

Financial statements of

PowerStream Inc.

December 31, 2009

PowerStream Inc.

December 31, 2009

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Auditors' Report

To the Shareholders of
PowerStream Inc.

We have audited the balance sheet of PowerStream Inc. as at December 31, 2009 and the statements of earnings and comprehensive income and retained earnings and of cash flows for the year then ended. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Corporation as at December 31, 2009 and the results of its operations and its cash flows for the year then ended, in accordance with Canadian generally accepted accounting principles.

Deloitte & Touche LLP

Chartered Accountants
Licensed Public Accountants
March 31, 2010

PowerStream Inc.

Balance sheet

as at December 31, 2009

(in thousands of dollars)

	\$
Assets	
Current	
Cash	42,612
Accounts receivable, net of allowance (Note 21(b)(i))	73,633
Unbilled revenue	88,160
Income taxes recoverable	1,525
Inventories	3,869
Prepays and other	2,581
	212,380
Property, plant and equipment (Note 6)	601,764
Regulatory assets (Note 8(a))	26,433
Deferred charges, net of amortization of \$31	644
Intangibles (Note 7)	3,614
Future income tax assets (Note 8(b)(ii) and 23(b))	61,665
Goodwill	42,543
	949,043
Liabilities	
Current	
Accounts payable and accrued liabilities (Note 10)	111,405
Income taxes payable	5,034
Due to related parties (Note 11)	12,049
Short-term debt (Note 13)	40,000
Liability for subdivision development	3,375
	171,863
Long-term liabilities	
Bank term loan (Note 12(a))	50,000
Debentures payable (Note 12(b))	123,091
Notes payable (Note 12(c))	182,430
Regulatory liabilities (Note 8(b))	91,140
Customers' deposits (Note 14)	16,726
Employee future benefits (Note 15)	12,036
Liability for subdivision development	4,917
Construction deposits	23,172
Other liabilities	5,421
	508,933
Shareholders' equity	
Share capital (Note 17)	247,183
Retained earnings	21,064
	268,247
	949,043

Approved on behalf of the Board



Director



Director

PowerStream Inc.

Statement of earnings and comprehensive income and retained earnings year ended December 31, 2009

(in thousands of dollars)

	\$
Revenue	
Sale of energy	621,719
Distribution revenue	146,076
Other revenue	9,889
Total revenue	777,684
Cost of power purchased	621,719
	155,965
Operating expenses	62,601
Earnings before amortization, interest and income taxes	93,364
Amortization of property, plant and equipment and intangibles (net of \$2,582 charged to other accounts)	42,125
Net interest expense (Note 26)	21,614
Income before income taxes	29,625
Income tax expense (Note 23(a))	8,561
Net earnings and comprehensive income for the year	21,064

PowerStream Inc.

Statement of cash flows year ended December 31, 2009

(in thousands of dollars)

	\$
Operating activities	
Net earnings for the year	21,064
Adjustments to determine cash provided by operating activities	
Amortization of property, plant and equipment	42,006
Accretion of debentures payable	629
Amortization of intangibles	2,701
Amortization of deferred charges	31
Employee future benefits	923
Future income taxes	6,759
Decrease in regulatory assets/liabilities	(23,280)
Gain on disposal of property, plant and equipment	(218)
Net change in non-cash operating working capital (Note 24)	(25,478)
	<u>25,137</u>
Financing activities	
Decrease in liability for subdivisions development	(3,164)
Increase in due to related parties	2,150
Increase in long-term customers' deposits	1,223
Decrease in other liabilities	(47)
Obligations to predecessor shareholders (Note 18)	(31,082)
Increase in short-term debt	15,000
Construction deposits	23,172
	<u>7,252</u>
Investing activities	
Proceeds on disposal of property, plant and equipment	248
Purchase of intangibles	(6,314)
Expenditure on property, plant and equipment, net of contribution of capital construction	(67,419)
	<u>(73,485)</u>
Net decrease in cash during the year	(41,096)
Cash, beginning of year	83,708
Cash, end of year	<u>42,612</u>

Supplementary cash flow information (Note 25)

PowerStream Inc.

Notes to the financial statements

December 31, 2009

(in thousands of dollars)

1. Amalgamation

The City of Vaughan through its wholly owned subsidiary Vaughan Holdings Inc.; the Town of Markham through its wholly owned subsidiary, Markham Enterprises Corporation; and the City of Barrie, through its wholly owned subsidiary Barrie Hydro Holdings Inc; agreed to amalgamate PowerStream Inc. and Barrie Hydro Distribution Inc. on January 1, 2009 and continue as a corporation amalgamated under the laws of Ontario.

The amalgamated corporation retained the PowerStream Inc. corporate name.

Upon the amalgamation, shares of PowerStream Inc. held by Vaughan Holdings Inc. and Markham Enterprises Corporation, and shares of Barrie Hydro Distribution Inc. held by Barrie Hydro Holdings Inc. were exchanged for shares of the newly amalgamated Corporation, PowerStream Inc., as follows:

- (a) the common shares of PowerStream Inc. held by Vaughan Holdings Inc. were converted into 45,315 issued and fully-paid common shares of the amalgamated corporation;
- (b) the common shares of PowerStream Inc. held by Markham Enterprises Corporation were converted into 34,185 issued and fully-paid common shares of the amalgamated corporation; and
- (c) the common shares of Barrie Hydro Distribution Inc. held by Barrie Hydro Holdings Inc. were converted into 20,500 issued and fully-paid common shares of the amalgamated corporation.

The ultimate shareholders of the amalgamated PowerStream Inc., being the Corporation of the City of Vaughan, the Corporation of the Town of Markham, and the Corporation of the City of Barrie entered into a shareholders' agreement effective January 1, 2009.

The contribution of the net assets of the amalgamated corporation has been recorded at the carrying value of the predecessor Corporations as at January 1, 2009 in the balance sheet as follows:

	\$
Net assets contributed	
Current assets (including cash \$ 83,708)	234,816
Current liabilities	(155,350)
	79,466
Property, plant and equipment	566,180
Goodwill	42,543
Other assets	26,171
Long-term liabilities	(436,095)
Obligations to predecessor shareholders	(31,082)
	247,183
Consideration	
Shareholders' contributions	247,183
	247,183

PowerStream Inc.

Notes to the financial statements

December 31, 2009

(in thousands of dollars)

2. Description of the business

In these financial statements, PowerStream Inc. (the "Corporation") refers to both the newly amalgamated entity PowerStream Inc. and the predecessor corporation. The Corporation is owned by the Corporation of the City of Vaughan, through its wholly owned subsidiary, Vaughan Holdings Inc.; the Corporation of the Town of Markham, through its wholly owned subsidiary, Markham Enterprises Corporation; and City of Barrie, through its wholly owned subsidiary, Barrie Hydro Holdings Inc.

The principal activity of the Corporation is to distribute electricity in the service area of Alliston, Aurora, Barrie, Beeton, Bradford West Gwillimbury, Markham, Penetanguishene, Richmond Hill, Thornton, Tottenham and Vaughan in the Province of Ontario, under licenses issued by the Ontario Energy Board ("OEB"). The Corporation is regulated under the OEB and adjustments to the distribution rates require OEB approval.

3. Electricity industry regulation

The Ontario Energy Board Act, 1998 gave the OEB increased powers and responsibilities to regulate the electricity industry. These powers and responsibilities include the power to approve or fix rates for the transmission and distribution of electricity, the power to provide continued rate protection for rural and remote electricity customers and the responsibility for ensuring that distribution companies fulfill obligations to connect and service customers. The OEB may prescribe license requirements and conditions including, among other things, specified accounting records, regulatory accounting principles, and filing process requirements for rate-setting purposes.

