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Oded Hubert
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BY COURIER

September 27, 2016

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

Dear Ms. Walli:

EB-2016-0276 – Hydro One Networks Inc. MAAD S86 to Purchase all of the issued and outstanding shares of Orillia Power Distribution Corporation – Prefiled Evidence

Please find attached Hydro One Networks Inc.'s prefiled evidence on Orillia Power Distribution Corporation. Two (2) hard copies will be sent to the Board shortly.

An electronic copy of this cover letter and the attached prefiled evidence has been filed through the Ontario Energy Board's Regulatory Electronic Submission System (RESS).

Sincerely,

ORIGINAL SIGNED BY JOANNE RICHARDSON ON BEHALF OF ODED HUBERT

Oded Hubert

ONTARIO ENERGY BOARD

IN THE MATTER OF an application made by Hydro One Inc. for leave to purchase all of the issued and outstanding shares of Orillia Power Distribution Corporation, made pursuant to section 86(2)(b) of the *Ontario Energy Board Act, 1998*.

AND IN THE MATTER OF an application made by Orillia Power Distribution Corporation seeking to include a rate rider in the 2016 Board-approved rate schedules of Orillia Power Distribution Corporation to give effect to a 1% reduction relative to 2016 base distribution delivery rates (exclusive of rate riders), made pursuant to section 78 of the *Ontario Energy Board Act, 1998*.

AND IN THE MATTER OF an application made by Orillia Power Distribution Corporation for leave to transfer its distribution system to Hydro One Networks Inc., made pursuant to section 86(1)(a) of the *Ontario Energy Board Act, 1998*.

AND IN THE MATTER OF an application made by Orillia Power Distribution Corporation for leave to transfer its rate order to Hydro One Networks Inc., made pursuant to section 18 of the *Ontario Energy Board Act, 1998.*

AND IN THE MATTER OF an application made by Orillia Power Distribution Corporation seeking cancellation of its distribution licence, made pursuant to section 77(5) of the *Ontario Energy Board Act, 1998*.

AND IN THE MATTER OF an application made by Hydro One Networks Inc. seeking an order to amend its distribution licence, made pursuant to section 74 of the *Ontario Energy Board Act, 1998*, to serve the customers of the former Orillia Power Distribution Corporation.

APPLICATION

1.0 INTRODUCTION

Hydro One Inc. ("HOI") is a corporation incorporated under the laws of the Province of Ontario and is the parent company of Hydro One Networks Inc. ("Hydro One"). Hydro One is a licensed distributor regulated by the Ontario Energy Board in accordance with the *Ontario Energy Board Act, 1998* (the "Act"). A corporate organizational chart of Hydro One, both before and after the transaction, is provided as **Attachment 1**.

Hydro One's distribution system serves approximately 1.3 million customers in its service territory (see **Attachment 2** for further customer details).

Orillia Power Distribution Corporation ("OPDC") is, at the date of this Application, a wholly owned subsidiary of Orillia Power Corporation ("OPC"). OPC is a holding company, currently wholly owned by The Corporation of the City of Orillia (the "City"). A corporate organizational chart of OPC is provided as **Attachment 3**.

OPDC's distribution system serves approximately 13,445 Residential and General Service customers in the OPDC service territory (see **Attachment 4** for further customer details).

2.0 OVERVIEW OF APPLICATION

On August 15, 2016, the City and Orillia Power Corporation (the "Vendor") and HOI (the "Purchaser") entered into a Share Purchase Agreement (the "Agreement"), the effect of which is that the Vendor and the City have agreed to sell, and the Purchaser has agreed to purchase, all of the issued and outstanding shares of OPDC. The purchase price is $41.3 million, comprising a cash payment of approximately $26.4 million for the shares and the assumption of OPDC's

short- and long-term debt (including regulatory deferral account balances) of approximately $14.9 million. The Agreement contemplates the closing of the transaction on the first business day of a month and at least 90 days following the Parties' receipt of all required approvals, including Ontario Energy Board ("the Board" or "OEB") approval of this Application.

The Agreement (see **Attachment 5**) contemplates the following items in addition to the sale of the shares:

(a) OPDC will apply to the OEB for approval to include a negative rate rider to OPDC's electricity rates[1] to reduce base distribution delivery rates by one per cent across residential and general service rate classes, and to have such reduced rates apply for the next five years (see **Exhibit A, Tab 2, Schedule 1 Section 2.0** for further detail);
(b) The Purchaser or its affiliates shall offer all active employees of OPDC continued employment in the City of Orillia for a period of at least one year;
(c) The Purchaser shall establish an advisory committee (the "Advisory Committee") to provide a forum for communication between the Purchaser and the community;
(d) After closing, the community will be eligible for Hydro One's community programs;
(e) The purchase price is subject to adjustment, within 90 days following closing, for working capital, net fixed assets, regulatory accounts and long term debt, as defined in the Agreement.

The resolutions that give way for the execution of the Agreement are provided as **Attachment 6**.

This Application adheres to the principles of the "*Report of the Board on Rate-Making Associated with Distributor Consolidation*" issued on March 26, 2015 ("Amended Report"). The Amended Report provides Board policy pronouncements pertaining to rate-making for associated distributor consolidation transactions. These include: (1) an extension to the rate

[1] The rider will be applied OPDC's 2016 Rates as approved by the Board in EB-2015-0024

rebasing deferral period, to a duration of up to ten years after the close of the transaction; (2) a requirement for use of an earning sharing mechanism ("ESM") where an applicant seeks a deferral period greater than five years and up to ten years; (3) utilization of the incremental capital investment module ("ICM") by the consolidating entity during the rate rebasing period; and (4) clarifications as to which incentive plan would apply to distributors who are party to a merger, amalgamation, acquisition, and divestiture ("MAAD") transaction during any deferred rebasing period. Further guidance was provided by the Board with the release of the "*Handbook to Distributor and Transmitter Consolidations and Filing Requirements for Consolidation Applications"* (the "Handbook") released on January 19, 2016. Hydro One has considered the intent of these reports in developing this Application.

The proposed Transaction will both benefit and protect ratepayers:

- Ratepayers will receive the benefit of: (i) a reduction of 1% in their base distribution delivery rates in Years 1 to 5; (ii) a rate increase of less than inflation in years 6 to 10 (inflation less productivity stretch factor); and (iii) a further sharing of $3.4 million, a result of the guaranteed ESM, in Years 11 forward. In addition, customers will benefit in the longer term from the lower ongoing cost structures.
- The implementation of a guaranteed ESM protects OPDC ratepayers from the risk of Hydro One failing to achieve the forecast level of synergy
-

3.0 OEB APPROVAL REQUESTS

The following OEB approvals are requested under Sections 86(2)(b), (86(1)(a), 77(5) and 74 of the Act:

- Hydro One is applying to the Board pursuant to section 86(2)(b) of the Act, seeking leave to acquire all the issued and outstanding shares of Orillia Power Distribution Corporation from the City.

- OPDC is applying pursuant to section 86(1)(a) of the Act to dispose of its distribution system to Hydro One.
- OPDC is applying pursuant to section 18 of the Act to transfer its rate order to Hydro One.
- If the Board grants leave for OPDC to dispose of its distribution system to Hydro One, after closing and upon integration of the proposed transactions, OPDC requests, pursuant to section 77(5) of the Act, that its electricity distribution licence be cancelled. Hydro One requests, pursuant to section 74 of the Act, that Hydro One's distribution licence be amended such that Appendix B, Tab 1 of Schedule 1 include *The City of Orillia, County of Simcoe as at October 31, 1991*, as described in Schedule 1 of OPDC's licence.
- Upon completion of integration, HOI will transfer the assets and liabilities of the electricity distribution business from OPDC to Hydro One.
-

4.0 OTHER APPROVALS AND CONSIDERATIONS

- Hydro One is applying for approval to defer the rate rebasing of OPDC for ten years from the date of closing of the proposed transaction, consistent with the new Board policy set out in the Amended Report.
- Hydro One is applying for approval to continue to track costs to the regulatory asset accounts currently approved by the OEB for OPDC and to seek disposition of their balances at a future date. See **Exhibit A, Tab 2, Schedule 1, Section 3** for further details.
- All OPDC rate riders will continue as per OPDC's existing rate schedules until expiry.
- Hydro One is applying for approval to utilize US GAAP for OPDC financial reporting.
- Hydro One is applying for approval to use an ESM to operate during the extended deferred rebasing period (i.e., years six to ten), consistent with page 16 of the Handbook. Hydro One's proposed ESM is described in **Exhibit A, Tab 3, Schedule 1**.
- Hydro One is applying to use an Incremental Capital Module ("ICM") during the extended deferred rate rebasing period, as described on page17 of the Handbook.

- During the extended deferred rebasing period, rates of customers of OPDC will be set using the Price Cap Index adjustment mechanism as described in **Exhibit A, Tab 2, Schedule 1**.
- The net book value of OPDC's assets, as at December 31, 2015, is $22.5 million.

This transaction was completed on a commercial basis between a willing seller and a willing buyer. It is a demonstration of the types of benefits that can be realized from voluntary consolidation, and it will deliver cost synergies and economy of scale savings contemplated by the Ontario Distribution Sector Review Panel. Hydro One submits that the evidence supports approval of the Application, as the transaction will have a positive or neutral effect on the attainment of the OEB's statutory objectives, and the customers of both local distribution companies will be held harmless. This is achieved as result of the following:

- The application has no adverse impact on the price, adequacy, reliability and quality of electricity service of OPDC or Hydro One;
- The application has no adverse impact on the promotion of electricity conservation and demand management, the use and generation of electricity from renewable energy sources, and it facilitates the implementation of a smart grid in Ontario;
- Hydro One is committed to promoting the education of consumers through community involvement and customer consultation for future rate-setting applications;
- The implementation of Hydro One's ESM benefits and protects OPDC customers during the extended deferred rebasing period by guaranteeing a share of excess earning of $3.4 million, established on an aggressive estimate of savings from the transaction. The guaranteed amount of $3.4 million corresponds to approximately 45% of OPDC's current Board-approved revenue requirement;
- The transaction eliminates the duplication of effort between Hydro One and OPDC and results in a single electricity service provider for the Orillia area, the northeastern portion of Simcoe County. This will ultimately create downward pressure on cost structures across both Hydro One and OPDC service areas.

Hydro One respectfully requests a written hearing for this Application.

Hydro One requests that a copy of all documents filed with the Board be served on the Applicant and the Applicant's counsel, as follows:

a) The Applicant:

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IMPACT OF THE PROPOSED TRANSACTION

1.0 INTRODUCTION

This exhibit provides HOI's impact assessment of the proposed transaction and also provides a discussion of the impact of the transaction on OPDC's and Hydro One's future operations in relation to the OEB's statutory objectives. It elaborates on how the transaction promotes economic efficiency and cost-effectiveness in the distribution sector and also discusses other related matters pertaining to this transaction.

2.0 IMPACT OF THE PROPOSED TRANSACATION

The Handbook's *Filing Requirements for Consolidation Applications* requires applicants to provide evidence to demonstrate the impact of the proposed transaction with respect to the OEB's first two statutory objectives. The Handbook recognizes that there are other instruments and tools that will ensure that the OEB's remaining statutory objectives, relating to conservation and demand management, implementation of smart grid and the use and generation of electricity from renewable resources, will not be adversely impacted by a consolidation. Therefore, the Board has determined that there is no need or merit in further review of these statutory objectives as part of a consolidation transaction[1].

SECTION 2.1: OBJECTIVE 1 – PROTECT CONSUMERS WITH RESPECT TO PRICE AND ADEQUACY, RELIABILITY AND QUALITY OF ELECTRICITY SERVICE

This Application demonstrates that the cost structures from proceeding with the transaction will result in expected ongoing operations, maintenance and administrative ("OM&A") savings of

[1] Handbook, Page 6

approximately $3.9 million per year and reductions in capital expenditures of approximately $0.6 million per year (based on the level of savings achieved by Year 10). These efficiencies, representing an ongoing OM&A reduction of approximately 60% of OPDC's 2015 OM&A costs (65% of the Year 10 status quo forecast), will result in downward pressure on OPDC's cost structures relative to the status quo and will be realized while maintaining adequacy, reliability and quality of electricity service. Table 1 illustrates the projected cost savings from this transaction. These will be further discussed in Section 2.2.

Table 1: Projected Cost Savings - $M

	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10
OM&A										
Status Quo Forecast	4.8	4.9	5.0	5.1	5.2	5.3	5.4	5.5	5.6	5.8
Hydro One Forecast	4.1	2.1	2.0	1.7	1.7	1.7	1.8	1.8	1.9	1.9
Projected Savings	**0.7**	**2.8**	**2.9**	**3.4**	**3.5**	**3.6**	**3.6**	**3.7**	**3.8**	**3.9**
Capital										
Status Quo Forecast	2.7	2.8	2.9	3.0	3.1	3.2	3.3	3.4	3.5	3.6
Hydro One Forecast	3.6	2.3	2.4	2.3	2.4	2.5	2.6	2.7	2.9	3.0
Projected Savings	**(0.9)**	**0.5**	**0.5**	**0.7**	**0.7**	**0.7**	**0.7**	**0.7**	**0.6**	**0.6**

Hydro One's 2015 OM&A cost to serve customers in its high density residential rate class (UR) is $173/customer[2], compared to OPDC's cost of $362/customer[3]. Hydro One's urban rate class covers areas containing 3,000 or more customers with a density of at least 60 customers per kilometer. As such, it is reasonable to believe that if this transaction proceeds, Hydro One will be able to serve OPDC's service area, which has about 13,500 customers and a density of 58

[2] EB-2013-0416, 2015 Draft Rate Order Filed April 10, 2015
[3] As shown in the 2015 OEB Yearbook

customers per km of line, at a cost that is comparable to Hydro One's UR rate class (approximately 90% of OPDC's customers are residential).

Price of Electricity Service

The acquired OPDC customers will have rates adjusted in the next ten years as discussed below.

Rate-setting in Years 1-5 of the Deferred Rebasing Period

2016 base distribution delivery rates will be reduced by 1% and frozen for a period of five years from closing of this transaction[4].

Table 2 shows the customer bill impact of this reduction applied to the average consumption levels for residential and general service rate classes. The impacts on total bill as well as distribution rates are provided. The rate reductions vary slightly from the 1% reduction as a result of rounding errors from using two decimal places for fixed charges and four decimal places for volumetric charges, as prescribed by the Board, and also due to the fact that the 1% rate reduction does not apply to other existing rate riders or LV rates included in the table below under distribution rates.

Table 2: Bill Impacts for OPDC Customers

Rate Class[5]	Change in Distribution Delivery Rates	Change in Total Bill (%)
Residential	(0.92%)	(0.20%)
General Service less than 50 kW	(1.08%)	(0.23%)
General Service 50 to 999 kW	(0.97%)	(0.07%)

[4] A negative rate rider that will result in a 1% reduction of 2016 base delivery rates as approved by the OEB in EB-2015-0024 will be implemented over that term.
[5] The proposed 1% rate reduction does not apply to the other rate classes.

At the same time, OPDC's residential distribution rates will continue to be adjusted to move to a fully fixed distribution charge, per OEB Policy "*A New Distribution Rate Design for Residential Customers*" (EB-2012-0410). In EB-2015-0024, the OEB approved a four-year transition period for OPDC to move to fixed rates, beginning in 2016.

Detailed calculations of customer bill impacts and the determination of the rate riders can be found in **Attachment 7** and **Attachment 8**. The proposed rate schedules, which include the requested rate rider for the area currently served by OPDC, effective after closing, are filed as **Attachment 9.**

The cost of providing this rate rider (approximately $79,000 per year[6]) will be recovered from synergies that are generated from consolidating OPDC's operations into Hydro One. This negative rate rider will be discontinued at the end of Year 5.

All other OPDC tariffs will remain as approved in OPDC's last rate order[7], with the exception of Specific Service Charges. Customers of the former OPDC using these services will be charged the rates approved for Hydro One Distribution in rate order EB-2015-0079.

Rate-setting in Years 6-10 of the Deferred Rebasing Period

Beginning in year six through to year ten, rates for the former customers of OPDC will be set using the Price Cap adjustment mechanism, outlined in the Amended Report. At the commencement of year six, Hydro One will apply the OEB's Price Cap Index formula utilizing the former OPDC's efficiency cohort factor (0.3%). This will be anchored to the current OPDC base distribution delivery rates as approved by the OEB in EB-2015-0024.

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[6] 2015 OPDC FS – OPDC Distribution Revenue ($7,857k) multiplied by 1%
[7] EB-2015-0024

Earnings Sharing Mechanism

Since Hydro One is requesting a 10-year deferred rebasing period, Hydro One will also be implementing an ESM, in accordance with the Amended Report. As outlined in the Handbook, the ESM as set out in the Amended Report may not achieve the intended objectives for all types of consolidation proposals. Hydro One is therefore proposing an ESM that protects OPDC customer interests during the extended deferred rebasing period. Further details on Hydro One's proposed ESM are found in **Exhibit A, Tab 3, Schedule 1**.

Hydro One Legacy Customers

The proposed transaction also protects Hydro One's existing customers. On March 12, 2015, Hydro One received approval for rates effective from January 1, 2015, to December 31, 2017. That application was based on Hydro One's existing customer base: in other words, it did not include any capital or OM&A costs associated with serving customers or with maintaining or operating assets in the service territory of any acquired local distribution company ("LDC"), including OPDC. As such, this transaction will not impact Hydro One's existing customers with respect to price.

In 2017, Hydro One intends to file a five-year Custom Incentive Regulation application for rates effective from 2018 through to 2022. That application will not include any costs associated with serving the customers of OPDC. Costs to serve these customers will not be included in any Hydro One revenue requirement application until the deferred rebasing period has expired.

Once the deferred rebasing period has expired, Hydro One's existing customers are expected to derive a small price benefit, as the company's fixed costs of operations will be spread over a wider customer base.

Adequacy, Reliability and Quality of Electricity Service

Once the transaction is approved by the OEB, the Vendor intends to transfer OPDC's regulated distribution assets so that they are owned by Hydro One Inc. Transfer of the distribution system is expected to occur within 18 months after the close of the Agreement. Once integration is complete, the assets will be integrated with, and form part of Hydro One's existing distribution system. This change in control is expected to improve adequacy, reliability and quality of service.

Hydro One endeavors to maintain or improve reliability and quality of electricity service for all of its customers. Hydro One currently has existing assets serving many customers in close proximity to the current OPDC service territory (please see map filed as **Attachment 10**), making Hydro One a natural consolidator for OPDC. As part of the proposed consolidation, Hydro One will retain local knowledge from existing OPDC staff. This local knowledge, in coordination with Hydro One's regional operations and staff, will allow Hydro One to maintain or improve reliability.

The existing reliability metrics for OPDC and Hydro One's local metrics are provided in Table 3 below. Hydro One has used distribution stations (Bass Lake D.S, Rugby D.S & Silver Lake DS) in the vicinity of OPDC to compare with OPDC's metrics provided in the OEB Yearbook.

Table 3: Reliability Metrics*

	2013	2013	2014	2014	2015	2015
	Hydro One	**Orillia Power**[8]	**Hydro One**	**Orillia Power**	**Hydro One**	**Orillia Power**
Duration (SAIDI)	2.28	1.13	0.57	2.15	3.16	1.06
Frequency (SAIFI)	1.02	1.03	0.30	1.28	1.01	2.44

*Excluding LOS[9]

Based on reliability statistics for 2013 to 2015, Hydro One customers in the vicinity of the City of Orillia experienced a level of service in terms of duration and frequency of interruptions similar to the level experienced by OPDC customers. For 2014, Hydro One performed better than OPDC in terms of duration of outages, whereas OPDC performed better in 2013 and 2015; for 2013, 2014 and 2015, Hydro One performed better than OPDC in terms of frequency of outages. Hydro One anticipates that reliability may in fact improve with the combination of pre-existing Hydro One and former OPDC resources optimized for the broader Orillia area.

In the long term, OPDC customers are expected to benefit from operational efficiencies expected by having the OPDC assets integrated into Hydro One's larger distribution system. Scale efficiencies are expected in the areas of operating and maintaining the distribution system, planning capital replacement and the overhead and management functions. The foregoing is discussed further in Section 2.2.

Other Items

There are no net metering customers in the current OPDC service area. Therefore, the net metering thresholds as a result of this consolidation will remain unchanged.

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[8] Data-source is the OEB Yearbook

[9] Loss of Supply ("LOS") interruptions attributable to assets that are not part of the Hydro One distribution System or the OPDC Distribution System

Hydro One has agreed to establish an Advisory Committee to provide a forum for communication between Hydro One and the community. Under the terms of the Agreement, the Vendor may appoint three representatives to the committee, and Hydro One will include both senior management and local staff representation.

The City of Orillia will retain the current OPDC Operating Centre on West Street for future redevelopment. Hydro One has agreed to enter into a five-year lease agreement with the City to lease this centre. Conditional on the completion of the sale, Hydro One intends to commence construction, during the lease period, of a permanent operations and administration building within the City of Orillia. This new centre will consolidate operations between Hydro One's pre-existing Orillia Operating Centre and OPDC's Operating Centre on West Street.

SECTION 2.2: OBJECTIVE 2 – PROMOTE ECONOMIC EFFICIENCY AND COST EFFECTIVENESS AND FACILITATE THE MAINTENANCE OF A FINANCIALLY VIABLE ELECTRICITY INDUSTRY

Hydro One submits that this transaction will promote economic efficiency and cost effectiveness which will result in lower ongoing cost structures.

Economic efficiency is attained through sector consolidation, which ultimately eliminates redundant activities. Cost effectiveness reduces OM&A and capital expenditures and is achieved by leveraging Hydro One's economies of scale. These together result in sustained operational efficiencies, both quantitative and qualitative.

With the integration of OPDC's staff and operations with Hydro One's existing operations, Hydro One expects sustained operational efficiencies to be realized in distribution operations, administration, information technology and customer service.

Staff Integration

As Hydro One already has an operating organization in place that provides many of the same functions as OPDC, certain redundant positions will no longer be required. Table 4 shows the existing OPDC labour split between direct and indirect staff. Direct staff, such as line and forestry employees, work directly on the distribution assets. Indirect staff are considered support staff such as back-office, customer service, finance, etc.

Table 4: Current OPDC Staff Positions

	Direct	Indirect
Management	-	8
Back Office	-	8
Trades & Technical	15	7
Total	**15**	**23**

OPDC's direct staff will be integrated into Hydro One's local operations and will become part of the area's pool of resources working within the larger Hydro One service area, which encompasses OPDC's current service territory. Hydro One will expand its local complement of direct staff positions by only 9 staff to serve its expanded territory (i.e., existing Orillia area plus OPDC), compared to the 15 direct positions currently required by OPDC to operate only the existing OPDC service area. The remaining 29 direct and indirect staff currently employed by OPDC are expected to move to other positions within Hydro One once integration is complete.

Although certain functions and positions will be eliminated as part of the integration process leading to efficiency gains, Hydro One, due to its size and current staff retirement profile, is able to offer continued employment to existing OPDC staff. OPDC personnel currently in these roles will have the opportunity to transition to existing positions within the Hydro One organization. This will allow Hydro One to leverage the industry knowledge of existing OPDC staff to meet customer needs. As Hydro One will now be planning the electricity requirements for the entire

Orillia area, it will be able to more efficiently manage both the operating and capital costs associated with serving customers across the area.

Distribution Operations

Local area operating and capital savings will result in a more efficient distribution system due to the elimination of an artificial electrical boundary and thereby realizing benefits from contiguity.

Hydro One's existing service territory is situated immediately adjacent to the territory served by OPDC. The geographic advantage of contiguity allows for economies of scale to be realized at the field and operational levels through the eventual integration of OPDC's and Hydro One's local systems.

The elimination of the artificial electrical boundary between these contiguous distributors will result in operational efficiencies in various areas. Hydro One will be able to rationalize local space needs through the elimination or repurposing of duplicate facilities such as service and operating centres; more efficiently schedule operating and maintenance work and dispatch crews over a larger service area; and, more efficiently utilize work equipment (e.g., trucks and other tools), leading to lower capital replacement needs over time. The elimination of the service area boundary allows for more rational and efficient planning and development of the distribution system. All of the above provide the potential to result in operating and capital savings, both immediate and over time, which will provide long-term benefits to ratepayers relative to the status quo.

This situation is common throughout the Province and is shown in the attached map (see **Attachment 11**) depicting the current fragmented pattern of the local distribution system, with small- and medium-sized LDCs contiguous to or surrounded by Hydro One.

Hydro One's Asset Risk Assessment ("ARA") process will also assist in achieving ongoing distribution operational efficiencies. Hydro One's ARA process determines the state of Hydro One's distribution system, identifies current asset needs, and creates a line of sight to future needs, which enables an in-depth view of asset risk, and improved decision-making. The ARA incorporates field asset assessment including visual inspections and evaluation. This process allows Hydro One to assess the state of its assets, assess the risks that those assets pose and to develop appropriate plans in order to ensure reliability and service quality are met. This assessment will allow Hydro One to consider the state of the OPDC distribution system, identify current asset needs, and create a line of sight to future asset needs.

Administration

Sustained administrative efficiencies will result due to (a) the elimination of redundant activities and (b) efficiencies resulting from economies of scale.

The following stand-alone OPDC activities provide examples of what will be consolidated into Hydro One's portfolio of activities.

- Financial: financial accounting, planning, forecasting, management reporting, procurement, treasury, tax, and audit functions.
- Regulatory and legal: rate-setting applications, OEB initiatives, compliance, RRR reporting, and other regulatory reporting (e.g., CDM program administration costs, IESO Market Rules).
- Executive and governance: duplicative functions performed by OPDC senior management would be eliminated, and OPDC's Board of Directors would no longer be required.
- Human Resources: Hydro One will have savings in recruitment, training, and staff development costs, as trained and experienced OPDC staff will be available to Hydro

One to replace expected retirements and other attrition. As well, there will be a reduction in external consultants and contractor engagement between the two companies.

Hydro One's cost of borrowing is typically lower than that of local LDCs, leading to savings in financing costs over time. For example, in February 2016, Hydro One Inc. issued $500 million of 5-year debt with a 1.84% coupon rate, $500 million of 10-year debt with a 2.77% coupon rate, and $350 million of 30-year debt with a 3.91% coupon rate. The cost of long-term debt included in OPDC's rates is 6.25% compared to the 4.86% approved in Hydro One Distribution's rates. OPDC's current debt will be retired by OPDC on or prior to the closing of this acquisition. Consequently, the savings that arise from Hydro One's ability to refinance OPDC's debt upon maturation at a lower rate will lead to lower debt return on rate base, relative to the status quo.

Benefits are also expected to accrue to various agencies within the Ontario energy industry. For example, the costs to regulate and administer the sector may be reduced as this and further acquisitions are completed. The IESO, the OEB, and Ministry of Energy can achieve potential savings through reduced regulatory burden and industry oversight. Further, enhanced regional planning efficiencies may also be achieved by having fewer distribution companies planning for larger areas. For instance, capital can be deployed more efficiently than with the current fragmented approach.

Information Technology

A larger customer base resulting from the creation of a larger regional distributor leads to costs for processing systems, such as billing, customer care, human resources and financial, being spread over a larger group of customers. Consolidation of these functions is expected to result in efficiency benefits as duplicate systems are eliminated, leading to lower capital, operating and maintenance costs over time.

1 The integration of Hydro One and OPDC will allow for efficiency gains to be realized through
2 eliminating duplication in transaction-processing functions. For example, Hydro One currently
3 processes financial, human resource, information technology, and work management transactions
4 for its existing customers and staff. OPDC processes very similar transactions for its own
5 service area. This means that if the transaction proceeds, Hydro One has the opportunity to
6 eliminate these sources of duplication.
7
8 OPDC utilizes a Survelent Supervisory Control and Data Acquisition System (SCADA) which
9 monitors and controls the distribution network. Integration of OPDC into Hydro One will result
10 in the OPDC SCADA being integrated onto Hydro One's SCADA system and eliminating the
11 need for the master stations. This represents a savings of IT capital and ongoing upgrades.
12
13 *Customer Service*
14 A top-tier Customer Service function is critical to the success of Hydro One. Hydro One
15 continues to focus on improving our customer's experience. The following describes some of
16 the initiatives and ongoing customer services that Hydro One provides its customers, and which
17 would be offered to the customers of OPDC.
18
19 *Call Centre*
20 The Hydro One Call Centre is open from 7:30 a.m. to 8:00 p.m., Monday to Friday, or 4½ hours
21 per day longer than OPDC's call centre and is supported by an award-winning 24/7 Interactive
22 Voice Response ("IVR") system in addition to customer service staff. This IVR provides
23 customers the ability to self-serve, for many of their most common account and service needs,
24 such as reporting a power outage and obtaining their current account balance. This allows the
25 customer to quickly and accurately get responses to many of their inquiries and allows call centre
26 agents to focus on the more complex questions.

Outages

When an outage occurs, Hydro One customers can use other channels, such as online access via their home computer or smart-phone for information about outage details, including estimated restoration time. Customers have the option to sign up for e-mail or text outage notifications for up-to-date outage information and, as of December 2016, customers can also sign up for other digital notices, to include notifications that their eBill is ready, how much electricity they are consuming mid-month, and payment receipt alerts. All of these alerts provide Hydro One customers with the information they need to effectively manage their energy consumption and their finances. OPDC customers, currently do not have these outage notifications, but upon integration, these channels will be become available to OPDC customers as well.

Initiatives to Help Customers Manage their Bills

Hydro One is committed to delivering industry leading Conservation and Demand Management ("CDM") initiatives that help customers save on their electricity usage and bills. OPDC customers would benefit from provincial programs that are not currently included in OPDC's CDM Plan such as the Process and System Upgrade Program, Energy Manager, and Social Benchmarking as well as other Hydro One leading edge offerings including the Green Button and Air Source Heat Pump programs.

In addition to CDM, to help customers who are struggling with the cost of electricity, Hydro One typically tops-up Low Income Energy Assistance Program funding to help those least able to afford their electricity bills. This is not done by OPDC today.

When Things Don't Go As Planned…

Hydro One provides Service Guarantees to ensure that if Hydro One fails to meet commitments (e.g., misses an appointment, takes longer than 5 business days to connect a new service once all

connection requirements are met, does not return a phone call within one business day)[10], the customer's account is proactively credited $50.

Where a customer has a problem or concern with Hydro One that they do not believe was dealt with effectively, there is an escalated complaints investigation department in place (the Customer Relations Centre), which is empowered to resolve disputes. Furthermore, if a customer believes they have been unfairly treated by Hydro One and/or a customer has already passed through established complaints processes and is not satisfied with the resolution, customers can appeal to the internal Ombudsman's Office. This Office provides an independent assessment of the customer's issue and ensures that issue resolution is performed fairly.

Incremental Transaction and Integration Costs

Both parties to the transaction will have incurred some incremental costs associated with the transaction.

Hydro One's incremental transaction costs are estimated to be $3 million. These include legal, advisory, and tax costs relating to completion of the transaction, and costs associated with the necessary regulatory approvals.

Integration costs include incremental up-front costs to transfer the customers into Hydro One's customer and outage management. These costs are estimated to be between $5 million and $6 million. Hydro One is not expecting to incur any incremental ongoing costs.

All of the above incremental costs will be financed through productivity gains associated with the transaction, will not be included in Hydro One's revenue requirement, and thus will not be funded by ratepayers.

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[10] The terms and conditions for these Service Guarantees can be found at: http://www.hydroone.com/OurCommitment/Pages/Exceptions.aspx

Financial Viability/Premium/Financing

As contemplated in the share purchase agreement, Hydro One Inc. will pay $41.3 million for the acquisition of OPDC. This comprises a cash payment of approximately $26.4 million for the shares and the assumption of short and long-term debt of approximately $14.9 million. The purchase price represents the commercial value of the underlying assets established through negotiations with an arms length third party. The 2015 net book value of OPDC's assets is $22.5 million.

The premium paid over the asset's book value will not have a material impact on Hydro One Inc.'s financial viability. This transaction price accounts for less than 1% of Hydro One Distribution's net fixed assets. In addition, the premium paid will not be included in Hydro One's revenue requirement and thus will not be funded by ratepayers. Copies of OPDC's, Hydro One Distribution and Hydro One Inc.'s Financial Statements for 2014 and 2015 are provided in **Attachments 12 to 17**.

HOI will initially finance the proposed transaction through cash or its short-term commercial paper program, which is operational and fully backed by a syndicated bank line of credit maturing June, 2021. Long-term financing will be through its Medium-Term Note program, which is fully operational and valid until January 2018, and planned to be renewed thereafter.

3.0 OTHER RELATED MATTERS

Regulatory Assets and Rate Riders

OPDC is requesting a rate rider to reduce the residential and general service rate classes' base distribution delivery rates that are effective May 1, 2016, by 1% for years one through five of the deferral period. All other OPDC rate riders will continue as per their existing rate schedules until expiry.

The OPDC regulatory assets currently approved by the OEB will continue to be tracked in their respective accounts, and disposition will be sought at a future date. Also, Hydro One requests approval for a regulatory account to track costs associated with the ESM, as described in **Exhibit A, Tab 3, Schedule 1**.

Incremental Capital Module

To encourage consolidation, the Handbook has now explicitly extended the availability of an ICM, for any prudent discrete capital projects, for consolidating distributors that are on either Price Cap Incentive Regulation ("PCIR") or Annual IR Index. Currently, OPDC rates are set in accordance with PCIR.

Hydro One understands, from the Handbook, that an ICM will be made available for the Orillia business segment should the need arise.

US GAAP

OPDC's financial statements are currently prepared under IFRS. Hydro One Distribution received OEB approval to utilize US Generally Accepted Accounting Principles (**"US GAAP"**) as its approved framework for rate setting, regulatory accounting and regulatory reporting in the Decision with Reasons in EB-2011-0399 (issued on March 23, 2012). In addition, in the Hydro One Norfolk MAAD (EB-2013-0187/196/198) Decision and Order, the Board decided that using US GAAP methodology in accounting for Norfolk Power Distribution Inc. (the acquired utility) will be more efficient than continuing to use Modified IFRS. Since that Decision, the OEB has also approved the use of US GAAP for Haldimand County Hydro Inc. (EB-2014-0244) and Woodstock Hydro Services Inc. (EB-2014-0213) in their MAAD applications.

Hydro One requests similar approval to utilize US GAAP for accounting purposes in relation to OPDC. Approval to use US GAAP for OPDC will simplify any future rate integration, will avoid incremental costs or productivity losses by simplifying processes and avoiding the need for workarounds, and will facilitate Hydro One Inc.'s consolidated reporting for securities filing purposes (including future U.S. Securities and Exchange Commission), thus avoiding incremental costs and/or reduced productivity. By using one uniform standard of reporting, Hydro One seeks to achieve integration and scale efficiencies. Given the relative small size of the OPDC operations (when compared to Hydro One), Hydro One believes it would be inefficient and costly to maintain two different accounting regimes for divisions within Hydro One.

Compliance Matters

Pending approval of this transaction and after notification to the Board that integration is completed, OPDC's distribution system and Rate Order will be transferred to Hydro One, and Hydro One's distribution licence will be amended to include the OPDC service territory. The customers, assets, systems, processes and operations of OPDC will be fully integrated into Hydro One's business activities.

Hydro One confirms that it is materially in compliance with its regulatory requirements, subject to any approved regulatory exemptions. The list of specific code requirements from which Hydro One has been exempted can be found in Schedule 3 of Hydro One's Electricity Distribution Licence.

To the best of OPDC's knowledge, it is in compliance with all relevant licence and code requirements per its Electricity Distribution Licence. It is expected that following the approval and completion of the transaction and after integration of OPDC's distribution business activities

into those of Hydro One, Hydro One will continue to be materially compliant with all applicable Legislation, Regulations, Market Rules, other Licence Conditions and Codes.

Hydro One's compliance policy will continue to require that confirmed instances of non-compliance be disclosed and mitigated as necessary including applications for exemptions from such requirements, if necessary. Any potential instances of non-compliance associated with OPDC's distribution business activities will be addressed during the integration process.

During the period after closing of the transaction and prior to full integration, service level agreements in compliance with the OEB's *Affiliate Relationships Code for Electricity Distributors and Transmitters* will be drafted between OPDC and Hydro One affiliates.

SUMMARY

For the reasons addressed in the preceding sections, both qualitative and quantitative savings and efficiencies are expected to result from this transaction. Overall, Hydro One's analysis shows the ongoing synergies will accrue as a result of this transaction, benefiting ratepayers of both utilities. These attributes allow Hydro One and OPDC to conclude that the transaction will not cause harm to ratepayers, and indeed will provide benefits to all ratepayers in the long term. Moreover, this application embodies the current regulatory policies and principles of the Board in pursuing the objectives established by section 1 of the Act.

EARNING SHARING MECHANISM

1.0 INTRODUCTION

Consistent with the Amended Report, Hydro One is proposing to implement an ESM to operate during the term of the extended deferred rebasing period[1] (i.e., for years six to ten beyond the initial five-year deferral period). The ESM will ensure that customers share in the increased benefits from consolidation during that period.

The Handbook provides further details on the Board's expectations of an ESM, and in some instances, references details that would apply specifically to a transaction, including these key aspects:

- Consolidating entities that propose to defer rebasing beyond five years must implement an ESM for the period beyond five years. The ESM is designed to protect customers and ensure that they share in any increased benefits from consolidation during the deferred rebasing period;
- Excess earnings are shared with consumers on a 50:50 basis for all earnings that are more than 300 basis points above the consolidated entity's annual ROE;
- Earnings will be assessed each year once audited financial statements are available, and excess earnings beyond 300 basis points will be shared with customers annually;
- An ESM as set out in the 2015 Report may not achieve the intended objective of customer protection for all types of consolidation proposals. For these cases, applicants are invited to propose an ESM that better achieves the objective of protecting customer interests during the deferred rebasing period[2].

[1] EB-2014-0138, Amended Report, page 6
[2] Handbook, Pages 16-17

With these factors in mind, Hydro One is proposing an ESM that simplifies its administration, thereby keeping costs low and providing a guaranteed cost reduction to ratepayers, while adhering to the Board's principles outlined in its recent policies and decisions on consolidation applications.

2.0 PROPOSED ESM

Hydro One's ESM will guarantee a cumulative $3.4 million sharing of earnings with former OPDC customers as a result of the implementation of the ESM in years six to ten.

The following are the key aspects of Hydro One's proposal, each of which will be discussed in detail below:

- *Term and Eligibility* - Hydro One is proposing to implement an ESM in years six through ten of the deferred rebasing period. Excess earnings above 300 basis points on the allowed ROE in that period will be shared 50:50 with customers of the former OPDC.
- *Mechanics of the ESM* - The ESM has been calculated on forecast OM&A and capital costs based upon Table 1 in the evidence, provided at **Exhibit A, Tab 2, Schedule 1**.
- *Ratepayer Refund* - The projected over-earning amounts shared with customers will be recorded in a regulatory account, interest-improved, and used to offset future rate mitigation that might be required after the deferral period.

2.1 Term and Eligibility

Hydro One is proposing to implement an ESM in years six through ten of the deferred rebasing period, consistent with the Amended Report and the Handbook. The ESM will employ a 50:50 sharing of earnings 300 basis points over OPDC's current-approved ROE. The excess earnings will be shared with customers, who at the time of disposition are customers of Hydro One in what it currently OPDC service territory. The sharing of the earnings solely with OPDC's customers is consistent with the Board's direction in the Handbook, where the Board suggested

that "a large distributor that acquires a small distributor may demonstrate the objective of consumer protection by proposing an ESM where excess earnings will accrue only to the benefits of the customers of the acquired distributor"[3]. Also consistent with the comments delivered by the Board in Hydro One's WHSI MAAD Decision[4], the over-earnings will be calculated on the operations of the acquired entity opposed to the consolidated new entity's earnings.

2.2 Details of the Proposed ESM

An essential aspect of consolidation is to attain as many synergies as possible to the ultimate benefit of all ratepayers of the consolidating entities. Elimination of redundant financial records, external audits and reporting is a key element to lowering cost structures. Hydro One is on record that it does not intend to provide separate financial statements for any of the acquired utilities. This was discussed during the Woodstock MAAD oral hearing[5]. To do so would not only decrease forecast synergies but would also add new one-time and ongoing costs to set up business units in Hydro One's financial systems, thus diminishing costs savings that would otherwise be available to ratepayers.

Hydro One proposes to fully integrate OPDC into its Distribution business within 18 months of the close of the transaction. Once complete, the companies will be fully integrated, both operationally and financially, including having one set of financial records. Since separate financial statements will no longer exist for OPDC, Hydro One will not be in a position to report the earnings of the acquired distributor. Instead, Hydro One proposes to calculate excess earnings in years six to ten based upon forecast costs as presented in Table 1.

Hydro One proposes to commit in this Application to a pre-calculated earning sharing that will guarantee a defined benefit to ratepayers of OPDC as set out in Section 2.3 below. An ESM

[3] Handbook, Page 16
[4] EB-2014-0213, Page 17
[5] EB-2014-0213, Transcript, Day 2, page 48

using forecast OM&A and capital expenditures has two benefits. Firstly, it reduces both ongoing and one-time costs to serve the customers in the Orillia business segment, maximizing their share of excess earnings. The tracking of actual costs would substantially reduce the savings available from consolidation activities. Secondly, it provides Hydro One with a strong incentive to achieve the forecast efficiency savings, which are significant as a percent of the existing OM&A and rate base of OPDC. Committing to a pre-calculated refund, regardless of actual costs, drives Hydro One to seek as many efficiencies as possible. Once achieved, this will result in lower ongoing cost structures, to the benefit of all Hydro One ratepayers.

A significant benefit to OPDC customers is that the OM&A costs used in the model are *incremental* costs only, which do not include corporate overheads. Including corporate overheads would reduce net income, thereby reducing shared earnings. The OM&A forecast used in the proposed ESM reflects an aggressive estimate of savings associated with Hydro One's position as a natural consolidator in the province, and relies on Hydro One's plans to fully integrate OPDC's operations with its own. The forecast OM&A costs are about one-third of OPDC's status quo OM&A forecast, representing a two thirds savings of existing OM&A.

The section below describes the key components used in the Hydro One ESM model.

1

Table 5: ESM Components

Rate Base
▪ OPDC's Board-approved rate base[6] was adjusted for net in-service additions that have accumulated since its last rate rebasing to calculate rate base at the closing of the transaction. ▪ Additions to rate base during the deferred rebasing period are the forecast in-service capital additions provided in Table 1 plus working capital.
Revenue
▪ OPDC's 2016 approved distribution rates are adjusted by the PCIR mechanism for the extended deferral period: The inflation rate is sourced from the IHS Global Insights June 2016 inflation forecast for Ontario. OPDC's productivity factor is 0.3%. ▪ OPDC's distribution revenues are calculated using this rate multiplied by the forecast load and customer profiles of the OPDC service area.
OM&A
▪ OM&A costs during the deferred rebasing period align with the forecast provided in Table 1. Note: These are incremental costs and do not include any overhead allocations. ▪ Hydro One is assuming all operational risks during the 10-year deferred rebasing period. These risks include: ▪ The risk that the OM&A forecast is not achieved; ▪ The risk that assets are not in the condition anticipated; ▪ The risk that the anticipated load and customer profile growth does not materialize. Hydro One will also need to manage, over a 10-year period, any changes to labour (collective agreements, benefits, pension) and material costs, the impact of innovation and technology on operations, and any political and regulatory changes. Irrespective of the actual results, OPDC customers will receive the ESM sharing benefit. As a result of the risks assumed by Hydro One in committing to the guaranteed ESM, a 20% risk factor has been applied to the OM&A forecast. This means that prior to calculating the forecast savings from the transaction that would be shared with customers, Hydro One has multiplied the forecast OM&A costs by 1.20.
Depreciation
▪ The acquired assets are depreciated based on their remaining useful life as determined by Hydro One. The assets purchased post-transaction in Table 1 are depreciated in accordance with Hydro One Distribution's approved depreciation rates.
Financing Costs
▪ The cost of debt is that embedded in OPDC's current approved rates: ▪ Long-term debt is 6.25%. ▪ Short-term debt is 1.33%.
Taxes
▪ Taxes are calculated using the existing provincial and federal tax rates, totaling 26.5%.
Return on Equity
▪ The ROE used to establish the 300 basis point differential is OPDC's current-approved ROE of 9.85%[7].

2

[6] EB-2009-0273, Draft Rate Order
[7] EB-2009-0273

2.3 ESM Results

Table 6 below provides Hydro One's proposed refund to customers using the ESM as above-described. Hydro One believes that the proposed ESM, based upon forecast cost savings, benefits and provides a fair return to ratepayers both during the deferred rebasing period and beyond. OPDC ratepayers receive a guaranteed sharing of $3.4 million earned during the ESM period. Hydro One will have a strong incentive to ensure that these savings are achieved so that its ability to recover acquisition costs will not be eroded. The resultant synergy savings will then form the basis of future revenue requirements, which will benefit all of Hydro One customers through lower cost structures. Pursuing the more conventional ESM alternative of tracking costs separately and maintaining separate financial records would increase both OM&A and capital costs, which would ultimately erode the synergies of this transaction, thereby reducing the ESM share that will be available to the customers of the former OPDC.

1 **Table 6: Earning Sharing Mechanism Sharing - Years 6 to 10**

2 **($000's)**

Deferral Period Year	**6**	**7**	**8**	**9**	**10**
Calendar Year	**2022**	**2023**	**2024**	**2025**	**2026**
Rate Base	40,231	41,869	43,576	45,371	47,242
Equity Component of Rate Base	16,092	16,748	17,430	18,148	18,897
Revenue	8,600	8,792	8,996	9,199	9,410
OM&A[8]	2,090	2,137	2,186	2,237	2,288
Depreciation	1,036	1,091	1,147	1,211	1,278
Interest	1,429	1,488	1,548	1,612	1,679
Tax	849	865	881	893	905
Net Profit After Tax	**$3,196**	**$3,211**	**$3,234**	**$3,246**	**$3,260**
Achieved ROE (%)	19.86%	19.18%	18.55%	17.89%	17.25%
Less: Approved ROE% for OPDI	(9.85%)	(9.85%)	(9.85%)	(9.85%)	(9.85%)
ROE% above Approved ROE%	10.01%	9.33%	8.70%	8.04%	7.40%
Less: 300 Basis Points Threshold	(3.00%)	(3.00%)	(3.00%)	(3.00%)	(3.00%)
Total Over-Earnings (%)	7.01%	6.33%	5.70%	5.04%	4.40%
Total Over-Earnings	$1,128	$1,059	$994	$914	$832
50% of Overearnings Shared with to OPDC customers	$564	$530	$497	$457	$416
Tax Effected Earnings Sharing (26.5%)	$767	$721	$676	$622	$566
Cumulative Tax Effected Earnings Sharing (Years 6 to 10)					**$3,352**

3

[8] Includes risk factor adjustment

2.4 Ratepayer Refund

Hydro One will record the guaranteed refund due to ratepayers in a deferral account. These amounts will be interest-improved, in accordance with the OEB's prescribed interest rates. Hydro One will accrue the balance in this account until the end of the extended deferred rebasing period. At this time, OPDC customers are expected to be transitioned to a new Hydro One rate class. In year ten of the deferral period, Hydro One will apply to the Board to dispose of the balance in this account in one of the following manners: (1) Hydro One will apply these funds to offset the cost of any rate mitigation that may be required to transition these customers to their new rates. That application will recommend the duration of the disposition period; (2) If the total balance in the deferral account is not completely required to fund rate mitigation, then Hydro One will offer rate mitigation for a defined period of time, and any remaining balance will be disposed of via a one-time credit; or (3) If no rate mitigation is required, the balance of the deferral account will be completely refunded to the customers by a one-time credit. This method of disposition ensures that there is no cross-subsidization between the legacy Hydro One customers and OPDC customers[9].

OPDC last had its rates rebased in 2010. If this application is approved, the next rebasing of distribution rates which includes costs for OPDC would be 2027. Though there will be significant savings as a result of this consolidation, the 17-year gap between rebasing may result in a disparity between cost structures and rates. Regardless of the rate class to which these customers will be transitioned, rate mitigation may be required. The disposition of the accumulated earnings in years 11 and forward will help to offset any required rate mitigation. It is for this reason that Hydro One proposes recording the ESM refund amount in a deferral account for future disposition.

[9] Hydro One at a later date will file a separate application to request the establishment of a regulatory account to track these costs.

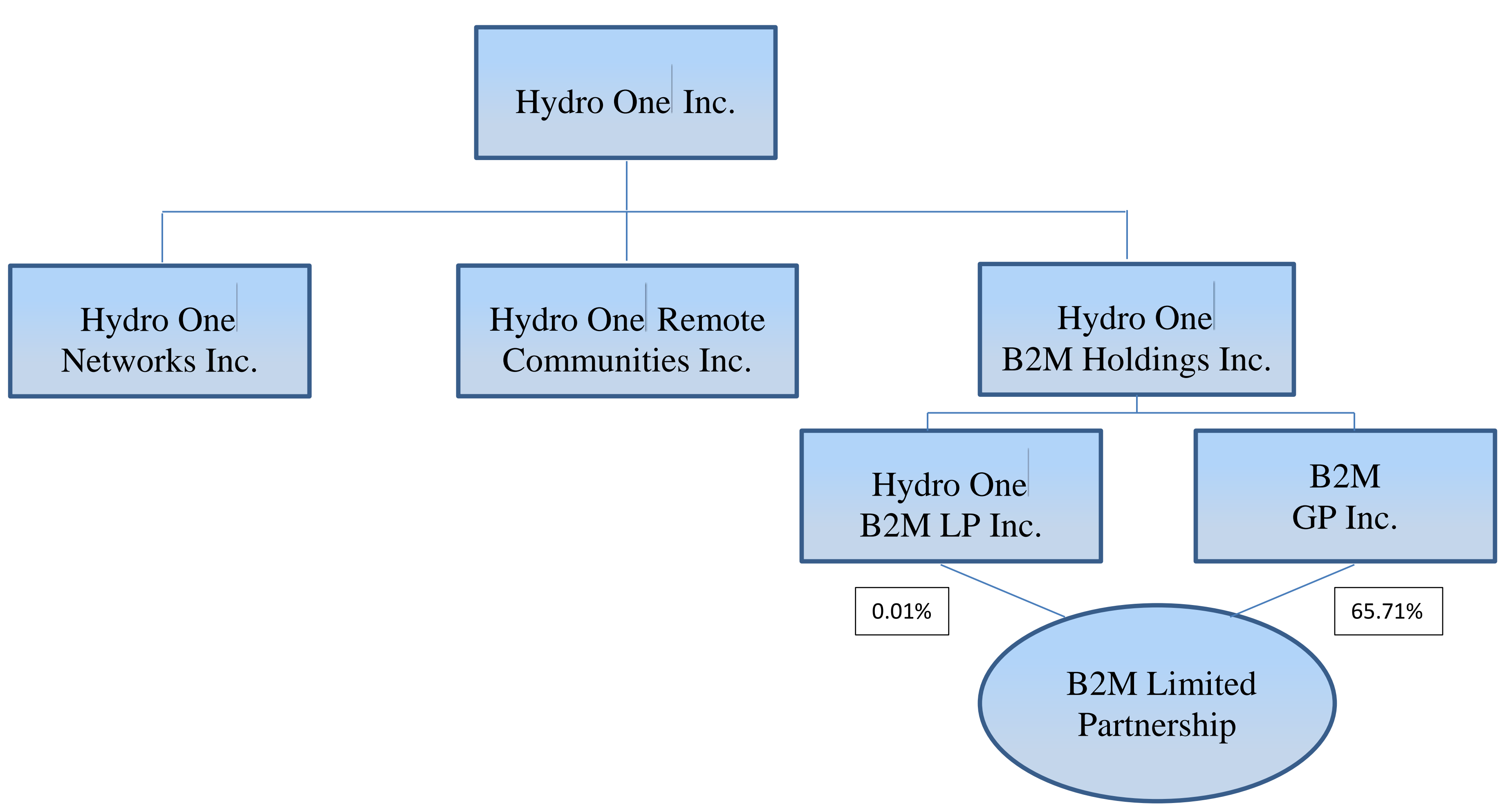
2.5 ESM Summary

Hydro One believes that the proposed ESM meets the objectives of the Board's policy. The guaranteed refund to customers not only accommodates the circumstances of the transaction; it also provides an incentive for Hydro One to derive increased efficiencies and provides a mechanism to help mitigate rates at the next rebasing. This allows the shareholder to continue to recover transaction costs, while ensuring that customers of the former OPDC are protected from the risk of unrealized synergies, and benefit from the efficiencies and savings that the new distributor expects to achieve from consolidation.

The proposed refund to customers is a significant amount: Hydro One is guaranteeing a $3.4 million refund to the former customers of OPDC. This equates to approximately 45% of OPDC's current Board-approved revenue requirement[10].

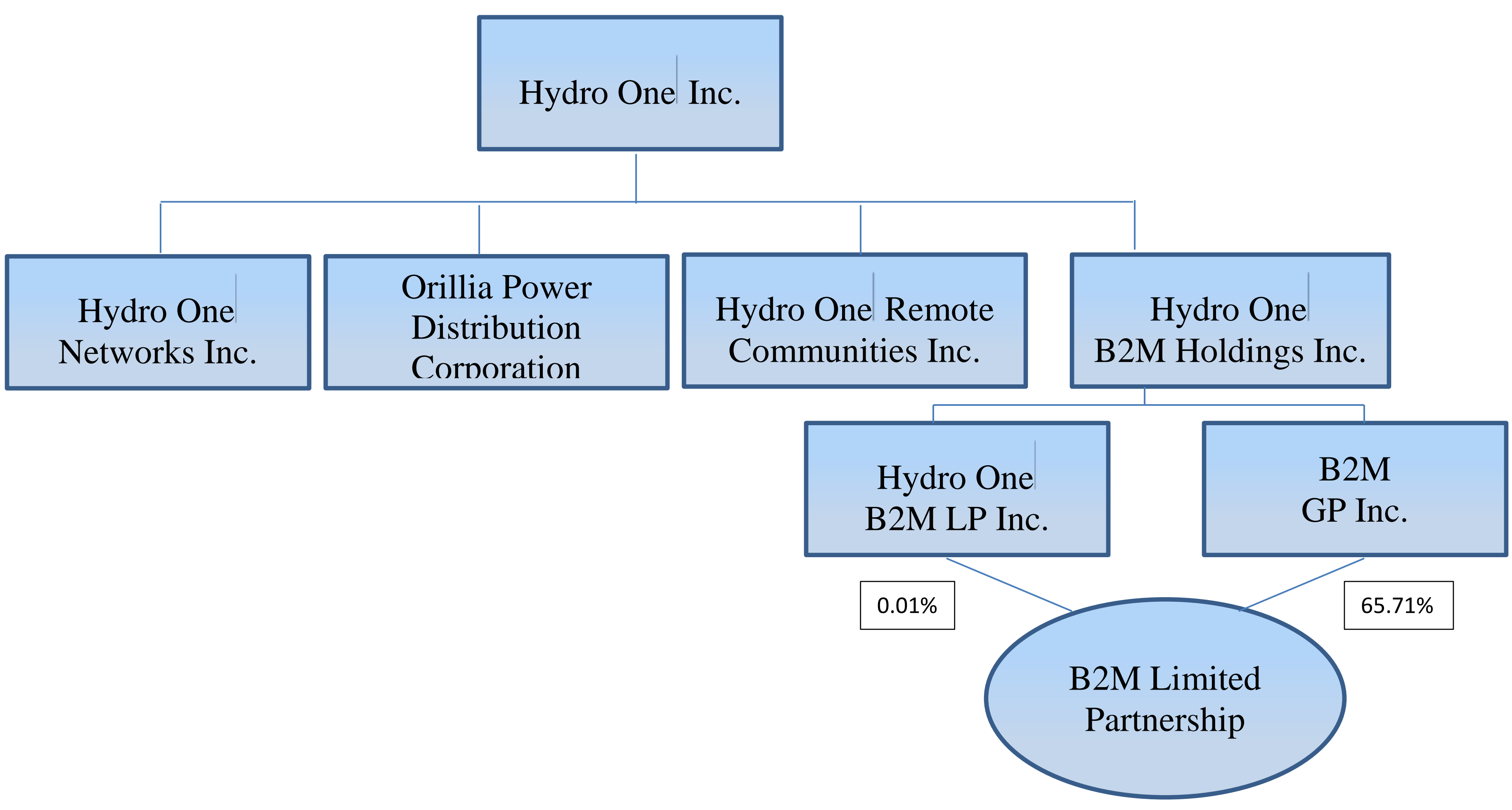
[10] EB-2009-0273

Hydro One Inc. Corporate Structure (Pre-Acquisition)*



* This diagram represents Hydro One's corporate structure prior to close of the OPDC transaction.

Hydro One Inc. Corporate Structure (Post-Acquisition)*



* This diagram represents Hydro One's corporate structure after the close of the OPDC transaction.

Hydro One Customer Counts

	Number of Customers
Residential	1,174,775
General Service < 50kW	110,868
General Service >= 50kW	8,260
Large User	0
Sub-Transmission	486
Total	**1,294,389**

ORILLIA POWER CORPORATION

City of Orillia
(Sole Shareholder)

Orillia Power Corporation
(100% Municipally owned - Holding Company)

Orillia Power Distribution Corporation
100% owned Sub. - Local Distribution Corporation

Orillia Power Generation Corporation
100% owned Sub. – Generation of Green Energy

Affiliates involved in green energy production either 100% or 50% owned by OPGC

Updated: September 16, 2016

OPDC Customer Counts

	Number of Customers
Residential	11,916
General Service < 50kW	1,361
General Service >= 50kW	168
Large User	-
Sub-Transmission	-
Total	**13,445**

EXECUTION VERSION

THE CORPORATION OF THE CITY OF ORILLIA

- and -

ORILLIA POWER CORPORATION

- and -

HYDRO ONE INC.

SHARE PURCHASE AGREEMENT

Dated the 15th day of August, 2016

EXECUTION VERSION

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SHARE PURCHASE AGREEMENT

THIS AGREEMENT made the 15th day of August, 2016 (the "**Effective Date**").

B E T W E E N:

THE CORPORATION OF THE CITY OF ORILLIA, a municipal corporation under the laws of Ontario, (the "**City**")

- and -

ORILLIA POWER CORPORATION, a corporation incorporated under the laws of Ontario (the "**Vendor**")

- and -

HYDRO ONE INC., a corporation incorporated under the laws of Ontario (the "**Purchaser**")

Recitals

1. Orillia Power Distribution Corporation (the "**Corporation**") is a local electricity distribution company incorporated under the *Business Corporations Act* (Ontario) that distributes electricity within the boundaries of the City of Orillia; and

2. The Vendor and the City wish to sell to the Purchaser, and the Purchaser wishes to purchase from the Vendor, all of the issued and outstanding shares of the Corporation, on and subject to the terms and conditions set forth herein.

THIS AGREEMENT WITNESSES THAT in consideration of the respective covenants, agreements, representations and warranties of the Parties herein contained and for other good and valuable consideration (the receipt and sufficiency of which are acknowledged by each Party), the Parties covenant and agree as follows.

ARTICLE I
INTERPRETATION

1.1 **Defined Terms**. In this Agreement, including the recitals, and schedules hereto, unless the context otherwise specifies or requires, the following terms shall have the respective meanings specified or referred to below and grammatical variations of such terms shall have corresponding meanings:

(a) "**Account 1576**" has the meaning ascribed thereto in Section 6.7.

(b) "**Advisory Committee**" has the meaning ascribed thereto in Section 6.3.

(c) "**Affiliate**" has the meaning ascribed thereto in the OBCA.

(d) "**Agreement**" means this share purchase agreement, including all schedules attached hereto, as amended, supplemented, restated and replaced from time to time in accordance with its provisions.

(e) "**Applicable Law**" means any and all applicable laws, including Environmental Laws, common law, statutes, codes, licensing requirements, directives, rules, regulations, protocols, policies, by laws, guidelines, orders, injunctions, rulings, awards, judgments or decrees or any requirement or decision or agreement with or by any Government Authority, including without limitation, the OEB.

(f) "**Auditor**" means BDO Canada LLP.

(g) "**Business**" means, the electricity distribution business carried on by the Corporation, in the City of Orillia.

(h) "**Business Day**" means a day other than a Saturday, Sunday, statutory holiday in Ontario or any other day on which the principal chartered banks located in the City of Toronto are not open for business during normal banking hours.

(i) "**Change in Applicable Law**" means:

(i) the enactment, introduction or tabling of any Canadian federal or provincial legislation (whether by statute, regulation, order in council, notice of ways and means motion or otherwise);

(ii) a ruling, order or decision of the OEB, including a ruling, order or decision of the OEB, relating to an electricity distribution utility other than the Corporation;

(iii) the issuance, modification or revision of the OEB's existing Electricity Distribution Rate Handbook, or the issuance of any rule, procedure, code, policy or directive by the OEB; and

(iv) a directive, guideline or policy statement of a Governmental Authority;

(j) "**City**" means the Corporation of the City of Orillia.

(k) "**City Property**" means the Corporation's property listed in Schedule 6.4.

(l) "**Claim**" means any demand, action, investigation, inquiry, suit, proceeding, claim, assessment, judgment or settlement or compromise relating thereto and includes any act, omission or state of fact actionable under or contrary to Applicable Law (including for clarity and without limitation, in contract, tort, or equity).

(m) "**Closing**" means completion of the Transactions contemplated herein on the Closing Date and in accordance with the provisions of this Agreement.

(n) "**Closing Date**" means the first date which is the first Business Day of a month and at least ninety (90) days following the date that the Required Approval has been obtained or such earlier or later date as may be agreed to by the Parties in writing. Notwithstanding any other provision of this Agreement, Closing is intended to occur at the very beginning the day which follows the financial period end.

