁽⁹⁾	\$365,618
	2009	\$184,275	\$82,776	\$25,362	\$292,413
Ben La Pianta Vice-President, Distribution Grid Management Toronto Hydro –Electric System Limited	2011	\$231,712	\$118,421	\$31,440 ⁽¹⁰⁾	\$381,573
	2010	\$216,813	\$116,472	\$19,066 ⁽¹¹⁾	\$352,351
	2009	\$181,374	\$81,732	\$24,916	\$288,022
Ivano Labricciosa Vice-President, Asset Management Toronto Hydro –Electric System Limited	2011	\$222,813	\$118,482	\$31,356 ⁽¹²⁾	\$372,652
	2010	\$212,780	\$112,574	\$31,975	\$357,329
	2009	\$179,337	\$74,391	\$48,413	\$302,141

Notes:

- (1) Amounts shown in this table are in Canadian dollars and have been rounded to the nearest dollar.
- (2) Amounts shown reflect actual amounts paid during the year.
- (3) Each NEO's annual performance-based incentive compensation for a fiscal year is determined and paid in the next fiscal year. Accordingly, amounts reflected in respect of a particular year (i.e. 2011) represent the annual performance-based incentive compensation earned by the NEO for the achievement of performance objectives in respect of that fiscal year (i.e. 2011) but which amounts are paid in the following fiscal year (i.e. 2012).
- (4) Amounts shown in this column reflect all other compensation earned by the NEO during the year. Unless otherwise noted in footnotes to follow, the amounts shown include the aggregate value of perquisites and other personal benefits provided to the NEO, where such perquisites and personal benefits are not generally available to all employees and are worth \$50,000 or more, or are worth 10% or more of the NEO's total salary for the year. Perquisites or other personal benefits that exceed 25% of the total value of perquisites and other personal benefits reported for an NEO for the year have been identified in footnotes to follow. Perquisites and other personal benefits have been calculated by using the actual cost.
- (5) Mr. Haines was appointed as CEO on October 1, 2009. Prior to that, Mr. Haines was President of the LDC.
- (6) Amount shown includes \$33,135 for vehicle lease costs.
- (7) Amount shown includes \$18,490 for vehicle lease costs.
- (8) In this instance, the aggregate value of perquisites and other personal benefits represent approximately 8% of the NEO's total salary for the year. Amount shown includes \$12,471 for vehicle lease costs.
- (9) In this instance, the aggregate value of perquisites and other personal benefits represent approximately 9% of the NEO's total salary for the year.
- (10) Amount shown includes \$18,111 for vehicle lease costs.
- (11) In this instance, the aggregate value of perquisites and other personal benefits represent approximately 9% of the NEO's total salary for the year.
- (12) Amount shown includes \$17,846 for vehicle lease costs.

(b) Compensation of NEOs in 2011 – Narrative Discussion

(i) Base Salaries

The NEOs' annual base salaries for 2011 were: \$423,625 in the case of Mr. Haines, \$258,703 in the case of Mr. Couillard, \$245,065 in the case of Mr. Priore, \$232,289 in the case of Mr. La Pianta, and \$223,198 in the case of Mr. Labricciosa.

(ii) Performance-Based Incentive Compensation

The respective allowable performance-based incentive compensation amounts for each NEO for 2011 were as follows: 65% of the base salary, in the case of Mr. Haines, 40% of the base salary in the case of Mr. Couillard, 40% of the base salary in the case of Mr. Priore, 40% of the base salary in the case of Mr. La Pianta, and 40% of the base salary in the case of Mr. Labricciosa.

The weightings attributed to Mr. Haine's 2011 performance-based incentive compensation were as follows: 80% based on the performance of the Corporation and 20% based on the achievement of individual performance objectives. For all other NEOs, the performance-based incentive compensation weightings were as follows: 60% based on the performance of the Corporation, 20% based on the Corporation's achievement of divisional objectives, and 20% based on the NEO's achievement of individual performance objectives.

