

1 **COST OF CAPITAL**

2

3 In accordance with Section 2.5 of the OEB Filing Requirements for Electricity Distribution
4 Rate Applications (July 12, 2018), this Schedule provides an overview of Toronto Hydro's
5 capital structure and financing plans for 2018, 2019 and 2020.

6

7 **1. CAPITAL STRUCTURE**

8 Toronto Hydro's sets its capital structure for ratemaking purposes in accordance with
9 the OEB's Cost of Capital guidelines issued December 11, 2009 in the Report of the
10 Board on the Cost of Capital for Ontario's Regulated Utilities (EB-2009-0084) ("Report of
11 the Board"). For Toronto Hydro, the debt to equity split for the test years is set at
12 60:40. The debt component in each year includes a deemed four percent short-term
13 debt component.

14

15 **2. FINANCING PLANS**

16 **2.1 Equity**

17 Toronto Hydro Corporation ("THC") is the sole shareholder of Toronto Hydro.

18

19 Toronto Hydro's forecasted Return on Equity ("ROE") for the 2020 Test Year is based on
20 the OEB's formulaic approach as outlined in the Report of the Board. For 2020, the ROE
21 calculation uses the March 2018 bond yield spread¹ and the Ten-Year Government of
22 Canada Bond Yield Forecast.²

¹ Difference between the average 30-Year A-Rated Canadian Utility bond yield from Bloomberg L.P. and the average 30-Year Government of Canada bond as published by the Bank of Canada

² The average of the forecast Ten-Year Government of Canada bond yield as at December 31, 2019 and September 30, 2020 from Bloomberg L.P.

1 Table 1, below, shows the projected ROE for 2020, and details of the derivation based
 2 on OEB's formulaic approach.

3

4 **Table 1: Return on Equity**

Year	Return on Equity
2020	8.82%

Return on Equity (ROE) forecast			
Initial ROE			9.75
Change in LCBF from September 2009			
LCBF		2.490	
Base LCBF		4.250	
Difference		-1.760	
	0.5 X Difference		-0.880
Change in A-rated Utility Bond Yield Spread from September 2009			
A-rated Utility Bond Spread (March 2018)		1.314	
Base A-rated Utility Bond Yield Spread		1.415	
Difference		-0.101	
	0.5 X Difference		-0.050
2020 Projected ROE based on March 2018 data			8.82

5

6 Toronto Hydro uses the 2020 ROE forecast for the purpose of calculating revenue
 7 requirement for the 2020 Test Year (Exhibit 6, Tab 1) and the derivation of the C-factor
 8 in the Custom Price Cap Index (Exhibit 1B, Tab 4, Schedule 1). To determine the final
 9 revenue requirement for 2020 and the updated C-factor, Toronto Hydro will rely on the
 10 ROE approved by the OEB in late 2019. Toronto Hydro proposes that the deemed ROE

1 throughout the 2020-2024 rate cycle be the rate that the OEB sets in late 2019 for 2020
2 rebasing applications.

3

4 **2.2 Financial Market Overview and Forecast**

5 2017 marked the second most active year on record (after 2013) in the Canadian bond
6 market with total corporate issuance of C\$120 billion (compared to C\$121 billion in
7 2013). Elevated issuance in 2017 was driven by positive investor sentiment combined
8 with low Government of Canada yields which provided attractive funding opportunities
9 for corporate issuers. In 2017, global markets experienced less volatility and
10 uncertainty, and the Canadian markets benefitted from strong demand from investors,
11 notable oversubscription of issuances and minimal new issue pricing concessions. This
12 trend was also seen in the utility sector.

13

14 In the third quarter of 2017, the Bank of Canada increased interest rates twice by 25
15 bps. A further 25 bps rate increase occurred in January 2018 following the release of
16 strong economic data in December 2017. In conjunction with the rate moves the
17 Government of Canada yields had risen with the 10 year yield by approximately 50 bps
18 relative to the lows in 2017. The expectation of further unwinding of monetary easing
19 policies by central banks and a return to rate normalization is an expected global trend
20 after years of low absolute interest rates. This expectation is being supported by
21 stronger economic growth conditions globally, and in the US by more recent tax reform.
22 Concerns that this trend may create tighter labour markets, higher wages and inflation
23 may continue to drive interest rates higher in 2018. Canadian rates are forecasted to
24 continue to rise, although at a slower pace than in the U.S.

