

Consolidated Financial Statements of

GUELPH MUNICIPAL HOLDINGS INC.

Year ended December 31, 2015
(Expressed in thousands of dollars)



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INDEPENDENT AUDITORS' REPORT

To the shareholder of Guelph Municipal Holdings Inc.

We have audited the accompanying consolidated financial statements of Guelph Municipal Holdings Inc., which comprise the consolidated balance sheet as at December 31, 2015 and the consolidated statements of comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the consolidated Financial Statements

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

Auditors' Responsibility

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

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

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



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Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of Guelph Municipal Holdings Inc. as at December 31, 2015 and its consolidated results of operations and its consolidated cash flows for the year ended December 31, 2015 in accordance with International Financial Reporting Standards.

KPMG LLP

Chartered Professional Accountants, Licensed Public Accountants

April 25, 2016
Waterloo, Canada

GUELPH MUNICIPAL HOLDINGS INC.

Consolidated Balance Sheets

December 31, 2015, with comparative information for 2014
(Expressed in thousands of dollars)

	2015	2014
Assets		
Current assets:		
Cash	\$ 32,556	\$ 2,680
Accounts receivable (note 4)	21,945	18,652
Unbilled revenue	15,284	10,889
Income taxes recoverable	-	1,706
Inventory (note 5)	2,181	1,832
Other current assets	649	627
Total current assets	72,615	36,386
Property, plant and equipment (note 6)	155,713	151,278
Intangible assets (note 7)	832	413
Deferred income taxes (note 8)	5,327	4,948
Deferred charges	-	40
Total non-current assets	161,872	156,679
Total assets	\$ 234,487	\$ 193,065

GUELPH MUNICIPAL HOLDINGS INC.

Consolidated Balance Sheets

December 31, 2015, with comparative information for 2014
(Expressed in thousands of dollars)

	2015	2014
Liabilities and Shareholder's Equity		
Current liabilities:		
Accounts payable and accrued liabilities	\$ 27,440	\$ 24,724
Income tax payable	4,336	-
Deferred credits - budget billing	858	1,142
Customer deposits - current portion (note 9)	2,651	5,577
<u>Total current liabilities</u>	<u>35,285</u>	<u>31,443</u>
Senior unsecured debentures (note 12)	94,245	64,600
Employee future benefits (note 11)	10,474	10,039
Customer deposits - long-term portion (note 9)	4,506	2,874
Deferred revenue	20,038	15,460
<u>Total non-current liabilities</u>	<u>129,263</u>	<u>92,973</u>
<u>Total liabilities</u>	<u>164,548</u>	<u>124,416</u>
Shareholder's equity:		
Share capital (note 18)	67,530	67,530
Other comprehensive loss	(933)	(933)
Retained earnings	3,342	2,052
	<u>69,939</u>	<u>68,649</u>
Commitments and contingencies (note 17)		
Guarantees (note 20)		
<u>Total liabilities and shareholder's equity</u>	<u>\$ 234,487</u>	<u>\$ 193,065</u>

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

On behalf of the Board:



Director



Director

GUELPH MUNICIPAL HOLDINGS INC.

Consolidated Statements of Comprehensive Income

Year ended December 31, 2015, with comparative information for 2014
(Expressed in thousands of dollars)

	2015	2014
Revenue:		
Electricity sales	\$ 242,665	\$ 212,562
Other services	978	917
	<u>243,643</u>	<u>213,479</u>
Cost of electricity sold	<u>201,233</u>	<u>190,885</u>
	42,410	22,594
Other operating revenue (note 13)	3,761	3,993
Net operating revenue	<u>46,171</u>	<u>26,587</u>
Expenses:		
Operations and maintenance	12,379	12,445
General and administrative	14,593	11,607
Impairment of property, plant and equipment	8,677	-
	<u>35,649</u>	<u>24,052</u>
Earnings before the undernoted	<u>10,522</u>	<u>2,535</u>
Financial and other expenses (income):		
Interest on notes payable, less amounts capitalized	3,643	3,323
Interest income	(132)	(113)
Other	114	99
	<u>3,625</u>	<u>3,309</u>
Earnings (loss) before undernoted	<u>6,897</u>	<u>(774)</u>
Income tax expense (recovery): (note 8)		
Provision for payments in lieu of corporate taxes	4,485	(403)
Deferred income taxes	(379)	1,131
	<u>4,106</u>	<u>728</u>
Net earnings (loss) from operations for the year	<u>2,791</u>	<u>(1,502)</u>
Other comprehensive income (loss):		
Actuarial losses on employee future benefit plans	-	(774)
Total comprehensive income (loss) for the year	<u>\$ 2,791</u>	<u>\$ (2,276)</u>

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

GUELPH MUNICIPAL HOLDINGS INC.

Consolidated Statements of Changes in Equity
(In thousands of Canadian dollars)

Year ended December 31, 2015, with comparative information for 2014

	Share capital	Other Comprehensive income (loss)	Retained earnings	Total
Balance at December 31, 2014	\$ 67,530	\$ (159)	\$ 5,054	\$ 72,425
Dividends	-	-	(1,500)	(1,500)
Total comprehensive loss for the year	-	(774)	(1,502)	(2,276)
Balance at December 31, 2014	67,530	(933)	2,051	68,648
Dividends	-	-	(1,500)	(1,500)
Total comprehensive income for the year	-	-	2,791	2,791
Balance, December 31, 2015	\$ 67,530	\$ (933)	\$ 3,342	\$ 69,939

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

GUELPH MUNICIPAL HOLDINGS INC.

Consolidated Statements of Cash Flows

Year ended December 31, 2015, with comparative information for 2014
(Expressed in thousands of dollars)

