

**CONSOLIDATED
FINANCIAL STATEMENTS OF**

NEWMARKET HYDRO HOLDINGS INC.

December 31, 2013

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INDEPENDENT AUDITORS' REPORT

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To the Shareholders of
Newmarket Hydro Holdings Inc.

Report on the Consolidated Financial Statements

We have audited the accompanying consolidated financial statements of Newmarket Hydro Holdings Inc., which comprise the consolidated balance sheet as at December 31, 2013, and the consolidated statements of retained earnings, income and cash flows for the year then ended, and 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 Canadian generally accepted accounting principles, and for such internal controls as management determines are 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 the auditors' 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, the auditors consider internal controls relevant to the Company'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 Company's internal controls. 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.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Newmarket Hydro Holdings Inc. as at December 31, 2013, and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

Collins Barrow Kawarthas LLP

Chartered Professional Accountants
Peterborough, Ontario
June 26, 2014

NEWMARKET HYDRO HOLDINGS INC.**CONSOLIDATED BALANCE SHEET**

As at December 31, 2013

	2013	2012
	\$	\$
ASSETS		
Current assets		
Cash	8,778,807	7,943,135
Short-term investments (note 3)	3,349,379	3,339,347
Accounts receivable	9,394,733	8,947,648
Inventory	808,950	947,105
Prepaid expenses	376,146	395,761
Income taxes receivable	571,239	915,112
Unbilled revenue	9,819,789	8,525,292
	33,099,043	31,013,400
Other assets		
Property, plant and equipment (note 4)	55,288,116	53,885,877
Future income taxes (note 5)	3,500,000	3,560,000
	58,788,116	57,445,877
	91,887,159	88,459,277
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities		
Accounts payable and accrued liabilities (note 6)	12,083,736	10,639,451
Note payable	87,412	87,412
Current portion of deposits held	425,000	325,000
	12,596,148	11,051,863
Long-term liabilities		
Long-term debt (note 7)	24,742,821	24,742,821
Deposits held	2,875,806	3,096,717
Employee future benefits (note 8)	1,107,432	1,059,572
Deferral accounts (note 9)	5,358,684	4,739,270
	34,084,743	33,638,380
Non-controlling interest (note 11)	2,990,276	2,896,574
Shareholders' equity		
Share capital (note 12)	29,609,342	29,609,342
Retained earnings	12,606,650	11,263,118
	42,215,992	40,872,460
	91,887,159	88,459,277

Approved on behalf of the Board

Director_____
Director*The accompanying notes are an integral part of these financial statements*

NEWMARKET HYDRO HOLDINGS INC.
CONSOLIDATED STATEMENT OF RETAINED EARNINGS
For the year ended December 31, 2013

	2013	2012
	\$	\$
Retained earnings - beginning of year	11,263,118	9,893,449
Net income for the year	3,318,166	2,821,669
Dividends (note 13)	(1,974,634)	(1,452,000)
Retained earnings - end of year	12,606,650	11,263,118

The accompanying notes are an integral part of these financial statements

NEWMARKET HYDRO HOLDINGS INC.**CONSOLIDATED STATEMENT OF INCOME**

For the year ended December 31, 2013

	2013	2012
	\$	\$
Revenue		
Service revenue	15,152,692	13,094,439
Cost of power revenue (note 2h)	66,052,608	58,954,390
Other operating revenue	1,026,176	1,111,386
	82,231,476	73,160,215
Cost of power purchased	66,052,608	58,954,390
Gross profit	16,178,868	14,205,825
Expenses		
Customer billing and collecting	1,903,757	1,925,847
Amortization	2,745,298	2,661,719
Interest on long-term debt	1,344,336	1,331,890
Administration	2,944,634	2,641,334
System operation and maintenance	2,595,424	2,239,264
	11,533,449	10,800,054
Income before undernoted items and income taxes	4,645,419	3,405,771
Other expenses (income)		
Loss (gain) on sale of property, plant and equipment	103,273	(179,701)
Investment income	(102,195)	(224,452)
Non-controlling interest (note 11)	93,702	81,179
	94,780	(322,974)
Income before income taxes	4,550,639	3,728,745
Provision for income taxes (note 5)		
Current	1,172,473	497,076
Future	60,000	410,000
	1,232,473	907,076
Net income for the year	3,318,166	2,821,669