(o) "**Closing Date Financial Statements**" means audited financial statements for the Corporation for the fiscal period ended on the Closing Date, prepared in accordance with GAAP consistently applied on the same basis as the Initial Financial Statements, and consisting of a balance sheet as of such date and statements of operations, retained earnings, and cash flow for such period, together with notes thereto as at such date of the Corporation's auditors, addressed to the Vendor and the Corporation, the Purchaser and the Guarantor.

(p) "**Closing Date Long Term Debt**" means the amount of Long Term Debt based on the Closing Date Financial Statements.

(q) **Closing Date NFA**" means the amount of NFA in the Closing Date Financial Statements.

(r) "**Closing Date Regulatory Accounts**" means the amount of the Net Regulatory Accounts based on the Closing Date Financial Statements.

(s) "**Closing Date Working Capital**" means the amount of Working Capital in the Closing Date Financial Statements.

(t) "**Collective Agreement**" has the meaning ascribed thereto in Section 3.1(q)(i).

(u) "**Common Shares**" means the common shares in the share capital of the Corporation.

(v) "**Confidential Disclosure Schedule**" means that confidential disclosure schedule dated as of the Effective Date which the Vendor delivered to the Purchaser contemporaneous with the execution of this Agreement.

(w) "**Confidential Information**" has the meaning ascribed thereto in Subsection 6.10(b)(i).

(x) "**Confidentiality Agreement**" means the confidentiality provisions in the Exclusivity Agreement between the Corporation, and the Purchaser dated September 22, 2015, as amended from time to time.

(y) "**Corporation**" means Orillia Power Distribution Corporation.

(z) "**Contract**" means any agreement, indenture, contract, lease, deed of trust, licence, option, instrument or other commitment, whether written or oral.

(aa) "**CTA**" means the *Corporations Tax Act* (Ontario) or the Taxation Act, 2007 (Ontario) and any regulation made thereunder.

(bb) “**Current Rates**” means those Rates specified in the Rate Order, and as presented under the column entitled “2016” in Schedule 6.6 of this Agreement.

(cc) “**Data Room**” means the data site located at https://extranet.blg.com/clients/Orillia/Pages/Collaboration/BLGClientExtranetDocuments.aspx?lang=1033 as at August 3, 2016.

(dd) “**Deductible**” has the meaning ascribed thereto in Section 12.7(a)(i).

(ee) “**Deposit**” has the meaning ascribed thereto in Section 2.3(a).

(ff) “**Direct Claim**” has the meaning ascribed thereto in Section 12.3.

(gg) “**EA**” means the *Electricity Act*, 1998 (Ontario), as amended from time to time.

(hh) “**Easements**” means the right in perpetuity to use, traverse, enjoy or have access to, over, in or under any real property, and includes those easements that are registered, unregistered or granted by operation of Applicable Law.

(ii) “**Effective Date**” means the date of this Agreement as first stated above.

(jj) “**Employee Fact Sheet**” has the meaning ascribed thereto in Section 3.1(r)(i).

(kk) “**Employee Plans**” has the meaning attributed to that term in Section 3.1(p)(i).

(ll) “**Employees**” has the meaning ascribed thereto in Section 3.1(r)(i).

(mm) “**Encumbrance**” means any encumbrance, lien, charge, hypothec, pledge, mortgage, title retention agreement, security interest of any nature, adverse claim, exception, reservation, easement, right of occupation, any matter capable of registration against title, option, right of pre-emption, privilege or any Contract to create any of the foregoing.

(nn) “**Environment**” means the environment or natural environment as defined in any Environmental Law and includes air, surface water, ground water, land surface, soil, sub surface strata and sewer system.

(oo) “**Environmental Approvals**” means all permits, certificates, licences, authorizations, consents, registrations, directions, instructions, waste generation numbers or approvals required pursuant to Environmental Laws with respect to Real Property or the operation of the Corporation or its Business.

(pp) “**Environmental Laws**” means all Applicable Law relating in whole or in part to the protection of the Environment or to public health and safety, and includes those relating to the manufacture, processing, distribution, use, treatment, storage, disposal, discharge, transportation or handling of Hazardous Substances.

(qq) "**ETA**" means Part IX of the *Excise Tax Act* (Canada) and any regulation made thereunder.

(rr) "**Five Year Fixed Payment Amount**" means $270,000.

(ss) "**Fixed Assets**" means fixed assets, furniture, furnishings, parts, tools, personal property fixtures, plants, buildings, structures, erections, improvements, appurtenances, machinery, equipment, computer hardware and software, substations, transformers, vaults, distribution lines, transmission lines, conduits, ducts, pipes, wires, rods, cables, fibre optic strands, devices, appliances, material, poles, pipelines, fittings and any other similar or related item of the Business.

(tt) "**GAAP**" means the generally-accepted accounting principles (including the methods of application of such principles and, as applicable, International Financial Reporting Standards) accepted or recommended by the Canadian Institute of Chartered Accountants which are applicable in Canada as at the date on which any calculation made hereunder is to be effective.

(uu) "**Governmental Authority**" means any domestic government, whether federal, provincial, territorial, local, regional, municipal, or other political jurisdiction, and any agency, authority, instrumentality, court, tribunal, board, commission, bureau, arbitrator, arbitration tribunal or other tribunal, or any quasi-governmental or other entity, insofar as it exercises a legislative, judicial, regulatory, administrative, expropriation or taxing power or function of or pertaining to government including the OEB.

(vv) "**Hazardous Substances**" means any hazardous substance or any pollutant or contaminant, toxic or dangerous waste, substance, or material as defined in or regulated by any Environmental Law including, without limitation, friable asbestos and poly chlorinated biphenyls.

(ww) "**HONI**" means Hydro One Networks Inc.

(xx) "**HST**" means all taxes payable under Part IX of the ETA (including where applicable both the federal and provincial portion of those taxes) or under any provincial legislation imposing a similar value added or multi staged tax.

(yy) "**IFRS**" means International Financial Reporting Standards.

(zz) "**Indemnified Party**" has the meaning ascribed thereto in Section 12.3.

(aaa) "**Indemnifying Party**" has the meaning ascribed thereto in Section 12.3.

(bbb) "**Independent Auditor**" has the meaning ascribed thereto in Section 2.4(d).

(ccc) "**Initial Financial Statements**" means the audited financial statements of the Corporation as at December 31, 2015 prepared in accordance with IFRS.

(ddd) "**Initial Long Term Debt**" means the Long Term Debt shown in the Initial Financial Statements.

(eee) "**Initial NFA**" means the NFA in the Initial Financial Statements.

(fff) "**Initial Regulatory Accounts**" means the Net Regulatory Accounts shown in the Initial Financial Statements.

(ggg) "**Initial Working Capital**" means the Working Capital calculated based on the Initial Financial Statements.

(hhh) "**Leased Property**" has the meaning ascribed thereto in Subsection 3.1(l)(i).

(iii) "**Licences**" has the meaning ascribed thereto in Subsection 3.1(z).

(jjj) "**Long Term Debt**" means long term debt as shown in the Corporation's financial statements. For greater certainty, Long Term Debt excludes the current portion of long term debt.

(kkk) "**Long Term Debt Calculation**" has the meaning ascribed thereto in subsection 2.4(a)(iii).

(lll) "**Losses**" means any and all loss, liability, damage, cost, expense (including, reasonable legal fees, accountants', investigators', engineers' and consultants' fees and expenses, interest, penalties and amounts paid in settlements), charge, fine, penalty or assessment, suffered or incurred by the Person seeking indemnification, directly resulting from or arising out of any Claim, including the costs and expenses of any action, suit, proceeding, investigation, inquiry, arbitration award, grievance, demand, assessment, judgment, settlement or compromise relating thereto, including without limitation a gross up to account for any tax payable or a reduction in the "cost amount", as defined in subsection 248(1) of the Tax Act of any property owned by the Purchaser or the Corporation or a successor entity in the taxation year as a result of receiving the indemnification amount but: (i) excluding any contingent liability until it becomes actual; (ii) reduced by any net Tax benefit; (iii) reduced by any recovery, settlement or otherwise under or pursuant to any insurance coverage; or pursuant to any claim, recovery, settlement or payment by or against any other Persons; and (iv) excluding any incidental, indirect, special or consequential loss, liability or damage and loss of profits other than damages of a Third Party in respect of a Third Party Claim.

(mmm) "**Material Adverse Effect**" means any change or effect that has a material adverse effect on the Property or obligations and liabilities of the Corporation or the operations or results of operations of the Business after taking into account any insurance which may be available with respect to such a change or effect. For greater clarity, a Material Adverse Effect does not include a Change in Law.

(nnn) "**Material Contract**" means any Contract for the supply of goods or services which has a value exceeding Fifty Thousand Dollars ($50,000.00) in annual payments excluding any collective bargaining agreements, and shall be deemed to include any

software licence other than of the shrink-wrap or click-wrap variety and every Contract in relation to Employee Plans, as further described in Schedule 3.1(o).

(ooo) "**Municipality**" means The Corporation of the City of Orillia.

(ppp) "**NFA**" means the aggregate value of Corporation's property, plant, and equipment net of deferred revenue as provided in its financial statements but shall include intangible assets only to the extent recoverable in rates.

(qqq) "**Negative Rate Rider**" has the meaning ascribed thereto in Section 6.6(a)(i) of this Agreement.

(rrr) "**Net Regulatory Accounts**" means the aggregate value of the regulatory deferral account debit balances net the regulatory deferral account credit balances as provided in the Corporation's financial statements.

(sss) "**NFA Calculation**" has the meaning ascribed thereto in Section 2.4(a)(ii).

(ttt) "**NFA Index**" shall be equal to 1.1.

(uuu) "**OBCA**" means the *Business Corporations Act* (Ontario), as in effect on the date hereof.

(vvv) "**OEB**" means the Ontario Energy Board and its successors.

(www) "**OEB Act**" means the *Ontario Energy Board Act*, 1998, as in effect on the date hereof.

(xxx) "**OEB Approval**" means the approval of the OEB to the Transactions contemplated herein pursuant to the OEB Act.

(yyy) "**OEB Percentage Rate Reduction**" means the percentage by which the arithmetic average of Reduced Rates is lower than the arithmetic average of Current Rates.

(zzz) "**OMERS Plan**" means the Ontario Municipal Employees Retirement System Primary Pension Plan.

(aaaa) "**Partial Rate Rider**" means the approved negative rate rider that results in an average reduction in Current Rates of less than one percent (1%) across all Rate Classes.

(bbbb) "**Party**" means a party to this Agreement, and "**Parties**" means both of them.

(cccc) "**Permitted Encumbrance**" means the encumbrances listed in Schedule 1.1(zzz).

(dddd) "**Person**" means any individual, partnership, limited partnership, joint venture, syndicate, sole proprietorship, company or corporation with or without share capital, unincorporated association, trust, trustee, executor, administrator or other legal personal representative, regulatory body or agency, government or governmental agency, authority or entity however designated or constituted.

(eeee) "**PILs**" means payment in lieu of corporate taxes required to be made under Section 93 of the EA.

(ffff) "**Pre-Closing Tax Period**" means any Tax period ending on or before the day prior to the Closing Date, and, with respect to a Straddle Period, the portion of such Tax period ending on the day prior to the Closing Date.

(gggg) "**Property**" means the property and assets used by the Corporation to conduct its Business, including without limitation, the Real Property, the Leased Property, the Easements, the Intellectual Property and Fixed Assets.

(hhhh) "**Property Taxes**" has the meaning ascribed thereto in Section 8.4.

(iiii) "**Purchase Price**" has the meaning ascribed thereto in Section 2.2.

(jjjj) "**Purchased Shares**" has the meaning ascribed thereto in Section 2.1.

(kkkk) "**Purchaser**" means Hydro One Inc. a corporation incorporated under the laws of Ontario.

(llll) "**Purchaser Indemnified Parties**" has the meaning ascribed thereto in Section 12.1.

(mmmm) "**Purchaser's Objection**" has the meaning ascribed thereto in Section 2.4(b).

(nnnn) "**Rate**" or "**Rates**" means the rate or rates for the distribution of electricity.

(oooo) "**Rate Adjustment Difference**" means a difference equal to one percent (1%) minus the OEB Percentage Rate Reduction.

(pppp) "**Rate Adjustment Factor**" means a factor equal to the Rate Adjustment Difference divided by one percent (1%).

(qqqq) "**Rate Classes**" means those classes of Rates specified in Schedule 6.7(a) of this Agreement.

(rrrr) "**Rate Freeze Period**" means the period commencing on the Closing Date and ending on the date which is five (5) years after the Closing Date.

(ssss) "**Rate Order**" means the order issued by the OEB approving the Corporation's Rates in effect as at May 1, 2016, and as set out in matter EB-2015-0024.

(tttt) "**Real Property**" has the meaning ascribed thereto in Subsection 3.1(l).

(uuuu) "**Reduced Rates**" means the reduced Rates that result from the application of a Negative Rate Rider or a Partial Rate Rider to the Current Rates.

(vvvv) "**Regulatory Accounts Calculation**" has the meaning ascribed thereto in Section 2.4(a)(iv).

(wwww) "**Release**" has the meaning ascribed thereto in any Environmental Law and includes, without limitation, any presence, release, spill, leak, pumping, pouring, addition, emission, emptying, discharge, injection, escape, leaching, disposal, dispersal, migration, dumping, deposit, spraying, burial, abandonment, incineration, seepage or placement.

(xxxx) "**Remedial Order**" means any complaint, direction, order or sanction issued, filed or imposed by any Governmental Authority pursuant to any Environmental Law and includes any order requiring any remediation or clean-up of any Hazardous Substance or requiring that any Release or any other activity be reduced, modified or eliminated.

(yyyy) "**Representative**" means, with respect to any Party, its Affiliates and, if applicable, its and their respective directors, officers, employees, agents and other representatives and advisors.

(zzzz) "**Required Approval**" has the meaning ascribed thereto in Section 7.1.

(aaaaa) "**Statutory Plans**" means benefit plans that the Corporation are required by domestic or foreign statutes to participate in or contribute to in respect of an employee, director or officer of the Corporation or any beneficiary or dependent thereof, including the Canada Pension Plan, and plans administered pursuant to applicable health, Tax, workplace safety insurance, workers' compensation and employment insurance legislation.

(bbbbb) **Straddle Period**" means any Tax period that includes the Closing Date, but does not begin on the Closing Date or end on the day prior to the Closing Date.

(ccccc) "**Subsidiary**" has the meaning ascribed thereto in the OBCA.

(ddddd) "**Tax**" or "**Taxes**" means the PILs payable pursuant to Section 93 of the EA and all domestic and foreign federal, provincial, municipal, territorial or other taxes, imposts, rates, levies, assessments and government fees, charges or dues lawfully levied, assessed or imposed against the Corporation including, without limitation, all income, capital gains, sales, excise, use, property, capital, goods and services, business transfer and value added taxes, all customs and import duties, workers' compensation premiums, Canada Pension Plan premiums, Employment Insurance premiums, and payments pursuant to Part VI of the EA together with all interest, fines and penalties with respect thereto.

(eeeee) "**Tax Act**" means the *Income Tax Act* (Canada) and any regulations thereunder.

(fffff) "**Tax Return**" means all returns, information returns, declarations, designations, forms, schedules, elections, reports and other documents of every nature whatsoever (and includes related or supporting information) filed, or required to be filed with any Governmental Authority with respect to any Taxes, including those required pursuant to Part VI of the EA, or with respect to the administration of any Laws or administrative requirements relating to any Taxes and any amendments thereof.

(ggggg) "**Third Party Claim**" has the meaning ascribed thereto in Section 12.3.

(hhhhh) "**Time of Closing**" means the close of business on the Closing Date.

(iiiii) "**Transactions**" means the purchase and sale of the Purchased Shares and all other transactions contemplated by this Agreement.

(jjjjj) "**Vendor**" means the Orillia Power Corporation.

(kkkkk) "**Vendor's Counsel**" means Borden Ladner Gervais LLP, a limited liability partnership duly constituted under the laws of the Province of Ontario.

(lllll) "**Working Capital**" means the working capital of the Corporation, which is the amount by which the net book value of the current assets, excluding cash, exceeds the net book value of the current liabilities and customer security deposits. The current assets are the sum of accounts receivable, unbilled energy and distribution revenue, payment in lieu of taxes receivable, inventories, prepaid expenses, due from related parties and other current assets. The current liabilities are the sum of bank indebtedness, accounts payable and accrued liabilities, payment in lieu of taxes payable and current portion of long term debt, due to related parties and other current liabilities.

(mmmmm) "**Working Capital Calculation**" has the meaning ascribed thereto in Section 2.4(a)(i).

1.2 **Construction**. This Agreement has been negotiated by each Party with the benefit of legal representation, and any rule of construction to the effect that any ambiguities are to be resolved against the drafting party does not apply to the construction or interpretation of this Agreement.

1.3 **Certain Rules of Interpretation**. In this Agreement:

(a) the division into Articles and Sections and the insertion of headings and the Table of Contents are for convenience of reference only and do not affect the construction or interpretation of this Agreement;

(b) the expressions "hereof", "herein", "hereto", "hereunder", "hereby" and similar expressions refer to this Agreement and not to any particular portion of this Agreement; and

(c) unless specified otherwise or the context otherwise requires:

(i) references to any Article, Section or Schedule are references to the Article or Section of, or Schedule to, this Agreement;

(ii) "including" or "includes" means "including (or includes) but is not limited to" and is not to be construed to limit any general statement preceding it to the specific or similar items or matters immediately following it;

(iii) "the aggregate of", "the total of", "the sum of", or a phrase of similar meaning means "the aggregate (or total or sum), without duplication, of";

(iv) references to Contracts are deemed to include all present amendments, supplements, restatements and replacements to those Contracts as of the date of this Agreement;

(v) references to any legislation, statutory instrument or regulation or a section thereof are references to the legislation, statutory instrument, regulation or section as of the date of this Agreement except that with respect to Vendor's obligations to comply with Applicable Law regarding Taxes, the reference date shall be the relevant point in time prior to Closing;

(vi) words in the singular include the plural and vice versa and words in one gender include all genders.

1.4 **Knowledge**. In this Agreement, any reference to the knowledge of the Vendor or the City means to the best of the knowledge, information and belief of the Vendor or the City after making due inquiries regarding the relevant matter of all relevant Representatives of the Corporation, the City and the Vendor.

1.5 **Computation of Time**. In this Agreement, unless specified otherwise or the context otherwise requires:

(a) a reference to a period of days is deemed to begin on the first day after the event that started the period and to end at 5:00 p.m. on the last day of the period, but if the last day of the period does not fall on a Business Day, the period ends at 5:00 p.m. on the next succeeding Business Day;

(b) all references to specific dates mean 11:59 p.m. on the dates;

(c) all references to specific times are references to Toronto time; and

(d) with respect to the calculation of any period of time, references to "from" mean "from and excluding" and references to "to" or "until" mean "to and including".

1.6 **Performance on Business Days**. If any action is required to be taken pursuant to this Agreement on or by a specified date that is not a Business Day, the action is valid if taken on or by the next succeeding Business Day.

1.7 **Calculation of Interest**. In calculating interest payable under this Agreement for any period of time, the first day of the period is included and the last day is excluded.

1.8 **Currency and Payment**. In this Agreement, unless specified otherwise:

(a) references to dollar amounts or "$" are to Canadian dollars; and

(b) any payment is to be made by an official bank draft drawn on a Canadian chartered bank, wire transfer or any other method (other than cash payment) that provides immediately available funds;

1.9 **Schedules and Exhibits**. The following schedules are attached to and form part of this Agreement:

Schedule 1.1(zzz)	-	Permitted Encumbrances
Schedule 3.1(l)	-	Real Property, Leased Property and Easements
Schedule 3.1(m)	-	Intellectual Property
Schedule 3.1(n)	-	Contracts and Commitments
Schedule 3.1(o)	-	Material Contracts
Schedule 3.1(p)	-	Employee Plans
Schedule 3.1(q)	-	Collective Agreement
Schedule 3.1(s)	-	Insurance Policies
Schedule 3.1(v)	-	Taxes
Schedule 3.1(z)	-	Licences
Schedule 6.2	-	Participation in Community Events
Schedule 6.4	-	City Property
Schedule 6.6	-	Rate Classes
Schedule 9.1(c)	-	Purchaser Consents
Schedule 9.2(c)		Vendor Consents

ARTICLE II
PURCHASE AND SALE OF PURCHASED SHARES

2.1 **Purchase and Sale of Purchased Shares**. Subject to the terms and conditions hereof, the Vendor agrees to sell, assign and transfer to the Purchaser and the Purchaser agrees to purchase from the Vendor all of the issued and outstanding shares of the Corporation, as described in the table below (the "**Purchased Shares**"):

Class of Shares	Issued	Shareholder
Common Shares	1001	Orillia Power Corporation

2.2 **Purchase Price**. The purchase price payable by the Purchaser to the Vendor for the Purchased Shares (the "**Purchase Price**") shall, subject to any adjustment in accordance with Section 2.4, be the sum of twenty-six million and three hundred and fifty thousand dollars ($26,350,000).

2.3 **Payment of Purchase Price**.

The Purchase Price shall be payable as follows:

(a) concurrently with the execution and delivery of this Agreement, the sum of one million five hundred thousand dollars ($1,500,000) delivered to the Vendor's Counsel in trust, by wire transfer, which amount shall hereinafter be referred to as the "**Deposit**", and

such Deposit to be held by Vendor's Counsel in trust in an interest bearing account and released in accordance with the terms and conditions of this Agreement; and

(b) the balance on Closing by wire transfer of immediately available funds to the Vendor;

(c) if applicable, the amounts payable pursuant to Section 2.4(c) and Section 2.6 below as set out therein.

The Vendor and the City shall cause the Vendor's Counsel to pay to the Purchaser immediately following Closing, all accrued interest on the Deposit.

2.4 **Adjustment to Purchase Price**.

(a) Subject to Section 2.5, within ninety (90) days following the Closing Date, the Vendor shall cause the preparation and delivery of audited financial statements for the Corporation, the Closing Date Financial Statements together with the Working Capital Calculation, the NFA Calculation, the Regulatory Accounts Calculation and the Long Term Debt Calculation, to the Parties, all of which shall be audited by the Auditors, together with the Auditors' working papers. The Purchase Price contemplated in Section 2.2 shall be increased or decreased on a dollar for dollar basis as set out below:

(i) for the difference between the Closing Date Working Capital and the Initial Working Capital as shown in the Working Capital Calculation ("**Working Capital Calculation**");

(ii) for an amount equal to the amount obtained when the NFA Index is multiplied by the difference between the Closing Date NFA and the Initial NFA as shown in the NFA Calculation ("**NFA Calculation**");

(iii) For the difference between the Closing Date Long Term Debt and the Initial Long Term Debt as shown in the Long Term Debt Calculation ("**Long Term Debt Calculation**"); and

(iv) for the difference between the Closing Date Regulatory Accounts and the Initial Regulatory Accounts as shown in the Regulatory Accounts Calculation ("**Regulatory Accounts Calculation**").

The Purchaser shall pay the Vendor, as applicable, on a dollar for dollar basis (A) the amount by which the Closing Date Working Capital exceeds the Initial Working Capital; (B) an amount equal to the amount obtained when the NFA Index is multiplied by the amount by which the Closing Date NFA exceeds the Initial NFA; (C) the amount by which the Initial Long Term Debt exceeds the Closing Date Long Term Debt; and (D) the amount by which the Closing Date Regulatory Accounts exceeds the Initial Regulatory Accounts. The Vendor shall pay the Purchaser, as applicable, on a dollar for dollar basis, (A) the amount by which the Initial Working Capital exceeds the Closing Date Working Capital; (B) an amount equal to the amount obtained when the NFA Index is multiplied by the amount by which the Closing Date NFA is less than the Initial NFA; (C) the amount by which the Closing Date Long Term Debt exceeds the

Initial Long Term Debt; and (D) the amount by which the Initial Regulatory Accounts exceeds the Closing Date Regulatory Accounts.

An illustration of the purchase price adjustments in this subsection is set out in Schedule 2.4(a) hereto.

(b) The Purchaser shall have a period of thirty (30) Business Days from the later of (i) the receipt of the Closing Date Financial Statements, the Working Capital Calculation, the NFA Calculation, Regulatory Accounts Calculation and the Long Term Debt Calculation; and (ii) the date on which the Purchaser is provided with access to the Auditor's working papers relating to the Closing Date Financial Statements, the Working Capital Calculation, the NFA Calculation, Regulatory Accounts Calculation and the Long Term Debt Calculation within which to notify the Vendor in writing that it disputes any amounts contained in the Closing Date Financial Statements, the Working Capital Calculation, the NFA Calculation, Regulatory Accounts Calculation and/or the Long Term Debt Calculation (the "**Purchaser's Objection**"), failing which the Purchaser shall be deemed to have accepted such amounts. The Purchaser's Objection shall set forth a specific description of the basis of the Purchaser's Objection and the adjustments to the Closing Date Financial Statements, the Working Capital Calculation, the NFA Calculation, Regulatory Accounts Calculation and/or the Long Term Debt Calculation which the Purchaser believes should be made. Any items not specifically disputed during such thirty (30) Business Day period shall be deemed to have been accepted by the Purchaser.

(c) Subject to Section 2.4(d), payment of the adjustment to the Purchase Price pursuant to Section 2.4(a) shall be made by the applicable Party within thirty (30) Business Days following the later of (i) the date that the Closing Date Financial Statements, the Working Capital Calculation, the NFA Calculation, Regulatory Accounts Calculation and the Long Term Debt Calculation are received by the Purchaser; and (ii) the date on which the Purchaser is provided with access to the Auditor's working papers relating to the Closing Date Financial Statements, the Working Capital Calculation, the NFA Calculation, Regulatory Accounts Calculation and the Long Term Debt Calculation.

(d) If the Vendor and the Purchaser cannot agree on the adjustment of the Purchase Price pursuant to Section 2.4(a) within the time limit for payment of the adjustment to the Purchase Price pursuant to Section 2.4(b), the Vendor and the Purchaser will submit any unresolved matter within a further five (5) day period, to an independent, nationally recognized accounting firm selected by the Vendor and the Purchaser (the "**Independent Auditor**") for resolution or, failing agreement, as appointed by the Ontario Superior Court of Justice. The Independent Auditor will be given access to all materials and information reasonably requested by it for such purpose. The rules and procedures to be followed in the arbitration proceedings will be determined by the Independent Auditor in its discretion. The Independent Auditor will make its determination as soon as practicable and, in any case, within thirty (30) days of the matter being submitted to it. The Independent Auditor determination of all such matters will be final and binding on the Parties and will not be subject to appeal by any Party. The fees and expenses of the Independent Auditor will be borne equally

between the Vendor and the Purchaser. The Closing Date Financial Statements and amounts specified in Section 2.4(a) will be modified to the extent required to give effect to the Independent Auditor's determination and will be deemed to have been approved as of the date of such determination.

2.5 **Access**. Following the Closing, the Purchaser shall provide the Vendor and the Auditor with timely access to all books, records, documents, materials, and other information and Representatives of the Corporation reasonably requested by the Vendor for purposes of preparation and delivery of the Closing Date Financial Statements together with the Working Capital Calculation, the NFA Calculation, Regulatory Accounts Calculation and the Long Term Debt Calculation.

2.6 **Rate Reduction Adjustment**.

(a) In the event the OEB does not approve any negative rate rider, the Purchaser shall pay the Vendor, within five (5) Business Days after the Closing Date, a lump sum amount equal to the Five Year Fixed Payment Amount in immediately available funds.

(b) In the event that the OEB approves a Partial Rate Rider, the Purchaser will pay the Vendor, within five (5) Business Days after the Closing Date, an amount equal to the Five Year Fixed Payment Amount times the Rate Adjustment Factor.

2.7 **Deposit**. The Deposit shall be held by the Vendor's solicitor in trust, and shall be invested in an interest bearing account with interest accruing to the Purchaser except as set forth below. On Closing, the Deposit shall be applied on account of the Purchase Price and any and all interest accrued thereon shall be paid to the Purchaser forthwith following Closing. Notwithstanding the foregoing, if the conditions set forth in Section 9.1 have not been satisfied or complied with and the Purchaser does not waive compliance therewith on such terms as may be agreed in writing, the Deposit, together with any interest earned thereon shall be refunded to the Purchaser in accordance with Section 9.1. If, however, the Transactions are not completed on the Closing Date and the conditions set forth in Section 9.1 have been satisfied, complied with or waived, the Deposit, together with any interest earned thereon, may be retained by the Vendor to the extent permitted under Section 9.2.

2.8 **Valuation of Assets**. The Vendor and Purchaser agree to file the same allocation in respect of the Transactions. In the event that the Vendor and the Purchaser are unable to reach agreement on the allocation of the Purchase Price within sixty (60) days of delivery of the Closing Date Financial Statements, the parties shall appoint an independent valuator at their joint expense, to determine the appropriate allocation in accordance with this clause, whose decision shall be binding on all Parties unless manifestly incorrect.

ARTICLE III
REPRESENTATIONS AND WARRANTIES

3.1 **Representations and Warranties of the Vendor**. The Vendor represents and warrants to the Purchaser as follows and acknowledges that, except as otherwise expressly provided herein, the Purchaser is relying on such representations and warranties in connection with the transactions contemplated herein:

(a) **Organization**. The Vendor and the Corporation are duly incorporated and validly subsisting under the laws of the Province of Ontario and have the corporate power, capacity and authority to own or lease or dispose of its property and assets and to carry on the business presently carried on by it under the laws of the Province of Ontario. No proceedings have been instituted or are pending for the dissolution, winding up or liquidation of the Vendor or the Corporation.

(b) **Corporate Power of the Vendor and City and Due Authorization**. The Vendor and the City have all requisite and statutory power, authority and capacity to enter into, and to perform its obligations under this Agreement and to transfer the legal and beneficial title and ownership of the Purchased Shares to the Purchaser free and clear of all Encumbrances. Each of the Vendor and the City has duly taken, or has caused to be taken, all action required to be taken by the Vendor or the City to authorize the execution and delivery of this Agreement and any other agreement or document to be delivered pursuant hereto by the Vendor or the City in the performance of its obligations hereunder.

(c) **Binding Agreement**. This Agreement has been duly executed by the Vendor and the City and will, upon delivery, constitute valid and binding obligations of the Vendor and the City, enforceable against each in accordance with its terms, except as enforcement may be limited by bankruptcy, insolvency and other Applicable Laws affecting the rights of creditors generally and except that equitable remedies may be granted only in the discretion of a court of competent jurisdiction.

(d) **Authorized and Issued Capital of the Corporation**. The authorized share capital of the Corporation consists of an unlimited number of Common Shares, of which only the Purchased Shares have been validly allotted and issued and are outstanding as fully paid and non-assessable shares, and will be the only outstanding shares of the Corporation at Closing.

(e) **Ownership of Shares**. The Vendor is the sole beneficial and registered owner of the Purchased Shares, with good and marketable title thereto, free and clear of all Encumbrances (other than the rights of the Purchaser hereunder) and has the exclusive right to dispose of the Purchased Shares as herein provided. Without limiting the generality of the foregoing, none of the Purchased Shares is subject to any voting trust, shareholder agreement or voting agreement.

(f) **Options**. No Person (other than the Purchaser under this Agreement) has the benefit of any Contract or any right or privilege (whether by Applicable Law, pre-emptive or contractual) binding upon or which may at any time in the future become binding upon the Vendor or the City, to acquire or obtain in any other way an interest in any of the Purchased Shares.

(g) **Subsidiaries**. The Corporation has no Subsidiaries and has never had any interest in any shares of any other corporation nor any interest in any partnership or other entity, except as disclosed in Schedule 3.1(g) .

(h) **No Violations**. Neither the execution nor delivery of this Agreement nor the completion of the transactions herein contemplated will result in the violation of:

(i) any provision of the by-laws of the Vendor or the City;

(ii) any Contract to which the Vendor, the City or the Corporation is a party or by which the Vendor, the City or the Corporation or any of their respective properties is bound, which would have a material adverse effect on the Vendor's or the Corporation's ability to perform its obligations under this Agreement; or

(iii) subject to the Required Approval, to the Vendor's and the City's knowledge, any Applicable Law or requirement of a Government Authority having jurisdiction over each of the Vendor, the City or the Corporation, which would have a material adverse effect on the Vendor's or the City's ability to perform its obligations under this Agreement.

(i) **Consents and Approvals**. Other than the Required Approval, there is no requirement for the Vendor, the City or the Corporation to make any filing with, give any notice to or obtain any licence, permit, certificate, registration, authorization, consent or approval of, any Government Authority as a condition to the lawful consummation of the Transaction.

(j) **Compliance with Applicable Law**. The Corporation has complied in all material respects with all Applicable Laws relating to its Business, the failure to comply with which would have a Material Adverse Effect. The Corporation is not in violation or default under, and to the Vendor's knowledge, no event has occurred which, with the lapse of time or the giving of notice or both, would result in the violation of or default under, the terms of any judgment, decree, order injunction or writ of any court or other Government Authority with respect to the Business, which would have a Material Adverse Effect.

(k) **Corporate Records**. The corporate records and minute books of the Corporation produced by the Vendor in the Data Room are in all material respects a complete and accurate record of the material business transacted at meetings of, and contain all resolutions passed by, the directors and the sole shareholder of the Corporation held since the incorporation of the Corporation. To the Vendor's knowledge, each and all such meetings were duly called and held and all such resolutions and by laws were duly passed. The share certificate books, registers of shareholders, registers of transfers, registers of directors and other corporate registers of each are complete and accurate.

(l) **Real Property**.

(i) to the Vendor's knowledge Schedule 3.1(l) sets forth a list of lands owned in fee simple (the "**Real Property**") and property leased (the "**Leased Property**") by the Corporation and Easements held by the Corporation.

(ii) To the Vendor's knowledge, the Corporation does not own real property or have rights under any leases, and has not agreed to acquire or lease, any real property other than as listed in Schedule 3.1(l).

(iii) neither the Vendor nor the Corporation has received any, nor to the Vendor's knowledge are there any pending or threatened, notices of violation or alleged violation of any Applicable Laws against or affecting any Real Property or Leased Property.

(iv) The Real Property, Leased Property and Easements provide the required rights of occupancy, possession, use, entry and exit, as applicable, as are reasonably necessary to carry on the Business.

(v) Other than listed in Schedule 3.1(l), no Person has any right to purchase any of the Real Property and no Person other than the Corporation is using or has any right to use, is in possession or occupancy, of any part of the Real Property.

(vi) to the Vendor's knowledge there exists no option, right of first refusal, or other contractual rights with respect to any of the Real Property, except such rights as provided in this Agreement.

(vii) neither the Vendor nor the Corporation has entered into any contract to sell, transfer, encumber, or otherwise dispose of or impair the right, title and interest of the Corporation in and to Real Property, Leased Property or Easements, except any Permitted Encumbrances listed in Schedule 1.1(zzz).

(viii) Neither the Vendor nor the Corporation has received any notification of, nor are there any outstanding or incomplete work orders in respect of any Fixed Assets on such Real Property, Leased Property, Easements or of any current non-compliance (other than non-compliances which are legal non-conforming under relevant zoning by laws) with Applicable Law, including without limitation, building and zoning by laws and regulations, and no by law which would reasonably be expected to have a Material Adverse Effect on the Business is currently being contemplated by the City.

(ix) All accounts for work and services performed or materials placed or furnished upon or in respect of the construction and completion of any Fixed Assets on Real Property, Leased Property or Easements have been fully paid and no Person is entitled to claim a lien under the *Construction Lien Act* (Ontario) or other similar legislation for such work.

(x) to the Vendor's knowledge, there are no matters affecting the right, title and interest of the Corporation, as applicable, in and to the real property used in its Business which would have a Material and Adverse Effect on the ability of the Corporation to carry on its Business thereon.

(xi) The Corporation holds its interests in the Leased Property pursuant to valid leases described in Schedule 3.1(l), true copies of which have been provided to

the Purchaser in the Data Room, which contain all of the rights and obligations of the parties related to the use and occupancy of each such property, have not been altered or amended and are in full force and effect and under which neither the landlord nor the tenant is in default, nor to the Vendor's knowledge are there circumstances which, but for the passing of time or giving of notice or both, would constitute a default by either party. The Corporation has not waived or omitted to take any action in respect of any material rights under any such lease.

(xii) neither the Vendor nor the Corporation has made an application for the rezoning of any Real Property or Leased Property and to the Vendor's knowledge there is no proposed or pending change to any zoning affecting the Real Property or Leased Property.

(xiii) No part of the Real Property or Leased Property is subject to any building or use restriction which would prevent or limit its current use in the Business.

(xiv) to the Vendor's knowledge, no Fixed Assets constituting a part of the Real Property, Leased Property or Easements encroaches on real property not forming part of such property.

(xv) no part of the Real Property has ever been used as a landfill or for the disposal of waste.

(xvi) Except as disclosed in the Confidential Disclosure Schedule, no asbestos, asbestos containing materials, polychlorinated biphenyls ("**PCBs**") and PCB wastes are used, stored or otherwise present in or on the Real Property except for PCBs contained in the electrical transformers which are in service and which form an integral part of, and are necessary for the operation of the Business. The Vendor has disclosed to the Purchaser in the Data Room all inspection reports received from the Ministry of the Environment in connection with the handling, transportation and storage by the Corporation of PCBs or any other Hazardous Substance; and

(xvii) Except as disclosed in the Confidential Disclosure Schedule, there are no Hazardous Substances in, on or under the Real Property owned or occupied by the Corporation, used in the Business or concerning the condition of which the Corporation is otherwise responsible and there are no underground storage tanks on the Real Property or Leased Property and any underground storage tanks formerly on the Real Property or Leased Property have been removed and any affected soil, surface water or ground water has been remediated in compliance with all Applicable Law including, without limitation, Environmental Law.

(m) **Intellectual Property**. Schedule 3.1(m) sets forth and describes all trade secrets and any licensed property or technology used in whole or in part by the Business, and all material trademarks, trade names, service marks, brand names, patents, copyrights,

industrial designs and other industrial property rights, and all applications therefor, in each case specifying whether the item is owned used by the Corporation under a licence agreement or arrangement from another Person. The Corporation has valid rights to use such intellectual property in the Business

(n) **Contracts and Commitments**. Except as set forth in Schedule 3.1(n), the Corporation is not party to or bound by any of the following:

(i) any offer letter or employment contract or consulting contract in the nature of an employment contract or any other Contract with any director, officer or employee, including any agreements or arrangements relating to compensation, other than oral Contracts of indefinite hire terminable by the employer without cause on reasonable notice; or

(ii) any agreement, contract or commitment limiting the freedom of the Corporation to engage in any line of business or to compete with another Person.

(o) **Material Contracts**. The Vendor has previously delivered by placing them in the Data Room, true and complete copies of all Material Contracts, all of which are in full force and effect and unamended and no material default exists under any such Material Contract on the part of the Corporation or, to the knowledge of the Vendor, on the part of any other party to such Contracts, and there are no current or pending negotiations with respect to the renewal, repudiation or amendment of any such Material Contract.

(p) **Employee Plans**.

(i) Except as set forth in the Data Room and further described in Schedule 3.1(n) and Schedule 3.1(p), the Corporation is not party to, bound by, subject to and has no liability or contingent liability, either as purchaser or supplier, relating to any employment agreement or any agreement or arrangement relating to information provided under Section 3.1(n), salary, wages, deferred compensation, bonus, incentive or other compensation, commission, fee, profit sharing, severance, termination pay, supplementary employment insurance, vacation entitlements, insurance, health, welfare, disability, pension, retirement, hospitalization, medical, prescription drug, dental, eye care, arrangements for personal use of any corporate assets based on past practice and other similar benefits, plans or arrangements, including as may be included in any Collective Agreement (the "**Employee Plans**"), whether funded or unfunded, formal or informal, written or unwritten, that is maintained, contributed to, or required to be maintained or contributed to, by the Corporation, or to which the Corporation is a party, directly or indirectly for the benefit of the Employees and their respective beneficiaries and dependents, other than Statutory Plans.

(ii) Other than the OMERS Plan, the Purchaser has been provided access to a true and complete copy of each Employee Plan (as amended to date) together with true and complete copies of all material documents relating to each such Employee Plan excluding OMERS, including, as applicable, all booklets,

summaries, notices or manuals prepared for or circulated to Employees generally concerning each such Employee Plan and all contracts through which the Corporation obtains benefits, plans and arrangements for the benefit of Employees or former employees.

(iii) All obligations of the Corporation due prior to Closing under the Employee Plans, OMERS and the Statutory Plans (whether pursuant to the terms thereof or any Applicable Law) have been or will be satisfied in all material respects.

(iv) Other than the OMERS Plan, with respect to which the Vendor makes no representation, and other than any grievance that has been resolved or settled, as applicable, all Employee Plans are, and have been, established, registered (where required), and administered, in material compliance with (i) the terms thereof; (ii) all Applicable Law; and (iii) applicable Collective Agreements and neither the Vendor nor the Corporation has received, in the last four (4) years, any notice from any Person questioning or challenging such compliance (other than in respect of any claim related solely to that Person), nor does the Vendor or the Corporation have any knowledge of any such notice from any Person questioning or challenging such compliance beyond the last four (4) years. Except as disclosed in Schedule 3.1(p) and other than the OMERS Plan or as set out in the Collective Agreement, there are no promised improvements, increases or changes to, the benefits provided under any Employee Plan, nor does any Employee Plan provide for benefit increases or the acceleration of funding obligations that are contingent upon or will be triggered by the execution of this Agreement or the Closing.

(v) Except as disclosed in Schedule 3.1(p), no Employee Plan, other than the OMERS Plan, provides benefits beyond retirement or other termination of service to employees or former employees of the Corporation or to the beneficiaries or dependants of such employees or former employees. Other than the OMERS Plan, with respect to which the Vendor makes no representation, no Employee Plan requires or permits a retroactive increase in premiums or payments.

(vi) All employee data necessary to administer the Corporation' participation in the Employee Plans is in the possession of the Corporation and is complete, correct and in a form which is sufficient for the proper administration of the Corporation' participation in the OMERS Plan and the other Employee Plans in accordance with the terms thereof and all Applicable Laws.

(vii) OMERS is the only pension or retirement plan or arrangement in which employees or former employees of the Corporation participate and/or to which the Corporation contributes as a participating employer.

(viii) All obligations of the Corporation to or under OMERS (whether pursuant to the terms thereof or Applicable Law) have been satisfied, and there are no

outstanding defaults or violations thereunder by the Corporation or by any predecessor thereof.

(ix) There are no obligations of the Corporation with respect to unfunded actuarial liabilities, past service unfunded liabilities or solvency deficiencies respecting the Corporation's participation in OMERS.

(q) **Labour Matters**.

(i) Except as set forth in Schedule 3.1(q) (the "**Collective Agreement**") the Corporation is not a party to or bound by or subject to any agreement or arrangement with any labour union or employee association and has not made any commitment to or conducted any negotiation or discussion with any labour union or employee association with respect to any future agreement or arrangement.

(ii) There is no strike or lockout occurring or affecting, or to the Vendor's knowledge threatened against, the Corporation.

(r) **Employees**.

(i) The Purchaser has been provided with a complete and accurate confidential list of the names of all individuals who are employees (the "**Employees**") of the Corporation specifying title, compensation, years of service, whether they are union or non-union, and the benefits under the Employee Plans to which they are entitled (the "**Employee Fact Sheet**").

(ii) Except as disclosed in the Employee Fact Sheet, no Employee is on long term disability leave, extended absence or receiving benefits pursuant to the *Workplace Safety and Insurance Act* (Ontario).

(iii) The Corporation has been operated in material compliance with all Applicable Laws relating to employees, including employment standards and all laws relating to full or in part to the protection of employee health and safety, human rights, labour relations and pay equity. Except as disclosed in the Employee Fact Sheet:

(A) there have been no Claims nor, to the Vendor's knowledge, are there any threatened complaints, under such laws against the Corporation;

(B) to the Vendor's knowledge, nothing has occurred which might lead to a Claim or complaint against the Corporation, under any such laws; and

(C) there are no outstanding decisions or settlements or pending settlements which place any obligation upon the Corporation to do or refrain from doing any act with respect to its Employees.

(iv) All assessments under the *Workplace Safety and Insurance Act* (Ontario) in relation to the Business of the Corporation have been paid or accrued and the Corporation is not subject to any special or penalty assessment under such legislation which has not been paid.

(s) **Insurance**. Schedule 3.1(s) sets forth all insurance policies, other than those already disclosed in the Schedule 3.1(o), (specifying the insurer, the amount of the coverage, the type of insurance, the policy number and any pending claims thereunder, maintained by the Corporation on its Property or personnel, including former personnel) of the Business. The Vendor, and not the Corporation, is the subscriber to the MEARIE Reciprocal Agreement.

(t) **Environmental**.

To the knowledge of the Vendor and except as disclosed in the Confidential Disclosure Schedule

(i) the Business conducted on or at real property while occupied or used by the Corporation, has been and is now in compliance in all material respects with all applicable Environmental Laws. Any Release by the Corporation, of any Hazardous Substance into the Environment complied and complies in all material respects with all applicable Environmental Laws, and not in a manner that could reasonably be expected to have a Material Adverse Effect;

(ii) the Corporation has obtained all requisite Environmental Approvals, which Environmental Approvals are valid and in full force and effect, have been and are being complied with in all material respects and there have been and are no proceedings commenced or threatened to revoke or amend any Environmental Approvals in a manner that could reasonably be expected to have a Material Adverse Effect. The Confidential Disclosure Schedule lists all of the Environmental Approvals held by the Corporation;

(iii) the Corporation has not been and is not now the subject of any Remedial Order nor, is any investigation or evaluation threatened or commenced as to whether any such Remedial Order is necessary;

(iv) the Corporation has never been prosecuted for or convicted of any offence under Environmental Laws, nor has the Corporation been found liable in any proceeding to pay any damages, fine or judgment to any Person as a result of any Release or threatened Release of any Hazardous Substance into the Environment or as the result of any breach of any Environmental Laws. No notice has been received by the Vendor or by the Corporation of any investigation or evaluation by any Governmental Authority or of any Claims, pending or threatened, and there are no investigations or evaluations threatened or commenced as to whether any offence by any of the foregoing has occurred. There are no Claims that have been threatened or commenced against the Corporation as a result of any Release or threatened Release of any Hazardous

Substance into the Environment or as the result of the breach of any Environmental Laws.

(u) **Litigation**. Except as set out in the Confidential Disclosure Schedule, there are no Claims (whether or not purportedly on behalf of the Corporation) pending or, to the Vendor's knowledge, threatened against or affecting, the Corporation at law or in equity, or before or by any Governmental Authority, or by or before an arbitrator or arbitration board which, either individually or in the aggregate, would have a Material Adverse Effect or prevent the Vendor or the City from fulfilling any of its obligations set out in, or arising in connection with, this Agreement.

(v) **Taxes**.

(i) the Corporation is exempt from Tax under the Tax Act and the CTA but is required to make PILS payments under the EA in an amount equal to the Tax that it would be liable to pay under the Tax Act and CTA if it were not exempt from Tax under those statutes.

(ii) the Corporation has filed in the prescribed manner and within the prescribed times all Tax Returns required to be filed by it in all applicable jurisdictions with respect to taxation periods ended on or before the Closing Date. All such Tax Returns are complete and correct and disclose all Taxes required to be paid for the periods covered thereby. The Corporation has never been required to file any Tax Returns with, and has never been liable to pay or remit Taxes to, any Governmental Authority outside Ontario or Canada. The Corporation has paid in full when due all Taxes and all instalments of Taxes due on or before the Closing Date. There are no liens for unpaid Taxes on any of the Corporation's Property. Without restricting the generality of the foregoing, all Taxes shown on all Tax Returns or on any assessments or reassessments in respect of any such Tax Returns have been paid in full when due except to the extent that the Corporation has properly objected to such assessments or reassessments in accordance with Applicable Law. The Vendor has furnished to the Purchaser true, complete and accurate copies of all Tax Returns and any amendments thereto filed by the Corporation since 2012 and all notices of assessment and reassessment and all correspondence with Governmental Authorities relating thereto as well as true, complete and accurate copies of all tax returns and any amendments filed thereto, and all notices of assessment and reassessment and all correspondence with Governmental Authorities or tax advisors relating thereto. The provision for taxes in the Initial Financial Statement constitutes an adequate provision for the payment of all unpaid Taxes in respect of all periods up to and including the period to which the Initial Financial Statement relates.

(iii) Assessments under the EA and ETA have been issued to the Corporation covering all periods up to and including its fiscal year ended December 31, 2015.

(iv) There are no audits, assessments, reassessments or other Claims in progress or, to the knowledge of the Vendor, threatened against the Corporation, in respect of any Taxes and, in particular, there are no currently outstanding reassessments or written enquiries which have been issued or raised by any Governmental Authority relating to any such Taxes except for those items listed in Schedule 3.1(v). The Vendor is not aware of any contingent liability of the Corporation for Taxes or any grounds that could prompt an assessment or reassessment for Taxes, and the Corporation has not received any indication from any Governmental Authority that any assessment or reassessment is proposed with respect to taxation periods ended on or before the Closing Date.

(v) the Corporation has not entered into any agreements, waivers or other arrangements with any Governmental Authority providing for an extension of time with respect to the issuance of any assessment or reassessment, the filing of any Tax Return, or the payment of any Taxes by or in respect of the Corporation. The Corporation is not a party to any agreements or undertakings with respect to Taxes.

(vi) The Corporation is a registrant for purposes of the ETA, and the HST registration number is:

865120596RT001.

All input tax credits claimed by the Corporation pursuant to the ETA has been proper, correctly calculated and documented. The Corporation has collected and remitted when due all Taxes, including GST/HST and RST, as required by tax legislation.

(vii) The Vendor is not a non-resident for the purposes of the *Tax Act*.

(viii) The Corporation maintains its books and records in compliance with section 230 of the *Tax Act*.

(ix) The Vendor has provided to the Purchaser true, complete and accurate copies of all Canadian federal and Ontario income Tax Returns of the Corporation for the last four (4) completed taxation years and all related communications to or from all Governmental Authorities. Canadian federal and provincial income, sales (including goods and services and harmonized sales and provincial or territorial sales) and capital tax assessments have been issued to the Corporation for all taxation years or periods up to and including its taxation year ended as of Closing Date. No notice of determination of loss for the Corporation from a Governmental Authority has been requested by or issued to the Corporation.

(x) The Corporation is not party, or bound by or obligated by contract or otherwise, to any undertaking regarding any Tax allocation, indemnity or sharing contract or arrangement, and neither is it liable for the Taxes of any other Person as a transferee or successor.

(xi) The value of consideration paid or received by the Corporation for the acquisition, sale, transfer or provision of property (including intangibles) or the provision of services (including financial transactions) from or to any Person with which it was not dealing at arm's length at the relevant time was the fair market value of such property acquired, provided or sold or services purchased or provided.

(w) **Withholding**. The Corporation has deducted, withheld, collected and remitted when due to each Governmental Authority, all Taxes which it is required to deduct, withhold, collect and remit. Without limiting the generality of the foregoing, the Corporation has withheld from each amount paid or credited or deemed to have been paid or credited, and each taxable benefit conferred upon or distribution paid or deemed to have been paid to any of its past or present employees, officers or directors, and to any non-resident of Canada, the amount of all Taxes and other deductions required to be withheld therefrom, including without limitation, all employee and employer portions for Workers' Compensation, Canada Pension Plan, Employer Health Tax and Employment Insurance and has paid the same to the proper tax or other receiving officers within the time required under any applicable legislation. The Corporation has remitted to the appropriate tax authority when required by law to do so all amounts collected by it on account of sales taxes including HST. The Corporation has not received any requirement, demand or request from any Governmental Authority pursuant to section 224 of the Tax Act or any similar provision of Applicable Law that remains unsatisfied in any respect.

(x) **Ownership of Property**. The Corporation is the sole legal and beneficial, and where interests are registerable, the sole registered owner, of all of the property used in connection with, directly or indirectly, ancillary to, or reasonably necessary for the operation of the Business with good and valid title thereto (with good and marketable title to the Real Property in fee simple) free and clear of all Encumbrances other than minor easements for the supply of utilities, and those Permitted Encumbrances listed in Schedule 1.1(zzz). All of the Fixed Assets used in connection with, directly or indirectly, ancillary to, or reasonably necessary for the operation of the Business are in good working order, condition and repair subject to reasonable wear and tear, have been properly and regularly maintained and are in material compliance with all Applicable Laws. There has been no assignment, subletting or granting of any licence (of occupation or otherwise) of or in respect of any such property or any granting of any contract or right capable of becoming a Contract or option for the purchase of any of such property other than pursuant to the provisions of, or as disclosed in, this Agreement.

(y) **Financial Statements**. The Initial Financial Statements were prepared and the Closing Date Financial Statements will be prepared in accordance with IFRS applied on a basis consistent with that of the preceding period and present, or will present (in the case of the Closing Date Financial Statements), fairly:

(i) in the case of the Initial Financial Statements, all of the assets, liabilities and financial position of the Corporation as at December 31, 2015, and the sales,

earnings, results of operation and changes in financial position of the Corporation for the 12 month period then ended; and

(ii) in the case of the Closing Date Financial Statements, the assets and liabilities of the Corporation as at the Time of Closing.

(z) **Licences**. Schedule 3.1(z) sets out a complete list of all licences, permits, approvals, consents, certificates, registrations and authorizations ("**Licences**") held by or granted to the Corporation, and there are no other licences, permits, approvals, consents, certificates, registrations or authorizations necessary to carry on the Business. Each Licence is valid, subsisting and in good standing and the Corporation is not in default or in breach of any Licence and, to the Vendor's knowledge, no proceeding is threatened or pending to revoke or limit any Licence.

(aa) **Bank Accounts**. The Confidential Disclosure Schedule sets forth a complete list of every financial institution in which the Corporation maintains any depository account, trust account or safety deposit box and the names of all persons authorized to draw on or who have access to such accounts or safety deposit box.

(bb) **Absence of Guarantees**. The Corporation has not given, agreed to give nor shall give, nor is a party or bound by, any guarantee or indemnity in respect of indebtedness, or other obligations, of any Person, or any other commitment by which the Corporation is, or is contingently, responsible for such indebtedness or other obligations.

(cc) **By-Laws**. Other than by laws of general application, no by law of the City exists which materially adversely affects the Corporation or the Business. Other than by laws of general application, no by law which would materially adversely affect the Corporation or the Business is currently being contemplated by the City or, to the City's or the Vendor's Knowledge, has been proposed by any Person.

(dd) **Limitation**. The Vendor and the City make no representation or warranty to the Purchaser except as specifically set forth in this Agreement and this Agreement contains all representations and warranties of the Vendor and the City relating to the Purchased Shares and the Transaction.

(ee) **Effect of Disclosure**. All disclosure contained in a particular representation and warranty set forth in this Agreement (or any Schedule referred to therein) shall be deemed for the purposes of this Agreement to have been made with respect to all of the representations and warranties in this Section 3.1 to which such disclosure might be applicable. Notwithstanding anything else contained herein, the Vendor shall have no liability to the Purchaser with respect to any failure by it to disclose the existence of any matter, document or thing, or to make any other disclosure in the context of a particular representation and warranty set out in this Section 3.1 where the existence of such matter, document or thing has been disclosed as part of another representation or warranty contained in this Agreement or in any Schedule annexed hereto.

3.2 **Representations and Warranties of the Purchaser**. The Purchaser represents and warrants to the Vendor as follows and acknowledges that the Vendor is relying on such representations and warranties in connection with the transactions contemplated herein:

(a) **Organization**. The Purchaser is a corporation duly incorporated and validly subsisting corporation under the laws of Ontario and has the corporate power to own or lease its property and assets and to carry on the business presently carried on by it.

(b) **Corporate Power of the Purchaser and Due Authorization**. The Purchaser has all requisite corporate power, authority and capacity to enter into, and to perform its obligations under this Agreement. The Purchaser has duly taken, or has caused to be taken, all corporate action required to be taken by the Purchaser to authorize the execution and delivery of this Agreement by the Purchaser in the performance of its obligations hereunder and has the financial ability to complete the Purchase and pay the Purchase Price.

(c) **Binding Agreement**. This Agreement has been duly executed by the Purchaser and will, upon delivery, constitute a valid and binding obligation of the Purchaser, enforceable against it in accordance with its terms, except as enforcement may be limited by bankruptcy, insolvency and other laws affecting the rights of creditors generally and except that equitable remedies may be granted only in the discretion of a court of competent jurisdiction.

(d) **No Violations**. Neither the execution nor delivery of this Agreement nor the completion of the transactions herein contemplated will result in the violation of:

(i) any provision of the constating documents, by laws or any unanimous shareholder agreement of the Purchaser;

(ii) any Contract to which the Purchaser is a party or by which the Purchaser or any of its property or assets is bound, which would have a material adverse effect on the Purchaser's ability to perform its obligations under this Agreement; or

(iii) subject to obtaining the regulatory approvals set forth in Article VII, any terms or provisions of any Applicable Law of any authority having jurisdiction over the Purchaser which would have a materially adverse effect on the Purchaser's ability to perform its obligations under this Agreement.

(e) **Investment Canada Act**. The Purchaser is not a "non-Canadian" within the meaning of the *Investment Canada Act* (Canada). The Purchaser is not a "non-resident" for tax purposes.

(f) **Financial Capability**. The Purchaser has sufficient funds in place to pay the Purchase Price on the Closing Date on the terms and conditions contained in this Agreement.

(g) **Consents and Approvals**. Except for the Required Approval, there is no requirement for the Purchaser to make any filing with, give any notice to or obtain any licence, permit, certificate, registration, authorization, consent or approval of, any governmental

or regulatory authority as a condition to the lawful consummation of the transactions contemplated by this Agreement.

(h) **Litigation**. There is no legal proceeding in progress, pending, threatened against or affecting the Purchaser and, to the best of the knowledge and belief of the Purchaser, there are no grounds on which any such legal proceeding might be commenced with any reasonable likelihood of success and no judgment, decree, injunction, ruling, order or award of any tribunal outstanding against or affecting the Purchaser which, in any such case, might adversely affect the ability of the Purchaser to enter into this Agreement or to perform its obligations hereunder.

(i) **Limitation**. The Purchaser makes no representation or warranty to the Vendor except as specifically set forth in this Section 3.2 and this Agreement contains all representations and warranties of the Purchaser relating to the transactions contemplated hereby.

(j) **Effect of Disclosure**. All disclosure contained in a particular representation and warranty set forth in this Agreement (or any Schedule referred to therein) shall be deemed for the purposes of this Agreement to have been made with respect to all of the representations and warranties in this Section 3.2 to which such disclosure might be applicable. Notwithstanding anything else contained herein, the Purchaser shall not have any liability to the Vendor with respect to any failure by it to disclose the existence of any matter, document or thing, or to make any other disclosure in the context of a particular representation and warranty set out in this Section 3.2 where the existence of such matter, document or thing has been disclosed as part of another representation or warranty contained in this Agreement or in any Schedule annexed hereto.

ARTICLE IV
SURVIVAL OF REPRESENTATIONS AND WARRANTIES

4.1 Survival of Representation and Warranties.

(a) The representations and warranties of the Vendor set out in Section 3.1 shall survive the Closing and, notwithstanding such Closing or any investigation made by or on behalf of the Purchaser with respect thereto, shall continue in full force and effect for the benefit of the Purchaser provided, however, that no Claim in respect thereof (other than with respect to representations and warranties regarding Taxes, for which the limitation period shall end six (6) months after the time that the taxation period ending on the Closing Date has become statute barred or for reassessment by the Tax authority, shall be valid unless it is made within a period of one (1) year from the Closing Date and, upon the expiry of such limitation period, the Vendor shall have no further liability to the Purchaser with respect to the representations and warranties referred to in such section, except in respect of Claims which have been made by the Purchaser to the Vendor in writing prior to the expiration of such period.

(b) The representations and warranties of the Purchaser set out in Section 3.2 shall survive the Closing and, notwithstanding such Closing or any investigation made by or on behalf of the Vendor with respect thereto, shall continue in full force and effect for the benefit of the Vendor provided, however, that no Claim in respect thereof shall be valid unless it is made within a period of one (1) year from the Closing Date and, upon the expiry of such limitation period, the Purchaser shall have no further liability to the Vendor with respect to the representations and warranties referred to in such section, except in respect of Claims which have been made by the Vendor to the Purchaser in writing prior to the expiration of such period.

ARTICLE V
COVENANTS OF THE VENDOR

5.1 **Access to the Corporation**. The Vendor shall forthwith make available to the Purchaser and its authorized Representatives in the Data Room copies of all title documents, Contracts, financial statements, policies, plans, reports, licences, orders, permits, books of account, accounting records and all other material documents, information and data, relating to the Business in the possession or control of the Vendor or the Corporation. The Vendor shall afford the Purchaser and its authorized Representatives access to the property of the Corporation upon written request and at least five (5) Business Days' prior written notice during the Corporation's normal business hours and provided that the Purchaser and its Representatives shall not impede the day to day operation of the Business. The Purchaser shall not undertake any drilling or subsurface investigations under any of the Property except with the prior approval of the Vendor, such approval to be granted in the discretion of the Vendor except that the Vendor may not withhold approval where there are reasonable grounds to suspect a change in the condition of the Property since the date of this Agreement and provided that no such investigation may unreasonably interfere with Vendor's operations. The Vendor and the Purchaser shall co-operate in good faith in arranging any confidential meetings as the Purchaser should reasonably request with senior executives of the Corporation employed in the Business.

5.2 **Conduct of Business Prior to Closing**. During the period from the date of the Initial Financial Statements to the Closing Date, the Vendor has caused and shall cause the Business of the Corporation to be conducted in the ordinary course substantially consistent with past practice (except as may be otherwise required or contemplated by the provisions of this Agreement), and shall not permit or authorize the Corporation to enter into new borrowing arrangements with financing having a term longer than thirty (30) days from Closing which financing may be made secured by a general security agreement, subject to Purchaser's approval acting reasonably or sell or otherwise dispose of any of its Property other than sales or dispositions of Property in the ordinary course not exceeding two hundred and fifty thousand dollars ($250,000) in the aggregate. The Corporation shall obtain Purchaser's prior written consent, which consent may be unreasonably withheld, to any Material Contract contemplated to be entered into following the Effective Date. During such period there shall be no change in the Business, operation, affairs, personnel and/or financial condition of the Corporation, except for changes occurring in the ordinary course of business which in aggregate would not reasonably be expected to have a Material Adverse Effect. The Parties further expressly acknowledge that, notwithstanding anything herein contained, during the period from execution of this Agreement to the Closing

Date, the Corporation shall be permitted to declare and pay dividends to the Vendor out of cash on hand.