	2015	2014
Cash flows from operating activities:		
Total comprehensive income (loss) for the year	\$ 2,791	\$ (2,276)
Adjustments for:		
Income tax expense	4,106	449
Depreciation and amortization	6,972	6,352
Impairment of property, plant and equipment	8,677	-
Amortization of deferred revenue	(562)	(426)
Interest income	(132)	(113)
Interest expense	3,757	3,422
Gain on disposal of property, plant and equipment	(31)	22
	<u>25,578</u>	<u>7,430</u>
Change in:		
Accounts receivables	(3,293)	1,448
Unbilled revenue	(4,395)	(906)
Inventory	(349)	(328)
Other current assets	(22)	4
Deferred charges	40	-
Accounts payable and accrued liabilities	2,385	(80)
Deferred credits - budget billing	(284)	83
Employee future benefits	435	1,490
	<u>(5,483)</u>	<u>1,711</u>
Income taxes refunded	1,556	165
Net cash from operating activities	<u>21,651</u>	<u>9,306</u>
Cash flows from investing activities:		
Purchase of property, plant and equipment	(19,765)	(18,099)
Purchase of intangible assets	(602)	(168)
Proceeds from disposal of property, plant and equipment	42	90
	<u>(20,325)</u>	<u>(18,177)</u>
Cash flows from financing activities:		
Issuance of long term debentures	29,607	-
Contributions in aid of construction	5,140	2,372
Net change in customer deposits	(1,294)	2,135
Dividends paid	(1,500)	(1,500)
Interest paid	(3,535)	(3,520)
Interest received	132	113
	<u>28,550</u>	<u>(400)</u>
Increase (decrease) in cash	<u>29,876</u>	<u>(9,271)</u>
Cash, beginning of year	2,680	11,951
Cash, end of year	<u>\$ 32,556</u>	<u>\$ 2,680</u>

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

GUELPH MUNICIPAL HOLDINGS INC.

Notes to Consolidated Financial Statements

Year ended December 31, 2015

(Expressed in thousands of dollars)

1. Reporting entity:

Guelph Municipal Holdings Inc. (the "Corporation" or "GMHI") is wholly-owned by the City of Guelph. GMHI was incorporated on August 16, 2011 under the laws of the Province of Ontario, Canada. The address of the Corporation's registered office is 395 Southgate Drive, Guelph, Ontario.

As a result of the Corporation's amalgamation with Guelph Hydro Inc. ("GHI") on September 6, 2014, the principal activity of the Corporation, via its wholly-owned subsidiary, Guelph Hydro Electric Systems Inc. ("GHESI"), is to distribute electricity to the residents and businesses in the City of Guelph and the Village of Rockwood under a license issued by the Ontario Energy Board ("OEB"). GHESI is regulated by the OEB and adjustments to GHESI's distribution rates require OEB approval. The Corporation, via its wholly-owned subsidiary, Envida Community Energy Inc. ("Envida"), also as a result of the above noted amalgamation, owns generation assets that produce electricity, and district energy assets that distribute thermal energy.

These financial statements are presented on a consolidated basis and include the following subsidiaries: Guelph Hydro Electric Systems Inc. and Envida Community Energy Inc. Hereafter, for purposes of these notes, unless specifically referenced, any and all references to rate regulation or regulatory activities of the Corporation imply the activities of the Corporation's regulated subsidiary, GHESI.

2. Basis of presentation:

(a) Statement of compliance:

The Corporation's financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as adopted by the International Accounting Standards Board ("IASB") and interpretations as issued by the International Financial Reporting Interpretations Committee ("IFRIC") of the IASB.

(b) Approval of the financial statements:

The financial statements were approved by the Board of Directors on April 25, 2016.

(c) Basis of measurement:

The financial statements have been prepared on the historical cost basis except for the following:

- (i) Where held, financial instruments at fair value through profit or loss, including those held for trading, are measured at fair market value.
- (ii) Contributed assets are initially measured at fair market value.

The methods used to measure fair values are discussed further in note 3 (c) and note 20.

GUELPH MUNICIPAL HOLDINGS INC.

Notes to Consolidated Financial Statements, continued

Year ended December 31, 2015
(Expressed in thousands of dollars)

2. Basis of presentation (continued):

(d) Functional and presentation currency:

These financial statements are presented in Canadian dollars, which is the Corporation's functional currency. All financial information presented in Canadian dollars has been rounded to the nearest thousand.

(e) Use of estimates and judgments:

The preparation of financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses and disclosure of contingent assets and liabilities. Actual results may differ from those estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the year in which the estimates are revised and in any future periods affected.

In particular, information about significant areas of estimation uncertainty and critical judgments in applying accounting policies that have the most significant effect on the amounts recognized in these financial statements is included in the following notes:

- (i) Note 4 and Note 19(a) – Receivables: allowance for impairment
 - (ii) Note 6 – Property, plant and equipment: impairment, useful lives and the identification of significant components of property, plant and equipment
 - (iii) Note 8 – Income taxes: utilization of tax losses
 - (iv) Note 11 – Employee future benefits: measurement of the defined benefit obligation
 - (v) Note 17 – Commitments and contingencies
 - (vi) Note 19 – Financial instruments and risk management: valuation of long-term debt.
- (f) Rate regulation:

Effect of rate-setting regulations on the Corporation's activities and on these financial statements:

GHESI is regulated by the OEB, under the authority granted by the *Ontario Energy Board Act (1988)*. Among other things, the OEB has the power and responsibility to approve or set rates for the transmission and distribution of electricity, to provide continued rate protection for rural and remote electricity consumers, and to ensure that distribution companies fulfill obligations to connect and service customers. In its capacity to approve or set rates, the OEB has the authority to specify regulatory accounting treatments that may differ from IFRS for enterprises operating in a non-rate regulated environment.

GUELPH MUNICIPAL HOLDINGS INC.

Notes to Consolidated Financial Statements, continued

Year ended December 31, 2015

(Expressed in thousands of dollars)

2. Basis of presentation (continued):

On August 16, 2013, GHESI filed its 2014 electricity distribution rates application using the OEB's 4th Generation IRM as the basis for its application. The OEB rendered its Decision on December 5, 2013 which approved a distribution rate increase of 1.4 per cent for all customers.

On August 13, 2014, GHESI filed its 2015 electricity distribution rates application using the OEB's 4th Generation IRM as the basis for its application. The OEB rendered its Decision on December 4, 2014 which approved a distribution rate increase of 1.3 per cent for all customers.

In addition to the distribution rate increase, the OEB approved GHESI's recovery of deferral and variance account balances in the amount of \$6.9 million to be recovered over a one-year period. These recoveries relate to past difference between the costs charged by the IESO and Hydro One (including whole market, transmission connection and network, commodity, global adjustment, and low voltage charges) and OEB-approved non-distribution charges billed to GHESI's customers.

On April 24, 2015, GHESI filed a cost of service rate application for its 2016 electricity distribution rates application. The OEB rendered its Decision on November 26, 2015 which approved a distribution rate increase of 4.86 per cent for all customers.

The continuing restructuring of Ontario's electricity industry and other regulatory developments, including current and possible future consultation between the OEB and interested stakeholders may affect the distribution rates that GHESI may charge and the costs that GHESI may recover, including the balance of its regulatory assets.

3. Significant accounting policies:

The accounting policies set out below have been applied consistently in all years presented in these consolidated financial statements.

