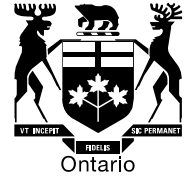


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BY E-MAIL

September 22, 2011

Board Secretary
Ontario Energy Board
2300 Yonge Street, Ste. 2700
Toronto ON M4P 1E4

Attention: Ms. Kirsten Walli, Board Secretary

Dear Ms. Walli:

**Re: Board Staff Interrogatories
Hydro One Networks Inc. US GAAP Proposal
2012 Electricity Transmission Revenue Requirement and Rates
Board File No. EB-2011-0268**

In accordance with Procedural Order No. 1, please find attached Board staff interrogatories for this proceeding. Please forward the attached to Hydro One Networks Inc. and to all intervenors in the proceeding.

Sincerely,

Original Signed By

Harold Thiessen
Case Manager – EB-2011-0268
Senior Project Advisor - Applications

Attachment

**BOARD STAFF INTERROGATORIES
HYDRO ONE NETWORKS INC.
2012 ELECTRICITY TRANSMISSION RATES (US GAAP)
APPLICATION EB-2011-0268
September 22, 2011**

1. Ref: Exhibit C1/Tab1/Sch2

The approximate \$200 million increase in OM&A – the impact of certain overheads not capitalized in the 2010 Transmission decision (EB-2010-0002) – is proposed to be reversed in this application, as per Table 1 Exhibit C1/Tab1/Sch2/pp1&2. This will work to increase capital expenditures by about \$200 million in 2012.

- i) Regarding Hydro One's current proposal to reduce 2012 OM&A by \$200 million: Are there any debits or credits formerly included in 2012 OM&A (using IFRS principles) that would not be allowed under US GAAP rules? Please explain and estimate the amounts of these debits or credits.
- ii) Regarding Hydro One's current proposal to increase 2012 rate base by \$200 million: Are there any debits or credits formerly not included in 2012 rate base (using IFRS principles) that would not be allowed under US GAAP rules? Please explain and estimate the amounts of these debits or credits.

2. Ref: Exhibit A/Tab2/Sch1/p.2

With reference to the proposed reduction in 2012 revenue requirement, please provide an estimated bill impact change (as provided in previous transmission rate cases). Please include all assumptions and appropriate detail.

3. Ref: Exhibit A/Tab2/Sch1/p.2

Hydro One seeks acknowledgement and approval that if US GAAP is approved for Hydro One Transmission rates, that it is appropriate for Hydro One to also use US GAAP for Distribution rates. Please provide an estimate of how a notional Hydro One distribution revenue requirement will be affected by replacing MIFRS with US GAAP. Please provide a detailed impact on Capital Expenditures, OM&A levels, Rate Base, PILs and Revenue Requirement.

4. Ref: Exhibit A/Tab3/Sch1/p1

Hydro One states that, "In May 2011 it became known that there was an option for rate regulated entities to apply to its securities regulator for an exemption to permit use of US GAAP for the preparation of financial statements."

- i) What event occurred in May 2011?
- ii) Had Hydro One not contemplated the use of US GAAP before this time? For example, in the fall of 2010 before the Board's EB-2010-0002 decision?

5. Ref: Exhibit A/Tab3/Sch1/p.4

At Line 16, Hydro One indicates that use of US GAAP for regulatory purposes is in the best interests of all stakeholders. Please provide further details backing up this assertion, listing specific stakeholders and how their interests are best served under US GAAP rather than MIFRS.

6. Ref: Ontario Regulation 395/11

Ontario Regulation 395/11 requires that Hydro One Inc. prepare its financial statements in accordance with US GAAP for any financial year on or after January 1, 2012.

- i) Please file a copy of this Regulation.
- ii) Please confirm that this Regulation is now in force.
- iii) Please confirm that there is no time limitation on the use of US GAAP in the Regulation.

7. Ref: Exhibit B/Tab1/Sch1: Ontario Securities Commission decision, July 21, 2011

Please confirm that the exemption granted in this decision expires on December 31, 2014.

8. Ref: Exhibit B/Tab 1/Sch2/p. 1 Letter of July 7, 2011 from Osler to the Ontario Securities Commission

Hydro One requested a 3 year exemption from the OSC from January 1, 2012 to January 1, 2015. Why did Hydro One choose a 3 year exemption? What factors were considered in applying for this time period? Were certain issues anticipated to be resolved in that time frame?