The accompanying notes are an integral part of these financial statements

NEWMARKET HYDRO HOLDINGS INC.**CONSOLIDATED STATEMENT OF CASH FLOWS**

For the year ended December 31, 2013

	2013	2012
	\$	\$
CASH PROVIDED FROM (USED FOR)		
Operating activities		
Net income for the year	3,318,166	2,821,669
Items not affecting cash		
Amortization	2,745,298	2,661,719
Future income taxes	60,000	410,000
Loss (gain) on sale of property, plant and equipment	103,273	(179,701)
Employee future benefits	47,860	185,231
Increase in non-controlling interest (note11)	93,702	81,180
	6,368,299	5,980,098
Change in non-cash working capital items (note 14)	73,403	(299,268)
	6,441,702	5,680,830
Investing activities		
Purchase of property, plant and equipment	(4,271,200)	(6,334,839)
Proceeds on disposal of property, plant and equipment	20,390	1,595,447
Increase in deferral accounts	619,414	3,072,743
	(3,631,396)	(1,666,649)
Financing activity		
Dividends	(1,974,634)	(1,452,000)
Increase in cash	835,672	2,562,181
Cash - beginning of year	7,943,135	5,380,954
Cash - end of year	8,778,807	7,943,135
Other information		
Interest paid	1,404,398	1,352,638
Income taxes paid	1,533,600	1,213,600

The accompanying notes are an integral part of these financial statements

NEWMARKET HYDRO HOLDINGS INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
For the year ended December 31, 2013

1. NATURE OF OPERATIONS

Newmarket Hydro Holdings Inc. ("the Company") was incorporated April 10, 2000 under the Business Corporations Act of the Province of Ontario. The Company commenced operations on November 1, 2000. Newmarket Hydro Holdings Inc. is wholly-owned by the Town of Newmarket.

The principal activity of the Company is to distribute electricity to the residents and businesses in the Town of Newmarket and the Township of Tay under a licence issued by the Ontario Energy Board (OEB). The Company is regulated by the OEB and adjustments to its distribution rates require OEB approval.

2. SIGNIFICANT ACCOUNTING POLICIES

These consolidated financial statements are prepared in accordance with Canadian generally accepted accounting principles. The significant policies are detailed as follows:

(a) Consolidation

These financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP"). The consolidated financial statements include the accounts of its subsidiary, Newmarket-Tay Power Distribution LTD. Tay Hydro Inc. has a 7% interest in Newmarket-Tay Power Distribution Ltd.

(b) Electricity regulation

The Company is subject to rate regulation by the Ontario Energy Board (OEB). The OEB is charged with the responsibility of approving rates for the transmission and distribution of electricity. The following regulatory policy is practiced in a rate regulated environment:

Deferral accounts

Deferral accounts consist of deferred qualifying transition costs and various rate and retail variance accounts. Deferral accounts include amounts recoverable and repayable. The amounts included in these accounts are deferred for accounting purposes because it is probable that they will be recovered (repaid) in future rates. Deferral accounts recognized at December 31, 2013 are disclosed in note 9. The Company continually assesses the likelihood of the recovery of recoverable assets. If recovery is no longer considered probable, the amounts are charged to operations in the year the assessment is made.

(c) Cash

Cash consists of balances with a major financial institution.

(d) Short-term investments

Investments are recorded at fair value. Unrealized gains and losses as a result of fair value adjustments at year end are included in investment income for the year.

NEWMARKET HYDRO HOLDINGS INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
For the year ended December 31, 2013

2. SIGNIFICANT ACCOUNTING POLICIES, continued

(e) Inventory

Inventory is valued at the lower of cost and net realizable value with cost being determined on a weighted average basis.

(f) Property, plant and equipment

Property, plant and equipment are recorded at cost. The Company provides for amortization using the straight-line method at rates designed to amortize the cost of the property, plant and equipment over their estimated useful lives. The annual amortization rates are as follows:

Buildings	25 to 30 years
Transmission and distribution	40 to 50 years
Office equipment	5 to 10 years
Leasehold improvements	7 years
Computer software	3 to 5 years
Operational equipment	10 to 15 years
Transportation equipment	5 to 10 years
Land rights	30 years

Contributions for capital construction consist of third party contributions toward the cost of constructing distribution assets. The third party contribution is calculated through an economic evaluation as per the OEB Distribution Service Code. Contributed capital amounts are recorded as received and amortized over the same period as the asset to which they relate being 30 to 50 years.