1 Corporate credit spreads started to tighten in 2017, partially offsetting the rising
2 Government of Canada yields and allowing the absolute all-in yields of issuances to
3 remain relatively stable during the 2015-2017 period. This is evidenced by the all-in
4 coupon rate of 3.485 percent on the most recent THC's 30-year issuance on November
5 14, 2017, compared to an all-in coupon rate of 3.55 percent on THC's 30-year issuance
6 on March 16, 2015. From now until 2020, the assumption is for THC's 10-year bond
7 spread to be 111 basis points and 30-year bond spread to be 150 basis points. These
8 spreads are determined from the weekly indicative quotes provided by designated
9 banks in THC's revolving credit facility. These 10-year and 30-year spreads represent the
10 average of the quotes received over a historical period from January 2014 to March
11 2018.

13 **2.3 Medium and Long-Term Debt**

14 Toronto Hydro's issues debt at the THC level via medium term notes in the Canadian
15 public debt market. This requires THC to obtain and maintain credit ratings. As of July
16 1, 2018, THC's debentures were rated by DBRS and S&P as follows:

18 **Table 2: Rating of THC Debentures**

Rating Agency	Commercial Paper	Long-Term Debt
DBRS	R-1 (Low)	A Stable
Standard & Poor's ("S&P")	Not rated	A

19

20 The most recent ratings reports from DBRS and S&P are provided in (Exhibit 1C, Tab 3,
21 Schedule 8).

22

23 Toronto Hydro is assigned debt through promissory notes between the Toronto Hydro
24 and its parent, THC. The promissory notes are written on the same terms as the parent

1 debt as the borrowing is done on behalf of the corporation's affiliates. A fee of five
 2 basis points is charged for administration.

3

4 As of July 1st, 2018 Toronto Hydro had outstanding long-term debt in the amount of
 5 \$2.10 billion, as detailed in Table 3 below.

6

7 **Table 3: Long-Term Debt**

Description	Maturity	Outstanding Principal (\$)	Rate (%)
\$245M Prom Note	Nov. 12, 2019	245,057,739	4.54
\$300M Prom Note	Nov. 18, 2021	300,000,000	3.59
\$15M Prom Note	Jan. 1, 2022	15,000,000	3.32
\$250M Prom Note	Apr. 10, 2023	250,000,000	2.96
\$200M Prom Note	Aug. 25, 2026	200,000,000	2.572
\$200M Prom Note	May 21, 2040	200,000,000	5.59
\$200M Prom Note	Sept. 16, 2044	200,000,000	4.13
\$200M Prom Note	July 28, 2045	200,000,000	3.60
\$200M Prom Note	Feb. 28, 2048	200,000,000	3.535
\$200M Prom Note	Apr. 9, 2063	200,000,000	4.01
\$45M Prom Note	Apr. 9, 2063	45,000,000	3.988
\$45M Prom Note	Due on demand	45,000,000	4.16% (using deemed LTD rate)
Total		2,100,057,739	3.83

8

9 Forecasted new debt issuance for 2018-2020 is driven primarily by Toronto Hydro's
 10 capital plans and the repayment requirements of the maturing debt. Details of the
 11 forecasted debt issues for 2018-2020 are shown in Table 4.

1 **Table 4: Forecasted Long-Term Debt Issues**

Description	Issue Date	Term	Principal (\$)	Underlying Govt Bond Rate (%)	Corporate Spread Forecast (%)	Forecast Coupon Rate (%)
\$200M Prom Note (Series 14)	Feb 15, 2019	10 Years	200,000,000	2.20	1.16	3.36
\$250M Prom Note (Series 15)	Oct 15, 2019	30 Years	250,000,000	2.34	1.55	3.89
\$200M Prom Note (Series 16)	July 2, 2020	10 Years	200,000,000	2.33	1.16	3.49

2

3 Forecasted debt rates are based on the 10-Year and 30-Year Government of Canada
 4 Bond Yield Forecast (Bloomberg L.P.), when applicable, plus Toronto Hydro's estimate of
 5 corporate spreads at the time of issuance (inclusive of the five basis point
 6 administration fee).

7

8 Toronto Hydro applies the weighted average forecasted debt rates in its Cost of Capital,
 9 rather than applying the OEB's deemed debt rate, since this debt is based on market
 10 rates. Toronto Hydro proposes that the embedded debt rates set for 2020 apply
 11 throughout the 2020-2024 rate cycle.

