TORONTO HYDRO Corporation

CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2013

INTERIM CONSOLIDATED BALANCE SHEETS

[in thousands of Canadian dollars, unaudited]

	As at June 30, 2013 $	As at December 31, 2012 $
ASSETS		
Current		
Cash and cash equivalents	**33,474**	76,592
Accounts receivable, net of allowance for doubtful accounts *[note 11[b]]*	**185,278**	175,159
Unbilled revenue *[note 11[b]]*	**299,731**	278,086
Income tax receivable	**8,250**	7,879
Inventories	**8,293**	7,555
Regulatory assets *[note 7]*	**-**	1,658
Other assets	**7,683**	5,363
Total current assets	**542,709**	552,292
Property, plant and equipment, net *[note 5]*	**2,574,872**	2,526,666
Intangible assets, net *[note 6]*	**165,420**	134,080
Regulatory assets *[note 7]*	**185,177**	119,556
Other assets	**14,572**	12,442
Deferred income tax assets	**172,519**	194,318
Total assets	**3,655,269**	3,539,354
LIABILITIES AND SHAREHOLDER'S EQUITY		
Current		
Bank indebtedness *[note 8]*	**100,000**	-
Accounts payable and accrued liabilities *[note 11[b]]*	**413,991**	383,371
Restructuring accrual	**4,931**	11,954
Customers' advance deposits	**37,621**	40,048
Deferred conservation credit	**21,324**	20,316
Debentures *[note 9]*	**-**	470,050
Post-retirement benefits *[note 10]*	**8,970**	9,925
Other liabilities *[note 15]*	**2,052**	1,850
Regulatory liabilities *[note 7]*	**5,962**	-
Total current liabilities	**594,851**	937,514
Customers' advance deposits	**6,835**	6,790
Debentures *[note 9]*	**1,449,306**	999,540
Post-retirement benefits *[note 10]*	**247,921**	243,965
Other liabilities *[note 15]*	**9,152**	9,385
Regulatory liabilities *[note 7]*	**176,069**	196,809
Asset retirement obligations	**5,222**	5,079
Total liabilities	**2,489,356**	2,399,082
Commitments, contingencies and subsequent events *[notes 2, 15 and 16]*		
Shareholder's equity		
Share capital *[note 13]*	**567,817**	567,817
Retained earnings	**598,096**	572,455
Total shareholder's equity	**1,165,913**	1,140,272
Total liabilities and shareholder's equity	**3,655,269**	3,539,354

The accompanying notes are an integral part of the interim consolidated financial statements.

INTERIM CONSOLIDATED STATEMENTS OF NET INCOME AND COMPREHENSIVE INCOME

[in thousands of Canadian dollars, except for per share amounts, unaudited]

	Three months ended June 30, 2013 $	Three months ended June 30, 2012 $	Six months ended June 30, 2013 $	Six months ended June 30, 2012 $
Revenues	**792,905**	709,700	**1,549,785**	1,409,360
Costs				
Purchased power	**645,915**	565,053	**1,258,180**	1,127,483
Operating expenses	**62,711**	49,646	**132,819**	117,828
Depreciation and amortization	**35,308**	35,132	**70,022**	70,560
	743,934	649,831	**1,461,021**	1,315,871
Income before the following:	**48,971**	59,869	**88,764**	93,489
Net financing charges *[note 17]*	**(17,317)**	(18,170)	**(35,911)**	(36,820)
Restructuring costs	**-**	-	**-**	(27,796)
Income before income taxes	**31,654**	41,699	**52,853**	28,873
Income tax expense (recovery) *[note 18]*	**(5,901)**	161	**(3,283)**	161
Net income and comprehensive income for the period	**37,555**	41,538	**56,136**	28,712
Basic and fully diluted net income per share *[note 13]*	**37,555**	41,538	**56,136**	28,712

INTERIM CONSOLIDATED STATEMENTS OF SHAREHOLDER'S EQUITY

[in thousands of Canadian dollars, unaudited]

	Three months ended June 30, 2013 $	Three months ended June 30, 2012 $	Six months ended June 30, 2013 $	Six months ended June 30, 2012 $
Share capital ***[note 13]***	**567,817**	567,817	**567,817**	567,817
Retained earnings, beginning of period	**567,041**	492,639	**572,455**	534,431
Net income for the period	**37,555**	41,538	**56,136**	28,712
Dividends *[notes 13 and 14]*	**(6,500)**	(6,000)	**(30,495)**	(34,966)
Retained earnings, end of period	**598,096**	528,177	**598,096**	528,177
Total shareholder's equity	**1,165,913**	1,095,994	**1,165,913**	1,095,994

The accompanying notes are an integral part of the interim consolidated financial statements.