5.3 **Delivery of Books and Records**.

(a) At Closing, the Vendor shall cause to be delivered to the Purchaser all of the books and records of and relating to the Corporation and the Business including at a minimum with respect to records supporting data required to be retained by the Tax authority, records for the past seven (7) years; and

(b) Notwithstanding Section 5.3(a), the Vendor shall be entitled to retain copies of any documents or other data delivered to the Purchaser pursuant to Section 5.3(a) provided that those documents are reasonably required by the City or the Vendor to perform its obligations hereunder or under Applicable Law.

5.4 **Resignation of Directors**. The Vendor shall cause all of the directors and officers of the Corporation to resign in favour of nominees of the Purchaser, such resignation to be effective at Closing and releases from such individuals of all claims they may have against the Corporation (other than in respect of unpaid salaries and accrued vacation pay).

5.5 **Transfer of Purchased Shares**. The City shall take, and shall cause the Vendor and the Corporation to take, all necessary steps and proceedings to permit the Purchased Shares to be duly and validly transferred to the Purchaser and to have such transfers duly and validly recorded on the books of the Corporation so that the Purchaser is entered onto the books of the Corporation as the holder of the Purchased Shares and to issue share certificates to the Purchaser representing the Purchased Shares.

5.6 **Non-Assignable Assets**. The Vendor and the City will use their respective best efforts to transfer any property used in the Business but held by the Vendor or the City to the Corporation (including obtaining any required third party consents) and in the absence of any such consent or effective transfer, Vendor or City as the case may be, shall hold such asset in trust for the benefit of the Corporation or as it may direct.

5.7 **Dispositions of Property**. The Vendor covenants and agrees that between the date of this Agreement and Closing, the Vendor shall not, and shall cause the Corporation not to transfer or acquire any Property unless it is the City Property or Property acquired from, or transferred to a person dealing at arm's length with the Vendor and its subsidiaries in the ordinary course of business.

5.8 **Debt to City**. The Vendor shall retire all of the Corporation's debt to the City on or prior to Closing, provided that the Vendor may obtain replacement financing as contemplated in Section 5.2.

5.9 **Special Payments to Employees**. Vendor shall cause the Corporation to pay out in full on or prior to Closing, all obligations of the Corporation for retention bonuses, change in control provisions and like obligations arising in connection with the employment of any person.

5.10 **Continued Pole Access**. For purposes of existing and future municipal attachments on hydro poles in the City of Orillia, the City will enter into a joint use agreement with each of HONI and the Purchaser in accordance with the terms of HONI's applicable standard document, Agreement for Licensed Occupancy of Power Utility Distribution Poles Rates. Vendor will provide an inventory of municipal attachments to the Distribution Facilities, on Closing.

5.11 **15 Industrial Street Easements.** On or prior to Closing, the City shall grant the Corporation and register on title, the following easements in favour of the Corporation on terms which are assignable to HONI, in form and content satisfactory to the City and the Purchaser acting reasonably:

(a) an easement for electrical distribution over Part 2, on a draft reference plan prepared by Dearden and Stanton Ltd., Ontario Land Surveyors dated July 21, 2016 (CAD File: RF26926/D-2711, revised August 9, 2016);

(b) an easement for ingress and egress over Part 8 on a draft reference plan prepared by Dearden and Stanton Ltd., Ontario Land Surveyors dated July 21, 2016 (CAD File: RF26926/D-2711, revised August 9, 2016); and

(c) an easement for electrical distribution and ingress and egress over Part 5 on a draft reference plan prepared by Dearden and Stanton Ltd., Ontario Land Surveyors dated July 21, 2016 (CAD File: RF26926/D-2711, revised August 9, 2016).

5.12 **15 Industrial Street License Agreement.** Prior to Closing, the Corporation is permitted to enter into a license agreement on terms satisfactory to the Purchaser and the relevant parties, acting reasonably, between the Corporation, Ontario Provincial Police, Orillia Power Generation Corporation and if required, the City, relating to the use of a telecommunications tower and related equipment (including anchors and guy wires) at 15 Industrial Street, Orillia, used by Ontario Provincial Police, Orillia Power Generation Corporation, and as the case may be, the City, relating to a joint use agreement dated November 1997.

5.13 **306 Peter Street North License Agreement.** Prior to Closing, the Corporation is permitted to enter into a license agreement with Orillia Power Generation Corporation (in favour of Orillia Power Generation Corporation as licensee) relating to telecommunications equipment currently situated within the fenced in substation portion of the lands at 306 Peter Street North, on terms requiring the relocation of such telecommunications equipment to a mutually acceptable location outside of the fenced in portion of the substation lands and otherwise on terms satisfactory to the Purchaser and Orillia Power Generation Corporation, acting reasonably .

ARTICLE VI
COVENANTS OF THE PURCHASER

6.1 **Employment and Location Guarantee.** The Purchaser hereby covenants and agrees that for a period of at least one (1) year following the Closing Date, it will, subject to its rights to dismiss for just cause, guarantee the continued employment with the Corporation, Purchaser, HONI or other Affiliate of the Purchaser, in Orillia, Ontario, of each Employee who is an active Employee of the Corporation on the Closing Date, i) on the same or similar terms and conditions including Employee Plans of their current employment for so long as they remain employed by

the Corporation, and ii) as of their date of transfer to HONI, calculated on the same basis as provided to employees hired by HONI on the transfer date, except that service with the Corporation will be recognized as service with the Purchaser and HONI for seniority purposes. The foregoing shall not prohibit the relocation of Employees with their prior consent. From and after the date on which the Purchaser integrates the Business within HONI, Employees may apply for positions within the Purchaser and its Affiliates and will be considered for such positions on a fair and equal basis with other employees of the Purchaser and its Affiliates. In order to receive credit for their seniority and service with the Corporation in such application, the Employee must waive the benefit of the location guarantee from and after the application date.

6.2 **Participation in Community Events**. After Closing, the community shall be eligible for the benefits of HONI's community programs as described in Schedule 6.2.

6.3 **Advisory Committee**. The Purchaser shall establish an advisory committee (the "**Advisory Committee**") as soon as practicable after Closing to provide a forum for communication between the Purchaser and the community. In establishing the Advisory Committee, the Purchaser shall select one (1) senior HONI employee and one (1) local HONI employee as its Representatives, in consultation with officials of the Vendor. The Vendor has the right to appoint at least three (3) community members to the Advisory Committee.

6.4 **Transfer of City Property**. The Purchaser acknowledges and agrees that the real property set out in Schedule 6.4 and all associated obligations associated with this real property (the "**City Property**"), shall be transferred by the Corporation to the City prior to Closing.

6.5 **Employee-Related Matters**. The Purchaser acknowledges that from and after Closing, it shall be responsible for all obligations owing to present and former employees, and the employees' respective beneficiaries of the Corporation and their predecessors and of the Business relating to such employment, including all obligations and liabilities relating to wages, severance pay, notice of termination of employment or pay in lieu of such notice, damages for wrongful dismissal or other employee benefits or claims, including vacation pay, and Employee Plans (but excluding in respect of or in connection with OMERS) regardless of whether these arose before or after Closing. From and after the Time of Closing the Purchaser shall indemnify and save harmless the Vendor from and against any and all losses, damages, expenses, liabilities, claims and demands whatsoever made or brought against the Vendor by any person or Employee, association or trade union or by any Governmental Authority or any other Person or body which in any way pertains to or arises out of such liability including, without limiting the generality of the foregoing, any and all losses, damages, expenses, liabilities, claims and demands whatsoever with respect to wages, severance pay, notice of termination of employment or pay in lieu of such notice, damages for wrongful dismissal or other employee benefits or claims, including vacation pay, and Employee Plans and including any interest, award, judgment or penalty relating thereto and any costs or expenses incurred by the Vendor in defending any such claim or demand. For greater certainty, nothing in this Section 6.5 releases Vendor from its obligations under this agreement including with respect to disclosures and representations and warranties regarding employees and liabilities.

6.6 **Rate Rider**.

(a) Notwithstanding Section 2.6, the Purchaser acknowledges, agrees and covenants to:

(i) within the time frame specified in Section 7.1 and as part of the Required Approval, seek OEB approval for a negative rate rider to reduce Current Rates by one percent (1%) across all Rate Classes ("**Negative Rate Rider**"); and

(ii) request that the Reduced Rates shall:

(A) be effective immediately following Closing or as approved by the OEB, whichever is later; and

(B) be maintained without change during the Rate Freeze Period.

(b) If the OEB does not approve the Negative Rate Rider in accordance with Subsection 6.6(a), and does not approve a Partial Rate Rider, the Purchaser acknowledges, agrees and covenants to maintain Rates at Current Rates during the Rate Freeze Period. For greater clarity, this subsection 6.6(b) shall not affect the obligations of the Purchaser under Section 2.6 which are in addition to the Purchaser's obligations under this Section 6.6(b).

6.7 **Existing Customer Rebates.** Notwithstanding Sections 2.6, 6.6(a) and 6.6(b), the Purchaser acknowledges, agrees and covenants that it will apply to the OEB in a timely manner in 2017 for a rate adder to dispose of the balance in account 1576 ("**Account 1576**") as of December 31, 2016, which adder will be effective January 1, 2018 to December 31, 2018, and that it will make a similar application in 2018 for the disposition of the balance in account 1576 as of December 31, 2017 of the preceding year if that balance is in excess of eighty thousand dollars ($80,000). More particularly, the Purchaser will seek OEB approval of a rate adder similar to that sought by the Corporation and approved by the OEB in OEB File No. EB-2015-0286, being an application to establish a rate adder, effective January 1, 2016, to dispose of the balance in OEB Account 1576 as of December 31, 2014

6.8 **Smart Grid, Conservation and Demand Management**. Following Closing, the Purchaser will place continued importance on smart grid development and conservation and demand management initiatives in the operations of the Corporation or any successor by integrating such matters into its capital program and performance of service standards contemplated (reference).

6.9 **Books and Records**. The Purchaser shall preserve the books and records delivered by the Vendor to it pursuant to Section 5.3 for a period of eight (8) years from the Closing Date, or for such longer period as is required by any Applicable Law, and will permit the Vendor or its authorized Representatives reasonable access thereto in connection with the affairs of the Vendor relating to its matters.

6.10 **Confidentiality**.

(a) Each Party hereby covenants and agrees that it shall keep confidential and not use (except for the purposes of the Transaction) or disclose except as required by Applicable Law, any and all information received by it from another Party leading up to or in connection with the execution of this Agreement and completion of the transactions contemplated hereby, whether or not received prior to or after the Effective Date, concerning the business and affairs of the other Party or its Affiliates.

(b) In the event that this Agreement is terminated in accordance with the provisions hereof,

(i) the Purchaser hereby covenants and agrees that it, and its Affiliates, shall keep confidential, in accordance with the terms of the Confidentiality Agreement, any and all information and trade secrets received by the Purchaser from the Vendor, whether or not received prior to or after the date of this Agreement, concerning the business and affairs of the Vendor and/or the Corporation (the "**Confidential Information**").

(ii) the Purchaser shall:

(A) promptly return to the Vendor all documents, computer disks, other forms of electronic storage or other materials furnished by the Vendor, or the Corporation or by any of their respective Representatives to the Purchaser or its Representatives constituting Confidential Information, together with all copies and summaries thereof in the possession or under the control of the Purchaser or its Representatives and materials generated by the Purchaser or its Representatives that include or refer to any part of the Confidential Information, without retaining a copy of any such material; or

(B) alternatively, provided that the prior written consent of the Vendor has been obtained, promptly destroy all documents or other matters constituting Confidential Information in the possession or under the control of the Purchaser or its Representatives;

and the Purchaser shall confirm such return and/or destruction of Confidential Information to the Vendor in writing and certified by two senior officers of the Purchaser;

(iii) the Purchaser shall promptly destroy the portion of the Confidential Information which consist of analyses, compilations, forecasts, studies, other material or documents prepared by the Purchaser or its Representatives and shall confirm such destruction in writing and certified by two senior officers of the Purchaser;

(iv) any oral or visual Confidential Information will continue to be subject to the terms of the Confidentiality Agreement and the terms of this Section 6.10; and

(v) the Purchaser shall not, directly, use for its own purposes, any Confidential Information discovered or acquired by the Purchaser's Representatives as a result of the Vendor, or the Corporation making available to them any Confidential Information.

6.11 **Industrial Street Substation**. In the event Purchaser desires to dispose of all or part of the real property received as part of the Transaction in connection with the Industrial St. substation, the Vendor shall be offered a first right of refusal to purchase the lands at fair market value, valued as if free from contamination, notice of which interest is permitted to be registered on title to the property.

6.12 **Survival**. The covenants contained in this Article VI shall survive the Closing Date.

ARTICLE VII
REQUIRED APPROVAL

7.1 **OEB Approval**. Each of the Purchaser and the Vendor shall as promptly as practicable after the execution of this Agreement (but in no event later than forty five (45) days after the execution of this Agreement), file or cause to be filed with the OEB an application required to be made under Subsection 86(1) and Subsection 86(2) of the *OEB Act* in respect of the OEB Approval as it relates to the sale of the Corporation to the Purchaser and the acquisition from the Purchaser of all or substantially all of Corporation's assets by Hydro One Networks Inc. (the "**Required Approval**"). Each of the Purchaser and the Vendor shall use their best efforts (which shall not be less than commercially reasonable efforts) to cooperate and assist the other, so that the Required Approval can be obtained as soon as reasonably possible, and in any event prior to the Closing Date. All the costs and expenses incurred by the Parties in connection with the application for the OEB Approval shall be borne each Party.

7.2 **Ontario Minister of Finance Notice**. The Vendor and the Corporation each shall as promptly as practicable after the execution of this Agreement (but in no event later than the day before the Closing Date), file or cause to be filed with the Ontario Minister of Finance the notification required under Subsection 4(2) of Ontario Regulation 124/99 made under the EA. If necessary, the Vendor will also file or cause to be filed with the Ontario Minister of Finance such notification as required by Applicable Law within thirty (30) days after the Closing Date.

ARTICLE VIII
TAX MATTERS

8.1 **Preparation and Filing of Tax Returns**. The Vendor shall prepare and submit on behalf of the Corporation all Tax Returns that are not due for filing until after the Closing Date to the Purchaser for approval at least thirty (30) Business Days before the filing due date thereof except for the debt retirement charge and sales tax returns, which shall be prepared and submitted to the Purchaser for approval at least seven (7) Business Days before the filing due date thereof. The Purchaser shall provide the Vendor and its Representatives access to such books and records of the Corporation relating to the period preceding Closing as the Vendor reasonably request for purposes of preparing those Tax Returns. After the Purchaser has approved those Tax Returns (which the Purchaser must approve provided that the Tax Returns

are in compliance with Applicable Law and consistent with past practice of the Corporation), the Purchaser shall, on a timely basis, cause the Corporation to file the Tax Returns, and provide a copy with proof of filing to the Purchaser.

8.2 **Books and Records Relating to Taxes**. Within thirty (30) Business Days after the Closing Date, the Vendor and the City shall deliver to the Purchaser the copies of all documents relating to Taxes of the Corporation in respect of the period preceding Closing that the Vendor retained pursuant to Section 5.3(b) and all working papers, correspondence and other documents prepared after the Closing Date which relate to Taxes for such periods.

8.3 **Notification Requirements**. The Purchaser shall promptly forward to the Vendor all written notifications and other written communications from any Governmental Authority received by the Purchaser or the Corporation relating to Taxes of the Corporation for all periods preceding Closing, and shall promptly inform the Vendor of any audit proposed to be undertaken and any adjustment proposed in writing to be made by any Governmental Authority in respect of a Pre Closing Period. Notwithstanding the obligation of the Purchaser to give prompt notice as required above, the failure of the Purchaser to give that prompt notice shall not relieve the Vendor of its obligations under this Article VIII except to the extent (if any) that the Vendor shall have been prejudiced thereby.

8.4 **Vendor Indemnification**.

From and after the Closing Date, the Vendor shall be responsible for and shall indemnify and save harmless the Purchaser for all Taxes payable by the Corporation for all such periods that are a Pre-Closing Tax Period (and except to the extent such Taxes payable are recorded as a current liability on the Closing Date Financial Statements). The Purchaser shall pay to the Vendor as an increase in the purchase price any Tax refunds received by or credited to the Corporation after the Closing Date provided that such Tax refunds and credits relate a Pre-Closing Tax Period (and except to the extent that such Tax refunds and credits have been recorded as a current asset on the Closing Date Financial Statements).

8.5 **Purchaser’s Contest Rights**. Subject to Section 8.6, the Purchaser shall have the sole right to control, defend, settle, compromise, or prosecute in any manner an audit, examination, investigation, and other proceeding with respect to any Tax Return of the Corporation. The Purchaser shall keep the Vendor duly informed of any proceedings in connection with any matter for which the Purchaser may have a right to indemnification pursuant to this Article VIII or Article XII and promptly provide the Vendor with copies of all correspondence and documents relating to those proceedings. The Vendor shall execute or cause to be executed such documents and shall take such action as reasonably requested by the Purchaser to enable the Purchaser to take any action the Purchaser deems appropriate with respect to any proceedings in respect of which the Purchaser has contest rights under this Agreement.

8.6 **Vendor’s Contest Rights**.

(a) The Vendor may at any time by written notice to the Purchaser elect to control, defend, settle, compromise or prosecute in any manner an audit, examination, investigation, or other proceeding with respect to Taxes or Tax issues related to any matter in respect of

which the Purchaser may have a right of indemnification pursuant to this Article VIII or Article XII, except that:

(i) the Vendor shall deliver to the Purchaser a written agreement that the Purchaser is entitled to indemnification for all Losses arising out of that audit, examination or other proceeding and that the Vendor shall be liable for the entire amount of those Losses;

(ii) the Vendor may not, without the written consent of the Purchaser, settle or compromise Taxes or Tax issues related to any matter which may affect Tax liabilities of the Corporation for a period following Closing; and

(iii) the Vendor shall pay to the Purchaser the amount of all Taxes (including, for greater certainty, interest and penalties) specified in the notice of assessment or other Claim from the Governmental Authority which are due and payable and to which the Purchaser's indemnity Claim relates within ten (10) Business Days before the amount is required to be paid to the Governmental Authority or within ten (10) Business Days after the Purchaser has forwarded to the Vendor a Claim for indemnity.

(b) If the consent of the Purchaser to a settlement or compromise arranged by the Vendor is not obtained for any reason, the indemnification liability of the Vendor shall be limited to the proposed settlement amount. The Purchaser and/or the Corporation, as applicable, shall execute or cause to be executed such documents or take such action as reasonably requested by the Vendor to enable the Vendor to take any action it deems appropriate with respect to any proceedings in respect of which the Vendor has contest rights under this Agreement. In addition:

(i) the Vendor shall keep the Purchaser duly informed of any proceedings in connection with any matter which may affect the Taxes payable by the Purchaser or the Corporation; and

(ii) the Purchaser shall be promptly provided with copies of all correspondence and documents relating to those proceedings and may, at its option and its own expense, participate in those proceedings through counsel of its choice.

8.7 **Indemnification Procedures**. Except to the extent expressly provided to the contrary in this Article VIII, the general procedures regarding notice and pursuit of indemnification Claims set forth in Article XII shall apply to all Claims for indemnification made under this Article VIII, except that notwithstanding any provision of Article XII to the contrary, if a Claim for indemnification involves any matter covered in this Article VIII, then the contest provisions of Sections 8.5 and 8.6, as applicable, shall control regarding the defence and handling of any such third party Claim that could give rise to an indemnification obligation on the part of the Vendor. Notwithstanding Article IV, the time period during which a Claim for indemnification may be made under this Article VIII or Section 3.1(u) shall survive Closing and continue in full force and effect until, but not beyond, the one hundred and eightieth (180th) day following the expiration of the period, if any, during which an assessment, reassessment or other form of

recognized document assessing liability for Taxes under applicable Tax legislation in respect of any taxation year to which those representations and warranties and provisions under this Article VIII and Section 3.1(v) could be issued under that Tax legislation to the Corporation. Claims for indemnification regarding Tax matters shall not be subject to the limits set out in Article XII.

ARTICLE IX
CONDITIONS OF CLOSING

9.1 **Conditions of Closing in Favour of the Purchaser**. The Transaction including sale and purchase of the Purchased Shares are subject to the following conditions for the exclusive benefit of the Purchaser, to be fulfilled or performed at or prior to Closing:

(a) **Representations and Warranties**. The representations and warranties of the Vendor contained in this Agreement which are qualified as to materiality shall be true and correct and those not qualified as to materiality shall be true and correct in all material respects at Closing, with the same force and effect as if such representations and warranties were made at and as of such time, and a certificate of two (2) senior officers of the Vendor dated the Closing Date to that effect shall have been delivered to the Purchaser.

(b) **Covenants**. All of the obligations, covenants and agreements contained in this Agreement to be complied with or performed by the Vendor at or prior to Closing shall have been complied with or performed, and a certificate of two (2) senior officers of the Vendor dated the Closing Date to that effect shall have been delivered to the Purchaser.

(c) **Consents and Required Approval**. There shall have been obtained, from all appropriate Persons such consents as listed in Schedule 9.1(c), as may be required in connection with the completion of the Transaction, including without limitation, the Required Approval.

(d) **No Action to Restrain**. No order of any court of competent jurisdiction or administrative agency shall be in existence and, no action or proceeding shall be pending or threatened in writing by any Person, to restrain or prohibit:

(i) the purchase and sale of the Purchased Shares; or

(ii) any of the Corporation from carrying on the Business as the Business is being carried on as at the date hereof.

(e) **Material Adverse Effect**. There shall not have occurred any Material Adverse Effect since the date of this Agreement.

(f) **Resignation of Directors**. All directors and officers of the Corporation shall have tendered their resignations and each such individual and the Vendor shall have duly executed and delivered comprehensive releases of all their claims (other than in respect of unpaid salaries and accrued vacation pay and rights to indemnity) respectively against the Corporation.

(g) **No Transfer Tax Payable**. Neither the Vendor nor the City shall be liable for transfer tax, imposed under section 94 of the EA or similar legislation under any successor statute, in relation to the sale or purchase of the Purchased Shares.

If any of the conditions contained in this Section 9.1 shall not be performed or fulfilled at or prior to the Closing or any other timeframe specified above to the satisfaction of the Purchaser, acting reasonably, the Purchaser may, by notice to the Vendor, terminate this Agreement and the obligations of the Vendor and the Purchaser under this Agreement, or if the Vendor terminates this Agreement because of a failure of conditions 9.1(c) or (d) or because the Vendor or City would be liable for transfer tax in relation to the sale of the Purchased Shares, then in any such event the Purchaser shall be released from all obligations hereunder except those set forth in Section 6.10 and in the Confidentiality Agreement and the Vendor shall direct the Vendor's solicitor to refund the Deposit and all accrued interest thereon to the Purchaser and Purchaser shall be released from all obligations hereunder. Any such condition may be waived in whole or in part by the Purchaser without prejudice to any claims it may have for breach of such condition.

9.2 **Conditions of Closing in Favour of the Vendor**. The purchase and sale of the Purchased Shares is subject to the following terms and conditions for the exclusive benefit of the Vendor, to be fulfilled or performed at or prior to Closing:

(a) **Representations and Warranties**. The representations and warranties of the Purchaser contained in this Agreement which are qualified as to materiality shall be true and correct and those not qualified as to materiality shall be true and correct in all material respects at Closing, with the same force and effect as if such representations and warranties were made at and as of such time, and a certificate of two (2) senior officers of the Purchaser dated the Closing Date to that effect shall have been delivered to the Purchaser.

(b) **Covenants**. All of the obligations, covenants, and agreements contained in this Agreement to be complied with or performed by the Purchaser at or prior to Closing shall have been complied with or performed, and a certificate of a senior officers of the Purchaser dated the Closing Date to that effect shall have been delivered to the Vendor.

(c) **Consents and Required Approval**. There shall have been obtained, from all appropriate Persons such consents as listed in Schedule 9.2(c), as may be required in connection with the completion of the Transaction, including without limitation, the Required Approval.

(d) **No Action to Restrain**. No order of any court of competent jurisdiction or administrative agency shall be in existence and, no action or proceeding shall be pending or threatened in writing by any Person, to restrain or prohibit the purchase of the Purchased Shares.

(e) **No Transfer Tax Payable**. Neither the Vendor nor the City shall be liable for transfer tax, imposed under section 94 of the EA or similar legislation under any successor statute, in relation to the sale of the Purchased Shares.

If any of the conditions in this Section 9.2 shall not be performed or fulfilled at or prior to Closing to the satisfaction of the Vendor, acting reasonably, the Vendor may, by notice to the Purchaser, terminate this Agreement and the obligations of the Vendor and the Purchaser under this Agreement, and in such event the Vendor shall be released from all obligations hereunder except those set forth in the Confidentiality Agreement and the Vendor shall be entitled to the Deposit and accrued interest thereon only in circumstances resulting in termination for failure of performance or fulfillment by the Purchaser of the conditions listed in Section 9.2(a) and 9.2(b), as its sole and exclusive remedy for all matters arising out of this Agreement and Purchaser shall be released from all obligations hereunder. In the event of termination for failure of any other condition in Section 9.2, the Purchaser shall be entitled to the Deposit and accrued interest as if there was a failure of a condition in Section 9.1. Any such condition may be waived in whole or in part by the Vendor without prejudice to any Claims it may have for breach of such condition.

ARTICLE X
CLOSING ARRANGEMENTS

10.1 **Place of Closing**. The closing shall take place on the Closing Date at the offices of the Purchaser at Toronto, Ontario.

10.2 **Transfer**. On Closing, upon fulfilment of all the conditions set out in Article IX that have not been waived in writing by the Purchaser or the Vendor, the Vendor shall deliver to the Purchaser certificates representing all the Purchased Shares, duly endorsed in blank for transfer and will cause transfers of such shares to be duly and regularly recorded in the name of the Purchaser whereupon, subject to all other terms and conditions hereof being complied with, payment of the Purchase Price shall be paid and satisfied in the manner provided in Article II.

ARTICLE XI
ARBITRATION

11.1 **Arbitration**.

(a) Any dispute, controversy or claim arising out of or in connection with, or relating to, this Agreement, including the Confidentiality Agreement, or the performance, breach, termination or validity thereof, shall be finally settled by arbitration. Either Party may initiate arbitration within a reasonable time after any such dispute, controversy or claim has arisen, by delivering a written demand for arbitration upon the other Party. The arbitration shall be conducted in accordance with the *Arbitration Act*, 1991 (Ontario). The arbitration shall take place in Toronto, Ontario, and shall be conducted in English.

(b) The arbitration shall be conducted by a single arbitrator having no financial or personal interest in the outcome of the arbitration. The arbitrator shall be appointed jointly by agreement of the Parties. In the event the Parties are unable to agree on the appointment of the arbitrator within ten (10) days after notice of a demand for arbitration is given by either Party, then either Party shall be free to apply to the Superior Court of Ontario for an Order appointing the arbitrator. Absent agreement or an award in the arbitration to the contrary, the arbitration fees and expenses shall be paid by the Parties jointly.

(c) The arbitrator shall have the authority to award any remedy or relief that a court could order or grant in accordance with this Agreement, including, without limitation, specific performance of any obligation created under this Agreement, the issuance of an interim, interlocutory or permanent injunction, or the imposition of sanctions for abuse or frustration of the arbitration process.

(d) The arbitral award shall be in writing, stating the reasons for the award and be final and binding on the Parties with no rights of appeal. The award may include an award of costs, including reasonable legal fees and disbursements and fees and expenses of the arbitrator. Judgment upon the award may be entered by any court having jurisdiction thereof or having jurisdiction over the relevant Party or its assets.

ARTICLE XII
INDEMNIFICATION

12.1 **Indemnification by the Vendor**. Subject to the limitations contained in Section 4.1 respecting survival of the representations and warranties of the Parties and to Sections 12.5 and 12.7, the Vendor covenants and agrees to indemnify and save harmless the Purchaser and its Affiliates (the "**Purchaser Indemnified Parties**") effective as and from the Closing Time, from all Losses suffered by a Purchaser Indemnified Party as a result of all Claims which may be made or brought against a Purchaser Indemnified Party, including Claims or Losses suffered by a Purchaser Indemnified (or made or brought by a Purchaser Indemnified Party against the Vendor pursuant to this Agreement) or the Corporation as a result of or arising directly or indirectly out of or in connection with:

(a) any breach by the Vendor of or any inaccuracy of any representation or warranty contained in this Agreement or in any agreement, instrument, certificate or other document delivered pursuant hereto;

(b) any breach or non-performance by the Vendor of any covenant to be performed by it that is contained in this Agreement or in any agreement, certificate or other document delivered pursuant hereto; and

(c) any Claim or Losses in connection with the Corporation or the Business to the extent the circumstances giving rise thereto arose on or prior to Closing.

12.2 **Indemnification by the Purchaser**. Subject to the limitations contained in Section 4.1 respecting survival of the representations and warranties of the Parties and to Section 12.5 and 12.7, the Purchaser agrees to indemnify and save harmless the Vendor from all Losses suffered or incurred by the Vendor as a result of or arising directly or indirectly out of or in connection with any Claim relating to:

(a) any breach by the Purchaser of or any inaccuracy of any representation or warranty contained in this Agreement or in any agreement, instrument, certificate or other document delivered pursuant hereto;

(b) any breach or non-performance by the Purchaser of any covenant to be performed by it that is contained in this Agreement or in any agreement, certificate or other document delivered pursuant hereto; and

(c) the operations of the Business and the ownership of the Purchased Shares in respect of the period after Closing.

12.3 **Notice of Claim**. In the event that a Party (the "**Indemnified Party**") shall become aware of any Claim in respect of which the other Party (the "**Indemnifying Party**") agreed to indemnify the Indemnified Party pursuant to this Agreement, the Indemnified Party shall promptly give written notice thereof to the Indemnifying Party. Such notice shall specify whether the Claim arises as a result of a claim by a third party (a "**Third Party**") against the Indemnified Party (a "**Third Party Claim**") or whether the Claim does not so arise (a "**Direct Claim**"), and shall also specify with reasonable particularity (to the extent that the information is available):

(a) the factual basis for the Claim; and

(b) the amount of the Claim, if known.

If, through the fault of the Indemnified Party, the Indemnifying Party does not receive notice of any Claim in time to effectively contest the determination of any liability susceptible of being contested, the Indemnifying Party shall be entitled to set off against the amount claimed by the Indemnified Party the amount of any Losses incurred by the Indemnifying Party resulting from the Indemnified Party's failure to give such notice on a timely basis.

12.4 **Direct Claims**. With respect to any Direct Claim, following receipt of notice from the Indemnified Party of the Claim, the Indemnifying Party shall have thirty (30) days to make such investigation of the Claim as is considered necessary or desirable. For the purpose of such investigation, the Indemnified Party shall make available to the Indemnifying Party the information relied upon by the Indemnified Party to substantiate the Claim, together with all such other information as the Indemnifying Party may reasonably request. If both parties agree at or prior to the expiration of such thirty (30) day period (or any mutually agreed upon extension thereof) to the validity and amount of such Claim, the Indemnifying Party shall immediately pay to the Indemnified Party the full agreed upon amount of the Claim, failing which the matter shall be referred to binding arbitration in such manner as the parties may agree or shall be determined by a court of competent jurisdiction.

12.5 **Third Party Claims**. With respect to any Third Party Claim, the Indemnifying Party shall have the right, at its expense, to participate in or assume control of the negotiation, settlement or defence of the Claim and, in such event, the Indemnifying Party shall reimburse the Indemnified Party for all the Indemnified Party's out of pocket expenses as a result of such participation or assumption. If the Indemnifying Party elects to assume such control, the Indemnified Party shall have the right to participate in the negotiation, settlement or defence of such Third Party Claim and to retain counsel to act on its behalf, provided that the fees and disbursements of such counsel shall be paid by the Indemnified Party unless the Indemnifying Party consents to the retention of such counsel or unless the named parties to any action or

proceeding include both the Indemnifying Party and the Indemnified Party and a representation of both the Indemnifying Party and the Indemnified Party by the same counsel would be inappropriate due to the actual or potential differing interests between them (such as the availability of different defences). If the Indemnifying Party, having elected to assume such control, thereafter fails to defend the Third Party Claim within a reasonable time, the Indemnified Party shall be entitled to assume such control and the Indemnifying Party shall be bound by the results obtained by the Indemnified Party with respect to such Third Party Claim. If any Third Party Claim is of a nature such that the Indemnified Party is required by applicable law to make a payment to any Third Party with respect to the Third Party Claim before the completion of settlement negotiations or related legal proceedings, the Indemnified Party may make such payment and the Indemnifying Party shall, forthwith after demand by the Indemnified Party, reimburse the Indemnified Party for such payment. If the amount of any liability of the Indemnified Party under the Third Party Claim in respect of which such a payment was made, as finally determined, is less than the amount that was paid by the Indemnifying Party to the Indemnified Party, the Indemnified Party shall, forthwith after receipt of the difference from the Third Party, pay the amount of such difference to the Indemnifying Party.

12.6 **Settlement of Third Party Claims**. If the Indemnifying Party fails to assume control of the defence of any Third Party Claim, the Indemnified Party shall have the exclusive right to contest, settle or pay the amount claimed. Whether or not the Indemnifying Party assumes control of the negotiation, settlement or defence of any Third Party Claim, the Indemnifying Party shall not settle any Third Party Claim without the written consent of the Indemnified Party, which consent shall not be unreasonably withheld or delayed; provided, however, that the liability of the Indemnifying Party shall be limited to the proposed settlement amount if any such consent is not obtained for any reason.

12.7 **Limitation on Claims**.

(a) Subject to Section 8.7 and notwithstanding Sections 12.1 and 12.2:

(i) no Claim for indemnification hereunder may be made by the Purchaser against the Vendor, except for breach of a covenant contained in Article V, until the aggregate amount of Claims in respect of which the Purchaser may so claim exceeds three million dollars ($3,000,000) (the "**Deductible**"), and then only for the amount of any Claims exceeding the Deductible;

(ii) the maximum aggregate amount of indemnification exceeding the Deductible which may be payable by the Vendor under this Agreement for matters other than breach of covenant contained in Article V or Taxes, shall not exceed an aggregate of three million dollars ($3,000,000), for any reason whatsoever; and

(iii) if any payment made pursuant to this Article XII is subject to HST (or other applicable Tax) or is deemed by Applicable Law to be inclusive of HST (or other applicable Tax), the Indemnifying Party shall pay to the Indemnified Party an amount equal to the HST (or other applicable Tax) in connection with the payment and any additional amount hereunder.

(b) Neither Party shall be required to indemnify or save harmless the other Party in respect of any breach or inaccuracy of any representation or warranty made under Article III (except with respect to Section 3.1(x) TAX) unless notice is provided by the Indemnified Party to the Indemnifying Party in accordance with Section 12.3 on or prior to the expiration of the applicable time period related to such representation and warranty as set out in Article XII.

(c) The Indemnifying Party shall only be liable for Losses suffered by the Indemnified Party in respect of a Claim after taking into account:

(i) insurance proceeds received by the Indemnified Party in respect of the occurrence giving rise to the Claim; and

(ii) Tax benefits accruing to the Indemnified Party relating to the actions taken by the Indemnified Party in respect of the Claim.

12.8 **Exclusivity**. The provisions of this Article XII shall apply, subject to Article VIII, to any Claim for or in respect of any breach of any covenant, representation, warranty, indemnity or other provision of this Agreement or any agreement, certificate or other document delivered pursuant to this Agreement (other than a claim for specific performance or injunctive relief) with the intent that all such Claims shall be subject to the limitations and other provisions contained in this Article XII except as otherwise expressly set out.

12.9 **Special Indemnities**. The Vendor shall indemnify the Purchaser and its affiliates with respect to the following matters and shall provide such indemnity in a stand-alone form on Closing:

(a) Losses related to having formerly held registered title to or occupied the City Property;

(b) Losses associated with operations from 15 Industrial St. prior to Closing or with adverse environmental conditions in or around the property originating prior to Closing, such indemnity limited to Losses discovered within 10 years of Closing;

(c) Losses associated with the presence of chlorinated solvent known to exist in or near 188 Jarvis St.

(d) Losses associated with claims made against the Corporation arising from the transfer to the Corporation of obligations of Orillia Water Light and Power pursuant to transfer by-laws made pursuant to the EA; and

(e) With respect to the absence of valid and enforceable customary easement rights in perpetuity for Distribution Facilities (excluding stations) located on property other than the public road allowance, the cost of obtaining such easement rights according to Purchaser's schedule of costs or if Purchaser is unable to obtain such rights at such price despite reasonable good faith efforts, the cost of relocating the plant and obtaining such easement rights in the new location, provided that before relying on this indemnity, Purchaser shall apply to the OEB for a regulatory deferral account specific to the amounts for which Purchaser would otherwise be so indemnified pursuant

hereto, and if successful, Vendor's obligation to indemnify shall be limited to amounts not permitted to be included in the account and amounts accruing in such deferral account but not dispositioned as a rate rider to be recovered after the ten year period following Closing. Purchaser may rely on this indemnity only to the extent Purchaser has not initiated discussions to rectify the Distribution Facility occupancy with the property owner. This indemnity obligation shall terminate ten years following Closing.

Notwithstanding any other provision of this Agreement, the provisions of Section 12.7 shall not apply to indemnities under this Section 12.9. For greater certainty, the guarantee of the City shall apply to performance of this indemnity obligation.

12.10 **Duty to Mitigate**. Nothing in this Agreement in any way restricts or limits the obligation under Applicable Laws of an indemnified party to mitigate any loss which it may suffer or incur by reason of any breach by an indemnifying party of any representation, warranty, covenant or obligation of the indemnifying party under this Agreement.

ARTICLE XIII
MISCELLANEOUS

13.1 **Further Assurances**. Each Party to this Agreement covenants and agrees that, from time to time subsequent to the Closing Date, it will, at the request and expense of the requesting Party, execute and deliver all such documents, including, without limitation, all such additional conveyances, transfers, consents and other assurances and do all such other acts and things as any other party hereto, acting reasonably, may from time to time request be executed or done in order to better evidence or perfect or effectuate any provision of this Agreement or of any agreement or other document executed pursuant to this Agreement or any of the respective obligations intended to be created hereby or thereby.

13.2 **Announcements**. The Parties shall make a joint public announcement with respect to this Agreement and the transactions herein contemplated, at such time and in such manner as may be mutually agreed upon by the Parties. Except as required by law, no other public announcement, press release, notices, statements and communications to third parties shall be made by either Party hereto without the prior consent and approval of the other Party, provided that the Parties hereby acknowledge that the Parties may be compelled to disclose details of this Agreement and the Transactions contemplated herein in respect of the OEB Approval and that the Vendor or the Purchaser may be compelled to disclose details of this Agreement and the Transactions herein contemplated pursuant to the *Municipal Freedom of Information and Protection of Privacy Act* (Ontario) or the *Freedom of Information and Protection of Privacy Act* (Ontario).

13.3 **Brokerage, Commissions, etc**. It is understood and agreed that no broker, agent or other intermediary has acted for the Vendor, the City, the Corporation or the Purchaser, in connection with the transaction herein contemplated. The Vendor agrees to indemnify and save harmless the Purchaser from and against any claim for commission or other remuneration payable or alleged to be payable to any broker, agent or other intermediary who purports to act or to have acted for the Vendor or the City in connection with the transactions herein contemplated.

The Purchaser agrees to indemnify and save harmless the Vendor from and against any claim for commission or other remuneration payable or alleged to be payable to any broker, agent or other intermediary, who purports to act or to have acted for the Purchaser in connection with the transactions herein contemplated.

13.4 **Notices**.

(a) Any notice or other communication required or permitted to be given hereunder shall be in writing and shall be delivered in person, transmitted by telecopy or sent by registered mail, charges prepaid, addressed as follows:

(i) if to the Vendor or City:

50 Andrew Street South
Suite 300
Orillia, ON L3V 7T5
Attention: Chief Administrative Officer

(ii) if to the Purchaser:

Hydro One Inc.
483 Bay Street
Toronto, ON M5G 2P5
Attention: General Counsel

Fax No.: (416) 345 6056

(b) Any such notice or other communication shall be deemed to have been given and received on the day on which it was delivered or transmitted (or, if such day is not a Business Day, on the next following Business Day) or, if mailed, on the third Business Day following the date of mailing; provided, however, that if at the time of mailing or within three Business Days thereafter there is or occurs a labour dispute or other event that might reasonably be expected to disrupt the delivery of documents by mail, any notice or other communication hereunder shall be delivered or transmitted by telecopy as aforesaid.

(c) A Party may at any time change its address for service from time to time by giving notice to the other parties in accordance with this Section 13.4.

13.5 **Best Efforts**. The Parties acknowledge and agree that, for all purposes of this Agreement, an obligation on the part of the Party to use its best efforts (which shall not be less than commercially reasonable efforts) to obtain any waiver, consent, approval, permit, licence or other document shall not require such Party to make any payment to any person for the purpose of procuring the same, other than payments for amounts due and payable to such person, payments for incidental expenses incurred by such person and payments required by any applicable law or regulation.

13.6 **Costs and Expenses**. Except as otherwise provided for herein, all costs and expenses (including, without limitation, the fees and disbursements of legal counsel) incurred in connection with this Agreement and the transactions herein contemplated shall be paid by the Party incurring such costs and expenses.

13.7 **Counterparts**. This Agreement may be executed in counterparts, each of which shall constitute an original and all of which taken together shall constitute one and the same instrument.

13.8 **Vendor Guarantee**. The City guarantees the full and prompt payment and performance by Vendor of Vendor's obligations hereunder.

[SIGNATURE PAGES FOLLOW]

IN WITNESS WHEREOF this Agreement has been executed by the Parties.

THE CORPORATION OF THE CITY OF ORILLIA

By: ____________________
Name:
Title: Mayor

By: ____________________
Name: Gayle Jackson
Title: City Clerk

ORILLIA POWER CORPORATION

By: ____________________
Name: PAT HURLEY
Title: CEO OPC

HYDRO ONE INC.

By: ____________________
Name:
Title: President and Chief Executive Officer

SCHEDULE 1.1(ZZZ) – PERMITTED ENCUMBRANCES

1. Instrument No. RO1438096 registered June 2, 2000 is a Transfer of Easement;
2. Instrument No. SC877594 registered January 13, 2011 is a Transfer containing a reservation;
3. Instrument No. SC950244 registered December 6, 2011 is a Transfer of Easement;
4. Instrument No. SC950245 registered December 6, 2011 is a Transfer of Easement;
5. Instrument No. SC950246 registered December 6, 2011 is a Transfer of Easement;
6. Instrument No. RO204275 registered June 15, 1965 is a Bylaw;
7. Instrument No. RO256979 registered November 16, 1967 is a Bylaw;
8. Instrument No. RO854223 registered December 18, 1981 is a Transfer of Easement;
9. 4600 Uhtoff Line (Fittons Substation lands) – unregistered interest in favour of Rogers Communications relating to a point of presence shelter and related equipment in regards to an agreement dated July 1, 2002 between SCBN Telecommunications Inc. and Orillia Power Distribution Corporation and the rights derived therefrom;
10. 306 Peter Street North (North Substation lands) – license agreement to be entered into between Orillia Power Distribution Corporation and Orillia Power Generation Corporation (in favour of Orillia Power Generation Corporation) relating to telecommunications equipment currently situated within the fenced in substation portion of the lands, which telecommunications equipment shall be relocated to a mutually acceptable location outside of the fenced in portion of the substation lands;
11. 15 Industrial Street:

    a. use by Rogers relating to a point of presence shelter relating to a point of presence shelter and related equipment in regards to an agreement dated April 13, 2005 between SCBN Telecommunications Inc. and Orillia Power Distribution Corporation and the rights derived therefrom; and

    b. license agreement to be entered into between Orillia Power Distribution Corporation, Ontario Provincial Police, the City and Orillia Power Generation Corporation relating to the use of a telecommunications tower and related equipment (including anchors and guy wires) used by Ontario Provincial Police and the City and Orillia Power Generation Corporation (as the case may be) relating to a joint use agreement dated November 1997.

EXECUTION VERSION

SCHEDULE 2.4(A) – PURCHASE PRICE ADJUSTMENTS

OPDC - Illustrative Purchase Price and Closing Adjustment *DRAFT July 26th, 2016*

(Note: Audited Financials as of December 31, 2015 for Orillia Power Distribution Corporation)

Purchase Price Summary

	Purchase Price	Illustrative Purchase Price Adjustment	Illustrative Adjusted Purchase Price
Purchase Price	$26,350,000	$900,000	$27,250,000

Purchase Price Adjustment - SPA Definitions

SPA Definitions	OPDC 2015A F/S 12/31/2015	Illustrative Closing Financial Statements	Illustrative Purchase Price Adjustment
Working Capital Calculation	$416,000	$516,000	$100,000
NFA Calculation (1.1x NFA Index Multiplier)	$22,545,000	$23,545,000	$1,100,000
Long Term Debt Calculation	$10,497,000	$10,997,000	($500,000)
Regulatory Accounts Calculation	($825,000)	($625,000)	$200,000
			$900,000

Supporting Calculations

	OPDC 2015A F/S 12/31/2015	Illustrative Closing Financial Statements	Illustrative Purchase Price Adjustment
Working Capital Calculation - SPA Definition			
Cash	n/a	n/a	
Accounts receivable	$3,419,000	$3,419,000	
Unbilled energy and distribution revenue	$4,153,000	$4,153,000	
Payment in lieu of taxes receivable	$0	$0	
Inventories	$501,000	$501,000	
Prepaid expenses	$170,000	$170,000	
Due from related parties	$867,000	$867,000	
Other Current Assets	$0	$0	
Current Assets	$9,110,000	$9,110,000	
Bank indebtedness	$2,000,000	$2,000,000	
Accounts payable and accrued liabilities	$5,759,000	$5,659,000	
Payment in lieu of taxes payable	$217,000	$217,000	
Customer security deposits	$133,000	$133,000	
Current portion of long term debt	$210,000	$210,000	
Due to related parties	$55,000	$55,000	
Other Current Liabilities	$0	$0	
Customer security deposits	$320,000	$320,000	
Current Liabilities & Customer Deposits	$8,694,000	$8,594,000	
Working Capital - (Assets net Liabilities)	$416,000	$516,000	$100,000
NFA Calculation - SPA Definition			
Property, plant and equipment	$23,586,000	$24,586,000	
Intangable assets	$125,000	$125,000	
Less: Deferred revenue	($1,166,000)	($1,166,000)	
NFA	$22,545,000	$23,545,000	$1,000,000
NFA Index			1.1x
			$1,100,000
Long Term Debt Calculation - SPA Definition			
Long term debt	$10,497,000	$10,997,000	
Long Term Debt	$10,497,000	$10,997,000	($500,000)
Regulatory Accounts Calculation - SPA Definition			
Regulatory deferral account debit balances	$2,162,000	$2,162,000	
Regulatory deferral account credit balances	($2,987,000)	($2,787,000)	
Net Regulatory Accounts - Asset/(Liability) balance	($825,000)	($625,000)	$200,000

SCHEDULE 3.1(G) – SUBSIDIARIES

The Corporation held a 1.231% ownership interest in EnerConnect (a settlement services provider). The Corporation sold all of its interest in 2007.

SCHEDULE 3.1(L) - REAL PROPERTY, LEASED PROPERTY AND EASEMENTS

	Description	PIN/Postal Code
	Real Property	
1.	Westmount Substation – 347 Mississauga Street, Orillia, ON	PIN 58638-0137 (LT)
2.	Jarvis Substation – 188 Jarvis Street/Cowen Street, Orillia, ON	PIN 58663-0068 (LT)
3.	Lakeview Substation – 450 Sundial Drive, Orillia, ON	PIN 58622-0057 (LT)
4.	North Substation – 306 Peter Street North, Orillia, ON	PIN 58658-0032 (LT)
5.	Central Substation – 24 Market Street, Orillia, ON	PIN 58650-0205 (LT)
6.	Progress Park Substation – 44/45 Wood Land Drive, Orillia, ON	PIN 58569-0012 (LT)
7.	Vacant land – Couchiching Point Area	PIN 58686-0093 (LT)
8.	Fittons Substation – 4600 Uhtoff Line	PIN 58574-0037 (LT)
9.	15 Industrial St., namely Parts 6 and 9 on draft reference plan prepared by Dearden and Stanton Ltd., Ontario Land Surveyors dated July 21, 2016 (CAD File: RF26926/D-2711, revised August 8, 2016)	Part of PIN 58670-0027 (LT) re Part 6 and Part of PIN 58670-0028 (LT) re Part 9
10.	James St. Substation – 372 West St. S., namely Part 1 on draft reference plan prepared by Dearden and Stanton Ltd., Ontario Land Surveyors dated July 25, 2016 (CAD File: PT26925/C-8077)	Part of PIN 58671-0047 (LT)
	Leased Property	
1.	Nil	
	Easements	
1.	See below	
2.	Ontario Ministry of Natural Resources Underwater Electric Power Cable Licence of Occupation No. 9381 dated December 22, 1981	Part 1, Water Lot Location CL 2646, Township of Orillia Southern Division

Other Uses		
1.	4600 Uhtoff Line (Fittons Substation lands) – unregistered interest in favour of Rogers Communications relating to a point of presence shelter and related equipment in regards to an agreement dated July 1, 2002 between SCBN Telecommunications Inc. and Orillia Power Distribution Corporation and the rights derived therefrom	
2.	306 Peter Street North (North Substation lands) – license agreement to be entered into between Orillia Power Distribution Corporation and Orillia Power Generation Corporation (in favour of Orillia Power Generation Corporation) relating to telecommunications equipment currently situated within the fenced in substation portion of the lands, which telecommunications equipment shall be relocated to a mutually acceptable location outside of the fenced in portion of the substation lands	
3.	15 Industrial Street: (a) use by Rogers relating to a point of presence shelter relating to a point of presence shelter and related equipment in regards to an agreement dated April 13, 2005 between SCBN Telecommunications Inc. and Orillia Power Distribution Corporation and the rights derived therefrom (b) license agreement to be entered into between Orillia Power Distribution Corporation, Ontario Provincial Police, the City and Orillia Power Generation Corporation relating to the use of a telecommunications tower and related equipment (including anchors and guy wires) used by Ontario Provincial Police and the City and Orillia Power Generation Corporation (as the case may be) relating to a joint use agreement dated November 1997.	

EASEMENTS

Address	PIN	INSTR. No.
16 Andrew Street Orillia, ON	58650-0165 (LT) Plan 51R37619	SC950248 SC950247 R0317270

155 Atherley Road Orillia, ON	Registered Plan 388 Lot 3	N/A
161 Atherley Road Orillia, ON	Registered Plan 388 Lot 4	N/A
167 Atherley Road Orillia, ON	Registered Plan 388 Lot 6	N/A
171 Atherley Road Orillia, ON	Registered Plan 388 Lot 7	N/A
177 Atherley Road Orillia, ON	Registered Plan 388 Lot 7	N/A
181 Atherley Road Orillia, ON	Registered Plan 388 Lot 8	N/A
235 Atherley Road Orillia, ON	Registered Plan 559 Part Lot 1	N/A
354 Atherley Road	58686-0092, 58686-0076, 58686-0060 Plan 51R37559	
679 Atherley Road Orillia, ON	Registered Plan 292 Lot	246368
240 Barrie Road Orillia, ON	Registered Plan 964 Lot 77	
441 Barrie Road Orillia, ON	59012-0001 (LT) to 59012-0084 (LT) Condo Pl 12	SC1167745 (Common Elements)
1 Brammer Drive Orillia, ON	58621 - 009LT Plan 51R38579 Lot 4, Con 6 Parts 1, 3, 4, 5, 6, 7, 9, 10 & 11 58621 - 009LT Plan 51R38579 Parts 5, 7, 8, 9, 10, 11, 12 & 13	SC1063108 SC1063161
23 Brammer Drive Orillia, ON	58621 - 0033(LT) Plan 51R39957	SC1213547
24 Brammer Drive Orillia, ON	58621 - 0025(LT) Plan 51R20329	SC556451
25 Brant St. Orillia, ON	58655-0066 (LT) **Now 58655-0145 (LT)** Plan 51R-36116	SC660205 SC660206
760-770 Broadview Ave Orillia, ON	Plan 51R-5499 + 51R5129	SC560491
Canterbury Circle (591 Sundial Drive) Orillia, ON	58626-0362(LT), 58626-0339 Plan 51M973	SC925730 SC919253

4040 Carlyon Line Orillia, ON	58576-002	94922
25 Cedar Island Road Orillia, ON	Plan 51R-31235, 51R-31497	SC103275, SC103394
151 Cedar Island Road (SC613333) Orillia, ON	58669-0058(LT) Plan 51R-31235	N/A
162 Cedar Island Road Orillia, ON	Plan 51R-29599	N/A
17 Coldwater Road Orillia, ON	Plan No 180, Plan 51R-13565	N/A
26 Coldwater Street Orillia, ON	Plan 8 Lot 2 to 3 Ptd. Lot 4 Drawing X-2223	N/A
31 Coldwater Road Orillia, ON	51E-25831	SC533430
51 Coldwater Road Orillia, ON	Reg Plan 137 Lot 7 Dwg X8-994	N/A
54 + 60 Coldwater Street Orillia, ON	Plan 8, Lot 8 Part 9S	N/A
93 Coldwater Street E Orillia, ON	Plan 51R-7773	N/A
188 Coldwater Road Orillia, ON	PIN 58654-0060 & 58654-0122	SC802928
293 Coldwater Road Orillia, ON	Plan R189-B	N/A
1 Commerce Road Orillia, ON	58626-0005(LT) Plan 51R-34166	SC419149
5 Commerce Road Orillia, ON	58626-005(LT) Plan 51R-34166	N/A
77 - 111 Commerce Road + 611 Sundial Dr. Orillia, ON	Plan 51R7981	N/A
24 Colborne St Orillia, ON	58667-0088, 58667-0126, 58667-0127, 58667-0091, Plan 51R32181	N/A
170 Colborne St Orillia, ON	Plan R893	N/A
Couchiching Point Road Orillia, ON	Plan 51R-7667	637012 & 637018
440 Couchiching Point Road Orillia, ON	Plan 51R6824	RO619959

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2 Elmer Ave. Orillia, ON	Plan R964, Lot 73	N/A
9 Ferguson Road Orillia, ON	58577-0125 (LT) Plan 51R386553	N/A
9 Ferguson Road Orillia, ON	58577-0125 (LT) Plan 51R38663	N/A
38 Fittons Heights Orillia, ON	N/A	N/A
52 Fittons Road East Orillia, ON	58628-0054(LT) **Now 58628-0082(LT)** Plan 51R-33634	SC331648
Fittons Road East 1/2 Lot 5 Con 4 Orillia, ON	N/A	N/A
440 Forest Avenue N Orillia, ON	58684-0029(LT) Plan 51R-34163	N/A
Forest Home - PT LT 12 Con 2 Orillia, ON	58570-0015(LT) Plan 51R-33479	N/A
282 Franklin Street Orillia, ON	58675-0211(LT) Plan 51R-30458	N/A
2 Front Street N Orillia, ON	Plan 51R-7900	N/A
2 Front Street S Orillia, ON	Plan X-2245	N/A
9 + 25 Front Street N Orillia, ON	58667-0156, 58667-0156(LT) Plan 51R13701, 51R31703	SC298176, SC6824 SC298240, RO1039171
51 Front Street N Orillia, ON	1360506 Plan 51R-27125	N/A
150 Front Street (part 11) Orillia, ON	58670-0013, 58670-0012, 58670-0010 Plan 51R-21771, 51R-29148	N/A
180 + 182 Front Street S Orillia, ON	58670-0013, 58670-0012, 58670-0010 Plan 51R-29148, 133, 51R-21771 Lot 4,8,9,11	397827
Front Street S CPR Right of Way Orillia, ON	N/A	N/A
Grape Island Lot 1 + 2 Orillia, ON	N/A	N/A
Grape Island Lot 3 Orillia, ON	N/A	N/A
Grape Island Lot 5 Orillia, ON	Plan # 948	N/A

248 Hilda Street Orillia, ON	58675-0081(LT) Plan 51R-27454	SC899053
1 Hunter Valley Road Orillia, ON	58633-0005(LT) Plan 51R-37258	SC878611
Huronia Road (Boyles Industries) Orillia, ON	Plan 51R-12544	836740
475 Huronia Road Orillia, ON	N/A	N/A
4535 Huronia Road Orillia, ON	58621-009(LT) Plan 51R38579 Plan 51R-38579	SC42568, SC1063108 RO1103668
Industrial Street Orillia, ON	58670-0112(LT) Plan 51R-36244 Part 1	SC698666
15 Industrial Street Orillia, ON	58670-0026(LT), 58670-0027(LT) 58670-0028(LT), 58574-0037(LT) Plan 51R20312	SC389000, SC389001 SC389002, RO443432
5 Invermara Court Orillia, ON	58684-0269(LT) Plan 51R-32424	N/A
10 Invermara Court Orillia, ON	58684-0348 Plan 51R34511	SC651477
1 James Street W Orillia, ON	E-26 Dwg. X-1361	N/A
175 James Street E Orillia, ON	58642-0017(LT) Plan 51R-39908	SC1220883
275 James Street Orillia, ON	58675-0211(LT) Plan 51R-30458	1461035
188 Jarvis Street Orillia, ON	58663-0027(LT), 58663-0067(LT) Plan 51R35886	SC6650272
Jarvis Street + Cowan Orillia, ON	Plan 51R33242	OR122904
100 King Street Orillia, ON	Dwg X8-1039	N/A
6 Kitchener Street Orillia, ON	58568-0034(LT) Plan 51R-36095	SC660482
338 MacIsaac Drive Orillia, ON	58684-0064(LT) Plan 51R-35590	SC623196
24 Market Street Orillia, ON	58650-0179(LT), 58650-0185(LT) Plan R51R38085	SC950249
24 Market Street Orillia, ON	58650-0046(LT) Plan R51R38085	SC950244

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18 Matchedash Street North Orillia, ON	58667-0059(LT) Plan 51R-35175	SC700518
188 Memorial Ave Orillia, ON	Registered Plan #673	64297
214 Memorial Ave Orillia, ON	Registered Plan No. 671	N/A
265 Memorial Ave Orillia, ON	Registered Plan No.673, 5lR-5684, 5lR-635l	N/A
269 Memorial Ave Orillia, ON	Registered Plan 673 R-876 Part of Lot 312	737720
841 Memorial Avenue Orillia, ON	58569-0004(LT) Plan 51R-31299	SC121586
845 Memorial Avenue Orillia, ON	58569-0073(LT) Plan 51R-31495	SC121581
995 Memorial Avenue (Line 15) Orillia, ON	Plan 51R33479 Lot of Lot 12. Conc 2. City of Orillia	N/A
36 Mississaga Street E. Orillia, ON	N/A	N/A
52 Mississaga Street East Orillia, ON	58667-0023(LT) Plan 51R-38958	SC1128242
62 Mississaga Street East Orillia, ON	58667-0024(LT) Plans 51R-36596 & 51R-29760	SC759597
142 Mississaga Street W. Orillia, ON	Registered Plan No.180	N/A
177-179 Mississaga Street E. Orillia, ON	Plan 51R-13701 Dwg. XD8-1105	N/A
290 Mississaga St. W - pole line anchors Orillia, On	58848-0043 LT Plan 51R-39304	N/A
347 Mississaga Street W Orillia, ON	58638-013 51R-10539	N/A
354 Mississaga Street W Orillia, ON	Lot 59 Plan 426	N/A
1002-1028 Mississaga Street W Orillia, ON	58636-0074(LT) Plan 51R-36306	N/A
1095 Mississaga Street Orillia, ON	Plan 51R-556762, 51R-4325, 51R-18149 51R-4741 (part of plan 1147)	N/A
Mississauga Street W. - Pt Lot 3, Plan 426, Bell Canada Orillia, ON	Plan 51R-754223 (Part of Plans 426, Plan 51R-10539)	N/A

Mooney Cres Orillia, ON	Reg Plan #420, #1490 Plan 51R-6776, 51R-6824	35362, 35363, 35365
3000 Old Barrie Road Orillia, ON	*58572-0009(LT)* ***Now 58572-0345(LT)*** *Plan 51R-33239*	SC325486
3075 Old Barrie Road Orillia, ON	58570--009(LT) Plan 51R-33239	N/A
246 Oxford Street Orillia, ON	58675-0094(LT) Plan 51R-38048	SC1017699
11 Peter Street S Orillia, ON	N/A	N/A
25 Peter Street N Orillia, ON	PT LT 4/ Plan8	1430712
7975 Provincial Hwy 12 Orillia, ON	Plan 51R-30388	N/A
6 Queen St - Con 11 Lot 67 Ramara	PIN 58688-0041 Plan 22194 - Part 1, Plan 40R-28	N/A
478 Regent Street Orillia, ON	58682-0186 (LT) Plan 51R-33828	SC502940
316 Rodger Road Orillia, On	58684-0052 (LT) Plan 51R-40244	SC1270221
Rynard Dr + , Coldwater Road Closing Orillia, ON	58654-0001 (LT) Plan 51R-35160	RO247674
Rynard Dr Lots 1, 2, 3, 4 Orillia, ON	Plan-1, Section 51M-468	
Rynard Farm - 1967 Orillia, ON	N/A	247674
Rynard Farm and Collegiate Drive Orillia, ON	58654-0001(LT) Plan 51R-35160	N/A
3 Shellswell Crescent Orillia, ON	58571-0058(LT) Plan 51R-31974	SC274231
24 Simcoe Street Orillia, ON	Plan 51R-35247, Pl 432	SC559950
N/S Simcoe Street Orillia, ON	58678-0034(LT) Plan 51R-35247	SC559950
Taylor Drive Orillia, ON	Plan 51R-38188	SC1146424
University Avenue (anchors) Orillia, ON	58570-0009(LT), 58572-0345(LT) Plan 51R-37234	SC821572
University Avenue (anchors) Orillia, ON	58572-0340(LT), 58572- 0479(LT) Plan 51R-37508	N/A

University Avenue Orillia, ON	58572-0479(LT) 58572-0483(LT) Plan 51R-37508	SC979274
500 University Avenue Orillia, ON	58572-0344(LT) 58572-0347(LT) Plan 51R-37247	SC814296
735 University Avenue Orillia, ON	58572 -0478(LT) Part 9 and 10 Plan 51R37508	SC876707
469 to 499 Victoria Cres Orillia, ON	N/A	N/A
9 Westmount Drive Orillia, ON	58638-0268(LT) Plan 51R-1707	N/A
451 West Street N Orillia, ON	Plan R01348881 (A999)	303275
West Street - Southwood Estates Orillia, ON	Plan 1472	192022
8 West Street Orillia, ON	Reg. Plan No. 8 (OR351)	N/A
26 West Street N. Orillia, ON	R-944	N/A
29 West Street Orillia, ON (24 Market St Opera House Txfr)	PLAN 180, 51R-38085	SC950249, SC950250
29 West St & Nottawasaga St Orillia, ON	51R-38085	SC950246
56 West Street North Orillia, ON	Lot #7 Conc. 9 Dwg X-1369	N/A
62 West Street N. Orillia, ON	50-439 Plan R-949	N/A
65 West Street N. Orillia, ON	Plan of Easement Dwg. X-2234	N/A
174 West Street - pole line anchors Orillia, On	58671-0099 (LT)	N/A
175 West Street South Orillia, ON	58671-0099(LT) Plan 51R-39305	SC1127920
384 West Street N. Orillia, ON	Plan R-949	N/A
450 West Street N Orillia, ON	58626-0343(LT) Plan 51R-3416	N/A
451 West Street N Orillia, ON	Reg No. 01348881 Doc. No. 303275	N/A
466 West Street North	58625-0011(R)	RO1469482

Orillia, ON	**Now 58625-0014(LT)** Plan 51R-34166	
800 West Ridge Blvd. Orillia, ON	58572-0180 LT Plan 51 M843	SC489951
59 William Street Orillia, ON	58651-0189(LT) Plan 51R-35177	SC633608
146 Line #15 North Oro-Medonte, ON	58571-0059(LT) Plan 51R-31974	SC323483
204 Line 15N Oro-Medonte, ON	58571-0033(LT) Plan 51R-32103	SC248937
NARROWS - Atherley Bridge	Plan 51R-9969	N/A
Leacock Property Lot 10 Con 6	Lot 10 Con 6 Town of Orillia	N/A

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SCHEDULE 3.1(M) – INTELLECTUAL PROPERTY

- Orillia Power Trademark No. 921963

SCHEDULE 3.1(N) – CONTRACTS AND COMMITMENTS

Nil.