The Corporation is required to charge its customers for the following amounts (all of which, other than the distribution rate, essentially represent a pass through of amounts payable to third parties):

- (i) **Electricity Price and Related Rebates:** The electricity price and related rebates represent a pass through of the commodity cost of electricity.
- (ii) **Distribution Rate:** The distribution rate is designed to recover the costs incurred by the Corporation in delivering electricity to customers, as well as earn the OEB allowed rate of return. Distribution charges are regulated by the OEB and typically comprise a fixed charge and a usage-based (consumption) charge.

The volume of electricity consumed by the Corporation's customers during any period is governed by events largely outside the Corporation's control (principally sustained periods of hot or cold weather which increase the consumption of electricity and sustained periods of moderate weather which decrease the consumption of electricity).

- (iii) **Retail Transmission Rate:** The retail transmission rate represents a pass through of costs charged to the Corporation for the transmission of electricity from generating stations to the Corporation's service area. Retail transmission rates are regulated by the OEB.
- (iv) **Wholesale Market Service Charge:** The wholesale market service charge represents a pass through of various wholesale market support costs charged by the Independent Electricity System Operator (IESO).

Any differences between the actual cost of electricity, transmission and wholesale market services and the amounts charged to customers are recorded in retail settlement variance accounts ("RSVA amounts"). These RSVA amounts are reviewed by the OEB and periodically rate adjustments are requested and approved by the OEB to "true up" the amounts charged to customers for these services.

Electricity distribution rates as described above are approved by the OEB and allow the Corporation to recover its reasonable costs and the OEB allowed market based rate of return.

PowerStream Inc.

Notes to the financial statements

December 31, 2009

(in thousands of dollars)

3. Electricity industry regulation (continued)

In its 2009 rate application, the Corporation received approval to repay the net regulatory liabilities accrued from January 1, 2005 to December 31, 2007 plus interest thereon to April 30, 2009 over the period September 1, 2009 to April 30, 2011, for the former PowerStream Inc. rate zone. In its 2010 rate application, for the former Barrie Hydro Distribution Inc. rate zone, the Corporation has applied to refund the net regulatory liabilities accrued from January 1, 2005 to December 31, 2008 plus interest thereon to April 30, 2010 over the period May 1, 2010 to April 30, 2011.

In 2008, the OEB approved distribution rates for the former Barrie Hydro Distribution Inc. rate zone for the period May 1, 2008 to April 30, 2009 based on updated values for assets and costs, a deemed debt equity ratio of 60:40 and an allowed return on deemed equity of 8.57%. In 2009, the OEB approved distribution rates for the former PowerStream Inc. rate zone effective for the period May 1, 2009 to April 30, 2010 based on updated values for assets and costs, a deemed debt equity ratio of 60:40 and an allowed return on deemed equity of 8.01%.

The OEB has established a multi-year electricity distribution rate-setting plan for distributors to streamline the process for approving distribution rates and charges. The OEB issued guidelines along with an Incentive Regulation Models ("IRM") to be used to calculate annual rate adjustments. The guidelines effectively adjusted Base Distribution Rates for inflation less a productivity factor. Following the rebasing, both rate zones are on the 3rd Generation IRM method for setting rates for 2010.

The Corporation has filed 3rd Generation IRM rate filings for its 2010 distribution rates for both rate zones. New rates are expected to be approved effective May 1, 2010.

Under the Green Energy and Green Economy Act, 2009, the Corporation and other Ontario electricity distributors have new responsibilities for enabling renewable generation, including investing in a smart grid, to accommodate any changes this may have on the local distribution of electricity. The OEB has approved several new deferral accounts to capture incremental costs related to these new initiatives for recovery in future periods.

The continuing restructuring of Ontario's electricity industry and other regulatory developments, including current and possible future consultations between the OEB and interested stakeholders may affect the distribution rates and other permitted recoveries.

4. Significant accounting policies

The Corporation's financial statements are the representations of management prepared in accordance with Canadian generally accepted accounting principles ("GAAP") and accounting policies provided by its regulator, the OEB, as contained in the Accounting Procedures Handbook for Electric Distribution Utilities, issued under the authority of the Ontario Energy Board Act, 1998.

The financial statements reflect the following significant accounting policies:

(a) Rate setting

The Corporation is regulated by the OEB under authority of the Ontario Energy Board Act, 1998. The OEB is charged with the responsibility of approving or setting rates for the transmission and distribution of electricity and the responsibility for ensuring that distribution companies fulfill obligations to connect and service customers. The OEB also has the authority to provide rate protection for certain electricity customers.

PowerStream Inc.

Notes to the financial statements

December 31, 2009

(in thousands of dollars)

4. Significant accounting policies (continued)

(a) Rate setting (continued)

As the Corporation is regulated by the OEB, the timing of accounting recognition and measurement of assets and liabilities arising from rate regulation may differ from that otherwise expected under Canadian generally accepted accounting principles for non-rate regulated enterprises. The Corporation has determined that its assets and liabilities arising from rate-regulated activities qualify for recognition under Canadian GAAP and this recognition is consistent with U.S. Statement of Financial Accounting Standards No. 71 – "Accounting for the Effects of Certain Types of Regulation".

(b) Revenue recognition

(i) Electricity distribution and sale

Revenue from the sale and distribution of electricity is recorded on the basis of cyclical billings based on electricity usage and also includes unbilled revenue accrued in respect of electricity delivered but not yet billed.

(ii) Other revenue

Other revenue related to sales of other services is recognized as services are rendered. Contract revenue is accounted for using the percentage of completion method, whereby revenue is recognized proportionately with the degree of completion of the services under contract. Losses on contracts are fully recognized when they become evident.

(c) Financial instruments

The Corporation has made the following balance sheet classifications in connection with its financial assets and financial liabilities:

- Cash is classified as financial assets "Held-for-Trading" and is measured at fair value.
- Accounts receivable are classified as "Loans and Receivables" and are measured at amortized cost using the effective interest method.
- Other non-current assets are classified as "Held-to-Maturity Investments" and are measured at amortized cost, which, after initial recognition, is considered equivalent to fair value.
- Accounts payable, accrued liabilities, amounts due to related parties, short-term debt, bank term loan, debentures payable and notes payable are classified as "Other Financial Liabilities" and are measured at amortized cost using the effective interest method.

Financial assets and liabilities are initially recorded at fair value. The fair value is the amount of the consideration that would be agreed upon in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act. Subsequent measurement depends on how each financial instrument is classified on the balance sheet.

PowerStream Inc.

Notes to the financial statements

December 31, 2009

(in thousands of dollars)

4. Significant accounting policies (continued)

(c) Financial instruments (continued)

In accordance with the amendments to CICA Handbook Section 3862, the Corporation has classified fair value measurements using a fair value hierarchy that reflects the three levels of the inputs used in making the fair value measurements. The fair value hierarchy has the following levels:

- (i) Level 1: Unadjusted quoted prices in active markets for identical assets or liabilities;
- (ii) Level 2: Observable inputs other than quoted prices included in Level 1, such as derived prices for similar assets and liabilities; or quoted prices in inactive markets; and
- (iii) Level 3: Unobservable inputs for the assets or liabilities that are not based on observable market data.

(d) Inventories

Inventories, which consists of parts and supplies acquired for internal construction or consumption, is stated at the lower of cost and net realizable value. Cost is determined on a weighted-moving average basis. Any impairment losses taken on inventories are reversed if and when net realizable value subsequently recovers. Major spare parts and standby equipment are recorded as part of property, plant and equipment and amortized once they are put into use.

(e) Property, plant and equipment and amortization

Property, plant and equipment are recorded at cost and includes contracted services, materials, labour, engineering costs, interest and overheads. Certain assets may be acquired or constructed with financial assistance in the form of contributions from developers or customers and in some instances a portion may be refunded by the Corporation based on economic evaluation (discounted cash flow), in accordance with the OEB Distribution System Code. Such contributions, whether in cash or in-kind, are offset against the related asset cost. Contributions in-kind are valued at their fair value at the date of their contribution.