The performance objectives of the Corporation for 2011 were as follows:

Corporate Objective	Measure	Target	Weight
Safety	Number of recordable injuries x 200,000 / exposure hours.	4.50	5.0%
Safety Leadership	Number of safety inspections completed as percentage of plan.	95%	5.0%
Attendance (number of days absent)	Average days absent per employee.	7.75	5.0%

Corporate Objective	Measure	Target	Weight
Consolidated Operating Expenses (\$ millions)	Operating expenses per the Corporation's Consolidated Financial Statements.	\$259.9	15.0%
Consolidated Net Income (\$ millions)	Net Income per the Corporation's Consolidated Financial Statements.	\$73.0	15.0%
Distribution Plan Capital per Unit (\$ thousands)	Total electricity distribution capital spent in 2011 (including planned and unplanned refurbishment, customer growth net of contribution) divided by related units of work completed in period.	\$1.18	30.0%
Worst Performing Feeders	Total number of feeders experiencing more than seven sustained outages in a year, with outages defined as interruptions greater than one minute.	37	5.0%
SAIDI (in minutes)	Measure of the annual system average interruption duration for customer served, not including MED.	82.0	5.0%
SAIFI (in minutes)	Measure of the frequency of service interruptions for customers served, not including MED.	1.66	5.0%
Call Centre Index	Average of call centre responses within thirty seconds and call quality.	83%	10.0%

The divisional performance objectives for 2011 were as follows:

Divisional Objective	FINANCE		ASSET MANAGEMENT		DISTRIBUTION SERVICES		DISTRIBUTION GRID MANAGEMENT	
	Target	Weight (%)	Target	Weight (%)	Target	Weight (%)	Target	Weight (%)
	Jean-Sebastien Couillard		Ivano Labricciosa		Dino Priore		Ben La Pianta	
Safety	4.5	5	4.5	5	4.5	10	4.5	10
Safety Leadership	N/A	N/A	95%	10	95%	15	95%	15
Attendance (number of days absent)	3.2	2.5	7	5	7.3	10	9.3	10
	(Finance)	(Finance)						
	7.8	2.5						
	(Facilities)	(Facilities)						
Consolidated Operating Expense (\$ millions)	\$259.9	30	\$24.2	5	\$102.0	5	\$102.0	15
Consolidated Net Income (\$ millions)	\$77.5	35	\$77.5	5	\$77.5	5	\$77.5	5
Distribution Plant Capital per Unit (\$ thousands)	\$1.18	20	\$1.18	25	\$1.18	40	\$1.18	15
Worst Performing Feeders	N/A	N/A	37	20	37	5	37	10
SAIDI (in minutes)	N/A	N/A	82	5	82	5	82	15
SAIFI (in minutes)	N/A	N/A	1.7	20	1.7	5	1.7	5
Call Centre Service Index	83.00%	5	N/A	N/A	N/A	N/A	N/A	N/A

The Corporation achieved all of its 2011 corporate and divisional objectives, except for the objectives related to SAIFI and attendance. Each of the NEOs achieved his individual performance objectives for 2011. Each of the corporate, divisional and individual performance objectives were reasonably difficult to attain and served to encourage success in the NEO performance and in the Corporation's financial and operational results.

The percentage of total compensation that relates to the achievement of each NEO's individual performance objectives were as follows: 11 % for Mr. Haines, 9% for Mr. Couillard, 9% for Mr. Priore, 7% for Mr. La Pianta and 8% for Mr. Labricciosa.

(iii) *Personal Benefits and Perquisites*

In 2011, the NEOs received personal benefits and perquisites as described in section 12.2(d)(iii) under the heading "Personal Benefits and Perquisites", and as quantified in the Summary Compensation Table in section 12.3(a) above.

(iv) *Pension Plan*

In 2011, each of the NEOs participated in the OMERS pension plan. The OMERS pension plan is a group pension plan that is generally available to all salaried employees and does not discriminate in scope, terms or operation between employees of the same classification. See section 4.6(a) under the heading "Employees" and section 12.2(d)(iv) under the heading "Pension Plan" for further information on the OMERS pension plan.