(g) Related parties

Related party transactions are in the normal course of operations and have been measured at the exchange amount which is the amount of consideration established and agreed to by the related parties. Details of related party transactions and balances are disclosed in note 10.

(h) Employee future benefits

The Company pays certain health, dental and life insurance benefits on behalf of its retired employees. The Company recognizes these post-retirement costs in the period in which the employees earn the benefits. The cost of employee future benefits earned by employees is actuarially determined using the projected benefit method prorated on length of service and management's best estimate of salary escalation, retirement ages of employees, employee turnover and expected health and dental care costs. The most recent actuarial valuation of the obligation was performed for December 31, 2012. Details related to the post-employment benefits are detailed in note 8.

NEWMARKET HYDRO HOLDINGS INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
For the year ended December 31, 2013

2. SIGNIFICANT ACCOUNTING POLICIES, continued

(i) Revenue recognition

Service revenue and cost of power revenue is recorded on the basis of regular meter readings and estimated customer usage since the last meter reading date to the end of the period. The related cost of power revenue is recorded on the basis of the power billed by the Independent Electricity System Operator. Other operating revenue is recorded when services are provided.

The cost of power is shown on the statement of income net of rebates. The total gross cost of power was \$72,380,505 with \$6,327,897 of incentives for a net amount of \$66,052,608 (2012 - \$63,685,270 with \$4,730,880 of incentives for a net amount of \$58,954,390).

(j) Income taxes

Under the Electricity Act, 1998, the Company is required to make payments in lieu of income taxes (PILS) to the Ontario Electricity Financial Corporation (OEFC). Future income taxes are calculated using the liability method of tax accounting. In providing for corporate income taxes, temporary differences between the tax basis of assets or liabilities and their carrying amounts are reflected as future income taxes. The tax rates anticipated to be in effect when these temporary differences reverse are used to calculate future income taxes. Additional details related to the calculation and method of accounting for PILS is included in note 5.

(k) Management estimates

The preparation of financial statements in accordance with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements, and the reported amounts of revenues and expenses during the reporting period.

Key areas where management has made complex or subjective judgments (often as a result of matters that are inherently uncertain) include, among others, the fair value of certain assets, useful lives of capital assets, impairment of assets, inventory provisions, amortization, revenues, allowance for doubtful accounts, environmental and asset retirement obligations, employee future benefits, deferral accounts and income taxes. Actual results could differ from these and other estimates, the impact of which would be recorded in future periods.

(l) Asset retirement obligations

Canadian generally accepted accounting principles require the Company to determine the fair value of the future expenditures required to settle legal obligations to remove fixed assets on retirement. If reasonably estimable, a liability is recognized equal to the present value of the estimated future removal expenditures.

Some of the Company's assets may have asset retirement obligations. As the Company expects to use the majority of its fixed assets for an indefinite period, no removal costs can be determined and, consequently, a reasonable estimate of the fair value of any asset retirement obligations has not been made at this time.

NEWMARKET HYDRO HOLDINGS INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
For the year ended December 31, 2013

2. SIGNIFICANT ACCOUNTING POLICIES, continued

(m) International Financial Reporting Standards (IFRS)

On February 13, 2008 the Accounting Standards Board (AcSB) confirmed that IFRS will be required to be adopted by publicly accountable enterprises and certain government enterprises for annual reporting purposes for fiscal years beginning on or after January 1, 2012. On September 10, 2011 the AcSB granted an optional one year deferral of IFRS adoption for entities subject to rate regulation. Subsequent to this, through a series of additional one year extensions, the mandatory change over date for entities with rate regulated activities has been extended to January 1, 2015. At its December 2012 meeting, the International Accounting Standards Board (IASB) decided to develop an interim IFRS on rate regulated activities that "grandfathers" existing recognition and measurement policies. The Company has elected to continue the deferral of transition to IFRS, pending resolution of these matters before the IASB.