(a) Cash and cash equivalents:

Cash equivalents include short-term investments with maturities of three months or less when purchased.

(b) Revenue recognition:

Revenue for GHESI is recognized as electricity is delivered to customers and is recorded on the basis of regular meter readings and estimated customer usage since the last meter reading date to the end of the year. The related cost of power is recorded on the basis of power used.

GUELPH MUNICIPAL HOLDINGS INC.

Notes to Consolidated Financial Statements, continued

Year ended December 31, 2015
(Expressed in thousands of dollars)

3. Significant accounting policies (continued):

GHESI is licensed by the OEB to distribute electricity. As a licensed distributor, GHESI is responsible for billing customers for electricity generated by third parties and the related costs of providing electricity service, such as transmission services and other services provided by third parties. GHESI is required, pursuant to regulation, to remit such amounts to these third parties, irrespective of whether GHESI ultimately collects these amounts from customers. GHESI has determined that it is acting as a principal for the electricity distribution and, therefore, has presented electricity revenue on a gross basis.

Customer billings for debt retirement charges are recorded on a net basis as GHESI acts as an agent for this revenue stream. GHESI may file to recover uncollected debt retirement charges from Ontario Electricity Financial Corporation ("OEFC") once each year.

Deferred revenue relating to contributions in aid of construction is amortized to income on a straight-line basis over the terms of the agreement with the customer or the economic useful life of the acquired or contributed asset, which represents the period of ongoing service to the customer.

All other revenues are recorded on a gross basis and are recognized when services are rendered.

Revenue for Envida is recorded on the basis of regular meter readings recording electricity production at the generation plant, solar energy facilities as well as the district energy combined heat and power facilities. In addition, there is a small amount of contracted fixed revenue being generated by the district energy combined heat and power business.

(c) Inventory:

Inventory is valued at the lower of cost and net realizable value, with cost being determined on an average cost basis, and items considered major spare parts are recorded as capital assets.

(d) Property, plant and equipment:

Items of property, plant and equipment are measured at cost or deemed cost established on the transition date, or, where the item is transferred from customers, its fair value, less accumulated depreciation and accumulated impairment losses.

Cost includes expenditures that are directly attributable to the acquisition of the asset. The cost of self-constructed assets includes the cost of materials and direct labour, and any other costs directly attributable to bringing the asset to a working condition for its intended use.

Borrowing costs on qualifying assets are capitalized as part of the cost of the asset and are based on the Corporation's average cost of borrowing.

When parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate items (major components) of property, plant and equipment.

The cost of replacing part of an item of property, plant and equipment is recognized in the carrying amount of the item if it is probable that the future economic benefits embodied within

GUELPH MUNICIPAL HOLDINGS INC.

Notes to Consolidated Financial Statements, continued

Year ended December 31, 2015

(Expressed in thousands of dollars)

3. Significant accounting policies (continued):

the part will flow to the Corporation and its cost can be measured reliably. The carrying amount of the replaced part is written off, and the related gain or loss is included in profit or loss. The costs of the day-to-day servicing of property, plant and equipment are recognized in profit or loss as incurred.

Depreciation is recognized in profit or loss on a straight-line basis over the estimated useful life of each part or component of an item of property, plant and equipment. Land is not depreciated. Construction-in-progress assets are not amortized until the project is complete and in service. The estimated useful lives are as follows:

Buildings and fixtures	15 - 50 years
Distribution lines	40 - 70 years
Distribution transformers	35 - 55 years
Distribution meters	30 years
Smart meters	15 years
Electricity generation equipment	10 - 15 years
District energy equipment	10 - 50 years
General office equipment	5 - 10 years
Computer equipment	5 years
Major tools	5 - 15 years
Data acquisition system	5 years
Trucks and rolling stock	5 - 10 years
Other capital assets	10 - 45 years

Depreciation methods, useful lives, and residual values are reviewed at each reporting date.

(e) Intangible assets:

(i) Computer software:

Computer software that is acquired or developed by the Corporation, including software that is not integral to the functionality of equipment purchased which has finite useful lives, is measured at cost less accumulated amortization and accumulated impairment losses.

(ii) Land rights:

Payments to obtain rights to access land ("land rights") are classified as intangible assets. These include payments made for easements, right of access and right of use over land for which the Corporation does not hold title. Land rights are measured at cost less accumulated amortization and accumulated impairment losses.

GUELPH MUNICIPAL HOLDINGS INC.

Notes to Consolidated Financial Statements, continued

Year ended December 31, 2015

(Expressed in thousands of dollars)

3. Significant accounting policies (continued):

(iii) Amortization:

Amortization is recognized in profit or loss on a straight-line basis over the estimated useful lives of intangible assets, other than goodwill, from the date that they are available for use. The estimated useful lives for the current and comparative years are:

Computer software	5 years
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Amortization methods and useful lives of all intangible assets are reviewed at each reporting date.

(f) Impairment:

(i) Financial assets:

A financial asset is assessed at each reporting date to determine whether there is any objective evidence that it is impaired. A financial asset is considered to be impaired if objective evidence indicates that one or more events have had a negative effect on the estimated future cash flows of that asset.

An impairment loss in respect of a financial asset measured at amortized cost is calculated as the difference between its carrying amount, and the present value of the estimated future cash flows discounted at the original effective interest rate. Interest on the impaired assets continues to be recognized through the unwinding of the discount.

All impairment losses are recognized in profit or loss. An impairment loss is reversed if the reversal can be related objectively to an event occurring after the impairment loss was recognized. For financial assets measured at amortized cost the reversal is recognized in profit or loss.

(ii) Non-financial assets:

The carrying amounts of the Corporation's non-financial assets, other than inventories and deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated.

For the purpose of impairment testing, assets are grouped together into the smallest group of assets that generate cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets (the "cash-generating unit"). The Corporation has determined that it has two cash-generating units being GHESI and Envida. The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax

GUELPH MUNICIPAL HOLDINGS INC.

Notes to Consolidated Financial Statements, continued

Year ended December 31, 2015

(Expressed in thousands of dollars)

3. Significant accounting policies (continued):

discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

An impairment loss is recognized if the carrying amount of an asset or its cash-generating unit exceeds its estimated recoverable amount. Impairment losses are recognized in profit or loss.

For assets other than goodwill, impairment recognized in prior periods is assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortization, if no impairment loss had been recognized.

(g) Provisions:

A provision is recognized if, as a result of a past event, the Corporation has a current legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability.

Decommissioning or dismantling:

When there is a legal or constructive obligation to remove and dispose of property, plant and equipment at the end of their useful life, a provision is recorded to cover such future removal and disposal costs.