TORONTO HYDRO Corporation

INTERIM CONSOLIDATED STATEMENTS OF CASH FLOWS

[in thousands of Canadian dollars, unaudited]

	Three months ended June 30,		Six months ended June 30,	
	2013	2012	**2013**	2012
	$	$	**$**	$
OPERATING ACTIVITIES				
Net income for the period	**37,555**	41,538	**56,136**	28,712
Adjustments for non-cash items				
Depreciation and amortization	**35,308**	35,132	**70,022**	70,560
Change in other non-current assets	**51**	51	**119**	330
Change in other non-current liabilities	**277**	1,376	**508**	164
Restructuring accrual	**-**	(3,608)	**-**	4,414
Post-retirement benefits	**1,603**	2,177	**3,001**	4,354
Deferred income taxes	**(835)**	534	**(705)**	546
Changes in non-cash working capital balances *[note 19]*	**(36,240)**	(48,300)	**(10,441)**	(23,796)
Net cash provided by operating activities	**37,719**	28,900	**118,640**	85,284
INVESTING ACTIVITIES				
Purchase of property, plant and equipment *[note 5]*	**(77,391)**	(45,760)	**(146,435)**	(89,061)
Purchase of intangible assets *[note 6]*	**(27,711)**	(4,132)	**(40,390)**	(26,209)
Proceeds from investments	**-**	-	**-**	34,000
Net change in regulatory assets and liabilities *[note 7]*	**(13,169)**	13,951	**(18,769)**	(3,910)
Proceeds on disposals of property, plant and equipment	**478**	232	**680**	733
Net cash used in investing activities	**(117,793)**	(35,709)	**(204,914)**	(84,447)
FINANCING ACTIVITIES				
Increase in bank indebtedness *[note 8]*	**100,000**	-	**100,000**	-
Dividends paid *[notes 13 and 14]*	**(6,500)**	(6,000)	**(30,495)**	(34,966)
Increase (decrease) in customers' advance deposits	**(602)**	957	**(2,382)**	1,603
Proceeds from debentures *[note 9]*	**449,741**	-	**449,741**	-
Increase in debt issuance costs *[note 9]*	**(2,694)**	-	**(2,694)**	-
Repayment of debentures *[note 9]*	**(470,057)**	-	**(470,057)**	-
Repayment of capital lease liability	**(484)**	(449)	**(957)**	(899)
Net cash provided by (used in) financing activities	**69,404**	(5,492)	**43,156**	(34,262)
Net decrease in cash and cash equivalents during the period	**(10,670)**	(12,301)	**(43,118)**	(33,425)
Cash and cash equivalents, beginning of period	**44,144**	133,132	**76,592**	154,256
Cash and cash equivalents, end of period	**33,474**	120,831	**33,474**	120,831
Supplementary cash flow information				
Total interest paid	**37,682**	37,561	**37,936**	37,824
Total income taxes paid (recovered)	**-**	2,736	**(3,106)**	6,066

The accompanying notes are an integral part of the interim consolidated financial statements.

1. INCORPORATION

On June 23, 1999, Toronto Hydro Corporation [the "Corporation"] was incorporated under the *Business Corporations Act* (Ontario), and is wholly-owned by the City of Toronto [the "City"]. The incorporation was required in accordance with the provincial government's *Electricity Act, 1998* (Ontario).

The Corporation supervises the operations and provides corporate, management services and strategic direction to two subsidiaries incorporated under the *Business Corporations Act* (Ontario) and wholly-owned by the Corporation:

[i] Toronto Hydro-Electric System Limited ["LDC"] (incorporated June 23, 1999) – distributes electricity to customers located in the City and is subject to rate regulation. LDC is also engaged in the delivery of conservation and demand management activities; and

[ii] Toronto Hydro Energy Services Inc. (incorporated June 23, 1999) – provides street lighting services.

The principal business of the Corporation and its subsidiaries is the distribution of electricity by LDC.

2. BASIS OF PRESENTATION

These unaudited interim consolidated financial statements of the Corporation have been prepared in accordance with United States ["US"] Generally Accepted Accounting Principles ["GAAP"] with respect to the preparation of interim financial information, and are presented in Canadian dollars. The disclosures in these statements do not conform in all respects to the requirements of US GAAP for annual consolidated financial statements. These unaudited interim consolidated financial statements follow the same accounting policies and methods of application as the audited consolidated financial statements of the Corporation for the year ended December 31, 2012, except as disclosed in note 4, and should be read in conjunction with the annual consolidated financial statements. The Ontario Securities Commission granted an exemption to allow the Corporation to file financial statements under US GAAP for the years commencing on or after January 1, 2012 but before January 1, 2015.

The Corporation has evaluated the events and transactions occurring after the interim consolidated balance sheet date through August 15, 2013 when the Corporation's interim consolidated financial statements were available to be issued after the approval by the Corporation's Board of Directors, and identified the events and transactions which required recognition in the interim consolidated financial statements and/or disclosure in the notes to the interim consolidated financial statements *[notes 3, 7, and 13]*.

3. REGULATION

Regulatory developments in Ontario's electricity industry, including current and possible future consultations between the Ontario Energy Board [the "OEB"] and interested stakeholders, may affect LDC's electricity distribution rates and other permitted recoveries in the future.

Electricity Distribution Rates

On May 10, 2012, LDC filed an application for electricity distribution rates for 2012, 2013, and 2014 using the Incentive Regulation Mechanism ["IRM"] framework, including the filing of an Incremental Capital Module ["ICM"] application [the "IRM/ICM Application"].

On October 31, 2012, LDC submitted an update to its IRM/ICM Application modifying the requested capital expenditures for 2012 and 2013 to $283,000,000 and $579,100,000, respectively, and requesting that consideration for 2014 be deferred to a second phase of the proceeding, once LDC had received a decision from the OEB in respect of phase one. On November 3, 2012, the OEB accepted LDC's request for a two-phase proceeding: phase one comprising LDC's 2012 and 2013 work program proposals and phase two comprising LDC's 2014 work program proposal.