On January 30, 2014, the AcSB issued interim Standard IFRS 14 *Regulatory Deferral Accounts*. IFRS 14 permits first-time adopters of IFRS to continue to use their previous GAAP accounting policies for the recognition, measurement, impairment and derecognition of regulatory deferral account balances.

The interim standard requires regulatory deferral account balances and movements therein to be presented as separate line items on the face of the financial statements. In addition, further disclosure is required to identify the nature of, and risk associated with, rate regulation, and the effect of rate regulation on the entity's financial position, performance and cash flows. IFRS 14 is effective from January 1, 2016, with early adoption permitted.

The IASB continues to move forward with its project to consider the broad issues of rate regulation with plans to publish a discussion paper on this subject in 2014, and a final comprehensive standard expected to follow in the coming years.

The Company has elected to continue the deferral of transition to IFRS, pending resolution of these matters before the IASB. The Company is continuing to assess the financial reporting impacts of the adoption to IFRS. At this time, the requirements of interim Standard IFRS 14 do not appear that they would have a significant impact on the financial reporting, future financial position or results of operations of the Company. However, the impact of any future changes that may be included in the discussion paper or the final comprehensive standard is not reasonably determinable. The impact of new IFRS standards and interpretations not yet effective has also not been assessed.

NEWMARKET HYDRO HOLDINGS INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
For the year ended December 31, 2013

3. **SHORT-TERM INVESTMENTS**

	2013 \$	2012 \$
Bond	-	500,000
Mutual funds	3,349,379	2,839,347
	<u>3,349,379</u>	<u>3,339,347</u>

Included in investment revenue is a loss on investments of \$34,318 (2012 - \$59,931 gain).

4. **PROPERTY, PLANT AND EQUIPMENT**

	Cost \$	Accumulated amortization \$	2013 Net book value \$	2012 Net book value \$
Land	4,220,923	-	4,220,923	3,612,170
Buildings	291,530	87,654	203,876	202,648
Transmission and distribution	95,445,502	47,613,556	47,831,946	46,749,412
Office equipment	818,263	450,750	367,513	394,540
Leasehold improvements	1,095,041	656,173	438,868	518,884
Computer software	1,124,124	589,226	534,898	512,997
Operational equipment	741,440	478,751	262,689	275,934
Transportation equipment	2,946,004	1,918,959	1,027,045	1,209,041
Land rights	517,173	116,815	400,358	410,251
	<u>107,200,000</u>	<u>51,911,884</u>	<u>55,288,116</u>	<u>53,885,877</u>

5. **INCOME TAXES**

a) The components of future income tax balances are as follows:

	2013 \$	2012 \$
Future income tax asset		
Tax basis of equipment in excess of carrying amount	2,956,000	2,957,000
Reserves deductible when paid	265,000	313,000
Cumulative eligible capital available for tax purposes	279,000	290,000
	<u>3,500,000</u>	<u>3,560,000</u>

NEWMARKET HYDRO HOLDINGS INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
For the year ended December 31, 2013

5. **INCOME TAXES, continued**

- b) The provision for income taxes recorded in the consolidated financial statements differs from the amount which would be obtained by applying the statutory income tax rate of 26.5% (2012 - 26.5%) to the income for the years as follows:

	2013 \$	2012 \$
Income for the year before income taxes	4,551,000	3,729,000
Anticipated income tax expense	1,206,015	988,185
Permanent expense differences	3,975	3,975
Impact of tax rate changes and other	22,483	(85,084)
Income tax expense	1,232,473	907,076

6. **ACCOUNTS PAYABLE AND ACCRUED LIABILITIES**

	2013 \$	2012 \$
Accounts payable - purchased power	4,816,413	3,755,206
Other trade accounts payable and accrued liabilities	3,967,438	3,685,979
Water and sewer billings payable (note 10)	1,792,634	1,704,054
Credits on customer accounts	1,270,166	901,976
Independent Electric System Operator	75,198	75,198
Ontario Power Authority program payable	161,887	517,038
	12,083,736	10,639,451

7. **LONG-TERM DEBT**

	2013 \$	2012 \$
Note payable, 5.48% - Town of Newmarket	22,000,000	22,000,000
Note payable, 5.48% - Township of Tay	1,742,821	1,742,821
Committed term facility, 3.07%, due December 31, 2015	1,000,000	1,000,000
	24,742,821	24,742,821

NEWMARKET HYDRO HOLDINGS INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
For the year ended December 31, 2013

7. LONG-TERM DEBT, continued

The notes are unsecured and have no specific terms of repayment. Since the holders of the notes have indicated that it is not their intention to request repayment of this amount during the next fiscal year, this amount has been classified as a non-current liability in the accompanying financial statements.