(h) Employee future benefits:

i. Pension plan:

The Corporation provides a pension plan for its full-time employees through the Ontario Municipal Employees Retirement System ("OMERS"). OMERS is a multi-employer pension plan which operates as the Ontario Municipal Employees Retirement Fund ("the Fund"), and provides pensions for employees of Ontario municipalities, and public utilities. The Fund is a contributory defined benefit pension plan, which is financed by equal contributions from participating employers and employees, and by the investment earnings of the Fund.

ii. Post-employment benefits, other than pension:

The Corporation provides some of its retired employees with life insurance and medical benefits beyond those provided by government sponsored plans.

The cost of these benefits is expensed as earned by employees through employment service. The accrued benefit obligations and the current service costs are actuarially determined by applying the projected unit credit method and reflect management's best

GUELPH MUNICIPAL HOLDINGS INC.

Notes to Consolidated Financial Statements, continued

Year ended December 31, 2015

(Expressed in thousands of dollars)

3. Significant accounting policies (continued):

estimate of certain underlying assumptions. Any actuarial gains (losses) will require a re-measurement of the net defined benefit liability or asset and will be recognized as other comprehensive income or loss in the year that it is known.

(i) Deferred revenue and assets transferred from customers:

Certain customers and developers are required to contribute towards the capital cost of construction in order to provide ongoing service. Cash contributions are initially recorded as current liabilities. Once the distribution system asset is completed or modified as outlined in the terms of the contract, the contribution amount is transferred to contributions in aid of construction.

When an asset is received as a capital contribution, the asset is initially recognized at its fair value, with the corresponding amount recognized as contributions in aid of construction.

The contributions in aid of construction account, which represents GHESI's obligation to continue to provide the customers access to the supply of electricity, is reported as deferred revenue, and is amortized to income on a straight-line basis over the terms of the agreement with the customer or the economic useful life of the acquired or contributed asset, which represents the period of ongoing service to the customer.

(j) Leased assets:

Leases in terms of which the Corporation assumes substantially all the risks and rewards of ownership are classified as finance leases. Upon initial recognition, the leased asset is measured at an amount equal to the lower of its fair value and the present value of the minimum lease payments. Subsequent to initial recognition, the asset is accounted for in accordance with the accounting policy applicable to that asset.

Other leases are operating leases and the leased assets are not recognized on the Corporation's balance sheet. Payments made under operating leases are recognized in profit or loss on a straight-line basis over the term of the lease.

(k) Finance income and finance costs:

Finance income is recognized as it accrues in profit or loss, using the effective interest method. Finance income comprises interest earned on cash and cash equivalents and on regulatory assets.

Finance costs comprise interest expense on borrowings, finance lease obligations, regulatory liabilities and unwinding of the discount on provisions and impairment losses on financial assets.

(l) Income taxes:

The income tax expense comprises current and deferred tax. Income tax expense is recognized in profit or loss except to the extent that it relates to items recognized directly in equity, in which case, it is recognized in equity.

GUELPH MUNICIPAL HOLDINGS INC.

Notes to Consolidated Financial Statements, continued

Year ended December 31, 2015
(Expressed in thousands of dollars)

3. Significant accounting policies (continued):

Under the *Electricity Act*, 1998, the Corporation makes payments in lieu of corporate taxes to the OEFC. These payments are calculated in accordance with the rules for computing taxable income and taxable capital and other relevant amounts contained in the *Income Tax Act (Canada)* and the *Corporations Tax Act (Ontario)* as modified by the *Electricity Act, 1998*, and related regulations. Prior to October 1, 2001, the Corporation was not subject to income or capital taxes. Payments in lieu of taxes are referred to as income taxes.

Current tax is the tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognized using the balance sheet method. Under this method, deferred income taxes reflect the net tax effects of temporary differences between the tax basis of assets and liabilities and their carrying amounts for accounting purposes, as well as for tax losses available to be carried forward to future years that are likely to be realized. Deferred tax assets and liabilities are measured using enacted or substantively enacted tax rates, at the reporting date, expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the year that includes the date of enactment or substantive enactment.

4. Accounts receivable:

	2015	2014
Revenue	\$ 19,419	\$ 16,368
Regulatory	867	1,047
Due from the City of Guelph	1,894	1,612
	22,180	19,027
Less allowance for doubtful accounts	(235)	(375)
	\$ 21,945	\$ 18,652

5. Inventory:

The amount of inventories consumed by the Corporation and recognized as an expense during 2015 was \$ 243 (2014 - \$211).

GUELPH MUNICIPAL HOLDINGS INC.

Notes to Consolidated Financial Statements, continued

Year ended December 31, 2015
(Expressed in thousands of dollars)

6. Property, plant and equipment:

(a) Cost or deemed cost:

	Land and buildings	Distribution equipment	Electricity generation equipment	Other fixed assets	Construction -in-Progress	Alternative Energy Projects	Total
Bal. at January 1, 2014	\$ 21,420	\$ 122,631	\$ 830	\$ 8,258	\$ 6,428	\$ -	\$ 159,567
Additions	484	5,403	-	2,487	9,848	-	18,222
Transfers	-	2,981	-	-	(9,647)	6,666	-
Disposals/retirements	-	-	-	(132)	-	-	(132)
Bal. at Dec. 31, 2014	\$ 21,904	\$ 131,015	\$ 830	\$ 10,613	\$ 6,629	\$ 6,666	\$ 177,657

	Land and buildings	Distribution equipment	Electricity generation equipment	Other fixed assets	Construction -in-Progress	Alternative Energy Projects	Total
Bal. at January 1, 2015	\$ 21,904	\$ 131,015	\$ 830	\$ 10,613	\$ 6,629	\$ 6,666	\$ 177,657
Additions	76	6,848	190	1,400	6,484	4,914	19,912
Transfers	-	4,675	-	-	(4,675)	-	-
Disposals/retirements	-	-	-	(112)	-	-	(112)
Impairment of property, plant and equipment	-	-	-	-	-	(8,677)	(8,677)
Bal. at Dec. 31, 2015	\$ 21,980	\$ 142,538	\$ 1,020	\$ 11,901	\$ 8,438	\$ 2,903	\$ 188,780

(b) Accumulated depreciation:

	Land and buildings	Distribution equipment	Electricity generation equipment	Other fixed assets	Construction -in-Progress	Alternative Energy Projects	Total
Bal. at January 1, 2014	\$ 2,359	\$ 13,897	\$ 331	\$ 3,566	\$ -	\$ -	\$ 20,153
Dep'n charge for the year	794	3,616	83	1,655	-	98	6,246
Disposals/retirements	-	-	-	(20)	-	-	(20)
Bal. at Dec. 31, 2014	\$ 3,153	\$ 17,513	\$ 414	\$ 5,201	\$ -	\$ 98	\$ 26,379

GUELPH MUNICIPAL HOLDINGS INC.

