Halton Hills
HYDRO

Date: January 10, 2018

To: The Board of Directors of Halton Hills Hydro Inc.

From: David J. Smelsky, CPA, CMA

Subject: **Credit Facilities and Interest Risk**

Board Members:

Update Credit Facility
Attached is a copy of the TD Commercial Banking credit facilities, dated December 17, 2017. This document reflects the approval of the $23.0M Credit Facility for the construction of Transformer Station (MTS#1) and changes to Debt Service Coverage Ratio Covenants during the construction period.

Summary of Facilities:

1) $9,000,000 Revolving Operation line, in the form of prime based loans, bankers' acceptances, letter of credit or stand-by letters of guarantee IESO Prudential.

- Interest on prime based loans is at prime rate + 0.00%.
- Financial Covenants required are;
    - Maximum Total Interest Bearing Debt to Capitalization ratio of 0.60:1
    - Debt Service Coverage Ratio of 1.20:1, on a rolling 4 quarter basis

Currently, $1,754,315 of the credit facility is utilized in the form of a letter of credit as security to the Independent Electricity System Operator (IESO). Therefore, the remaining available operating line is $7,245,685.

2) $2,456,762 Committed Reducing Term Facility – Smart Meter Loan
3) $2,576,170 Committed Reducing Term Facility – 2011 Capex Funding
4) $1,599,537 Committed Reducing Term Facility – 2012 Capex Funding
5) $2,038,910 Committed Reducing Term Facility – 2013, 2014 Capex Funding
6) $3,646,826 Committed Reducing Term Facility – 2015 Capex Funding
7) $4,759,999 Committed Reducing Term Facility – 2016 Capex Funding
8) $23,000,000 Interim Demand Loan –Construction of MTS#1
9) $23,000,000 Committed Reducing Term Facility – to repay Facility 8)

All loan facilities are being amortized over 30 years.

Interest Risk:

- HHHI currently has $15.46MM in floating prime rate debt and $1.59MM in fixed rate debt outstanding.
- In addition, HHHI will be requiring an additional $23MM in funding needs which will be drawn on a construction loan followed by a "take-out" loan upon completion of MTS#1 in 2019.
- The interest rates on the takeout loan as well as the floating prime rate term loans are currently "at risk" as prime rate fluctuates.
- For the takeout loan facility, an opportunity exists to remove this risk by locking-in the interest rate that would pay via an Interest Rate Swap. This is a common risk strategy employed by many LDC's throughout Ontario.
- For the floating-rate term loans, these can be converted to fixed rate loans to create cash flow certainty.

Fixed Rate Financing with Swaps:

- HHHI would borrow required funds through a floating-rate loan, known as a Bankers Acceptance (BAs)
- As BA Rate resets every month, HHHI would fix the rate by entering into an Interest Rate Swap with the TD Bank
  - ➢ TD Bank pays HHHI the BA interest + 1.4% Stamping Fee
  - ➢ HHHI pays TD Bank a Fixed Rate
  - ➢ Changes in the BA rate become inconsequential as it is paid to HHHI via the Swap

Next Steps:

- HHHI staff will complete a risk assessment and develop an interest risk strategy to mitigate the interest exposure. To date, HHHI has recognized an interest savings as the floating prime rate is currently 3.20%. Whereas, a 30year BA rate is 2.70% + 1.40% Stamping Fee = 4.30%
- Economic indicators reflect an upward pressure on future interest rates.
- The risk assessment will evaluate the interest risk on the $23.0MM (Facility 9) looking out 20, 25, and 30 years. A 'Forward Start' date can be established today, mitigating the interest rate risk for the projected draw down date in 2019.

Date: March 15, 2018

To: The Board of Directors of Halton Hills Hydro Inc.

From: David J. Smelsky, CPA, CMA, C.Dir.

Subject: **Update - Credit Facilities and Interest Risk**

Board Members:

Credit Facility-Update

Attached is a copy of the 'signed' TD Commercial Banking credit facilities. The only change from the prior document presented in the January board meeting package is on page 4 – Assignment Fee- reduced from $25,000 to $12,500.