On April 2, 2013, the OEB issued a partial decision and order for phase one of the proceeding comprising LDC's 2012 and 2013 work program proposals. The OEB's decision determined that eligible capital funding under the ICM framework was to be calculated on an in-service basis. This correlates to the approval of capital expenditures amounting to $203,330,000 for 2012 and $484,220,000 for 2013. New rates became effective June 1, 2013. In 2015, LDC will be allowed to seek recovery for capital spent in 2012 and 2013 that has not yet been approved by the OEB in the current ICM decision due to the standard operation of the regulatory model.

On August 1, 2013, LDC filed an application with the OEB requesting approval for the disposition of balances in its smart meter deferral account related to smart meter installations in 2008, 2009 and 2010. In the application, LDC requested two new rate riders effective May 1, 2014. The first rate rider relates to the recovery of $23,927,000, which represents the cumulative revenue requirement net of recoveries from an existing smart meter rate rider. This existing smart meter rate rider would be discontinued when the new rate riders become effective. The second rate rider relates to the recovery of $9,631,000, which represents the forecasted 2014 incremental revenue requirement until LDC may be permitted to transfer the smart meter assets out of regulatory assets. LDC expects to apply to the OEB for both the transfer of the 2008, 2009 and 2010 smart meter costs from regulatory assets to property, plant and equipment and intangible assets, and the transfer of the net book value of the stranded meters from property, plant and equipment to regulatory assets, at the time of its next scheduled rebasing in 2015.

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

a) *Property, plant and equipment*

Effective April 2, 2013, property, plant and equipment relating to eligible capital expenditures approved under the ICM framework for the 2012 and 2013 work program proposals are reclassified from construction in progress to regulatory assets once an asset is determined to be in-service, as directed by the OEB. The assets are then depreciated in the regulatory asset account at the estimated useful lives previously specified for property, plant and equipment. Corresponding ICM revenue is recognized based on in-service assets.

b) *Use of estimates*

The preparation of the Corporation's unaudited interim consolidated financial statements in accordance with US GAAP requires management to make estimates and assumptions which affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the interim consolidated financial statements, and the reported amounts of revenues and expenses for the period. The estimates are based on historical experience, current conditions and various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities as well as identifying and assessing the accounting treatment with respect to commitments and contingencies. Significant areas requiring the use of management estimates relate to unbilled revenue, regulatory assets and liabilities, environmental liabilities and asset retirement obligations, employee future benefits, income taxes (including deferred income taxes), and revenue recognition. Actual results could differ from those estimates, including changes as a result of future decisions made by the OEB, the Ministry of Energy of Ontario, or the Ministry of Finance of Ontario ["Ministry of Finance"].

[all tabular amounts in thousands of Canadian dollars, unaudited]

c) Adoption of New Accounting Pronouncements

In December 2011, the Financial Accounting Standards Board issued Accounting Standards Update ["ASU"] No. 2011-11, "Balance Sheet (Topic 210): *Disclosures about Offsetting Assets and Liabilities*" ["ASU 2011-11"]. The amendments require an entity to disclose both gross and net information about financial instruments and transactions eligible for offset in the consolidated balance sheets. ASU 2011-11 is effective for fiscal years, and interim periods within those years, beginning on or after January 1, 2013. Retrospective application is required. The ASU No. 2013-01, "Balance Sheet (Topic 210): *Clarifying the Scope of Disclosures about Offsetting Assets and Liabilities*", was issued in January 2013 to amend the scope of ASU 2011-11 to clarify that the disclosure requirements are limited to derivatives, repurchase and reverse repurchase agreements, and securities borrowing and lending transactions that are either offset in the consolidated balance sheets or subject to enforceable master netting arrangements or similar agreements. The adoption of these amendments did not impact the Corporation's consolidated balance sheets and related disclosures.

5. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment consist of the following:

	June 30 2013			**December 31 2012**		
	Cost $	**Accumulated depreciation $**	**Net book value $**	**Cost $**	**Accumulated depreciation $**	**Net book value $**
Land	**16,747**	**—**	**16,747**	16,747	—	16,747
Distribution lines	**3,032,419**	**1,517,627**	**1,514,792**	2,978,511	1,488,060	1,490,451
Transformers	**685,375**	**386,795**	**298,580**	672,981	377,900	295,081
Stations	**288,120**	**149,770**	**138,350**	286,229	145,601	140,628
Meters	**250,593**	**138,703**	**111,890**	243,152	133,789	109,363
Buildings	**165,606**	**72,915**	**92,691**	160,368	69,248	91,120
Rolling stock	**72,677**	**46,761**	**25,916**	73,239	43,834	29,405
Other capital assets	**73,155**	**49,674**	**23,481**	70,850	47,889	22,961
Equipment and tools	**46,387**	**35,002**	**11,385**	45,613	33,936	11,677
Computer hardware	**52,458**	**42,135**	**10,323**	50,511	40,003	10,508
Assets under capital lease	**13,866**	**3,945**	**9,921**	13,538	2,948	10,590
Communications	**32,642**	**27,556**	**5,086**	32,082	26,597	5,485
Construction in progress	**315,710**	**—**	**315,710**	292,650	—	292,650
	5,045,755	**2,470,883**	**2,574,872**	4,936,471	2,409,805	2,526,666

For the three months and the six months ended June 30, 2013, an Allowance for Funds Used During Construction ["AFUDC"] in the amount of $160,000 and $310,000 [three months and six months ended June 30, 2012 - $201,000 and $485,000] was capitalized to property, plant and equipment and credited to net financing charges.