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SCHEDULE 3.1(O) – MATERIAL CONTRACTS

1.	Infrastructure Ontario Financing Agreement dated June 15, 2009
2.	General Security Agreement dated October 31, 2000
3.	Liabilities Assumption Agreement dated November 1, 2000
4.	Infrastructure Ontario Debenture dated May 3, 2010
5.	Promissory Note due to the City of Orillia dated December 1, 2000
6.	TD Operating Line dated July 21, 2014
7.	TD Credit Facility dated November 2, 2014
8.	TD IESO Letter of Credit dated April 15, 2002
9.	TD General Security Agreement dated April 15, 2002
10.	Harris Licence Maintenance Agreements dated February 25, 2010 and July 29, 2010
11.	Harris Escrow Agreement dated February 23, 2010
12.	Swift Wheeling Agreement dated June 23, 1993 with Ontario Hydro as amended by an amending agreement dated May 9, 2005
13.	Minden Wheeling Agreement dated January 2, 1990 with Ontario Hydro as amended by an amending agreement dated May 5, 2009
14.	Services Agreement between Orillia Power Distribution Corporation and Orillia Power Generation Corporation dated January 1, 2001
15.	Independent Electricity Market Operator Participation Agreement dated January 3, 2002
16.	Smart Metering Agreement for Distributors dated April 26, 2013 with Independent Electricity System Operator
17.	CHEC Group Mutual Assistance Agreement revised February 27, 2013
18.	Group of Seven Emergency Mutual Assistance Plan revised dated September 25, 2013
19.	Emergency Mutual Assistance Plan for Use with Ontario's LDCs dated March 2004
20.	OWLP/OPP Joint Use 200' Communications Tower Agreement with Her Majesty the Queen in Right of the Province of Ontario as represented by the Ministry of the Solicitor General and Correctional Services on behalf of the Ontario Provincial Police dated

	November 24, 1997
21.	Master CDM Program Agreement with the Ontario Power Authority dated May 1, 2007
22.	Energy Conservation Agreement with Ontario Power Authority dated December 24, 2014
23.	Letter of Credit No. 0596-9764646-05 with the Toronto Dominion Bank (undated)
24.	EBT Hub Connector License Agreements with SPI Group Inc. dated October 1, 2010 and August 31, 2010
25.	Subdivision Agreements – Stone Ridge Subdivision PH 3, 4, 5
26.	Sudbury Hydro Emergency Mutual Assistance Plan dated March 31, 2006
27.	Greater Sudbury Hydro and OPDC Emergency Mutual Assistance Plan dated December 2015
28.	Canada Post License Agreement dated January 30, 1951
29.	Revenue Sharing and License Agreement dated April 18, 2013
30.	Cable Control Systems Inc. Locate Agreement dated December 2, 2015
31.	City Fuel Agreement dated February 7, 2006
32.	Advanced Metering Infrastructure Sale and Services Agreements (various dates)
33.	IESO Smart Meter Agreement dated April 26, 2013
34.	After Hours Answering Service Agreement dated October 26, 2015 with The Corporation of the City of Orillia
35.	Hydro One Supply Agreement with Ontario Hydro dated February 1, 1999
36.	IMO Participation Agreement dated January 3, 2002
37.	Service Provider Agreement with ITM Group Inc. dated September 1, 2006 and new rates email dated March 9, 2015
38.	OPA Energy Conservation Agreement dated October 31, 2014
39.	Great Plains Dynamics C/S Master Software License Agreement dated 1999
40.	Rodan Cooperation Agreement dated January 1, 2011 with Rodan Energy Solutions Inc.
41.	SCADA License Agreement dated May 18, 1988

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42.	One Call Service Agreement with Ontario One Call Ltd. dated March 6, 2003; after hours call answering service agreement dated November 26, 2012
43.	Westmount Station Purchase Order #POD020106 dated September 29, 2015
44.	Westmount Station Purchase Order #POD020338 dated February 5, 2016
45.	Westmount Station Purchase Order #POD020339 dated February 5, 2016
46.	Westmount Station Purchase Order #POD020346 dated February 5, 2016
47.	Costello Utility Consultants Confidentiality Agreement dated October 16, 2015
48.	Employee Plans referred to in Schedule 3.1(P)
49.	CCDC 2 Stipulated Price Contract Westmount Substation with K-Line Maintenance Construction Limited dated June 3, 2016

SCHEDULE 3.1(P) – EMPLOYEE PLANS

1.	Benefits Administration Agreement with MEARIE
2.	OMERS Participation Certificate Group Number 422091 dated November 1, 2000
3.	MEARIE Employee Benefit Booklet Inside Distribution Employees September 5, 2014
4.	MEARIE Employee Benefit Booklet Outside Distribution Employees September 19, 2014
5.	MEARIE Employee Benefit Booklet Salaried Employees January 2016

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SCHEDULE 3.1(Q) – COLLECTIVE AGREEMENT

1.	Collective Agreement for Inside Employees between Orillia Power Distribution Corporation and Local Union No. 636 of the International Brotherhood of Electrical Workers dated between September 1, 2014 and August 31, 2018
2.	Collective Agreement for Outside Employees between Orillia Power Distribution Corporation and Local Union No. 636 of the International Brotherhood of Electrical Workers dated between September 1, 2014 and August 31, 2018

SCHEDULE 3.1(S) – INSURANCE POLICIES

1.	MEARIE Comprehensive Liability Insurance Policy No. L2015ORIL1 dated January 1, 2016
2.	MEARIE Vehicle Insurance Policy No. V2015ORIL1 dated January 1, 2016
3.	MEARIE Property Program Policy No. P2015ORIL1 dated January 1, 2016
4.	Euler Hermes Bad Debt Insurance Policy dated December 31, 2016
5.	MEARIE Directors and Officers Liability Policy No. L2015ORIL1 dated January 1, 2016
6.	CHUBB Commercial Excess Insurance Policy No. 37112045 dated March 20, 2016
7.	Liberty International Underwriters Commercial Crime Policy dated May 11, 2015 Policy No. CMTOAAZMGY002
8.	Lloyd's Non-Owned Aviation Facility Insurance Policy No. NOA0052-15 dated May 5, 2015
9.	Group Accident Insurance Program for Orillia Power Corporation – Board of Directors AD&D coverage January 01, 2016

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SCHEDULE 3.1(V) – TAXES

1.	2010 T2 Tax Return
2.	2011 T2 Tax Return
3.	2012 T2 Tax Return
4.	2013 T2 Tax Return
5.	2014 T2 Tax Return
6.	2015 T2 Tax Return
7.	Canadian Revenue Agency Notice of Re-Assessment 2010
8.	Canadian Revenue Agency Notice of Assessment 2011
9.	Canadian Revenue Agency Notice of Assessment 2012
10.	Canadian Revenue Agency Notice of Assessment 2013
11.	Canadian Revenue Agency Notice of Assessment 2014
12.	Ontario Ministry of Revenue Notice of Assessment 2010
13.	Ontario Ministry of Revenue Notice of Assessment 2011
14.	Ontario Ministry of Revenue Notice of Assessment 2012
15.	Ontario Ministry of Revenue Notice of Assessment 2013
16.	Ontario Ministry of Revenue Notice of Assessment 2014
17.	Ontario Ministry of Revenue Notice of Assessment 2015

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SCHEDULE 3.1(Z) – LICENCES

1.	Ontario Energy Board Electricity Distribution License ED-2002-0530 valid until March 31, 2023
2.	Independent Electricity Market Operator Licence ID 104319
3.	Ontario Ministry of Transportation Motor Vehicle Inspection Station Licence No. 26-44229 (expired December 12, 2015)
4.	Electrical Contractor Registration Agency of the Electrical Safety Authority Electrical Contractor License #7008088 dated September 29, 2010
5.	HWIN Licences NAICS Code 1 – 221122 and NAICS Code 2 – 221111
6.	Ontario Ministry of Environment Certificate of Approval (Air) No. 8-1160-98-006 dated October 20, 1998
7.	Ontario Ministry of Environment Certificate of Approval (Waste) No. A-800924 dated August 25, 1998 as amended on March 28, 2001
8.	Environment Canada Chemicals Management Plan dated May 14, 2007
9.	Software License Agreement with Quindar Products Ltd. dated May 18, 1988
10.	Great Plains Dynamics C/S Master Software License Agreement dated 1999
11.	Software Escrow Agreement No. 2718 with N. Harris Computer Corporation Multi-User Plan dated May 18, 2007 and dated Jul 30, 2010
12.	Emergency Restoration Plan with Rodan dated August 5, 2004

SCHEDULE 6.2 – PARTICIPATION IN COMMUNITY EVENTS

1. Community Events: The Purchaser shall introduce itself to the community by working with the Advisory Committee to determine the optimum community events to participate in over a three year transition period from closing.

2. Community Promotion / Economic Development: The Purchaser shall make available to the City, at no cost, space on distribution poles in prominent commercial areas for the installation of vertical banners promoting tourism, community events or other messages approved by the City. To participate in this initiative, the City shall sign the Purchaser's municipal attachments agreement and accept responsibility and the terms and conditions for such attachments, and the location of such vertical banners and the associated hardware to install them must be pre-approved by the Purchaser.

3. Community "Ribbon Cutting" Event: The Purchaser commits to holding a special customer appreciation event to celebrate the opening of its Orillia facilities, which would give customers the opportunity to speak with local staff about their work, see specialized work equipment, receive information on energy conservation and electrical safety, including electrical safety demonstrations and give-aways for children.

4. School Electrical Safety Presentations: The Purchaser will integrate all Orillia publicly-funded schools into its rotational schedule for Electrical Safety Presentations targeted at Grade 5 students.

5. School Tree Planting Event and Environmental Talk: As part of its annual Arbour week school educational talks and tree planting events, the Purchaser commits to holding one event each year at a Orillia school for a minimum of three years following Closing.

6. Participation at career fairs held at local high schools, or post-secondary institutions to encourage students to consider furthering their education in the trades or in Science, Technology, Engineering and Math (STEM) programs that would prepare them for a career in the electricity industry.

   In addition to the above, the City and community charitable and non-profit organizations will have access to the Purchaser's community investment programs, which currently include:

   - Sponsorship of community-based events organized by municipalities and local not-for-profit organizations.

   - Employee Volunteer Grant Program of up to $1000 per employee for charitable or non-profit organizations with whom individual employees volunteer 50 or more hours in a year. Employees can re-apply for this grant annually.

   - Annual Charity Campaign contributions to local United Ways and Hydro One Employees' and Pensioners' Charity Campaign contributions to over 800 charities of their choice across Ontario ($1,2 million raised in the 2015 campaign). All employees can designate any local registered charity for payroll deduction.

Hydro One's Safe Communities Donations Program – up to $25,000 for projects being implemented by municipal, non-profit or charitable community groups to help enhance community safety and security (for example, to install security barriers, enhance walking trails for seniors, improve playground structures, etc.). Applications are reviewed twice a year.

SCHEDULE 6.4 – CITY PROPERTY

1. Queen and Creighton (All of PIN: 58688--0041 (LT))

2. 175 West Street South (All of PIN: 58643--0057 (LT))

3. 15 Industrial Street properties:

   a. Part of PIN: 58670--0026 (LT), being Parts 1, 2 and 3 on draft reference plan prepared by Dearden and Stanton Ltd., Ontario Land Surveyors dated July 21, 2016 (CAD File: RF26926/D-2711, revised August 8, 2016)

   b. Part of PIN: 58670--0027 (LT), being Parts 4, 5 and 7 on draft reference plan prepared by Dearden and Stanton Ltd., Ontario Land Surveyors dated July 21, 2016 (CAD File: RF26926/D-2711, revised August 8, 2016)

   c. Part of PIN: 58670--0028 (LT), being Parts 8, 10 and 11 on draft reference plan prepared by Dearden and Stanton Ltd., Ontario Land Surveyors dated July 21, 2016 (CAD File: RF26926/D-2711, revised August 8, 2016)

4. 360/370 West Street South (All of PIN: 58671--0046 (LT))

5. 372 West Street South:

   a. Part of PIN: 58671--0047 (LT), being Part 2 on draft reference plan prepared by Dearden and Stanton Ltd., Ontario Land Surveyors dated July 25, 2016 (CAD File: PT26925/C--8077)

6. 700 Harvey Settlement Road - (All of PIN: 58572--0333 (LT))

SCHEDULE 6.6 – RATE CLASSES

Rate Class	**Dx Charges**	**2016**
Residential	Service Charge ($/month)	17.68
	Distribution Volumetric Rate ($/kWh)	0.0127
GS < 50 kW	Service Charge ($/month)	37.42
	Distribution Volumetric Rate ($/kWh)	0.0165
GS 50 to 4999 kW	Service Charge ($/month)	340.60
	Distribution Volumetric Rate ($/kW)	3.5825

2016 Rates Approved per EB-2015-0024

SCHEDULE 9.1(C) – PURCHASER CONSENTS

Nil.

SCHEDULE 9.2(C) – VENDOR CONSENTS

Nil.

**CERTIFIED COPY OF RESOLUTION
OF THE BOARD OF DIRECTORS OF
HYDRO ONE INC.
(the "Corporation")**

The undersigned hereby certifies that set out below is a true copy of a resolution passed by all of the Directors at the meeting of the Board of Directors of Hydro One Inc. held on August 12, 2016.

**HYDRO ONE INC.
(the "Corporation")**

RESOLUTIONS OF THE BOARD OF DIRECTORS

RESOLVED THAT:

Orillia Power Acquisition

1. The acquisition by the Corporation of Orillia Power at up to the maximum purchase price of **[intentionally deleted]** and otherwise on such terms as management may in its discretion determine, be and is hereby approved. The President and Chief Executive Officer or his delegate(s), is hereby authorized and directed, for and on behalf of the Corporation to negotiate, finalize, execute and deliver any and all further documents, agreements, authorizations, elections or other instruments and to take any and all such further action as such officer or delegate(s), in such person's sole direction may deem necessary or desirable in order to give effect to the matters contemplated in this resolution, the execution and delivery of any such documents, agreements, authorizations, elections or other instruments or the doing of any such other act or thing by such person to be conclusive evidence of such determination.

Certified at Toronto, Ontario this 7th day of September, 2016.

Maureen Wareham
Corporate Secretary
Hydro One Inc.

RESOLUTION OF THE DIRECTORS OF ORILLIA POWER CORPORATION

WHEREAS The Corporation of the City of Orillia (the "City") is the sole shareholder of Orillia Power Corporation ("OPC") which is the sole shareholder of Orillia Power Distribution Corporation ("OPDC");

AND WHEREAS the City implemented a shareholder declaration (the "Declaration") on April 2, 2001 as Schedule "A" to By-Law Number 2001-48 which governs the relationship between the City, OPC, OPDC and Orillia Power Generation Corporation ("OPGC");

AND WHEREAS the City's prior approval is required to authorize OPC's sale of "substantially all of the assets of" OPDC pursuant to the provisions of the Declaration;

AND WHEREAS Hydro One Inc. ("HOI"), OPC and the City entered into a letter of intent dated September 22, 2015 whereby the City agreed to grant HOI the exclusive right to evaluate a potential transaction whereby HOI would acquire all of the issued and outstanding shares of OPDC (the "Shares") from OPC;

AND WHEREAS the City and OPC may wish to sell and HOI may wish to acquire the Shares on the terms and conditions of a share purchase agreement (the "SPA") to be entered into between OPC, HOI and the City;

AND WHEREAS in connection with the draft provisions of the SPA, OPC and OPGC are anticipated to agree to provide certain services to OPDC following closing of the SPA, as further contemplated by a Services Agreement which is anticipated to be entered into between OPC, OPDC and OPGC as of August 15, 2016 (the "Services Agreement");

AND WHEREAS in connection with the draft provisions of the SPA, Hydro One Networks Inc. ("HONI") is anticipated to agree to extend the benefits received by OPDC's customers from two wheeling agreements between OPDC and HONI each dated May 9, 2005 concerning the Swift Rapids GS and Minden GS respectively, by entering into two amending agreements between OPGC, HONI and OPDC as of August 15, 2016 (the "Wheeling Agreements");

AND WHEREAS in connection with the draft provisions of the SPA, the City is anticipated to agree to acquire and lease back the premises located at 360 West Street South to OPDC (the "Lease");

AND WHEREAS in connection with the draft provisions of the SPA, the City is anticipated to agree to acquire certain properties from OPDC at fair market value through a purchase and sale agreement ("Purchase Agreement") and dividend in-kind transaction to be entered into between the City and OPDC (the performance of the Purchase Agreement, Lease, Wheeling Agreements, Services Agreement and the SPA, shall collectively be referred to as the "Transaction" and these documents shall collectively be referred to as the "Transaction Documents");

AND WHEREAS the SPA is subject to approval by the Ontario Energy Board pursuant to section 86 of the *Ontario Energy Board Act, 1998* and the Ontario Energy Board's

Preliminary Filing Requirements for Mergers, Acquisitions, Amalgamations and Divestitures in the Ontario Electricity Transmission and Distribution Sector (the "MAADs Application");

AND WHEREAS the City is expected to approve the Transaction and submission of the MAADs Application to the Ontario Energy Board and this resolution will have no force or effect until the City approves the Transaction and submission of the MAADs Application to the Ontario Energy Board.

AND WHEREAS upon the City's approval of the Transaction, the City is expected to authorize OPC, and each of its subsidiaries OPDC and OPGC, to proceed with the Transaction.

BE IT RESOLVED THAT:

1. The performance of OPC's obligations under the SPA and Services Agreement are hereby approved, ratified and confirmed and the execution and delivery of the SPA and Services Agreement by Patrick Hurley and/or Grant Hipgrave, each an authorized signing officer, for and on behalf of OPC, is hereby approved, ratified and confirmed.
2. Patrick Hurley and/or Grant Hipgrave, each an authorized signing officer, are hereby authorized for and on behalf of OPC, in its own capacity, to execute and deliver all such other agreements, consents, notices, amendments, instruments, certificates and other documents including but not limited to amendments to the SPA and Services Agreement and all documents required to effect the closing of the SPA and Services Agreement and the performance of the SPA and Services Agreement and to do all acts and things necessary or advisable in connection with the SPA and Services Agreement.

THIS resolution is consented to in writing by the undersigned.

Per: ____________________
Greg Gee – Chair

Per: ____________________
Ray Hayhurst – Vice – Chair

Per: ____________________
Aubrey Ford – Director

Per: ____________________
Geoff Hewett – Director

Per: ____________________
Tom Hussey - Director

Customer Bill Impacts

	Residential					
	Volume	Current Rates	Current Charges ($)	Rates as per Acquisition Agreement	Charges as per Acquisition Agreement ($)	% Change
Monthly Consumption (kWh)	**750**					
Total Loss Factors	**1.0561**					
TOU - Off Peak Consumption	488	0.087	$42.41	$0.09	$42.41	
TOU - Mid Peak Consumption	128	0.132	$16.83	$0.13	$16.83	
TOU - On Peak Consumption	135	0.180	$24.30	$0.18	$24.30	
Total: Commodity			**$83.54**		**$83.54**	**0.00%**
DX Fixed Charge ($)	1	17.68	$17.68	$17.50	$17.50	
DX Fixed Charge Rate Riders ($)	1	-1.15	-$1.15	-$1.15	-$1.15	
DX Vol. Charge ($/kWh)	750	0.0127	$9.53	$0.01	$9.45	
DX Low Voltage Charge ($/kWh)	750	0.0006	$0.45	$0.00	$0.45	
DX Vol. Rate Riders ($/kWh)	750	-0.0015	-$1.13	$0.00	-$1.13	
Distribution Rates Only			**$27.66**		**$27.40**	**-0.92%**
Smart Meter Entity Charge ($)	1	0.79	$0.79	$0.79	$0.79	
Cost of Losses ($/kWh)	42	0.1114	$4.69	$0.11	$4.69	
Distribution Pass-through Charges			**$5.48**		**$5.48**	**0.00%**
Total: Distribution			**$33.13**		**$32.88**	**-0.77%**
TX-Network ($/kWh)	792	0.0054	$4.28	$0.01	$4.28	
TX-Connection ($/kWh)	792	0.0041	$3.25	$0.00	$3.25	
Total: Transmission			**$7.52**		**$7.52**	**0.00%**
WMSC ($/kWh)	792	0.0036	$2.85	$0.00	$2.85	
RRRP ($/kWh)	792	0.0013	$1.03	$0.00	$1.03	
OESP ($/kWh)	792	0.0011	$0.87	$0.00	$0.87	
SSA ($)	1	0.25	$0.25	$0.25	$0.25	
Total: Regulatory			**$5.00**		**$5.00**	**0.00%**
Total Bill (Before Taxes)			$129.20		$128.95	
HST		13%	$16.80	$0.13	$16.76	
Total Bill (Including HST)			**$146.00**		**$145.71**	**-0.20%**

Customer Bill Impacts

	General Service Less Than 50kW					
	Volume	**Current Rates**	**Current Charges ($)**	**Rates as per Acquisition Agreement**	**Charges as per Acquisition Agreement ($)**	**% Change**
Monthly Consumption (kWh)	**2,000**					
Total Loss Factors	**1.0561**					
TOU - Off Peak Consumption	1,300	0.087	$113.10	0.087	$113.10	
TOU - Mid Peak Consumption	340	0.132	$44.88	0.132	$44.88	
TOU - On Peak Consumption	360	0.180	$64.80	0.180	$64.80	
Total: Commodity			**$222.78**		**$222.78**	**0.00%**
DX Fixed Charge ($)	1	37.42	$37.42	37.05	$37.05	
DX Fixed Charge Rate Riders ($)	1	7.48	$7.48	7.48	$7.48	
DX Vol. Charge ($/kWh)	2,000	0.0165	$33.00	0.0163	$32.60	
DX Low Voltage Charge ($/kWh)	2,000	0.0006	$1.20	0.0006	$1.20	
DX Vol. Rate Riders ($/kWh)	2,000	-0.0064	-$12.80	-0.0064	-$12.80	
Distribution Rates Only			**$71.62**		**$70.85**	**-1.08%**
Smart Meter Entity Charge ($)	1	0.79	$0.79	0.79	$0.79	
Cost of Losses ($/kWh)	112	0.1114	$12.50	0.1114	$12.50	
Distribution Pass-through Charges			**$13.29**		**$13.29**	**0.00%**
Total: Distribution			**$84.91**		**$84.14**	**-0.91%**
TX-Network ($/kWh)	2,112	0.0045	$9.50	0.0045	$9.50	
TX-Connection ($/kWh)	2,112	0.0038	$8.03	0.0038	$8.03	
Total: Transmission			**$17.53**		**$17.53**	**0.00%**
WMSC ($/kWh)	2,112	0.0036	$7.60	0.0036	$7.60	
RRRP ($/kWh)	2,112	0.0013	$2.75	0.0013	$2.75	
OESP ($/kWh)	2,112	0.0011	$2.32	0.0011	$2.32	
DRC ($/kWh)	2,000	0.0007	$1.40	0.0007	$1.40	
SSA ($)	1	0.25	$0.25	0.25	$0.25	
Total: Regulatory			**$14.32**		**$14.32**	**0.00%**
Total Bill (Before Taxes)			$339.54		$338.77	
HST		13%	$44.14	13%	$44.04	
Total Bill (Including HST)			**$383.68**		**$382.81**	**-0.23%**

Customer Bill Impacts

	General Service 50 to 4,999 kW					
	Volume	**Current Rates**	**Current Charges ($)**	**Rates as per Acquisition Agreement**	**Charges as per Acquisition Agreement ($)**	**% Change**
Monthly Consumption (kWh)	**73,000**					
Peak (kW)	**100**					
Total Loss Factors	**1.0561**					
Commodity Charges	77,095	0.103	$7,940.82	0.103	$7,940.82	
Total: Commodity			**$7,940.82**		**$7,940.82**	**0.00%**
DX Fixed Charge ($)	1	340.6	$340.60	337.19	$337.19	
DX Fixed Charge Rate Riders ($)	1	0.00	$0.00	0.00	$0.00	
DX Vol. Charge ($/kW)	100	3.5825	$358.25	3.5467	$354.67	
DX Low Voltage Charge ($/kW)	100	0.2230	$22.30	0.2230	$22.30	
DX Vol. Rate Riders ($/kW)	100	0.4153	$41.53	0.4153	$41.53	
Distribution Rates Only			**$721.15**		**$714.16**	**-0.97%**
Total: Distribution			**$762.68**		**$755.69**	**-0.92%**
TX-Network ($/kW)	100	1.9991	$199.91	1.9991	$199.91	
TX-Connection ($/kW)	100	1.5382	$153.82	1.5382	$153.82	
Total: Transmission			**$353.73**		**$353.73**	**0.00%**
WMSC ($/kWh)	77,095	0.0036	$277.54	0.0036	$277.54	
RRRP ($/kWh)	77,095	0.0013	$100.22	0.0013	$100.22	
OESP ($/kWh)	77,095	0.0011	$84.80	0.0011	$84.80	
DRC ($/kWh)	73,000	0.007	$511.00	0.007	$511.00	
SSA ($)	1	0.25	$0.25	0.25	$0.25	
Total: Regulatory			**$973.82**		**$973.82**	**0.00%**
Total Bill (Before Taxes)			$10,031.05		$10,024.06	
HST		13%	$1,304.04	13%	$1,303.13	
Total Bill (Including HST)			**$11,335.08**		**$11,327.19**	**-0.07%**

Determination of Rate Riders as Per Acquisition Agreement

Rate Class	Distribution Charges	Rate Rider	
		A[1]	B = A(-1.01)[2]
Residential	Service Charge ($)	17.68	-0.18
	Distribution Volumetric Rate ($/kWh)	0.0127	-0.0001
General Service < 50kW	Service Charge ($)	37.42	-0.37
	Distribution Volumetric Rate ($/kWh)	0.0165	-0.0002
General Service 50 to 4,999kW	Service Charge ($)	340.6	-3.41
	Distribution Volumetric Rate ($/kWh)	3.5825	-0.0358

[1] OPDC Distribution Rates Effective May 1, 2016 (EB-2015-0024)
[2] Proposed Rate Riders per Acquisition Agreement

Hydro One Orillia

TARIFF OF RATES AND CHARGES

Effective and Implementation Date XXX X, 2016

This schedule supersedes and replaces all previously approved schedules of Rates, Charges and Loss Factors

EB-2016-XXXX

RESIDENTIAL SERVICE CLASSIFICATION

This classification applies to an account taking electricity at 750 volts or less where the electricity is used exclusively in a separate metered living accommodation. Customers shall be residing in single-dwelling units that consist of a detached house or one unit of a semi-detached, duplex, triplex or quadruplex house, with a residential zoning. Separately metered dwellings within a town house complex or apartment building also qualify as residential customers. Further servicing details are available in the distributor's Conditions of Service.

APPLICATION

The application of these rates and charges shall be in accordance with the Licence of the Distributor and any Code or Order of the Ontario Energy Board, and amendments thereto as approved by the Ontario Energy Board, which may be applicable to the administration of this schedule.

No rates and charges for the distribution of electricity and charges to meet the costs of any work or service done or furnished for the purpose of the distribution of electricity shall be made except as permitted by this schedule, unless required by the Distributor's Licence or a Code or Order of the Ontario Energy Board, and amendments thereto as approved by the Ontario Energy Board, or as specified herein.

Unless specifically noted, this schedule does not contain any charges for the electricity commodity, be it under the Regulated Price Plan, a contract with a retailer or the wholesale market price, as applicable. In addition, the charges in the MONTHLY RATES AND CHARGES - Regulatory Component of this schedule do not apply to a customer that is an embedded wholesale market participant.

It should be noted that this schedule does not list any charges, assessments, or credits that are required by law to be invoiced by a distributor and that are not subject to Ontario Energy Board approval, such as the Debt Retirement Charge, the Global Adjustment and the HST.

MONTHLY RATES AND CHARGES - Delivery Component

Service Charge	$	17.68
Rate Rider for Smart Meter Incremental Revenue Requirement - in effect until the effective date of the next cost of service-based rate order	$	2.56
Rate Rider for Disposition of Account 1576 - effective until December 31, 2016 - Approved on an Interim Basis	$	(3.63)
Rate Rider for Application of Tax Change (2016) – effective until April 30, 2017	$	(0.08)
Rate Rider for Smart Metering Entity Charge - effective until October 31, 2018	$	0.79
Fixed Acquisition Rate Rider – in effect until the effective date of the next cost of service application	$	(0.18)
Distribution Volumetric Rate	$/kWh	0.0127
Low Voltage Service Rate	$/kWh	0.0006
Volumetric Acquisition Rate Rider – in effect until the effective date of the next cost of service application	$/kWh	(0.0001)
Rate Rider for Disposition of Deferral/Variance Accounts (2016) - effective until April 30, 2017	$/kWh	0.0013
Rate Rider for Disposition of Deferral/Variance Accounts (2016) - effective until April 30, 2017 Applicable only for Non-Wholesale Market Participants	$/kWh	(0.0028)
Rate Rider for Disposition of Global Adjustment Account (2016) - effective until April 30, 2017 Applicable only for Non-RPP Customers	$/kWh	0.0068
Retail Transmission Rate - Network Service Rate	$/kWh	0.0054
Retail Transmission Rate - Line and Transformation Connection Service Rate	$/kWh	0.0041

MONTHLY RATES AND CHARGES - Regulatory Component

Wholesale Market Service Rate	$/kWh	0.0036
Rural or Remote Electricity Rate Protection Charge (RRRP)	$/kWh	0.0013
Ontario Electricity Support Program Charge (OESP)	$/kWh	0.0011
Standard Supply Service - Administrative Charge (if applicable)	$	0.25

Hydro One Orillia

TARIFF OF RATES AND CHARGES

Effective and Implementation Date XXX X, 2016

This schedule supersedes and replaces all previously approved schedules of Rates, Charges and Loss Factors

EB-2016-XXXX

ONTARIO ELECTRICITY SUPPORT PROGRAM RECIPIENTS

In addition to the charges specified on page 1 of this tariff of rates and charges, the following credits are to be applied to eligible residential customers.

APPLICATION

The application of the charges are in accordance with the Distribution System Code (Section 9) and subsection 79.2(4) of the Ontario Energy Board Act, 1998.

The application of these charges shall be in accordance with the Licence of the Distributor and any Code or Order of the Ontario Energy Board, and amendments thereto as approved by the Ontario Energy Board, which may be applicable to the administration of this schedule.

In this class:

"Aboriginal person" includes a person who is a First Nations person, a Métis person or an Inuit person;
"account-holder" means a consumer who has an account with a distributor that falls within a residential-rate classification as specified in a rate order made by the Ontario Energy Board under section 78 of the Act, and who lives at the service address to which the account relates for at least six months in a year;
"electricity-intensive medical device" means an oxygen concentrator, a mechanical ventilator, or such other device as may be specified by the Ontario Energy Board;
"household" means the account-holder and any other people living at the accountholder's service address for at least six months in a year, including people other than the account-holder's spouse, children or other relatives;
"household income" means the combined annual after-tax income of all members of a household aged 16 or over;

MONTHLY RATES AND CHARGES

Class A

(a) account-holders with a household income of $28,000 or less living in a household of one or two persons;
(b) account-holders with a household income of between $28,001 and $39,000 living in a household of three persons;
(c) account-holders with a household income of between $39,001 and $48,000 living in a household of five persons; and
(d) account-holders with a household income of between $48,001 and $52,000 living in a household of seven or more persons;
but does not include account-holders in Class E.

OESP Credit	$	(30.00)

Class B

(a) account-holders with a household income of $28,000 or less living in a household of three persons;
(b) account-holders with a household income of between $28,001 and $39,000 living in a household of four persons;
(c) account-holders with a household income of between $39,001 and $48,000 living in a household of six persons;
but does not include account-holders in Class F.

OESP Credit	$	(34.00)

Class C

(a) account-holders with a household income of $28,000 or less living in a household of four persons;
(b) account-holders with a household income of between $28,001 and $39,000 living in a household of five persons;
(c) account-holders with a household income of between $39,001 and $48,000 living in a household of seven or more persons;
but does not include account-holders in Class G.

OESP Credit	$	(38.00)

Class D

(a) account-holders with a household income of $28,000 or less living in a household of five persons; and
(b) account-holders with a household income of between $28,001 and $39,000 living in a household of six persons;
but does not include account-holders in Class H.

OESP Credit	$	(42.00)

Hydro One Orillia

TARIFF OF RATES AND CHARGES

Effective and Implementation Date XXX X, 2016

This schedule supersedes and replaces all previously approved schedules of Rates, Charges and Loss Factors

EB-2016-XXXX

ONTARIO ELECTRICITY SUPPORT PROGRAM RECIPIENTS

Class E

Class E comprises account-holders with a household income and household size described under Class A who also meet any of the following conditions:
(a) the dwelling to which the account relates is heated primarily by electricity;
(b) the account-holder or any member of the account-holder's household is an Aboriginal person; or
(c) the account-holder or any member of the account-holder's household regularly uses, for medical purposes, an electricity-intensive medical device at the dwelling to which the account relates.

OESP Credit	$	(45.00)

Class F

(a) account-holders with a household income of $28,000 or less living in a household of six or more persons;
(b) account-holders with a household income of between $28,001 and $39,000 living in a household of seven or more persons; or
(c) account-holders with a household income and household size described under Class B who also meet any of the following conditions:

i. the dwelling to which the account relates is heated primarily by electricity;
ii. the account-holder or any member of the account-holder's household is an Aboriginal person; or
iii. the account-holder or any member of the account-holder's household regularly uses, for medical purposes, an electricity-intensive medical device at the dwelling to which the account relates

OESP Credit	$	(50.00)

Class G

Class G comprises account-holders with a household income and household size described under Class C who also meet any of the following conditions:
(a) the dwelling to which the account relates is heated primarily by electricity;
(b) the account-holder or any member of the account-holder's household is an Aboriginal person; or
(c) the account-holder or any member of the account-holder's household regularly uses, for medical purposes, an electricity-intensive medical device at the dwelling to which the account relates.

OESP Credit	$	(55.00)

Class H

Class H comprises account-holders with a household income and household size described under Class D who also meet any of the following conditions:
(a) the dwelling to which the account relates is heated primarily by electricity;
(b) the account-holder or any member of the account-holder's household is an Aboriginal person ; or
(c) the account-holder or any member of the account-holder's household regularly uses, for medical purposes, an electricity-intensive medical device at the dwelling to which the account relates.

OESP Credit	$	(60.00)

Class I

Class I comprises account-holders with a household income and household size described under paragraphs (a) or (b) of Class F who also meet any of the following conditions:
(a) the dwelling to which the account relates is heated primarily by electricity;
(b) the account-holder or any member of the account-holder's household is an Aboriginal person; or
(c) the account-holder or any member of the account-holder's household regularly uses, for medical purposes, an electricity-intensive medical device at the dwelling to which the account relates.

OESP Credit	$	(75.00)

Hydro One Orillia

TARIFF OF RATES AND CHARGES

Effective and Implementation Date XXX X, 2016

This schedule supersedes and replaces all previously approved schedules of Rates, Charges and Loss Factors

EB-2016-XXXX

GENERAL SERVICE LESS THAN 50 KW SERVICE CLASSIFICATION

This classification refers to a non residential account taking electricity at 750 volts or less whose average monthly maximum demand is less than, or is forecast to be less than, 50 kW. Further servicing details are available in the distributor's Conditions of Service.

APPLICATION

The application of these rates and charges shall be in accordance with the Licence of the Distributor and any Code or Order of the Ontario Energy Board, and amendments thereto as approved by the Ontario Energy Board, which may be applicable to the administration of this schedule.

No rates and charges for the distribution of electricity and charges to meet the costs of any work or service done or furnished for the purpose of the distribution of electricity shall be made except as permitted by this schedule, unless required by the Distributor's Licence or a Code or Order of the Ontario Energy Board, and amendments thereto as approved by the Ontario Energy Board, or as specified herein.

Unless specifically noted, this schedule does not contain any charges for the electricity commodity, be it under the Regulated Price Plan, a contract with a retailer or the wholesale market price, as applicable. In addition, the charges in the MONTHLY RATES AND CHARGES - Regulatory Component of this schedule do not apply to a customer that is an embedded wholesale market participant.

It should be noted that this schedule does not list any charges, assessments, or credits that are required by law to be invoiced by a distributor and that are not subject to Ontario Energy Board approval, such as the Debt Retirement Charge, the Global Adjustment and the HST.

MONTHLY RATES AND CHARGES - Delivery Component

Service Charge	$	37.42
Rate Rider for Smart Meter Incremental Revenue Requirement - in effect until the effective date of the next cost of service-based rate order	$	7.48
Rate Rider for Smart Metering Entity Charge - effective until October 31, 2018	$	0.79
Fixed Acquisition Rate Rider – in effect until the effective date of the next cost of service application	$	(0.37)
Distribution Volumetric Rate	$/kWh	0.0165
Low Voltage Service Rate	$/kWh	0.0006
Volumetric Acquisition Rate Rider – in effect until the effective date of the next cost of service application	$/kWh	(0.0002)
Rate Rider for Disposition of Account 1576 - effective until December 31, 2016 - Approved on an Interim Basis	$/kWh	(0.0048)
Rate Rider for Disposition of Deferral/Variance Accounts (2016) - effective until April 30, 2017	$/kWh	0.0013
Rate Rider for Disposition of Deferral/Variance Accounts (2016) - effective until April 30, 2017 Applicable only for Non-Wholesale Market Participants	$/kWh	(0.0028)
Rate Rider for Disposition of Global Adjustment Account (2016) - effective until April 30, 2017 Applicable only for Non-RPP Customers	$/kWh	0.0068
Rate Rider for Application of Tax Change (2016) – effective until April 30, 2017	$/kWh	(0.0001)
Retail Transmission Rate - Network Service Rate	$/kWh	0.0045
Retail Transmission Rate - Line and Transformation Connection Service Rate	$/kWh	0.0038

MONTHLY RATES AND CHARGES - Regulatory Component

Wholesale Market Service Rate	$/kWh	0.0036
Rural or Remote Electricity Rate Protection Charge (RRRP)	$/kWh	0.0013
Ontario Electricity Support Program Charge (OESP)	$/kWh	0.0011
Standard Supply Service - Administrative Charge (if applicable)	$	0.25

Hydro One Orillia

TARIFF OF RATES AND CHARGES

Effective and Implementation Date XXX X, 2016

This schedule supersedes and replaces all previously approved schedules of Rates, Charges and Loss Factors

EB-2016-XXXX

GENERAL SERVICE 50 TO 4,999 KW SERVICE CLASSIFICATION

This classification applies to a non residential account whose average monthly maximum demand used for billing purposes is equal to or greater than, or is forecast to be equal to or greater than, 50 kW but less than 5,000 kW. Class A and Class B consumers are defined in accordance with O.Reg.429/04. Further servicing details are available in the distributor's Conditions of Service.

APPLICATION

The application of these rates and charges shall be in accordance with the Licence of the Distributor and any Code or Order of the Ontario Energy Board, and amendments thereto as approved by the Ontario Energy Board, which may be applicable to the administration of this schedule.

No rates and charges for the distribution of electricity and charges to meet the costs of any work or service done or furnished for the purpose of the distribution of electricity shall be made except as permitted by this schedule, unless required by the Distributor's Licence or a Code or Order of the Ontario Energy Board, and amendments thereto as approved by the Ontario Energy Board, or as specified herein.

Unless specifically noted, this schedule does not contain any charges for the electricity commodity, be it under the Regulated Price Plan, a contract with a retailer or the wholesale market price, as applicable. In addition, the charges in the MONTHLY RATES AND CHARGES - Regulatory Component of this schedule do not apply to a customer that is an embedded wholesale market participant.

It should be noted that this schedule does not list any charges, assessments, or credits that are required by law to be invoiced by a distributor and that are not subject to Ontario Energy Board approval, such as the Debt Retirement Charge, the Global Adjustment and the HST.

MONTHLY RATES AND CHARGES - Delivery Component

Service Charge	$	340.60
Fixed Acquisition Rate Rider – in effect until the effective date of the next cost of service application	$	(3.41)
Distribution Volumetric Rate	$/kW	3.5825
Low Voltage Service Rate	$/kW	0.2230
Volumetric Acquisition Rate Rider – in effect until the effective date of the next cost of service application	$/kW	(0.0358)
Rate Rider for Disposition of Account 1576 - effective until December 31, 2016 - Approved on an Interim Basis	$/kW	(1.7947)
Rate Rider for Disposition of Deferral/Variance Accounts (2016) - effective until April 30, 2017	$/kW	0.4856
Rate Rider for Disposition of Deferral/Variance Accounts (2016) - effective until April 30, 2017 Applicable only for Non-Wholesale Market Participants	$/kW	(1.0338)
Rate Rider for Disposition of Global Adjustment Account (2016) - effective until April 30, 2017 Applicable only for Non-RPP Customers	$/kW	2.7738
Rate Rider for Application of Tax Change (2016) – effective until April 30, 2017	$/kW	(0.0156)
Retail Transmission Rate - Network Service Rate	$/kW	1.9991
Retail Transmission Rate - Line and Transformation Connection Service Rate	$/kW	1.5382

MONTHLY RATES AND CHARGES - Regulatory Component

Wholesale Market Service Rate	$/kWh	0.0036
Rural or Remote Electricity Rate Protection Charge (RRRP)	$/kWh	0.0013
Ontario Electricity Support Program Charge (OESP)	$/kWh	0.0011
Standard Supply Service - Administrative Charge (if applicable)	$	0.25

Hydro One Orillia

TARIFF OF RATES AND CHARGES

Effective and Implementation Date XXX X, 2016

This schedule supersedes and replaces all previously approved schedules of Rates, Charges and Loss Factors

EB-2016-XXXX

STANDBY POWER SERVICE CLASSIFICATION

This classification applies to an account with load displacement facilities that contracts with the distributor to provide emergency standby power when its load displacement facilities are not in operation. The level of billing demand will be agreed to by the distributor and the customer, based on detailed manufacturer information/documentation such as nameplate rating of the load displacement facility. Further servicing details are available in the distributor’s Conditions of Service.

APPLICATION

The application of these rates and charges shall be in accordance with the Licence of the Distributor and any Code or Order of the Ontario Energy Board, and amendments thereto as approved by the Ontario Energy Board, which may be applicable to the administration of this schedule.

No rates and charges for the distribution of electricity and charges to meet the costs of any work or service done or furnished for the purpose of the distribution of electricity shall be made except as permitted by this schedule, unless required by the Distributor’s Licence or a Code or Order of the Ontario Energy Board, and amendments thereto as approved by the Ontario Energy Board, or as specified herein.

Unless specifically noted, this schedule does not contain any charges for the electricity commodity, be it under the Regulated Price Plan, a contract with a retailer or the wholesale market price, as applicable.

It should be noted that this schedule does not list any charges, assessments, or credits that are required by law to be invoiced by a distributor and that are not subject to Ontario Energy Board approval, such as the Debt Retirement Charge, the Global Adjustment and the HST.

MONTHLY RATES AND CHARGES - Delivery Component - APPROVED ON AN INTERIM BASIS

Distribution Volumetric Rate - $/kW of contracted amount	$/kW	1.0713

Hydro One Orillia

TARIFF OF RATES AND CHARGES

Effective and Implementation Date XXX X, 2016

This schedule supersedes and replaces all previously approved schedules of Rates, Charges and Loss Factors

EB-2016-XXXX

UNMETERED SCATTERED LOAD SERVICE CLASSIFICATION

This classification applies to an account taking electricity at 750 volts or less whose average monthly maximum demand is less than, or is forecast to be less than, 50 kW and the consumption is unmetered. Such connections include cable TV power packs, bus shelters, telephone booths, traffic lights, railway crossings, etc. The level of the consumption will be agreed to by the distributor and the customer, based on detailed manufacturer information/documentation with regard to electrical consumption of the unmetered load or periodic monitoring of actual consumption. Further servicing details are available in the distributor's Conditions of Service.

APPLICATION

The application of these rates and charges shall be in accordance with the Licence of the Distributor and any Code or Order of the Ontario Energy Board, and amendments thereto as approved by the Ontario Energy Board, which may be applicable to the administration of this schedule.

No rates and charges for the distribution of electricity and charges to meet the costs of any work or service done or furnished for the purpose of the distribution of electricity shall be made except as permitted by this schedule, unless required by the Distributor's Licence or a Code or Order of the Ontario Energy Board, and amendments thereto as approved by the Ontario Energy Board, or as specified herein.

Unless specifically noted, this schedule does not contain any charges for the electricity commodity, be it under the Regulated Price Plan, a contract with a retailer or the wholesale market price, as applicable. In addition, the charges in the MONTHLY RATES AND CHARGES - Regulatory Component of this schedule do not apply to a customer that is an embedded wholesale market participant.

It should be noted that this schedule does not list any charges, assessments, or credits that are required by law to be invoiced by a distributor and that are not subject to Ontario Energy Board approval, such as the Debt Retirement Charge, the Global Adjustment and the HST.

MONTHLY RATES AND CHARGES - Delivery Component

Service Charge (per connection)	$	10.59
Distribution Volumetric Rate	$/kWh	0.0095
Low Voltage Service Rate	$/kWh	0.0006
Rate Rider for Disposition of Account 1576 - effective until December 31, 2016 - Approved on an Interim Basis	$/kWh	(0.0048)
Rate Rider for Disposition of Deferral/Variance Accounts (2016) - effective until April 30, 2017	$/kWh	0.0012
Rate Rider for Disposition of Deferral/Variance Accounts (2016) - effective until April 30, 2017 Applicable only for Non-Wholesale Market Participants	$/kWh	(0.0028)
Rate Rider for Disposition of Global Adjustment Account (2016) - effective until April 30, 2017 Applicable only for Non-RPP Customers	$/kWh	0.0068
Rate Rider for Application of Tax Change (2016) – effective until April 30, 2017	$/kWh	(0.0001)
Retail Transmission Rate - Network Service Rate	$/kWh	0.0045
Retail Transmission Rate - Line and Transformation Connection Service Rate	$/kWh	0.0038

MONTHLY RATES AND CHARGES - Regulatory Component

Wholesale Market Service Rate	$/kWh	0.0036
Rural or Remote Electricity Rate Protection Charge (RRRP)	$/kWh	0.0013
Ontario Electricity Support Program Charge (OESP)	$/kWh	0.0011
Standard Supply Service - Administrative Charge (if applicable)	$	0.25

Hydro One Orillia

TARIFF OF RATES AND CHARGES

Effective and Implementation Date XXX X, 2016

This schedule supersedes and replaces all previously approved schedules of Rates, Charges and Loss Factors

EB-2016-XXXX

SENTINEL LIGHTING SERVICE CLASSIFICATION

This classification refers to accounts that are unmetered lighting load supplied to a sentinel light. Further servicing details are available in the distributor's Conditions of Service.

APPLICATION

The application of these rates and charges shall be in accordance with the Licence of the Distributor and any Code or Order of the Ontario Energy Board, and amendments thereto as approved by the Ontario Energy Board, which may be applicable to the administration of this schedule.

No rates and charges for the distribution of electricity and charges to meet the costs of any work or service done or furnished for the purpose of the distribution of electricity shall be made except as permitted by this schedule, unless required by the Distributor's Licence or a Code or Order of the Ontario Energy Board, and amendments thereto as approved by the Ontario Energy Board, or as specified herein.

Unless specifically noted, this schedule does not contain any charges for the electricity commodity, be it under the Regulated Price Plan, a contract with a retailer or the wholesale market price, as applicable. In addition, the charges in the MONTHLY RATES AND CHARGES - Regulatory Component of this schedule do not apply to a customer that is an embedded wholesale market participant.

It should be noted that this schedule does not list any charges, assessments, or credits that are required by law to be invoiced by a distributor and that are not subject to Ontario Energy Board approval, such as the Debt Retirement Charge, the Global Adjustment and the HST.

MONTHLY RATES AND CHARGES - Delivery Component

Service Charge (per connection)	$	3.88
Distribution Volumetric Rate	$/kW	10.1477
Low Voltage Service Rate	$/kW	0.1698
Rate Rider for Disposition of Account 1576 - effective until December 31, 2016 - Approved on an Interim Basis	$/kW	(1.7307)
Rate Rider for Disposition of Deferral/Variance Accounts (2016) - effective until April 30, 2017	$/kW	0.4427
Rate Rider for Disposition of Deferral/Variance Accounts (2016) - effective until April 30, 2017 Applicable only for Non-Wholesale Market Participants	$/kW	(1.0052)
Rate Rider for Disposition of Global Adjustment Account (2016) - effective until April 30, 2017 Applicable only for Non-RPP Customers	$/kW	2.4517
Rate Rider for Application of Tax Change (2016) – effective until April 30, 2017	$/kW	(0.0652)
Retail Transmission Rate - Network Service Rate	$/kW	1.4801
Retail Transmission Rate - Line and Transformation Connection Service Rate	$/kW	1.1710

MONTHLY RATES AND CHARGES - Regulatory Component

Wholesale Market Service Rate	$/kWh	0.0036
Rural or Remote Electricity Rate Protection Charge (RRRP)	$/kWh	0.0013
Ontario Electricity Support Program Charge (OESP)	$/kWh	0.0011
Standard Supply Service - Administrative Charge (if applicable)	$	0.25

Hydro One Orillia

TARIFF OF RATES AND CHARGES

Effective and Implementation Date XXX X, 2016

This schedule supersedes and replaces all previously approved schedules of Rates, Charges and Loss Factors

EB-2016-XXXX

STREET LIGHTING SERVICE CLASSIFICATION

This classification applies to an account for roadway lighting with a Municipality, Regional Municipality, Ministry of Transportation and private roadway lighting, controlled by photo cells. The consumption for these customers will be based on the calculated connected load times the required lighting times established in the approved Ontario Energy Board street lighting load shape template. Further servicing details are available in the distributor's Conditions of Service.

APPLICATION

The application of these rates and charges shall be in accordance with the Licence of the Distributor and any Code or Order of the Ontario Energy Board, and amendments thereto as approved by the Ontario Energy Board, which may be applicable to the administration of this schedule.

No rates and charges for the distribution of electricity and charges to meet the costs of any work or service done or furnished for the purpose of the distribution of electricity shall be made except as permitted by this schedule, unless required by the Distributor's Licence or a Code or Order of the Ontario Energy Board, and amendments thereto as approved by the Ontario Energy Board, or as specified herein.

Unless specifically noted, this schedule does not contain any charges for the electricity commodity, be it under the Regulated Price Plan, a contract with a retailer or the wholesale market price, as applicable. In addition, the charges in the MONTHLY RATES AND CHARGES - Regulatory Component of this schedule do not apply to a customer that is an embedded wholesale market participant.

It should be noted that this schedule does not list any charges, assessments, or credits that are required by law to be invoiced by a distributor and that are not subject to Ontario Energy Board approval, such as the Debt Retirement Charge, the Global Adjustment and the HST.

MONTHLY RATES AND CHARGES - Delivery Component

Service Charge (per connection)	$	4.56
Distribution Volumetric Rate	$/kW	15.1656
Low Voltage Service Rate	$/kW	0.1663
Rate Rider for Disposition of Account 1576 - effective until December 31, 2016 - Approved on an Interim Basis	$/kW	(1.7205)
Rate Rider for Disposition of Deferral/Variance Accounts (2016) - effective until April 30, 2017	$/kW	0.4688
Rate Rider for Disposition of Deferral/Variance Accounts (2016) - effective until April 30, 2017 Applicable only for Non-Wholesale Market Participants	$/kW	(0.9992)
Rate Rider for Disposition of Global Adjustment Account (2016) - effective until April 30, 2017 Applicable only for Non-RPP Customers	$/kW	2.4504
Rate Rider for Application of Tax Change (2016) – effective until April 30, 2017	$/kW	(0.0761)
Retail Transmission Rate - Network Service Rate	$/kW	1.4726
Retail Transmission Rate - Line and Transformation Connection Service Rate	$/kW	1.1469

MONTHLY RATES AND CHARGES - Regulatory Component

Wholesale Market Service Rate	$/kWh	0.0036
Rural or Remote Electricity Rate Protection Charge (RRRP)	$/kWh	0.0013
Ontario Electricity Support Program Charge (OESP)	$/kWh	0.0011
Standard Supply Service - Administrative Charge (if applicable)	$	0.25

Hydro One Orillia

TARIFF OF RATES AND CHARGES

Effective and Implementation Date XXX X, 2016

This schedule supersedes and replaces all previously approved schedules of Rates, Charges and Loss Factors

EB-2016-XXXX

microFIT SERVICE CLASSIFICATION

This classification applies to an electricity generation facility contracted under the Independent Electricity System Operator's microFIT program and connected to the distributor's distribution system. Further servicing details are available in the distributor's Conditions of Service.

APPLICATION

The application of these rates and charges shall be in accordance with the Licence of the Distributor and any Code or Order of the Ontario Energy Board, and amendments thereto as approved by the Ontario Energy Board, which may be applicable to the administration of this schedule.

No rates and charges for the distribution of electricity and charges to meet the costs of any work or service done or furnished for the purpose of the distribution of electricity shall be made except as permitted by this schedule, unless required by the Distributor's Licence or a Code or Order of the Ontario Energy Board, and amendments thereto as approved by the Ontario Energy Board, or as specified herein.

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It should be noted that this schedule does not list any charges, assessments, or credits that are required by law to be invoiced by a distributor and that are not subject to Ontario Energy Board approval, such as the Debt Retirement Charge, the Global Adjustment and the HST.

MONTHLY RATES AND CHARGES - Delivery Component

Service Charge	$	5.40

Hydro One Orillia

TARIFF OF RATES AND CHARGES

Effective and Implementation Date XXX X, 2016

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ALLOWANCES

Transformer Allowance for Ownership - per kW of billing demand/month	$/kW	(0.60)
Primary Metering Allowance for transformer losses - applied to measured demand and energy	%	(1.00)

SPECIFIC SERVICE CHARGES

The application of these rates and charges shall be in accordance with the Licence of the Distributor and any Code or Order of the Ontario Energy Board, and amendments thereto as approved by the Ontario Energy Board, which may be applicable to the administration of this schedule.

No charges to meet the costs of any work or service done or furnished for the purpose of the distribution of electricity shall be made except as permitted by this schedule, unless required by the Distributor's Licence or a Code or Order of the Ontario Energy Board, and amendments thereto as approved by the Ontario Energy Board, or as specified herein.

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Customer Administration

Arrears certificate	$	15.00
Easement charge for unregistered rights	$	15.00
Returned cheque charge (plus bank charges)	$	15.00
Account set up charge	$	30.00
Special meter reads	$	30.00
Meter dispute charge plus Measurement Canada fees (if meter found correct)	$	30.00

Non-Payment of Account

Late Payment - per month	%	1.50
Late Payment - per annum	%	19.56
Collection of account charge - no disconnection/Load Limiter	$	30.00
Collection/Disconnect/Load Limiter/Reconnect trip (at meter) - during regular hours	$	65.00
Collection/Disconnect/Load Limiter/Reconnect trip (at meter) - after regular hours	$	185.00
Collection/Disconnect/Load Limiter/Reconnect trip (at pole) - during regular hours	$	185.00
Collection/Disconnect/Load Limiter/Reconnect trip (at pole) - after regular hours	$	415.00

Other

Temporary service install & remove	$	500.00
Specific Charge for Cable and Telecom Companies Access to the Power Poles - $/pole/year	$	41.28
Charge for LDCs Access to the Power Poles - $/pole/year	$	see below
Specific Charge for Generator Access to the Power Poles - $/pole/year	$	see below
Service Layout Fee – Basic	$	635.00
Service Layout Fee – Complex	$	845.00
Crossing Application – Pipeline	$	2,540.00
Crossing Application – Water	$	3,225.00
Crossing Application – Railroad	$	6,095.00
Line Staking - $/meter	$	4.95
Central Metering – New Service < 45 kW	$	120.00
Conversion to Central Metering < 45 kW	$	1,045.00
Conversion to Central Metering > 45 kW	$	925.00
Tingle Voltage Test in excess of 4 hours – per hour (average 2 additional hours)	$	140.00
Standby Administration Charge – per month	$	520.00
Connection Impact Assessment (CIA) Charge – CAE Small DG & Net Metering	$	5,620.00
Connection Impact Assessment (CIA) Charge – Greater than CAE Small DG & Net Metering	$	12,055.00
Sentinel Lights Rental Rate – per month	$	9.25
Sentinel Lights Pole Rental Rate – per month	$	4.15
Joint Use for Municipality Streetlights per year	$	2.04

Hydro One Orillia

TARIFF OF RATES AND CHARGES

Effective and Implementation Date XXX X, 2016

This schedule supersedes and replaces all previously approved schedules of Rates, Charges and Loss Factors

EB-2016-XXXX

Specific Charge for LDCs Access to the Power Poles ($/pole/year)

LDC Rate for 10’ of power space	$	47.34
LDC Rate for 15’ of power space	$	56.81
LDC Rate for 20’ of power space	$	63.44
LDC Rate for 25' of power space	$	67.23
LDC Rate for 30' of power space	$	71.02
LDC Rate for 35' of power space	$	73.86
LDC Rate for 40' of power space	$	75.75
LDC Rate for 45' of power space	$	77.64
LDC Rate for 50' of power space	$	78.59
LDC Rate for 55' of power space	$	80.49
LDC Rate for 60’ of power space	$	81.43

Specific Charge for Generator Access to the Power Poles ($/pole/year)

Generator Rate for 10’ of power space	$	47.34
Generator Rate for 15’ of power space	$	56.81
Generator Rate for 20’ of power space	$	63.44
Generator Rate for 25' of power space	$	67.23
Generator Rate for 30' of power space	$	71.02
Generator Rate for 35' of power space	$	73.86
Generator Rate for 40' of power space	$	75.75
Generator Rate for 45' of power space	$	77.64
Generator Rate for 50' of power space	$	78.59
Generator Rate for 55' of power space	$	80.49
Generator Rate for 60’ of power space	$	81.43

Hydro One Orillia

TARIFF OF RATES AND CHARGES

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EB-2016-XXXX

RETAIL SERVICE CHARGES (if applicable)

The application of these rates and charges shall be in accordance with the Licence of the Distributor and any Code or Order of the Ontario Energy Board, and amendments thereto as approved by the Ontario Energy Board, which may be applicable to the administration of this schedule.

No rates and charges for the distribution of electricity and charges to meet the costs of any work or service done or furnished for the purpose of the distribution of electricity shall be made except as permitted by this schedule, unless required by the Distributor's Licence or a Code or Order of the Ontario Energy Board, and amendments thereto as approved by the Ontario Energy Board, or as specified herein.

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It should be noted that this schedule does not list any charges, assessments, or credits that are required by law to be invoiced by a distributor and that are not subject to Ontario Energy Board approval, such as the Debt Retirement Charge, the Global Adjustment and the HST.