When identifiable assets, such as buildings, distribution station equipment, equipment and furniture are retired or otherwise disposed of, their original cost and related accumulated amortization are removed from the accounts and the related gain or loss is included in the operating results for the related fiscal period.

Amortization of property, plant and equipment is provided for on the straight-line basis over the estimated service life of the assets. Amortization of contributions from developers or customers is amortized at the rates corresponding with the useful lives of the related property, plant and equipment. The estimated service lives of the various assets used in calculating amortization are summarized below:

Buildings	10 to 60 years
Transformer stations	40 years
Transformers and meters	25 to 40 years
Plant and equipment	10 to 30 years
Other	3 to 8 years

PowerStream Inc.

Notes to the financial statements

December 31, 2009

(in thousands of dollars)

4. Significant accounting policies (continued)

(e) *Property, plant and equipment and amortization (continued)*

Construction in progress comprises property, plant and equipment under construction; property, plant and equipment not yet placed into service; and pre-construction activities related to specific projects expected to be constructed. An allowance for the outlay of funds employed during the construction period has been applied to the related property, plant and equipment as allowed by the OEB.

(f) *Impairment of long-lived assets*

The Corporation reviews long-lived assets for impairment whenever events or circumstances indicate that the carrying amount of the long-lived assets is not recoverable. Any resulting impairment loss is recorded in the period in which the impairment occurs.

(g) *Intangibles*

Intangibles includes computer software and land rights. Computer software is stated at cost and amortized on a straight-line basis over three years while land rights are stated at cost, are not amortized and have an estimated indefinite useful life.

(h) *Regulatory assets and liabilities*

Regulatory assets/liabilities represent costs/revenue that have been deferred and that are expected to be disposed of through future rates. Retail Settlement Variances (RSVA) amounts are required to be recorded by the OEB and arise from differences in amounts billed to customers and retailers and the cost to the Corporation, for electricity, wholesale market services and transmission services. The Corporation accrues interest on regulatory assets and liabilities as permitted by the OEB.

As at December 31, 2009, regulatory assets and liabilities are comprised principally of deferred Smart Meter costs and retail settlement variances.

As at December 31, 2009, management has provided a provision against certain regulatory assets and liabilities. Management continues to assess the likelihood of recovery of its regulatory assets and believes that it is probable that its regulatory assets, net of the valuation allowance, and liability balances will be factored into the setting of future rates.

(i) *Goodwill*

Goodwill represents the excess of the purchase price over the fair value assigned to the Corporation's interest of the net identifiable assets acquired on the acquisition, by predecessor corporations of the former Richmond Hill Hydro Inc., Penetanguishene Hydro, Essa Hydro, New Techusmestch Hydro and Bradford Hydro. Goodwill is not amortized but is tested for impairment annually or more frequently if events or changes in circumstances indicate that the asset might be impaired. When the carrying amount of goodwill exceeds the implied fair value of goodwill an impairment loss is recognized in an amount equal to the excess.

PowerStream Inc.

Notes to the financial statements

December 31, 2009

(in thousands of dollars)

4. Significant accounting policies (continued)

(j) Pension and other post-employment benefits

The Corporation accounts for its participation in the Ontario Municipal Employees Retirement Fund ("OMERS"), a multi-employer public sector pension fund, as a defined contribution plan.

The Corporation actuarially determines the cost of other employment and post-employment benefits offered to employees using the projected benefit method prorated on service and based on management's best estimate assumptions. Under this method, the projected post-retirement benefit is deemed to be earned on a pro-rata basis over the years of service in the attribution period commencing at the date of hire, and ended at the earliest age the employee could retire and qualify for benefits. Compensated absences and termination benefits that do not vest or accumulate are recognized as an expense when the event occurs. This accounting policy for future employee benefits was applied on the prospective basis. The transitional obligation resulting from this treatment is being amortized over the average remaining service period of employees.

(k) Customers' deposits

Customer's deposits are cash collections from customers to guarantee the payment of energy bills and fulfillment of construction obligations. Deposits estimated to be refundable to customers within the next fiscal year are classified as a current liability. Interest is paid on customers' deposits.

(l) Payment in lieu of corporate income taxes

Effective January 1, 2009, the Corporation adopted amendments to the Canadian Institute of Chartered Accountants (CICA) Handbook section 3465, Income Taxes and CICA Handbook Section 1100, Generally Accepted Accounting Principles. These amendments established new standards for the recognition, measurement, presentation and disclosure of future income tax assets and liabilities.

The requirement for rate-regulated enterprises to recognize future income taxes, as well as a separate asset or liability for the future revenue or reduction in future revenue expected as a result of regulator's action in respect of future income taxes, applies for fiscal years beginning on or after January 1, 2009.

(m) Measurement uncertainty

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of revenue, expenses, assets and liabilities, as well as the disclosure of contingent assets and liabilities at the financial statement date. Accounts receivable, unbilled revenue, inventories, regulatory assets and liabilities, goodwill, employee future benefits and income taxes payable are reported based on amounts expected to be recovered/refunded and an appropriate allowance has been provided based on managements' best estimate of unrecoverable amounts. Due to the inherent uncertainty involved in making such estimates, actual results could differ from amounts recorded in these financial statements, including changes as a result of future decisions made by the OEB, the Minister of Energy and Infrastructure and the Minister of Finance.

PowerStream Inc.

Notes to the financial statements

December 31, 2009

(in thousands of dollars)

5. Changes in accounting policies

Current changes

(a) Rate-regulated operations

Effective January 1, 2009, the temporary exemption from CICA Handbook Section 1100, "Generally Accepted Accounting Principles", which permits the recognition and measurement of assets and liabilities arising from rate regulation, was withdrawn.

The Corporation has determined that its assets and liabilities arising from rate-regulated activities qualify for recognition under Canadian GAAP and this recognition is consistent with U.S. Statement of Financial Accounting Standards No. 71 - "Accounting for the Effects of Certain Types of Regulation".

As a result, the removal of the temporary exemption has no effect on the Corporation's results of operation as of December 31, 2009. The financial impact of the rate regulation continues to be disclosed in accordance with Accounting Guideline 19 - "Disclosures by Entities Subject to Rate Regulation".

In addition, CICA Handbook Section 3465, Income Taxes was amended to require the recognition of future income tax liabilities and assets. On January 1, 2009, the Corporation began to account for the differences between its financial statement carrying value and tax basis of assets and liabilities in accordance with CICA Handbook Section 3465, Income Taxes. As at January 1, 2009, the Corporation has recognized a future income tax asset of \$68,424 and a corresponding regulatory liability of \$68,424.

(b) Goodwill and intangible assets

Effective January 1, 2009, the Corporation adopted CICA Handbook Section 3064, Goodwill and Intangible Assets. This standard augments existing Handbook Section 3061, Property, Plant and Equipment and replaces Section 3062 Goodwill and Other Intangible Assets.

As accounting for Goodwill under CICA Handbook Section 3064 remains unchanged from CICA 3062, there was no effect on the Goodwill calculations.

As a result of adopting this new accounting standard, the Corporation reclassified computer application software and land rights at its net book value from property, plant and equipment to intangible assets (Note 7).

(c) Financial Instruments recognition, measurement and disclosure

In July 2009, the CICA amended Handbook Section 3855 on financial instruments recognition and measurement to incorporate certain changes to Canadian GAAP in order to reduce differences with International Financial Reporting Standards (IFRSs) and to ease the requirements regarding impairment of certain investment in debt instruments. The application of these amendments did not have any impact on the Corporation's financial statements since there are no investments in debt instruments for reclassification nor impairment losses to report on other than the allowance for doubtful accounts.

(i) Credit risk and fair value of financial assets and financial liabilities

In January 2009, the CICA issued an Emerging Issues Committee Abstract (EIC) 173 on credit risk and fair value of financial assets and financial liabilities which is applicable to all entities that have adopted Section 3855 on financial instruments recognition and measurement. It reached a consensus that an entity's own credit risk and the credit risk of the counterparty should be taken into account in determining the fair value of financial assets and liabilities including derivative instruments.