As at June 30, 2013, the net book value of stranded meters related to the deployment of smart meters amounting to $16,423,000 [December 31, 2012 - $17,647,000] was included in property, plant and equipment. In the absence of rate regulation, property, plant and equipment would have been $16,423,000 lower as at June 30, 2013 [December 31, 2012 - $17,647,000 lower].

[all tabular amounts in thousands of Canadian dollars, unaudited]

For the three months and the six months ended June 30, 2013, capital contributions in the amount of $6,799,000 and $9,719,000 [three months and six months ended June 30, 2012 - $6,380,000 and $9,307,000] were credited to property, plant and equipment.

For the three months and the six months ended June 30, 2013, the Corporation recorded depreciation expense of $30,515,000 and $60,742,000 [three months and six months ended June 30, 2012 - $30,008,000 and $59,773,000] of which $499,000 and $997,000 [three months and six months ended June 30, 2012 - $491,000 and $1,010,000] related to assets under capital lease.

6. INTANGIBLE ASSETS

Intangible assets consist of the following:

	June 30 2013			December 31 2012		
	Cost $	Accumulated amortization $	Net book value $	Cost $	Accumulated amortization $	Net book value $
Computer software	**250,644**	**183,008**	**67,636**	242,254	174,410	67,844
Contributions	**22,240**	**2,627**	**19,613**	19,649	2,175	17,474
Software in development	**28,774**	**—**	**28,774**	14,210	—	14,210
Contributions for work in progress	**49,397**	**—**	**49,397**	34,552	—	34,552
	351,055	**185,635**	**165,420**	310,665	176,585	134,080

For the three months and the six months ended June 30, 2013, the Corporation acquired $27,711,000 and $40,390,000 of intangible assets [three months and six months ended June 30, 2012 - $4,132,000 and $26,209,000]. Contributions for work in progress relate to payments for connection projects to increase electricity distribution system capacity. All intangible assets are subject to amortization when they become available for use. Software in development and contributions for work in progress relate to assets not currently available for use and therefore are not amortized.

For the three months and the six months ended June 30, 2013, AFUDC in the amount of $389,000 and $734,000 [three months and six months ended June 30, 2012 - $374,000 and $643,000] was capitalized to intangible assets and credited to net financing charges.

For the three months and the six months ended June 30, 2013, the Corporation recorded amortization expense on intangible assets of $4,563,000 and $9,050,000 [three months and six months ended June 30, 2012 - $5,124,000 and $10,787,000].

[all tabular amounts in thousands of Canadian dollars, unaudited]

7. REGULATORY ASSETS AND LIABILITIES

Regulatory assets consist of the following:

	June 30 2013 $	December 31 2012 $
Post-retirement benefits	**60,482**	61,499
Smart meters	**52,663**	55,599
ICM	**37,461**	—
Settlement variances	**34,027**	1,071
Regulatory assets recovery account	**—**	2,466
Other	**544**	579
Total regulatory assets	**185,177**	121,214
Less: Current portion of regulatory assets	**—**	1,658
Long-term portion of regulatory assets	**185,177**	119,556

Regulatory liabilities consist of the following:

	June 30 2013 $	December 31 2012 $
Deferred income taxes	**170,772**	193,276
Regulatory assets recovery account	**7,701**	—
Income and other taxes variance account	**2,415**	2,398
Other	**1,143**	1,135
Total regulatory liabilities	**182,031**	196,809
Less: Current portion of regulatory liabilities	**5,962**	—
Long-term portion of regulatory liabilities	**176,069**	196,809

For the three months and the six months ended June 30, 2013, LDC disposed of approved regulatory assets amounting to $2,541,000 and $3,629,000 through permitted distribution rate adjustments [three months and six months ended June 30, 2012 - net regulatory liabilities of $2,185,000 and $11,033,000].

The regulatory assets and liabilities of the Corporation consist of the following:

a) Post-Retirement Benefits

This regulatory asset account relates to the expected future electricity distribution charges to customers arising from timing differences in the recognition of actuarial losses and prior service costs of other post-retirement benefits. In the absence of rate regulation, these amounts would be recorded in other comprehensive income and accumulated other comprehensive income. The amount is amortized over the same period as the corresponding actuarial losses and prior service costs. The period in which recovery is expected cannot be determined at this time.

b) Smart Meters

The smart meters regulatory asset account relates to Ontario's decision to install smart meters throughout Ontario. LDC substantially completed its smart meter project as at December 31, 2010. In connection with this initiative, the OEB ordered LDC to record all expenditures and related revenues from 2008 to 2010 to a regulatory asset account and allowed LDC to keep the net book value of the stranded meters in property, plant and equipment. Effective January 1, 2011, LDC has recorded smart meter costs in property, plant and equipment and intangible assets as a regular distribution activity as directed by the OEB. On August 1, 2013, LDC filed an application with the OEB requesting approval for the disposition of balances in its smart meter deferral account related to smart meter installations in 2008, 2009 and 2010 *[note 3]*.

As at June 30, 2013, smart meter capital expenditures, net of accumulated depreciation, totalling $49,752,000 were recorded to regulatory assets [December 31, 2012 - $52,865,000]. In the absence of rate regulation, property, plant and equipment and intangible assets would have been $47,950,000 and $1,802,000 higher, respectively, as at June 30, 2013 [December 31, 2012 - $50,234,000 and $2,631,000 higher, respectively].

