

Hydro One Networks Inc.

8th Floor, South Tower
483 Bay Street
Toronto, Ontario M5G 2P5
www.HydroOne.com

Tel: (416) 345-5700
Fax: (416) 345-5870
Cell: (416) 258-9383
Susan.E.Frank@HydroOne.com

Susan Frank

Vice President and Chief Regulatory Officer
Regulatory Affairs



BY COURIER

February 7, 2012

Ms. Kirsten Walli
Secretary
Ontario Energy Board
Suite 2700, 2300 Yonge Street
Toronto, ON.
M4P 1E4

Dear Ms. Walli

EB-2011-0399 – Hydro One Networks' Distribution Request for Approval of US GAAP for Rate Setting, Regulatory Accounting & Reporting Purposes - Hydro One Reply Argument

Please find attached Two (2) hard copies of Hydro One Networks Reply Argument.

An electronic copy of this Argument has been filed using the Board's Regulatory Electronic Submission System.

Sincerely,

ORIGINAL SIGNED BY SUSAN FRANK

Susan Frank

Attach.

c. EB-2011-0399 - Intervenors (electronic only)

Hydro One Reply Argument

Introduction

Hydro One Networks Inc. (“Hydro One”) is pleased to file its reply argument in relation to its application for an order or orders approving Hydro One Distribution’s utilization of US Generally Accepted Accounting Principles (“US GAAP”) as its approved framework for rate setting, regulatory accounting and regulatory reporting commencing January 1, 2012, in a manner appropriate for a rate regulated entity.

Pursuant to the Procedural Order issued by the Board, all intervenors in Hydro One’s last distribution rates application EB-2009-0096 were made intervenors in this proceeding, as were all intervenors who participated in the Board initiated review of the Company’s 2012 electricity transmission revenue requirement under Board proceeding EB-2011-0268. In accordance with the Board’s Procedural Order, Hydro One received argument submissions from Board staff as well as:

- Builders, Owners and Managers Association of Toronto (“BOMA”);
- Canadian Manufacturers and Exporters (“CME”);
- Power Workers’ Union (“PWU”);
- School Energy Coalition (“SEC”); and
- Vulnerable Energy Consumers Coalition (“VECC”).

Hydro One observes that there is broad support for its request to utilize US GAAP as its regulatory accounting and rates setting framework for its distribution business effective January 1, 2012.

Hydro One notes that BOMA, CME, PWU, SEC, VECC and Board staff all support Hydro One’s request, including the proposed continuation of its approved 2011 distribution rates into 2012 on a US GAAP basis. All of these parties were satisfied, on the evidence before the Board, that the transition to US GAAP instead of Modified IFRS

("MIFRS") is of substantial benefit to ratepayers and the shareholder. No party raised any serious challenge to the benefit of the proposed change. The requested change is the same that has been approved by other regulators across Canada for other utilities, as well as that which was approved by this Board for Hydro One's transmission business.

Hydro One therefore asks that its proposal be approved.

Board staff and some intervenors did raise a few concerns to which Hydro One feels it should respond. Each of those will be addressed briefly below.

Impact of Hydro One's Ability to Perform Peer Group Comparisons

Board staff, VECC and CME raised concerns about Hydro One's ability to benchmark against its peer group of local Ontario distribution utilities if it transitions to US GAAP for rate setting and regulatory accounting purposes. The Board was cognisant of this concern and acknowledged it when approving the use of US GAAP for Hydro One's transmission business.

In that decision in EB-2011-0268 as a result, the Board directed Hydro One, in its next distribution cost of service application, to address this concern. As outlined in its application within this proceeding, Hydro One intends to respond to the Board's direction in this regard when it files its next cost of service rate application.

As noted in its reply to this concern in EB-2011-0268, Hydro One believes that it will continue to benchmark with other local utilities. OM&A cost comparisons can still be made. This would be possible following appropriate top down adjustments. The Company does acknowledge, as it has done in the past, that total cost benchmarking will become more of a challenge as time passes due to the inclusion of depreciation expenses in total costs. Further, the Board's difficulty with regards to benchmarking total costs has increased with the required adoption of MIFRS by LDCs as the latitude of variation of depreciation methodology and the resulting expenses between companies has increased. Hydro One will work towards developing solutions to allow appropriate total cost

benchmarking in the short term and in the long term. However, as the Board and its expert have recognized in the past, this will not diminish the difficulty of the Board to benchmark Hydro One against LDCs due to fundamental differences between their businesses.

Variance Accounts

Hydro One proposed discontinuance of the Impact for Changes in IFRS account. Nobody opposed discontinuance of this account. A similar account was discontinued by order of the Board for Hydro One's transmission business in EB-2011-0268.

Hydro One also proposed, akin to what was proposed and approved in EB-2011-0268, a new variance account – the impact for US GAAP account. Nobody opposed establishment of this account. Hydro One is proposing a symmetrical variance account akin to that which was approved by the Board for its transmission business.

Hydro One also proposes to continue, with revised scope, the IFRS incremental transition cost account. No serious challenges were made to this proposal.

Accordingly, Hydro One asks that the Board approve its proposals with respect to these variance accounts.

SEC and CME raised the concern that Hydro One was either directly or indirectly seeking, in this proceeding, Board approval to continue other variance accounts that would, in the usual course, not continue beyond 2011. Hydro One notes that the ongoing variance accounts referenced, will be subject to the Board's normal prudence review prior to disposition of any balances, as part of the next distribution cost of service proceeding.

Overhead Capitalization Practice Concerns

The Board in EB-2011-0268, in response to concerns raised by other intervenors, directed Hydro One to provide a review of its overhead capitalization policies in its next rates

case. Hydro One does intend to respond to this direction in its next transmission cost of service application.

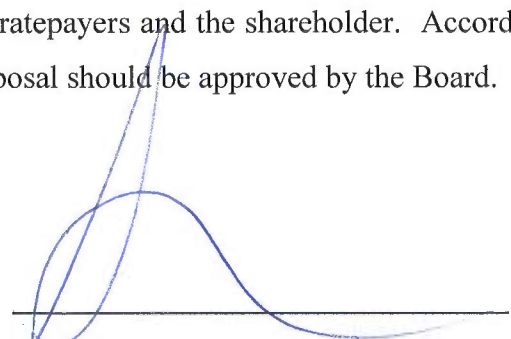
In this proceeding SEC requested clarification that the overhead capitalization review study applies to both transmission and distribution. As Hydro One outlined in Exhibit I, Tab 1, Schedule 12, as it utilizes the same capitalization methodology in both its transmission and distribution businesses, it applies the results of its overhead capitalization policy review to both its transmission and distribution businesses.

Summary

All parties overwhelmingly support Hydro One's proposal to utilize US GAAP as the basis for rate setting and regulatory accounting and reporting commencing January 1, 2012 for its distribution business. The few specific concerns raised by some intervenors can be addressed as part of the next distribution cost of service proceeding. US GAAP has already been approved by the Board for its transmission business. This would reduce the notional revenue requirement for distribution in 2012 by \$166M and avoids a future distribution rate increase in the region of 14 percent, solely attributable to a change to a modified IFRS capitalization policy.

Hydro One's proposal is of benefit to both ratepayers and the shareholder. Accordingly, Hydro One respectfully submits that its proposal should be approved by the Board.

All of which is respectfully submitted.



D.H. Rogers, Q.C.
Anita M. Varjadic
(original signed by A. Varjadic)