Interest Risk-Update:

- The TD Prime Interest Rate is 3.45% (effective January 18, 2018).
- On March 7, 2018 the Bank of Canada maintained its target rate at 1.50%.
- The Bank of Canada continues to monitor the economy's sensitivity to higher interest rates. The implications of the recent federal budget for the outlook for growth and inflation will be incorporated in the Banks' April projection along with the potential impact of issues south of the border. The next Bank of Canada interest rate announcement is scheduled for April 18, 2018.
- Derek Burleton – VP & Deputy Economist TD Bank believes the economic outlook is expected to warrant higher interest rates over time, with some continued monetary policy accommodation will likely be needed to keep the economy operating close to potential and inflation on target (current inflation is nearing 2%). The Bank of Canada will be cautious in considering future policy adjustments, but it is very likely we will see 0.25% increases in respective Q2-2018, Q4-2018 and again in Q1-2019.

The table below is a comparison of the current TD Prime rate to Term Loan rates for 2, 3, and 4 years:

Halton Hills Hydro
TD Prime Interest Rate vs. Term Rates - 2 year, 3 year, 4 year

Halton Hills Hydro Inc.						TD Prime Floating Rate			
Facility	Amount	Amortization	Rates				TD Prime less Term Rates		
			2 Year	3 Year	4 Year		2 Year	3 Year	4 Year
2	$2,433,139.13	30-Aug-41	3.59%	3.73%	3.82%	3.45%	-0.14%	-0.28%	-0.37%
3	$2,563,224.84	18-Aug-44	3.72%	3.86%	3.95%	3.45%	-0.27%	-0.41%	-0.50%
5	$2,028,006.36	15-Aug-43	3.65%	3.79%	3.88%	3.45%	-0.20%	-0.34%	-0.43%
6	$3,630,020.40	21-Jan-46	3.74%	3.88%	3.97%	3.45%	-0.29%	-0.43%	-0.52%
7	$4,733,332.15	25-Aug-47	3.77%	3.91%	4.00%	3.45%	-0.32%	-0.46%	-0.55%

Art Skidmore

To: HHHI Board of Directors
Cc: dsmelsky@haltonhillshydro.com
Subject: Interest Rates

Good Afternoon:

At our last Board meeting we discussed the possible interest rate risk to Halton Hills Hydro.

HHH currently has six Capital Expenditure loans totalling $16,802,427

We met with the TD bank yesterday and it appears that another rate increase in coming in July .25% and possibly another in December of .25%

Our current variable rate is 3.45% and projected prime at December 31, 2018 is 3.95%

We have the ability to lock in a rate until May 1, 2021 which is the effective date of next Cost of Service Rate Application

Today rates are:

Loan	Balance	Rate	P+I Payment
1	$ 2,385,893.71	3.65%	$ 12,575.30
2	$ 2,537,333.68	3.78%	$ 12,608.66
3	$ 1,569,925.36	3.73%	$ 8,031.74
4	$ 2,006,199.84	3.73%	$ 10,146.81
5	$ 3,596,409.10	3.85%	$ 17,480.38
6	$ 4,706,665.49	3.88%	$ 22,269.97

@ 18/05/25 Am

3.64%
3.77%
3.72%
3.72%
3.84%
3.87%

Typically interest rates move +- 4bps on a daily basis. Since we met the bank yesterday who had Tuesday's rates Loan six has moved downward by 6bps

I would recommend to the Board that we lock in the existing Capital Expenditure loans at the current rates

If you have any concerns please let us know so we can take the appropriate action

Thanks

Art Skidmore
President & CEO | Halton Hills Hydro Inc.
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Halton Hills
HYDRO

Date: June 15, 2018

To: The Board of Directors of Halton Hills Hydro Inc.

From: David J. Smelsky, CPA, CMA, C.Dir.

Subject: Interest Rate Strategy and Update

Board Members:

Overview

Halton Hills Hydro Inc. (HHHI) has various short and long term debts outstanding and wants to ensure the interest rate risk exposure is quantified and managed appropriately.

There are four main liabilities in question:
1) Six term loans ~ $16.8MM,
2) Takeout loan on the new transformer station ~ $23MM,
3) Capex for the years 2017- 2019, ~ $12MM, and
4) Shareholder Promissory Note ~ $16.1MM.