For the three months and the six months ended June 30, 2013, smart meter depreciation expense of $1,546,000 and $3,113,000 were deferred [three months and six months ended June 30, 2012 - $1,591,000 and $3,181,000]. In the absence of rate regulation, for the three months and the six months ended June 30, 2013, depreciation expense would have been $1,546,000 and $3,113,000 higher [three months and six months ended June 30, 2012 - $1,591,000 and $3,181,000 higher].

For the three months and the six months ended June 30, 2013, smart meter customer revenues of $1,491,000 and $2,977,000 were deferred [three months and six months ended June 30, 2012 - $1,454,000 and $2,886,000]. In the absence of rate regulation, for the three months and the six months ended June 30, 2013, revenues would have been $1,491,000 and $2,977,000 higher [three months and six months ended June 30, 2012 - $1,454,000 and $2,886,000 higher].

c) ICM

The ICM regulatory asset account relates to the partial decision and order from the OEB for LDC's 2012 and 2013 work program proposals and the associated rate rider, which became effective June 1, 2013 *[note 3]*. As directed by the OEB, this account is comprised of the net book value of the eligible in-service capital expenditures under ICM, offset by the amount collected through the rate rider. This account is also adjusted by the amount recognized into revenues related to the eligible in-service capital expenditures.

For the three months and the six months ended June 30, 2013, eligible in-service capital expenditures of $37,698,000 [three months and six months ended June 30, 2012 - $nil] were reclassified from property, plant and equipment to regulatory assets. As a non-cash transaction, this has been excluded from the statement of cash flows. As at June 30, 2013, eligible in-service capital expenditures, net of accumulated depreciation, totalling $37,468,000, were recorded in regulatory assets [December 31, 2012 - $nil]. In the absence of rate regulation, property, plant and equipment would have been $37,468,000 higher as at June 30, 2013 [December 31, 2012 - $nil impact].

For the three months and the six months ended June 30, 2013, LDC recorded depreciation expense of $230,000 [three months and six months ended June 30, 2012 - $nil] related to the eligible in-service capital expenditures.

For the three months and the six months ended June 30, 2013, the revenues related to the eligible in-service capital expenditures were $1,767,000 [three months and six months ended June 30, 2012 - $nil].

d) Settlement Variances

This account is comprised of the variances between amounts charged by LDC to customers, based on regulated rates, and the corresponding cost of non-competitive electricity service incurred by LDC. The settlement variances relate primarily to service charges, non-competitive electricity charges and the global adjustment. Accordingly, LDC has deferred the variances between the costs incurred and the related recoveries in accordance with the criteria set out in the accounting principles prescribed by the OEB. The balance for settlement variances continues to be calculated and attracts carrying charges in accordance with the OEB's direction.

For the three months and the six months ended June 30, 2013, settlement variances included in the Regulatory Assets Recovery Account ["RARA"] were adjusted by $3,358,000 [three months and six months ended June 30, 2012 - $3,019,000 and $12,249,000 were disposed through rate adjustments].

e) Regulatory Assets Recovery Account

The RARA consists of balances of regulatory assets or regulatory liabilities approved for disposition by the OEB through rate riders. The RARA is subject to carrying charges following the OEB prescribed methodology and related rates.

On February 22, 2011, the OEB approved the disposition of the Late Payment Penalties Settlement regulatory asset of $7,526,000, over a 21-month period commencing on August 1, 2011 and ending on April 30, 2013.

On April 2, 2013, the OEB approved the disposition of net regulatory liabilities of $6,509,000, primarily consisting of Payments In Lieu of Corporate Taxes ["PILs"] regulatory variance accounts, over an 11-month period commencing on June 1, 2013 and ending on April 30, 2014.

f) Deferred Income Taxes

This regulatory liability account relates to the expected future electricity distribution rate reduction for customers arising from timing differences in the recognition of deferred income tax assets.

As at June 30, 2013, LDC recorded a deferred income tax asset and a corresponding regulatory liability of $170,772,000 [December 31, 2012 - $193,276,000] with respect to its rate-regulated activities that will be included in the rate-setting process.

g) Income and Other Taxes Variance Account

The income and other taxes variance regulatory liability account relates to the differences that have resulted from a legislative or regulatory change to the tax rates or rules assumed in the rate adjustment model. As at June 30, 2013, the balance in this account consisted of an over-recovery from customers of $2,415,000 [December 31, 2012 - $2,398,000].

8. CREDIT FACILITIES

The Corporation is a party to a revolving credit facility expiring on October 10, 2017 [“Revolving Credit Facility”], pursuant to which the Corporation may borrow up to $600,000,000, of which up to $210,000,000 is available in the form of letters of credit. The Corporation’s Revolving Credit Facility also limits the debt to capitalization ratio to a maximum of 75%. As at June 30, 2013, the Corporation was in compliance with all covenants included in its Revolving Credit Facility.

Additionally, the Corporation is a party to:

- a demand facility with a Canadian chartered bank for $75,000,000 for the purpose of issuing letters of credit mainly to support LDC’s prudential requirements with the Independent Electricity System Operator [“Prudential Facility”]; and
- a demand facility with a second Canadian chartered bank for $20,000,000 for the purpose of working capital management [“Working Capital Facility”].

As at June 30, 2013, $100,000,000 had been drawn under the Revolving Credit Facility and no amounts had been drawn under the Working Capital Facility [December 31, 2012 - $nil]. As at June 30, 2013, $49,775,000 had been drawn on the Prudential Facility [December 31, 2012 - $49,227,000]. For the three months and the six months ended June 30, 2013, the average outstanding borrowings on the Corporation’s Revolving Credit Facility were $33,754,000 and $20,822,000 with a weighted average interest rate of 2.54% and 2.63%.