(v) *Retirement Benefits*

As of December 31, 2011, Mr. Haines, Mr. Couillard, Mr. Priore, Mr. La Pianta and Mr. Labricciosa have each provided Toronto Hydro with more than five years of service and are therefore eligible for post-retirement medical, dental, and life insurance benefits if they retire from the Corporation and begin collecting under the OMERS pension plan upon retirement.

(vi) *Retirement Allowance*

Mr. Haines is the only NEO entitled to a retirement allowance, which allowance is calculated based on completed years of service and is payable in the form of a lump-sum cash payment following Mr. Haines' termination or retirement from the Corporation. If Mr. Haines is terminated or retires from the Corporation during 2012, he will receive a \$50,000 retirement allowance. The amount of the retirement allowance payable to Mr. Haines will thereafter be increased by an additional \$90,000 per year (until 2016) and \$125,000 per year (from 2017 to 2020) for each full calendar year of service completed. The maximum retirement allowance payable to Mr. Haines is \$1,000,000, which Mr. Haines will earn if he remains in active service for the Corporation until December 31, 2020. In the event that Mr. Haines becomes permanently disabled while in active service for the Corporation, he will be deemed to remain in active service for the Corporation until December 31, 2020, at which point he will be considered to have retired and earned the maximum retirement allowance of \$1,000,000. In the event of the death of Mr. Haines while in active service for the Corporation, the retirement allowance which Mr. Haines would have earned as of the date of his death will be paid to his designated beneficiary or to the legal representative of Mr. Haines' estate.

(vii) *Termination Payments*

Both Mr. Haines and Mr. Couillard have entered into agreements with the Corporation which provide for certain payments upon termination.

If the employment of Mr. Haines is terminated without cause by the Corporation, then Mr. Haines is entitled to a payment equal to 24 months of base salary and performance pay that would have been paid had he continued to work for 24 months (approximately \$1,470,958 as at December 31, 2011), with the performance pay calculated based on the average annual performance pay earned by Mr. Haines during the 3 years preceding the date of termination. Mr. Haines would also be entitled to continued group health and dental benefit coverage for a period of 24 months from the date of termination.

If the employment of Mr. Couillard is terminated without cause by the Corporation then he is entitled to a payment equal to 18 months of base salary and performance pay that would have been paid had he continued to work for 18 months (approximately \$579,458 as at December 31, 2011), with the performance pay calculated based on the average annual performance pay earned by Mr. Couillard during the 3 years preceding the date of termination. Mr.

Couillard would also be entitled to continued group health and dental benefit coverage for a period of 18 months from the date of termination.

12.4 Compensation of Directors

(a) Director Compensation Table

Director Name	Fees Earned (\$)	All other compensation (\$)	Total (\$)
Clare Copeland	\$75,000	\$7,013 ⁽¹⁾	\$82,013
Patricia Callon	\$27,500	Nil	\$27,500
Brian Chu	\$27,500	Nil	\$27,500
Derek Cowbourne	\$22,500	Nil	\$22,500
Paulette Kennedy	\$26,500	Nil	\$26,500
Shoba Khetrapal	\$27,500	Nil	\$27,500
David Williams	\$23,500	Nil	\$23,500
Councillor Shelly Carroll	Nil	Nil	Nil
Councillor Josh Colle	Nil	Nil	Nil
Councillor Ron Moeser	Nil	Nil	Nil

Notes:

- (1) An amount in respect of health and dental plan benefits.