All of these liabilities carry an interest rate risk:

i. The six term loans, if continued under a floating interest rate.

ii. The interest rate on the takeout loan of the transformer station is currently unknown (September 2019).

iii. Interest rate on the capex budget for 2017-19 should it be rolled into an amortizing loan.

iv. The shareholder note (interest rate 4.12%) may need to be converted to bank financing at some point, which currently has an unknown interest rate (2020-21)

Strategy

For a bank financing solution, it is not necessary to consolidate the debt into a single loan. By keeping these items separate, HHHI can optimize the timing of the interest rate hedging and thus minimize overall risk.

On May 25, 2018 HHHI fixed the interest rate on the six term loans ($16.8M), locking in the rates to May 01, 2021:

Indicative Fixed Rates

Loan	Balance	Rate	P+I Payment
1	$ 2,385,893.71	3.64%	$ 12,562.54
2	$ 2,537,333.68	3.77%	$ 12,594.63
3	$ 1,569,925.36	3.72%	$ 8,023.20
4	$ 2,006,199.84	3.72%	$ 10,135.85
5	$ 3,596,409.10	3.84%	$ 17,460.17
6	$ 4,706,665.49	3.87%	$ 22,243.12

Note: May 1, 2021 is the date of the next Cost of Service rate application with the OEB.

The table below is a summary of the recommended action for each liability group. The liabilities are grouped into:

- short (next few months)
- medium term (approximately one year) action items.

Table: Summary of Recommendations

Priority	Liability	Size	Action Time Horizon	Recommendation
1	Term Loans (Six)	$16.8MM	Short Term / Medium	Short Term: Hedge interest rate risk right away by entering into six fixed rate term loans with a May 1, 2021 maturity.
				Medium Term: Consolidate the aggregate value of the six fixed rate term loans and forward lock the value to May 1, 2021 start date via a long-term interest rate swap.
2	Takeout Loan	$23MM	Short Term	Forward lock the takeout loan to a Sept. 1, 2019 or an earlier start date into a 30-year term/am interest rate swap
3	2017, 2018, 2019 CapEx	~$12MM	Medium	TermForward lock the aggregate value into an interest rate swap once the aggregate value can be approximated.
4	Shareholder Note	$16.1MM	TBD	Conversion to bank financing subject to formal credit approval by the bank, lock in interest rate at that time. No earlier than completion and commissioning of transformer station.

Halton Hills
HYDRO

Date: September 07, 2018

To: The Board of Directors of Halton Hills Hydro Inc.

From: David J. Smelsky, CPA, CMA, C.Dir.

Subject: **Financing Report Update**

Board Members:

Halton Hills Hydro Inc. (HHHI) has implemented mitigation strategies to minimize the interest rate risk exposure.

1. Six Term Loans ~ $16.8MM interest rates locked in to May 01, 2021. Please refer to the Term Facilities Table below:

Term Facilities
Halton Hills Hydro Inc.

Facility	Purpose	Interest Rate	Scheduled payment(Principal & Interest)	As per Bank Balance as at July 31, 2018	Current Portion of Term Loans	Long Term portion Of Term Loans	
2	Smart Meter Equip & Installation	3.63%	$ 12,417.71	$ 2,328,650.04	$ 26,815.70	$ 2,301,834.34	Smart meter Full amount moved to current portion in 2016
3	Capex - 2011	3.76%	$ 12,554.09	$ 2,502,816.17	$ 23,468.25	$ 2,479,347.92	Term Loan 3
4	Capex 2012 / 2013	3.71%	$ 7,952.39	$ 1,537,823.09	$ 15,943.74	$ 1,521,879.35	Term Loan 1
5	Capex 2013 / 2014	3.71%	$ 10,093.66	$ 1,977,019.95	$ 19,843.68	$ 1,957,176.27	Term Loan 2
6	Capex 2015	3.83%	$ 17,412.15	$ 3,551,661.83	$ 30,230.40	$ 3,521,431.43	Term Loan 4
7	Capex 2016	3.86%	$ 22,268.19	$ 4,665,472.75	$ 36,080.42	$ 4,629,392.33	Term Loan 5