9. Ref: Exhibit B/Tab1/Sch2/p.9: Letter of July 7, 2011 from Osler to the Ontario Securities Commission

At paragraph 38, the evidence states,

“The Exemption Sought would permit the Filer to use US GAAP for three financial years, commencing on January 1, 2012. This will allow the securities regulatory authorities to assess the consequences of granting the Exemption Sought in light of subsequent developments, including the potential for express recognition of rate regulated accounting under IFRS coincident with the adoption of IFRS in the United States... In short, the proposed sunset provision in the Exemption Sought provides not only the securities regulatory authorities, but also the Filer, with time to evaluate alternatives and determine the best way to proceed in light of the significant ramifications for the Filer of adopting IFRS, as currently formulated.”

Ref: Exhibit C/Tab1/Sch1/p. 4

At this reference, the evidence states,

“Hydro One notes that those who are involved in setting standards for US and international accounting are working closely together, and expect to do so more significantly in the future. As a result of this cooperative effort, US and international accounting frameworks continue to converge. The use of rate-regulated accounting remains as one of the few major differences requiring resolution.”

- i) When is the United States scheduled to adopt IFRS?
- ii) Board staff notes the May 26, 2011 U.S. Securities and Exchange Commission Staff Paper entitled: “Work Plan for the Consideration of Incorporating International Financial Reporting Standards into the Financial Reporting System for U.S. Issuers, Exploring a Possible Method of Incorporation.”¹ On page 1 of this paper it is stated: “The Commission has not yet made a decision as to whether and, if so, how, to incorporate IFRS into the financial reporting system for U.S. issuers.”

If the US determines not to adopt IFRS but continues to use US GAAP, would Hydro One seek a further exemption from the OSC for reporting years subsequent to 2014?

- iii) Please provide the basis for the following statements, including references to supporting material (e.g. the Securities and Exchange Commission website):
 - Those who are involved in setting standards for US and international accounting are working closely together.
 - Those who are involved in setting standards for US and international accounting expect to work closely together more significantly in the future.

¹ <http://www.sec.gov/spotlight/globalaccountingstandards/ifrs-work-plan-paper-052611.pdf>

- iv) Please provide examples of recent convergence of US and international accounting frameworks, particularly with respect to rate-regulated accounting.

10. Ref: EB-2008-0408 Addendum to Report of the Board, June 13, 2011

At page 19 of this Report, the Board indicates:

“The Board cautions utilities that the adoption of USGAAP as a short term solution may be counter-productive. If a utility is required to transition to IFRS for financial reporting purposes a few years after adopting USGAAP, certain transitional issues may not have been avoided, but delayed...”

- i) Please describe what indications exist to suggest that IAS16 will change sufficiently to avoid the problematic consequences of each of the three issues Hydro One identifies: capitalization, depreciation and recognition of regulatory assets.
- ii) Board staff notes the IASB’s most recently published Work Plan², which does not list rate-regulated activities as an active project in 2011 or 2012. Does Hydro One believe that the necessary work will be completed by accounting standards bodies to resolve the issues surrounding the use of rate-regulated accounting under IFRS by December 31, 2014?

If yes, please provide a summary of, or references to information from those accounting standards bodies that support that belief.

- iii) If the issues surrounding rate-regulated accounting under IFRS are not resolved by the time the exemption granted by the OSC expires, what action does Hydro One propose to take? Please explain the rationale for the proposed action.

11. Ref: EB-2008-0408 Addendum to Report of the Board, June 13, 2011

The Board’s Addendum, in Issue 2, makes provision for a Property Plant and Equipment deferral account to capture certain differences arising from the transition to IFRS. The Board notes at page 19 of the Addendum that the account may not be necessary for utilities that adopt US GAAP rather than IFRS. Does Hydro One intend to make use of the Property, Plant and Equipment deferral account? If yes, please explain why the account is necessary and provide an estimate of the amounts that would be captured in the account.

² <http://www.ifrs.org/NR/rdonlyres/C206BF1D-03CA-4B0F-831E-DA172F2466C6/0/Workplan14September2011.pdf>

12. Ref: Exhibit B/Tab2/Sch2 Hydro One July 15, 2011 Letter

On page 2 of this letter Hydro One asserts that there would be reduced costs if a consistent accounting framework were used. Please describe in detail the additional costs Hydro One would incur were the Board to require Hydro One to use MIFRS for rate applications and regulatory filing, while Hydro One Inc. is required to use US GAAP.