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13 **2.4 Preferred Shares**

14 Toronto Hydro has no plans to issue any preferred shares over the 2018-2020 period.

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16 **2.5 Short-Term Debt**

17 Over the 2018-2020 period, Toronto Hydro plans to issue short-term debt in order to
 18 better match its liquidity needs in an effort to minimize net financing charges. THC

1 maintains a revolving credit facility and also has the ability to issue commercial paper
2 available for Toronto Hydro when short-term funds are required.

3

4 One-Month Banker's Acceptance rates (Bloomberg L.P.) are used as a proxy for Toronto
5 Hydro's forecast of its short-term debt rate, plus a five basis point administration fee.
6 The rates are outlined in Table 5 below. The deemed short-term debt weighting of 4
7 percent applies to Toronto Hydro's capital structure.

8

9 **Table 5: Short-Term Rates**

Year	Short Term Rates
2018	1.83%
2019	2.44%
2020	2.61%

OEB Appendix 2-OA Capital Structure and Cost of Capital

This table must be completed for the last Board approved year and the test year.

Year: 2015 OEB Approved

Line No.	Particulars	Capitalization Ratio		Cost Rate	Return
		(%)	(\$)	(%)	(\$)
	Debt				
1	Long-term Debt	56.00%	\$1,809,917,329	4.28%	\$77,464,462
2	Short-term Debt	4.00% (1)	\$129,279,809	1.38%	\$1,784,061
3	Total Debt	60.0%	\$1,939,197,139	4.09%	\$79,248,523
	Equity				
4	Common Equity	40.00%	\$1,292,798,092	9.30%	\$120,230,223
5	Preferred Shares	0.00%	\$ -		\$ -
6	Total Equity	40.0%	\$1,292,798,092	9.30%	\$120,230,223
7	Total	100.0%	\$3,231,995,231	6.17%	\$199,478,746

Notes

(1)

4.0% unless an applicant has proposed or been approved for a different amount.

OEB Appendix 2-OA Capital Structure and Cost of Capital

This table must be completed for the last Board approved year and the test year.

Year: 2020 Test Year

Line No.	Particulars	Capitalization Ratio		Cost Rate	Return
		(%)	(\$)	(%)	(\$)
	Debt				
1	Long-term Debt	56.00%	\$2,584,564,841	3.71%	\$95,887,356
2	Short-term Debt	4.00% (1)	\$184,611,774	2.61%	\$4,818,367
3	Total Debt	60.0%	\$2,769,176,616	3.64%	\$100,705,723
	Equity				
4	Common Equity	40.00%	\$1,846,117,744	8.82%	\$162,827,585
5	Preferred Shares	0.00%	\$ -		\$ -
6	Total Equity	40.0%	\$1,846,117,744	8.82%	\$162,827,585
7	Total	100.0%	\$4,615,294,360	5.71%	\$263,533,308

Notes

(1)

4.0% unless an applicant has proposed or been approved for a different amount.

OEB Appendix 2-OB Debt Instruments

This table must be completed for all required historical years, the bridge year and the test year.