Notes to Consolidated Financial Statements, continued

Year ended December 31, 2015

(Expressed in thousands of dollars)

6. Property, plant and equipment (continued):

(b) Accumulated depreciation (continued):

	Land and buildings	Distribution equipment	Electricity generation equipment	Other fixed assets	Construction -in-Progress	Alternative Energy Projects	Total
Bal. at January 1, 2015	\$ 3,153	\$ 17,513	\$ 414	\$ 5,201	\$ -	\$ 98	\$ 26,379
Dep'n charge for the year	807	4,402	104	1,237	-	239	6,789
Disposals/retirements	-	-	-	(101)	-	-	(101)
Bal. at Dec. 31, 2015	\$ 3,960	\$ 21,915	\$ 518	\$ 6,337	\$ -	\$ 337	\$ 33,067

(c) Carrying amounts:

	Land and buildings	Distribution equipment	Electricity generation equipment	Other fixed assets	Construction -in-Progress	Alternative Energy Projects	Total
December 31, 2014	\$18,751	\$ 113,502	\$ 304	\$ 2,543	\$ 9,610	\$ 6,568	\$ 151,278
December 31, 2015	18,020	120,623	502	5,564	8,438	2,566	155,713

(d) Borrowing costs:

During the year, borrowing costs of \$148 (2014 - \$123) were capitalized as part of the cost of property, plant and equipment.

(e) Allocation of depreciation and amortization:

The depreciation of property, plant and equipment and the amortization of intangible assets has been allocated to profit or loss as follows:

	Cost of electricity sold	Distribution expenses	Administration expenses	Total
December 31, 2014:				
Depreciation of property, plant and equipment	\$ -	\$ 6,089	\$ 157	\$ 6,246
Amortization of intangible assets	-	-	106	106
	\$ -	\$ 6,089	\$ 263	\$ 6,352

GUELPH MUNICIPAL HOLDINGS INC.

Notes to Consolidated Financial Statements, continued

Year ended December 31, 2015
(Expressed in thousands of dollars)

6. Property, plant and equipment (continued):

e) Allocation of depreciation and amortization (continued):

	Cost of electricity sold	Distribution expenses	Administration expenses	Total
December 31, 2015:				
Depreciation of property, plant and equipment	\$	\$ 6,692	\$ 97	\$ 6,789
Amortization of intangible assets		-	183	183
	\$	\$ 6,692	\$ 280	\$ 6,972

f) Impairment of fixed assets:

	Cost	Accumulated Depreciation	Total
Hanlon Creek Business Park	\$ 5,170	\$ 116	\$ 5,054
Galt District Energy System	3,776	153	3,623
	\$ 8,946	\$ 269	\$ 8,677

(i) Assessment:

At December 31, 2015, due to continuing negative business segment cash flows, poor economic performance and the re-evaluation of its business contracts, the Company determined that these financial impairment triggers were present on its district energy cash generating units (DE CGU's). The Company tested its DE CGU's for impairment. The recoverable amounts of the Company's DE CGU's were estimated as the value-in-use based on the net present value of the before-tax cash flows from DE operations. The cash inflows were estimated using the remaining contract periods for current customers. The cash outflows were projected for the remaining contract periods based on the Company's detailed business plan for the business segment for the upcoming 2016 year.

In determining the appropriate discount rate of 4.17%, the Company applied the long term Bank of Canada Bond rate of 2.32% as the risk free rate and included an additional 1.85% premium to reflect an appropriate risk factor related to future cash flows.

GUELPH MUNICIPAL HOLDINGS INC.

Notes to Consolidated Financial Statements, continued

Year ended December 31, 2015

(Expressed in thousands of dollars)

6. Property, plant and equipment (continued):

(ii) Results of 2015 assessment:

At December 31, 2015 it was determined that the net book value of the Company's DE CGUs exceeded the recoverable amount and the Company recognized \$8,677 in impairment charges.

7. Intangible assets:

(a) Cost or deemed cost:

	Computer software	Land rights	Total
Balance at January 1, 2014	\$ 448	\$ 24	\$ 472
Additions in 2014	167	1	168
Balance at December 31, 2014	615	25	640
Additions in 2015	602	-	602
Balance at December 31, 2015	\$ 1,217	\$ 25	\$ 1,242

(b) Accumulated amortization:

	Computer software	Land rights	Total
Balance at January 1, 2014	\$ 121	\$ -	\$ 121
Amortization charges in 2014	106	-	106
Balance at December 31, 2014	227	-	227
Amortization charges in 2015	183	-	183
Balance at December 31, 2015	\$ 410	\$ -	\$ 410

(c) Carrying amounts:

	Computer software	Land rights	Total
Balance at December 31, 2014	\$ 388	\$ 25	\$ 413
Balance at December 31, 2015	\$ 807	\$ 25	\$ 832

GUELPH MUNICIPAL HOLDINGS INC.

Notes to Consolidated Financial Statements, continued

Year ended December 31, 2015

(Expressed in thousands of dollars)

8. Income taxes:

The income tax expense varies from amounts which would be computed by applying the Corporation's combined statutory income tax rate as follows:

	2015	2014
Basic rate applied to earnings (loss) before income tax	\$ 1,828	\$ (205)
Increase (decrease) in income tax resulting from:		
Losses not recognized for tax	2,501	967
Adjustment to prior year's taxes	(223)	(34)
Income tax expense	\$ 4,106	\$ 728
Effective rate applied to profit (loss) before income taxes	59.5%	94.1%

Significant components of the Corporation's deferred tax balances are as follows:

	2015	2014
Deferred tax assets (liabilities):		
Property, plant and equipment	\$ (6,215)	\$ (4,647)
Cumulative eligible capital	648	648
Employee benefits	2,776	2,660
Deferred Revenue – Contributed Capital	5,310	4,097
Non-capital loss carry forwards	2,808	2,190
Net deferred tax asset	\$ 5,327	\$ 4,948

At December 31, 2015, based on substantively enacted income tax rates, deferred tax assets of \$1,945 (2014 - \$2,103) have not been recorded. These deferred tax assets relate to tax bases of depreciable capital assets and employee future benefits in excess of amounts recorded for accounting purposes. Such deferred tax assets have not been recorded in the accounts as there is uncertainty as to whether the Corporation will realize the benefits related to these assets which would be realized as relatively modest reductions of future tax liability over many future years.