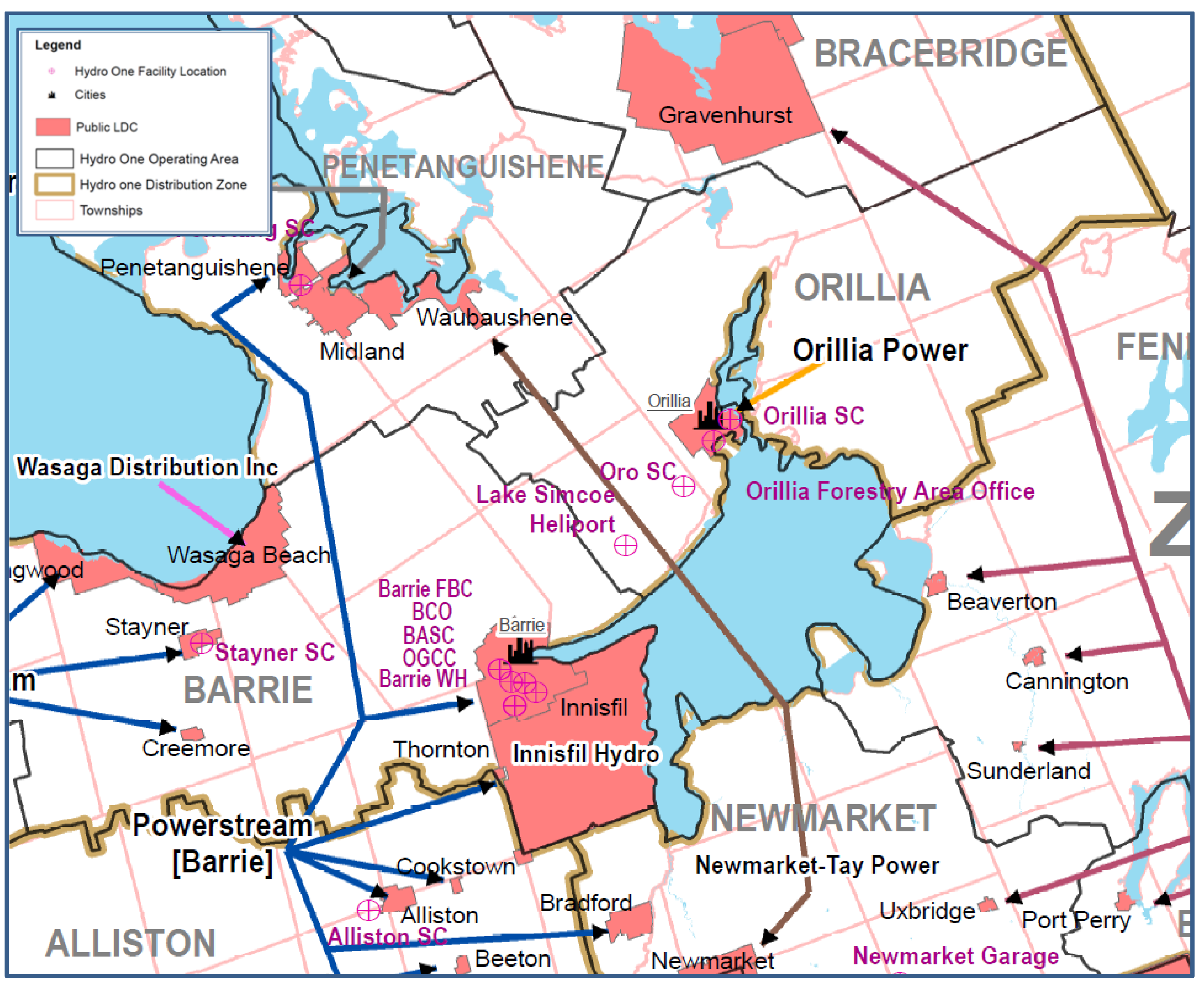
Retail Service Charges refer to services provided by a distributor to retailers or customers related to the supply of competitive electricity.

One-time charge, per retailer, to establish the service agreement between the distributor and the retailer	$	100.00
Monthly Fixed Charge, per retailer	$	20.00
Monthly Variable Charge, per customer, per retailer	$/cust.	0.50
Distributor-consolidated billing monthly charge, per customer, per retailer	$/cust.	0.30
Retailer-consolidated billing monthly credit, per customer, per retailer	$/cust.	(0.30)
Service Transaction Requests (STR)		
Request fee, per request, applied to the requesting party	$	0.25
Processing fee, per request, applied to the requesting party	$	0.50
Request for customer information as outlined in Section 10.6.3 and Chapter 11 of the Retail Settlement Code directly to retailers and customers, if not delivered electronically through the Electronic Business Transaction (EBT) system, applied to the requesting party		
Up to twice a year		
More than twice a year, per request (plus incremental delivery costs)		

LOSS FACTORS

If the distributor is not capable of prorating changed loss factors jointly with distribution rates, the revised loss factors will be implemented upon the first subsequent billing for each billing cycle.

Total Loss Factor - Secondary Metered Customer < 5,000 kW	1.0561
Total Loss Factor - Primary Metered Customer < 5,000 kW	1.0455


Legend
Hydro One Facility Location
Cities
Public LDC
Hydro One Operating Area
Hydro one Distribution Zone
Townships
BRACEBRIDGE
Gravenhurst
PENETANGUISHENE
Penetanguishene
Midland
Waubaushene
ORILLIA
Orillia Power
Orillia
Orillia SC
Oro SC
Orillia Forestry Area Office
Lake Simcoe
Heliport
Wasaga Distribution Inc
Wasaga Beach
Stayner
Stayner SC
Barrie FBC
BCO
BASC
OGCC
Barrie WH
Barrie
BARRIE
Innisfil
Innisfil Hydro
Creemore
Thornton
Beaverton
Cannington
Sunderland
NEWMARKET
Newmarket-Tay Power
Powerstream
[Barrie]
Cookstown
Alliston
Alliston SC
ALLISTON
Bradford
Beeton
Uxbridge
Port Perry
Newmarket
Newmarket Garage

Attachment 11

Province of Ontario Distribution Sector

Province of Ontario Distribution Sector
Disclaimer: This map should be used for reference purposes only - All information should be subject to validation/verification by appropriate agents before any other use. Date: 3/5/2015
Document Name: ONTARIO_H1_DISTRIBUTION_Overview_Map
ZONE 1
ZONE 2
ZONE 3A
ZONE 3B
ZONE 4
ZONE 5
ZONE 6
Legend
Hydro One Facility Location
Cities
Brampton Hydro Networks Inc.
Acquired LDC (Norfolk,Haldimand,Woodstock)
Public LDC
Private LDC
Hydro One Operating Area
Hydro one Distribution Zone
Townships
Northern Ontario
Lake Huron
Georgian Bay
Lake Ontario
Lake Erie
Michigan, U.S.A.
0 20 40 80 120 160 Kilometers 1:675,000
hydro one

Orillia Power Distribution Corporation

FINANCIAL STATEMENTS

December 31, 2015

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Independent Auditor's Report

To the Shareholder of Orillia Power Distribution Corporation

We have audited the accompanying financial statements of Orillia Power Distribution Corporation, which comprise the statement of financial position as at December 31, 2015 and the statements of comprehensive income, changes in equity and cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these 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 and whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the 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 evaluation the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

BDO Canada LLP, a Canadian limited liability partnership, is a member of BDO International Limited, a UK company limited by guarantee, and forms part of the international BDO network of independent member firms.

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Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of Orillia Power Distribution Corporation as at December 31, 2015, and the results of its operations and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Comparative Information

Without modifying our opinion we draw attention to Note 29 to the financial statements which describes that Orillia Power Distribution Corporation adopted International Financial Reporting Standards on January 1, 2015 with a transition date of January 1, 2014. These standards were applied retrospectively by management to the comparative information in these financial statements, including the statement of financial position as at December 31, 2014 and January 1, 2014, and the statements of comprehensive income, changes in equity and cash flows for the year ended December 31, 2015 and related disclosures. We were not engaged to report on the restated comparative information, and as such, it is unaudited.

BDO Canada LLP

Chartered Professional Accountants, Licensed Public Accountants

Orillia, Ontario
April 4, 2016

BDO Canada LLP, a Canadian limited liability partnership, is a member of BDO International Limited, a UK company limited by guarantee, and forms part of the international BDO network of independent member firms.

STATEMENT OF FINANCIAL POSITION

As at (in thousands of Canadian dollars)	Notes	December 31 2015	Unaudited December 31 2014	Unaudited January 1 2014
		$	$	$
ASSETS				
Current Assets				
Cash and cash equivalents	5	**602**	77	20
Accounts receivable	6	**3,419**	4,205	3,524
Unbilled energy and distribution revenue	7	**4,153**	3,800	3,985
Payment in lieu of taxes receivable	14	**-**	-	355
Inventories	8	**501**	526	618
Prepaid expenses		**170**	195	166
Due from related parties	25	**867**	768	827
Current assets		**9,712**	9,571	9,495
Non-current Assets				
Property, plant and equipment	9	**23,586**	22,485	20,330
Intangible assets	10	**125**	144	137
Deferred income tax asset	14	**1,079**	1,233	1,451
Non-current assets		**24,790**	23,862	21,918
Total assets		**34,502**	33,433	31,413
Regulatory deferral account debit balances	11	**2,126**	1,598	1,930
Total assets and regulatory deferral account debit balances		**36,628**	35,031	33,343

The accompanying notes are an integral part of these financial statements

STATEMENT OF FINANCIAL POSITION

As at
(in thousands of Canadian dollars)

	Notes	December 31 2015	Unaudited December 31 2014	Unaudited January 1 2014
		$	$	$
LIABILITIES AND SHAREHOLDER'S EQUITY				
Current Liabilities				
Bank indebtedness	12	**2,000**	200	950
Accounts payable and accrued liabilities	13	**5,759**	6,667	5,722
Payment in lieu of taxes payable	14	**217**	-	-
Customer security deposits	15	**133**	68	71
Current portion of long term debt	18	**210**	210	210
Due to related parties	25	**55**	57	-
Current liabilities		**8,374**	7,202	6,953
Non-current Liabilities				
Customer security deposits	15	**320**	277	238
Post-retirement benefits	16	**648**	637	752
Deferred revenue	17	**1,166**	1,060	-
Long term debt	18	**10,497**	10,707	10,917
Non-current liabilities		**12,631**	12,681	11,907
Shareholder's Equity				
Share capital	19	**8,236**	8,236	8,236
Retained earnings		**4,505**	4,862	3,645
Accumulated other comprehensive loss		**(105)**	(105)	(195)
Shareholder's equity		**12,636**	12,993	11,686
Total liabilities and shareholder's equity		**33,641**	32,876	30,546
Regulatory deferral account credit balances	11	**2,987**	2,155	2,797
Total equity, liabilities and regulatory deferral account credit balances		**36,628**	35,031	33,343

The accompanying notes are an integral part of these financial statements

Note regarding potential sale of the Company **2.8**

On Behalf of the Board of Directors:

Director Director

STATEMENT OF COMPREHENSIVE INCOME

Year ended December 31

(in thousands of Canadian dollars)

	Notes	2015 $	Unaudited 2014 $
Revenue			
Recovered energy purchases		**36,546**	33,821
Operating revenue	20	**8,535**	8,653
		45,081	42,474
Expenses			
Energy purchases		**36,292**	34,050
Operating expenses	21	**4,849**	4,598
Depreciation and amortization		**1,150**	1,101
Loss on disposal of property plant and equipment		**79**	16
		42,370	39,765
Operating profit		**2,711**	2,709
Finance income	22	**8**	14
Finance costs	22	**(682)**	(696)
Profit before payments in lieu of taxes		**2,037**	2,027
Provision for payment in lieu of taxes			
Current provision	14	**322**	74
Deferred provision	14	**154**	185
		476	259
Profit for the year before net movement in regulatory deferral account balances		**1,561**	1,768
Net movement in regulatory deferral account balances	11	**(688)**	(551)
Profit for the year after net movement in regulatory deferral account balances		**873**	1,217
Other comprehensive income:			
Items that will not be reclassified subsequently to profit and loss:			
Actuarial gain on defined benefit plans net of deferred taxes		**-**	90
Total comprehensive income for the year		**873**	1,307

The accompanying notes are an integral part of these financial statements

STATEMENT OF CHANGES IN EQUITY

Year ended December 31

(in thousands of Canadian dollars)

	Share Capital	Accumulated Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Consolidated Totals
	$	$	$	$
SUMMARY OF CHANGES IN EQUITY				
Balance at January 1, 2014 (unaudited)	8,236	3,645	(195)	11,686
Changes in equity during 2014				
Total comprehensive income for the year	-	1,217	90	1,307
Dividends paid	-	-	-	-
Balance at December 31, 2014 (unaudited)	8,236	4,862	(105)	12,993
Changes in equity during 2015				
Total comprehensive income for the year	**-**	**873**	**-**	**873**
Dividends paid	**-**	**(1,230)**	**-**	**(1,230)**
Balance at December 31, 2015	**8,236**	**4,505**	**(105)**	**12,636**

The accompanying notes are an integral part of these financial statements

STATEMENT OF CASH FLOWS

Year ended December 31

(in thousands of Canadian dollars)

	Notes	2015	Unaudited 2014
		$	$
Cash flows from operating activities			
Profit for the year after net movement in regulatory deferral account balances		**873**	1,217
Adjustments to reconcile profit to net cash used in operating activities			
Depreciation and amortization (non-cash)		**1,150**	1,101
Other non-cash or non-operating items included in profit	23	**1,899**	1,502
		3,922	3,820
Net changes in non-cash working capital	24	**(444)**	230
Income taxes paid	14	**(322)**	(74)
Cash generated from operating activities net of taxes paid		**3,156**	3,976
Cash flows from investing activities			
Purchase of property, plant, equipment and intangible assets	9, 10	**(2,311)**	(3,265)
Interest received	22	**8**	14
Changes in regulatory deferral account balances	11	**(384)**	(875)
Net cash used in investing activities		**(2,687)**	(4,126)
Cash flows from financing activities			
Borrowing on term debt facility	12	**2,000**	-
Repayment of long term debt	18	**(210)**	(210)
Deferred revenue	17	**135**	1,074
Customer security deposits	15	**43**	39
Interest paid	22	**(682)**	(696)
Dividends paid in cash		**(1,230)**	-
Net cash used in financing activities		**56**	207
Net increase (decrease) in cash and cash equivalents during the year		**525**	57
Cash and cash equivalents, beginning of the year		**77**	20
Cash and cash equivalents, end of the year		**602**	77

The accompanying notes are an integral part of these financial statements

NOTES TO THE FINANCIAL STATEMENTS

For the year ended December 31, 2015
(in thousands of Canadian dollars unless otherwise noted)

1. CORPORATE INFORMATION

Orillia Power Distribution Corporation (the "Company") owns and operates an electricity distribution system, which delivers electricity to approximately 13,500 customers located in Orillia, Ontario. The address of the Company's corporate office and principal place of business is 360 West Street South, Orillia, Ontario, Canada L3V 6J9.

Orillia Power Corporation is the sole shareholder of the Company.

The Company was incorporated under the Business Corporations Act (Ontario) on October 26, 2000. The Company operates under license issued by the Ontario Energy Board ("OEB"). The Company is regulated by the OEB and adjustments to the Company's distribution and power rates require OEB approval.

2. BASIS OF PREPARATION

2.1 Statement of compliance

The Financial Statements of the Company have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") and interpretations as issued by the International Financial Reporting Interpretations Committee ("IFRIC") of the IASB.

These are the Company's first Financial Statements prepared in accordance with IFRS and IFRS 1 First-time Adoption of International Financial Reporting Standards has been applied. They should be read in conjunction with the 2014 Canadian generally accepted accounting principles ("Canadian GAAP") Financial Statements and related notes. In this context, the term "Canadian GAAP" refers to generally accepted accounting principles before the adoption of IFRS.

The Financial Statements were authorized for issue by the Board of Directors on April 4, 2016.

2.2 First time adoption of IFRS

The transition to IFRS resulted in a decrease of shareholders equity of $195 and $93 at January 1, 2014 and December 31, 2014 respectively and an increase in Comprehensive Income for the year end December 31, 2014 of $102. In addition, the adoption of IFRS 14, Regulatory Deferral Accounts, resulted in a significant change in presentation, as regulatory deferral accounts are now presented separately from assets and liabilities and the change in regulatory deferral accounts is presented separately from net profit. An explanation of how the transition to IFRS has affected the reported financial position, financial performance and cash flows of the Company is provided in the last note to these financial statements.

2.3 Basis of measurement

The Financial Statements have been prepared on a historical cost basis.

2.4 Presentation currency

The Financial Statements are presented in Canadian dollars (CAD), which is also the Company's functional currency, and all values are rounded to the nearest one thousand dollars, unless when otherwise indicated.

2.5 Explanation of activities subject to rate regulation

The Ontario government enacted the Energy Competition Act, 1998, to introduce competition to the Ontario energy market. The Ontario Energy Board ("OEB") was granted a legislative mandate including broad powers relating to licensing, standards of conduct and service quality and the regulation of rates charged by the Company and other electricity distributors in Ontario.

The Company as an electricity generator and distributor, is licensed and regulated by the OEB. The OEB exercises statutory authority through setting or approving all rates charged by the distribution company and establishing standards of service quality for its customers. The Company's distribution rates are set by the OEB on an annual basis for May 1 to April 30.

2.6 Regulatory risk

Regulatory risk is the risk that the Province and its regulator, the Ontario Energy Board, could establish a regulatory regime that imposes conditions that restrict the electricity distribution business from achieving an acceptable rate of return that permits financial sustainability of its operations including the recovery of expenses incurred for the benefit of other market participants in the electricity industry such as transition costs and other regulatory assets. All requests for changes in electricity distribution charges require the approval of the OEB.

2.7 Recovery risk

Regulatory developments in Ontario's electricity industry, including current and possible future consultations between the OEB and interested stakeholders, may affect distribution rates and other permitted recoveries in the future. Orillia Power Distribution Corporation is subject to a cost of service regulatory mechanism under which the OEB establishes the revenues required (i) to recover the forecast operating costs, including depreciation and amortization and income taxes, of providing the regulated service, and (ii) to provide a fair and reasonable return on utility investment, or rate base. As actual operating conditions may vary from forecast, actual returns achieved can differ from approved returns.

2.8 Potential sale of the Company

The City of Orillia and Orillia Power Corporation are currently in negotiations with Hydro One to sell Orillia Power Distribution Corporation. A purchase agreement has not been signed between the negotiating parties as of the date of approval of these financial statements by the Board of Directors.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The preparation and presentation of financial statements can be significantly affected by the accounting policies selected by the Company. The financial statements reflect the following significant accounting policies, which are an integral part of understanding the financial results and financial position presented within.

The accounting policies set out below have been applied consistently to all periods presented in these Financial Statements and in preparing the opening IFRS Statement of Financial Position at January 1, 2014 for the purposes of the transition to IFRS, unless otherwise indicated.

3.1 Regulatory deferral accounts

The Company has applied early adoption of IFRS 14 Regulatory Deferral Accounts. In accordance with IFRS 14, the Company has continued to apply the accounting policies it applied in accordance with the pre-changeover Canadian GAAP for the recognition, measurement and impairment of assets and liabilities arising from rate regulation. These are referred to as regulatory deferral account balances.

Regulatory deferral account debit balances represent future revenues associated with certain costs incurred in the current period or in prior period(s), which are expected to be recovered from consumers in future periods through the rate-setting process. Regulatory deferral account credit balances are associated with the collection of certain revenues earned in the current period or in prior period(s), which are expected to be returned to consumers in future periods through the rate-setting process.

Regulatory deferral account balances can arise from differences in amounts collected from customers (based on regulated rates) and the corresponding cost of non-competitive electricity service incurred by the Company in the wholesale market administered by the Independent Electricity System Operator (the "IESO") after May 1, 2002. These amounts have been accumulated pursuant to regulation underlying the Electricity Act (the "EA") and deferred in anticipation of their future recovery (payment) from (to) distribution customers.

3.1 Regulatory deferral accounts (continued)

Explanation of Recognized Amounts

Regulatory deferral account balances are recognized and measured initially and subsequently at cost. They are assessed for impairment on the same basis as other non-financial assets as described below. Management continually assesses the likelihood of recovery of regulatory assets. If recovery through future rates is no longer considered probable, the amounts would be charged to the results of operations in the period that the assessment is made.

3.2 Revenue

Revenue is recognized to the extent that it is probable that economic benefits will flow to the Company and that the revenue can be reliably measured. Revenue is comprised of recovered energy purchases, distribution of energy, pole use rental, collection charges, investment income and other miscellaneous revenues.

Recovered energy purchases and distribution of energy

The Company is licensed by the OEB to distribute electricity. As a licensed distributor, the Company 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. The Company is required, pursuant to regulation, to remit such amounts to these third parties, irrespective of whether the Company ultimately collects these amounts from customers. The Company has determined that they are acting as a principal for the electricity distribution and, therefore, have presented the electricity revenues on a gross basis.

Revenues from recovered energy purchases and distribution of electricity is recognized on an accrual basis, including unbilled revenues accrued in respect of electricity delivered but not yet billed. Recovered energy purchases and distribution of energy revenue is comprised of customer billings based on actual monthly meter readings.

Other

Other revenues, which include revenues from pole use rental, collection charges, contributions in aid of construction and other miscellaneous revenues are recognized at the time services are provided.

Deferred revenue

Where the Company has an ongoing obligation to provide services, revenues are recognized as the service is performed and amounts billed in advance are recognized as deferred revenue.

Certain assets may be acquired or constructed with financial assistance in the form of contributions from customers when the estimated revenue is less than the cost of providing service or where special equipment is needed to supply the customers' specific requirements. Since the contributions in aid of construction will provide customers with ongoing access to the supply of electricity, these contributions are classified as deferred revenue and are amortized as revenue on a straight-line basis over the useful life of the constructed or contributed asset.

3.3 Cash and cash equivalents

Cash and cash equivalents include cash on hand, deposits held at call with financial institutions, other short-term, highly liquid investments with original maturities of three months or less that are readily convertible to known amounts of cash and subject to an insignificant risk of change in value.

3.4 Financial instruments

Recognition, initial measurement and derecognition

Financial assets and liabilities are recognized when the Company becomes a party to the contractual provisions of the financial instrument and are measured initially at fair value adjusted for transaction costs, except for those carried at fair value through comprehensive income which are measured initially at fair value. Subsequent measurement of financial assets and financial liabilities is described below.

Financial assets are derecognized when the contractual rights to the cash flows from the financial asset expire, or when the financial asset and substantially all the risks and rewards are transferred. A financial liability is derecognized when it is extinguished, discharged, cancelled or expires.

Classification and subsequent measurement of financial assets

For the purpose of subsequent measurement of financial assets, they are classified into the following categories upon initial recognition, loans and receivables and available-for-sale financial assets. The company currently does not have assets that would be classified as available for sale. All financial assets classified as loans and receivables are reviewed for impairment at least at each reporting date to identify whether there is any objective evidence of impairment. All income and expenses relating to financial assets that are recognized in profit or loss are presented within finance costs or finance income, except for impairment of trade receivables which is presented within operating expenses.

Financial assets classified as loans and receivables

Financial assets classified as loans and receivables include cash and cash equivalents, accounts receivable, unbilled energy and distribution revenue and due from related parties. Collectability of accounts receivable is reviewed on an ongoing basis. Individually significant receivables are considered for impairment when they are past due or when other objective evidence is received that a specific counterparty will default. Receivables that are not considered to be individually impaired are reviewed for impairment in groups, which are determined by reference to the industry and region of the counterparty and other shared credit risk characteristics. The impairment loss estimate is then based on recent historical counterparty default rates for each identified group. Accounts receivable which are known to be uncollectible are written off. A provision for doubtful receivables is established when there is objective evidence that the Company will not be able to collect all amounts due according to the original terms of the receivables. The amount of the provision is the difference between the asset's carrying amount and the present value of future cash flows. The amount of the provision is recognized in the Statement of Comprehensive Income.

Classification and subsequent measurement of financial liabilities

All of the Company's financial liabilities are classified as other financial liabilities, and include bank indebtedness, accounts payables and accrued liabilities, customer deposits, due to related parties, promissory notes and Infrastructure Ontario Loans. Other financial liabilities are measured subsequently at amortized cost using the effective interest method. All interest-related charges are reported in profit or loss and included within finance costs or finance income.

Customer Security Deposits

Customers may be required to post security to obtain electricity or other services, which are refundable. Cash and securities lodged with the Company by counterparties under electricity supply agreements are also included in this balance. Where the security posted is in the form of cash or cash equivalents, these amounts are recorded in the accounts as customer security deposits. Interest rates paid on customer deposits are based on the Bank of Canada's prime business rate less 2%.

3.5 Property, plant and equipment

Recognition and measurement

Property, plant and equipment ("PP&E") are recognized at cost, being the purchase price and directly attributable cost of acquisition or construction required to bring the asset to the location and condition necessary to be capable of operating in the manner intended by the Company, including eligible borrowing costs.

Depreciation of PP&E is recorded in the Statements of Comprehensive Income on a straight-line basis over the estimated useful life of the related asset. The estimated useful lives, residual values and depreciation methods are reviewed at the end of each annual reporting period, with the effect of any changes in estimate being accounted for on a prospective basis.

The estimated useful lives for PP&E are as follows:

Buildings and fixtures	10 - 50 years
Substations	15 - 60 years
Sub-transmission lines	45 - 60 years
Distribution system	40 - 60 years
Smart meters	15 years
Other capital assets	15 - 20 years
Land	not depreciated

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

Major spare parts

Major spares such as spare transformers and other items kept as standby/back up equipment are accounted for as PP&E since they support the Company's distribution system reliability.

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 net of payments to the developer recognized as deferred revenue (contributions in aid of construction).

Gains and losses on disposal

Gains and losses on disposal of an item of property, plant and equipment are determined by comparing the net proceeds from disposal with the carrying amount of the asset, and are included in the Statement of Comprehensive Income when the asset is disposed of. When an item of property, plant and equipment with related Contributions in aid of construction is disposed, the remaining deferred revenue is recognized in full in the Statement of Comprehensive Income.

3.6 Borrowing costs

The Company capitalizes interest expenses and other finance charges directly relating to the acquisition, construction or production of assets that take a substantial period of time to get ready for its intended use. Capitalization commences when expenditures are being incurred, borrowing costs are being incurred and activities that are necessary to prepare the asset for its intended use or sale are in progress. Capitalization is suspended during periods in which active development is interrupted and ceases when substantially all of the activities necessary to prepare the asset for its intended use or sale are complete.

3.7 Intangible assets

Computer software and land rights

Computer software that is acquired or developed by the Company, 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.

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 Company does not hold title. Land rights are measured at cost less accumulated amortization and accumulated impairment losses.

Amortization

Amortization is recognized in profit or loss on a straight-line basis over the estimated useful lives of intangible assets from the date that they are available for use. Amortization methods and useful lives of all intangible assets are reviewed at each reporting date.

The estimated useful lives for intangible assets are:

Land rights	40 years
Computer software	5 years

3.8 Impairment of non-financial assets

The Company conducts annual internal assessments of the values of property, plant and equipment, intangible assets and regulatory deferral account debit balances to determine whether there are events or changes in circumstances that indicate that their carrying amount may not be recoverable. Where the carrying value exceeds its recoverable amount, which is the higher of value in use and fair value less costs to sell, the asset is written down accordingly.

Where it is not possible to estimate the recoverable amount of an individual asset, the impairment test is carried out on the asset's cash-generating unit (‘CGU’), which is the lowest group of assets to which the asset belongs for which there are separately identifiable cash inflows that are largely independent of the cash inflows from other assets. The entire Company is considered one cash-generating unit for which impairment testing is performed. An impairment loss is charged to the Statement of Comprehensive Income, except to the extent it reverses gains previously recognized in other comprehensive income.

3.9 Provisions

A provision is recognized if, as a result of a past event, the Company has a present 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.

3.10 Post-retirement benefits

Defined contribution plan

The employees of the Company participate in the Ontario Municipal Employees Retirement System (“OMERS”). The Company also makes contributions to the OMERS plan on behalf of its employees. The plan has a defined benefit option at retirement available to some employees, which specifies the amount of the retirement benefit plan to be received by the employees based on length of service and rates of pay. The Company is only one of a number of employers that participates in the plan and the financial information provided to the Company on the basis of the contractual agreements is insufficient to measure the Company’s proportionate share in the plan assets and liabilities on defined benefit accounting requirements. As insufficient information is available to account for the plan as a defined benefit plan the contribution payable in exchange for services rendered during a period is recognized as an expense during that period.

3.10 Post-retirement benefits (continued)

Defined benefit plans

A defined benefit plan is a post-employment benefit plan other than a defined contribution plan. The Company's net obligation on behalf of its retired employees unfunded life insurance, extended medical and dental benefits is calculated by estimating the amount of future benefits that are expected to be paid out discounted to determine its present value. Any unrecognized past service costs are deducted.

The calculation is performed by a qualified actuary using the projected unit credit method every third year or when there are significant changes to workforce. When the calculation results in a benefit to the Company, the recognized asset is limited to the total of any unrecognized past service costs and the present value of economic benefits available in the form of any future refunds from the plan or reductions in future contributions to the plan. An economic benefit is available to the Company if it is realizable during the life of the plan, or on settlement of the plan liabilities.

Defined benefit obligations are measured using the projected unit credit method discounted to its present value using yields available on high quality corporate bonds that have maturity dates approximating to the terms of the liabilities. Remeasurements of the defined benefit obligation include actuarial gains and losses and are recognized directly within equity in other comprehensive income. Service costs are recognized in the Statement of Comprehensive Income in operating expenses, and include current and past service costs as well as gains and losses on curtailments.

Net interest expense is recognized the Statement of Comprehensive Income in finance expense, and is calculated by applying the discount rate used to measure the defined benefit obligation at the beginning of the annual period to the balance of the net defined benefit obligation, considering the effects of benefit payments during the period. Gains or losses arising from changes to defined benefits or plan curtailment are recognized immediately in the Statement of Comprehensive Income. Settlements of defined benefit plans are recognized in the period in which the settlement occurs.

Other long-term service benefits

Other employee benefits that are expected to be settled wholly within 12 months after the end of the reporting period are presented as current liabilities. Other employee benefits that are not expected to be settled wholly within 12 months after the end of the reporting period are presented as non-current liabilities and calculated using the projected unit credit method and then discounted using yields available on high quality corporate bonds that have maturity dates approximating to the expected remaining period to settlement.

3.11 Payment in lieu of taxes payable

Tax status

The Company is a Municipal Electricity Utility ("MEU") for purposes of the payments in lieu of taxes ("PILs") regime contained in the Electricity Act, 1998. As an MEU, the Company is exempt from tax under the Income Tax Act (Canada) and the Corporations Tax Act (Ontario).

Under the Electricity Act, 1998, the Company is required to make, for each taxation year, PILs to the Ontario Electricity Financial Corporation ("OEFC"), commencing October 1, 2001. 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 Corporation Tax Act (Ontario) as modified by the Electricity Act, 1998, and related regulations.

Current and deferred tax

Income tax expense is comprised of current and deferred tax. Current tax and deferred tax are recognized in comprehensive income except to the extent that it relates to items recognized directly in equity or regulatory deferral account balances. Current income taxes are recognized for the estimated income taxes payable or receivable on taxable income for the current year and any adjustment to income taxes payable in respect of previous years. Current income taxes are determined using tax rates and tax laws that have been enacted or substantively enacted by the year-end date.

3.11 Payment in lieu of taxes payable (continued)

Deferred tax assets and liabilities are recognized where the carrying amount of an asset or liability differs from its tax base. The amount of the deferred tax asset or liability is measured at the amount expected to be recovered from or paid to the taxation authorities. This amount is determined using tax rates and tax laws that have been enacted or substantively enacted by the year-end date and are expected to apply when the liabilities / (assets) are settled / (recovered). The Company recognized deferred tax arising from temporary difference on regulatory deferral account balances, post-retirement benefits and property, plant, equipment and intangible assets.

Recognition of deferred tax assets for unused tax losses, tax credits and deductible temporary differences is restricted to those instances where it is probable that future taxable profit will be available against which the deferred tax asset can be utilized.

At the end of each reporting period, the Company reassesses both recognized and unrecognized deferred tax assets. The Company recognizes a previously unrecognized deferred tax asset to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

3.12 Leased assets

Leases in terms of which the Company 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 Company's balance sheet. Payments made under operating leases are recognized in the Statement of Comprehensive Income on a straight-line basis over the lease term.

3.13 Finance income and finance costs

Finance income is comprised of interest income on funds invested such as cash and cash equivalents. Interest income is recognized as it accrues in the Statement of Comprehensive Income, using the effective interest method. Finance cost is comprised of interest payable on debt, post-retirement benefits and impairment losses recognized on financial assets.

3.14 Inventories

Cost of inventories comprise of direct materials, which typically consists of distribution assets not deemed as major spares, unless purchased for specific capital projects in process or as spare units. Costs, after deducting rebates and discounts, are assigned to individual items of inventory on the basis of weighted average cost. Decommissioned assets that are transferred to inventory are tested for impairment once they are removed from service and placed in inventory. Inventory is recognized at the lower of cost and net realizable value.

Net realizable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

3.15 Standards, amendments and interpretations not yet effective

At the date of authorization of these Financial Statements, certain new standards, amendments and interpretations to existing standards have been published by the IASB but are not yet effective, and have not been adopted early by the Company.

Management anticipates that all of the relevant pronouncements will be adopted in the Company’s accounting policies for the first period beginning after the effective date of the pronouncement. Information on new standards, amendments and interpretations that are expected to be relevant to the Company’s Financial Statements is provided below. Certain other new standards and interpretations have been issued but are not expected to have a material impact on the Company’s Financial Statements.

3.15 Standards, amendments and interpretations not yet effective (continued)

IFRS 9 Financial Instruments replaces IAS 39 Financial Instruments: Recognition and Measurement

IFRS 9 amends the requirements for classification and measurement of financial assets, impairment, and hedge accounting. IFRS 9 retains but simplifies the mixed measurement model and establishes three primary measurement categories for financial assets: amortized cost, fair value through profit or loss, and fair value through other comprehensive income. The basis of classification depends on the entity's business model and the contractual cash flow characteristics of the financial asset. The effective date for IFRS 9 is January 1, 2018. The Company is in the process of evaluating the impact of the new standard.

IFRS 15, Revenue from Contracts with Customers

IFRS 15 is based on the core principle to recognize revenue to depict the transfer of goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. IFRS 15 focuses on the transfer of control. IFRS 15 replaces all of the revenue guidance that previously existed in IFRSs. The effective date for IFRS 15 is January 1, 2018. The Company is in the process of evaluating the impact of the new standard.

IFRS 16, Leases

IFRS 16 requires a lessee to recognize a right-of-use asset and a lease liability. The right-of-use asset is treated similarly to other non-financial assets and depreciated accordingly. The liability accrues interest. This will typically produce a front-loaded expense profile whereas operating leases under IAS 17 would typically have had straight-line expenses. The new Standard is effective for annual reporting periods beginning on or after January 1, 2019, with early application permitted but only if the entity is also applying IFRS 15, Revenue from contracts with customers. The Company is in the process of evaluating the impact of the new standard.

4. USE OF ESTIMATES AND JUDGEMENTS

The Company makes certain estimates and assumptions regarding the future. Estimates and judgements are continually evaluated based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. In the future, actual experience may differ from these estimates and assumptions. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

Employee future benefits

The cost of post-employment life insurance, medical and dental benefits are determined using actuarial valuations. An actuarial valuation involves making various assumptions. Due to the complexity of the valuation, the underlying assumptions and its long term nature, post-employment medical and insurance benefits are highly sensitive to changes in these assumptions. All assumptions are reviewed at each reporting date.

Payments in lieu of taxes payable

The Company is required to make payments in lieu of tax calculated on the same basis as income taxes on taxable income earned. Significant judgement is required in determining the provision for income taxes. There are many transactions and calculations undertaken during the ordinary course of business for which the ultimate tax determination is uncertain. The Company recognizes liabilities for anticipated tax audit issues based on the Company's current understanding of the tax law. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the current and deferred tax provisions in the period in which such determination is made.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended December 31, 2015
(in thousands of Canadian dollars unless otherwise noted)

4. USE OF ESTIMATES AND JUDGEMENTS (continued)

Accounts receivable impairment

In determining the allowance for doubtful accounts, the Company considers historical loss experience of account balances based on the aging and arrears status of accounts receivable balances.

Regulatory deferral account debit and credit balances

In assessing the proper accounting treatment and determining the future disposition of regulatory deferral account debit and credit balances, the Company considers historical industry precedent and follows the latest available and reliable guidance as well as direction through written orders issued by the regulator.

5. CASH AND CASH EQUIVALENTS

The Company's bank accounts are held with a Canadian chartered bank and earn interest based upon its average monthly balance at the bank's prime less 1.9%. Prime rate as of December 31, 2015 was 2.7% (December 31, 2014 – 3.0%, January 1, 2014 – 3%)

6. ACCOUNTS RECEIVABLE

		Unaudited	Unaudited
	December 31	December 31	January 1
Accounts receivable	**2015**	2014	2014
	$	$	$
Due from distribution customers	**2,861**	3,798	3,296
Recoverable work	**298**	275	186
Conservation and feed in tariff initiatives	**193**	106	30
Other	**155**	158	149
	3,507	4,337	3,661
Allowance for doubtful accounts	**(88)**	(132)	(137)
	3,419	4,205	3,524
ACCOUNTS RECEIVABLES BY AGE			
0 - 60 days	**3,143**	3,933	3,406
61 - 90 days	**19**	22	10
Over 90 days	**345**	382	245
	3,507	4,337	3,661
CONTINUITY OF ALLOWANCE FOR DOUBTFUL ACCOUNTS			
Balance, beginning of year	**(132)**	(137)	(151)
Bad debt expense provision included in comprehensive income	**(104)**	(88)	(93)
Written off	**148**	93	107
Balance, end of year	**(88)**	(132)	(137)

6. ACCOUNTS RECEIVABLE (continued)

Due to its short term nature, the carrying amount of the accounts receivable approximates its fair value.

7. UNBILLED ENERGY AND DISTRIBUTION REVENUE

Unbilled energy and distribution revenue represents amounts for which the Company has a contractual right to receive cash through future billings and are un-billed at year end. All accounts are billed on a monthly basis based on power consumed in the previous month. The amount of allowance for doubtful accounts that has been provided as at December 31, 2015 for unbilled revenues is $NIL (December 31, 2014 – $NIL, January 1, 2014 – $NIL) as they are considered current.

		Unaudited	Unaudited
	December 31	December 31	January 1
Unbilled energy and distribution revenue	**2015**	2014	2014
	$	$	$
Unbilled energy and distribution revenue	**4,153**	3,800	3,985
	4,153	3,800	3,985

8. INVENTORIES

		Unaudited
Inventories	**2015**	2014
	$	$
Balance, beginning of year	**526**	618
Inventory purchased	**399**	497
Inventory used in:		
Capital projects (capitalized)	**(246)**	(400)
Operations and maintenance (expensed)	**(95)**	(104)
Recoverable work	**(82)**	(83)
Other adjustments	**(1)**	(2)
Balance, end of year	**501**	526

9. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment	2015	Unaudited 2014
	$	$
COST		
Balance, beginning of year	**23,491**	20,330
Purchase of property, plant, equipment	**2,269**	3,190
Disposals	**(123)**	(29)
Balance, end of year	**25,637**	23,491
ACCUMULATED DEPRECIATION		
Balance, beginning of year	**1,006**	-
Depreciation	**1,089**	1,035
Disposals	**(44)**	(29)
Impairment loss	**-**	-
Balance, end of year	**2,051**	1,006
CARRYING AMOUNTS		
Balance, beginning of year	**22,485**	20,330
Purchase of property, plant, equipment	**2,269**	3,190
Depreciation	**(1,089)**	(1,035)
Disposals	**(79)**	-
Impairment loss	**-**	-
Balance, end of year	**23,586**	22,485
SUMMARY OF CARRYING AMOUNTS BY CATEGORY		
Land and buildings	**1,181**	1,108
Distribution plant and equipment	**21,524**	20,399
Other	**816**	978
Work in progress	**65**	-
Balance, end of year	**23,586**	22,485

10. INTANGIBLE ASSETS

Intangible assets	2015	Unaudited 2014
	$	$
COST		
Balance, beginning of year	**200**	137
Purchase of intangibles	**42**	75
Disposals	**(34)**	(12)
Balance, end of year	**208**	200
ACCUMULATED AMORTIZATION		
Balance, beginning of year	**56**	-
Amortization	**61**	66
Disposals	**(34)**	(10)
Impairment loss	**-**	-
Balance, end of year	**83**	56
CARRYING AMOUNTS		
Balance, beginning of year	**144**	137
Purchase of intangibles	**42**	75
Amortization	**(61)**	(66)
Disposals	**-**	(2)
Impairment loss	**-**	-
Balance, end of year	**125**	144
SUMMARY OF CARRYING AMOUNTS BY CATEGORY		
Land rights	**12**	5
Computer software	**113**	139
Balance, end of year	**125**	144

11. REGULATORY DEFERRAL ACCOUNT BALANCES

All amounts deferred as regulatory deferral account debit balances are subject to approval by the OEB. As such, amounts subject to deferral could be altered by the regulators. Remaining recovery periods are those expected and the actual recovery or settlement periods could differ based on OEB approval. Carrying charges are applied to deferral variance accounts unless indicated otherwise using simple interest at the rate prescribed by the OEB applied to monthly opening balances in the account exclusive of accumulated interest.

11.1 Regulatory deferral account balances net of deferred income tax impacts

Due to previous, existing or expected future regulatory articles or decisions, the Company has the following amounts expected to be recovered by customers (returned to customers) in future periods and as such regulatory deferral account balances are comprised of net of deferred tax impacts:

			Unaudited	Unaudited
		December 31	December 31	January 1
Regulatory deferral account balances		**2015**	2014	2014
	Note	**$**	$	$
REGULATORY DEFERRAL ACCOUNT DEBIT BALANCES NET OF DEFERRED TAXES				
Regulatory deferral account debit balances	11.3	**2,893**	2,138	2,626
Deferred tax impact		**767**	540	696
		2,126	1,598	1,930
REGULATORY DEFERRAL ACCOUNT CREDIT BALANCES NET OF DEFERRED TAXES				
Regulatory deferral account credit balances	11.3	**4,064**	2,927	3,806
Deferred tax impact		**1,077**	772	1,009
		2,987	2,155	2,797

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11.2 Regulatory deferral account impacts on Statements of Comprehensive Income and Cash Flow

The following schedule summarizes the net movement in regulatory deferral account balances adjusted for related deferred tax impacts included in the Statement of Comprehensive Income and reducing profit for the year:

Net movement in regulatory balances including related deferred taxes	2015	Unaudited 2014
	$	$
Regulatory debit reallocated from other income - change in PP&E useful lives	**(648)**	(646)
Retail settlement variances between energy purchased and recovered from customers	**(254)**	229
Lost revenue adjustment reallocated from other revenue	**170**	57
Amortization of stranded meters reallocated from other revenue	**(34)**	(34)
Settlement of PILs variance deferral account	**-**	(67)
Regulatory interest and other	**-**	(9)
Net movement in regulatory balances before related deferred taxes	**(766)**	(470)
Deferred taxes related to changes in regulatory balances	**78**	(81)
	(688)	(551)

All of the above amounts are non-cash accruals added back to profit in order to arrive at cash flows from operating activities on the Statement of Cash Flow (see note 23). The following schedule summarizes the net movement in regulatory deferral account balances impacting cash and included in the investing activities section of the Statement of Cash Flow:

Changes in regulatory deferral account balances on cash flow statement	2015	Unaudited 2014
	$	$
NET REGULATORY DEFERRAL ACCOUNT BALANCES		
Regulatory deferral account debit balances	**2,893**	2,138
Regulatory deferral account credit balances	**4,064**	2,927
Net regulatory deferral account debit (credit) balances	**(1,171)**	(789)
CHANGES IN REGULATORY DEFERRAL ACCOUNT BALANCES (CASH FLOW STATEMENT)		
Net change in deferral account debit (credit) balances	**382**	(391)
Net movement in regulatory balances before related deferred taxes	**(766)**	(470)
Other	**-**	(14)
Changes in regulatory deferral account balances - cash flow	**(384)**	(875)
RECONCILED TO ABOVE AS FOLLOWS:		
Disposition of approved regulatory deferral account balances	**(397)**	(875)
Other	**(13)**	-
Changes in regulatory deferral account balances - cash flow	**(384)**	(875)

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For the year ended December 31, 2015
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11.3 Detail for regulatory deferral account balances

Regulatory deferral account debit balances are comprised of the following accounts:

Regulatory deferral account debit balances	Account #'s	December 31 2015 $	Unaudited December 31 2014 $	Unaudited January 1 2014 $
Low voltage	1550	**887**	399	522
Stranded meter capital	1555	**274**	308	342
Payment in lieu of taxes	1563	**20**	20	88
Lost revenue variance	1568	**299**	122	61
Network services - transmission	1584	**66**	58	316
Connection services - transmission	1586	**54**	-	199
Power	1588	**146**	272	-
Global adjustment	1589	**1,131**	932	1,068
Other regulatory deferral account debit balances		**16**	27	30
		2,893	2,138	2,626

Regulatory deferral account credit balances are comprised of the following accounts:

Regulatory deferral account credit balances	Account #'s	December 31 2015 $	Unaudited December 31 2014 $	Unaudited January 1 2014 $
Retail costs	1518 / 1548	**63**	59	54
IFRS - CGAAP Transitional PP&E amounts	1575	**14**	14	-
Change in PP&E useful lives estimates	1576	**1,936**	1,288	642
Disposition / recoveries	1595	**19**	405	242
Wholesale market services	1580	**2,032**	1,110	2,211
Connection services - transmission	1586	**-**	51	-
Power	1588	**-**	-	657
		4,064	2,927	3,806

11.4 Continuity schedules for regulatory deferral account balances

A continuity schedule from 2014 to 2015 for regulatory deferral account debit balances follows below:

Regulatory deferral account debit balances	Account #'s	Est. Yrs to Rec / Reverse	December 31 2015	Recovery / Reversal	Balances arising in the period	Unaudited December 31 2014
			$	$	$	$
Low voltage	1550	1 - 4	**887**	-	488	399
Stranded meter capital	1555	1 - 4	**274**	(34)	-	308
Payment in lieu of taxes	1563	1 - 4	**20**	-	-	20
Lost revenue variance	1568	1 - 4	**299**	-	177	122
Network services - transmission	1584	1 - 4	**66**	-	8	58
Connection services - transmission	1586	1 - 4	**54**	-	54	-
Power	1588	1 - 4	**146**	-	(126)	272
Global adjustment	1589	1 - 4	**1,131**	-	199	932
Other regulatory deferral account debit balances		1 - 4	**16**	(14)	3	27
			2,893	(48)	803	2,138

A continuity schedule from 2014 to 2015 for regulatory deferral account credit balances follows below:

Regulatory deferral account credit balances	Account #'s	Est. Yrs to Rec / Reverse	December 31 2015	Recovery / Reversal	Balances arising in the period	Unaudited December 31 2014
			$	$	$	$
Retail costs	1518 / 1548	1 - 4	**63**	-	4	59
IFRS - CGAAP Transitional PP&E amounts	1575	1 - 4	**14**	-	-	14
Change in PP&E useful lives estimates	1576	1 - 4	**1,936**	-	648	1,288
Disposition / recoveries	1595	1	**19**	-	(386)	405
Wholesale market services	1580	1 - 4	**2,032**	-	922	1,110
Connection services - transmission	1586	1 - 4	**-**	-	(51)	51
Power	1588	1 - 4	**-**	-	-	-
			4,064	-	1,137	2,927

11.5 Description of regulatory deferral account balances

A description of the nature of the regulatory deferral account debit and credit balances listed in the schedules are described below referenced by account number.

Account 1518 - Retail Cost Variance Account – Services

This account records the net of revenue derived from establishing retail service agreements, distributor-consolidated and retailer-consolidated billing and the costs of entering into retail service agreements and related administration, monitoring and other expenses necessary to maintain the contract, as well as the incremental costs incurred and any avoided costs credits to provide the related billing services.

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11.5 Description of regulatory deferral account balances (continued)

Account 1548 - Retail Cost Variance Account – STR

This account records the net of revenue derived from service transaction requests ("STR") in the form of a request fee, processing fee, and information request fee and the incremental cost of labour, internal information system maintenance costs and delivery costs related to the provision of these services.

Account 1550 – Low Voltage Charges Variance Account

This account records the net of revenue derived from amounts billed to customers through an OEB-approved rate for low voltage services and the amounts paid to Hydro One Networks Inc. for the related low voltage services provided to Orillia Power Distribution Corporation ("OPDC").

Account 1555 – Stranded Meters Account

Conventional meters were replaced by smart meters during the smart meter deployment from 2009 to 2011 and OPDC recorded the disposition of these stranded assets in Property, Plant & Equipment and a regulatory deferral debit balance in accordance with OEB Guidelines. This account records the net book value of the stranded conventional meters, to be amortized to depreciation expense until the next cost of service rate application. Carrying charges are not applied to this account.

Account 1563 – Residual PILs Contra Account

This account represents the residual amount remaining after the disposition of variances resulting from the true-up between certain proxy amounts used to set Payments in Lieu of Tax ("PILs") rates and the actual amount of PILS paid for the period 2001 through April 30, 2006. The OEB approved disposition on a final basis from May 1, 2012 to April 30, 2014.

Account 1568 – LRAM Variance Account

The OEB established a Lost Revenue Adjustment Mechanism variance account ("LRAMVA") to capture the differences between the results of actual, verified impacts of authorized Conservation and Demand Management ("CDM") activities undertaken by electricity distributors from 2011 to 2014 and the level of CDM program activities included in the distributor's load forecast (i.e. the level embedded into rates). Lost revenues are recorded annually and are included in the net movement in regulatory deferral account balances on the statement of comprehensive income. OPDC has proposed disposition of LRAMVA amounts related to CDM programs up to December 31, 2014 in its 2016 incentive rate-setting mechanism ("IRM") application. On March 3, 2016, the OEB announced that the LRAMVA balance included in OPDC's application will not be disposed of until the completion of a generic review of how demand savings should be reflected in the LRAMVA account, leaving the status of OPDC's claim uncertain as of the date of the financial statements.

Account 1575 – IFRS-CGAAP Transitional PP&E Amounts

This account records the property, plant and equipment difference arising as a result of an accounting policy change recognizing capital contributions as deferred revenue upon transition from previous Canadian GAAP to IFRS on January 1, 2014. The balance in this account represents the amortization of the transition year capital contributions previously expensed in 2014. The associated net book value is recorded as deferred revenue and will be amortized to income over a period that matches the remaining useful lives of the related fixed assets. Carrying charges are not applied to this account.

Account 1576 – Accounting Changes under CGAAP

This account records the financial differences arising as a result of changes OPDC made to accounting depreciation under CGAAP effective January 1, 2013. OPDC adopted new asset useful lives based on the 2010 "Kinectric's Report", part of an asset depreciation study initiated by the OEB for use by electricity distributors. Carrying charges are not applied to this account.

11.5 Description of regulatory deferral account balances (continued)

Account 1580 – Retail Settlement Variance Account - Wholesale Market Services

This account records the net of revenue derived from amounts billed to consumers through an OEB-approved rate for the cost of services required to operate the provincial electricity system and run the wholesale market and the amounts paid to the IESO for these system costs.

Account 1584 – Retail Settlement Variance Account – Retail Transmission Network Services

This account records the net of revenue derived from amounts billed to consumers through an OEB-approved rate for retail transmission network services and the amounts paid to Hydro One Networks Inc. for the related network costs.

Account 1586 – Retail Settlement Variance Account – Retail Transmission Connection Services

This account records the net of revenue derived from amounts billed to consumers through an OEB-approved rate for retail transmission connection services and the amounts paid to Hydro One Networks Inc. for the related connection costs.

Account 1588 – Retail Settlement Variance Account – Power

This account records the net of revenue derived from amounts billed to consumers for electricity costs and the amounts paid to the IESO and embedded generators for electricity purchased. OPDC purchases power on behalf of the customer and passes these costs on to the customer with no markup. This account captures variances due to theft of power and unaccounted-for energy as well as the difference between estimated and actual distribution line losses.

Account 1589 – Retail Settlement Variance Account – Global Adjustment

This account records the net of revenue derived from amounts billed to non-Regulated Price Plan (“non-RPP”) consumers for global adjustment costs and an allocation of amounts paid to the IESO for global adjustment charged on electricity purchased for non-RPP consumers. This account captures variances due to the timing of bills and difference between global adjustment rates billed to consumers and final charges billed to OPDC each month.

Account 1595 – Disposition of Regulatory Account Balances

This account records the net of the disposition of regulatory deferral account balances approved for recovery (or refund) in rates as part of the regulatory process and the amounts recovered (or refunded) through OEB-approved regulatory deferral account rate riders from the following OEB applications:

OPDC filed an IRM application on October 31, 2011 for 2012 distribution rates (EB-2011-0191). On April 19, 2012, the OEB approved the disposition of regulatory deferral debits of $843 and regulatory deferral credits of $1,898 over a two year period May 1, 2012 to April 30, 2014. The net disposition balance of $1,055 consisted of principal balances as of December 31, 2010 with carrying charges projected to April 30, 2012.

OPDC filed an IRM application on October 11, 2013 for 2014 distribution rates (EB-2013-0161). On April 24, 2014, the OEB approved the disposition of regulatory deferral debits of $1,236 and regulatory deferral credits of $2,280 over a one year period May 1, 2014 to April 30, 2015. The net disposition balance of $1,044 consisted of principal balances as of December 31, 2012 with carrying charges projected to April 30, 2014.

11.6 2016 Rate Applications

OPDC filed an application on October 19, 2015 for 2016 distribution rates (EB-2015-0286) seeking to establish a rate adder for the disposition of the balance in regulatory deferral credit account 1576 - Accounting Changes under CGAAP as of December 31, 2014. On January 14, 2016, the OEB approved on an interim basis the disposition of a regulatory deferral credit balance of $1,481 over a one year period January 1, 2016 to December 31, 2016. The approved disposition represents the balance in the account plus a rate of return component according to OEB filing requirements for cost of service applications. No carrying charges have been applied. OPDC will seek final disposition of this regulatory deferral credit balance at the time of its next cost of service application.

OPDC filed an IRM application on October 19, 2015 for 2016 distribution rates (EB-2015-0024) which included a request seeking disposition of the balances for regulatory deferral balances. On March 17, 2016, the OEB approved the disposition of regulatory deferral debits of $1,690 and regulatory deferral credits of $1,198 over a one year period May 1, 2016 to April 30, 2017. The net disposition balance of $492 consists of principal balances as of December 31, 2014 with carrying charges projected to April 30, 2016. OPDC's application included a request for disposition of an LRAMVA balance of $299 based on an estimate at the time of filing which has not been approved at the time of the financial statements, and is subject to a pending OEB generic review of how demand savings should be reflected in the LRAMVA accounts for all distributors.

12. BANK INDEBTEDNESS

The Company has credit facilities currently negotiated with a Canadian chartered bank. The facilities are subject to the borrower meeting certain covenant thresholds in order to pay dividends without bank permission. The agreement also includes financial covenants related to debt service coverage ratios and debt to capitalization ratios that must be met by the borrower. The Company is in compliance with all covenant requirements. Facilities are as follows:

OPDC - committed revolving operating loan available at the borrower's option by way of prime based loans, banker's acceptances and standby letters of guarantee ("L/G"), utilized to finance ongoing working capital requirements and any prudential letter of guarantee requirements. The operating loan is secured with a General Security Agreement on the assets of OPDC. Cash advances are at prime less 0.25% with a standby fee for the unused portion at 0.15%. L/Gs are issued at a cost of 0.50% per annum.

OPDC - committed reducing term (multiple draw) loan available at the borrower's option by way of fixed rate terms up to five years and floating prime based loans. Utilized to finance prior year capital expenditures and replenish working capital. The operating loan is secured with a General Security Agreement on the assets of OPDC. Cash advances are at prime less 0.25% with a standby fee for the unused portion at 0.15%. Currently, draws on this facility are interest only and have not been locked in to a fixed term or rate.

12. BANK INDEBTEDNESS (continued)

The following table outlines facilities available and utilized:

Bank indebtedness	December 31 2015	Unaudited December 31 2014	Unaudited January 1 2014
	$	$	$
BORROWING LIMITS ON CREDIT FACILITIES AVAILABLE			
OPDC - revolving operating loan for working capital purposes	**5,000**	5,000	5,000
OPDC - committed reducing term facility for capex	**5,000**	5,000	5,000
	10,000	10,000	10,000
CASH AMOUNTS BORROWED AND OUTSTANDING			
OPDC - revolving operating loan for working capital purposes	**-**	200	950
OPDC - committed reducing term facility for capex	**2,000**	-	-
	2,000	200	950
IRREVOCABLE LETTERS OF CREDIT OUTSTANDING			
OPDC - revolving operating loan for working capital purposes	**2,035**	2,035	2,035
OPDC - committed reducing term facility for capex	**-**	-	-
	2,035	2,035	2,035

13. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities	December 31 2015	Unaudited December 31 2014	Unaudited January 1 2014
	$	$	$
Power purchases	**2,774**	2,961	2,665
Accounts payable and accrued	**2,161**	2,727	2,220
Customer credit balances	**824**	979	837
	5,759	6,667	5,722

Due to its short term nature, the carrying amount of the accounts payable and accrued liabilities approximates its fair values.

14. CURRENT AND DEFERRED INCOME TAXES (PILS)

14.1 Current income tax expense included in Statement of Comprehensive Income

Combined statutory federal and provincial tax rates for Ontario are 26.5% on active business. Income tax expense varies from amounts which would be computed by applying the Company's combined statutory income tax rate as follows:

		Unaudited
Current provision	**2015**	2014
	$	$
Profit for the year after net movement in regulatory deferral account balances	**873**	1,217
Add back provision for payment in lieu of taxes	**476**	259
	1,349	1,476
Statutory federal and provincial combined rate	**26.5%**	26.5%
Provision for PILS at statutory rates	**357**	391
Increase (decrease) in PILS resulting from differences in tax base vs carrying values:		
Property plant and equipment and cumulative eligible capital	**(157)**	(188)
Regulatory deferral account balance changes	**107**	(83)
Other	**15**	(46)
	322	74

14.2 Payments in lieu of taxes receivable (payable)

		Unaudited	Unaudited
	December 31	December 31	January 1
Payment in lieu of taxes receivable and payable	**2015**	2014	2014
	$	$	$
Payment in lieu of taxes receivable	**-**	-	355
Payment in lieu of taxes payable	**(217)**	-	-
	(217)	-	355

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14. CURRENT AND DEFERRED INCOME TAXES (PILS) (continued)

14.3 Deferred income tax expense included in Statement of Comprehensive Income

Deferred income taxes recognized in the Statement of Comprehensive Income are as follows:

Deferred provision	2015	Unaudited 2014
	$	$
Included in profit for the year		
Property, plant, equipment and intangibles	**157**	188
Post-retirement benefits and sick pay accrual	**(3)**	(3)
	154	185
Included in other comprehensive profit for the year		
Post-retirement benefits and sick pay accrual	**-**	33
	-	33

14.4 Deferred income tax assets

Deferred income tax assets are provided for temporary differences between the financial statement carrying values of existing assets and liabilities and their respective tax bases. The following table outlines the Company's position with respect to deferred tax assets. 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. The Company believes that this asset should be recognized as it will be utilized through future activities.

Deferred income tax asset and liabilities	December 31 2015	Unaudited December 31 2014	Unaudited January 1 2014
	$	$	$
Asset (liability) due excess (shortfall) of tax basis over carrying value:			
Property, plant, equipment and intangibles	**894**	1,051	1,239
Post-retirement benefits	**172**	169	199
Sick pay accrual	**13**	13	13
	1,079	1,233	1,451

14. CURRENT AND DEFERRED INCOME TAXES (PILS) (continued)

14.5 Deferred tax balances related to regulatory deferral accounts

Deferred tax balances related to regulatory deferral account debit and credit balances are netted against the applicable regulatory deferral account debit or credit balances. They are not included with the other deferred income tax asset balances related to property, plant, equipment, intangibles, post-retirement benefits and loss carry forward.

		Unaudited	Unaudited
	December 31	December 31	January 1
Deferred income tax assets (liabilities) included with regulatory balances	**2015**	2014	2014
	$	$	$
Asset (liability) due excess (shortfall) of tax basis over carrying value:			
Asset included with regulatory deferral account credit balances	**1,077**	772	1,009
Liability included with regulatory deferral account debit balances	**(767)**	(540)	(696)
	310	232	313

15. CUSTOMER SECURITY DEPOSITS

Customer deposits represents cash deposits from electricity distribution customers and retailers, as well as construction deposits from customers and developers. Deposits from electricity distribution customers are refundable to customers demonstrating an acceptable level of credit risk as determined by the Company 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.

		Unaudited	Unaudited
	December 31	December 31	January 1
Customer security deposits	**2015**	2014	2014
	$	$	$
Customer deposits	**313**	289	259
Construction deposits	**140**	56	50
	453	345	309
Allocated to:			
Current	**133**	68	71
Long term	**320**	277	238
	453	345	309

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16. POST RETIREMENT BENEFITS

Defined contribution plan

The employees of the Company participate in the Ontario Municipal Employees Retirement System ("OMERS"). Although the plan has a defined retirement benefit plan for employees, the related obligation of the corporation cannot be identified. The OMERS plan has several unrelated participating municipalities and costs are not specifically attributed to each participant. The employer portions of amounts paid to OMERS were made for current service and recognized in comprehensive income are as follows:

		Unaudited
Contributions to OMERS on behalf of employees	**2015**	2014
	$	$
	360	**337**

Defined benefit plan

The Company provides certain unfunded health, dental and life insurance benefits on behalf of its retired employees. These benefits are provided through a group defined benefit plan. The Company has reported its share of the defined benefit costs and related liabilities, as calculated by an actuary, in these Financial Statements.