PowerStream Inc.

Notes to the financial statements

December 31, 2009

(in thousands of dollars)

5. Changes in accounting policies (continued)

Current changes (continued)

(c) Financial Instruments recognition, measurement and disclosure (continued)

(ii) Financial Instrument Disclosures

CICA Handbook Section 3862 on Financial Instrument Disclosures was amended and effective from fiscal years ending after September 30, 2009. These amendments include additional disclosure requirements in respect of fair valuation measurement and liquidity risk management disclosures. The amendments require an entity to classify fair value measurements using a fair value hierarchy that reflects the significance of the inputs used in making the measurements.

The adoption of CICA Handbook Sections 3855, 3862 and EIC 173 resulted in additional disclosures of the fair market value of Financial Instruments as described in Note 21(b).

Future accounting changes

(d) International Financial Reporting Standards ("IFRSs")

The Corporation is required to prepare their financial statements effective January 1, 2011 in accordance with IFRSs requirements.

The Corporation has an internal initiative to govern the conversion process to IFRSs and is currently in the process of evaluating the potential impact of IFRSs on its consolidated financial statements. The Corporation will continue to monitor the progress made by the International Accounting Standards Board (IASB) on the rate-regulated activities standard in consultation with other LDCs and its professional advisers.

6. Property, plant and equipment

	Cost	Accumulated amortization	Net book value
	\$	\$	\$
Land	8,923	-	8,923
Buildings	71,183	16,051	55,132
Transformer stations	107,429	33,742	73,687
Transformers and meters	310,368	153,188	157,180
Plant and equipment	843,257	405,670	437,587
Other	39,188	26,481	12,707
Construction in progress	59,227	-	59,227
	1,439,575	635,132	804,443
Capital contributions	253,973	51,294	202,679
	1,185,602	583,838	601,764

Included in property, plant and equipment costs is an amount of \$5,683 related to an "allowance for the outlay of funds" employed during the construction period as allowed by the OEB. In the absence of rate regulation, interest expense in the current year would have been higher by \$1,433. Further, transformers and meters amounting to \$1,061 were considered to be impaired and an impairment loss was recorded.

PowerStream Inc.

Notes to the financial statements

December 31, 2009

(in thousands of dollars)

7. Intangibles

The Corporation reclassified land rights and computer software from property, plant and equipment to Intangibles in accordance with CICA Handbook Section 3064, Goodwill and Intangible Assets.

	Cost	Accumulated amortization	Net book value
	\$	\$	\$
Land rights	729	-	729
Computer software	15,580	(12,695)	2,885
	16,309	(12,695)	3,614

8. Regulatory assets and liabilities

Regulatory assets and liabilities arise as a result of the rate-making process and consist of the following:

	\$
Regulatory assets	
Deferred smart meter costs	25,713
Other regulatory assets	720
Regulatory assets	26,433
Regulatory liabilities	
Retail settlement variance accounts	(1,010)
Future income taxes	(61,665)
Regulatory assets recovery account	(22,915)
PILs variance	(4,008)
Regulatory liabilities	(89,598)
Provision for regulatory assets and liabilities	(1,542)
Regulatory liabilities, net	(91,140)

(a) Regulatory assets

(i) Deferred smart meter costs

As part of the Ontario Government's initiative, the Corporation had installed 225,000 smart meters as at December 31, 2009 (2008 - 135,000). The Corporation has recorded the capital spending and incremental expenses incurred in connection with smart meters along with related funding collected from customer in the deferral accounts established by the OEB.

The Corporation applied and received approval for recovery of smart meter costs up to December 31, 2007 in its 2009 Cost of Service rate application. The approved amount of \$8,863 which has been reallocated consists of \$8,909 of property, plant and equipment, \$2,002 of revenue and \$1,956 of operating expense.

In the absence of this regulatory treatment, property, plant and equipment would be increased by \$19,883 with related amortization expense of \$878. Operating expenses would be increased by \$814. Other revenue would be increased by \$4,093 and interest revenue would be lower by \$164.

PowerStream Inc.

Notes to the financial statements

December 31, 2009

(in thousands of dollars)

8. Regulatory assets and liabilities (continued)

(a) Regulatory assets (continued)

(i) Deferred smart meter costs (continued)

This regulatory asset balance also includes the net book value less proceeds of stranded mechanical meters, which have been replaced by smart meters, in the amount of \$10,184. In the absence of this regulatory treatment, current year replaced meters with a net book value of \$3,747 would have been recorded as a loss on disposal of property, plant and equipment.

(ii) Other regulatory assets

This consists mainly of the costs related to the transition to IFRSs less the related amounts included in rates. It also includes costs related to the Green Energy and Green Economy Act, 2009 initiatives that are allowed to be deferred.

Under OEB regulations, these expenses are allowed to be deferred, which under Canadian GAAP would be recorded as expense for an unregulated business. Under non regulated reporting, expenses would have been \$661 higher in 2009 and interest income would have been lower in 2009 by \$36.

(b) Regulatory liabilities

(i) Retail settlement variance accounts

Retail settlement variances are variances that have occurred since May 1, 2002 when the competitive electricity market was declared open, to December 31, 2009, and have accumulated pursuant to direction from the OEB. Current balances represent variances from January 1, 2005 to December 31, 2009; balances up to December 31, 2004 were approved for settlement with customers in 2006 rates. Specifically, these amounts include:

- (a) Variances between the amount charged by the Independent Electricity System Operator ("IESO") for the operation of the markets and grid, the purchase of imported power by the IESO to augment Ontario's power supply and charged by the IESO as an uplift charge that is part of the wholesale market service charges, as well as various wholesale market settlement charges and transmission charges, as compared to the amount billed to consumers based on the OEB-approved wholesale market service rate and transmission rates; and
- (b) Differences between the amounts charged by the IESO and billed to consumers for energy costs. Energy charges by the IESO consist of the hourly price of electricity, global adjustment charges related to the Ontario Power Authority's long term contracted supply of electricity including renewables, and adjustments for electricity billed to customers at regulated price plan rates.

Under OEB regulations, the retail settlement variances are allowed to be deferred which under Canadian GAAP would be recorded as costs for an unregulated business. Under non regulated reporting, cost of power would have been \$4,484 higher in 2009 and interest expense would have been lower in 2009 by \$360.

PowerStream Inc.

Notes to the financial statements

December 31, 2009

(in thousands of dollars)

8. Regulatory assets and liabilities (continued)

(b) Regulatory liabilities (continued)

(ii) Future income taxes

Effective January 1, 2009, the Corporation adopted CICA handbook Section 3465, Income Taxes and accounted for future income taxes by taking into account the differences between the tax basis of assets and liabilities and their financial statement carrying value. The OEB allows the Corporation to recover amounts in rates for payments in lieu of corporate income taxes ("PILs") using the taxes payable method. No allowance is made for future income taxes as a result of temporary differences between the tax basis of assets and liabilities and their carrying amounts for accounting purposes. This regulatory liability account is related to the expected future distribution rate reduction for customers arising from the recognition of future income tax assets. Accordingly, a regulatory liability has been recorded to offset the future income tax asset.

(iii) Regulatory assets recovery account

The regulatory asset recovery account is comprised of the final balances of regulatory assets and regulatory liabilities approved for disposition by the OEB.

As at December 31, 2009, the balances include the following:

(a) Former Barrie Hydro Distribution Inc. rate zone

On May 1, 2008, the Corporation began recovery of regulatory asset balances in the amount of \$910 over a period of 36 months through rate riders. These recoveries are based on final balances approved by the OEB reflecting costs to December 31, 2006 and carrying interest accrued to April 30, 2008. In 2008 the approved amounts were netted with the recoveries account in accordance with OEB direction.