9. DEBENTURES

On April 9, 2013, the Corporation issued $250,000,000 of 2.91% senior unsecured debentures due April 10, 2023 [“Series 8”] and $200,000,000 of 3.96% senior unsecured debentures due April 9, 2063 [“Series 9”]. The Series 8 and Series 9 debentures bear interest payable semi-annually in arrears and contain covenants which, subject to certain exceptions, restrict the ability of the Corporation and LDC to create security interests, incur additional indebtedness or dispose of all or substantially all of their assets. The Corporation may redeem all or part of the Series 8 and Series 9 debentures prior to maturity at a price equal to the greater of the Canada Yield Price (determined in accordance with the terms of the debentures) and par, plus accrued and unpaid interest to the date fixed for redemption. The net proceeds of the debentures were used to repay the Corporation’s Series 1 and Series 5 debentures which matured on May 7, 2013 and May 6, 2013, respectively. Debt issuance costs of $2,694,000 relating to the Series 8 and Series 9 debentures were deferred as other assets in the period.

10. EMPLOYEE FUTURE BENEFITS

a) Pension

The Corporation provides a pension plan for its full-time employees through the Ontario Municipal Employees Retirement System. For the three months and the six months ended June 30, 2013, the Corporation’s contributions were $4,126,000 and $9,855,000 [three months and six months ended June 30, 2012 - $3,703,000 and $8,888,000].

[all tabular amounts in thousands of Canadian dollars, unaudited]

b) *Post-retirement benefits other than pension*

The components of net periodic benefit cost are:

	Three months ended June 30		Six months ended June 30	
	2013 $	2012 $	2013 $	2012 $
Service cost	**1,439**	1,288	**2,674**	2,576
Interest cost	**2,697**	2,915	**5,393**	5,829
Amortization of net actuarial loss	**506**	761	**1,013**	1,523
Amortization of prior service cost	**2**	267	**4**	533
Net periodic benefit cost	**4,644**	5,231	**9,084**	10,461
Capitalized as part of property, plant and equipment	**1,665**	1,875	**3,070**	3,409
Charged to operations	**2,979**	3,356	**6,014**	7,052

11. FINANCIAL INSTRUMENTS

a) *Recognition and measurement*

As at June 30, 2013 and December 31, 2012, the fair values of cash and cash equivalents, net accounts receivable, unbilled revenue, and accounts payable and accrued liabilities approximate their carrying values due to the short maturity of these instruments. The fair values of customers' advance deposits approximate their carrying values taking into account interest accrued on the outstanding balance. Obligations under capital lease are measured based on a discounted cash flow analysis and approximate the carrying value as management believes that the fixed interest rates are representative of current market rates.

The fair values of the debentures are calculated by discounting the related cash flows at the estimated yield to maturity of similar debt instruments, and are included in Level 2 of the fair value hierarchy. As at June 30, 2013, the fair values of the Corporation's debentures (including the current portion) were determined to be approximately $1,507,088,000 [December 31, 2012 - $1,615,860,000], with carrying values of $1,449,306,000 [December 31, 2012 - $1,469,590,000].

b) *Financial Risks*

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

The Corporation is exposed to a variety of financial risks, particularly credit risk, interest rate risk and liquidity risk.

Credit risk

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

[all tabular amounts in thousands of Canadian dollars, unaudited]

The Corporation's credit risk associated with accounts receivable is primarily related to electricity bill payments from LDC customers. LDC has approximately 723,000 customers, the majority of which are residential. LDC obtains security instruments from certain customers in accordance with direction provided by the OEB. As at June 30, 2013, LDC held security deposits in the amount of $44,456,000 [December 31, 2012 - $46,838,000], of which $22,400,000 [December 31, 2012 - $25,666,000] were related to security deposits on Offers to Connect to guarantee the payment of additional costs relating to expansion projects.

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

	June 30 2013 $	December 31 2012 $
Unbilled revenue	**299,731**	278,086
Accounts receivable		
Outstanding for not more than 30 days	**157,402**	153,513
Outstanding for more than 30 days and not more than 120 days	**24,130**	18,231
Outstanding for more than 120 days	**13,839**	14,113
Less: Allowance for doubtful accounts	**(10,093)**	(10,698)
Total accounts receivable, net	**185,278**	175,159
Total accounts receivable and unbilled revenue	**485,009**	453,245

Unbilled revenue represents amounts for which the Corporation has a contractual right to receive cash through future billings and are unbilled at period-end. Unbilled revenue is considered current and no allowance for doubtful accounts had been provided as at June 30, 2013 and December 31, 2012.

As at June 30, 2013, there were no significant concentrations of credit risk with respect to any customer. The credit risk related to cash and cash equivalents is mitigated by the Corporation's treasury policies on assessing and monitoring the credit exposures of counterparties. The Corporation's maximum exposure to credit risk is approximately equal to the carrying value of its financial assets.

Interest rate risk

The Corporation is exposed to short-term interest rate risk on the net of cash and cash equivalents, short-term borrowings under its Revolving Credit Facility and Working Capital Facility *[note 8]* and customers' advance deposits. The Corporation attempts to minimize interest rate risk by reducing its exposure to floating rate instruments, while ensuring that all payment obligations are met on an ongoing basis.