The accrued benefit liability and the expense for the years ended December 31, 2015 and 2014 were based on results and assumptions determined by actuarial valuation as at December 31, 2014 and are as follows:

		Unaudited
	December 31	December 31
Post-retirement benefits	**2015**	2014
	$	$
Defined benefit obligation, beginning of year	**637**	752
Amounts recognized in profit for the year		
Current service costs	**11**	8
Finance costs on obligation	**24**	29
	35	37
Benefit payments	**(27)**	(29)
Experience gains (losses) included in other comprehensive loss	3	(123)
Defined benefit obligation, end of year	**648**	637

The plan is exposed to a number of risks, including:

- Interest rate risk: decreases/increases in the discount rate used (high quality corporate bonds) will increase/decrease the defined benefit obligation.
- Longevity risk: changes in the estimation of mortality rates of current and former employees.
- Health care cost risk: increases in cost of providing health, dental and life insurance benefits.

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16. POST RETIREMENT BENEFITS (continued)

Assumptions used in the actuarial valuation in order to determine the present value of the unfunded obligation are as follows:

		Unaudited
	December 31	December 31
Assumptions used in actuarial valuation	**2015**	2014
Discount rate	**3.9%**	**3.9%**
Consumer price index	**2.0%**	**2.0%**
Compensation increase	**2.0%**	**2.3%**
Health cost increases	**4.6%**	**4.6%**
Dental cost increase	**4.8%**	**4.6%**
Retirement age	**58**	**58**

17. DEFERRED REVENUE

Deferred revenue consists of capital contributions received from developers during the construction and acquisition of distribution property, plant and equipment which has not yet been recognized into other revenue. Such capital contributions are recorded as deferred revenue and recognized to other revenue over the life of the related assets as follows:

		Unaudited
Deferred revenue	**2015**	2014
	$	$
Balance, beginning of year	**1,060**	-
Contributions in aid of construction received	**135**	1,074
Contributions in aid of construction amortized to other revenue	**(29)**	(14)
Balance, end of year	**1,166**	1,060

18. LONG TERM DEBT

		Unaudited	Unaudited
	December 31	December 31	January 1
Long term debt	**2015**	2014	2014
	$	$	$
Promissory note due to City of Orillia - OPDC	**9,762**	9,762	9,762
Ontario Infrastructure Projects Corporation ("OIPC")	**945**	1,155	1,365
	10,707	10,917	11,127
Current portion of OIPC long term debt	**210**	210	210
	10,497	10,707	10,917
Principal repayments anticipated over the next five years and thereafter:			
2014	**-**	-	210
2015	**-**	210	210
2016	**210**	210	210
2017	**210**	210	210
2018	**210**	210	210
2019	**210**	210	210
2020	**105**	105	105
Thereafter	**9,762**	9,762	9,762
	10,707	10,917	11,127

Promissory notes payable to City of Orillia

The promissory notes payable to the City of Orillia, the shareholder of Orillia Power Corporation, the parent Company, bear interest for the current year at 6.25% per annum (December 31, 2014 – 6.25%, January 1, 2014 - 6.25%). The interest rate is reviewed annually and payments of interest are required to be made quarterly on the last day of March, June, September and December. The promissory notes are due December 31, 2030 and payments to the City of Orillia are interest only. Under the terms of the notes, the City of Orillia can demand repayment of up to 20% of the original principal in a calendar year with the payment to be made March 31 provided the City gives six months' notice to the Company. No such demand has been made by the City as of the date of approval of these financial statements. The fair value of the notes at current market borrowing rates approximates $11,256. The notes are secured by a general security agreement on all the assets of the Company.

Debenture payable to Infrastructure Ontario

The Company has entered into a financing arrangement with Ontario Infrastructure Projects Corporation (OIPC), to provide debenture financing for its smart meter infrastructure expenditures. On May 3, 2010 a debenture in the amount of $2,100 was issued based on a 10-year term and an annual interest rate of 4.39%. The Company incurred $48 (2014 - $57) in interest expense to OIPC in 2015. Under the terms of the debenture, the Company must make principal repayments of $210 annually, until the debenture is retired in 2020. The financing arrangement grants OIPC a general security agreement against the Company, in third priority behind the Toronto Dominion Bank and the City of Orillia. The agreement restricts dividends paid by Orillia Power Distribution Corporation to amounts that meet the definition of "Permitted Distributions" unless waived by OIPC.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended December 31, 2015
(in thousands of Canadian dollars unless otherwise noted)

19. SHARE CAPITAL

Nature and purpose of equity

The reserves recorded in equity on the Company's Statement of Financial Position include "Share capital" and "Retained earnings". Share capital is used to record the issuance of equity. Retained earnings is used to record the Company's change in retained earnings from year to year.

Share capital

An unlimited number of common shares with no par value are authorized for issue. All shares are ranked equally with regards to the Company's residual assets and there was no change in share capital during 2015 and 2014. The Company does not have preference shares.

		Unaudited	Unaudited
	December 31	December 31	January 1
Share capital	**2015**	2014	2014
	$	$	$
Share capital	**8,236**	8,236	8,236
	8,236	8,236	8,236
Issued and fully paid:			
Common shares	**1,001**	1,001	1,001

20. OPERATING REVENUE

		Unaudited
Operating revenue	**2015**	2014
	$	$
Distribution revenue	**7,857**	8,048
Other revenue	**678**	605
	8,535	8,653

21. OPERATING EXPENSES

Operating expenses	2015	Unaudited 2014
	$	$
EXPENSES BY NATURE		
Board and staff costs	**2,678**	2,798
Operations and maintenance	**711**	745
General adminstration and overhead	**1,088**	947
Bad debts	**104**	88
Donations	**268**	20
	4,849	4,598
EXPENSES BY FUNCTION		
Operations and maintenance	**1,980**	2,074
Billing and collection	**1,160**	1,099
Administration and general	**1,709**	1,425
	4,849	4,598

22. FINANCE INCOME AND FINANCE COSTS

Finance income and finance costs	2015	Unaudited 2014
	$	$
FINANCE INCOME		
Recognized in profit or loss:		
Interest income on bank deposits	**8**	14
	8	14
FINANCE COSTS		
Recognized in profit or loss:		
Interest on City prommisory notes	**610**	610
Interest on non-related debt	**48**	57
Interest on post retirement benefits	**24**	29
	682	696

NOTES TO THE FINANCIAL STATEMENTS

For the year ended December 31, 2015
(in thousands of Canadian dollars unless otherwise noted)

23. NON-CASH OR NON-OPERATING ADJUSTMENTS INCLUDED IN PROFIT OR LOSS

In order to arrive at cash flows from operating activities on the Statement of Cash Flows the following items need to be added or subtracted from profit for the year:

		Unaudited
Other non-cash or non-operating items included in profit	**2015**	2014
	$	$
NON-REGULATORY ITEMS (NON-CASH OR NON-OPERATING)		
Payments in lieu of taxes included in profit and loss	**476**	259
Loss on disposal of property, plant and equipment	**79**	16
Amortization of deferred revenue	**(29)**	(14)
Post-retirement benefits	**11**	8
Finance income	**(8)**	(14)
Finance expense	**682**	696
	1,211	951
REGULATORY ITEMS (NON-CASH)		
Net movement in regulatory balances including related deferred taxes	**688**	551
	1,899	1,502

24. NET CHANGES IN NON-CASH WORKING CAPITAL

		Unaudited
Net changes in non-cash working capital	**2015**	2014
	$	$
Accounts receivable	**786**	(681)
Unbilled energy and distribution revenue	**(353)**	185
Payment in lieu of taxes receivable	**-**	355
Inventories	**25**	92
Prepaid expenses	**25**	(29)
Due from related parties	**(99)**	59
Bank indebtedness to finance working capital requirements	**(200)**	(750)
Accounts payable and accrued liabilities	**(908)**	945
Payment in lieu of taxes payable	**217**	-
Customer security deposits	**65**	(3)
Due to related parties	**(2)**	57
	(444)	230

NOTES TO THE FINANCIAL STATEMENTS

For the year ended December 31, 2015
(in thousands of Canadian dollars unless otherwise noted)

25. RELATED PARTY TRANSACTIONS

The ultimate parent

Orillia Power Corporation is the 100% owner of Orillia Power Distribution Corporation. The common shares of Orillia Power Corporation are owned by the Corporation the City of Orillia, the ultimate parent, which constitutes a local government. Consequently, the Company is exempt from some of the general disclosure requirements of IAS 24 with relation to transactions with government-related parties, and has applied the government-related disclosure requirements.

Key management personnel compensation

Key management personnel are defined in IAS 24 as “those persons having authority and responsibility for planning, directing and controlling the activities of the entity, directly or indirectly, including any director (whether executive or otherwise) of that entity”. Key management personnel of the Company have been defined as members of its board of directors, officers and senior managers reporting directly to the President and Chief Executive Officer.

		Unaudited
Key management personnel compensation	**2015**	2014
	$	$
Board of directors	**69**	51
Officers and senior managers	**447**	539
	516	590

25. RELATED PARTY TRANSACTIONS (continued)

Transactions with related parties

The Company provides electricity and other services to the Corporation of the City of Orillia (“City”). The Company also purchases services and pays property taxes and promissory note interest to the City. The Company has a shared services agreement with an affiliate, Orillia Power Generation Corporation. The control centre, building space, purchasing and administrative staff are shared among the two companies as outlined in the agreement. The company has Affiliate Relationships Code and Standard Supply Service Code exemptions approved by the Ontario Energy Board to allow the shared services.

Related party transactions	2015	Unaudited 2014
	$	$
Financing activities with The Corporation of the City of Orillia ("City")		
Finance costs paid to the City	**610**	610
Operating activities with The Corporation of the City of Orillia ("City")		
Power sold to the City	**2,339**	2,236
Other services sold to the City	**128**	79
Goods and services purchased from the City	**69**	80
Property taxes paid to the City	**70**	67
Balances outstanding with The Corporation of the City of Orillia ("City")		
Due from City included in receivables	**224**	293
Due to City included in payables	**9**	157
Investing and financing activities with affiliates		
Dividends paid to parent	**1,230**	-
Operating activities with affiliates - sold to		
Goods and services sold to Orillia Power Corporation	**6**	8
Goods and services sold to Orillia Power Generation	**1,049**	950
Operating activities with affiliates - purchased from		
Goods and services purchased from Orillia Power Corporation	**69**	51
Goods and services purchased from Orillia Power Generation	**122**	166
Due from related parties		
Due from Orillia Power Generation	**863**	768
Due from 2429106 Ontario Inc.	**4**	-
Due to related parties		
Due to Orillia Power Corporation	**55**	57

26. COMMITMENTS AND CONTINGENCIES

IESO prudential security commitments

Purchasers of electricity in Ontario, through the Independent Electricity Systems Operator (“IESO”), are required to provide security to mitigate the risk of their default based on their expected activity in the market. The IESO could draw on these guarantees if the Company fails to make a payment required by default notice issued by the IESO. As at December 31, 2015, the Company has provided prudential support to the IESO in the form of an irrevocable, automatically renewing bank letter of credit in the amount of $2,035 (December 31, 2014 - $2,035, January 1, 2014 - $2,035).

Donation commitment

In 2012, Orillia Power Corporation pledged to make a donations of $1,250 payable over five years to the local hospital foundation. Total payments of $1,000 have now been made by companies within the corporate entity towards this pledge. The Board of Directors has authorized Orillia Power Distribution Corporation to make the last payment of $250 prior to July 2016 at which time the commitment to the hospital foundation will have been 100% fulfilled.

Membership commitment

In 2015, the Company renewed a three year membership commitment in the Cornerstone Hydro Electric Concepts Association Inc. (“CHEC”), an association of approximately fifteen distributors modelled after a co-operative to share resources and proficiencies. The Company can terminate its membership by giving sixty days’ notice and paying the unpaid balance of its three year commitment. As of December 31, 2015 the cost to terminate the membership is approximately $81.

Liability insurance

The Company belongs to the Municipal Electric Association Reciprocal Insurance Exchange (“MEARIE”), a self-insurance plan designed to pool all member risks. Any losses experienced by MEARIE are shared amongst all of its members. As of the date of Board of Directors approval of this financial report, the Company has not been made aware of any assessments for significant losses. The Company has contracted for a maximum total of $24 million in event coverage with MEARIE and $10 million in excess liability coverage with a secondary provider.

Legal proceeding contingencies

In 2012, a legal proceeding was commenced against the Company related to damages to Bell Canada property. The Company has turned this matter over to its liability insurer and the matter is currently before the Ontario Superior Court of Justice. At this time, it is not possible to quantify the effect, if any, on the financial statements of the Company. Management does not believe that the outcome of this matter will have a material impact on the financial statements.

In relation to a 2013 motor vehicle accident, a legal proceeding has been commenced against the Company. This matter has been turned over to the Company’s liability insurer and is currently before the Ontario Superior Court of Justice. At this time, it is not possible to quantify the effect, if any, on the financial statements of the Company. Management does not believe that the outcome of this matter will have a material impact on the financial statements.

27. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

As part of its operations, the Company carries out transactions that expose it to financial risks such as credit, liquidity and market risks. The following is a discussion of risks and related mitigation strategies that have been identified by the Company for financial instruments. This is not an exhaustive list of all risks, nor will the mitigation strategies eliminate all risks identified.

Cash and cash equivalents are measured at fair value. The carrying values of receivables, and accounts payable and accrued charges approximate fair value because of the short maturity of these instruments.

Credit risk

Financial assets carry credit risk that a counter-party will fail to discharge an obligation which would result in a financial loss.

Financial assets held by the Company, such as accounts receivable, expose it to credit risk. The Company earns its revenue from a broad base of approximately 13,500 customers located in the City of Orillia. No single customer accounts for revenue in excess of 10% of total revenue. The carrying amount of accounts receivable is reduced through the use of an allowance for impairment. The amount of the related impairment loss is recognized in the statement of profit or loss as are any subsequent recoveries of receivables previously provisioned. Further details on accounts receivable can be found in other notes to these financial statements.

Credit risk is managed through collection of security deposits from customers in accordance with OEB codes and regulations. Further details on customer security deposits can be found in other notes to these financial statements.

Market risk

The Company is not exposed to significant market risk given they do not have investments in foreign currency, and have minimal investment in interest bearing instruments.

Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they come due. The Company monitors its liquidity risk to ensure access to sufficient funds to meet operational and investing requirements. The Company's objective is to ensure that sufficient liquidity is on hand to meet obligations as they fall due while minimizing interest exposure. The Company has access to various operating lines of credit and monitors cash balances to ensure that sufficient levels of liquidity are on hand to meet financial commitments as they come due. Further details on accounts payable and accrued liabilities can be found in other notes to these financial statements.

28. CAPITAL MANAGEMENT

The Company considers its capital to be its share capital, accumulated retained earnings and accumulated other comprehensive income (loss). The Company's objectives when managing capital are:

- to safeguard the Company's ability to continue as a going concern, so that it can continue to provide adequate returns for shareholders and benefits for other stakeholders while maintaining its assets, and
- to provide an adequate return to shareholders by controlling costs and establishing rates that maximize rate of return commensurate with the level of risk, and
- to ensure the capital structure does not prevent the Company from taking advantage of potential growth opportunities provided that they do not expose the Company to unnecessary risk.

The Company manages its capital structure and makes adjustments to it in light of changes in economic conditions, annual profitability and the risk characteristics of the underlying assets. In order to maintain or adjust the capital structure, the Company will adjust the amount of dividends paid to shareholders, subject to the constraints imposed by lending agreements. The Company is subject to quarterly reporting and bank review of its interest coverage and debt capitalization ratios, in relation to its various bank credit lines.

Consistent with others in the industry, the Company monitors capital on the basis of the debt-to-capital ratio calculated as long term debt divided by the sum of long term debt plus equity, as shown in the following table. For purposes of comparing the measures below to benchmarks, the Company was initially incorporated at a debt to capital ratio of 0.48.

		Unaudited	Unaudited
	December 31	December 31	January 1
Debt to capital ratio	**2015**	2014	2014
	$	$	$
Sum of long term debt and shareholder's equity			
Long term debt	**10,707**	10,917	11,127
Shareholder's equity	**12,636**	12,993	11,686
	23,343	23,910	22,813
Key Ratio - Debt to Capital			
Ratio of debt to debt plus equity	**0.46**	0.46	0.49

29. FIRST TIME ADOPTION OF INTERNATIONAL FINANCIAL REPORTING STANDARDS

IFRS 1, First Time Adoption of International Financial Reporting Standards, requires that comparative financial information be provided. As a result, the first date at which the Company has applied IFRS was January 1, 2014 (the "Transition Date"). IFRS 1 requires first-time adopters to retrospectively apply all effective IFRS standards as of the reporting date, which for the Company will be December 31, 2015. However, it also provides for certain optional exemptions and certain mandatory exceptions for first-time IFRS adoption. Prior to transition to IFRS, the Company prepared its financial statement in accordance with Canadian generally accepted accounting principles ("pre-changeover Canadian GAAP").

29.1 Mandatory exceptions and optional elections

The IFRS 1 applicable exemptions and exceptions applied in the conversion from pre-changeover Canadian GAAP to IFRS are as follows:

29.1 Mandatory exceptions and optional elections (continued)

Derecognition of financial assets and liabilities

The Company has applied the derecognition requirements in IAS 39 prospectively for transactions occurring on or after January 1, 2014. As a result any non-derivative financial assets or non-derivative financial liabilities derecognized in accordance with pre-changeover Canadian GAAP as a result of a transaction that occurred before January 1, 2014, have not been recognized in accordance with IFRS unless they qualify for recognition as a result of a later transaction or event.

Estimates

The estimates previously made by the Company under pre-changeover Canadian GAAP were not revised for the application of IFRS, except where necessary to reflect any difference in accounting policy or where there was objective evidence that those estimates were in error. As a result, the Company has not used hindsight to revise estimates.

Government loans

The Company classifies government loans received as financial liabilities or equity instruments in accordance with IAS 32 Financial Instruments: Presentation. At the date of transition, these loans are measured at the pre-changeover Canadian GAAP carrying amount as a government grant. No benefit element is recognized for below market interest rate loans. The loans are subsequently measured using an effective interest rate calculated at the date of transition and the guidance in IAS 20 Accounting for Government Grants and Disclosure of Government Assistance is applied after the date of transition.

Borrowing costs

The Company has elected to apply the optional election in the transitional provisions of IAS 23 Borrowing Costs which permits prospective capitalization of borrowing costs on qualifying assets from the Transition Date.

Deemed cost for Operations subject to Rate Regulation

The Company has elected the deemed cost exemption applicable to entities subject to rate regulation as described under IFRS 1. The election permits the Company, at the date of transition to IFRS, to use the previous Canadian GAAP carrying amount of items of PP&E and intangible assets as deemed cost (thereby eliminating any accumulated depreciation balances existing at the date of transition); hence there will be no impact on retained earnings for opening balances of PP&E and intangible assets at the date of transition. In accordance with the election, the Company has tested these items of property, plant and equipment and intangible assets at the date of transition to IFRS. No impairment losses were recognized.

Transfers of Assets from Customers

The Company has elected to apply the IFRS 1 election to only apply IFRIC 18 prospectively from the date of transition to non-repayable supply contributions made by customers.

29.2 Reconciliations of pre-changeover Canadian GAAP to IFRS

IFRS 1 requires an entity to reconcile cash flows, equity, and comprehensive income for prior periods as shown below.

In the statement of changes in cash flows, there is a reclassification from the movement in regulatory assets and regulatory liabilities to a movement in the regulatory deferral account balance. These are both shown as movements within investing activities and as such do not result in material adjustments to the net cash flow balance.

The explanations for the impact of the transition to IFRS on the specific accounts is described below. Reconciliation of equity and comprehensive income as previously reported under Canadian GAAP to IFRS are provided below. Other than employee post-retirement benefits, sick pay benefits and the related deferred taxes, all other items have no impact on Equity or Comprehensive Income as they are reclassifications within the relevant statements.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended December 31, 2015
(in thousands of Canadian dollars unless otherwise noted)

29.2 Reconciliations of pre-changeover Canadian GAAP to IFRS (continued)

STATEMENT OF FINANCIAL POSITION As at (in thousands of Canadian dollars)	Notes	Previous GAAP Dec. 31, 2013	Amounts Reclassed	Impact of transition to IFRS	IFRS January 1, 2014
		$	**$**	**$**	**$**
ASSETS					
Current Assets					
Cash and cash equivalents		20	-	-	20
Accounts receivable		3,524	-	-	3,524
Unbilled energy and distribution revenue		3,985	-	-	3,985
Payment in lieu of taxes receivable		355	-	-	355
Inventories		618	-	-	618
Prepaid expenses		166	-	-	166
Future income tax asset	(a)	233	(233)	-	-
Due from related parties		827	-	-	827
Current assets		9,728	(233)	-	9,495
Non-current Assets					
Property, plant and equipment		20,330	-	-	20,330
Intangible assets		137	-	-	137
Regulatory assets	(b)	342	(342)	-	-
Deferred income tax asset	(a) (c) (d)	1,458	(80)	73	1,451
Non-current assets		22,267	(422)	73	21,918
Total assets		**31,995**	**(655)**	**73**	**31,413**
Regulatory deferral account debit balances	(b) (c) (e)	-	1,930		1,930
Total assets and regulatory deferral account debit balances		**31,995**	**1,275**	**73**	**33,343**

29.2 Reconciliations of pre-changeover Canadian GAAP to IFRS (continued)

STATEMENT OF FINANCIAL POSITION As at (in thousands of Canadian dollars)	Notes	Previous GAAP Dec. 31, 2013	Amounts Reclassed	Impact of transition to IFRS	IFRS January 1, 2014
		$	$	$	$
LIABILITIES AND SHAREHOLDER'S EQUITY					
Current Liabilities					
Bank indebtedness		950	-	-	950
Accounts payable and accrued liabilities	(f)	5,681	-	41	5,722
Customer security deposits		71	-	-	71
Current portion of long term debt		210	-	-	210
Current liabilities		6,912	-	41	6,953
Non-current Liabilities					
Customer security deposits		238	-	-	238
Post-retirement benefits	(g)	525	-	227	752
Regulatory liabilities	(e) (h)	1,522	(1,522)	-	-
Long term debt		10,917	-	-	10,917
Non-current liabilities		13,202	(1,522)	227	11,907
Shareholder's Equity					
Share capital		8,236	-	-	8,236
Contributed capital	(i)	2,351	(2,351)	-	-
Retained earnings	(i)	1,294	2,351	-	3,645
Accumulated other comprehensive loss	(d) (f) (g)	-	-	(195)	(195)
Shareholder's equity		11,881	-	(195)	11,686
Total liabilities and shareholder's equity		**31,995**	**(1,522)**	**73**	**30,546**
Regulatory deferral account credit balances	(c) (h)	-	2,797	-	2,797
Total equity, liabilities and regulatory deferral account credit balances		**31,995**	**1,275**	**73**	**33,343**

NOTES TO THE FINANCIAL STATEMENTS

For the year ended December 31, 2015
(in thousands of Canadian dollars unless otherwise noted)

STATEMENT OF COMPREHENSIVE INCOME

Year ended December 31 (in thousands of Canadian dollars)	Notes	2014 Previous GAAP	Amounts Reclassed	Impact of transition to IFRS	2014 IFRS
		$	$	$	$
Revenue					
Recovered energy purchases		33,821	-	-	33,821
Operating revenue	(j) (k) (l) (m	7,933	720	-	8,653
		41,754	720	-	42,474
Expenses					
Energy purchases	(n)	33,821	229	-	34,050
Operating expenses	(o) (p) (q)	4,647	(33)	(16)	4,598
Depreciation and amortization	(m)	1,087	14	-	1,101
Loss on disposal of property plant and equipment	(l)	-	16	-	16
	-	39,555	226	(16)	39,765
Operating profit		2,199	494	16	2,709
Finance income	(r)	9	5	-	14
Finance costs		(667)	(29)	-	(696)
Profit before payments in lieu of taxes		1,541	470	16	2,027
Provision for payment in lieu of taxes					
Current provision		74	-	-	74
Deferred provision	(s) (t) (u)	262	(114)	37	185
		336	(114)	37	259
Profit for the year before net movement in regulatory deferral account balance		1,205	584	(21)	1,768
Net movement in regulatory deferral account balances	(v)	-	(551)		(551)
Profit for the year after net movement in regulatory deferral account balances		1,205	33	(21)	1,217
Other comprehensive income:					
Items that will not be reclassified subsequently to profit and loss:					
Actuarial gain on defined benefit plans net of deferred taxes	(t) (w)	-	(33)	123	90
Total comprehensive income for the year		**1,205**	**-**	**102**	**1,307**

29.2 Reconciliations of pre-changeover Canadian GAAP to IFRS (continued)

EXPLANATIONS OF AMOUNTS RECLASSIFIED AND IFRS TRANSITION IMPACTS

(a) Reclassification of current deferred taxes to non-current deferred tax assets $233
(b) Reclassification of regulatory assets $342 to regulatory deferral account debit balances
(c) Deferred income tax assets reduced by amount of $313 reallocated to related regulatory balances
(d) Deferred tax impact of post retirement benefits and sick pay accrual on transition date comprehensive income $73
(e) Debits included in regulatory liabilities reallocated to regulatory deferral account debits
(f) Estimated balance of transition date sick leave benefit accrual of $41
(g) Estimated balance of transition date post retirement benefit accrual of $227 included in comprehesive income
(h) Credits included in regulatory liabilities reallocated to regulatory deferral account credit balances
(i) Contributed capital included in equity since incorporation reallocated to retained earnings $2,351
(j) Regulatory debit from depreciation difference in useful lives $646 reclassified to net movement in regulatory
(k) Other regulatory revenues and expenses $44 reclassified to net movement in regulatory
(l) Loss on disposal of PP&E $16 reclassified from other revenue
(m) Amortization of deferred revenue $14 reclassified to depreciation and amortization
(n) Variance between energy purchased and recovered $229 reallocated to net movement in regulatory
(o) Decrease in post retirement benefits expense of $19
(p) Increase in sick leave benefit accrual of $3
(q) Retailer cost variances $4 reallocated to net movement in regulatory
(r) Interest on deferral account balances $5 reallocated to net movement in regulatory
(s) Increase in deferred tax provision re post retirement benefits $37
(t) Reallocation of deferred tax expense related to actuarial gain on post retirement benefits $33
(u) Reallocation of deferred tax expense re regulatory debits and credits $81
(v) Amounts reallocated to net movement in regulatory $551=(n)-(j)-(k)-(q)-(r)-(u)
(w) Experience gain per actuarial valuation $123

END OF FINANCIAL STATEMENT

Orillia Power Distribution Corporation
Financial Statements
December 31, 2014

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Independent auditor's report

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To the Directors of Orillia Power Distribution Corporation:

We have audited the accompanying financial statements of Orillia Power Distribution Corporation, which comprise the balance sheet as at December 31, 2014, and the statement of earnings and retained earnings and cash flow statement for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Canadian generally accepted accounting principles, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express an opinion on these 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 financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the 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 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 financial statements present fairly, in all material respects, the financial position of Orillia Power Distribution Corporation as at December 31, 2014, and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

Grant Thornton LLP

Orillia, Canada
March 26, 2015

Chartered Accountants
Licensed Public Accountants

Orillia Power Distribution Corporation

Statements of Earnings and Retained Earnings

(In Thousands)

Year Ended December 31	2014	2013
Revenue		
Sale of power	$ 33,821	$ 31,684
Distribution	8,038	7,851
Other (Note 4)	(105)	(184)
	41,754	39,351
Costs		
Power purchased	33,821	31,684
Operations, maintenance and administration	4,647	4,615
Amortization	1,087	1,020
	39,555	37,319
Earnings from operations	2,199	2,032
Interest income	9	3
Interest on long term debt	(667)	(676)
Earnings before payments in lieu of taxes	1,541	1,359
Payments in lieu of taxes (Note 12)	336	309
Net earnings	$ 1,205	$ 1,050
Retained earnings, beginning of year	$ 1,294	$ 244
Net earnings	1,205	1,050
Retained earnings, end of year	$ 2,499	$ 1,294

See accompanying notes to the financial statements.

Orillia Power Distribution Corporation
Balance Sheet

(In Thousands)

December 31	2014	2013
Assets		
Current		
Cash and cash equivalents	$ 77	$ 20
Receivables	4,205	3,524
Unbilled revenue	3,800	3,985
Payments in lieu of taxes recoverable	-	355
Inventory (Note 7)	526	618
Prepaids	195	166
Due from related parties (Note 3)	711	827
Future income tax asset (Note 12)	-	233
	9,514	9,728
Property and equipment (Note 4)	21,409	20,330
Intangible assets (Note 5)	146	137
Regulatory assets (Note 6)	408	342
Future income tax asset (Note 12)	1,429	1,458
	$ 32,906	$ 31,995
Liabilities		
Current		
Bank credit line (Note 18)	$ 200	$ 950
Payables and accruals	6,623	5,681
Current portion of long term debt (Note 9)	210	210
	7,033	6,841
Customer and retailer deposits	345	309
Employee future benefits (Note 8)	552	525
Regulatory liabilities (Note 6)	1,183	1,522
Long term debt (Note 9)	10,707	10,917
	19,820	20,114
Shareholder's Equity		
Capital stock (Note 10)	8,236	8,236
Contributed capital	2,351	2,351
Retained earnings	2,499	1,294
	13,086	11,881
	$ 32,906	$ 31,995

Commitments and Contingencies (Note 11 and Note 13)

On Behalf of the Board

_________________ Director _________________ Director

See accompanying notes to the financial statements.

Orillia Power Distribution Corporation
Statement of Cash Flows

(In Thousands)

Year Ended December 31	2014	2013
Increase (decrease) in cash and cash equivalents		
Operating		
Net earnings	$ 1,205	$ 1,050
Amortization	1,087	1,020
Future income tax (Note 12)	262	224
Employee future benefits	27	4
	2,581	2,298
Change in non-cash operating working capital (Note 14)	266	293
	2,847	2,591
Financing		
Long term debt repayments	(210)	(210)
Investing		
Net (addition) reduction in regulatory assets	(66)	34
Net reduction in regulatory liabilities	(339)	(55)
Net additions to property, equipment and intangible assets	(2,175)	(2,724)
	(2,580)	(2,745)
Net increase (decrease) in cash and cash equivalents	57	(364)
Cash and cash equivalents, beginning of year	20	384
Cash and cash equivalents, end of year	$ 77	$ 20

See accompanying notes to the financial statements.

Orillia Power Distribution Corporation
Notes to the Financial Statements
(In Thousands)
December 31, 2014

1. Nature of operations

Orillia Power Distribution Corporation (the Company) was incorporated on October 26, 2000 under the *Business Corporations Act* (Ontario) and is wholly owned by Orillia Power Corporation. The principal business of the Company is the distribution of electricity to the residents and businesses within the City of Orillia.

The Company is regulated by the Ontario Energy Board (OEB) under the authority of the Ontario Energy Board Act, 1998. The OEB prescribes license requirements and conditions to electricity distributors, which may include among other things, specified accounting records, regulatory accounting principles, separation of accounts for distinct businesses and guidelines for establishing just and reasonable rates.

2. Summary of significant accounting policies

Cash and cash equivalents

Cash and cash equivalents include cash on hand and balances with banks.

Inventory

Inventory consists of repair parts, supplies and materials for maintenance and future capital expansion. The inventory is measured at the lower of the weighted average cost of similar items and net realizable value. Cost includes all acquisition costs incurred in bringing inventory to its present location and condition. Net realizable value is the estimated selling price in the ordinary course of business, less any applicable selling expenses. The Company classifies rebates received from vendors as a reduction to the cost of inventory.

Revenue recognition

The sale of power and distribution revenue attributable to the delivery of electricity to customers is recorded on the basis of regular meter readings using rates approved by the Ontario Energy Board and is recognized in the period that power is consumed. Customer usage since the date of the last meter reading to year end is estimated as unbilled revenue. Other revenue and interest income are recognized when earned.

Rate regulation

The rates of the Company's electricity distribution business are subject to regulation by the OEB, under the authority granted by the Ontario Energy Board Act (1998). The OEB is charged with the responsibility of approving or setting rates for the transmission and distribution of electricity, ensuring continued rate protection for rural and remote electricity consumers and the responsibility for ensuring that distribution companies fulfil obligations to connect and service customers.

2. Summary of significant accounting policies (Continued)

Rate regulation (Continued)

The OEB regulates distribution rates under an Incentive Regulation Mechanism (IRM) process. This requires that all Ontario distributors periodically re-base distribution rates under a cost of service methodology. The Company re-based rates effective May 1, 2010 and is next scheduled to re-base rates effective May 1, 2016. A formulaic approach to establishing annual rates is utilized in years where a re-basing application has not been filed.

The OEB has the general power to include or exclude costs, revenues, losses or gains in the rates of a specific period, resulting in a change in the timing of accounting recognition from that which would have applied in an unregulated company. This change in timing gives rise to the recognition of regulatory assets and liabilities. These regulatory assets and liabilities reflect the fact that revenue and expenses are recognized in the financial statements in different periods consistent with their inclusion in rates, as directed by the regulator, than would be the case for an enterprise that is unregulated. Specific regulatory assets and liabilities recognized at December 31, 2014 are disclosed in Note 6.

The Company continually assesses the likelihood of recovery of each of its regulatory assets and believes that it is probable that its regulatory assets and liabilities will be factored into the setting of future rates. If future recovery through rates is no longer considered probable, the appropriate carrying amount will be written off in the period that the assessment is made.

Property and equipment

Property and equipment are recorded at cost and include contracted services, materials, labour, engineering costs and overheads. Significant renewals and enhancements to existing assets are capitalized only if the service life of the asset is extended, reliability or productivity is improved above original design standards or associated operating costs are lowered. Maintenance and repair costs are expensed as incurred.

In the case of capital expenditures that become part of the distribution system, expenditures are analysed to determine the appropriate componentization or asset classification and the amortization period is set at the estimated useful life for that asset category. When property and equipment is sold or scrapped, the cost of the asset and the related accumulated amortization is removed when identifiable from the accounts, with the resulting net gain or loss being included in operations for the year.

Orillia Power Distribution Corporation
Notes to the Financial Statements
(In Thousands)
December 31, 2014

2. Summary of significant accounting policies (Continued)

Intangible assets

Intangible assets represent computer applications software and land rights. These assets are carried at cost net of accumulated amortization.

Amortization

Property and equipment and intangible assets are amortized using the straight-line method over periods approximating their estimated useful lives as follows:

Land rights	5	years
Buildings	10-50	years
Sub-stations/sub-transmission lines	15-60	years
Distribution system	25-60	years
Smart meters	15	years
Other capital assets	5-20	years

Fixed assets retirement obligations

Canadian generally accepted accounting principles (GAAP) 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. An equivalent amount is capitalized as an inherent cost of the associated fixed assets.

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 date can be determined and, consequently, a reasonable estimate of the fair value of any asset retirement obligations can not be made at the balance sheet date.

2. Summary of significant accounting policies (Continued)

Impairment of long-lived assets

Long-lived assets are tested for impairment when events or changes in circumstances indicate that their carrying amounts may not be recoverable. When indicators of impairment of the carrying value of the long-lived assets exist and the carrying value is greater than the fair value, an impairment loss is recognized to the extent that the fair value is below the carrying value. It is management's opinion that the long-lived assets are not exposed to any impairment and no impairment losses have been recognized.

Corporate income taxes

Current Income Taxes
Under the Electricity Act, 1998, the Company is required to make payments in lieu of corporate taxes to Ontario Electricity Financial Corporation (OEFC). These payments are calculated in accordance with the rules for computing 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.

Future Income Taxes
Future income taxes are provided for using the liability method and are recognized on temporary differences between the carrying amount of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit. Future income taxes are calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realized, based on the tax rates (and tax laws) that have been enacted or substantively enacted by the balance sheet date.

Future income tax liabilities are generally recognized on all taxable temporary differences and future tax assets are recognized to the extent that it is more likely than not that they be realized from taxable profits available against which deductible temporary differences can be utilized. The carrying amount of future income tax assets is reviewed at each balance sheet date and reduced to the extent that all or part of the future income tax assets have not met the "more likely than not" criterion. Previously unrecognized future income tax assets are reassessed at each balance sheet date and are recognized to the extent that it has become more likely than not of being recovered from future taxable profits.

2. Summary of significant accounting policies (Continued)

Employee future benefits

Pension plan
The Company provides pension benefits for its employees through the Ontario Municipal Employees Retirement System (OMERS). This multi-employer pension plan provides pensions for employees of Ontario municipalities, local boards, public utilities and school boards. It is a contributory defined benefit pension plan financed by equal contributions from participating employers and employees and by investment earnings of the fund. The Company recognizes the expense related to this plan as contributions are made.

Employee future benefits other than pension plan
The Company provides life insurance benefits to employees hired prior to January 1, 2008 when they are no longer providing active service. The Company also provides certain health and dental benefits for eligible management employees who retire after September 1, 2013. This benefit is payable from retirement date to age 65. Employee future benefits expense is recognized in the period in which the employee renders services. Employee future benefits other than pension plans are recorded on an accrual basis. The accrued benefit obligation and current service costs are actuarially determined using the projected benefit method pro-rated on service and based on assumptions that reflect management's best estimate. The current service cost for a period is equal to the present value of expected future benefits attributed to employee's services rendered in the period.

Use of estimates

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. These estimates and assumptions are based on management's historical experience, best knowledge of current events and actions that the Company may undertake in the future. Significant accounting estimates include allowance for doubtful accounts, unbilled revenue, inventory obsolescence, estimated useful lives of property and equipment, accrued benefit obligations and remaining recovery (settlement) for regulated assets (liabilities). Actual results could differ from those estimates.

2. Summary of significant accounting policies (Continued)

Financial instruments, hedges, and comprehensive income

The Company has made the following classifications for the purpose of measuring the value of the financial instruments:

- Cash and cash equivalents have been classified as "held for trading". They are initially measured at fair market value and the gains and losses resulting from the revaluation at fair value at the end of each period are recognized in net earnings.
- Receivables, unbilled revenue and due from related parties are classified as "loans and receivables". They are recorded at cost, which, upon their initial measurement, is equal to their fair value. Subsequent measurements of receivables are recorded at amortized cost which usually corresponds to the amount initially recorded less any allowance for doubtful accounts.
- Payables and accruals, customer and retailer deposits, bank credit line and long term debt are classified as "other financial liabilities". They are initially measured at fair value and the gains and losses resulting from their subsequent measurement at amortized cost, at the end of each period, are recognized in earnings.

Unless otherwise noted, it is management's opinion that they are not exposed to significant interest, currency or credit risks arising from its financial instruments.

The following is a discussion of principal risks and related mitigation strategies, related to financial instruments, that have been identified by the Company.

Credit risk

Financial instruments are exposed to credit risk as a result of the risk of the counter-party defaulting on its obligations. The Company monitors and limits its exposure to credit risk on a continuous basis. The Company provides reserves for credit risks based on the financial condition and short and long-term exposures to counterparties.

The carrying amount of receivables is reduced through the use of an allowance for doubtful accounts and the amount of the related impairment loss is recognized in the statement of earnings. Subsequent recoveries of receivables previously provisioned are credited to the statement of earnings.

Interest rate risk

The Company is exposed to interest rate risk in holding certain financial instruments. The Company's objective is to minimize net interest expense.

Orillia Power Distribution Corporation
Notes to the Financial Statements
(In Thousands)
December 31, 2014

3. Related party transactions

Transactions involving the sale of electricity are in the normal course of operations and are measured at the exchange amount, which is equal to the fair value as prescribed by regulation. Transactions involving other services have been recorded in these financial statements at the carrying amounts, which were equal to historical cost or fair value. Fair values represent fees for equivalent services provided to third parties in the normal course of operations as prescribed by regulations. The Company had the following related party transactions:

		2014		2013
Orillia Power Generation Corporation (OPGC) - a company under common control				
Services purchased from OPGC	$	**166**	$	299
Sales / services provided to OPGC		**950**		1,154
City of Orillia - the shareholder of Orillia Power Corporation, the parent company				
Power sold		**2,236**		2,330
Other services sold		**79**		190
Purchases		**80**		95
Property taxes		**67**		64
Interest incurred		**610**		610
Orillia Power Corporation (OPC) - parent company				
Services purchased from OPC		**51**		57
Sales / services provided to OPC		**8**		22

Balances outstanding at December 31:

		2014		2013
Due from Orillia Power Generation Corporation - related company	$	**768**	$	883
Due to Orillia Power Corporation - parent company		**57**		56

During the year, the Company incurred interest of $610 (2013 - $610) on a promissory note payable, to the City of Orillia, the shareholder of Orillia Power Corporation, the parent company. Included in payables and accruals is $157 (2013 - $16) due to the City of Orillia. Included in receivables is $293 (2013 - $206) due from the City of Orillia.

Orillia Power Distribution Corporation
Notes to the Financial Statements
(In Thousands)
December 31, 2014

4. Property and equipment

	Cost	Accumulated Amortization	2014 Net Book Value	2013 Net Book Value
Land	$ 280	$ -	$ 280	$ 280
Buildings	1,762	934	828	807
Sub-stations/sub-transmission lines	15,454	5,408	10,046	9,067
Distribution system	19,210	9,932	9,278	9,008
Other capital assets	4,528	3,551	977	1,168
	$ 41,234	$ 19,825	$ 21,409	$ 20,330

Beginning in 2013, the Company applied more detailed componentization to some of its assets and adjusted amortization rates in line with the estimated useful lives of the various asset components. As a result of this change, 2014 amortization expense and accumulated amortization are estimated to be $646 lower than they would have been without the change (2013 - $642). In accordance with OEB requirements, the impact of the change in amortization rates has been recorded as a $646 reduction in other revenue and an equivalent increase in regulatory liabilities.

5. Intangible assets

	Cost	Accumulated Amortization	2014 Net Book Value	2013 Net Book Value
Land rights	$ 46	$ 42	$ 4	$ 2
Software	290	148	142	135
	$ 336	$ 190	$ 146	$ 137

Orillia Power Distribution Corporation
Notes to the Financial Statements

(In Thousands)
December 31, 2014

6. Regulatory assets and liabilities

As described in Note 2, the Company has recorded the following regulatory assets and liabilities:

		2014		2013
Regulatory assets				
Regulatory assets	$	308	$	342
Retail settlement variances		100	$	-
	$	408	$	342
Regulatory liabilities				
Regulatory liabilities	$	1,183	$	237
Retail settlement variances		-		1,285
	$	1,183	$	1,522

Retail settlement variances
The Company accounts for differences between amounts charged by the Independent Electricity System Operator (energy commodity costs, costs of market operation, wholesale market settlement charges) and Hydro One (transmission charges) and the amounts billed to customers by the Company based on the OEB approved rates in retail settlement variance accounts.

Other regulatory assets / liabilities
These accounts include amounts deferred as required by OEB guidelines, including changes to fixed asset useful lives, effective January 1, 2013. The net book value of stranded meters related to the deployment of smart meters remains in regulatory assets as per OEB guidance. Application to recover these costs will be included in the next cost of service application.

7. Inventory

		2014		2013
Opening Balance	$	618	$	645
Inventory purchased		497		719
Inventory used in capital projects (capitalized)		(400)		(508)
Inventory used in operations & maintenance (expensed)		(104)		(142)
Inventory used in billable / recoverable projects		(83)		(95)
Inventory adjustment / other		(2)		(1)
Closing balance	$	526	$	618

8. Employee future benefits

Pension plan
Current service contributions to OMERS for 2014 were $337 (2013 - $324).

Employee future benefits other than pension plan
The Company measures its accrued benefits obligation for accounting purposes as at December 31 of each year. The latest actuarial valuation was performed as at December 31, 2014. Key economic assumptions used to determine the valuation are Consumer Price Index; 2.0% per annum, discount rate; 3.9% per annum and salary increase rate; 3.3%. A reconciliation of the Company's accrued benefits obligation is as follows:

		2014		2013
Employee future benefits obligation, beginning of year	$	525	$	521
Benefit expense		56		39
Benefit plan payments		(29)		(35)
Employee future benefits obligation, end of year	$	552	$	525

9. Long term debt

		2014		2013
Promissory note payable	$	9,762	$	9,762
Debenture payable - Infrastructure Ontario		1,155		1,365
		10,917		11,127
Less: current portion of long term debt		210		210
	$	10,707	$	10,917

The promissory note payable to the City of Orillia, the shareholder of Orillia Power Corporation, the parent Company, bears interest for the current year at 6.25% per annum (2013 – 6.25%). The interest rate is reviewed annually. Payments of interest are required to be made quarterly on the last day of March, June, September and December. The promissory note is due December 31, 2030. Under the terms of the note, the City of Orillia can demand repayment of up to 20% of the original principal in a calendar year.

Orillia Power Distribution Corporation
Notes to the Financial Statements
(In Thousands)
December 31, 2014

9. **Long term debt** (Continued)

The Company has entered into a financing arrangement with Ontario Infrastructure Projects Corporation (Infrastructure Ontario), to provide debenture financing for its smart meter infrastructure expenditures. On May 3, 2010 a debenture in the amount of $2,100 was finalized based on a 10-year term and an annual interest rate of 4.39%. The Company incurred $57 (2013 - $66) in interest expense to Infrastructure Ontario in 2014. Under the terms of the debenture, the Company must make annual principal repayments of $210 every year, until the debenture is retired in 2020. The repayment schedule is based on a semi-annual principal repayment of $105 in May and November of each year. The financing arrangement grants Infrastructure Ontario a general security agreement against the Company, in third priority behind the Toronto Dominion Bank and the City of Orillia.

10. Capital stock

	2014	2013
Authorized:		
The Company is authorized to issue an unlimited number of common shares		
Issued:		
1,001 common shares	$ 8,236	$ 8,236

11. Commitments

IESO prudential security
Purchasers of electricity in Ontario, through the Independent Electricity Systems Operator (IESO), are required to provide security to mitigate the risk of their default based on their expected activity in the market. The IESO could draw on these guarantees if the Company fails to make a payment required by default notice issued by the IESO. As at December 31, 2014, the Company has provided prudential support to the IESO in the form of a bank letter of credit in the amount of $2,035 (2013 - $2,035).

Orillia Power Distribution Corporation
Notes to the Financial Statements
(In Thousands)
December 31, 2014

12. Future income tax asset and payments in lieu of taxes

Future income tax assets and liabilities are provided for temporary differences between the financial statement carrying values of existing assets and liabilities and their respective tax bases. The significant components of future income tax assets and liabilities are as follows:

Future income tax asset:

	2014	2013
Excess of tax basis of capital assets and intangibles over carrying value	$ 1,311	$ 1,319
Regulatory assets and liabilities	(28)	233
Employee future benefit obligation	146	139
	$ 1,429	$ 1,691

Disclosed on the balance sheet as follows:

	2014	2013
Current	$ -	$ 233
Long term	1,429	1,458
	$ 1,429	$ 1,691

Provision for payments in lieu of taxes:

	2014	2013
Current	$ 74	$ 85
Future	262	224
	$ 336	$ 309

The Company has a capital loss of $30 that can be carried forward indefinitely

13. Contingencies

In 2012, a legal proceeding was commenced against the Company related to damages to Bell Canada property. The Company has turned this matter over to its liability insurer and the matter is currently before the Ontario Superior Court of Justice. At this time, it is not possible to quantify the effect, if any, on the financial statements of the Company. Management does not believe that the outcome of this matter will have a material impact on the financial statements.

In relation to a 2013 motor vehicle accident, a legal proceeding has been commenced against the Company. This matter has been turned over to the Company's liability insurer and is currently before the Ontario Superior Court of Justice. At this time, it is not possible to quantify the effect, if any, on the financial statements of the Company. Management does not believe that the outcome of this matter will have a material impact on the financial statements.

Orillia Power Distribution Corporation
Notes to the Financial Statements
(In Thousands)
December 31, 2014

14. Supplemental cash flow information

	2014	2013
Change in non-cash operating working capital		
Receivables	$ (681)	$ (567)
Unbilled revenue	185	(190)
Inventory	92	27
Prepaids	(29)	4
Due from related parties	116	(51)
Bank credit line	(750)	950
Payables and accruals	942	640
Payments in lieu of taxes	355	(469)
Customer and retailer deposits	36	(51)
	$ 266	$ 293
Interest received	$ 14	$ 16
Interest paid	$ 518	$ 679
Payment in lieu of taxes (received) paid	$ (282)	$ 554

15. Public liability insurance

The Company is a member of the Municipal Electric Association Reciprocal Insurance Exchange (MEARIE), which was created on January 1, 1987. A reciprocal insurance exchange may be defined as a group of persons formed for the purpose of exchanging reciprocal contracts of indemnity or inter-insurance with each other through the same attorney. MEARIE provides general liability insurance to the Company of $34 million per occurrence.

16. Capital disclosures

The Company's objectives when managing capital are:

- to safeguard the Company's ability to continue as a going concern, so that it can continue to provide adequate returns for shareholders and benefits for other stakeholders, and
- to provide an adequate return to shareholders by controlling costs and establishing rates that maximize rate of return commensurate with the level of risk.

16. Capital disclosures (Continued)

The Company manages its capital structure and makes adjustments to it in light of changes in economic conditions, annual profitability and the risk characteristics of the underlying assets. In order to maintain or adjust the capital structure, the Company will adjust the amount of dividends paid to shareholders, subject to the constraints imposed by lending agreements. The Company is subject to annual reporting and bank review of its interest coverage and debt capitalization ratios, in relation to the bank credit line.

Consistent with others in the industry, the Company monitors capital on the basis of the debt-to-capital ratio. This ratio is calculated as long term debt divided by the sum of long term debt plus equity, as shown on the balance sheet. Equity consists of share capital, contributed capital and retained earnings. The debt- to-capital ratio at December 31, 2014 is 46% (2013 - 48%).

17. Future accounting pronouncements

International Financial Reporting Standards (IFRS)

The CICA has announced that Canadian publicly accountable enterprises will be required to adopt International Financial Reporting Standards (IFRS), as issued by the International Accounting Standards Board (IASB), effective January 1, 2011. The Canadian Accounting Standards Board (AcSB) subsequently released rulings that qualifying entities with rate-regulated activities have the option to defer their adoption of IFRS until annual periods beginning on or after January 1, 2015. The Company has elected to apply the deferral option.

IFRS will require increased financial statement disclosure. Although IFRS uses a conceptual framework similar to Canadian generally accepted accounting principles, there will be some differences in accounting policies, that will need to be addressed. The Company is currently in the process of implementing its plan for the adoption of IFRS, effective January 1, 2015. For 2015 reporting, the 2014 results will be restated under IFRS, for comparative purposes.

18. Bank credit line

The Company has a $5,000 (2013 - $5,000) operating loan agreement with its bank to fund working capital and prudential security requirements. Amounts outstanding at year end on the loan include a standby letter of credit in favour of the IESO for $2,035 (2013 - $2,035) and cash advances of $200 (2013 - $950). The operating loan is secured with a General Security Agreement on the Company's assets.

HYDRO ONE INC.
MANAGEMENT'S REPORT

The Consolidated Financial Statements, Management's Discussion and Analysis (MD&A) and related financial information have been prepared by the management of Hydro One Inc. (Hydro One or the Company). Management is responsible for the integrity, consistency and reliability of all such information presented. The Consolidated Financial Statements have been prepared in accordance with United States Generally Accepted Accounting Principles and applicable securities legislation. The MD&A has been prepared in accordance with National Instrument 51-102.

The preparation of the Consolidated Financial Statements and information in the MD&A involves the use of estimates and assumptions based on management's judgment, particularly when transactions affecting the current accounting period cannot be finalized with certainty until future periods. Estimates and assumptions are based on historical experience, current conditions and various other assumptions believed to be reasonable in the circumstances, with critical analysis of the significant accounting policies followed by the Company as described in Note 2 to the Consolidated Financial Statements. The preparation of the Consolidated Financial Statements and the MD&A includes information regarding the estimated impact of future events and transactions. The MD&A also includes information regarding sources of liquidity and capital resources, operating trends, risks and uncertainties. Actual results in the future may differ materially from the present assessment of this information because future events and circumstances may not occur as expected. The Consolidated Financial Statements and MD&A have been properly prepared within reasonable limits of materiality and in light of information up to February 11, 2016.

Management is responsible for establishing and maintaining adequate internal control over financial reporting for the Company. In meeting its responsibility for the reliability of financial information, management maintains and relies on a comprehensive system of internal control and internal audit. The system of internal control includes a written corporate conduct policy; implementation of a risk management framework; effective segregation of duties and delegation of authorities; and sound and conservative accounting policies that are regularly reviewed. This structure is designed to provide reasonable assurance that assets are safeguarded and that reliable information is available on a timely basis. In addition, management has assessed the design and operating effectiveness of the Company's internal control over financial reporting in accordance with the criteria set forth in Internal Control – Integrated Framework (2013), issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this assessment, management concluded that the Company maintained effective internal control over financial reporting as of December 31, 2015. The effectiveness of these internal controls is reported to the Audit Committee of the Hydro One Board of Directors, as required.

The Consolidated Financial Statements have been audited by KPMG LLP, independent external auditors appointed by the shareholder of the Company. The external auditors' responsibility is to express their opinion on whether the Consolidated Financial Statements are fairly presented in accordance with United States Generally Accepted Accounting Principles. The Independent Auditors' Report outlines the scope of their examination and their opinion.

The Hydro One Board of Directors, through its Audit Committee, is responsible for ensuring that management fulfills its responsibilities for financial reporting and internal controls. The Audit Committee of Hydro One met periodically with management, the internal auditors and the external auditors to satisfy itself that each group had properly discharged its respective responsibility and to review the Consolidated Financial Statements before recommending approval by the Board of Directors. The external auditors had direct and full access to the Audit Committee, with and without the presence of management, to discuss their audit findings.

The President and Chief Executive Officer and the Chief Financial Officer have certified Hydro One's annual Consolidated Financial Statements and annual MD&A, related disclosure controls and procedures and the design and effectiveness of related internal controls over financial reporting.

On behalf of Hydro One's management:

Mayo Schmidt	Michael Vels
President and Chief Executive Officer	Chief Financial Officer

HYDRO ONE INC.
INDEPENDENT AUDITORS' REPORT

To the Shareholder of Hydro One Inc.

We have audited the accompanying Consolidated Financial Statements of Hydro One Inc., which comprise the consolidated balance sheets as at December 31, 2015 and December 31, 2014, the consolidated statements of operations and comprehensive income, changes in equity and cash flows for the years 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 United States Generally Accepted Accounting Principles, 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 audits. We conducted our audits 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 in our audits 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 consolidated financial position of Hydro One Inc. as at December 31, 2015 and December 31, 2014, and its consolidated results of operations and its consolidated cash flows for the years then ended in accordance with United States Generally Accepted Accounting Principles.

KPMG LLP

Chartered Professional Accountants, Licensed Public Accountants

Toronto, Canada
February 11, 2016

HYDRO ONE INC.
CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME
For the years ended December 31, 2015 and 2014

Year ended December 31 *(millions of Canadian dollars, except per share amounts)*	**2015**	**2014**
Revenues		
Distribution (includes $159 related party revenues; 2014 – $159) *(Note 23)*	4,949	4,903
Transmission (includes $1,554 related party revenues; 2014 – $1,567) *(Note 23)*	1,536	1,588
Other	44	57
	6,529	6,548
Costs		
Purchased power (includes $2,335 related party costs; 2014 – $2,633) *(Note 23)*	3,450	3,419
Operation, maintenance and administration *(Note 23)*	1,130	1,192
Depreciation and amortization *(Note 5)*	757	722
	5,337	5,333
Income before financing charges and income taxes	1,192	1,215
Financing charges *(Note 6)*	376	379
Income before income taxes	816	836
Income taxes *(Notes 7, 23)*	114	89
Net income	**702**	**747**
Other comprehensive income	–	–
Comprehensive income	**702**	**747**
Net income and comprehensive income attributable to:		
Noncontrolling interest *(Note 22)*	10	(2)
Preferred shareholder	13	18
Common shareholder	679	731
	702	**747**
Earnings per common share *(Note 20)*		
Basic	$6,340	$7,319
Diluted	$6,340	$7,319
Dividends per common share declared *(Note 19)*	$8,750	$2,696

See accompanying notes to Consolidated Financial Statements.

HYDRO ONE INC.
CONSOLIDATED BALANCE SHEETS
At December 31, 2015 and 2014

December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Assets		
Current assets:		
Cash and cash equivalents *(Note 13)*	89	100
Accounts receivable (net of allowance for doubtful accounts – $61; 2014 – $66) *(Note 8)*	772	1,016
Due from related parties *(Note 23)*	184	224
Regulatory assets *(Note 11)*	36	31
Materials and supplies	21	23
Deferred income tax assets *(Note 7)*	19	19
Derivative instruments *(Note 13)*	–	2
Prepaid expenses and other assets	24	35
	1,145	1,450
Property, plant and equipment *(Note 9)*:		
Property, plant and equipment in service	25,911	25,356
Less: accumulated depreciation	9,319	9,134
	16,592	16,222
Construction in progress	1,144	1,025
Future use land, components and spares	157	154
	17,893	17,401
Other long-term assets:		
Regulatory assets *(Note 11)*	3,015	3,200
Deferred income tax assets *(Note 7)*	1,610	7
Intangible assets (net of accumulated amortization – $274; 2014 – $305) *(Note 10)*	336	276
Goodwill *(Note 4)*	163	173
Deferred debt issuance costs	34	36
Derivative instruments *(Note 13)*	1	–
Other	6	7
	5,165	3,699
Total assets	**24,203**	**22,550**

See accompanying notes to Consolidated Financial Statements.

HYDRO ONE INC.
CONSOLIDATED BALANCE SHEETS (continued)
At December 31, 2015 and 2014

December 31 *(millions of Canadian dollars, except number of shares)*	**2015**	**2014**
Liabilities		
Current liabilities:		
Bank indebtedness *(Note 13)*	–	2
Short-term notes payable *(Notes 12, 13)*	1,491	–
Accounts payable	152	173
Accrued liabilities *(Notes 15, 16)*	591	611
Due to related parties *(Note 23)*	132	227
Accrued interest	96	100
Regulatory liabilities *(Note 11)*	19	47
Derivative instruments *(Note 13)*	–	3
Long-term debt payable within one year (includes $nil measured at fair value; 2014 – $252) *(Notes 12, 13)*	500	552
	2,981	1,715
Long-term debt (includes $51 measured at fair value; 2014 – $nil) *(Notes 12, 13)*	8,224	8,373
Other long-term liabilities:		
Post-retirement and post-employment benefit liability *(Note 15)*	1,541	1,533
Pension benefit liability *(Note 15)*	952	1,236
Regulatory liabilities *(Note 11)*	236	168
Deferred income tax liabilities *(Note 7)*	206	1,313
Environmental liabilities *(Note 16)*	185	221
Net unamortized debt premiums	17	18
Due to related parties *(Note 21, 23)*	10	–
Asset retirement obligations *(Note 17)*	9	9
Long-term accounts payable and other liabilities	17	17
	3,173	4,515
Total liabilities	**14,378**	**14,603**

Contingencies and Commitments (Notes 25, 26)
Subsequent Events (Note 28)

Preferred shares *(Notes 18, 19)*	–	323
Noncontrolling interest subject to redemption *(Note 22)*	23	21
Equity		
Common shares *(Notes 18, 19)*	6,000	3,314
Retained earnings	3,759	4,249
Accumulated other comprehensive loss	(9)	(9)
Total Hydro One shareholder's equity	9,750	7,554
Noncontrolling interest *(Note 22)*	52	49
Total equity	**9,802**	**7,603**
	24,203	**22,550**

See accompanying notes to Consolidated Financial Statements.

On behalf of the Board of Directors:

David Denison
Chair

Philip Orsino
Chair, Audit Committee

HYDRO ONE INC.
CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY
For the years ended December 31, 2015 and 2014

Year ended December 31, 2015 *(millions of Canadian dollars)*	**Common Shares**	**Retained Earnings**	**Accumulated Other Comprehensive Loss**	**Total Hydro One Shareholder's Equity**	**Non-controlling Interest** *(Note 22)*	**Total Equity**
January 1, 2015	3,314	4,249	(9)	7,554	49	7,603
Net income	–	692	–	692	7	699
Other comprehensive income	–	–	–	–	–	–
Distributions to noncontrolling interest	–	–	–	–	(4)	(4)
Dividends on preferred shares	–	(13)	–	(13)	–	(13)
Dividends on common shares	–	(875)	–	(875)	–	(875)
Common shares issued *(Note 18)*	2,923	–	–	2,923	–	2,923
Hydro One Brampton spin-off *(Note 4)*	(196)	(258)	–	(454)	–	(454)
Hydro One Telecom and MBSI spin-offs *(Note 4)*	(41)	(36)	–	(77)	–	(77)
December 31, 2015	6,000	3,759	(9)	9,750	52	9,802

Year ended December 31, 2014 *(millions of Canadian dollars)*	**Common Shares**	**Retained Earnings**	**Accumulated Other Comprehensive Loss**	**Total Hydro One Shareholder's Equity**	**Non-controlling Interest** *(Note 22)*	**Total Equity**
January 1, 2014	3,314	3,787	(9)	7,092	–	7,092
Net income	–	749	–	749	(1)	748
Other comprehensive income	–	–	–	–	–	–
Amount contributed by noncontrolling interest	–	–	–	–	50	50
Dividends on preferred shares	–	(18)	–	(18)	–	(18)
Dividends on common shares	–	(269)	–	(269)	–	(269)
December 31, 2014	3,314	4,249	(9)	7,554	49	7,603

See accompanying notes to Consolidated Financial Statements.