The committed term facility was drawn for the purpose of the purchase of smart meters. The Company is required to make monthly interest payments only with 100% of the remaining balance due December 31, 2015. At December 31, 2013, the Company was in compliance with all covenants. A general security agreement covering all assets of the Company has been pledged as security for the committed term facility.

8. EMPLOYEE FUTURE BENEFITS

The Company provides certain health, dental and life insurance benefits for retired employees pursuant to the Company's policy. The accrued benefit obligation and net periodic expense for the year were determined by actuarial valuation. The most recent valuation was performed for December 31, 2012.

The unamortized past service cost obligation resulting from the inclusion of the former Tay Hydro Electric Distribution Company Inc. employees in the plan, is being amortized over the remaining service life of those employees, being 11 years with 5 years remaining to be amortized.

Significant actuarial assumptions employed for the valuations are as follows: future general inflation level of 2.5%, discount rate of 3.9%, salary and wage level increases at 3.3% per annum. A 8% annual increase in the per capita cost for health benefits was used for 2013. This rate will decrease to 7.47% for 2014; 6.93% for 2015; 6.4% for 2016; 5.87% for 2017; 5.33 for 2018; 4.8% for 2019 and thereafter. A 6.88% annual rate of increase in the per capita cost of covered dental costs was used for 2013. This rate will decrease to 6.5% for 2014; 6.13% for 2015; 5.75% for 2016; 5.38% for 2017; 5.0% for 2018 and thereafter.

Information about the Company's defined benefit plan is included as follows:

	2013 \$	2012 \$
Accrued benefit obligation, beginning of period	1,059,572	874,341
Current service cost	80,827	147,561
Actuarial loss	-	57,888
Amortization of past service costs	13,204	13,204
Benefits paid	(46,171)	(33,422)
	1,107,432	1,059,572
Unamortized past service cost	57,217	70,421
	1,164,649	1,129,993

NEWMARKET HYDRO HOLDINGS INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
For the year ended December 31, 2013

9. DEFERRAL ACCOUNTS

	2013 \$	2012 \$
Deferral accounts approved for recovery	2,139,096	2,130,324
Recovered to date	(2,913,758)	(2,678,320)
Repayment - payment in lieu of taxes	(755,086)	(1,333,036)
	(1,529,748)	(1,881,032)
Power purchased for resale	(581,759)	(819,156)
Smart meters	(381,848)	(380,407)
Change in useful life of property, plant and equipment	(3,120,305)	(1,762,969)
Retail settlements and other	254,976	104,294
	(3,828,936)	(2,858,238)
	(5,358,684)	(4,739,270)

Pursuant to The Ontario Energy Board Decision on EB 2011-0184 the Company is returning an unintentional over collection of charges related to Payments in Lieu of Taxes. These charges were collected from 2002 to 2006. The repayment of \$755,086 (2012 - \$1,333,036) will continue through the 2014 fiscal year.

In 2012, the Company has adjusted the estimated useful life related to the amortization period for certain capital assets, based upon the Ontario Energy's Board regulatory accounting direction as contained in the revised 2012 Accounting Procedures Handbook for Electricity Distributors. As a result of OEB direction related to the settlement of these amounts, the Company has recorded a payable in the deferral account of \$3,120,305 (2012 - \$1,762,969) and a reduction in service revenue of \$1,357,336 in 2013 (2012 - \$1,762,969).

10. ADVANCES FROM RELATED COMPANIES AND RELATED PARTY TRANSACTIONS

- (a) During the year, the Company entered into transactions with its majority parent, Newmarket Hydro Holdings Inc. (NHHI) and with The Town of Newmarket which is the sole shareholder of Newmarket Hydro Holdings Inc. Revenue charged during the year included energy, street light capital and street light maintenance charged at commercial rates to the Town of Newmarket.

Included in accounts payable (note 6) are water and sewer amounts collected which are due to the Town. These amounts are collected and remitted in accordance with a contract with URB Olameter and remitted on their behalf.