(b) Former PowerStream Inc. rate zone

On September 1, 2009, the Corporation began refunding net regulatory liabilities in the amount of \$28,089 over a period of twenty months through rate riders. These recoveries are based on final balances approved by the OEB reflecting costs to December 31, 2007 and carrying interest accrued to April 30, 2009. In 2009 the approved amounts were netted with the recoveries account in accordance with OEB direction.

The billed amounts are recorded in the regulatory assets recovery account and interest is applied at the OEB prescribed interest rate for carrying charges. Under non regulated reporting, revenues would be decreased by \$5,036 and interest expense in 2009 would have been \$573 lower.

(iv) Payments in lieu of corporate income taxes ("PILs") variance

PILs are recorded based on the OEB PILs methodology of PILs billed amount versus PILs proxy amount variance and an annual Spreadsheet Implementation Model for PILs ("SIMPILs") filing with specified true-ups. Under non regulated reporting, revenues would have been \$241 higher and interest expense would have been \$51 lower.

PowerStream Inc.

Notes to the financial statements

December 31, 2009

(in thousands of dollars)

8. Regulatory assets and liabilities (continued)

(b) Regulatory liabilities (continued)

(iv) Payments in lieu of corporate income taxes ("PILs") variance (continued)

The OEB has undertaken a combined proceeding (EB-2008-0381) to review the balances set up in this account, for a group of utilities (the former Barrie Hydro Distribution Inc., ENWIN Utilities Ltd. and Halton Hills Hydro Inc.) and determine the amounts to be recovered from or repaid to customers.

The Corporation has used the SIMPIL model and followed instructions provided by the OEB in setting up the balances in this account for the period October 2001 to April 30, 2006 and a revised model as directed by the OEB thereafter.

As an outcome of this proceeding, the OEB will provide clarification of the existing rules and interpretations as to how these rules should have been applied. It is the OEB's stated intention that these clarifications and interpretations will be used as a reference in determining the amounts for disposition by other utilities.

This proceeding is in the early stages and the outcome is indeterminable at this time. Any adjustments will be recorded when known.

(v) Provision for regulatory assets and liabilities

Management has determined that there is uncertainty concerning the future recovery of certain regulatory assets and liabilities. Based on this uncertainty, a provision in the amount of \$1,542 has been recorded.

Under the OEB's new guidelines for disposition of variance and deferral accounts, the Corporation has applied for disposal of most regulatory asset and liability balances as at December 31, 2008 in its 2010 incentive rate mechanism service rate application for the former Barrie Hydro Distribution Inc. rate zone. Under the same guidelines, former PowerStream Inc. rate zone did not meet the threshold and did not apply for disposition of variance and deferral accounts.

Management will continue to assess the likelihood of recovery of the regulatory assets and liabilities amount recorded. In the event that Management determines the recovery for these amounts is no longer probable, these amounts will be expensed in the period for which the determination is made.

9. Credit facilities

The Corporation executed an unsecured credit facility with a Canadian chartered bank on December 17, 2008 which is renewable annually. This credit facility agreement provides an extendible 364-day committed revolving credit facility of \$75,000, an uncommitted demand facility of \$25,000 for a specific purpose, an uncommitted Letter of Guarantee facility of \$15,000 and a committed term facility of \$50,000.

As at December 31, 2009, the Corporation had utilized \$12,000 of the Letter of Guarantee facility to provide the IESO with a letter of credit for prudential support. With the opening of Ontario's electricity market to wholesale and retail competition on May 1, 2002 ("Open Access"), the IESO requires all purchasers of electricity in Ontario to provide security to mitigate the risk of their default based on their expected purchases from the IESO administered spot market. The IESO could draw on the letter of credit if the Corporation defaults on its payment.

PowerStream Inc.

Notes to the financial statements

December 31, 2009

(in thousands of dollars)

9. Credit facilities (continued)

The 364-day committed revolving credit facility can be drawn upon by direct advances, bearing interest at prime plus 0.25% or Bankers' Acceptances of a stamping fee plus 137 basis points (1.37%) per annum. The uncommitted demand facility bears an interest rate of prime plus 0.00%, or Bankers' Acceptance of a stamping fee plus 100 basis points (1.00%) per annum. The Letter of Guarantee facility bears a charge of 50 basis points (0.50%) per annum.

The committed term facility was fully drawn by the Corporation in February 2008 (Note 12(a)). The \$25,000 uncommitted demand facility was drawn by the Corporation in December 2008 and remains outstanding as at December 31, 2009. As of December 2009, the Corporation has utilized \$15,000 of the committed revolving credit facility (Note 13).

10. Accounts payable and accrued liabilities

	\$
Accounts payable - energy purchases	57,581
Current portion of customers' deposits	1,000
Other accounts payable and accrued liabilities (including construction deposits of \$129 to be refunded in a year)	52,824
	<u>111,405</u>

11. Related party balances and transactions

The amount due to the Corporation of the City of Vaughan ("Vaughan"), the Corporation of the City of Barrie ("Barrie") and the Corporation of the Town of Markham ("Markham") is comprised of amounts payable to Vaughan, Markham and Barrie and their wholly-owned subsidiaries.

Components of the amounts due to related parties are as follows:

	\$
The Corporation of the City of Vaughan	
Net balance payable of inter entity transactions, without interest	<u>5,523</u>
The Corporation of the Town of Markham	
Net balance payable of inter entity transactions, without interest	<u>4,951</u>
The Corporation of the City of Barrie	
Net balance payable of inter entity transactions, without interest	<u>1,575</u>
	<u>12,049</u>

PowerStream Inc.

Notes to the financial statements

December 31, 2009

(in thousands of dollars)

11. Related party balances and transactions (continued)

Other significant related party transactions not otherwise disclosed separately in the financial statements, are summarized below:

	City of Vaughan	Town of Markham	City of Barrie
	\$	\$	\$
Revenue			
Energy and distribution	4,094	3,903	3,726
Shared services	1,916	1,401	1,620
Expenses			
Facilities rental	732	120	-
Realty taxes	530	158	303
Operations	482	95	-

12. Long-term debt

(a) Bank term loan

The bank term loan is a 5 year fixed rate term loan with a Canadian Chartered Bank which bears interest at an annual rate of 5.08%. It is a non-amortizing loan with repayment at the end of the contracted term, February 26, 2013. The financial covenants require a Total Debt to Capitalization Ratio of no greater than 0.60:1, and to maintain an Interest Coverage Ratio of no less than 1.25:1.

Interest expense relating to the bank term loan for the year ended December 31, 2009 was \$2,540.

(b) Debentures payable

\$

6.45% unsecured debentures due August 15, 2012,
interest payable in arrears semi-annually on
August 15 and February 15

123,091

In August 2002, the four predecessor corporations (Hydro Vaughan Distribution Inc., Markham Hydro Distribution Inc., Richmond Hill Hydro Inc. and Barrie Hydro Distribution Inc.) raised gross proceeds of \$125,000 through a private placement offering. These predecessor corporations were four of five local distribution companies ("LDC") that participated in the Electricity Distributors Finance Corporation ("EDFIN") 10 Year Debentures Issued (Series 2002-1) that was offered on a private placement. EDFIN is a specific purpose corporation managed by MEARIE Management Inc., for the purpose of providing the LDCs with efficient access to the debt capital markets. Each LDC has executed a debenture which is a direct and unsecured obligation of the LDC. The LDC's obligations are several and not joint, and each LDC is liable for its own obligation and not that of any other LDC.

PowerStream Inc.
Notes to the financial statements
December 31, 2009
(in thousands of dollars)

12. Long-term debt (continued)

(b) Debentures payable (continued)

The debentures are recorded at amortized cost, using the effective interest method. Interest expense relating to debentures payable was \$8,691 which included \$629 of accretion.

The debentures are subject to the financial covenant that the consolidated funded obligation does not exceed 75% of the total consolidated capitalization of the Corporation.