HYDRO ONE INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
For the years ended December 31, 2015 and 2014

Year ended December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Operating activities		
Net income	702	747
Environmental expenditures	(19)	(18)
Adjustments for non-cash items:		
Depreciation and amortization (excluding removal costs)	667	641
Regulatory assets and liabilities	(3)	(69)
Deferred income taxes *(Note 7)*	(2,817)	10
Other	24	–
Changes in non-cash balances related to operations *(Note 24)*	187	(55)
Net cash from (used in) operating activities	(1,259)	1,256
Financing activities		
Long-term debt issued	350	628
Long-term debt retired	(585)	(776)
Short-term notes issued	1,491	–
Common shares issued	2,600	–
Dividends paid	(888)	(287)
Amount contributed by noncontrolling interest *(Note 22)*	–	72
Distributions paid to noncontrolling interest	(5)	–
Change in bank indebtedness	(2)	(29)
Other	(7)	(3)
Net cash from (used in) financing activities	2,954	(395)
Investing activities		
Capital expenditures *(Note 24)*		
Property, plant and equipment	(1,594)	(1,481)
Intangible assets	(37)	(23)
Capital contributions received *(Note 24)*	62	–
Acquisition of Haldimand Hydro *(Note 4)*	(66)	–
Acquisition of Woodstock Hydro *(Note 4)*	(24)	–
Investment in Hydro One Brampton *(Note 4)*	(53)	–
Acquisition of Norfolk Power *(Note 4)*	–	(66)
Proceeds from investment	–	250
Other	6	(6)
Net cash used in investing activities	(1,706)	(1,326)
Net change in cash and cash equivalents	(11)	(465)
Cash and cash equivalents, beginning of year	100	565
Cash and cash equivalents, end of year	**89**	**100**

See accompanying notes to Consolidated Financial Statements.

1. DESCRIPTION OF THE BUSINESS

Hydro One Inc. (Hydro One or the Company) was incorporated on December 1, 1998, under the *Business Corporations Act* (Ontario) and is wholly owned by Hydro One Limited.

On October 31, 2015, Hydro One Limited, a subsidiary of the Province of Ontario (Province), acquired Hydro One. The principal businesses of Hydro One are the transmission and distribution of electricity to customers within Ontario.

In November 2015, Hydro One Limited and the Province completed an initial public offering (IPO) on the Toronto Stock Exchange of 15% of Hydro One Limited's 595 million outstanding common shares. See Note 18 for reorganization of Hydro One.

2. SIGNIFICANT ACCOUNTING POLICIES

Basis of Consolidation

These Consolidated Financial Statements include the accounts of the Company and its wholly owned subsidiaries. Intercompany transactions and balances have been eliminated.

On August 31, 2015, Hydro One completed the spin-off of its subsidiary, Hydro One Brampton Networks Inc. (Hydro One Brampton) to the Province. See note 4 – Business Combinations. These Consolidated Financial Statements include the results of operations of Hydro One Brampton up to August 31, 2015.

On November 6, 2015, Hydro One completed the spin-off of its subsidiaries, Hydro One Telecom Inc. (Hydro One Telecom) and Municipal Billing Services Inc. (MBSI). See note 4 – Business Combinations. These Consolidated Financial Statements include the results of operations of Hydro One Telecom and MBSI up to November 6, 2015.

Basis of Accounting

These Consolidated Financial Statements are prepared and presented in accordance with United States (US) Generally Accepted Accounting Principles (GAAP) and in Canadian dollars.

Hydro One performed an evaluation of subsequent events through to February 11, 2016, the date these Consolidated Financial Statements were issued, to determine whether any events or transactions warranted recognition and disclosure in these Consolidated Financial Statements. See Note 28 – Subsequent Events.

Use of Management Estimates

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues, expenses, gains and losses during the reporting periods. Management evaluates these estimates on an ongoing basis based upon historical experience, current conditions, and assumptions believed to be reasonable at the time the assumptions are made, with any adjustments being recognized in results of operations in the period they arise. Significant estimates relate to regulatory assets and regulatory liabilities, environmental liabilities, pension benefits, post-retirement and post-employment benefits, asset retirement obligations, goodwill and asset impairments, contingencies, unbilled revenues, allowance for doubtful accounts, derivative instruments, and deferred income tax assets and liabilities. Actual results may differ significantly from these estimates.

Rate Setting

The Company's Transmission Business consists of the transmission business of Hydro One Networks, as well as its 66% interest in B2M Limited Partnership (B2M LP). The Company's Distribution Business consists of the distribution businesses of Hydro One Networks, Haldimand County Utilities Inc. (Haldimand Hydro), Hydro One Remote Communities Inc. (Hydro One Remote Communities), and Woodstock Hydro Holdings Inc. (Woodstock Hydro).

The Ontario Energy Board (OEB) has approved the use of US GAAP for rate setting and regulatory accounting and reporting by Hydro One Networks' transmission and distribution businesses, as well as by Hydro One Remote Communities.

Transmission

On January 8, 2015, pursuant to an application filed with the OEB, the OEB approved the 2015 Hydro One transmission rates revenue requirement, excluding the B2M LP revenue requirement, of $1,477 million.

On June 30, 2015, B2M LP updated its application (originally filed March 30, 2015) with the OEB for 2015-2019 transmission rates, requesting approval of revenue requirement of $39 million, $36 million, $37 million, $38 million and $37 million for the respective years. On December 29, 2015, the OEB issued a Decision and Order approving the 2015-2019 rates revenue requirement, and on January 14, 2016, the OEB approved the B2M LP revenue requirement recovery through the 2016 Uniform Transmission Rates, and the establishment of a deferral account to capture costs of Tax Rate and Rule changes.

Distribution

On March 12, 2015, the OEB issued a Decision and Rate Order approving a revenue requirement of $1,326 million for 2015, $1,430 million for 2016 and $1,486 million for 2017. The revenue requirements for 2016 and 2017 are estimates that may change based on 2016 and 2017 Rate Orders. On April 23, 2015, the Final Rate Order for 2015 rates was approved by the OEB.

On September 24, 2014, Hydro One Remote Communities filed an Incentive Regulation Mechanism application with the OEB for 2015 rates, seeking approval for increased base rates for the distribution and generation of electricity of 1.7%. On March 19, 2015, the OEB approved an increase of approximately 1.6% to basic rates for the distribution and generation of electricity, with an effective date of May 1, 2015.

Regulatory Accounting

The OEB has the general power to include or exclude revenues, costs, gains or losses in the rates of a specific period, resulting in a change in the timing of accounting recognition from that which would have been applied in an unregulated company. Such change in timing involves the application of rate-regulated accounting, giving rise to the recognition of regulatory assets and liabilities. The Company's regulatory assets represent certain amounts receivable from future customers and costs that have been deferred for accounting purposes because it is probable that they will be recovered in future rates. In addition, the Company has recorded regulatory liabilities that generally represent amounts that are refundable to future customers. The Company continually assesses the likelihood of recovery of each of its regulatory assets and continues to believe that it is probable that the OEB will factor its regulatory assets and liabilities into the setting of future rates. If, at some future date, the Company judges that it is no longer probable that the OEB will include a regulatory asset or liability in setting future rates, the appropriate carrying amount will be reflected in results of operations in the period that the assessment is made.

Cash and Cash Equivalents

Cash and cash equivalents include cash and short-term investments with an original maturity of three months or less.

Revenue Recognition

Transmission revenues are collected through OEB-approved rates, which are based on an approved revenue requirement that includes a rate of return. Such revenue is recognized as electricity is transmitted and delivered to customers.

Distribution revenues attributable to the delivery of electricity are based on OEB-approved distribution rates and are recognized on an accrual basis and include billed and unbilled revenues. Billed revenues are based on electricity delivered as measured from customer meters. Unbilled revenues are based on an estimate of electricity delivered determined by historical trends of consumption and are estimated at the end of each month. The unbilled revenue estimate is affected by energy consumption, weather, and changes in the composition of customer classes.

Distribution revenue also includes an amount relating to rate protection for rural, residential and remote customers, which is received from the Independent Electricity System Operator (IESO) based on a standardized customer rate that is approved by the OEB.

Revenues also include amounts related to sales of other services and equipment. Such revenue is recognized as services are rendered or as equipment is delivered.

Revenues are recorded net of indirect taxes.

Accounts Receivable and Allowance for Doubtful Accounts

Billed accounts receivable are recorded at the invoiced amount, net of allowance for doubtful accounts. Unbilled accounts receivable are recorded at their estimated value. Overdue amounts related to regulated billings bear interest at OEB-approved rates. The allowance for doubtful accounts reflects the Company's best estimate of losses on billed accounts receivable balances. The Company estimates the allowance for doubtful accounts on customer receivables by applying internally developed loss rates to the outstanding receivable balances by aging category. Loss rates applied to the accounts receivable balances are based on historical overdue balances, customer payments and write-offs. Accounts receivable are written-off against the allowance when they are deemed uncollectible. The existing allowance for doubtful accounts will continue to be affected by changes in volume, prices and economic conditions.

Noncontrolling interest

Noncontrolling interest represents the portion of equity ownership in subsidiaries that is not attributable to shareholders of Hydro One. Noncontrolling interest is initially recorded at fair value and subsequently the amount is adjusted for the proportionate share of net income (loss) and other comprehensive income (loss) attributable to the noncontrolling interest and any dividends or distributions paid to the noncontrolling interest.

If a transaction results in the acquisition of all, or part, of a noncontrolling interest in a subsidiary, the acquisition of the noncontrolling interest is accounted for as an equity transaction. No gain or loss is recognized in consolidated net income or comprehensive income as a result of changes in the noncontrolling interest, unless a change results in the loss of control by the Company.

Income Taxes

By virtue of being wholly owned by the Province, Hydro One was exempt from tax under the *Income Tax Act* (Canada) and the *Taxation Act, 2007* (Ontario) (Federal Tax Regime). However, under the *Electricity Act*, Hydro One was required to make payments in lieu of tax (PILs) to the Ontario Electricity Financial Corporation (OEFC) (PILs Regime). The PILs were, in general, based on the amount of tax that Hydro One would otherwise be liable to pay under the Federal Tax Regime if it was not exempt from taxes under those statutes.

In connection with the IPO of Hydro One Limited, Hydro One's exemption from tax under the Federal Tax Regime ceased to apply. Upon exiting the PILs Regime, Hydro One is required to make corporate income tax payments to the Canada Revenue Agency (CRA) under the Federal Tax Regime.

Current and deferred income taxes are computed based on the tax rates and tax laws enacted as at the balance sheet date. Tax benefits associated with income tax positions taken, or expected to be taken, in a tax return are recorded only when the "more-likely-than-not" recognition threshold is satisfied and are measured at the largest amount of benefit that has a greater than 50% likelihood of being realized upon settlement. Management evaluates each position based solely on the technical merits and facts and circumstances of the position, assuming the position will be examined by a taxing authority having full knowledge of all relevant information. Significant management judgment is required to determine recognition thresholds and the related amount of tax benefits to be recognized in the Consolidated Financial Statements. Management re-evaluates tax positions each period in which new information about recognition or measurement becomes available.

Deferred Income Taxes

Deferred income taxes are provided for using the liability method. Deferred income taxes are recognized based on the estimated future tax consequences attributable to temporary differences between the carrying amount of assets and liabilities in the Consolidated Financial Statements and their corresponding tax bases.

Deferred income tax liabilities are generally recognized on all taxable temporary differences. Deferred tax assets are recognized to the extent that it is more-likely-than-not that these assets will be realized from taxable income available against which deductible temporary differences can be utilized.

Deferred income taxes are calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realized, based on the tax rates and tax laws that have been enacted as at the balance sheet date. Deferred income taxes that are not included in the rate-setting process are charged or credited to the Consolidated Statements of Operations and Comprehensive Income.

If management determines that it is more-likely-than-not that some or all of a deferred income tax asset will not be realized, a valuation allowance is recorded against the deferred income tax asset to report the net balance at the amount expected to be realized. Previously unrecognized deferred income tax assets are reassessed at each balance sheet date and are recognized to the extent that it has become more-likely-than-not that the tax benefit will be realized.

The Company records regulatory assets and liabilities associated with deferred income taxes that will be included in the rate-setting process.

The Company uses the flow-through method to account for investment tax credits (ITCs) earned on eligible scientific research and experimental development expenditures, and apprenticeship job creation. Under this method, only non-refundable ITCs are recognized as a reduction to income tax expense.

Materials and Supplies

Materials and supplies represent consumables, small spare parts and construction materials held for internal construction and maintenance of property, plant and equipment. These assets are carried at average cost less any impairments recorded.

Property, Plant and Equipment

Property, plant and equipment is recorded at original cost, net of customer contributions, and any accumulated impairment losses. The cost of additions, including betterments and replacement asset components, is included on the Consolidated Balance Sheets as property, plant and equipment.

The original cost of property, plant and equipment includes direct materials, direct labour (including employee benefits), contracted services, attributable capitalized financing costs, asset retirement costs, and direct and indirect overheads that are related to the capital project or program. Indirect overheads include a portion of corporate costs such as finance, treasury, human resources, information technology and executive costs. Overhead costs, including corporate functions and field services costs, are capitalized on a fully allocated basis, consistent with an OEB-approved methodology.

Property, plant and equipment in service consists of transmission, distribution, communication, administration and service assets and land easements. Property, plant and equipment also includes future use assets, such as land, major components and spare parts, and capitalized project development costs associated with deferred capital projects.

Transmission

Transmission assets include assets used for the transmission of high-voltage electricity, such as transmission lines, support structures, foundations, insulators, connecting hardware and grounding systems, and assets used to step up the voltage of electricity from generating stations for transmission and to step down voltages for distribution, including transformers, circuit breakers and switches.

Distribution

Distribution assets include assets related to the distribution of low-voltage electricity, including lines, poles, switches, transformers, protective devices and metering systems.

Communication

Communication assets include fibre optic and microwave radio systems, optical ground wire, towers, telephone equipment and associated buildings.

Administration and Service

Administration and service assets include administrative buildings, personal computers, transport and work equipment, tools and other minor assets.

Easements

Easements include statutory rights of use for transmission corridors and abutting lands granted under the *Reliable Energy and Consumer Protection Act, 2002*, as well as other land access rights.

Intangible Assets

Intangible assets separately acquired or internally developed are measured on initial recognition at cost, which comprises purchased software, direct labour (including employee benefits), consulting, engineering, overheads and attributable capitalized financing charges. Following initial recognition, intangible assets are carried at cost, net of any accumulated amortization and accumulated impairment losses. The Company's intangible assets primarily represent major computer applications.

Capitalized Financing Costs

Capitalized financing costs represent interest costs attributable to the construction of property, plant and equipment or development of intangible assets. The financing cost of attributable borrowed funds is capitalized as part of the acquisition cost of such assets. The capitalized financing costs are a reduction of financing charges recognized in the Consolidated Statements of Operations and Comprehensive Income. Capitalized financing costs are calculated using the Company's weighted average effective cost of debt.

Construction and Development in Progress

Construction and development in progress consists of the capitalized cost of constructed assets that are not yet complete and which have not yet been placed in service.

Depreciation and Amortization

The cost of property, plant and equipment and intangible assets is depreciated or amortized on a straight-line basis based on the estimated remaining service life of each asset category, except for transport and work equipment, which is depreciated on a declining balance basis.

The Company periodically initiates an external independent review of its property, plant and equipment and intangible asset depreciation and amortization rates, as required by the OEB. Any changes arising from OEB approval of such a review are implemented on a remaining service life basis, consistent with their inclusion in electricity rates. The last review resulted in changes to rates effective January 1, 2015. A summary of average service lives and depreciation and amortization rates for the various classes of assets is included below:

	Average	Rate	
	Service Life	Range	Average
Transmission	56 years	1% – 2%	2%
Distribution	46 years	1% – 7%	2%
Communication	16 years	1% – 15%	6%
Administration and service	18 years	1% – 20%	6%

The cost of intangible assets is included primarily within the administration and service classification above. Amortization rate for computer applications software and other intangible assets is 10%.

In accordance with group depreciation practices, the original cost of property, plant and equipment, or major components thereof, and intangible assets that are normally retired, is charged to accumulated depreciation, with no gain or loss being reflected in results of operations. Where a disposition of property, plant and equipment occurs through sale, a gain or loss is calculated based on proceeds and such gain or loss is included in depreciation expense. Depreciation expense also includes the costs incurred to remove property, plant and equipment where no asset retirement obligations have been recorded.

Goodwill

Goodwill represents the cost of acquired local distribution companies that is in excess of the fair value of the net identifiable assets acquired at the acquisition date. Goodwill is not included in rate base.

Goodwill is evaluated for impairment on an annual basis, or more frequently if circumstances require. The Company performs a qualitative assessment to determine whether it is more-likely-than-not that the fair value of the applicable reporting unit is less than its carrying amount. If the Company determines, as a result of its qualitative assessment, that it is not more-likely-than-not that the fair value of the applicable reporting unit is less than its carrying amount, no further testing is required. If the Company determines, as a result of its qualitative assessment, that it is more-likely-than-not that the fair

value of the applicable reporting unit is less than its carrying amount, a goodwill impairment assessment is performed using a two-step, fair value-based test. The first step compares the fair value of the applicable reporting unit to its carrying amount, including goodwill. If the carrying amount of the applicable reporting unit exceeds its fair value, a second step is performed. The second step requires an allocation of fair value to the individual assets and liabilities using purchase price allocation in order to determine the implied fair value of goodwill. If the implied fair value of goodwill is less than the carrying amount, an impairment loss is recorded as a reduction to goodwill and as a charge to results of operations.

For the year ended December 31, 2015, based on the qualitative assessment performed as at September 30, 2015, the Company has determined that it is not more-likely-than-not that the fair value of each applicable reporting unit assessed is less than its carrying amount. As a result, no further testing was performed, and the Company has concluded that goodwill was not impaired at December 31, 2015.

Long-Lived Asset Impairment

When circumstances indicate the carrying value of long-lived assets may not be recoverable, the Company evaluates whether the carrying value of such assets, excluding goodwill, has been impaired. For such long-lived assets, the Company evaluates whether impairment may exist by estimating future estimated undiscounted cash flows expected to result from the use and eventual disposition of the asset. When alternative courses of action to recover the carrying amount of a long-lived asset are under consideration, a probability-weighted approach is used to develop estimates of future undiscounted cash flows. If the carrying value of the long-lived asset is not recoverable based on the estimated future undiscounted cash flows, an impairment loss is recorded, measured as the excess of the carrying value of the asset over its fair value. As a result, the asset's carrying value is adjusted to its estimated fair value.

Within its regulated business, the carrying costs of most of Hydro One's long-lived assets are included in rate base where they earn an OEB-approved rate of return. Asset carrying values and the related return are recovered through approved rates. As a result, such assets are only tested for impairment in the event that the OEB disallows recovery, in whole or in part, or if such a disallowance is judged to be probable.

Hydro One regularly monitored the assets of its unregulated Hydro One Telecom subsidiary prior to spin-off for indications of impairment. Management assessed the fair value of such long-lived assets using commonly accepted techniques, which included but were not limited to, the use of recent third party comparable sales for reference and internally developed discounted cash flow analysis. Significant changes in market conditions, changes to the condition of an asset, or a change in management's intent to utilize the asset was generally viewed by management as triggering events to reassess the cash flows related to these long-lived assets. As at December 31, 2015 and 2014, no asset impairment had been recorded for assets within either the Company's regulated or unregulated businesses.

Costs of Arranging Debt Financing

For financial liabilities classified as other than held-for-trading, the Company defers the external transaction costs related to obtaining debt financing and presents such amounts as deferred debt issuance costs on the Consolidated Balance Sheets. Deferred debt issuance costs are amortized over the contractual life of the related debt on an effective-interest basis and the amortization is included within financing charges in the Consolidated Statements of Operations and Comprehensive Income. Transaction costs for items classified as held-for-trading are expensed immediately.

Comprehensive Income

Comprehensive income is comprised of net income and other comprehensive income (OCI). Hydro One presents net income and OCI in a single continuous Consolidated Statement of Operations and Comprehensive Income.

Financial Assets and Liabilities

All financial assets and liabilities are classified into one of the following five categories: held-to-maturity; loans and receivables; held-for-trading; other liabilities; or available-for-sale. Financial assets and liabilities classified as held-for-trading are measured at fair value. All other financial assets and liabilities are measured at amortized cost, except accounts receivable and amounts due from related parties, which are measured at the lower of cost or fair value. Accounts receivable and amounts due from related parties are classified as loans and receivables. The Company considers the carrying amounts of accounts receivable and amounts due from related parties to be reasonable estimates of fair value because of the short time to maturity of these instruments. Provisions for impaired accounts receivable are recognized as adjustments to the allowance for

doubtful accounts and are recognized when there is objective evidence that the Company will not be able to collect amounts according to the original terms. All financial instrument transactions are recorded at trade date.

Derivative instruments are measured at fair value. Gains and losses from fair valuation are included within financing charges in the period in which they arise. The Company determines the classification of its financial assets and liabilities at the date of initial recognition. The Company designates certain of its financial assets and liabilities to be held at fair value, when it is consistent with the Company's risk management policy disclosed in Note 13 – Fair Value of Financial Instruments and Risk Management.

Derivative Instruments and Hedge Accounting

The Company closely monitors the risks associated with changes in interest rates on its operations and, where appropriate, uses various instruments to hedge these risks. Certain of these derivative instruments qualify for hedge accounting and are designated as accounting hedges, while others either do not qualify as hedges or have not been designated as hedges (hereinafter referred to as undesignated contracts) as they are part of economic hedging relationships.

The accounting guidance for derivative instruments requires the recognition of all derivative instruments not identified as meeting the normal purchase and sale exemption as either assets or liabilities recorded at fair value on the Consolidated Balance Sheets. For derivative instruments that qualify for hedge accounting, the Company may elect to designate such derivative instruments as either cash flow hedges or fair value hedges. The Company offsets fair value amounts recognized on its Consolidated Balance Sheets related to derivative instruments executed with the same counterparty under the same master netting agreement.

For derivative instruments that qualify for hedge accounting and which are designated as cash flow hedges, the effective portion of any gain or loss, net of tax, is reported as a component of accumulated OCI (AOCI) and is reclassified to results of operations in the same period or periods during which the hedged transaction affects results of operations. Any gains or losses on the derivative instrument that represent either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness are recognized in results of operations. For fair value hedges, changes in fair value of both the derivative instrument and the underlying hedged exposure are recognized in the Consolidated Statements of Operations and Comprehensive Income in the current period. The gain or loss on the derivative instrument is included in the same line item as the offsetting gain or loss on the hedged item in the Consolidated Statements of Operations and Comprehensive Income. Additionally, the Company enters into derivative agreements that are economic hedges which either do not qualify for hedge accounting or have not been designated as hedges. The changes in fair value of these undesignated derivative instruments are reflected in results of operations.

Embedded derivative instruments are separated from their host contracts and carried at fair value on the Consolidated Balance Sheets when: (a) the economic characteristics and risks of the embedded derivative are not clearly and closely related to the economic characteristics and risks of the host contract; (b) the hybrid instrument is not measured at fair value, with changes in fair value recognized in results of operations each period; and (c) the embedded derivative itself meets the definition of a derivative. The Company does not engage in derivative trading or speculative activities and had no embedded derivatives at December 31, 2015 or 2014.

Hydro One periodically develops hedging strategies taking into account risk management objectives. At the inception of a hedging relationship where the Company has elected to apply hedge accounting, Hydro One formally documents the relationship between the hedged item and the hedging instrument, the related risk management objective, the nature of the specific risk exposure being hedged, and the method for assessing the effectiveness of the hedging relationship. The Company also assesses, both at the inception of the hedge and on a quarterly basis, whether the hedging instruments are effective in offsetting changes in fair values or cash flows of the hedged items.

Employee Future Benefits

Employee future benefits provided by Hydro One include pension, post-retirement and post-employment benefits. The costs of the Company's pension, post-retirement and post-employment benefit plans are recorded over the periods during which employees render service.

The Company recognizes the funded status of its defined benefit pension, post-retirement and post-employment plans on its Consolidated Balance Sheets and subsequently recognizes the changes in funded status at the end of each reporting year. Defined benefit pension, post-retirement and post-employment plans are considered to be underfunded when the projected benefit obligation exceeds the fair value of the plan assets. Liabilities are recognized on the Consolidated Balance Sheets for

any net underfunded projected benefit obligation. The net underfunded projected benefit obligation may be disclosed as a current liability, long-term liability, or both. The current portion is the amount by which the actuarial present value of benefits included in the benefit obligation payable in the next 12 months exceeds the fair value of plan assets. If the fair value of plan assets exceeds the projected benefit obligation of the plan, an asset is recognized equal to the net overfunded projected benefit obligation. The post-retirement and post-employment benefit plans are unfunded because there are no related plan assets.

Pension benefits

Pension costs are recorded on an accrual basis for financial reporting purposes. Pension costs are actuarially determined using the projected benefit method prorated on service and are based on assumptions that reflect management's best estimate of the effect of future events, including future compensation increases. Past service costs from plan amendments and all actuarial gains and losses are amortized on a straight-line basis over the expected average remaining service period of active employees in the plan, and over the estimated remaining life expectancy of inactive employees in the plan. Pension plan assets, consisting primarily of listed equity securities as well as corporate and government debt securities, are fair valued at the end of each year. Hydro One records a regulatory asset equal to the net underfunded projected benefit obligation for its pension plan.

Post-retirement and post-employment benefits

Post-retirement and post-employment benefits are recorded and included in rates on an accrual basis. Costs are determined by independent actuaries using the projected benefit method prorated on service and based on assumptions that reflect management's best estimates. Past service costs from plan amendments are amortized to results of operations based on the expected average remaining service period. Hydro One records a regulatory asset equal to the incremental net unfunded projected benefit obligation for post-retirement and post-employment plans recorded at each year end based on annual actuarial reports.

For post-retirement benefits, all actuarial gains or losses are deferred using the "corridor" approach. The amount calculated above the "corridor" is amortized to results of operations on a straight-line basis over the expected average remaining service life of active employees in the plan and over the remaining life expectancy of inactive employees in the plan. The post-retirement benefit obligation is remeasured to its fair value at each year end based on an annual actuarial report, with an offset to the associated regulatory asset, to the extent of the remeasurement adjustment.

For post-employment obligations, the associated regulatory liabilities representing actuarial gains on transition to US GAAP are amortized to results of operations based on the "corridor" approach. Post transition, the actuarial gains and losses on post-employment obligations that are incurred during the year are recognized immediately to results of operations. The post-employment benefit obligation is remeasured to its fair value at each year end based on an annual actuarial report, with an offset to the associated regulatory asset, to the extent of the remeasurement adjustment.

All post-retirement and post-employment future benefit costs are attributed to labour and are either charged to results of operations or capitalized as part of the cost of property, plant and equipment and intangible assets.

Multiemployer Pension Plan

Former employees of Haldimand Hydro and Woodstock Hydro participate in the Ontario Municipal Employees Retirement System Fund (OMERS Plan), a multiemployer, contributory, defined benefit public sector pension fund. Former employees of Norfolk Power Inc. (Norfolk Power) ceased to contribute to the OMERS Plan upon integration of Norfolk Power into Hydro One Networks in September 2015. These employees are now included in Hydro One's defined benefit pension plan. OMERS Plan provides retirement pension payments based on members' length of service and salary. Both the participating employers and members are required to make plan contributions. The OMERS Plan assets are pooled together to provide benefits to all plan participants and the plan assets are not segregated by member entity. The OMERS Plan is registered with the Financial Services Commission of Ontario under Registration #0345983.

The OMERS Plan is accounted for as a defined contribution plan by Hydro One because it is not practicable to determine the present value of the Company's obligation, the fair value of plan assets or the related current service cost applicable to employees of Haldimand Hydro and Woodstock Hydro. Hydro One recognizes its contributions to the OMERS Plan as pension expense, with a portion being capitalized. The expensed amount is included in operation, maintenance and administration costs in the Consolidated Statements of Operations and Comprehensive Income.

Stock-Based Compensation

Hydro One measures share grant plans based on fair value of share grants as estimated based on the grant date Hydro One Limited share price. The costs are recognized in the financial statements using the graded-vesting attribution method for share grant plans that have both a performance condition and a service condition. The Company records a regulatory asset equal to the accrued costs of share grant plans recognized in each period, as management considers it to be probable that such costs will be recovered in the future through the rate-setting process.

The Company also records the liabilities associated with its Directors' Deferred Share Unit (DSU) Plan at fair value at each reporting date until settlement, recognizing compensation expense over the vesting period on a straight-line basis. The fair value of the DSU liability is based on Hydro One Limited's common share closing price at the end of each reporting period.

Loss Contingencies

Hydro One is involved in certain legal and environmental matters that arise in the normal course of business. In the preparation of its Consolidated Financial Statements, management makes judgments regarding the future outcome of contingent events and records a loss for a contingency based on its best estimate when it is determined that such loss is probable and the amount of the loss can be reasonably estimated. Where the loss amount is recoverable in future rates, a regulatory asset is also recorded. When a range estimate for the probable loss exists and no amount within the range is a better estimate than any other amount, the Company records a loss at the minimum amount within the range.

Management regularly reviews current information available to determine whether recorded provisions should be adjusted and whether new provisions are required. Estimating probable losses may require analysis of multiple forecasts and scenarios that often depend on judgments about potential actions by third parties, such as federal, provincial and local courts or regulators. Contingent liabilities are often resolved over long periods of time. Amounts recorded in the Consolidated Financial Statements may differ from the actual outcome once the contingency is resolved. Such differences could have a material impact on future results of operations, financial position and cash flows of the Company.

Provisions are based upon current estimates and are subject to greater uncertainty where the projection period is lengthy. A significant upward or downward trend in the number of claims filed, the nature of the alleged injuries, and the average cost of resolving each claim could change the estimated provision, as could any substantial adverse or favourable verdict at trial. A federal or provincial legislative outcome or structured settlement could also change the estimated liability. Legal fees are expensed as incurred.

Environmental Liabilities

Environmental liabilities are recorded in respect of past contamination when it is determined that future environmental remediation expenditures are probable under existing statute or regulation and the amount of the future expenditures can be reasonably estimated. Hydro One records a liability for the estimated future expenditures associated with contaminated land assessment and remediation and for the phase-out and destruction of polychlorinated biphenyl (PCB)-contaminated mineral oil removed from electrical equipment, based on the present value of these estimated future expenditures. The Company determines the present value with a discount rate equal to its credit-adjusted risk-free interest rate on financial instruments with comparable maturities to the pattern of future environmental expenditures. As the Company anticipates that the future expenditures will continue to be recoverable in future rates, an offsetting regulatory asset has been recorded to reflect the future recovery of these environmental expenditures from customers. Hydro One reviews its estimates of future environmental expenditures annually, or more frequently if there are indications that circumstances have changed.

Asset Retirement Obligations

Asset retirement obligations are recorded for legal obligations associated with the future removal and disposal of long-lived assets. Such obligations may result from the acquisition, construction, development and/or normal use of the asset. Conditional asset retirement obligations are recorded when there is a legal obligation to perform a future asset retirement activity but where the timing and/or method of settlement are conditional on a future event that may or may not be within the control of the Company. In such a case, the obligation to perform the asset retirement activity is unconditional even though uncertainty exists about the timing and/or method of settlement.

When recording an asset retirement obligation, the present value of the estimated future expenditures required to complete the asset retirement activity is recorded in the period in which the obligation is incurred, if a reasonable estimate can be made. In general, the present value of the estimated future expenditures is added to the carrying amount of the associated asset and

the resulting asset retirement cost is depreciated over the estimated useful life of the asset. Where an asset is no longer in service when an asset retirement obligation is recorded, the asset retirement cost is recorded in results of operations.

Some of the Company's transmission and distribution assets, particularly those located on unowned easements and rights-of-way, may have asset retirement obligations, conditional or otherwise. The majority of the Company's easements and rights-of-way are either of perpetual duration or are automatically renewed annually. Land rights with finite terms are generally subject to extension or renewal. As the Company expects to use the majority of its facilities in perpetuity, no asset retirement obligations currently exist for these assets. If, at some future date, a particular facility is shown not to meet the perpetuity assumption, it will be reviewed to determine whether an estimable asset retirement obligation exists. In such a case, an asset retirement obligation would be recorded at that time.

The Company's asset retirement obligations recorded to date relate to estimated future expenditures associated with the removal and disposal of asbestos-containing materials installed in some of its facilities and with the decommissioning of specific switching stations located on unowned sites.

3. NEW ACCOUNTING PRONOUNCEMENTS

Recent Accounting Guidance Not Yet Adopted

In January 2015, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2015-01, Income Statement – Extraordinary and Unusual Items (Subtopic 225-20): Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Items. This ASU eliminates the requirements for reporting entities to consider whether an underlying event or transaction is extraordinary and to show the item separately in the income statement. This ASU is effective for fiscal years, and interim periods within these years, beginning after December 15, 2015. The adoption of this ASU is not anticipated to have an impact on the Company's consolidated financial statements.

In February 2015, the FASB issued ASU 2015-02, Consolidation (Topic 810): Amendments to the Consolidation Analysis. This ASU provides guidance about the analysis that a reporting entity must perform to determine whether it should consolidate certain types of legal entities. This ASU is effective for fiscal years, and interim periods within those years, beginning after December 15, 2015. The adoption of this ASU is not anticipated to have an impact on the Company's consolidated financial statements.

In April 2015, the FASB issued ASU 2015-03, Interest – Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs. This ASU requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability. The recognition and measurement guidance for debt issuance costs are not affected. This ASU is effective for fiscal years, and interim periods within those years, beginning after December 15, 2015. Upon adoption of this ASU in the first quarter of 2016, the Company's deferred debt issuance costs that are currently presented under other long-term assets will be reclassified as a deduction from the carrying amount of long-term debt.

In April 2015, the FASB issued ASU 2015-04, Compensation – Retirement Benefits (Topic 715): Practical Expedient for the Measurement Date of an Employer's Defined Benefit Obligation and Plan Assets. This ASU permits an entity with a fiscal year-end that does not coincide with a month-end and an entity that has a significant event in an interim period that calls for a remeasurement of defined benefit plan assets and obligations to measure the defined benefit plan assets and obligations using the month-end that is closest to the entity's fiscal year-end. This ASU is effective for fiscal years, and interim periods within these years, beginning after December 15, 2015. The adoption of this ASU is not anticipated to have an impact on the Company's consolidated financial statements.

In April 2015, the FASB issued ASU 2015-05, Intangibles – Goodwill and Other – Internal-Use Software (Subtopic 350-40): Customer's Accounting for Fees Paid in a Cloud Computing Arrangement. This ASU provides guidance to customers about whether a cloud computing arrangement includes a software license, as well as the related accounting for the arrangement. This ASU is effective for fiscal years, and interim periods within these years, beginning after December 15, 2015. The Company is currently assessing the impact of adoption of this ASU on its consolidated financial statements.

In August 2015, the FASB issued ASU 2015-14, Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date. This ASU defers by one year the effective date of ASU 2014-09, Revenue from Contracts with Customers (Topic 606) issued by the FASB in May 2014. ASU 2014-09 provides guidance on revenue recognition that depicts the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange

for those goods and services. The guidance in ASU 2014-09 is now effective for fiscal years, and interim periods within those years, beginning after December 15, 2017. The Company is currently assessing the impact of adoption of ASU 2014-09 on its consolidated financial statements.

In September 2015, the FASB issued ASU 2015-16, Business Combinations (Topic 805): Simplifying the Accounting for Measurement-Period Adjustments. The amendments in this ASU require that an acquirer recognize adjustments to provisional amounts that are identified during the measurement period of a business combination in the reporting period in which the adjustment amounts are determined. The amendments in this update require that the acquirer to present separately on the face of the income statement or disclose in the notes the portion of the amount recorded in current-period earnings by line item that would have been recorded in previous reporting periods if the adjustment to the provisional amounts had been recognized as of the acquisition date. This ASU is effective for fiscal years, and interim periods within those years, beginning after December 15, 2015. Upon adoption of this ASU in the first quarter of 2016, the Company will apply the guidance in this ASU to future measurement adjustments related to business combinations, as applicable.

In November 2015, the FASB issued ASU 2015-17, Income Taxes (Topic 740): Balance Sheet Classification of Deferred Taxes. The amendments in this ASU require that all deferred tax assets and liabilities be classified as noncurrent on the balance sheet. This ASU is effective for fiscal years, and interim periods within those years, beginning after December 15, 2016. Upon adoption of this ASU in the first quarter of 2017, the current portions of the Company's deferred income tax assets and liabilities will be reclassified as noncurrent assets and liabilities on the consolidated Balance Sheets.

In January 2016, the FASB issued ASU 2016-01, Financial Instruments – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities. This ASU requires equity investments to be measured at fair value with changes in fair value recognized in net income, and requires enhanced disclosures and presentation of financial assets and liabilities in the financial statements. This ASU also simplifies the impairment assessment of equity investments without readily determinable fair values by requiring a qualitative assessment to identify impairment. This ASU is effective for fiscal years, and interim periods within those years, beginning after December 15, 2017. The Company is currently assessing the impact of adoption of this ASU on its consolidated financial statements.

4. BUSINESS COMBINATIONS

Acquisition of Woodstock Hydro

On October 31, 2015, Hydro One acquired 100% of the common shares of Woodstock Hydro, an electricity distribution company located in southwestern Ontario. The total purchase price for Woodstock Hydro was approximately $32 million.

The following table summarizes the preliminary determination of the fair value of the assets acquired and liabilities assumed:

(millions of Canadian dollars)	
Cash and cash equivalents	3
Working capital	4
Property, plant and equipment	28
Intangible assets	1
Deferred income tax assets	2
Goodwill	17
Long-term debt	(17)
Other long-term liabilities	(2)
Post-retirement and post-employment benefit liability	(1)
Derivative instruments	(3)
	32

The preliminary determination of the fair value of assets acquired and liabilities assumed has been based upon management's preliminary estimates and certain assumptions with respect to the fair values of the assets acquired and liabilities assumed. Due to the timing of the transaction, the Company has not yet completed the final fair value measurements as at December 31, 2015. In addition, the purchase agreement provides for final purchase price adjustments based on agreed working capital and other balances at the acquisition date which have not yet been finalized. The Company will continue to review information and perform further analysis prior to finalizing the total purchase price and the fair values of the assets acquired and liabilities

assumed. The actual total purchase price and the fair values of the assets acquired and liabilities assumed may differ from the amounts above.

Goodwill of approximately $17 million arising from the Woodstock Hydro acquisition consists largely of the synergies and economies of scale expected from combining the operations of Hydro One and Woodstock Hydro. All of the goodwill was assigned to Hydro One's Distribution Business segment. Woodstock Hydro contributed revenues of $12 million and net income of $2 million to the Company's consolidated financial results for the year ended December 31, 2015. All costs related to the acquisition have been expensed through the Consolidated Statements of Operations and Comprehensive Income. Woodstock Hydro's financial information is not material to the Company's consolidated financial results for the year ended December 31, 2015 and therefore, has not been disclosed on a pro forma basis.

Hydro One Brampton Spin-off

On August 31, 2015, Hydro One completed the spin-off of its subsidiary, Hydro One Brampton. The spin-off was accounted as a non-monetary, nonreciprocal transfer with the Province, based on its carrying values at August 31, 2015. Transactions that immediately preceded the spin-off as well as the spin-off were as follows:

- Hydro One subscribed for 357 common shares of Hydro One Brampton for an aggregate subscription price of $53 million;
- Hydro One transferred to a company wholly owned by the Province all the issued and outstanding shares of Hydro One Brampton as a dividend-in-kind; and all of the long-term intercompany debt in aggregate principal amount of $193 million plus accrued interest of $3 million owed by Hydro One Brampton to Hydro One as a return of stated capital of $196 million on its common shares.

In connection with the Hydro One Brampton spin-off, the following assets and liabilities of Hydro One Brampton were transferred:

(millions of Canadian dollars)	
Working capital	33
Property, plant and equipment and intangibles (net)	360
Other long-term assets	6
Long-term liabilities	(205)

As a result of the spin-off, goodwill related to Hydro One Brampton of $60 million was eliminated from the Consolidated Balance Sheet.

Acquisition of Haldimand Hydro

On June 30, 2015, Hydro One acquired 100% of the common shares of Haldimand Hydro, an electricity distribution company located in southwestern Ontario. The final total purchase price for Haldimand Hydro was approximately $73 million.

The following table summarizes the determination of the fair value of the assets acquired and liabilities assumed:

(millions of Canadian dollars)	
Cash and cash equivalents	3
Working capital	5
Property, plant and equipment	52
Deferred income tax assets	1
Goodwill	33
Long-term debt	(18)
Regulatory liabilities	(3)
	73

The determination of the fair value of assets acquired and liabilities assumed has been based upon management's estimates and certain assumptions with respect to the fair values of the assets acquired and liabilities assumed.

Goodwill of approximately $33 million arising from the Haldimand Hydro acquisition consists largely of the synergies and economies of scale expected from combining the operations of Hydro One and Haldimand Hydro. All of the goodwill was assigned to Hydro One's Distribution Business segment. Haldimand Hydro contributed revenues of $32 million and net income

of $6 million to the Company's consolidated financial results for the year ended December 31, 2015. All costs related to the acquisition have been expensed through the Consolidated Statements of Operations and Comprehensive Income. Haldimand Hydro's financial information is not material to the Company's consolidated financial results for the year ended December 31, 2015 and therefore, has not been disclosed on a pro forma basis.

Acquisition of Norfolk Power

On August 29, 2014, Hydro One acquired 100% of the common shares of Norfolk Power, an electricity distribution and telecom company located in southwestern Ontario. Norfolk Power was a holding company for two subsidiaries, Norfolk Power Distribution Inc. (NPDI) and Norfolk Energy Inc. The total purchase price for Norfolk Power, net of the long-term debt assumed, was approximately $68 million. The purchase price was finalized in 2015, with no adjustments to the preliminary purchase price allocation as disclosed at December 31, 2014.

The following table summarizes the determination of the fair value of the assets acquired and liabilities assumed:

(millions of Canadian dollars)	
Working capital	6
Property, plant and equipment	56
Deferred income tax assets	1
Goodwill	40
Bank indebtedness	(3)
Derivative instruments	(3)
Long-term debt	(26)
Post-retirement and post-employment benefit liability	(1)
Environmental liability	(1)
Long-term accounts payable and other liabilities	(1)
	68

The determination of the fair values of assets acquired and liabilities assumed has been based upon management's estimates and certain assumptions with respect to the fair values of the assets acquired and liabilities assumed.

Goodwill of approximately $40 million arising from the Norfolk Power acquisition consists largely of the synergies and economies of scale expected from combining the operations of Hydro One and Norfolk Power. All of the goodwill was assigned to Hydro One's Distribution Business segment. Norfolk Power contributed revenues of $18 million and net income of less than $1 million to the Company's consolidated financial results for the year ended December 31, 2014. All costs related to the acquisition have been expensed through the Consolidated Statements of Operations and Comprehensive Income. Norfolk Power's financial information was not material to the Company's consolidated financial results for the year ended December 31, 2014 and therefore, has not been disclosed on a pro forma basis.

Other

On November 6, 2015, Hydro One completed the spin-off of its subsidiary, Hydro One Telecom. The spin-off was accounted as a non-monetary, nonreciprocal transfer with Hydro One Limited, based on its carrying values at November 6, 2015. Hydro One transferred to Hydro One Limited all the issued and outstanding shares of Hydro One Telecom totalling $17 million, and all of the intercompany debt receivable held by Hydro One due from Hydro One Telecom and Hydro One Telecom Link Limited totalling $21 million, as a return of stated capital of $38 million on its common shares.

On November 6, 2015, Hydro One completed the spin-off of its subsidiary, MBSI. The spin-off was accounted as a non-monetary, nonreciprocal transfer with Hydro One Limited, based on its carrying values at November 6, 2015. Hydro One transferred to Hydro One Limited all the issued and outstanding shares of MBSI and all of the intercompany debt receivable held by Hydro One due from MBSI, as a return of stated capital of $3 million on its common shares.

5. DEPRECIATION AND AMORTIZATION

Year ended December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Depreciation of property, plant and equipment	594	565
Amortization of intangible assets	54	53
Asset removal costs	90	81
Amortization of regulatory assets	19	23
	757	722

6. FINANCING CHARGES

Year ended December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Interest on long-term debt	417	432
Other	16	12
Less: Interest capitalized on construction and development in progress	(52)	(49)
Gain on interest-rate swap agreements	(2)	(10)
Interest earned on investments	(3)	(6)
	376	379

7. INCOME TAXES

Income taxes / provision for PILs differs from the amount that would have been recorded using the combined Canadian federal and Ontario statutory income tax rate. The reconciliation between the statutory and the effective tax rates is provided as follows:

Year ended December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Income taxes / provision for PILs at statutory rate	216	222
Increase (decrease) resulting from:		
Net temporary differences included in amounts charged to customers:		
Capital cost allowance in excess of depreciation and amortization	(37)	(72)
Pension contributions in excess of pension expense	(25)	(24)
Overheads capitalized for accounting but deducted for tax purposes	(15)	(15)
Interest capitalized for accounting but deducted for tax purposes	(13)	(13)
Environmental expenditures	(5)	(5)
Non-refundable investment tax credits	(2)	(3)
Post-retirement and post-employment benefit expense in excess of cash payments	(1)	3
Prior year's adjustments	(1)	(4)
Other	(2)	(1)
Net temporary differences	(101)	(134)
Net tax benefit resulting from transition from PILs Regime to Federal Tax Regime	(9)	–
Hydro One Brampton spin-off	7	–
Net permanent differences	1	1
Total income taxes / provision for PILs	114	89

The major components of income tax expense are as follows:

Year ended December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Current income taxes / provision for PILs	2,931	79
Deferred income taxes / provision for (recovery of) PILs	(2,817)	10
Total income taxes / provision for PILs	114	89
Effective income tax rate	13.97%	10.63%

The provision for PILs / current income taxes is remitted to, or received from, the OEFC (PILs Regime) and the CRA (Federal Tax Regime). At December 31, 2015, $12 million (2014 – $39 million) due from the OEFC was included in due from related parties and $1 million (2014 – $nil) due from the CRA was included in prepaid expenses and other assets on the Consolidated Balance Sheet.

In connection with the IPO, Hydro One's exemption from tax under the Federal Tax Regime ceased to apply. Under the PILs Regime, Hydro One was deemed to have disposed of its assets immediately before it lost its tax exempt status under the Federal Tax Regime, resulting in Hydro One making payments in lieu of tax (Departure Tax) totalling $2.6 billion. To enable Hydro One to make the Departure Tax payment, Hydro One Limited subscribed for 39,598 common shares of Hydro One for $2.6 billion. Hydro One used the proceeds of this share subscription to pay the Departure Tax.

At December 31, 2015, the total income taxes / provision for PILs includes deferred income taxes / recovery of PILs of $2,817 million (2014 – deferred provision of $10 million), including $2,798 million (2014 – $nil) resulting from transition from the PILs Regime to the Federal Tax Regime, that is not included in the rate-setting process, using the liability method of accounting. Deferred income taxes / PILs balances expected to be included in the rate-setting process are offset by regulatory assets and liabilities to reflect the anticipated recovery or disposition of these balances within future electricity rates.

Deferred Income Tax Assets and Liabilities

Deferred income tax assets and liabilities arise from differences between the carrying amounts and tax basis of the Company's assets and liabilities. At December 31, 2015 and 2014, deferred income tax assets and liabilities consisted of the following:

December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Deferred income tax assets		
Depreciation and amortization in excess of capital cost allowance	918	(4)
Post-retirement and post-employment benefits expense in excess of cash payments	572	8
Environmental expenditures	75	4
Non-capital losses	62	–
Other	2	(1)
Total deferred income tax assets	1,629	7
Less: current portion	19	–
	1,610	7

December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Deferred income tax liabilities		
Regulatory amounts that are not recognized for tax purposes	(153)	(140)
Partnership interest	(41)	(38)
Goodwill	(10)	(21)
Capital cost allowance in excess of depreciation and amortization	(1)	(1,713)
Post-retirement and post-employment benefits expense in excess of cash payments	−	559
Environmental expenditures	−	59
Other	(1)	–
Total deferred income tax liabilities	(206)	(1,294)
Less: current portion	−	19
	(206)	(1,313)

During 2015 and 2014, there were no changes in the rate applicable to future taxes. The Company has recorded a valuation allowance in the amount of $278 million (2014 – $nil) in respect of non-depreciable capital property.

8. ACCOUNTS RECEIVABLE

December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Accounts receivable – billed	374	496
Accounts receivable – unbilled	459	586
Accounts receivable, gross	833	1,082
Allowance for doubtful accounts	(61)	(66)
Accounts receivable, net	772	1,016

In 2015, the Company revised the method to estimate the unbilled accounts receivable by using new technology that improved the estimation process. This change has been accounted for on a prospective basis in the consolidated financial statements at December 31, 2015. At December 31, 2015, the change in estimation technology resulted in a reduction in unbilled accounts receivable of approximately $121 million, with a corresponding offset to various components of the retail settlement variance accounts (RSVA). The change in estimate had no significant impact on 2015 net income.

The following table shows the movements in the allowance for doubtful accounts for the years ended December 31, 2015 and 2014:

Year ended December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Allowance for doubtful accounts – January 1	(66)	(36)
Write-offs	37	24
Additions to allowance for doubtful accounts	(32)	(54)
Allowance for doubtful accounts – December 31	(61)	(66)

9. PROPERTY, PLANT AND EQUIPMENT

December 31, 2015 *(millions of Canadian dollars)*	**Property, Plant and Equipment**	**Accumulated Depreciation**	**Construction in Progress**	**Total**
Transmission	13,803	4,625	853	10,031
Distribution	9,205	3,177	238	6,266
Communication	1,006	609	18	415
Administration and service	1,531	848	35	718
Easements	523	60	–	463
	26,068	9,319	1,144	17,893

December 31, 2014 *(millions of Canadian dollars)*	**Property, Plant and Equipment**	**Accumulated Depreciation**	**Construction in Progress**	**Total**
Transmission	13,209	4,416	626	9,419
Distribution	9,076	3,225	320	6,171
Communication	1,100	615	56	541
Administration and service	1,502	793	23	732
Easements	623	85	–	538
	25,510	9,134	1,025	17,401

Financing charges capitalized on property, plant and equipment under construction were $50 million in 2015 (2014 – $48 million).

10. INTANGIBLE ASSETS

December 31, 2015 *(millions of Canadian dollars)*	**Intangible Assets**	**Accumulated Amortization**	**Development in Progress**	**Total**
Computer applications software	579	270	24	333
Other	7	4	–	3
	586	274	24	336

December 31, 2014 *(millions of Canadian dollars)*	**Intangible Assets**	**Accumulated Amortization**	**Development in Progress**	**Total**
Computer applications software	573	303	3	273
Other	5	2	–	3
	578	305	3	276

Financing charges capitalized to intangible assets under development were $1 million in 2015 (2014 – $1 million). The estimated annual amortization expense for intangible assets is as follows: 2016 – $57 million; 2017 – $57 million; 2018 – $57 million; 2019 – $47 million; and 2020 – $30 million.

11. REGULATORY ASSETS AND LIABILITIES

Regulatory assets and liabilities arise as a result of the rate-setting process. Hydro One has recorded the following regulatory assets and liabilities:

December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Regulatory assets:		
Deferred income tax regulatory asset	1,445	1,327
Pension benefit regulatory asset	952	1,236
Post-retirement and post-employment benefits	240	273
Environmental	207	239
RSVA	110	11
Pension cost variance	37	90
2015-2017 rate rider	20	–
DSC exemption	10	16
Share-based compensation	10	–
B2M LP start-up costs	8	–
OEB cost assessment differential	–	12
Other	12	27
Total regulatory assets	3,051	3,231
Less: current portion	36	31
	3,015	3,200
Regulatory liabilities:		
External revenue variance	87	54
Green Energy expenditure variance	76	83
CDM deferral variance	53	25
Deferred income tax regulatory liability	23	21
PST savings deferral	4	19
Other	12	13
Total regulatory liabilities	255	215
Less: current portion	19	47
	236	168

Deferred Income Tax Regulatory Asset and Liability

Deferred income taxes are recognized on temporary differences between the carrying amount of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable income. The Company has recognized regulatory assets and liabilities that correspond to deferred income taxes that flow through the rate-setting process. In the absence of rate-regulated accounting, the Company's income tax expense would have been recognized using the liability method and there would be no regulatory accounts established for taxes to be recovered through future rates. As a result, the 2015 income tax expense would have been higher by approximately $101 million (2014 – $132 million).

Pension Benefit Regulatory Asset

In accordance with OEB rate orders, pension costs are recorded on a cash basis as employer contributions are paid to the pension fund in accordance with the *Pension Benefits Act* (Ontario). The Company recognizes the net unfunded status of pension obligations on the Consolidated Balance Sheets with an offset to the associated regulatory asset. A regulatory asset is recognized because management considers it to be probable that pension benefit costs will be recovered in the future through the rate-setting process. The pension benefit obligation is remeasured to its fair value at each year end based on an annual actuarial report, with an offset to the associated regulatory asset, to the extent of the remeasurement adjustment. In the absence of rate-regulated accounting, 2015 OCI would have been higher by $284 million (2014 – lower by $391 million).

Post-Retirement and Post-Employment Benefits

The Company recognizes the net unfunded status of post-retirement and post-employment obligations on the Consolidated Balance Sheets with an incremental offset to the associated regulatory assets. A regulatory asset is recognized because management considers it to be probable that post-retirement and post-employment benefit costs will be recovered in the future through the rate-setting process. The post-retirement and post-employment benefit obligation is remeasured to its fair value at each year end based on an annual actuarial report, with an offset to the associated regulatory asset, to the extent of the remeasurement adjustment. In the absence of rate-regulated accounting, 2015 OCI would have been higher by $33 million (2014 – $35 million).

Environmental

Hydro One records a liability for the estimated future expenditures required to remediate environmental contamination. Because such expenditures are expected to be recoverable in future rates, the Company has recorded an equivalent amount as a regulatory asset. In 2015, the environmental regulatory asset decreased by $24 million (2014 – $33 million) to reflect related changes in the Company's PCB liability, and increased by $1 million (2014 – $13 million) due to changes in the land assessment and remediation liability. The environmental regulatory asset is amortized to results of operations based on the pattern of actual expenditures incurred and charged to environmental liabilities. The OEB has the discretion to examine and assess the prudency and the timing of recovery of all of Hydro One's actual environmental expenditures. In the absence of rate-regulated accounting, 2015 operation, maintenance and administration expenses would have been lower by $23 million (2014 – $20 million). In addition, 2015 amortization expense would have been lower by $19 million (2014 – $18 million), and 2015 financing charges would have been higher by $10 million (2014 – $11 million).

RSVA

Hydro One has deferred certain retail settlement variance amounts under the provisions of Article 490 of the OEB's Accounting Procedures Handbook. In March 2015, the OEB approved the disposition of the total RSVA balance accumulated from January 2012 to December 2013, including accrued interest, to be recovered through the 2015-2017 Rate Rider. In 2015, the Company revised its method to estimate the unbilled accounts receivable based on new technology implemented to improve the accuracy of the estimation process. At December 31, 2015, the change in estimate reduced unbilled accounts receivable by approximately $121 million, with a corresponding offset to various components of RSVA. The change in estimate had no significant impact on 2015 net income.

Pension Cost Variance

A pension cost variance account was established for Hydro One Networks' transmission and distribution businesses to track the difference between the actual pension expenses incurred and estimated pension costs approved by the OEB. The balance in this regulatory account reflects the excess of pension costs paid as compared to OEB-approved amounts. In March 2015, the OEB approved the disposition of the distribution business portion of the total pension cost variance account at December

31, 2013, including accrued interest, which will be recovered through the 2015-2017 Rate Rider. In the absence of rate-regulated accounting, 2015 revenue would have been lower by $6 million (2014 – $10 million).

2015-2017 Rate Rider

In March 2015, as part of its decision on Hydro One Networks' Distribution rate application for 2015-2019 the OEB approved the disposition of certain deferral and variance accounts, including RSVAs and accrued interest. The 2015-2017 Rate Rider account includes the balances approved for disposition by the OEB and will be disposed over a 32-month period in accordance with the OEB decision.

DSC Exemption

In June 2010, Hydro One Networks filed an application with the OEB regarding the OEB's new cost responsibility rules contained in the OEB's October 2009 Notice of Amendment to the Distribution System Code (DSC), with respect to the connection of certain renewable generators that were already connected or that had received a connection impact assessment prior to October 21, 2009. The application sought approval to record and defer the unanticipated costs incurred by Hydro One Networks that resulted from the connection of certain renewable generation facilities. The OEB ruled that identified specific expenditures can be recorded in a deferral account subject to the OEB's review in subsequent Hydro One Network distribution applications. In March 2015, the OEB approved the disposition of the DSC exemption deferral account at December 31, 2013, including accrued interest, which will be recovered through the 2015-2017 Rate Rider. In addition, the OEB also approved Hydro One's request to discontinue this deferral account, and there were no additions to this regulatory account in 2015.

Share-based Compensation

The Company recognizes costs associated with stock-based compensation in a regulatory asset as management considers it probable that stock-based compensation costs will be recovered in the future through the rate-setting process. At December 31, 2015 the stock-based compensation costs relate to the share grant plans, are measured at fair value estimated based on grant date Hydro One Limited share price and recognized using the graded-vesting attribution method. In the absence of rate-regulated accounting 2015 operation, maintenance and administration expenses would have been higher by $5 million (2014 – $nil).

B2M LP Start-up Costs

In December 2015, OEB issued its decision on B2M LP's application for 2015-2019 and as part of the decision approved the recovery of $8 million of start-up costs relating to B2M LP. The costs will be recovered over a 4 year period beginning in 2016, in accordance with the OEB decision.

OEB Cost Assessment Differential

In April 2010, the OEB issued its Decision regarding Hydro One Networks' distribution rate application for 2010 and 2011. As part of this decision, the OEB also approved the distribution-related OEB Cost Assessment Differential Account to record the difference between the amounts approved in rates and actual expenditures with respect to the OEB's cost assessments. In March 2015, the OEB approved the disposition of the OEB Cost Assessment Differential Account at December 31, 2013, including accrued interest, which will be recovered through the 2015-2017 Rate Rider. In addition, the OEB also approved Hydro One's request to discontinue this deferral account, and there were no additions to this regulatory account in 2015.

External Revenue Variance

In May 2009, the OEB approved forecasted amounts related to export service revenue, external revenue from secondary land use, and external revenue from station maintenance and engineering and construction work. In November 2012, the OEB again approved forecasted amounts related to these revenue categories and extended the scope to encompass all other external revenues. The external revenue variance account balance reflects the excess of actual external revenues compared to the OEB-approved forecasted amounts.

Green Energy Expenditure Variance

In April 2010, the OEB requested the establishment of deferral accounts which capture the difference between the revenue recorded on the basis of Green Energy Plan expenditures incurred and the actual recoveries received.

CDM Deferral Variance Account

As part of Hydro One Networks' application for 2013 and 2014 transmission rates, Hydro One agreed to establish a new regulatory deferral variance account to track the impact of actual Conservation and Demand Management (CDM) and demand response results on the load forecast compared to the estimated load forecast included in the revenue requirement. At December 31, 2014, the balance in the CDM deferral variance account relates to the actual 2013 CDM compared to the amounts included in 2013 revenue requirement. At December 31, 2015, the balance also includes the difference between the actual 2014 CDM compared to the amounts included in 2014 revenue requirement. The OEB rate order specifically states that the IESO (Ontario Power Authority (OPA) prior to January 1, 2015) data used to calculate the difference between forecasted and actual savings will be provided one year in arrears, and as a result, no amount should be recorded in advance of notification from the IESO of actual results.

PST Savings Deferral Account

The provincial sales tax (PST) and goods and services tax (GST) were harmonized in July 2010. Unlike the GST, the PST was included in operation, maintenance and administration expenses or capital expenditures for past revenue requirements approved during a full cost-of-service hearing. Under the harmonized sales tax (HST) regime, the HST included in operation, maintenance and administration expenses or capital expenditures is not a cost ultimately borne by the Company and as such, a refund of the prior PST element in the approved revenue requirement is applicable, and calculations for tracking and refund were requested by the OEB. For Hydro One Networks' transmission revenue requirement, PST was included between July 1, 2010 and December 31, 2010 and recorded in a deferral account, per direction from the OEB. For Hydro One Networks' distribution revenue requirement, PST was included between July 1, 2010 and December 31, 2015 and recorded in a deferral account, as directed by the OEB. In March 2015, the OEB approved the disposition of the PST Savings Deferral account at December 31, 2013, including accrued interest, which will be recovered through the 2015-2017 Rate Rider.

12. DEBT AND CREDIT AGREEMENTS

Short-Term Notes and Credit Facilities

Hydro One meets its short-term liquidity requirements in part through the issuance of commercial paper under its Commercial Paper Program which has a maximum authorized amount of $1.5 billion. These short-term notes are denominated in Canadian dollars with varying maturities not exceeding 365 days. The Commercial Paper Program is supported by the Company's committed revolving credit facilities totalling $2.3 billion. At December 31, 2015, Hydro One had $1,491 million in commercial paper borrowings outstanding (December 31, 2014 – $nil).

At December 31, 2015, Hydro One's consolidated committed, unsecured and unused credit facilities totalling $2.3 billion consisted of the following:

(millions of Canadian dollars)	Maturity	Amount
Revolving standby credit facility	June 2020	1,500
Three-year senior, revolving term credit facility	October 2018	800
Total		2,300

The Company may use the credit facilities for working capital and general corporate purposes. If used, interest on the credit facilities would apply based on Canadian benchmark rates. The obligation of each lender to make any credit extension under its credit facility is subject to various conditions including, among other things, that no event of default has occurred or would result from such credit extension.

Long-Term Debt

The Company issues notes for long-term financing under its Medium-Term Note (MTN) Program. The maximum authorized principal amount of notes issuable under this program is $3.5 billion. At December 31, 2015, $3.5 billion remained available for issuance until January 2018.