2. Interim Construction Demand Loan – Interest Rate Swap

   - HHHI is currently working with the TD Bank to set up a fixed rate financing swap for the $23MM
   - A fixed rate loan is created with the combination of an interest rate swap and a Bankers Acceptance (BA) loan.
   - Documents to be executed;
     - ISDA Master Agreement and Schedules:
       -supporting Board Resolution
       -supporting Incumbency Certificate
       -supporting Legal Opinion

     - Regulatory Documents:
       -ISDA Cross-Border Letter
       -ISDA Canadian Representation Letter
       -Registering an LEI number

   - HHHI has engaged Osler, Hoskin & Harcourt LLP for legal assistance in reviewing the documents.
   - At the next board meeting – November 29, 2018; HHHI will present the ISDA Master Agreement and Regulatory Documents and request the Board's authorization to the execute the agreements.

- Note: If HHHI were to lock-in today, the interest swap rate = 4.20% for 30 year term. The objective of the interest rate swap is to hedge the interest rate exposure on $23MM, by establishing a fixed interest rate today, for 30 years. Alternatively, a conventional loan renewing every five years has an inherent interest rate risk during periods of rising interest rates.

3. Capex borrowing requirements for 2017, 2018 and 2019

   - 2017 Capital Expenditure – Cash Flow replenishment:

2017 CapEx Funding Replenishment:

2017 CapEx	$ 8,555,129
Less: Capital Contribution	(1,482,936)
	7,072,193
Funding 60/40 Debt Equity	60.0%
Proceeds New Term Loan	$ 4,243,316

4. Shareholder Promissory Note ~ $16MM

   a. In order to establish the $23MM MTS#1 Construction Loan Facility, the TD Bank required the Town of Halton Hills (ultimate shareholder) to postpone monetization of the promissory note. With reference to the December 21, 2017 TD Bank Loan Agreement, (copy provided to the Board January 18, 2018), the Intercreditor Agreement was signed by the Town of Halton Hills on August 24, 2018. Interest payments relating to the Promissory note (4.12% or $665,049 annually) will continue to be paid to the Town.

   b. The Town of Halton Hills requires repayment of the $16MM in 2021. Conversion to bank financing is subject to formal credit approval by the bank. Interest rate will be locked in at that time.

4. Bank Covenants:

With reference to the December 21, 2017 TD Bank Loan Agreement, HHHI is required to maintain certain Financial Covenants:

a. Debt Equity Ratio 60/40 (Tested Quarterly)
   - Maintain a maximum Total Interest Bearing Debt to Capitalization ratio 0.60:1
   - Interest Bearing Debt includes all interest bearing debt for the HHHI <u>less</u> the Promissory Note to the town of Halton Hills postponed in favour of the Bank.
   - Capitalization is defined as Interest Bearing Debt plus shareholder equity, plus contributed capital, plus preference share capital <u>less</u> any goodwill and investments in related companies.

   <u>Note:</u>
   - <u>TD Financial</u> Debt Equity Ratio forecast to December 31, 2018 is 45.0/55.0 (with Promissory Note Postponement treated as Equity)

   - <u>OEB Regulated</u> Debt Equity Ratio forecast to December 31, 2018 is 63.5/36.5

b. Debt-Service Coverage-DSC (Tested Annually)
The typical minimum DSC coverage is 1.20X's. During the interim MTS#1 construction period, the TD Bank has adjusted the DSC coverage to assist HHHI with this 'lumpy capital expenditure'.

DSC - Comparison Forecast to Covenant			
Year-End	Forecast		Minimum Covenant
31-Dec-18	1.10		1.00
31-Dec-19	1.10		1.05
31-Dec-20	1.19		1.10
31-Dec-21	1.21		1.20

Term Facilities

Halton Hills Hydro Inc.

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7	Capex 2016	3.86%	$ 22,268.19	$ 4,665,472.75	$ 36,080.42	$ 4,629,392.33	Term Loan 5
8	Interim Construction Demand Loan	Floating rate		$ 12,194,411.52	$ -	$ 12,194,411.52	Term Loan 6
			$ 82,698.19	$ 28,757,855.35	$ 152,382.19	$ 28,605,473.16	

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