(c) Notes payable

	\$
Promissory note issued to the City of Vaughan	78,236
Deferred interest on promissory note issued to the City of Vaughan	8,743
Promissory note issued to the Town of Markham	67,866
Deferred interest on promissory note issued to the Town of Markham	7,585
Promissory note issued to the City of Barrie	20,000
	182,430

On June 1, 2004, an unsecured 20 year term promissory note was issued to the Corporation of the City of Vaughan ("Vaughan") in the amount of \$78,236. Interest thereon commenced on June 1, 2004 at an annual rate of 5.58%.

On June 1, 2004, an unsecured 20 year term promissory note was issued to the Corporation of the Town of Markham ("Markham") in the amount of \$67,866. Interest thereon commenced on June 1, 2004 at an annual rate of 5.58%.

On December 31, 2008, an unsecured 16 year term promissory note was issued to the Corporation of the City of Barrie ("Barrie") in the sum of \$20,000. Interest for 2009 is at an annual rate of 6.50%, and will change to 5.58% in 2010 and after.

The three promissory notes are repayable 90 days following demand by Vaughan, Markham and Barrie, with subordination and conditions. These notes have been classified as long-term as it is not the intent of Vaughan, Markham or Barrie to demand repayment within the next year.

At the request of the City of Vaughan and the Town of Markham, eight quarters of interest have been deferred commencing October 1, 2006. This deferred interest will be repayable in full on October 31, 2013 and is subject to the same interest rate and conditions as the original note.

Interest of \$4,853 on the note payable to the City of Vaughan, \$4,210 on the note payable to the Town of Markham and interest of \$1,300 to the City of Barrie was charged to interest expense during the year. This includes interest on the related deferred interest balance for the City of Vaughan and the Town of Markham.

PowerStream Inc.

Notes to the financial statements

December 31, 2009

(in thousands of dollars)

13. Short-term debt

	\$
Short-term demand facility with a Canadian Bank with an interest rate at prime rate or Banker's Acceptance plus 100 basis points per annum, whichever is lower. The terms of this facility are renewable annually.	25,000
Drawn down on the Corporation's \$75,000 364-day committed revolving credit facility with a Canadian Bank. The interest rate for this facility is at prime rate plus 0.25% per annum, or Banker's Acceptance plus 137 basis points per annum, whichever is lower. The terms of this facility are renewable annually.	15,000
	40,000

14. Customers' deposits

	\$
Service deposits	17,726
Less amounts expected to be refunded within one year, included in accounts payable and accrued liabilities (Note 10)	1,000
Non-current portion of customers' deposits	16,726

15. Employee future benefits

The Corporation pays certain health, dental and life insurance benefits under unfunded benefit plans on behalf of its retired employees.

The Corporation measures its accrued benefit obligation for accounting purposes every three years. The latest actuarial valuation was performed as at December 31, 2009.

A reconciliation of the Corporation's accrued benefit obligation to the amounts recorded in the financial statements is as follows:

	\$
Accrued benefit obligation	16,490
Unamortized transitional obligation	(482)
Unamortized net actuarial losses	(3,972)
Accrued benefit liability	12,036

PowerStream Inc.

Notes to the financial statements

December 31, 2009

(in thousands of dollars)

15. Employee future benefits (continued)

Details of the accrued benefit obligation are as follows:

	\$
Accrued benefit obligation, beginning of the year	13,441
Current service cost	260
Interest cost on obligation	878
Benefit payments	(393)
Actuarial losses	2,304
Accrued benefit obligation, end of the year	16,490

The plan expense for the year is determined as follows:

	\$
Current service cost	260
Interest cost on obligation	878
Amortization of transitional obligation	70
Amortization of net actuarial losses	108
Plan expense	1,316

The significant actuarial assumptions adopted in measuring the Corporation's accrued benefit obligation are as follows:

	%
Discount rate	5.50-6.50
Rate of compensation increase	3.50
Medical benefits costs escalation - hospitalization	5.00-9.00
Medical benefits costs escalation - extended health care	5.00-9.00
Dental benefits costs escalation	5.00

Sensitivity analysis

Assumed health care cost trend rates have a significant effect on the amounts reported for the health care plans. A one-percentage-point change in assumed health care cost trend rates would have the following effects for 2009:

	Increase	Decrease
	\$	\$
Total service and interest cost	152	(130)
Accrued benefit obligation	2,229	(1,802)

PowerStream Inc.

Notes to the financial statements

December 31, 2009

(in thousands of dollars)

16. Pension

The Corporation participates in the Ontario Municipal Employees Retirement System ("OMERS") for its full time employees, as a 'Defined Contribution Plan'. OMERS is a multi-employer defined benefit pension plan which provides pensions for employees of Ontario municipalities, local boards, public utilities and school boards. The fund is financed by equal contributions from participating employers and employees, and by the investment earnings of the fund. The Corporation incurred \$2,536 of contribution expense during the year ended December 31, 2009.

17. Share capital

The Corporation's authorized share capital is made up of an unlimited number of common shares. The issued share capital is as follows:

	\$
100,000 common shares	247,183

Of the total 100,000 common shares issued 45,315 common shares are registered under Vaughan Holdings Inc. (wholly owned by The Corporation of the City of Vaughan), 34,185 common shares are registered under Markham Enterprises Corporation (wholly owned by The Corporation of the Town of Markham) and 20,500 common shares are registered under Barrie Hydro Holdings Inc. (wholly owned by The Corporation of the City of Barrie).

18. Dividends

During 2009, the Corporation established a dividend policy to distribute a minimum dividend of 50% of net income with consideration given to the:

- (a) Cash position at the beginning of the year;
- (b) Working capital requirements for the current year; and
- (c) Net capital expenditures required for the current year.

During 2009, the Corporation paid \$11,274 to the shareholders based on the combined net income of the predecessor corporations. In addition, the Corporation made a special payment of \$19,808 to the shareholders as the final closing adjustment for the amalgamation of PowerStream Inc. and Barrie Hydro Distribution Inc..

19. Commitments

(a) Town of Markham

The Corporation retained cashing services from the Town of Markham to facilitate customers paying electricity bills. The total commitment for these services is \$84 for the year 2010.

(b) City of Vaughan

The Corporation rents certain outdoor and indoor facilities from the City of Vaughan. The total commitment for these services to 2012 is \$529.

PowerStream Inc.
Notes to the financial statements
December 31, 2009
(in thousands of dollars)

19. Commitments (continued)

(c) Leases for the operation centres

(i) Cochrane Operation Centre

In November 2007, the Corporation entered into a lease agreement with a third party for an operations centre and warehouse. The lease term is from December 1, 2007 to March 31, 2010. The agreement also provided the Corporation with the ability to exercise two 3-month extension terms and accordingly the final terminating date of the agreement is September 30, 2010. The extension terms were not exercised and accordingly the lease contract ended on March 31, 2010. The total commitment for this lease from January 1, 2010 to March 31, 2010 is \$134.

(ii) Operation Centre

On October 9, 2008, the Corporation entered into a 25 year lease agreement relating to a new operation centre. The lease term commenced January 1, 2010 and occupancy occurred in March 2010. Therefore, the leased building asset valued at \$18,280 and the corresponding liability will be recorded at commencement of the lease. Upon entering into this lease arrangement, the Corporation evaluated whether substantially all of the benefits and risks of ownership related to this operation centre have been transferred to the Corporation (the lessee) in order to determine if the lease is classified and recorded as capital or operating. The component of the annual basic rent related to the land is classified and recorded as an operating lease and the component related to the building is classified as a capital lease.

The annual basic rent as per the lease agreement is as follows:

Fiscal year	Annual basic rent
	\$
2010-2019	2,286
2020-2029	2,457
2030-2034	2,621

(d) Contractual commitments

Markham TS#4

In 2007, the Corporation engaged third parties to construct a new 230KV to 28KV Transformer Station in the Markham area - Markham TS#4 to serve the north side of Hwy 407 west of Warden. The transformer station is expected to be energized by April 28, 2010 and the commitment from January 1, 2010 to April 28, 2010 is approximately \$3,000.