(b) Compensation of Directors – Narrative Discussion

Directors of the Corporation, other than Councillors of the City, are compensated for their services as directors through a combination of retainer fees and meeting attendance fees. These fees are set by the sole shareholder of the Corporation, the City. The annual retainer fees are as follows: chair of the Board – \$75,000 and each of the other directors – \$12,500. The meeting attendance fees are as follows: each meeting of the Board and the subsidiaries attended – \$1,000 and each meeting of the Audit Committee, Corporate Governance Committee, Compensation Committee and Health and Safety Committee attended — \$1,000, subject to annual maximum fees per committee member of \$5,000 for the Audit Committee, Corporate Governance Committee, and the Health and Safety Committee and \$4,000 for the Compensation Committee. The Chair receives no meeting attendance fees. Councillors receive no remuneration for their services as directors of the Corporation.

Mr. Copeland also receives health and dental benefits through participation in the same health and dental plan offered to all Toronto Hydro employees.

PART 13- LEGAL PROCEEDINGS

LDC is a party to various legal proceedings relating to the period before July 1999 when Toronto Hydro acquired the assets and liabilities of the Toronto Hydro-Electric Commission. In addition, LDC is a party to various legal proceedings arising since that time in the normal course of business. The pending legal proceedings containing material claims affecting LDC are described below.

13.1 Christian Helm Class Action

On December 6, 2010, a statement of claim in a proposed class action was issued against LDC. The claim seeks general and special damages in the amount of \$100.0 million for disgorgement of unjust gains allegedly resulting from the receipt of interest on overdue accounts at a rate exceeding 5% per annum in contravention of the Interest Act. A statement of defence has been filed. Prior to any certification of the action as a class proceeding, cross summary judgment motions were heard in June 2011 to determine whether the Interest Act has been breached. On February 1, 2012, prior to the release of the decisions on the summary judgment motions, the parties reached a settlement of the matter, which settlement now requires court approval. The Settlement Approval Hearing is scheduled for April 30, 2012. If the settlement receives court approval, damages and costs of approximately \$6.0 million shall be paid by LDC.

If the settlement does not receive court approval, the decision on the cross summary judgment motions will be released. In this event, if the court finds a breach of the Interest Act, subject to appeals, the proceeding will continue, and LDC will rely on other defences. While LDC believes it has a defence to this claim, there is no guarantee that it will be successful in defending the action and therefore, the outcome of this proceeding could have a material impact on the Corporation's consolidated financial statements and results of operations.

13.2 2 Secord Avenue

An action was commenced against LDC in September 2008 in the Ontario Superior Court of Justice under the Class Proceedings Act seeking damages in the amount of \$30.0 million as compensation for damages allegedly suffered as a result of a fire and explosion in an underground vault at 2 Secord Avenue on July 20, 2008. This action is at a preliminary stage. The statement of claim has been served on LDC, a statement of defence and third party claim have been served by LDC and a third party defence and counterclaim against LDC seeking damages in the amount of \$51.0 million have been filed. A certification order has been issued. Affidavits of documents have been produced by LDC to the other parties and examinations for discovery have commenced and are continuing. Given the preliminary status of this action, it is not possible to reasonably quantify the effect, if any, of this action on the financial performance of the Corporation. If damages were awarded, LDC would make a claim under its liability insurance which the Corporation believes would cover any damages which may become payable by LDC in connection with the action.

On December 20, 2010, LDC was served with a statement of claim by the City seeking damages in the amount of \$2.0 million as a result of the fire at 2 Secord Avenue. A statement of defence and third party claim have been served. Given the preliminary status of this action, it is not possible to reasonably quantify the effect, if any, of this action on the financial performance of the Corporation. If damages were awarded, LDC would make a claim under its liability insurance which the Corporation believes would cover any damages which may become payable by LDC in connection with the action.

By order of the court, the above actions, and a smaller non-class action commenced in April 2009 involving the same incident, will be tried at the same time or consecutively.