At December 31, 2015, a deferred tax asset of \$5,327 (2014 - \$4,948) has been recorded. The utilization of this tax asset is dependent on future taxable profits in excess of profits arising from the reversal of existing taxable temporary differences.

GUELPH MUNICIPAL HOLDINGS INC.

Notes to Consolidated Financial Statements, continued

Year ended December 31, 2015
(Expressed in thousands of dollars)

9. Customer deposits:

Customer deposits represent cash deposits from electricity distribution customers and retailers, as well as construction deposits.

Deposits from electricity distribution customers are refundable to customers demonstrating an acceptable level of credit risk as determined by the Corporation in accordance with policies set out by the OEB or upon termination of their electricity distribution service.

Construction deposits represent cash prepayments for the estimated cost of capital projects recoverable from customers and developers. Upon completion of the capital project, these deposits are transferred to contributions in aid of construction.

Customer deposits comprise:

	2015	2014
Customer deposits	\$ 2,504	\$ 4,040
Construction deposits	4,653	4,411
Total customer deposits	\$ 7,157	\$ 8,451

10. Pension agreement:

The Corporation provides a pension plan for its employees through the Ontario Municipal Employees Retirement System ("OMERS"). OMERS is a multi-employer pension plan which operates as the Ontario Municipal Employee Retirement Fund (the "Fund") and provides pensions for employees of Ontario municipalities and public utilities. The Fund is a contributory defined benefit pension plan, which is financed by equal contributions from participating employers and employees, and by the investment earnings of the Fund. The Corporation uses defined contribution plan accounting as it is only liable for contributions to the Plan. The Corporation's contribution for employees' current service for the year ended December 31, 2015 was \$1,096 (2014 - \$1,054).

GUELPH MUNICIPAL HOLDINGS INC.

Notes to Consolidated Financial Statements, continued

Year ended December 31, 2015
(Expressed in thousands of dollars)

11. Employee future benefits:

Components of employee future benefits recognized are as follows:

	2015	2014
Post-retirement benefits - accrued benefit liability, as previously reported	\$ 9,814	\$ 9,359
Accrued sick leave benefit	660	681
	<u>\$ 10,474</u>	<u>\$ 10,040</u>

Post-retirement benefits:

The Corporation pays certain medical and life insurance benefits on behalf of some of its retired employees. The Corporation recognizes these post-retirement costs in the period in which employees' services were rendered. The accrued benefit liability at December 31, 2015 of \$9,814 was based on an actuarial valuation completed in 2014 using a discount rate of 4.05%. The restated accrued benefit liability at December 31, 2014 of \$9,359 (previously reported to be \$7,929) and the expense for the year ended December 31, 2014, were based on an actuarial valuation completed in 2014, using a discount rate of 4.05%.

GUELPH MUNICIPAL HOLDINGS INC.

Notes to Consolidated Financial Statements, continued

Year ended December 31, 2015

(Expressed in thousands of dollars)

11. Employee future benefits (continued):

Changes in the present value of the defined benefit unfunded obligation and the accrued benefit liability:

	2015	2014
Defined benefit obligation, beginning of year	\$ 9,359	\$ 7,929
Current service cost	273	211
Interest cost	374	387
Re-measurement of obligation	-	1,053
Benefits paid during the year	(192)	(221)
Accrued benefit liability, end of year	\$ 9,814	\$ 9,359

Components of net benefit expense recognized are as follows:

	2015	2014
Current service cost	\$ 273	\$ 211
Interest cost	374	387
Net benefit expense recognized	\$ 647	\$ 598

The full amount of the Corporation's net benefit expense was charged to operations in 2014 and 2015.

GUELPH MUNICIPAL HOLDINGS INC.

Notes to Consolidated Financial Statements, continued

Year ended December 31, 2015

(Expressed in thousands of dollars)

11. Employee future benefits (continued):

The significant actuarial assumptions used in the valuation are as follows (weighted average):

	2015	2014
Accrued benefit obligation:		
Discount rate	4.05%	4.05%
Benefit cost for the year:		
Withdrawal rate	1%	1%
Assumed health care cost trend rates:		
Initial health care cost trend rate	5%	5%

The approximate effect on the accrued benefit obligation of the entire plan and the estimated net benefit expense of the entire plan if the health care trend rate assumption was increased or decreased by 1%, and all other assumptions were held constant, is as follows:

	Defined Benefit Obligation	Periodic Benefit Cost
1% increase in health care trend rate	\$ 11,542	\$ 787
1% decrease in health care trend rate	8,348	538

Historical information

Amounts for the current and previous year, for the entire plan, are as follows:

	2015	2014
Defined benefit obligation	\$ 9,814	\$ 9,359
Experience adjustments	-	1,053

GUELPH MUNICIPAL HOLDINGS INC.

Notes to Consolidated Financial Statements, continued

Year ended December 31, 2015
(Expressed in thousands of dollars)

11. Employee future benefits (continued):

The main actuarial assumptions utilized for the valuation are as follows:

General inflation - future general inflation levels, as measured by the changes in the Consumer Price Index, were assumed 2.0% in 2015, and thereafter (2014 - 2.0%).

Discount (interest) rate - the discount rate used to determine the present value of future liabilities and the expense for the year ended December 31, 2015, was 4.05% (2014 - 4.05%).

Historical information

Salary levels - future general salary and wage levels were assumed to increase at 3.3% (2014 - 3.3%) per annum.

Medical costs - medical costs were assumed to increase 5% for 2014, 5% for 2015, 5% for 2016, and 5% thereafter.

Dental costs - dental costs were assumed to increase 5% for 2014, 5% for 2015, 5% for 2016, and 5% thereafter.

Accrued sick leave benefit:

The Corporation allows regular employees the equivalent of one and one-half days per month sick time credit to be applied in case of illnesses or accidents not covered by Workers' Compensation. A maximum of eighteen days sick time credit is accrued to each employee's credit each year and is reduced by the amount of sick time utilized each year. At the end of the year, the remaining credit if any is added to each employee's sick time credit accumulation. Any unused sick time credit is forfeited when employment ceases with the Corporation. As at December 31, 2015 the estimated valued of the expected future payment to be made as a result of the unused sick time credits amounted to \$660 (2014 - \$681).

GUELPH MUNICIPAL HOLDINGS INC.