Included in long term debt (note 7) are notes payable to related parties.

NEWMARKET HYDRO HOLDINGS INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
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10. **ADVANCES FROM RELATED COMPANIES AND RELATED PARTY TRANSACTIONS,**
continued

(b) Transactions

These transactions are measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

	2013 \$	2012 \$
Revenue		
Energy sales	2,995,243	3,642,968
Services - Street light capital	12,147	4,097
Services - Street light maintenance	267,809	267,809
	<u>3,275,199</u>	<u>3,914,874</u>
Expenses		
Interest	1,205,600	1,205,600
Rent and property tax	386,770	382,244
	<u>1,592,370</u>	<u>1,587,844</u>

(c) The following amount is due from the Town of Newmarket and included in the financial statements:

	2013 \$	2012 \$
Accounts receivable	333,155	318,309

11. **NON-CONTROLLING INTEREST**

The changes in non-controlling interest consist of:

	2013 \$	2012 \$
Balance - beginning of the year	2,896,574	2,815,394
Proportional share of income	232,336	197,180
Proportional share of dividends paid	(138,634)	(116,000)
Balance - end of the year	<u>2,990,276</u>	<u>2,896,574</u>

NEWMARKET HYDRO HOLDINGS INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
For the year ended December 31, 2013

12. SHARE CAPITAL

Authorized

Unlimited number of common shares

Issued

	2013	2012
	\$	\$
10,000 common shares	29,609,342	29,609,342

13. DIVIDENDS

During the year the Company declared and paid \$1,974,634 of dividends. \$138,634 of this amount was charged against the non-controlling interest as described in note 11.

14. CHANGE IN NON-CASH WORKING CAPITAL ITEMS

	2013	2012
	\$	\$
Increase in short-term investments	(10,032)	(173,522)
Increase in accounts receivable	(447,085)	(821,542)
Decrease (increase) in inventory	138,155	(114,143)
Decrease (increase) in prepaid expenses	19,615	(27,804)
Decrease (increase) in income taxes receivable	343,873	(119,062)
Decrease (increase) in unbilled revenue	(1,294,497)	1,001,791
Increase (decrease) in accounts payable and accrued liabilities	1,444,284	(97,319)
Increase (decrease) in deposits held	(120,910)	52,333
	73,403	(299,268)

15. SHORT TERM CREDIT FACILITIES

The Company has \$3,500,000 available in operating facilities from a major chartered bank. The facilities are 364 day revolving operating loan, bearing interest at prime plus 0.5%, to be repaid within one year from date of acquisition unless extended by the bank. A standby fee of 10 basis points, payable quarterly in arrears applies to any unused portion of the facility. As at the balance sheet date, the Company has no balance outstanding (2012 - Nil) on this facility. The operating loan includes restrictive clauses with respect to repayment.

In addition, the Company has provided prudential support in the amount of \$2,765,940 to the Independent Electricity System Operator. The prudential support is secured by a letter of credit with a major chartered bank for \$2,765,940 and contains restrictive clauses with respect to debt repayments.

A general security agreement covering all assets of the Company has been pledged as security for the operating facilities.

NEWMARKET HYDRO HOLDINGS INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
For the year ended December 31, 2013

16. PENSION AGREEMENT

The Company makes contributions to the Ontario Municipal Employees' Retirement Fund (O.M.E.R.S.), which is a multi-employer plan, on behalf of its employees. The plan is a defined benefit plan which specifies the amount of retirement benefits to be received by the employees based on the length of service and rates of pay.

The amount contributed to O.M.E.R.S. for the year ended was \$438,733 (2012 - \$386,294).

17. CAPITAL DISCLOSURES

The Company's primary objective when managing capital is to address the expectations as provided in the Shareholder Agreement between the Company's parent company, Newmarket Hydro Holdings Inc. and its shareholder, the Town of Newmarket. The expectation is that the Company will maintain a prudent financial structure in order to safeguard the Company's assets and to provide adequate returns for its shareholders and benefits to the stakeholders.

The Ontario Energy Board sets rates based on a deemed capital structure of 60% debt and 40% equity.

Changes to the Company's capital structure are constrained by existing covenants contained in the banking agreement. The Company must maintain a maximum debt to capitalization ratio of 0.60 to 1 and maintain a debt service coverage ratio of 1.2.