13.3 2369 Lakeshore Boulevard West

A third party action was commenced against LDC in October 2009 in the Ontario Superior Court of Justice under the Class Proceedings Act seeking damages in the amount of \$30.0 million as compensation for damages allegedly suffered as a result of a fire in the electrical room at 2369 Lakeshore Boulevard West on March 19, 2009. Subsequently, in March 2010, the plaintiff in the main action amended its statement of claim to add LDC as a defendant. The plaintiff in the main action seeks damages in the amount of \$10.0 million from LDC. Both actions are at a preliminary stage and the certification hearing is scheduled for September 2012. Statements of defence to the main action and to the third party claim have not been filed. Accordingly, given the preliminary status of these actions, it is not possible at this time to reasonably quantify the effect, if any, of these actions on the financial performance of the Corporation. If damages were awarded, LDC would make a claim under its liability insurance

which the Corporation believes would cover any damages which may become payable by LDC in connection with these actions.

Another third party action was commenced against LDC in October 2009 in the Ontario Superior Court of Justice seeking damages in the amount of \$30.0 million as compensation for damages allegedly suffered as a result of the fire at 2369 Lakeshore Boulevard West. Subsequently, in March 2010, the plaintiff in the main action amended its statement of claim to add LDC as a defendant. The plaintiff in the main action seeks damages in the amount of \$0.4 million from LDC. LDC has filed a statement of defence, crossclaim and counterclaim. Examinations for discovery have not taken place but are to be completed by February 29, 2012 pursuant to a court ordered timetable. Accordingly, given the preliminary status of these actions, it is not possible at this time to reasonably quantify the effect, if any, of these actions on the financial performance of the Corporation. If damages were awarded, LDC would make a claim under its liability insurance which the Corporation believes would cover any damages which may become payable by LDC in connection with these actions.

On August 29, 2011, LDC was served with a statement of claim by the owner of the building and the property management company for the building seeking damages in the amount of \$2.0 million as a result of the fire at 2369 Lakeshore Boulevard West. LDC has filed a statement of defence and counterclaim. Given the preliminary status of this action, it is not possible to reasonably quantify the effect, if any, of this action on the financial performance of the Corporation. If damages were awarded, LDC would make a claim under its liability insurance which the Corporation believes would cover any damages which may become payable by LDC in connection with the action.

13.4 Adamopoulos

An action was commenced against LDC in November 2004 in the Ontario Superior Court of Justice seeking damages in the amount of \$7.8 million as compensation for damages allegedly suffered as a result of a motor vehicle accident involving an LDC vehicle on January 9, 2001. The plaintiff's motion increasing its claim for damages to \$23.8 million was granted on July 7, 2010. This matter has been settled and a court order has been issued dismissing the action and all related claims by payment of a total amount of approximately \$4.6 million. LDC's liability insurance covered the settlement amount.

13.5 Late Payment Charges Class Action

By Order dated July 22, 2010, the Ontario Superior Court of Justice consolidated and approved the settlement of two class actions against LDC, one commenced in 1994 and the other, against all MEUs, in 1998. The actions sought \$500.0 million and \$64.0 million, respectively, in restitution for late payment charges collected by them from their customers that were in excess of the interest limit stipulated in section 347 of the Criminal Code. The claims made against LDC and the definition of the plaintiff classes were identical in both actions such that any damages payable by LDC in the first action would reduce the damages payable by LDC in the second action, and vice versa.

The July 22, 2010 court order formalized a settlement pursuant to which the defendant MEUs will pay the amount of \$17.0 million plus costs and taxes in settlement of all claims. The amount allocated for payment by each MEU is its proportionate share of the settlement amount based on its percentage of distribution service revenue over the period for which it has exposure for repayment of late payment penalties exceeding the interest rate limit in the Criminal Code. Under the settlement, all of the MEUs involved in the settlement, including LDC, requested an order from the OEB allowing for the future recovery from customers of all costs related to the settlement. On February 22, 2011, the OEB issued its final decision allowing LDC to recover its share of the settlement in the amount of \$7.5 million from customers. The payment to settle LDC's portion of the class action suit was made on June 30, 2011. On July 7, 2011, the OEB authorized LDC to begin the recovery of the balance on August 1, 2011. The full recovery of the balance will be done over a 21-month period ending April 30, 2013.