Notes to Consolidated Financial Statements, continued

Year ended December 31, 2015
(Expressed in thousands of dollars)

12. Long-term debt:

(a) Loan payable to the Federation of Canadian Municipalities:

On May 17, 2014, Envida elected to retire its loan payable to the Federation of Canadian Municipalities which had a maturity date of June 30, 2018 and which bore interest at a rate of 2.37%. In addition to repaying the outstanding principal of \$825, Envida also paid an early payment penalty of \$17 plus accrued interest since the last interest payment of \$7. In order to make this lump sum payment, Envida replaced this loan payable with a promissory note from its parent company Guelph Municipal Holdings Inc.

b) Senior unsecured debentures

The Series "A" senior unsecured debentures have a maturity date of December 6, 2030 and have an interest rate of 5.264% per annum. Interest is payable in equal semi-annual installments, in arrears, on June 6 and December 6 each year commencing June 6, 2014 until maturity. The debentures were issued on December 6, 2013. The debentures are represented by a single Global Debenture Certificate registered in the name of CDS & Co. In order to put the debentures in place, the Corporation incurred debt issuance costs in the amount of \$500.

The Series "B" senior unsecured debentures have a maturity date of September 25, 2045 and have an interest rate of 4.121% per annum. Interest is payable in equal semi-annual installments, in arrears, on March 25 and September 25 each year commencing March 25, 2016 until maturity. The debentures were issued on September 25, 2015. The debentures are represented by a single Global Debenture Certificate registered in the name of CDS & Co. In order to put the debentures in place, the Corporation incurred debt issuance costs in the amount of \$393.

	2015	2014
Senior unsecured debentures, maturity 2030	\$ 65,000	\$ 65,000
Senior unsecured debentures, maturity 2045	30,000	-
Less: cost of debt issuance	(755)	(400)
Senior unsecured debentures, net proceeds	\$ 94,245	\$ 64,600

GUELPH MUNICIPAL HOLDINGS INC.

Notes to Consolidated Financial Statements, continued

Year ended December 31, 2015

(Expressed in thousands of dollars)

13. Other income:

Other income comprises:

	2015	2014
Late payment charges	\$ 152	\$ 116
Pole and other rental income	432	343
Collection and other service charges	410	436
Waterworks revenue	1,244	1,172
Customer contributions	562	426
Conservation and Demand Management Performance Bonus	-	1,255
Miscellaneous	961	245
Total other income	\$ 3,761	\$ 3,993

14. Employee benefits:

	2015	2014
Salaries and wages	\$ 10,916	\$ 10,000
Contributions to multi-employer plan	1,096	1,054
Expenses related to defined benefit plans	647	598
	\$ 12,659	\$ 11,652

15. Finance income and expense:

	2015	2014
Interest income on bank deposits	\$ (132)	\$ (113)
Finance income	(132)	(113)
Interest expense on long-term debt	3,794	3446
Interest adjustment re: capitalized borrowing costs	(148)	(123)
Interest expense on deposits	32	27
Other	79	72
	3,757	3,422
Net finance costs recognized in profit or loss	\$ 3,625	\$ 3,309

GUELPH MUNICIPAL HOLDINGS INC.

Notes to Consolidated Financial Statements, continued

Year ended December 31, 2015

(Expressed in thousands of dollars)

16. Related party transactions:

a) Parent and ultimate controlling party:

The sole shareholder of the Corporation is Guelph Municipal Holdings Inc. ("GMHI"), which in turn is wholly-owned by the City of Guelph. The City produces financial statements that are available for public use.

b) Key management personnel:

The key management personnel of the Corporation has been defined as members of its board of directors and executive management team members and is summarized in the table below.

	2015	2014
Directors' fees	\$ 181	\$ 196
Salaries and other short-term benefits	3,348	2,778
Post-employment benefits	48	62
	<u>\$ 3,577</u>	<u>\$ 3,036</u>

c) Transactions with ultimate parent (the City):

The following summarizes the Corporation's related party transactions, recorded at the exchange amounts and balances with the City for the year ended December 31:

	2015	2014
Revenue:		
Energy sales (at commercial rates)	\$ 8,245	\$ 8,238
Energy sales (solar & district energy)	195	95
Waterworks revenue	1,243	1,172
Street light maintenance	353	303
Expenses:		
Subcontracting	7	16
Rent, percentage rent, land lease	53	60
Property taxes	327	327
Balances:		
Accounts receivable	1,894	1,612
Accounts payable and accrued charges	53	343

GUELPH MUNICIPAL HOLDINGS INC.

Notes to Consolidated Financial Statements, continued

Year ended December 31, 2015
(Expressed in thousands of dollars)

16. Related party transactions (continued):

- d) Transactions with subsidiaries of the City:

A listing of the various entities under the control of the City is set out on the City's website.

The Corporation's transactions with subsidiaries of the City consist of sales of electricity at market rates.

17. Commitments and contingencies:

In November 2004, Envida entered into a renewable energy supply contract with the OEFC. In November 2005, the agreement was assigned by the OEFC to the Ontario Power Authority ("OPA"). Under this agreement, Envida has agreed to supply contract energy up to a maximum amount for twenty years at a price fixed by the contract.

In 2012, the renewable supply agreement with the OPA was amended by re-setting the capacity to be delivered under the contract. The amended agreement sets the contract capacity of the landfill generator to 2.5 MW for the seven contract-years, and 1.7 MW for each contract-year thereafter.

In September 2004, Envida entered into a land lease and gas utilization agreement with the City. Under the agreement, on an annual basis, Envida agrees to pay the City:

- (a) \$5 in advance of each fiscal year, for the use of the lands and access lands; and
- (b) An amount for the cubic feet of landfill gas used by Envida for the preceding fiscal year based on a rate agreed upon at the time of signing the agreement adjusted annually by the Consumer Price Index – Ontario.
- (c) A percentage rent based on 10% (2014 – 10%) of the difference between gross revenues arising from the sale of electricity and the value of electricity generated at a rate of \$57/MWh. In 2015, the amount incurred was \$11 (2014 - \$15).

In June 2011, Envida commenced supplying the OPA with electrical energy under a twenty year Feed-in-Tariff power purchase agreement. The electrical energy is produced by a roof-top mounted array of photo-voltaic solar panels. The OPA will purchase all energy produced by photo-voltaic array. The price that the OPA pays for the electrical energy is fixed by the contract.

From time to time, the Corporation is involved in various litigation matters arising in the ordinary course of its business. The Corporation has no reason to believe that the disposition of any such current matter could reasonably be expected to have a materially adverse impact on the Corporation's financial position, results of operations or its ability to carry on any of its business activities.