PowerStream Inc.

Notes to the financial statements

December 31, 2009

(in thousands of dollars)

20. Contingencies

(a) Legal claims

The Corporation has been named as a defendant in several actions. No provision has been recorded in the financial statements for these potential liabilities as the Corporation expects that these claims are adequately covered by its insurance.

(b) Other claims - Late Payment Charges Class Action

This action has been brought under the Class Proceedings Act, 1992. The plaintiff class seeks \$500 million in restitution for amounts paid to Toronto Hydro and to other Ontario municipal electric utilities ("LDCs") who received late payment penalties which constitute interest at an effective rate in excess of 60% per year, contrary to section 347 of the Criminal Code. Pleadings have closed in this action. The action has not yet been certified as a class action and no discoveries have been held, as the parties were awaiting the outcome of a similar proceeding brought against Enbridge Gas Distribution Inc. (formerly Consumers Gas).

On April 22, 2004, the Supreme Court of Canada released a decision in the Consumers Gas case rejecting all of the defenses which had been raised by Enbridge, although the Court did not permit the Plaintiff class to recover damages for any period prior to the issuance of the Statement of Claim in 1994 challenging the validity of late payment penalties. The Supreme Court remitted the matter back to the Ontario Superior Court of Justice for determination of the damages. At the end of 2006, a mediation process resulted in the settlement of the damages payable by Enbridge and that settlement was approved by the Ontario Superior Court.

In 2007, Enbridge filed an application to the OEB to recover the Court-approved amount and related amounts from ratepayers. On February 4, 2008, the OEB approved recovery of the said amounts from ratepayers over a five year period.

After the release by the Supreme Court of Canada of its 2004 decision in the Consumers Gas case, the plaintiffs in the LDC late payment penalties class action indicated their intention to proceed with their litigation against the LDCs. The parties are in settlement discussions but no settlement has been reached. At this time, it is not possible to quantify the effect, if any, on the financial statements.

PowerStream Inc.

Notes to the financial statements

December 31, 2009

(in thousands of dollars)

20. Contingencies (continued)

(c) *Ministry of Finance Tax audits*

The Ministry of Finance (the "Ministry") conducted PILs audits in 2008 on the three predecessor utilities, namely Richmond Hill Hydro Inc., Markham Hydro Distribution Inc. and Hydro Vaughan Distribution Inc. for the period January 1, 2004 through to May 31, 2004 and for PowerStream Inc. in 2009 for the periods June 1, 2004 through to December 31, 2004 and January 1, 2005 through to October 31, 2005. There is still an outstanding matter regarding the treatment of the retail settlement variance accounts (RSVA) for tax purposes.

There has been inconsistent practice of tax treatment of certain regulatory asset/liability accounts among LDCs across Ontario.

In accordance with OEB regulations, the Corporation has recorded the variance between amounts charged by the Corporation to its customers (at the OEB prescribed rates) and the costs charged to the Corporation for electricity, market services and transmission services, namely retail settlement variances, as regulatory assets or liabilities on the financial statements. Similar treatment has been followed for tax purposes. The Ministry is questioning this treatment of the RSVA for tax purposes and is suggesting that RSVA liabilities may be considered income for tax purposes.

The Ministry is currently reviewing the treatment of RSVA for tax purposes on a province wide basis. The impact of a tax ruling may result in a reassessment of taxes payable which could have an impact on results, financial position and cash flows in the future. The outcome of the Ministry's review is not determinable and as such, no provision has been made in the financial statements.

PowerStream Inc.

Notes to the financial statements

December 31, 2009

(in thousands of dollars)

21. Financial instruments and risk management

(a) *Recognition and measurement*

CICA Handbook Section 3855 established the standards for recognizing and measuring financial assets, financial liabilities and non-financial derivatives. The Corporation's accounting policies relating to the recognition and measurement of financial instruments are disclosed in Note 4(c).

(b) *Risk management*

The Corporation's carrying value and fair value of financial instruments are as follows:

Description	Carrying value	Fair value
	\$	\$
Assets		
Cash	42,612	42,612
Accounts receivable (net of allowance for doubtful accounts)	73,633	73,633
	116,245	116,245
Liabilities		
Accounts payable and accrued liabilities	111,405	111,405
Due to related parties	12,049	12,049
Short-term debt	40,000	40,000
Bank term loan	50,000	53,686
Debentures payable	123,091	135,391
Notes payable	182,430	198,901
	518,975	551,432

PowerStream Inc.

Notes to the financial statements

December 31, 2009

(in thousands of dollars)

21. Financial instruments and risk management (continued)

(b) Risk management (continued)

The Corporation understands the risks inherent in its business and defines them broadly as anything that could impact its ability to achieve its strategic objectives. The Corporation's exposure to a variety of risks such as credit risk, interest rate risk and liquidity risk as well as related mitigation strategies have been discussed below. However, the risks described below are not exhaustive of all the risks nor will the mitigation strategies eliminate the Corporation's exposure to all risks listed.

(i) Credit risk

The Corporation's primary source of credit risks to its accounts receivable result from customer's failing to discharge their dues for electricity consumed and billed. The Corporation has approximately 321,000 residential and commercial customers. In order to mitigate such potential credit risks, the Corporation has taken various measures in respect of its Energy customers such as collecting security deposits amounting to \$21,872 in accordance with OEB guidelines, reviewing Dun & Bradstreet (D&B) reports for the top 3000 commercial customers with an outstanding balance of \$5 or more, in-house collection department as well as external collection agencies and a bad debt insurance policy for \$4,500 related to energy receivables. Thus, the Corporation monitors and limits its exposure to such credit risks on an ongoing basis.

Pursuant to their respective terms, accounts receivable are aged as follows at December 31:

	Total	%
	\$	
Outstanding	75,808	100
Less than 30 days	55,965	73
30 - 60 days	4,346	6
61 - 90 days	4,336	6
Greater than 91 days	11,161	15
Less: Allowance for doubtful accounts	(2,175)	(3)
	<u>73,633</u>	

As at December 31, 2009, there was no significant concentration of credit risk with respect to any class of financial assets.

PowerStream Inc.

Notes to the financial statements

December 31, 2009

(in thousands of dollars)

21. Financial instruments and risk management (continued)

(b) Risk management (continued)

(ii) Interest rate risk

The Corporation limits its exposure to interest rate risk by issuing long term fixed rate debt in the form of debentures, promissory notes and bank loans. It also ensures that all payment obligations are met by adopting proper capital planning.

During fiscal 2009, the Board of Directors approved a swap and derivative transaction policy to enable the Corporation to enter into agreements such as interest rate swaps, and foreign exchange swaps where 100% of the floating rate risk is hedged into fixed rate for prudent risk management purposes and not speculative purposes. The Corporation has not entered into any such transactions.

As part of the Corporations' revolving demand operating credit facility, the Corporation may utilize the line of credit for working capital and/or capital expenditure purposes. Such short term borrowing may expose the Corporation to short term interest rate fluctuations as follows:

Interest rate and fees

364 Day Revolving Facility	
Prime Based Loans	PR*+0.25% p.a.
Bankers Acceptances	SF*+1.37% p.a.
Demand Facility	
Prime Based Loans	PR*+0.00% p.a.
Bankers Acceptances	SF*+1.00% p.a.
Letter of Guarantee Facility	0.50% p.a.
Committed Term Facility (Fixed Rate for 5 Years)	5.08%

Note:

PR* - Prime Rate, **SF*** - Stamping Fee

Cash balances that are not required for day to day obligations earn an interest of Prime minus 1.7% per annum. These interest rate fluctuations could impact the level of interest income earned by the Corporation.

PowerStream Inc.