PART 14 - MATERIAL CONTRACTS

Except for the indenture and the supplemental indentures under which the Debentures were issued, Toronto Hydro has not entered into any material contract (other than contracts entered into in the ordinary course of business) in the most recently completed financial year, or before the most recently completed financial year, if such contract is still in effect.

Copies of these material contracts are available on the SEDAR website at www.sedar.com.

PART 15 - NAMED AND INTERESTS OF EXPERTS

The external auditor of the Corporation is KPMG LLP. KPMG LLP is independent within the meaning of the Rules of Professional Conduct of the Institute of Chartered Accountants of Ontario.

PART 16 - TRANSFER AGENTS AND REGISTRARS

The trustee and registrar for the Corporation is BNY Trust Company of Canada, located in Toronto, Ontario.

PART 17 - ADDITIONAL INFORMATION

Additional information relating to the Corporation, including copies of the Consolidated Financial Statements and Management's Discussion and Analysis, are available on the SEDAR website at www.sedar.com.

ANNEX A - AUDIT COMMITTEE CHARTER

1. General

- (1) The board of directors (*Board*) of Toronto Hydro Corporation (*Corporation*) has established the Audit Committee (*Committee*) to assist the Board in fulfilling its corporate governance and oversight responsibilities with respect to financial reporting, internal financial control structure, financial risk management systems and external audit functions.
- (2) The composition, responsibilities and authority of the Committee are set out in this Charter.
- (3) This Charter and the by-laws of the Corporation and such other procedures, not inconsistent therewith, as the Committee may adopt from time to time shall govern the meetings and procedures of the Committee.

2. Composition

- (1) The Committee shall be composed of at least three directors of the Corporation (*Members*):
 - (a) all Members shall be *independent* (as determined by the Board in accordance with the rules of the Canadian Securities Administrators with respect to the role and composition of audit committees); and
 - (b) at least one of whom, including the chair of the Committee (*Chair*) is *financially literate* (i.e., have the ability to read and understand a set of financial statements that present a breadth and level of complexity of accounting issues that are generally comparable to the breadth and complexity of the accounting issues that can reasonably be expected to be raised by the financial statements of the Corporation).
- (2) Members shall be appointed by the Board on the recommendation of the Chair of the Board and shall serve until they resign, cease to be a Director or are removed or replaced by the Board.
- (3) The Chair of the Board shall designate one of the Members as Chair.
- (4) The Secretary of the Corporation shall be secretary of the Committee (*Secretary*).

3. Responsibilities

The Committee shall assist the Board in fulfilling its corporate governance and oversight responsibilities with respect to financial reporting, internal financial control structure, financial risk management systems and external audit functions.

The Committee shall have the responsibilities set out below.

(1) Managing the Relationship between the Corporation and its External Auditors

The Committee shall be responsible for managing the relationship between the Corporation and its external auditors, including:

- (a) appointing and replacing the external auditors, subject to shareholder approval;
- (b) setting the compensation of the external auditors subject to the approval of the board of directors or shareholder, as applicable;

- (c) overseeing the work of the external auditors, including resolving disagreements between management and the external auditors with respect to financial reporting;
- (d) pre-approving all audit services and permitted non-audit services to be provided to the Corporation and its subsidiary entities by the external auditors;
- (e) having the external auditors report to the Committee in a timely manner with respect to all required matters, including those set out in paragraph 3(2);
- (f) reviewing and approving the hiring policies of the Corporation with respect to present and former partners and employees of the external auditors;
- (g) ensuring the rotation of the audit partner having primary responsibility for the external audit of the Corporation, the audit partner responsible for reviewing the external audit and the external auditors at such intervals as may be required; and
- (h) reviewing and assessing the performance, independence and objectivity of the external auditors.