Year 2019

Row	Description	Lender	Affiliated or Third-Party Debt?	Fixed or Variable-Rate?	Start Date	Term (years)	Principal (\$)	Rate (%) (Note 2)	Interest (\$) (Note 1)	Additional Comments, if any
1	2009 Serie	THC	Affiliated	Fixed Rate	12-Nov-09	10	\$ 245,057,739	4.54%	\$ 9,632,045	
2	2010 Serie	THC	Affiliated	Fixed Rate	20-May-10	30	\$ 200,000,000	5.59%	\$ 11,180,000	
3	2011 Serie	THC	Affiliated	Fixed Rate	18-Nov-11	10	\$ 300,000,000	3.59%	\$ 10,770,000	
4	2012 Prom	THC	Affiliated	Fixed Rate	1-Jan-12	10	\$ 15,000,000	3.32%	\$ 498,000	
5	2012 Prom	THC	Affiliated	Fixed Rate	1-Jan-12	N/A	\$ 45,000,000	4.16%	\$ 1,872,000	Payable on demand - deemed LTD rate for 2018
6	2013 Serie	THC	Affiliated	Fixed Rate	9-Apr-13	10	\$ 250,000,000	2.96%	\$ 7,400,000	
7	2013 Serie	THC	Affiliated	Fixed Rate	9-Apr-13	50	\$ 200,000,000	4.01%	\$ 8,020,000	
8	2014 Serie	THC	Affiliated	Fixed Rate	16-Sep-14	30	\$ 200,000,000	4.13%	\$ 8,260,000	
9	2015 Serie	THC	Affiliated	Fixed Rate	16-Mar-15	30	\$ 200,000,000	3.60%	\$ 7,200,000	
10	2013 Serie	THC	Affiliated	Fixed Rate	2-Sep-15	50	\$ 45,000,000	3.988%	\$ 1,794,600	
11	2016 Serie	THC	Affiliated	Fixed Rate	14-Jun-16	10	\$ 200,000,000	2.572%	\$ 5,144,000	
12	2017 Serie	THC	Affiliated	Fixed Rate	14-Nov-17	30	\$ 200,000,000	3.535%	\$ 7,070,000	
13	2019 Serie	THC	Affiliated	Fixed Rate	15-Feb-19	10	\$ 200,000,000	3.36%	\$ 5,891,507	Expected issu
14	2019 Serie	THC	Affiliated	Fixed Rate	15-Oct-19	30	\$ 250,000,000	3.89%	\$ 2,078,219	Expected issu
Total							\$ 2,295,926,700	3.78%	\$ 86,810,371	

Notes

- 1 If financing is in place only part of the year, calculate the pro-rated interest and input in the cell.
- 2 Input actual or deemed long-term debt rate in accordance with the guidelines in *The Report of the Board on the Cost of Capital for Ontario's*
- 3 Add more lines above row 12 if necessary.

OEB Appendix 2-OB Debt Instruments

This table must be completed for all required historical years, the bridge year and the test year.

Year 2020

Row	Description	Lender	Affiliated or Third-Party Debt?	Fixed or Variable-Rate?	Start Date	Term (years)	Principal (\$)	Rate (%) (Note 2)	Interest (\$) (Note 1)	Additional Comments, if any
1	2010 Serie	THC	Affiliated	Fixed Rate	20-May-10	30	\$ 200,000,000	5.59%	\$ 11,180,000	
2	2011 Serie	THC	Affiliated	Fixed Rate	18-Nov-11	10	\$ 300,000,000	3.59%	\$ 10,770,000	
3	2012 Prom	THC	Affiliated	Fixed Rate	1-Jan-12	10	\$ 15,000,000	3.32%	\$ 498,000	
4	2012 Prom	THC	Affiliated	Fixed Rate	1-Jan-12	N/A	\$ 45,000,000	4.16%	\$ 1,872,000	Payable on demand - deemed LTD rate for 2018
5	2013 Serie	THC	Affiliated	Fixed Rate	9-Apr-13	10	\$ 250,000,000	2.96%	\$ 7,400,000	
6	2013 Serie	THC	Affiliated	Fixed Rate	9-Apr-13	50	\$ 200,000,000	4.01%	\$ 8,020,000	
7	2014 Serie	THC	Affiliated	Fixed Rate	16-Sep-14	30	\$ 200,000,000	4.13%	\$ 8,260,000	
8	2015 Serie	THC	Affiliated	Fixed Rate	16-Mar-15	30	\$ 200,000,000	3.60%	\$ 7,200,000	
9	2013 Serie	THC	Affiliated	Fixed Rate	2-Sep-15	50	\$ 45,000,000	3.988%	\$ 1,794,600	
10	2016 Serie	THC	Affiliated	Fixed Rate	14-Jun-16	10	\$ 200,000,000	2.572%	\$ 5,144,000	
11	2017 Serie	THC	Affiliated	Fixed Rate	14-Nov-17	30	\$ 200,000,000	3.535%	\$ 7,070,000	
12	2019 Serie	THC	Affiliated	Fixed Rate	15-Feb-19	10	\$ 200,000,000	3.36%	\$ 6,720,000	Expected issuance
13	2019 Serie	THC	Affiliated	Fixed Rate	15-Oct-19	30	\$ 250,000,000	3.89%	\$ 9,725,000	Expected issuance
14	2020 Serie	THC	Affiliated	Fixed Rate	2-Jul-20	10	\$ 200,000,000	3.49%	\$ 3,499,562	Expected issuance
Total							\$ 2,405,273,973	3.71%	\$ 89,153,162	

Notes

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- 3 Add more lines above row 12 if necessary.