The Company's current capital structure is defined as follows:

	2013 \$	2012 \$
Long term debt	24,742,821	24,742,821
Total debt	24,742,821	24,742,821
Share capital	29,609,342	29,609,342
Retained earnings	12,616,446	11,263,118
Non-controlling interest	2,990,276	2,896,574
Capital	45,216,064	43,769,034
Debt-to-adjusted capital ratio	0.55	0.57

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18. FINANCIAL INSTRUMENTS

Fair value

The carrying value of the accounts receivable and accounts payable and accrued liabilities approximate their fair value due to their short-term nature.

The short-term investments are carried at fair value, with changes in value recognized in income in the year.

The fair value of the advances from parent company detailed in note 10 are less than carrying value, as the amounts have no terms of repayment, the fair value cannot be calculated with any degree of certainty.

The carrying value of long-term debt approximates the fair value as the interest rates are consistent with the current rates offered to the Company for debt with similar terms.

Interest rate risk

The Company manages exposure to interest rate risk through a combination of fixed and floating rate borrowings. Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Company is exposed to interest rate cash flow risk to the extent that the floating rate credit facility bears interest at a floating rate. The Company is also exposed to interest rate price risk to the extent that loans bear interest at fixed rates (note 7 and 10).

Credit risk

Credit risk arises from the potential that a counter party will fail to perform its obligations. The Company is exposed to credit risk from customers. However, the Company has a significant number of customers which minimizes the concentration of credit risk. An allowance for collection of doubtful accounts in the amount of \$214,867 (2012 - \$220,523) has been recorded.

Market risk

The securities held as short term investments exposes the Company to market risk due to the potential for changes in market prices.

Liquidity risk

The Company does have a liquidity risk in the accounts payable and accrued liabilities of \$12,083,736 (2012 - \$10,639,451). Liquidity risk is the risk that the Company cannot repay its obligations when they become due to its creditors. The Company reduces its exposure to liquidity risk by ensuring that it documents when authorized payments become due; maintains an adequate line of credit to repay trade creditors and repays long term debt interest and principal as they become due. In the opinion of management the liquidity risk exposure to the Company is low and is not material.

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19. COMMITMENT

The company has an operating lease agreement with the Town of Newmarket, expiring December 31, 2017 for the rental of the building. Minimum lease payments over the next five year period under this commitment are as follows;

	\$
2014	275,000
2015	275,000
2016	275,000
2017	275,000
	<hr/> 1,100,000 <hr/>

20. CONTINGENT LIABILITIES

(a) In the normal course of business, the Company enters into agreements that meet the definition of a guarantee. The guarantees include indemnities under lease agreements, purchase and sale agreements, confidentiality agreements, outsourcing, service and information agreements. The nature of these indemnification agreements prevents the Company from making a reasonable estimate of the maximum exposure due to the difficulties in assessing the amount of liability related to the likelihood and predictability of future events. Historically, the Company has not made any significant payments under similar indemnification agreements and therefore no amount has been accrued in the balance sheet with respect to these agreements.

(b) Indemnity has been provided to all directors and/or officers of the Company for various items including, but not limited to, all costs to settle suits or actions due to association with the Company, subject to certain restrictions. The Company has purchased directors' and officers' liability insurance to mitigate the cost of any potential suits or actions. The amount of any potential future liability which exceeds the amount of insurance coverage cannot reasonably be determined.

(c) The Company participates with other municipal utilities in Ontario in an agreement to exchange reciprocal contracts of indemnity through the Municipal Electric Association Reciprocal Insurance Exchange. Under this agreement, the Company is contingently liable for additional assessments to the extent that premiums collected are not sufficient to cover actual losses, claims and costs experienced.

(d) The Company is currently assessing the Connection and Cost Recovery Agreement for Holland Transformer Station with Hydro One Networks. Under this agreement, there are potential capital contributions towards the Holland Transformer Station at year five (2014) and year ten (2019) of the agreement based upon actual load on the station. The Company at this time cannot reasonably estimate the amount of any capital contributions that may be required.

21. COMPARATIVE FIGURES

The financial statements have been reclassified, where applicable, to conform to the presentation used in the current year. The changes do not affect prior year earnings.