13. Ref: Exhibit B/Tab2/Sch2, Hydro One July 15, 2011 Letter

- i) What are Hydro One's costs of transitioning to US GAAP? Please provide detailed estimates.

- ii) If Hydro One transitions to IFRS for January 1, 2015, what are the estimated costs of that transition?

14. Ref: Exhibit C/Tab1/Sch1/pp. 3&4

Hydro One states:

“In addition, US GAAP allows continued use of group depreciation methods. IAS 16 does not. If US GAAP is approved as Hydro One's regulatory accounting and reporting framework, Hydro One will continue its existing depreciation accounting policies, including the use of group depreciation. This results in depreciation rates and annual depreciation expenses that will be lower over the long run and which more closely reflect the average service life of all in-service assets. This will avoid future rate increases that would accompany the use of item depreciation which does not take into consideration the dispersion of asset expected service lives within a group.”

Board staff notes that IAS 16 paragraph 9 states:

“This Standard does not prescribe the unit of measure for recognition, ie what constitutes an item of property, plant and equipment. Thus, judgement is required in applying the recognition criteria to an entity's specific circumstances. It may be appropriate to aggregate individually insignificant items, such as moulds, tools and dies, and to apply the criteria to the aggregate value.”

- i) Why would depreciation expense be lower “over the long run“ if Hydro One uses US GAAP for regulatory purposes as compared to MIFRS? Please explain and quantify the difference.

- ii) Did Hydro One consider using the “vintage basis” of depreciation, in which like assets are categorized together for depreciation purposes and the combined cost of the assets is allocated over their estimated useful life?

iii) Would depreciation expense still be lower under US GAAP if Hydro One used the vintage basis of depreciation, or another similar basis, under MIFRS?

15.Ref: Exhibit B/Tab2/Sch1/p.2

In this letter, Hydro One mentions changes to capitalization from MIFRS to US GAAP. Please provide a table of the specific items that contribute to the change in Rate Base due to adopting US GAAP capitalization rather than MIFRS, including the drivers for the change.

16.Ref: Exhibit C/Tab1/Sch1/p.3

Please confirm that the third word on line 11 of page 3 should be “indirects”.

17.Ref: Exhibit C/Tab1/Sch1/p.4

Line 15 of this reference states:

“In the future, once appropriate normalization adjustments have been made, local benchmarking can still take place.”

Please describe what normalization adjustments are being referred to.

18.Ref: Exhibit C1/Tab1/Sch2/p.1

Hydro One shows a \$200 million reduction in OM&A for 2012 under the US GAAP scenario. Please provide additional detail on these reductions by major category:

Sustaining (Stations, Lines, Engineering and Environmental)
Development (Research, Standards, and Smart Zone)
Operations (Operations, Operations Support, Environment-Health-Safety
Large Customer & Generator Relations)
Shared Services (CCFS, Asset Management, IT, Cornerstone, Cost of
Sales and Other)
Customer Care
Taxes (Property Tax, Indemnity Payments and Rights Payments)

Please include the actual amounts by detailed category and an explanation for the reductions due to the application of US GAAP rather than MIFRS.

19.Ref: Exhibit D1/Tab1/Sch1/p.1

Hydro One has requested that three Regulatory Asset accounts be discontinued. Please indicate if any amounts have been entered into these accounts and if so, how Hydro One proposes to deal with these account balances. Please state if any

of the balances that were entered into these accounts have been incorporated into the proposed revenue requirement in this application.

20.Ref: Exhibit D1/Tab1/Sch1/p.3 IFRS – Incremental Transition Costs Account

- i) Please indicate if any entries have been made to this account and the rationale for making these entries, and report the current balances as of June 30, 2011. Please state the amount of IFRS Transition Costs that were embedded in the 2011 and 2012 revenue requirement approved in EB-2010-0002.
- ii) Please describe Hydro One's intention for recovery of amounts in the Impact for US GAAP Account; specifically, how and when are the amounts proposed to be recovered?

21.Ref: Exhibit D1/Tab1/Sch1/p.3 Impact for US GAAP Account

- i) Please describe the differences between CGAAP and US GAAP referred to in this section and provide an estimate of the debits and credits that Hydro One anticipates will be recorded in this account.
- ii) Please confirm that no other deferral and variance accounts are affected by the change to US GAAP from MIFRS.
- iii) Has Hydro One identified any impact relating to the transition to US GAAP on balances embedded in revenue requirements or deferral/variance account balances approved in EB-2010-0002 or prior decisions specifically relating to employee future benefits and financial instruments?