As at June 30, 2013, the Corporation was exposed to interest rate risk predominately from short-term borrowings under its Revolving Credit Facility, while most of its remaining obligations were either non-interest bearing or bear fixed interest rates, and its financial assets were predominately short-term in nature and mostly non-interest bearing. The Corporation estimates that a 100 basis point increase (decrease) in short-term interest rates, with all other variables held constant, would result in an increase (decrease) of approximately $1,110,000 to annual net financing charges.

Liquidity risk

The Corporation is exposed to liquidity risk related to its ability to fund its obligations as they become due. The Corporation monitors and manages its liquidity risk to ensure access to sufficient funds to meet operational and investing requirements. The Corporation has access to credit facilities and debt capital markets and monitors cash balances daily. The Corporation's objective is to ensure that sufficient liquidity is on hand to meet obligations as they fall due while minimizing net financing charges. Liquidity risks associated with financial commitments are as follows:

[all tabular amounts in thousands of Canadian dollars, unaudited]

June 30, 2013						
	Due within 1 year $	**Due within 2 years $**	**Due within 3 years $**	**Due within 4 years $**	**Due within 5 years $**	**Due after 5 years $**
Financial liabilities						
Bank indebtedness	**100,000**	—	—	—	—	—
Accounts payable and accrued liabilities [(1)]	**413,991**	—	—	—	—	—
Obligations under capital lease	**2,535**	**2,523**	**2,514**	**2,509**	**2,509**	—
Senior unsecured debentures						
Series 2 – 5.15% due November 14, 2017	—	—	—	—	**250,000**	—
Series 3 – 4.49% due November 12, 2019	—	—	—	—	—	**250,000**
Series 6 – 5.54% due May 21, 2040	—	—	—	—	—	**200,000**
Series 7 – 3.54% due November 18, 2021	—	—	—	—	—	**300,000**
Series 8 – 2.91% due April 10, 2023	—	—	—	—	—	**250,000**
Series 9 – 3.96% due April 9, 2063	—	—	—	—	—	**200,000**
Interest payments on debentures	**61,015**	**60,995**	**60,995**	**60,995**	**54,558**	**690,543**
	577,541	**63,518**	**63,509**	**63,504**	**307,067**	**1,890,543**

(1) As at June 30, 2013, amount included $9,109,000 of accrued interest on debentures.

Hedging and Derivative risk

As at June 30, 2013 and December 31, 2012, the Corporation had not entered into any hedging or derivative financial instruments.

Foreign exchange risk

As at June 30, 2013, the Corporation had limited exposure to the changing values of foreign currencies. While the Corporation purchases goods and services which are payable in US dollars, and purchases US currency to meet the related payables commitments when required, the impact of these transactions is not material to the interim consolidated financial statements.

12. FINANCIAL ASSISTANCE

The City has authorized the Corporation to provide financial assistance to its subsidiaries, and LDC to provide financial assistance to other subsidiaries of the Corporation, in the form of guarantees, letters of credit, direct loans or otherwise, for the purpose of enabling them to carry on their businesses, with financial assistance provided to subsidiaries other than LDC not to exceed an aggregate amount of $500,000,000.

As at June 30, 2013, the Corporation had drawn letters of credit in the amount of $49,775,000 [December 31, 2012 - $49,227,000] *[note 8]* on its Prudential Facility in respect of the operations of LDC.

[all tabular amounts in thousands of Canadian dollars, unaudited]

13. SHARE CAPITAL

Share capital consists of the following:

	June 30 2013 $	December 31 2012 $
Authorized		
The authorized share capital of the Corporation consists of an unlimited number of common shares		
Issued and outstanding		
1,000 common shares	**567,817**	567,817

The weighted daily average number of shares outstanding for the three months and the six months ended June 30, 2013 was 1,000 [three months and six months ended June 30, 2012 - 1,000]. Basic and fully diluted net income per share was determined by dividing the net income for the period by the weighted daily average number of shares outstanding.

Dividends

On February 28, 2013, the Board of Directors of the Corporation declared dividends in the amount of $23,995,000. The dividends were comprised of $17,995,000 with respect to net income for the year ended December 31, 2012, which was paid to the City on March 8, 2013, and $6,000,000 with respect to the first quarter of 2013, which was paid to the City on March 28, 2013.

On May 16, 2013, the Board of Directors of the Corporation declared a dividend in the amount of $6,500,000 with respect to the second quarter of 2013, which was paid to the City on June 28, 2013.

On August 15, 2013, the Board of Directors of the Corporation declared a dividend in the amount of $6,250,000 with respect to the third quarter of 2013. The dividend is payable on September 30, 2013.

14. RELATED PARTIES

For the Corporation, transactions with related parties include transactions with the City. All transactions with the City are conducted at prevailing market prices and normal trade terms.

Revenues include amounts charged to the City primarily for electricity, street lighting and ancillary services. Operating expenses and capital expenditures include amounts charged by the City for purchased road cut repairs, property taxes and other services. Dividends are paid to the City *[note 13]*.

Accounts receivable include receivables from the City primarily for electricity, street lighting and ancillary services. Unbilled revenue includes receivables from the City related to the provision of electricity and other services provided and not yet billed. Other assets include amounts primarily for prepaid land leases from the City. Accounts payable and accrued liabilities include amounts payable to the City related to road cut repairs and other services, as well as amounts received from the City for the construction of electricity distribution assets. Advance deposits include amounts received from the City for future expansion projects.