Notes to the financial statements

December 31, 2009

(in thousands of dollars)

21. Financial instruments and risk management (continued)

(b) Risk management (continued)

(iii) Liquidity risk

Liquidity risks are those risks associated with the Corporation's inability to meet obligations associated with financial liabilities such as repayment of principal or interest payments on debts. The Corporation monitors its liquidity risks on a regular basis to ensure there is sufficient cash flow to meet the obligations as they fall due as well as minimize the interest expense. Cash flow forecasts are prepared to monitor liquidity risks. Liquidity risks associated with financial liabilities are as follows:

Maturity period	Principal *	Interest	Total
	\$	\$	\$
Less than 1 year	123,454	-	123,454
1-5 years	231,327	33,673	265,000
6-10 years	-	-	-
Over 10 years	166,102	133,621	299,723
	520,883	167,294	688,177

* The principal includes \$1,908 of deferred issuing cost amortization

(iv) Hedging and derivatives risk

The Corporation has not entered into hedging and derivative financial instruments and hence the Corporation is not exposed to risks of this nature. The Corporation does not have commodity price risk.

(v) Foreign exchange risk

The Corporation has minimal exposure to fluctuations in foreign currencies. The Corporation purchases goods and services from the US which are payable in US dollars, however the impact of these transactions to the financial statement are minimal.

In addition to the above, the Corporation maintains appropriate types and levels of insurance with major insurers. With respect to liability insurance, the Corporation is a member of the Municipal Electricity Association Reciprocal Insurance Exchange ("MEARIE"). A reciprocal insurance exchange may be defined as a group of persons formed for the purpose of exchanging reciprocal contracts of indemnity or inter-insurance with each other. MEARIE is licensed to provide general liability insurance to its members.

Insurance premiums charged to each member consist of a levy per thousands of dollars of service revenue subject to a credit or surcharge based on each member's claims experience. Coverage is provided to a level of \$24,000 per incident.

PowerStream Inc.

Notes to the financial statements

December 31, 2009

(in thousands of dollars)

22. Capital disclosures

The Corporation's main objectives in the management of capital are to:

- (i) Ensure that there is access to various funding options at the lowest possible rates for the various capital initiatives and working capital requirements necessary for the distribution business.
- (ii) Ensure compliance with various covenants related to its long-term/short-term debt, promissory notes and debentures.
- (iii) Consistently maintain a high credit rating for the Corporation.
- (iv) Maintain a split of 60% debt, 40% equity as recommended by the OEB.
- (v) Ensure interest rate fluctuations are mitigated primarily by long term borrowings as well as capital planning.
- (vi) Deliver appropriate financial returns to shareholders.

The Corporation considers shareholders' equity, long-term debt and certain short-term debt as its Capital. The capital structure as at December 31, 2009 is as follows:

	\$
Shareholders' equity	
Share capital	247,183
Retained earnings	21,064
Total	268,247
Short-term debt (Note 13)	40,000
Long-term debt (Note 12)	
Bank term loan	50,000
Debenture payable	123,091
Notes payable	182,430
Total	395,521
Total capital	663,768

As at December 31, 2009, the Corporation was in compliance with all covenants included in its short-term debt, bank term loan, debentures payable and notes payable. Details relating to debt covenants are disclosed in Note 12.

The Corporation is within the debt and equity requirements of the OEB.

The Corporation's dividend policy is disclosed in Note 18.

PowerStream Inc.

Notes to the financial statements

December 31, 2009

(in thousands of dollars)

23. Corporate income taxes

(a) Current taxes

The provision for payments in lieu of corporate income taxes (PILs) differs from the amount that would have been recorded using the combined Canadian federal and provincial statutory income tax rates. The reconciliation between the statutory and effective tax rates is provided as follows:

	\$
Income from operations before PILs	29,625
Statutory Canadian federal and provincial income tax rates	33.00%
<hr/>	
Expected tax provision on income at statutory rates	9,776
Increase (decrease) in income taxes resulting from timing differences:	
Amortization/CCA differences	(2,755)
Post employment benefits	305
Eligible capital expenditures	(227)
Other reserves	590
Revenue and overheads related to smart meters recognized for tax purposes but capitalized for accounting purposes	401
Other	577
Permanent differences	(106)
Provision for PILs	8,561
<hr/>	

(b) Future income tax assets and liabilities

As per CICA Handbook Section 3465, a future income tax asset or future income tax liability would be recognized for the tax effects that will arise if an asset is realized or a liability is settled for its carrying amount. Future income tax assets of \$61,665, and a corresponding regulatory liability of \$61,665 was recorded as at December 31, 2009.

24. Net change in non-cash operating working capital

	\$
Accounts receivable	(9,586)
Unbilled revenue	(11,501)
Income taxes recoverable	2,206
Inventories	126
Prepaid and other	96
Accounts payable, accrued liabilities and customers' deposits	(11,853)
Income taxes payable	5,034
<hr/>	
	(25,478)
<hr/>	

PowerStream Inc.

Notes to the financial statements

December 31, 2009

(in thousands of dollars)

25. Supplementary cash flow information

	\$
Cash paid during the year for:	
Interest	21,298
Payments in lieu of corporate income taxes	10,026

26. Net interest expense

	\$
Interest expense - notes payable, bank term loan, short-term debt and debentures payable	21,886
Interest income	(272)
	<u>21,614</u>

27. Guarantees

In the normal course of business, the Corporation enters into agreements that meet the definition of a guarantee as follows:

- (a) The Corporation has provided indemnities under lease agreements for the use of various operating facilities. Under the terms of these agreements the Corporation agrees to indemnify the counterparties for various items including, but not limited to, all liabilities, loss, suits, and damages arising during, on or after the term of the agreement. The maximum amount of any potential future payment cannot be reasonably estimated.
- (b) Indemnity has been provided to all directors and/or officers of the Corporation for various items including, but not limited to, all costs to settle suits or actions due to association with the Corporation, subject to certain restrictions. The Corporation has purchased directors' and officers' liability insurance to mitigate the cost of any potential future suits or actions. The term of the indemnification is not explicitly defined, but is limited to the period over which the indemnified party served as a trustee, director or officer of the Corporation. The maximum amount of any potential future payment cannot be reasonably estimated.
- (c) In the normal course of business, the Corporation has entered into agreements that include indemnities in favor of third parties, such as purchase and sale agreements, confidentiality agreements, engagement letters with advisors and consultants, outsourcing agreements, leasing contracts, information technology agreements and service agreements. These indemnification agreements may require the Corporation to compensate counterparties for losses incurred by the counterparties as a result of breaches in representation and regulations or as a result of litigation claims or statutory sanctions that may be suffered by the counterparty as a consequence of the transaction. The terms of these indemnities are not explicitly defined and the maximum amount of any potential reimbursement cannot be reasonably estimated.

The nature of these indemnification agreements prevents the Corporation from making a reasonable estimate of the maximum exposure due to the difficulties in assessing the amount of liability which stems from the unpredictability of future events and the unlimited coverage offered to counterparties. Historically, the Corporation has not made any significant payments under such or similar indemnification agreements and therefore no amount has been accrued in the balance sheet with respect to these agreements.

PowerStream Inc.

Notes to the financial statements

December 31, 2009

(in thousands of dollars)

28. Subsequent event

On March 16, 2010 Ontario Regulations 66/10 and 67/10 were filed for the purpose of creating a means for the Province of Ontario to recover \$53,695 from electricity distributors and the IESO relating to the period from April 1, 2009 to March 31, 2010 in order to partially fund conservation programs delivered by the Ministry of Energy and Infrastructure. Ontario Regulation 67/10 is an amendment to existing regulation 275/04, under the Ontario Energy Board Act, which deals with bill presentment for low volume consumers.

The Corporation is required to remit \$3,100, representing its apportioned amount to the Minister of Finance by July 30, 2010. The Corporation will be allowed to recover this apportioned amount through a uniform provincial kWh charge. A preliminary analysis estimates the charge to be about 0.037cents/kWh.