22.Ref: Exhibit D1/Tab1/Sch1 – Employee Future Benefits

The Board granted continuance of the Pension Cost Differential Account in the EB-2010-0002 Hydro One Transmission Decision.

Page 59 of Hydro One Inc.'s December 31, 2010 audited financial statements, states:

The pension cost variance account was established for Hydro One Networks' Transmission and Distribution Businesses to track the difference between the actual pension costs incurred by the Company and estimated pension costs approved by the OEB. The balance in this account reflects the excess of pension costs paid compared to OEB-approved amounts.

Page 60 of Hydro One Inc.'s December 31, 2010 audited financial statements states:

Deferred Pension

In accordance with the OEB's 1999 transitional rate order, pension costs are recorded in results of operations when employer contributions are paid into the pension plan. The Company's deferred pension asset represents the cumulative difference between employer contributions and pension costs and the deferred pension regulatory liability results from the Company's recognition, as the result of OEB direction, of revenues and expenses in different periods than would be the case for an unregulated enterprise. In the absence of rate-regulated accounting, operating, maintenance and administration expense would have been lower by \$22 million (2009 - higher by \$9 million).

The balance in Hydro One Inc.'s December 31, 2010 audited financial statements for Hydro One's Deferred Pension Asset was \$460 million debit and the balance in the Deferred Pension Regulatory Liability was \$460 million credit.

As per Hydro One Inc.'s December 31, 2010 audited financial statements, a portion of page 67 is reproduced below:

	Pension 2010	Pension 2009	Employee Future Benefits other than Pension 2010	Employee Future Benefits other than Pension 2009
Funded status				
Unfunded benefit obligation	(297)	(230)	(1,178)	(1,004)
Unamortized net actuarial losses (gains)	746	640	144	10
Unamortized past service costs	11	14	11	14
Deferred pension asset (accrued benefit liability)	460	424	(1,023)	(980)
Less: Current portion	-	-	43	40
Deferred pension asset (long-term liability)	460	424	(980)	(940)

- i) Please file a copy of Hydro One Inc.'s December 31, 2010 audited financial statements.
- ii) Please confirm that Hydro One as at December 31, 2010 records pension costs using the cash basis and records employee future benefits other than pension using the accrual basis. If this is not the case, please explain.
- iii) Please confirm that under both IFRS and US GAAP Hydro One would cease to be able to use the cash basis to record pension costs, and must change to the accrual basis. If this is not the case, please explain. If Hydro One must make this change, please provide estimated dollar impacts for:
 - the impact of this change on the 2012 revenue requirement approved in EB-2010-0002;
 - how this impact is reflected in the proposed 2012 revenue requirement in this application; and
 - the impact on balances in any deferral/variance account.

iv) Is Hydro One seeking to continue the Pension Cost Differential Account?

v) *Deferred Pension Asset*

Board staff notes that the Deferred Pension Asset, as described on page 67 of Hydro One Inc.'s December 31, 2010 audited financial statements, had a balance of \$460 million debit as at December 31, 2010. Included in this amount was \$746 million debit of unamortized net actuarial losses.

Board staff further notes that an additional amount of unamortized net actuarial losses of \$144 million relating to employee future benefits other than pension was recorded in Hydro One Inc.'s December 31, 2010 audited financial statements.

a) Does Hydro One intend to put part of the balance of the Deferred Pension Asset (or any of its components), as described on page 67 of Hydro One Inc.'s December 31, 2010 audited financial statements, into the Pension Cost Differential Account?

Please note that this question relates to the balance of the Deferred Pension Asset that existed as at December 31, 2010 of \$460 million, or any amount that existed prior to, or exists beyond December 31, 2010. Please explain and provide the proposed amounts.

b) Are any of these amounts proposed to be put in the requested Impact for US GAAP Account? Please explain and provide the proposed amounts.

c) Did Hydro One incorporate any part of the balance or an estimate of the Deferred Pension Asset (or any of its components) as described on page 67 of Hydro One Inc.'s December 31, 2010 audited financial statements, into the 2012 revenue requirement approved in EB-2010-0002?