(2) **Overseeing the External Audit**

The Committee shall be responsible for overseeing the external audit of the Corporation, including:

- (a) reviewing and approving the engagement letter and the audit plan, including financial risk areas identified by the external auditors and management;
- (b) reviewing and assessing the accounting and reporting practices and principles used by the Corporation in preparing its financial statements, including:
 - (1) all significant accounting policies and practices used, including changes from preceding years and any proposed changes for future years;
 - (2) all significant financial reporting issues, estimates and judgments made;
 - (3) all alternative treatments of financial information discussed by the external auditors and management, the results of such discussions and the treatments preferred by the external auditors;
 - (4) any major issues identified by the external auditors with respect to the adequacy of internal control systems and procedures and any special audit steps adopted in light of material deficiencies and weaknesses;
 - (5) the effect of regulatory and accounting initiatives and off-balance sheet transactions or structures on the financial statements;
 - (6) any errors or omissions in, and any required restatement of, the financial statements for preceding years;
 - (7) all significant tax issues;
 - (8) the reporting of all material contingent liabilities; and
 - (9) any material written communications between the external auditors and management;

- (c) reviewing and assessing the results of the external audit and the external auditors' opinion on the financial statements;
- (d) reviewing and discussing with the external auditors and management any management or internal control letters issued or proposed to be issued by the external auditors;
- (e) reviewing and discussing with the external auditors any problems or difficulties encountered by them in the course of their audit work and management's response (including any restrictions on the scope of activities or access to requested information and any significant disagreements with management); and
- (f) reviewing and discussing with legal counsel any legal matters that may have a material impact on the financial statements, operations, assets or compliance policies of the Corporation and any material reports or enquiries received by the Corporation and its subsidiary entities from regulators or government agencies.

(3) **Overseeing the Internal Audit**

The Committee shall be responsible for overseeing the internal audit of the Corporation, including:

- (a) periodically reviewing the Internal Audit Charter and making recommendations to the Board;
- (b) reviewing and approving the audit plan, including significant risk exposures identified by the internal auditor and management;
- (c) reviewing and discussing with the internal auditors and management the results of any internal audits;
- (d) reviewing and discussing with the internal auditors any problems or difficulties encountered by them in the course of their audit work and management's response (including any restrictions on the scope of activities or access to requested information and any significant disagreements with management);
- (e) appointing and replacing the internal auditor;
- (f) reviewing and assessing the performance of the internal auditor;
- (g) ensure the Committee is kept informed of emerging trends and successful practices in internal auditing; and
- (h) confirm there is effective and efficient coordination of activities between internal and external auditors.

(4) **Reviewing and Approving and Recommending to the Board for Approval the Financial Statements, MD&A and Interim Reports of the Corporation**

The Committee shall review and approve, and where required recommend to the Board for approval, the financial statements, management's discussion and analysis of financial condition and results of operations (*MD&A*) and interim financial reports of the Corporation, annual information form (AIF) and other public disclosure of financial information extracted from the financial statements of the Corporation with particular focus on:

- (a) the quality and appropriateness of accounting and reporting practices and principles and any changes thereto;

- (b) major estimates or judgments, including alternative treatments of financial information discussed by management and the external auditors, the results of such discussions and the treatment preferred by the external auditors;
- (c) material financial risks;
- (d) material transactions;
- (e) material adjustments;
- (f) compliance with loan agreements;
- (g) material off-balance sheet transactions and structures;
- (h) compliance with accounting standards;
- (i) compliance with legal and regulatory requirements; and
- (j) disagreements with management.

(5) **Overseeing Internal Financial Control Structure and Financial Risk Management Systems**

The Committee shall be responsible for overseeing the internal financial control structure and financial risk management systems of the Corporation, including:

- (a) reviewing and discussing with management and the external auditors the quality and adequacy of internal control over financial reporting structures of the Corporation, including any major deficiencies or weakness and the steps taken by management to rectify these deficiencies or weaknesses;
- (b) reviewing and discussing with management, the internal auditor and the external auditors the risk assessment and risk management policies of the Corporation, the major financial risk exposures of the Corporation and the steps taken by management to monitor and control these exposures;
- (c) reviewing and discussing with the Chief Executive Officer and the Chief Financial Officer of the Corporation the procedures undertaken by them in connection with the certifications required to be given by them in connection with annual and other filings required to be made by the Corporation under applicable securities laws; and
- (d) periodically reviewing the Treasury Policy and signing policies for the Corporation and its subsidiaries, making recommendations to the Board in respect of such policies and reviewing performance under those policies with Management.