GUELPH MUNICIPAL HOLDINGS INC.

Notes to Consolidated Financial Statements, continued

Year ended December 31, 2015
(Expressed in thousands of dollars)

17. Commitments and contingencies (continued):

The Corporation is a member of the Municipal Electric Association Reciprocal Insurance Exchange (MEARIE). MEARIE is a pooling of property, casualty, and vehicle risks of many of the electrical utilities in Ontario. All members of the pool could potentially be subjected to an assessment for losses experienced by the pool for the years in which they were members on a pro-rata basis based on the total of their respective service revenues. It is anticipated that should such an assessment occur it would be funded over a period of up to 5 years. As at December 31, 2015, no assessments have been made.

18. Share capital:

	2015	2014
Authorized:		
Unlimited number of common shares		
Issued:		
67,530 common shares	\$ 67,530	\$ 67,530

19. Financial instruments and risk management:

Cash and cash equivalents are measured at fair value. The carrying values of receivables, and accounts payable and accrued charges approximating fair value because of the short maturity of these instruments. The carrying value of the customer deposits approximates fair value because the amounts are payable on demand.

The fair value of the \$65,000 Series "A" unsecured debenture at December 31, 2015 was \$73,068 (2014 - \$75,008) and the fair value of the Series "B" \$30,000 unsecured debenture at December 31, 2015 was \$29,648. The fair value is calculated based on the present value of future principal and interest cash flows, discounted at the current rate of interest at the reporting date. The interest rate used to calculate fair value at December 31, 2015 was 4.140% (2014 - 3.985%) on the \$65,000 debenture and was 4.190% on the \$30,000 debenture.

The Corporation's activities provide for a variety of financial risks, particularly credit risk, market risk and liquidity risk.

a) Credit risk:

Financial assets carry credit risk that a counterparty will fail to discharge an obligation which could result in a financial loss. Financial assets held by the Corporation, such as accounts receivable, expose it to credit risk. The Corporation earns its revenue from a broad base of customers located in the City. No single customer accounts for revenue in excess of 10% of total revenue.

GUELPH MUNICIPAL HOLDINGS INC.

Notes to Consolidated Financial Statements, continued

Year ended December 31, 2015

(Expressed in thousands of dollars)

19. Financial instruments and risk management (continued):

The carrying amount of accounts receivable is reduced through the use of an allowance for impairment and the amount of the related impairment loss is recognized in the income statement. Subsequent recoveries of receivables previously provisioned are credited to the income statement. The balance of the allowance for impairment at December 31, 2015 is \$235 (2014 - \$375). An impairment loss of \$142 (2014 - \$135) was recognized during the year. The Corporation's credit risk associated with accounts receivable is primarily related to payments from distribution customers. At December 31, 2015, approximately \$327 (2014 - \$478) is considered 60 days past due. The Corporation has approximately 54 thousand customers, the majority of which are residential. Credit risk is managed through collection of security deposits from customers in accordance with directions provided by the OEB. As at December 31, 2015, the Corporation held security deposits in the amount of \$4,653 (2014 - \$4,411).

b) Market risk:

Market risks primarily refer to the risk of loss resulting from changes in commodity prices, foreign exchange rates, and interest rates. The Corporation currently does not have material commodity or foreign exchange risk. The Corporation is exposed to fluctuations in interest rates as the regulated rate of return for the Corporation's distribution business is derived using a complex formulaic approach which is in part based on the forecast for long-term Government of Canada bond yields and the credit spread of A-rated utility bonds. This rate of return is approved by the OEB as part of the approval of distribution rates.

A 1% increase in the interest rate at December 31, 2015 would have increased interest expense on the long-term debt by \$950 (2014 - \$650), assuming all other variables remain constant. A 1% decrease in the interest rate would have an equal but opposite effect.

(c) Liquidity risk:

The Corporation monitors its liquidity risk to ensure access to sufficient funds to meet operational and investing requirements. The Corporation's objective is to ensure that sufficient liquidity is on hand to meet obligations as they fall due while minimizing interest exposure. As at December 31, 2015, the Corporation, through its parent company Guelph Municipal Holdings Inc. Centralized Banking Agreement, had access to a \$20,000 credit facility. The Corporation monitors cash balances daily to ensure that a sufficient level of liquidity is on hand to meet financial commitments as they come due. As at December 31, 2015, no amounts had been drawn under this \$20,000 credit facility (2014 - \$10,000).

As part of the \$20,000 credit facility, The Corporation has a bilateral facility for \$5,000 (the "LC" facility) for the purpose of issuing letters of credit mainly to support the prudential requirements of the IESO, of which \$4,000 has been drawn and posted with the IESO (2014 - \$4,000).

The majority of accounts payable, as reported on the balance sheet, are due within 30 days.

GUELPH MUNICIPAL HOLDINGS INC.

Notes to Consolidated Financial Statements, continued

Year ended December 31, 2015
(Expressed in thousands of dollars)

19. Financial instruments and risk management (continued):

(d) Capital disclosures:

The main objectives of the Corporation, when managing capital, are to ensure ongoing access to funding to maintain and improve the electricity distribution system, to comply with covenants related to its credit facilities, to prudently manage its capital structure with regard for recoveries of financing charges permitted by the OEB on its regulated electricity distribution business, and to deliver the appropriate financial returns.

The Corporation's definition of capital includes shareholder's equity and long-term debt. As at December 31, 2015, shareholder's equity amounts to \$69,924 (2014 - \$68,649) and long-term debt amounts to \$94,245 (2014 - \$64,600).

20. Guarantees:

GHESI has a Connection and Cost Recovery Agreement with Hydro One Networks Inc. (Networks) for the supply of two additional breaker positions at the Campbell transformer station (cost \$599), and the installation of a new metal clad switchgear to the two existing idle windings at Cedar TS (transformer station) with eight new feeder positions (cost \$5,582). The cost of the connections are debts owed to Networks that will be forgiven provided that GHESI meets or exceeds the specific load requirement and the incremental transformation connection revenue received by Networks. GHESI expects to meet the conditions of the guarantee and does not anticipate any payments to Networks.

GHESI has another Connection and Cost Recovery Agreement with Networks for the line connection of the Arlen municipal transformer station. The \$1,688 cost of the connection is a debt owed to Networks that will be forgiven provided that GHESI meets or exceeds the specific load requirement and the incremental transformer connection revenue received by Networks. GHESI expects to meet the conditions of the guarantee and does not anticipate any payment to Networks.