Please note that this question relates to the balance of the Deferred Pension Asset that that existed as at December 31, 2010 of \$460 million, or any amount that existed prior to, or exists beyond December 31, 2010. Please explain and provide the amounts.

d) Did Hydro One incorporate any part of the balance of the Deferred Pension Asset (or any of its components) as described on page 67 of Hydro One Inc.'s December 31, 2010 audited financial statements, into the proposed 2012 revenue requirement in this application?

Please note that this question relates to the balance of the Deferred Pension Asset that that existed as at December 31, 2010 of \$460 million, or any amount that existed prior to, or exists beyond December 31, 2010.

Please explain and provide the proposed amounts. Please differentiate between any amounts that were previously incorporated into the 2012 revenue requirement approved in EB-2010-0002, and any new amounts incorporated into the proposed 2012 revenue requirement.

- e) If any of the amounts described in the Deferred Pension Asset questions above are not incorporated into the proposed 2012 revenue requirement, does Hydro One propose to recover these amounts? If so, when and how is Hydro One proposing to recover the amounts?

23.Ref: Exhibit D1/Tab1/Sch1 – Employee Future Benefits

Page 34 of Hydro One Inc.'s December 31, 2010 audited financial statements states:

Employee Future Benefits

In the absence of RRA, the continuation of accounting for expenditures related to employer-sponsored pension plans on a cash basis is not permissible. Regulatory assets and liabilities, representing the cumulative difference between our Company's pension contributions currently accounted for on a cash basis at the direction of the regulator, and the costs that would be recognized on an accrual basis under Canadian GAAP, would not meet the definition of assets or liabilities under IFRS and hence will require de-recognition at the IFRS transition date. We have assessed our options with respect to the recognition of accumulated, unamortized actuarial gains and losses associated with employment benefits. The possible alternatives to account for these pension and other employee benefit amounts include charging unamortized actuarial gains and losses immediately upon adoption under IFRS 1 or recognizing an adjustment to those amounts retrospectively to comply with IAS 19, *Employee Benefits* (IAS 19). In the absence of rate-regulated accounting, we intend to recognize a retrospective adjustment for these amounts under IAS 19, without the IFRS 1 exemption. The impact of adopting IAS 19 retrospectively at December 31, 2010 would have been a reduction to retained earnings of \$319 million.

On page 34 of Hydro One Inc.'s December 31, 2010 audited financial statements, Hydro One stated that under IFRS it intended to recognize a retrospective adjustment for accumulated unamortized actuarial gains and losses associated with employee benefits. The impact of adopting IAS 19 retrospectively at December 31, 2010 would have been a reduction to retained earnings of \$319 million.

- i) Is an estimation of the amount of the impact of adopting IAS 19 retrospectively (or alternatively an estimation of charging unamortized actuarial gains and losses that would occur immediately upon adoption under IFRS 1), embedded in an amount included in the 2012 revenue requirement approved in EB-2010-0002?
- ii) If this is the case, please explain and disclose the amount incorporated into the approved revenue requirement. If this is not the case, please explain.
- iii) Please disclose any amount incorporated into the proposed 2012 revenue requirement, the Pension Cost Differential Account, or the Impact for US GAAP Account, for these types of costs that would occur under US GAAP.
- iv) Please explain how the treatment of these costs would differ under US GAAP when compared to each of IFRS and Canadian GAAP.

24. Ref: Exhibit D1/Tab1/Sch1 – Employee Future Benefits

US GAAP requirements were effective for fiscal years beginning after December 15, 1988 for pensions and December 31, 1994 for employee future benefits other than pensions (OPEBs). The Securities and Exchange Commission provides an exemption for foreign registrants which permits them to adopt the US GAAP requirements as of a date prior to the first period US GAAP information is prepared.

- a) Have Hydro One's external auditors confirmed that Hydro One qualifies for this Securities and Exchange Commission exemption and can use different effective dates than those articulated in US GAAP requirements?
- b) If Hydro One qualifies for this Securities and Exchange Commission exemption, what date does Hydro One propose to adopt the US GAAP requirements for pensions and OPEBs? Please indicate the reasons for the choice of date(s).

25. Ref: Exhibit C1/Tab1/Sch2 - Financial Instruments

Please explain the impact of the transition to US GAAP on Hydro One's financial instruments when compared to principles established under CGAAP and IFRS. . Please provide estimated dollar impacts and describe Hydro One's proposed method of recovery of this impact.