(6) **Establish and Review Certain Procedures**

The Committee shall establish adequate policies and procedures, or require that adequate policies and procedures are established, with respect to the following and shall annually assess the adequacy of these procedures:

- (a) the review of the public disclosure of financial information extracted from the financial statements of the Corporation;
- (b) the receipt, retention and treatment of complaints received by the Corporation with respect to accounting, internal accounting controls or auditing matters; and

- (c) the confidential, anonymous submission by employees of the Corporation of concerns regarding questionable accounting or auditing matters.

4. Authority

- (1) The Committee is authorized to carry out its responsibilities as set out in this Charter and to make recommendations to the Board arising there from.
- (2) The Committee may delegate by written policy to the Chair and the Chief Financial Officer of the Corporation (*CFO*) the authority, within specified limits, to authorize in advance all engagements of the external auditors to provide pre-approved services to the Corporation and its subsidiary entities. The Chair and the CFO shall report all engagements authorized by them to the Committee at its next meeting.
- (3) The Committee shall have direct and unrestricted access to the external and internal auditors, officers and employees and information and records of the Corporation.
- (4) The Committee is authorized to retain, and to set and pay the compensation of, independent legal counsel and other advisors if it considers this appropriate.
- (5) The Committee is authorized to invite officers and employees of the Corporation and outsiders with relevant experience and expertise to attend or participate in its meetings and proceedings if it considers this appropriate.
- (6) The external auditors shall have direct and unrestricted access to the Committee and shall report directly to the Committee.
- (7) The Corporation shall pay directly or reimburse the Committee for the expenses incurred by the Committee in carrying out its responsibilities.

5. Meetings and Proceedings

- (1) The Committee shall meet at least four times each year.
- (2) Any Member or the Secretary may call a meeting of the Committee. The external auditors or the CFO may ask a Member to call a meeting of the Committee.
- (3) The Chair shall approve the agenda of each meeting of the Committee, including input from the officers and employees of the Corporation, external auditors, other Members and other directors of the Corporation as appropriate. Meetings will include presentations by management or professional advisors and consultants when appropriate and allow sufficient time to permit a full and open discussion of agenda items.
- (4) Unless waived by all Members, a notice of each meeting of the Committee confirming the date, time, place and agenda of the meeting, together with any supporting materials, shall be forwarded to each Member at least three days before the date of the meeting.
- (5) The quorum for each meeting of the Committee is two Members. In the absence of the Chair, the other Members may appoint one of their number as chair of a meeting. The Chair of a meeting shall not have a second or casting vote.
- (6) The Chair or a delegate of the Chair shall report to the Board following each meeting of the Committee.
- (7) The Secretary or a delegate of the Secretary shall keep minutes of all meetings of the Committee, including all resolutions passed by the Committee. Minutes of all meetings shall be distributed to the Members. The

minutes shall be available for review by the other directors of the Corporation after approval thereof by the Committee.

- (8) An individual who is not a Member may be invited to attend a meeting of the Committee for all or part of the meeting. A standing invitation shall be given to the Chairman of the Board, the President and Chief Executive Officer of the Corporation, the CFO and the engagement partners of the external auditors except where the meeting, or part of the meeting, is for Members only or a private session with the external auditors.
- (9) The Committee shall meet regularly alone and in private sessions with the external auditors and management of the Corporation to facilitate full communication.

6. Review

- (1) This Charter shall be reviewed by the Corporate Governance Committee of the Corporation every 2 years and any recommended changes shall be referred first to the Audit Committee for review and comment and second, after consideration of the input from the Audit Committee, to the Board of the Corporation for consideration and disposition.