[all tabular amounts in thousands of Canadian dollars, unaudited]

15. COMMITMENTS

Future capital commitments and operating lease obligations

As at June 30, 2013, the future minimum annual lease payments under property operating leases and future commitments with remaining terms from one to five years and thereafter were as follows:

	Future capital commitments [3] $	Operating lease obligations and other $
2013 [1]	**27,396**	**3,215**
2014	**52,418**	**6,825**
2015	**2,621**	**6,336**
2016	**—**	**6,047**
2017	**—**	**2,294**
Thereafter	**—**	**—**
Total amount of future minimum payments [2]	**82,435**	**24,717**

(1) The amount disclosed represents the balance due over the period from July 1, 2013 to December 31, 2013.

(2) Refer to note 11 for repayments of senior unsecured debentures and bank indebtedness excluded from the table above.

(3) Reflect capital commitments for construction services and estimated capital contributions, with the majority related to the Copeland transformer station.

Capital lease obligations

As at June 30, 2013, the future minimum annual lease payments under capital leases with remaining lease terms from one to five years and thereafter were as follows:

	$
2013 [1]	**1,268**
2014	**2,528**
2015	**2,521**
2016	**2,509**
2017	**2,509**
Thereafter	**1,255**
Total amount of future minimum lease payments	**12,590**
Less: interest and executory costs	**1,386**
	11,204
Current portion included in Other liabilities	**2,052**
Long-term portion included in Other liabilities	**9,152**

(1) The amount disclosed represents the balance due over the period from July 1, 2013 to December 31, 2013.

16. CONTINGENCIES

a) Legal Proceedings

In the ordinary course of business, the Corporation is subject to various litigation and claims with customers, suppliers, former employees and other parties. On an ongoing basis, the Corporation assesses the likelihood of any adverse judgments or outcomes as well as potential ranges of probable costs and losses. A determination of the provision required, if any, for these contingencies is made after an analysis of each individual issue. The provision may change in the future due to new developments in each matter or changes in approach, such as a change in settlement strategy. The Corporation and its subsidiaries are subject to various legal actions that arise in the normal course of business and if damages were awarded under these actions, the Corporation and its subsidiaries would make a claim under their liability insurance which the Corporation believes would cover any damages which may become payable by the Corporation and its subsidiaries in connection with these actions.

2 Secord Avenue

An action was commenced against LDC in September 2008 in the Ontario Superior Court of Justice under the *Class Proceedings Act, 1992* (Ontario) seeking damages in the amount of $30,000,000 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 $51,000,000 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 $2,000,000 as a result of the fire at 2 Secord Avenue. A statement of defence and a 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 dated January 24, 2012, 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.

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, 1992* (Ontario) seeking damages in the amount of $30,000,000 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 $10,000,000 from LDC. Both actions are at a preliminary stage. The plaintiff has now scheduled its certification motion for September 2013. 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.

[all tabular amounts in thousands of Canadian dollars, unaudited]

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 $2,000,000 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.

b) 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 Municipal Electricity Utilities [“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 reviewed the balance of its PILs regulatory variance accounts and applied the guidelines provided by the OEB. LDC applied for disposition of the balance as part of its IRM/ICM Application filed on May 10, 2012. The OEB issued its decision and order on April 2, 2013 approving the disposition of the balance. The impact was recorded previously in the Corporation’s consolidated financial statements.

17. NET FINANCING CHARGES

Net financing charges consist of the following:

	Three months ended June 30		Six months ended June 30	
	2013 $	2012 $	2013 $	2012 $
Interest income	**957**	879	**1,366**	1,294
Interest expense				
Long-term debt	**(17,696)**	(18,630)	**(36,326)**	(37,260)
Other interest	**(578)**	(419)	**(951)**	(854)
	(17,317)	(18,170)	**(35,911)**	(36,820)

18. INCOME TAXES

The Corporation's effective tax rate for the three months and the six months ended June 30, 2013 was (18.64%) and (6.21%) [three months and six months ended June 30, 2012 - 0.39% and 0.56%]. The effective tax rate for the three months and the six months ended June 30, 2013 was lower than the three months and the six months ended June 30, 2012, primarily due to favourable resolution of issues identified in prior periods and related reassessments by the Ministry of Finance and recording deferred income taxes against regulatory assets and liabilities.

[all tabular amounts in thousands of Canadian dollars, unaudited]

19. NON-CASH WORKING CAPITAL BALANCES

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

	Three months ended June 30		Six months ended June 30	
	2013 $	2012 $	2013 $	2012 $
Accounts receivable	**8,578**	17,986	**(10,119)**	(9,111)
Unbilled revenue	**(25,406)**	(28,959)	**(21,645)**	(10,791)
Income tax receivable	**(4,896)**	(4,475)	**(371)**	(7,741)
Inventories	**(582)**	245	**(738)**	519
Other current assets	**(983)**	(112)	**(2,320)**	(1,580)
Accounts payable and accrued liabilities	**(5,278)**	(28,548)	**30,620**	(15,522)
Restructuring accrual	**(3,279)**	(1,790)	**(7,023)**	14,850
Deferred conservation credit	**(4,484)**	(2,572)	**1,008**	5,900
Other current liabilities	**90**	(75)	**147**	(320)
	(36,240)	(48,300)	**(10,441)**	(23,796)

20. SEASONAL OPERATIONS

The Corporation's quarterly 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. Consequently, the Corporation's revenues, all other things being equal, would tend to be higher in the first quarter as a result of higher energy consumption for winter heating, and in the third quarter due to air conditioning/cooling.