The following table presents the outstanding long-term debt at December 31, 2015 and 2014:

December 31 *(millions of Canadian dollars)*	**2015**	**2014**
2.95% Series 21 notes due 2015[1]	–	500
Floating-rate Series 22 notes due 2015[2]	–	50
4.64% Series 10 notes due 2016	450	450
Floating-rate Series 27 notes due 2016[2]	50	50
5.18% Series 13 notes due 2017	600	600
2.78% Series 28 notes due 2018	750	750
Floating-rate Series 31 notes due 2019[2]	228	228
4.40% Series 20 notes due 2020	300	300
1.62% Series 33 notes due 2020[1]	350	–
3.20% Series 25 notes due 2022	600	600
7.35% Debentures due 2030	400	400
6.93% Series 2 notes due 2032	500	500
6.35% Series 4 notes due 2034	385	385
5.36% Series 9 notes due 2036	600	600
4.89% Series 12 notes due 2037	400	400
6.03% Series 17 notes due 2039	300	300
5.49% Series 18 notes due 2040	500	500
4.39% Series 23 notes due 2041	300	300
6.59% Series 5 notes due 2043	315	315
4.59% Series 29 notes due 2043	435	435
4.17% Series 32 notes due 2044	350	350
5.00% Series 11 notes due 2046	325	325
4.00% Series 24 notes due 2051	225	225
3.79% Series 26 notes due 2062	310	310
4.29% Series 30 notes due 2064	50	50
	8,723	8,923
Add: Unrealized mark-to-market loss[1]	1	2
Less: Long-term debt payable within one year	(500)	(552)
Long-term debt	8,224	8,373

[1] The unrealized mark-to-market loss relates to $50 million of the Series 33 notes due 2020 (2014 – $250 million of the Series 21 notes due 2015). The unrealized mark-to-market loss is offset by a $1 million (2014 – $2 million) unrealized mark-to-market gain on the related fixed-to-floating interest-rate swap agreements, which are accounted for as fair value hedges. See Note 13 – Fair Value of Financial Instruments and Risk Management for details of fair value hedges.

[2] The interest rates of the floating-rate notes are referenced to the 3-month Canadian dollar bankers' acceptance rate, plus a margin.

In 2015, Hydro One issued $350 million (2014 – $628 million) of long-term debt under the MTN Program, and repaid $550 million of long-term debt MTN Program notes (2014 – $750 million).

Long-term debt totalling $35 million assumed by Hydro One as part of the Haldimand Hydro and Woodstock Hydro acquisitions was repaid in 2015.

The long-term debt is unsecured and denominated in Canadian dollars. The long-term debt is summarized by the number of years to maturity in Note 13 – Fair Value of Financial Instruments and Risk Management.

13. FAIR VALUE OF FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

Fair value is considered to be the exchange price in an orderly transaction between market participants to sell an asset or transfer a liability at the measurement date. The fair value definition focuses on an exit price, which is the price that would be received in the sale of an asset or the amount that would be paid to transfer a liability.

Hydro One classifies its fair value measurements based on the following hierarchy, as prescribed by the accounting guidance for fair value, which prioritizes the inputs to valuation techniques used to measure fair value into three levels:

Level 1 inputs are unadjusted quoted prices in active markets for identical assets or liabilities that Hydro One has the ability to access. An active market for the asset or liability is one in which transactions for the asset or liability occur with sufficient frequency and volume to provide ongoing pricing information.

Level 2 inputs are those other than quoted market prices that are observable, either directly or indirectly, for an asset or liability. Level 2 inputs include, but are not limited to, quoted prices for similar assets or liabilities in an active market, quoted prices for identical or similar assets or liabilities in markets that are not active and inputs other than quoted market prices that are observable for the asset or liability, such as interest-rate curves and yield curves observable at commonly quoted intervals, volatilities, credit risk and default rates. A Level 2 measurement cannot have more than an insignificant portion of the valuation based on unobservable inputs.

Level 3 inputs are any fair value measurements that include unobservable inputs for the asset or liability for more than an insignificant portion of the valuation. A Level 3 measurement may be based primarily on Level 2 inputs.

Non-Derivative Financial Assets and Liabilities

At December 31, 2015 and 2014, the Company's carrying amounts of accounts receivable, due from related parties, cash and cash equivalents, bank indebtedness, short-term notes payable, accounts payable, and due to related parties are representative of fair value because of the short-term nature of these instruments.

Fair Value Measurements of Long-Term Debt

The fair values and carrying values of the Company's long-term debt at December 31, 2015 and 2014 are as follows:

December 31 *(millions of Canadian dollars)*	**2015 Carrying Value**	**2015 Fair Value**	**2014 Carrying Value**	**2014 Fair Value**
Long-term debt				
$250 million of MTN Series 21 notes[1]	–	–	252	252
$50 million of MTN Series 33 notes[1]	51	51	–	–
Other notes and debentures[2]	8,673	9,942	8,673	10,159
	8,724	9,993	8,925	10,411

[1] The fair value of the $50 million MTN Series 33 notes and $250 million of the MTN Series 21 notes subject to hedging is primarily based on changes in the present value of future cash flows due to a change in the yield in the swap market for the related swap (hedged risk).

[2] The fair value of other notes and debentures, and the portion of the MTN Series 21 notes that are not subject to hedging, represents the market value of the notes and debentures and is based on unadjusted period-end market prices for the same or similar debt of the same remaining maturities.

Fair Value Measurements of Derivative Instruments

At December 31, 2015, Hydro One had an interest-rate swap in the amount of $50 million (2014 – $250 million) that was used to convert fixed-rate debt to floating-rate debt. This swap is classified as a fair value hedge. Hydro One's fair value hedge exposure was equal to about 1% (2014 – 3%) of its total long-term debt of $8,724 million (2014 – $8,925 million). At December 31, 2015, Hydro One's interest-rate swap designated as a fair value hedge was as follows:

- a $50 million fixed-to-floating interest-rate swap agreement to convert $50 million of the $350 million MTN Series 33 notes maturing April 30, 2020 into three-month variable rate debt.

At December 31, 2015, the Company had no interest-rate swaps classified as undesignated contracts (2014 – $409 million).

As part of the Norfolk Power and Woodstock Hydro acquisitions, Hydro One assumed liabilities associated with unrealized losses on derivative instruments (interest-rate swaps) totalling $6 million. Hydro One extinguished the interest rate swaps and repaid these liabilities in 2015.

Fair Value Hierarchy

The fair value hierarchy of financial assets and liabilities at December 31, 2015 and 2014 is as follows:

December 31, 2015 *(millions of Canadian dollars)*	Carrying Value	Fair Value	Level 1	Level 2	Level 3
Assets:					
Cash and cash equivalents	89	89	89	–	–
Derivative instruments					
Fair value hedge – interest-rate swap	1	1	1	–	–
	90	90	90	–	–
Liabilities:					
Short-term notes payable	1,491	1,491	1,491	–	–
Long-term debt	8,724	9,993	–	9,993	–
	10,215	11,484	1,491	9,993	

December 31, 2014 *(millions of Canadian dollars)*	Carrying Value	Fair Value	Level 1	Level 2	Level 3
Assets:					
Cash and cash equivalents	100	100	100	–	–
Derivative instruments					
Fair value hedges – interest-rate swaps	2	2	–	2	–
	102	102	100	2	–
Liabilities:					
Bank indebtedness	2	2	2	–	–
Derivative instruments					
Undesignated contracts – interest-rate swaps	3	3	–	3	–
Long-term debt	8,925	10,411	–	10,411	–
	8,930	10,416	2	10,414	–

Cash and cash equivalents include cash and short-term investments. The carrying values are representative of fair value because of the short-term nature of these instruments.

The fair value of the derivative instruments is determined using inputs other than quoted prices that are observable for these assets. The fair value is primarily based on the present value of future cash flows using a swap yield curve to determine the assumptions for interest rates.

The fair value of the hedged portion of the long-term debt is primarily based on the present value of future cash flows using a swap yield curve to determine the assumption for interest rates. The fair value of the unhedged portion of the long-term debt is based on unadjusted period-end market prices for the same or similar debt of the same remaining maturities.

There were no significant transfers between any of the fair value levels during the years ended December 31, 2015 and 2014.

Risk Management

Exposure to market risk, credit risk and liquidity risk arises in the normal course of the Company's business.

Market Risk

Market risk refers primarily to the risk of loss that results from changes in costs, foreign exchange rates and interest rates. The Company is exposed to fluctuations in interest rates as its regulated return on equity is derived using a formulaic approach that takes into account anticipated interest rates, but is not currently exposed to material commodity price risk or material foreign exchange risk.

The OEB-approved adjustment formula for calculating return on equity in a deemed regulatory capital structure of 60% debt and 40% equity provides for increases and decreases depending on changes in benchmark rates of return for Government of Canada debt. The Company estimates that a 1% decrease in the forecasted long-term Government of Canada bond yield used in determining its rate of return would reduce the Company's transmission business' 2015 net income by approximately $20 million (2014 – $20 million) and its distribution business' 2015 net income by approximately $13 million (2014 – $10 million). The Company's net income is adversely impacted by rising interest rates as Hydro One's maturing long-term debt is refinanced at market rates. Hydro One periodically utilizes interest rate swap agreements to mitigate elements of interest rate risk.

Hydro One uses a combination of fixed and variable-rate debt to manage the mix of its debt portfolio. Hydro One also uses derivative financial instruments to manage interest-rate risk. Hydro One utilizes interest-rate swaps, which are typically designated as fair value hedges, as a means to manage its interest rate exposure to achieve a lower cost of debt. In addition, the Company may utilize interest-rate derivative instruments to lock in interest-rate levels in anticipation of future financing.

A hypothetical 10% increase in the interest rates associated with variable-rate debt would not have resulted in a significant decrease in Hydro One's net income for the years ended December 31, 2015 or 2014.

Fair Value Hedges

For derivative instruments that are designated and qualify as fair value hedges, the gain or loss on the derivative as well as the offsetting loss or gain on the hedged item attributable to the hedged risk are recognized in the Consolidated Statements of Operations and Comprehensive Income. The net unrealized loss (gain) on the hedged debt and the related interest-rate swaps for the years ended December 31, 2015 and 2014 are included in financing charges as follows:

Year ended December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Unrealized loss (gain) on hedged debt	(1)	(3)
Unrealized loss (gain) on fair value interest-rate swaps	1	3
Net unrealized loss (gain)	–	–

At December 31, 2015, Hydro One had $50 million (2014 – $250 million) of notional amounts of fair value hedges outstanding related to interest-rate swaps, with assets at fair value of $1 million (2014 – $2 million). During the years ended December 31, 2015 and 2014, there was no significant impact on the results of operations as a result of any ineffectiveness attributable to fair value hedges.

Credit Risk

Financial assets create a risk that a counterparty will fail to discharge an obligation, causing a financial loss. At December 31, 2015 and 2014, there were no significant concentrations of credit risk with respect to any class of financial assets. The Company's revenue is earned from a broad base of customers. As a result, Hydro One did not earn a significant amount of revenue from any single customer. At December 31, 2015 and 2014, there was no significant accounts receivable balance due from any single customer.

At December 31, 2015, the Company's provision for bad debts was $61 million (2014 – $66 million). Adjustments and write-offs were determined on the basis of a review of overdue accounts, taking into consideration historical experience. At December 31, 2015, approximately 6% (2014 – 6%) of the Company's net accounts receivable were aged more than 60 days.

Hydro One manages its counterparty credit risk through various techniques including: entering into transactions with highly-rated counterparties; limiting total exposure levels with individual counterparties consistent with the Company's Board-approved Credit Risk Policy; entering into master agreements which enable net settlement and the contractual right of offset; and monitoring the financial condition of counterparties. In addition to payment netting language in master agreements, the Company establishes credit limits, margining thresholds and collateral requirements for each counterparty. Counterparty credit limits are based on an internal credit review that considers a variety of factors, including the results of a scoring model, leverage, liquidity, profitability, credit ratings and risk management capabilities. The determination of credit exposure for a particular counterparty is the sum of current exposure plus the potential future exposure with that counterparty. The current exposure is calculated as the sum of the principal value of money market exposures and the market value of all contracts that have a positive mark-to-market position on the measurement date. The Company would offset the positive market values against negative values with the same counterparty only where permitted by the existence of a legal netting agreement such as an International Swap Dealers Association master agreement. The potential future exposure represents a safety margin to protect against future fluctuations of interest rates, currencies, equities, and commodities. It is calculated based on factors

developed by the Bank of International Settlements, following extensive historical analysis of random fluctuations of interest rates and currencies. To the extent that a counterparty's margining thresholds are exceeded, the counterparty is required to post collateral with the Company as specified in each agreement. The Company monitors current and forward credit exposure to counterparties both on an individual and an aggregate basis. The Company's credit risk for accounts receivable is limited to the carrying amounts on the Consolidated Balance Sheets.

Derivative financial instruments result in exposure to credit risk since there is a risk of counterparty default. The credit exposure of derivative contracts, before collateral, is represented by the fair value of contracts at the reporting date. At December 31, 2015, the counterparty credit risk exposure on the fair value of these interest-rate swap contracts was $1 million (2014 – $3 million). At December 31, 2015, Hydro One's credit exposure for all derivative instruments, and applicable payables and receivables, had a credit rating of investment grade, with one financial institution as the counterparty.

Liquidity Risk

Liquidity risk refers to the Company's ability to meet its financial obligations as they come due. Hydro One meets its short-term liquidity requirements using cash and cash equivalents on hand, funds from operations, the issuance of commercial paper, and the revolving standby facilities totaling $2.3 billion. The short-term liquidity under the Commercial Paper Program, and anticipated levels of funds from operations should be sufficient to fund normal operating requirements.

At December 31, 2015, accounts payable and accrued liabilities in the amount of $743 million (2014 – $784 million) were expected to be settled in cash at their carrying amounts within the next 12 months.

At December 31, 2015, Hydro One had long-term debt in the principal amount of $8,723 million (2014 – $8,923 million). Principal repayments and related weighted average interest rates are summarized by the number of years to maturity in the following table:

Years to Maturity	Long-term Debt Principal Repayments *(millions of Canadian dollars)*	Weighted Average Interest Rate *(%)*
1 year	500	4.3
2 years	600	5.2
3 years	750	2.8
4 years	228	1.2
5 years	650	2.9
	2,728	3.5
6 – 10 years	600	3.2
Over 10 years	5,395	5.4
	8,723	4.7

Interest payments on long-term debt are summarized by year in the following table:

Year	Interest Payments *(millions of Canadian dollars)*
2016	397
2017	386
2018	355
2019	332
2020	322
	1,792
2021-2025	1,496
2026 +	4,080
	7,368

14. CAPITAL MANAGEMENT

The Company's objectives with respect to its capital structure are to maintain effective access to capital on a long-term basis at reasonable rates, and to deliver appropriate financial returns. In order to ensure ongoing access to capital, the Company targets to maintain strong credit quality. The Company considers its capital structure to consist of shareholder's equity, preferred shares, long-term debt, short-term notes payable, and cash and cash equivalents. At December 31, 2015 and 2014, the Company's capital structure was as follows:

December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Long-term debt payable within one year	500	552
Short-term notes payable	1,491	–
Less: cash and cash equivalents	89	100
	1,902	452
Long-term debt	8,224	8,373
Preferred shares	–	323
Common shares	6,000	3,314
Retained earnings	3,759	4,249
	9,759	7,563
Total capital	19,885	16,711

The Company has customary covenants typically associated with long-term debt. Among other things, Hydro One's long-term debt and credit facility covenants limit the permissible debt to 75% of its total capitalization, limit the ability to sell assets and impose a negative pledge provision, subject to customary exceptions. At December 31, 2015 and 2014, Hydro One was in compliance with all of these covenants and limitations.

15. PENSION AND POST-RETIREMENT AND POST-EMPLOYMENT BENEFITS

Hydro One has a defined benefit pension plan, a supplementary pension plan, and post-retirement and post-employment benefit plans. The defined benefit pension plan (Pension Plan) is contributory and covers all regular employees of Hydro One and its subsidiaries, except employees of Haldimand Hydro and Woodstock Hydro. Employees of Haldimand Hydro and Woodstock Hydro participate in the OMERS Plan. The supplementary pension plan provides members of the Pension Plan with benefits that would have been earned and payable under the Pension Plan but for limitations imposed by the *Income Tax Act* (Canada). The supplementary pension plan obligation is included with other post-retirement and post-employment benefit obligations on the Consolidated Balance Sheets.

The OMERS Plan

Hydro One contributions to the OMERS Plan for the year ended December 31, 2015 were $2 million (2014 – $2 million). At December 31, 2015, Company contributions payable included in accrued liabilities on the Consolidated Balance Sheets were less than $1 million (2014 – less than $1 million). Hydro One contributions do not represent more than 5% of total contributions to the OMERS Plan, as indicated in OMERS' most recently available annual report for the year ended December 31, 2014.

At December 31, 2014, the OMERS Plan was 90.8% funded, with an unfunded liability of $7.1 billion. This unfunded liability could result in future payments by participating employers and members. Hydro One future contributions could be increased substantially if other entities withdraw from the plan.

Pension Plan, Post-Retirement and Post-Employment Plans

The Pension Plan provides benefits based on highest three-year average pensionable earnings. For new management employees who commenced employment on or after January 1, 2004, and for new Society of Energy Professionals-represented staff hired after November 17, 2005, benefits are based on highest five-year average pensionable earnings. After retirement, pensions are indexed to inflation.

Company and employee contributions to the Pension Plan are based on actuarial valuations performed at least every three years. Annual Pension Plan contributions for 2015 of $177 million (2014 – $174 million) were based on an actuarial valuation effective December 31, 2013 and the expected level of pensionable earnings. Estimated annual Pension Plan contributions for 2016 are approximately $180 million, based on the actuarial valuation as at December 31, 2013 and projected levels of pensionable earnings. Future minimum contributions beyond 2016 will be based on an actuarial valuation effective no later than December 31, 2016. Contributions are payable one month in arrears. All of the contributions are expected to be in the form of cash.

Hydro One recognizes the overfunded or underfunded status of the Pension Plan, and post-retirement and post-employment benefit plans (Plans) as an asset or liability on its Consolidated Balance Sheets, with offsetting regulatory assets and liabilities as appropriate. The underfunded benefit obligations for the Plans, in the absence of regulatory accounting, would be recognized in AOCI. The impact of changes in assumptions used to measure pension, post-retirement and post-employment benefit obligations is generally recognized over the expected average remaining service period of the employees. The measurement date for the Plans is December 31.

Year ended December 31 *(millions of Canadian dollars)*	Pension Benefits		Post-Retirement and Post-Employment Benefits	
	2015	2014	2015	2014
Change in projected benefit obligation				
Projected benefit obligation, beginning of year	7,535	6,576	1,582	1,531
Current service cost	186	145	43	41
Interest cost	302	312	64	73
Benefits paid	(334)	(319)	(47)	(45)
Net actuarial loss (gain)	(6)	821	(27)	(18)
Change due to Hydro One Brampton spin-off	–	–	(5)	–
Change due to Hydro One Telecom spin-off	–	–	(19)	–
Projected benefit obligation, end of year	7,683	7,535	1,591	1,582
Change in plan assets				
Fair value of plan assets, beginning of year	6,299	5,731	–	–
Actual return on plan assets	582	703	–	–
Benefits paid	(334)	(319)	–	–
Employer contributions	177	174	–	–
Employee contributions	40	35	–	–
Administrative expenses	(33)	(25)	–	–
Fair value of plan assets, end of year	6,731	6,299	–	–
Unfunded status	952	1,236	1,591	1,582

Hydro One presents its benefit obligations and plan assets net on its Consolidated Balance Sheets within the following line items:

December 31 *(millions of Canadian dollars)*	Pension Benefits		Post-Retirement and Post-Employment Benefits	
	2015	2014	2015	2014
Accrued liabilities	–	–	50	49
Pension benefit liability	952	1,236	–	–
Post-retirement and post-employment benefit liability	–	–	1,541	1,533
Unfunded status	952	1,236	1,591	1,582

The funded or unfunded status of the pension, post-retirement and post-employment benefit plans refers to the difference between the fair value of plan assets and the projected benefit obligations for the Plans. The funded/unfunded status changes over time due to several factors, including contribution levels, assumed discount rates and actual returns on plan assets.

The following table provides the projected benefit obligation (PBO), accumulated benefit obligation (ABO) and fair value of plan assets for the Pension Plan:

December 31 *(millions of Canadian dollars)*	**2015**	**2014**
PBO	7,683	7,535
ABO	7,020	6,887
Fair value of plan assets	6,731	6,299

On an ABO basis, the Pension Plan was funded at 96% at December 31, 2015 (2014 – 91%). On a PBO basis, the Pension Plan was funded at 88% at December 31, 2015 (2014 – 84%). The ABO differs from the PBO in that the ABO includes no assumption about future compensation levels.

Components of Net Periodic Benefit Costs

The following table provides the components of the net periodic benefit costs for the years ended December 31, 2015 and 2014 for the Pension Plan:

Year ended December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Current service cost, net of employee contributions	146	110
Interest cost	302	312
Expected return on plan assets, net of expenses	(406)	(369)
Actuarial loss amortization	119	103
Prior service cost amortization	2	2
Net periodic benefit costs	163	158
Charged to results of operations[1]	81	81

[1] The Company follows the cash basis of accounting consistent with the inclusion of pension costs in OEB-approved rates. During the year ended December 31, 2015, pension costs of $177 million (2014 – $174 million) were attributed to labour, of which $81 million (2014 – $81 million) was charged to operations, and $96 million (2014 – $93 million) was capitalized as part of the cost of property, plant and equipment and intangible assets.

The following table provides the components of the net periodic benefit costs for the years ended December 31, 2015 and 2014 for the post-retirement and post-employment benefit plans:

Year ended December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Current service cost, net of employee contributions	43	41
Interest cost	64	73
Actuarial loss amortization	14	18
Prior service cost amortization	–	2
Net periodic benefit costs	121	134
Charged to results of operations	55	62

Assumptions

The measurement of the obligations of the Plans and the costs of providing benefits under the Plans involves various factors, including the development of valuation assumptions and accounting policy elections. When developing the required assumptions, the Company considers historical information as well as future expectations. The measurement of benefit obligations and costs is impacted by several assumptions including the discount rate applied to benefit obligations, the long-term expected rate of return on plan assets, Hydro One's expected level of contributions to the Plans, the incidence of mortality, the expected remaining service period of plan participants, the level of compensation and rate of compensation increases, employee age, length of service, and the anticipated rate of increase of health care costs, among other factors. The impact of changes in assumptions used to measure the obligations of the Plans is generally recognized over the expected average remaining service period of the plan participants. In selecting the expected rate of return on plan assets, Hydro One considers historical economic indicators that impact asset returns, as well as expectations regarding future long-term capital market performance, weighted by target asset class allocations. In general, equity securities, real estate and private equity investments are forecasted to have higher returns than fixed-income securities.

The following weighted average assumptions were used to determine the benefit obligations at December 31, 2015 and 2014:

Year ended December 31	Pension Benefits 2015	Pension Benefits 2014	Post-Retirement and Post-Employment Benefits 2015	Post-Retirement and Post-Employment Benefits 2014
Significant assumptions:				
Weighted average discount rate	4.00%	4.00%	4.10%	4.00%
Rate of compensation scale escalation (without merit)	2.50%	2.50%	2.50%	2.50%
Rate of cost of living increase	2.00%	2.00%	2.00%	2.00%
Rate of increase in health care cost trends[1]	–	–	4.36%	4.36%

[1] 6.38% per annum in 2016, grading down to 4.36% per annum in and after 2031 (2014 – 6.52% in 2015, grading down to 4.36% per annum in and after 2031)

The following weighted average assumptions were used to determine the net periodic benefit costs for the years ended December 31, 2015 and 2014. Assumptions used to determine current year-end benefit obligations are the assumptions used to estimate the subsequent year's net periodic benefit costs.

Year ended December 31	2015	2014
Pension Benefits:		
Weighted average expected rate of return on plan assets	6.50%	6.50%
Weighted average discount rate	4.00%	4.75%
Rate of compensation scale escalation (without merit)	2.50%	2.50%
Rate of cost of living increase	2.00%	2.00%
Average remaining service life of employees *(years)*	13	11
Post-Retirement and Post-Employment Benefits:		
Weighted average discount rate	4.00%	4.75%
Rate of compensation scale escalation (without merit)	2.50%	2.50%
Rate of cost of living increase	2.00%	2.00%
Average remaining service life of employees *(years)*	13.8	12
Rate of increase in health care cost trends[1]	4.36%	4.39%

[1] 6.52% per annum in 2015, grading down to 4.36% per annum in and after 2031 (2014 – 6.81% in 2014, grading down to 4.39% per annum in and after 2031)

The discount rate used to determine the current year pension obligation and the subsequent year's net periodic benefit costs is based on a yield curve approach. Under the yield curve approach, expected future benefit payments for each plan are discounted by a rate on a third party bond yield curve corresponding to each duration. The yield curve is based on "AA" long-term corporate bonds. A single discount rate is calculated that would yield the same present value as the sum of the discounted cash flows.

The effect of a 1% change in health care cost trends on the projected benefit obligation for the post-retirement and post-employment benefits at December 31, 2015 and 2014 is as follows:

December 31 *(millions of Canadian dollars)*	2015	2014
Projected benefit obligation:		
Effect of a 1% increase in health care cost trends	252	248
Effect of a 1% decrease in health care cost trends	(196)	(193)

The effect of a 1% change in health care cost trends on the service cost and interest cost for the post-retirement and post-employment benefits for the years ended December 31, 2015 and 2014 is as follows:

Year ended December 31 (millions of Canadian dollars)	2015	2014
Service cost and interest cost:		
Effect of a 1% increase in health care cost trends	22	23
Effect of a 1% decrease in health care cost trends	(16)	(17)

The following approximate life expectancies were used in the mortality assumptions to determine the projected benefit obligations for the pension and post-retirement and post-employment plans at December 31, 2015 and 2014:

December 31, 2015				**December 31, 2014**			
Life expectancy at 65 for a member currently at				**Life expectancy at 65 for a member currently at**			
Age 65		**Age 45**		**Age 65**		**Age 45**	
Male	Female	Male	Female	Male	Female	Male	Female
23	25	24	26	23	25	24	26

Estimated Future Benefit Payments

At December 31, 2015, estimated future benefit payments to the participants of the Plans were:

(millions of Canadian dollars)	**Pension Benefits**	**Post-Retirement and Post-Employment Benefits**
2016	316	53
2017	328	55
2018	339	57
2019	350	59
2020	360	61
2021 through to 2025	1,928	342
Total estimated future benefit payments through to 2025	3,621	627

Components of Regulatory Assets

A portion of actuarial gains and losses and prior service costs is recorded within regulatory assets on Hydro One's Consolidated Balance Sheets to reflect the expected regulatory inclusion of these amounts in future rates, which would otherwise be recorded in OCI. The following table provides the actuarial gains and losses and prior service costs recorded within regulatory assets:

Year ended December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Pension Benefits:		
Actuarial loss (gain) for the year	(181)	511
Actuarial loss amortization	(119)	(103)
Prior service cost amortization	(2)	(2)
	(302)	406
Post-Retirement and Post-Employment Benefits:		
Actuarial loss (gain) for the year	(27)	(18)
Actuarial loss amortization	(14)	(18)
Prior service cost amortization	–	(2)
	(41)	(38)

The following table provides the components of regulatory assets that have not been recognized as components of net periodic benefit costs for the years ended December 31, 2015 and 2014:

Year ended December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Pension Benefits:		
Prior service cost	–	2
Actuarial loss	952	1,234
	952	1,236
Post-Retirement and Post-Employment Benefits:		
Actuarial loss	240	273
	240	273

The following table provides the components of regulatory assets at December 31 that are expected to be amortized as components of net periodic benefit costs in the following year:

	Pension Benefits		Post-Retirement and Post-Employment Benefits	
December 31 *(millions of Canadian dollars)*	**2015**	**2014**	**2015**	**2014**
Prior service cost	–	2	–	–
Actuarial loss	96	119	8	10
	96	121	8	10

Pension Plan Assets

Investment Strategy

On a regular basis, Hydro One evaluates its investment strategy to ensure that Pension Plan assets will be sufficient to pay Pension Plan benefits when due. As part of this ongoing evaluation, Hydro One may make changes to its targeted asset allocation and investment strategy. The Pension Plan is managed at a net asset level. The main objective of the Pension Plan is to sustain a certain level of net assets in order to meet the pension obligations of the Company. The Pension Plan fulfills its primary objective by adhering to specific investment policies outlined in its Summary of Investment Policies and Procedures (SIPP), which is reviewed and approved by the Human Resource Committee of Hydro One's Board of Directors. The Company manages net assets by engaging knowledgeable external investment managers who are charged with the responsibility of investing existing funds and new funds (current year's employee and employer contributions) in accordance with the approved SIPP. The performance of the managers is monitored through a governance structure. Increases in net assets are a direct result of investment income generated by investments held by the Pension Plan and contributions to the Pension Plan by eligible employees and by the Company. The main use of net assets is for benefit payments to eligible Pension Plan members.

Pension Plan Asset Mix

At December 31, 2015, the Pension Plan target asset allocations and weighted average asset allocations were as follows:

	Target Allocation (%)	Pension Plan Assets (%)
Equity securities	55.0	58.2
Debt securities	35.0	36.4
Other[1]	10.0	5.4
	100.0	100.0

[1] Other investments include real estate and infrastructure investments.

At December 31, 2015, the Pension Plan held $9 million Hydro One corporate bonds (2014 – $nil) and $420 million of debt securities of the Province (2014 – $340 million).

Concentrations of Credit Risk

Hydro One evaluated its Pension Plan's asset portfolio for the existence of significant concentrations of credit risk as at December 31, 2015 and 2014. Concentrations that were evaluated include, but are not limited to, investment concentrations in a single entity, concentrations in a type of industry, and concentrations in individual funds. At December 31, 2015 and 2014, there were no significant concentrations (defined as greater than 10% of plan assets) of risk in the Pension Plan's assets.

The Pension Plan manages its counterparty credit risk with respect to bonds by investing in investment-grade and government bonds and with respect to derivative instruments by transacting only with financial institutions rated at least "A+" by Standard & Poor's Rating Services, DBRS Limited, and Fitch Ratings Inc., and "A1" by Moody's Investors Service, and also by utilizing exposure limits to each counterparty and ensuring that exposure is diversified across counterparties. The risk of default on transactions in listed securities is considered minimal, as the trade will fail if either party to the transaction does not meet its obligation.

Fair Value Measurements

The following tables present the Pension Plan assets measured and recorded at fair value on a recurring basis and their level within the fair value hierarchy at December 31, 2015 and 2014:

December 31, 2015 *(millions of Canadian dollars)*	**Level 1**	**Level 2**	**Level 3**	**Total**
Pooled funds	–	23	299	322
Cash and cash equivalents	191	–	–	191
Short-term securities	–	80	–	80
Real estate	–	–	2	2
Corporate shares – Canadian	923	–	–	923
Corporate shares – Foreign	2,931	–	–	2,931
Bonds and debentures – Canadian	–	2,074	–	2,074
Bonds and debentures – Foreign	–	199	–	199
Total fair value of plan assets[1]	4,045	2,376	301	6,722

[1] At December 31, 2015, the total fair value of Pension Plan assets excludes $27 million of interest and dividends receivable, and $18 million relating to accruals for pension administration expense and foreign exchange contracts payable.

December 31, 2014 *(millions of Canadian dollars)*	**Level 1**	**Level 2**	**Level 3**	**Total**
Pooled funds	–	18	142	160
Cash and cash equivalents	166	–	–	166
Short-term securities	–	176	–	176
Real estate	–	–	2	2
Corporate shares – Canadian	1,008	–	–	1,008
Corporate shares – Foreign	2,766	–	–	2,766
Bonds and debentures – Canadian	–	1,799	–	1,799
Bonds and debentures – Foreign	–	211	–	211
Total fair value of plan assets[1]	3,940	2,204	144	6,288

[1] At December 31, 2014, the total fair value of Pension Plan assets excludes $18 million of interest and dividends receivable, and $7 million relating to accruals for pension administration expense.

See Note 13 – Fair Value of Financial Instruments and Risk Management for a description of levels within the fair value hierarchy.

Changes in the Fair Value of Financial Instruments Classified in Level 3

The following table summarizes the changes in fair value of financial instruments classified in Level 3 for the years ended December 31, 2015 and 2014. The Pension Plan classifies financial instruments as Level 3 when the fair value is measured based on at least one significant input that is not observable in the markets or due to lack of liquidity in certain markets. The gains and losses presented in the table below may include changes in fair value based on both observable and unobservable inputs.

Year ended December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Fair value, beginning of year	144	119
Realized and unrealized gains	51	30
Purchases	106	23
Sales and disbursements	–	(28)
Fair value, end of year	301	144

There were no significant transfers between any of the fair value levels during the years ended December 31, 2015 and 2014.

The Company performs sensitivity analysis for fair value measurements classified in Level 3, substituting the unobservable inputs with one or more reasonably possible alternative assumptions. These sensitivity analyses resulted in negligible changes in the fair value of financial instruments classified in this level.

Valuation Techniques Used to Determine Fair Value

Pooled Funds

The pooled fund category mainly consists of private equity, real estate and infrastructure investments. Private equity investments represent private equity funds that invest in operating companies that are not publicly traded on a stock exchange. Investment strategies in private equity include limited partnerships in businesses that are characterized by high internal growth and operational efficiencies, venture capital, leveraged buyouts and special situations such as distressed investments. Real estate and infrastructure investments represent funds that invest in real assets which are not publicly traded on a stock exchange. Investment strategies in real estate include limited partnerships that seek to generate a total return through income and capital growth by investing primarily in global and Canadian limited partnerships. Investment strategies in infrastructure include limited partnerships in core infrastructure assets focusing on assets that generate stable, long-term cash flows and deliver incremental returns relative to conventional fixed-income investments. Private equity, real estate and infrastructure valuations are reported by the fund manager and are based on the valuation of the underlying investments which includes inputs such as cost, operating results, discounted future cash flows and market-based comparable data. Since these valuation inputs are not highly observable, private equity and infrastructure investments have been categorized as Level 3 within pooled funds.

Cash Equivalents

Demand cash deposits held with banks and cash held by the investment managers are considered cash equivalents and are included in the fair value measurements hierarchy as Level 1.

Short-Term Securities

Short-term securities are valued at cost plus accrued interest, which approximates fair value due to their short-term nature. Short-term securities have been categorized as Level 2.

Real Estate

Real estate investments represent investments in holding companies that invest in real estate properties. The investments in the holding companies are valued using net asset values reported by the fund manager. Real estate investments are categorized as Level 3.

Corporate Shares

Corporate shares are valued based on quoted prices in active markets and are categorized as Level 1. Investments denominated in foreign currencies are translated into Canadian currency at year-end rates of exchange.

Bonds and Debentures

Bonds and debentures are presented at published closing trade quotations, and are categorized as Level 2.

16. ENVIRONMENTAL LIABILITIES

The following tables show the movements in environmental liabilities for the years ended December 31, 2015 and 2014:

Year ended December 31, 2015 *(millions of Canadian dollars)*	**PCB**	**Land Assessment and Remediation**	**Total**
Environmental liabilities, January 1	172	67	239
Interest accretion	8	2	10
Expenditures	(8)	(11)	(19)
Revaluation adjustment	(24)	1	(23)
Environmental liabilities, December 31	148	59	207
Less: current portion	12	10	22
	136	49	185

Year ended December 31, 2014 *(millions of Canadian dollars)*	**PCB**	**Land Assessment and Remediation**	**Total**
Environmental liabilities, January 1	201	65	266
Interest accretion	9	2	11
Expenditures	(5)	(13)	(18)
Revaluation adjustment	(33)	13	(20)
Environmental liabilities, December 31	172	67	239
Less: current portion	8	10	18
	164	57	221

The following tables show the reconciliation between the undiscounted basis of the environmental liabilities and the amount recognized on the Consolidated Balance Sheets after factoring in the discount rate:

December 31, 2015 *(millions of Canadian dollars)*	**PCB**	**Land Assessment and Remediation**	**Total**
Undiscounted environmental liabilities	168	61	229
Less: discounting accumulated liabilities to present value	20	2	22
Discounted environmental liabilities	148	59	207

December 31, 2014 *(millions of Canadian dollars)*	**PCB**	**Land Assessment and Remediation**	**Total**
Undiscounted environmental liabilities	195	70	265
Less: discounting accumulated liabilities to present value	23	3	26
Discounted environmental liabilities	172	67	239

At December 31, 2015, the estimated future environmental expenditures were as follows:

(millions of Canadian dollars)	
2016	22
2017	25
2018	26
2019	28
2020	30
Thereafter	98
	229

Hydro One records a liability for the estimated future expenditures for land assessment and remediation and for the phase-out and destruction of PCB-contaminated mineral oil removed from electrical equipment when it is determined that future environmental remediation expenditures are probable under existing statute or regulation and the amount of the future expenditures can be reasonably estimated.

There are uncertainties in estimating future environmental costs due to potential external events such as changes in legislation or regulations, and advances in remediation technologies. In determining the amounts to be recorded as environmental liabilities, the Company estimates the current cost of completing required work and makes assumptions as to when the future expenditures will actually be incurred, in order to generate future cash flow information. A long-term inflation rate assumption of approximately 2% has been used to express these current cost estimates as estimated future expenditures. Future expenditures have been discounted using factors ranging from approximately 2.0% to 6.3%, depending on the appropriate rate for the period when expenditures are expected to be incurred. All factors used in estimating the Company's environmental liabilities represent management's best estimates of the present value of costs required to meet existing legislation or regulations. However, it is reasonably possible that numbers or volumes of contaminated assets, cost estimates to perform work, inflation assumptions and the assumed pattern of annual cash flows may differ significantly from the Company's current assumptions. In addition, with respect to the PCB environmental liability, the availability of critical resources such as skilled labour and replacement assets and the ability to take maintenance outages in critical facilities may influence the timing of expenditures.

PCBs

The Environment Canada regulations, enacted under the *Canadian Environmental Protection Act,* 1999, govern the management, storage and disposal of PCBs based on certain criteria, including type of equipment, in-use status, and PCB-contamination thresholds. Under current regulations, Hydro One's PCBs have to be disposed of by the end of 2025, with the exception of specifically exempted equipment. Contaminated equipment will generally be replaced, or will be decontaminated by removing PCB-contaminated insulating oil and retro filling with replacement oil that contains PCBs in concentrations of less than 2 ppm.

The Company's best estimate of the total estimated future expenditures to comply with current PCB regulations is $168 million (2014 – $195 million). These expenditures are expected to be incurred over the period from 2016 to 2025. As a result of its annual review of environmental liabilities, the Company recorded a revaluation adjustment in 2015 to reduce the PCB environmental liability by $24 million (2014 – $33 million).

Land Assessment and Remediation

The Company's best estimate of the total estimated future expenditures to complete its land assessment and remediation program is $61 million (2014 –$70 million). These expenditures are expected to be incurred over the period from 2016 to 2023. As a result of its annual review of environmental liabilities, the Company recorded a revaluation adjustment in 2015 to increase the land assessment and remediation environmental liability by $1 million (2014 – $13 million).

17. ASSET RETIREMENT OBLIGATIONS

Hydro One records a liability for the estimated future expenditures for the removal and disposal of asbestos-containing materials installed in some of its facilities and for the decommissioning of specific switching stations located on unowned sites. Asset retirement obligations, which represent legal obligations associated with the retirement of certain tangible long-lived assets, are computed as the present value of the projected expenditures for the future retirement of specific assets and are recognized in the period in which the liability is incurred, if a reasonable estimate of fair value can be made. If the asset remains in service at the recognition date, the present value of the liability is added to the carrying amount of the associated asset in the period the liability is incurred and this additional carrying amount is depreciated over the remaining life of the asset. If an asset retirement obligation is recorded in respect of an out-of-service asset, the asset retirement cost is charged to results of operations. Subsequent to the initial recognition, the liability is adjusted for any revisions to the estimated future cash flows associated with the asset retirement obligation, which can occur due to a number of factors including, but not limited to, cost escalation, changes in technology applicable to the assets to be retired, changes in legislation or regulations, as well as for accretion of the liability due to the passage of time until the obligation is settled. Depreciation expense is adjusted prospectively for any increases or decreases to the carrying amount of the associated asset.

In determining the amounts to be recorded as asset retirement obligations, the Company estimates the current fair value for completing required work and makes assumptions as to when the future expenditures will actually be incurred, in order to generate future cash flow information. A long-term inflation assumption of approximately 2% has been used to express these current cost estimates as estimated future expenditures. Future expenditures have been discounted using factors ranging from approximately 3.0% to 5.0%, depending on the appropriate rate for the period when expenditures are expected to be incurred. All factors used in estimating the Company's asset retirement obligations represent management's best estimates of the cost required to meet existing legislation or regulations. However, it is reasonably possible that numbers or volumes of contaminated assets, cost estimates to perform work, inflation assumptions and the assumed pattern of annual cash flows may differ significantly from the Company's current assumptions. Asset retirement obligations are reviewed annually or more frequently if significant changes in regulations or other relevant factors occur. Estimate changes are accounted for prospectively.

At December 31, 2015, Hydro One had recorded asset retirement obligations of $9 million (2014 – $9 million), consisting of $8 million (2014 – $8 million) related to the estimated future expenditures associated with the removal and disposal of asbestos-containing materials installed in some of its facilities, as well as $1 million (2014 – $1 million) related to the future decommissioning and removal of two switching stations. The amount of interest recorded is nominal.

18. SHARE CAPITAL

Common Shares

The Company is authorized to issue an unlimited number of common shares. At December 31, 2015, the Company had 142,239 common shares issued and outstanding.

The amount and timing of any dividends payable by Hydro One is at the discretion of the Hydro One Board of Directors and is established on the basis of Hydro One's results of operations, maintenance of its deemed regulatory capital structure, financial condition, cash requirements, the satisfaction of solvency tests imposed by corporate laws for the declaration and payment of dividends and other factors that the Board of Directors may consider relevant.

Preferred Shares

The Company is authorized to issue an unlimited number of preferred shares, issuable in series. At December 31, 2015, Hydro One had no issued and outstanding preferred shares.

On November 2, 2015, a special resolution of Hydro One Limited (as sole shareholder of Hydro One) was made to amend the articles of Hydro One to delete the share ownership restrictions and to amend the Hydro One preferred share terms to provide for basic redeemable preferred shares. When issued, the Class A preferred shares will be redeemable at the option of the Company. The holders of the Class A preferred shares will be entitled to receive, if and when declared by the Hydro One Board of Directors, non-cumulative preferred share dividends at a rate per year to be determined by the Hydro One Board of Directors. The holders of the Class A preferred shares will not be entitled to receive notice of, or to attend or to vote at, any meeting of the shareholders of Hydro One. The holders of the Class A preferred shares will be entitled to receive, before any distributions to the holders of common shares and any other shares ranking junior to the Class A preferred shares, an amount equal to the amount paid for the Class A preferred shares together with all dividends declared and unpaid up to the date of liquidation, dissolution or winding up of Hydro One, or the date of redemption.

Prior to October 31, 2015, the Company had 12,920,000 issued and outstanding 5.5% cumulative preferred shares held by the Province, with a redemption value of $25 per share or $323 million total value. These preferred shares were entitled to an annual cumulative dividend of $18 million, or $1.375 per share, which was payable on a quarterly basis. These preferred shares had conditions for their redemption that were outside the control of the Company because the Province could exercise its right to redeem in the event of change in ownership without approval of the Company's Board of Directors. At December 31, 2014, these preferred shares were classified on the Consolidated Balance Sheet as temporary equity because the redemption feature was outside the control of the Company. On October 31, 2015, these preferred shares were purchased and cancelled by Hydro One. See "Reorganization" below for further details.

Reorganization

Prior to the completion of the IPO, Hydro One and Hydro One Limited completed a series of transactions (Pre-IPO Transactions) that resulted in, among other things, on October 31, 2015, Hydro One Limited acquiring all of the issued and outstanding shares of Hydro One from the Province.

The following table presents the common shares issued during the year ended December 31, 2015. There were no common shares issued during the year ended December 31, 2014.

Year ended December 31, 2015	*(millions of Canadian dollars)*	*(number of shares)*
Pre-Closing Transactions:		
Common shares issued – purchase and cancellation of preferred shares *(a)*	323	2,640
Common shares issued *(b)*	2,600	39,598
Common shares issued *(c)*	–	1
Total common shares issued	2,923	42,239

(a) As part of the Pre-Closing Transactions, on October 31, 2015, Hydro One purchased and cancelled its 12,920,000 preferred shares previously held by the Province for cancellation at a price equal to the redemption price of the preferred shares totaling $323 million, which was satisfied by the issuance to the Province of 2,640 common shares of Hydro One.

(b) On November 4, 2015, Hydro One issued 39,598 common shares to Hydro One Limited for proceeds of $2.6 billion.

(c) On November 3, 2015, Hydro One declared a stock dividend on its common shares, which due to the number of shares issued and the resulting effect on the price per share was treated as a stock split. On November 5, 2015, Hydro One effected a reverse split and issued as consideration one common share to Hydro One Limited. There was no impact to the capital structure of Hydro One as a net result of the stock dividend and the reverse split.

19. DIVIDENDS

In 2015, preferred share dividends in the amount of $13 million (2014 – $18 million) and common share dividends in the amount of $875 million (2014 – $269 million) were declared.

In August 2015, Hydro One declared a dividend in-kind on its common shares payable in all of the issued and outstanding shares of Hydro One Brampton. See Note 4 – Business Combinations.

20. EARNINGS PER SHARE

Basic and diluted earnings per common share (EPS) is calculated by dividing net income attributable to common shareholder of Hydro One by the weighted average number of common shares outstanding. The weighted average number of shares outstanding at December 31, 2015 was 107,116 (2014 – 100,000). There were no dilutive securities during 2015 or 2014.

21. STOCK-BASED COMPENSATION

The following compensation plans were established by Hydro One Limited, however they represent components of compensation costs of Hydro One in current and future periods.

Share Grant Plans

At December 31, 2015, Hydro One Limited had two share grant plans, one for the benefit of certain members of the Power Workers' Union (the PWU Share Grant Plan) and one for the benefit of certain members of The Society of Energy Professionals (the Society Share Grant Plan). Hydro One and Hydro One Limited entered into an intercompany agreement, such that Hydro One will pay Hydro One Limited for the compensation costs associated with these plans.

The PWU Share Grant Plan provides for the issuance of common shares of Hydro One Limited from treasury to certain eligible members of the Power Workers' Union annually, commencing on April 1, 2017 and continuing until the earlier of April 1, 2028 or the date an eligible employee no longer meets the eligibility criteria of the PWU Share Grant Plan. To be eligible, an employee must be a member of the Pension Plan on April 1, 2015, be employed on the date annual share issuance occurs and continue to have under 35 years of service. The requisite service period for the PWU share grant plan begins on July 3, 2015, which is the date the share grant plans were ratified by the PWU. The number of common shares issued annually to each eligible employee will be equal to 2.7% of such eligible employee's salary as at April 1, 2015, divided by $20.50, being the price of the common shares of Hydro One Limited in the IPO. The aggregate number of Hydro One Limited common shares issuable under the PWU Share Grant Plan shall not exceed 3,981,763 common shares. In 2015, 3,952,212 Hydro One Limited common shares were granted under the PWU Share Grant Plan relevant to the total share based compensation recognized by Hydro One.

The Society Share Grant Plan provides for the issuance of common shares of Hydro One Limited from treasury to certain eligible members of The Society of Energy Professionals annually, commencing on April 1, 2018 and continuing until the earlier of April 1, 2029 or the date an eligible employee no longer meets the eligibility criteria of the Society Share Grant Plan. To be eligible, an employee must be a member of the Pension Plan on September 1, 2015, be employed on the date annual share issuance occurs and continue to have under 35 years of service. Therefore the requisite service period for the Society Share Grant Plan begins on September 1, 2015. The number of common shares issued annually to each eligible employee will be equal to 2.0% of such eligible employee's salary as at September 1, 2015, divided by $20.50, being the price of the common shares of Hydro One Limited in the IPO. The aggregate number of Hydro One Limited common shares issuable under the Society Share Grant Plan shall not exceed 1,434,686 common shares. In 2015, 1,367,158 Hydro One Limited common shares were granted under the Society Share Grant Plan relevant to the total share based compensation recognized by Hydro One.

The fair value of the Hydro One Limited share grants is estimated based on the grant date Hydro One Limited share price of $20.50 and is recognized using the graded-vesting attribution method as the share grant plans have both a performance condition and a service condition. Total fair value of shares granted in 2015 is $111 million (2014 – $nil). Total share based compensation recognized during 2015 was $10 million (2014 – $nil) and was recorded as a regulatory asset. The historical turnover rate relating to members of the Power Workers' Union and The Society of Energy Professionals is not believed to be reflective of a future turnover rate due to benefits conferred by the share grant plans. At December 31, 2015 the Company expects all eligible employees to receive the share grants until such time that they no longer meet the eligibility criteria and therefore, a forfeiture rate of 0% is assumed in amounts recognized during 2015. The Company will reevaluate this assumption in subsequent periods based on actual experience.

A summary of share grant activity under the Plan as of December 31, 2015 is presented below:

Years ended December 31, 2015	Share Grants *(Number)*	Weighted-Average Price
Outstanding – beginning of year	–	–
Granted (non-vested)	5,319,370	$20.50
Outstanding – end of year	5,319,370	–

Directors' DSU Plan

Under the Directors' DSU Plan, directors can elect to receive credit for their annual cash retainer in a notional account of DSUs in lieu of cash. Hydro One Limited's Board of Directors may also determine from time to time that special circumstances exist that would reasonably justify the grant of DSUs to a director as compensation in addition to any regular retainer or fee to which the director is entitled.

Each DSU represents a unit with an underlying value equivalent to the value of one common share of Hydro One Limited and is entitled to accrue Hydro One Limited common share dividend equivalents in the form of additional DSUs at the time dividends are paid, subsequent to declaration by Hydro One Limited's Board of Directors.

(number of DSUs)	2015	2014
DSUs outstanding – January 1	–	–
DSUs granted	20,525	–
DSUs outstanding – December 31	20,525	–

For the year ended December 31, 2015, an expense of less than $1 million (2014 – $nil) was recognized in earnings with respect to the DSU Plan. At December 31, 2015, a liability of less than $1 million (December 31, 2014 – $nil) related to outstanding DSUs has been recorded at the closing price of Hydro One Limited's common shares of $22.29 and is included in accrued liabilities on the Balance Sheet.

Employee Share Ownership Plan

Effective December 15, 2015, Hydro One Limited established an Employee Share Ownership Plan (ESOP). Under the ESOP, certain eligible management and non-represented employees may contribute between 1% and 6% of their base salary towards purchasing common shares of Hydro One Limited. The Company will match 50% of the employee's contributions, up to a maximum Company contribution of $25,000 per calendar year. No contributions were made under the ESOP during 2015.

Long-term Incentive Plan

Effective August 31, 2015, the Board of Directors of Hydro One Limited adopted a Long-term Incentive Plan (LTIP). Under the LTIP, long-term incentives will be granted to certain executive and management employees of Hydro One Limited and its subsidiaries, and all equity-based awards will be settled in newly-issued shares of Hydro One Limited from treasury, consistent with the provisions of the plan. The aggregate number of shares issuable under the LTIP shall not exceed 11,900,000 shares of Hydro One Limited.

The LTIP provides flexibility to award a range of vehicles, including restricted share units, performance share units, stock options, share appreciation rights, restricted shares, deferred share units and other share-based awards. The mix of vehicles is intended to vary by role to recognize the level of executive accountability for overall business performance. No long-term incentives were awarded during 2015.

22. NONCONTROLLING INTEREST

On December 16, 2014, the relevant Bruce to Milton Line transmission assets totalling $526 million were transferred from Hydro One Networks to B2M LP. This was financed by 60% debt ($316 million) and 40% equity ($210 million). On December 17, 2014, the Saugeen Ojibway Nation (SON) acquired a 34.2% equity interest in B2M LP for consideration of $72 million, representing the fair value of the equity interest acquired. The SON's initial investment in B2M LP consists of $50 million of Class A units and $22 million of Class B units.

The Class B units have a mandatory put option which requires that upon the occurrence of an enforcement event (i.e. an event of default such as a debt default by the SON or insolvency event), Hydro One purchase the Class B units of B2M LP for net book value on the redemption date. The noncontrolling interest relating to the Class B units is classified on the Consolidated Balance Sheet as temporary equity because the redemption feature is outside the control of the Company. The balance of the noncontrolling interest is classified within equity.

The following tables show the movements in noncontrolling interest for the years ended December 31, 2015 and December 31, 2014:

Year ended December 31, 2015 *(millions of Canadian dollars)*	**Temporary Equity**	**Equity**	**Total**
Noncontrolling interest – January 1, 2015	21	49	70
Distributions to noncontrolling interest	(1)	(4)	(5)
Net income attributable to noncontrolling interest	3	7	10
Noncontrolling interest – December 31, 2015	23	52	75

Year ended December 31, 2014 *(millions of Canadian dollars)*	**Temporary Equity**	**Equity**	**Total**
Noncontrolling interest – January 1, 2014	–	–	–
Amount contributed by noncontrolling interest	22	50	72
Net income (loss) attributable to noncontrolling interest	(1)	(1)	(2)
Noncontrolling interest – December 31, 2014	21	49	70

23. RELATED PARTY TRANSACTIONS

Hydro One is owned by Hydro One Limited. The Province is the majority shareholder of Hydro One Limited. The OEFC, IESO, Ontario Power Generation Inc. (OPG), the OEB, Hydro One Brampton and Hydro One Telecom are related parties to Hydro One because they are controlled or significantly influenced by the Province or by Hydro One Limited. Effective January 1, 2015, the OPA and IESO have merged and are now operating as IESO.

The Province

- During 2015, Hydro One paid dividends to the Province totalling $888 million (2014 – $287 million). In addition, on August 31, 2015, Hydro One declared a dividend in-kind on its common shares payable in all of the issued and outstanding shares of Hydro One Brampton. See Note 4 – Business Combinations.

IESO

- In 2015, Hydro One purchased power in the amount of $2,318 million (2014 – $2,601 million) from the IESO-administered electricity market.
- Hydro One receives revenues for transmission services from the IESO, based on OEB-approved uniform transmission rates. Transmission revenues for 2015 include $1,548 million (2014 – $1,556 million) related to these services.
- Hydro One receives amounts for rural rate protection from the IESO. Distribution revenues for 2015 include $127 million (2014 – $127 million) related to this program.
- Hydro One also receives revenues related to the supply of electricity to remote northern communities from the IESO. Distribution revenues for 2015 include $32 million (2014 – $32 million) related to these services.
- The IESO (OPA prior to January 1, 2015) funds substantially all of the Company's CDM programs. The funding includes program costs, incentives, and management fees. During 2015, Hydro One received $70 million (2014 – $33 million) related to these programs.

OPG

- In 2015, Hydro One purchased power in the amount of $11 million (2014 – $23 million) from OPG.
- Hydro One has service level agreements with OPG. These services include field, engineering, logistics and telecommunications services. In 2015, revenues related to the provision of construction and equipment maintenance services with respect to these service level agreements were $7 million (2014 – $12 million), primarily for the Transmission Business. Operation, maintenance and administration costs in 2015 and 2014 related to the purchase of services with respect to these service level agreements were not significant.

OEFC

- In 2015, Hydro One made PILs to the OEFC totalling $2.9 billion (2014 – $86 million), including Departure Tax of $2.6 billion (2014 – $nil).
- In 2015, Hydro One purchased power in the amount of $6 million (2014 – $9 million) from power contracts administered by the OEFC.
- During 2015, Hydro One paid a $8 million (2014 – $5 million) fee to the OEFC for indemnification against adverse claims in excess of $10 million paid by the OEFC with respect to certain of Ontario Hydro's businesses transferred to Hydro One on April 1, 1999. Hydro One has not made any claims under the indemnity since it was put in place in 1999. Hydro One and the OEFC, with the consent of the Minister of Finance, terminated the indemnity fee effective October 31, 2015.
- PILs and payments in lieu of property taxes were paid to the OEFC.

OEB

- Under the *Ontario Energy Board Act, 1998*, the OEB is required to recover all of its annual operating costs from gas and electricity distributors and transmitters. In 2015, Hydro One incurred $12 million (2014 – $12 million) in OEB fees.

Hydro One Brampton

- Effective August 31, 2015, Hydro One Brampton is no longer a subsidiary of Hydro One, but is indirectly owned by the Province. For change in ownership of Hydro One Brampton, see Note 4 – Business Combinations.
- Subsequent to August 31, 2015, Hydro One continues to provide certain management, administrative and smart meter network services to Hydro One Brampton pursuant to certain service level agreements, which are provided at market rates. These agreements will continue until the end of 2016 (except in the case of smart meter network services, which will continue until the end of 2017). Hydro One Brampton has the right to renew these agreements (other than smart meter network services) for additional one-year terms to end no later than December 31, 2019. Additionally, on August 31, 2015, Hydro One and Hydro One Brampton entered into a license agreement which permits Hydro One Brampton to use the "Hydro One" name and related licensed marks. These agreements will terminate if the Province disposes of its interest in Hydro One Brampton, except in the case of the smart meter network services agreement, which is anticipated to continue for a transition period after the Province disposes of its interest in Hydro One Brampton. During 2015, revenues related to the provision of services with respect to these service level agreements were $1 million.

Hydro One Telecom

- Effective November 6, 2015, Hydro One Telecom is no longer a subsidiary of Hydro One, but is owned by Hydro One Limited. For change in ownership of Hydro One Telecom, see Note 4 – Business Combinations.
- Subsequent to November 6, 2015, Hydro One Telecom continues to provide certain network and carrier management, engineering, and Internet/LAN services to Hydro One. Costs relating to these services in 2015 were $6 million, of which $4 million was charged to OM&A, and $2 million was capitalized. In addition, Hydro One provides certain services to Hydro One Telecom, including management, corporate functions and services, supply management, network maintenance, customer support and asset construction. Revenues related to these services in 2015 were not significant.

Hydro One Limited

- During 2015, Hydro One incurred certain IPO related expenses totaling $7 million (2014 – $nil) which will be reimbursed to the Company by Hydro One Limited.
- On November 4, 2015, Hydro One issued 39,598 common shares to Hydro One Limited for proceeds of $2.6 billion.

- In 2015, Hydro One Limited established certain stock-based compensation plans, however they represent components of costs of Hydro One in current and future periods. Hydro One and Hydro One Limited entered into an intercompany agreement, such that Hydro One will pay Hydro One Limited for the compensation costs associated with the share grant plans, and at December 31, 2015, Hydro One had a payable of $10 million (2014 – $nil) to Hydro One Limited associated with these plans. See Note 21 – Stock-based Compensation.

Sales to and purchases from related parties occur at normal market prices or at a proxy for fair value based on the requirements of the OEB's Affiliate Relationships Code. Outstanding balances at period end are interest free and settled in cash.

The amounts due to and from related parties as a result of the transactions referred to above are as follows:

(millions of Canadian dollars)	**December 31, 2015**	**December 31, 2014**
Due from related parties	184	224
Due to related parties[1]	(142)	(227)

[1] Included in due to related parties at December 31, 2015 are amounts owing to the IESO in respect of power purchases of $134 million (2014 – $214 million).

24. CONSOLIDATED STATEMENTS OF CASH FLOWS

The changes in non-cash balances related to operations consist of the following:

Year ended December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Accounts receivable	244	(93)
Due from related parties	40	(27)
Materials and supplies	2	–
Prepaid expenses and other assets	12	(13)
Accounts payable	(26)	39
Accrued liabilities	(27)	(35)
Due to related parties	(95)	(3)
Accrued interest	(4)	–
Long-term accounts payable and other liabilities	–	(3)
Post-retirement and post-employment benefit liability	41	80
	187	(55)

Capital Expenditures

The following table illustrates the reconciliation between investments in property, plant and equipment and the amount presented in the Consolidated Statements of Cash Flows after accounting for capitalized depreciation and the net change in related accruals:

Year ended December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Capital investments in property, plant and equipment	(1,622)	(1,511)
Capitalized depreciation and net change in accruals included in capital investments in property, plant and equipment	28	30
Capital expenditures – property, plant and equipment	(1,594)	(1,481)

The following table illustrates the reconciliation between investments in intangible assets and the amount presented in the Consolidated Statements of Cash Flows after accounting for the net change in related accruals:

Year ended December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Capital investments in intangible assets	(40)	(19)
Net change in accruals included in capital investments in intangible assets	3	(4)
Capital expenditures – intangible assets	(37)	(23)

Capital Contributions

Hydro One enters into contracts governed by the OEB Transmission System Code when a transmission customer requests a new or upgraded transmission connection. The customer is required to make a capital contribution to Hydro One based on the shortfall between the present value of the costs of the connection facility and the present value of revenues. The present value of revenues is based on an estimate of load forecast for the period of the contract with Hydro One. Once the connection facility is commissioned, in accordance with the OEB Transmission System Code, Hydro One will periodically reassess the estimated of load forecast which will lead to a decrease, or an increase in the capital contributions from the customer. The increase or decrease in capital contributions is recorded directly to fixed assets in service. In 2015, capital contributions from these reassessments totalled $62 million, which represents the difference between the revised load forecast of electricity transmitted compared to the load forecast in the original contract, subject to certain adjustments. No reassessments occurred in 2014.

Supplementary Information

Year ended December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Net interest paid	416	412
Income taxes / PILs paid	2,928	86

25. CONTINGENCIES

Legal Proceedings

Hydro One is involved in various lawsuits, claims and regulatory proceedings in the normal course of business. In the opinion of management, the outcome of such matters will not have a material adverse effect on the Company's consolidated financial position, results of operations or cash flows.

In September 2015, Hydro One and three of its subsidiaries were served with a class action suit in which the representative plaintiff is seeking up to $125 million in damages related to allegations of improper billing practices. Hydro One intends to defend the action. Due to the preliminary stage of legal proceedings, an estimate of a possible loss related to this claim cannot be made.

Transfer of Assets

The transfer orders by which the Company acquired certain of Ontario Hydro's businesses as of April 1, 1999 did not transfer title to some assets located on Reserves (as defined in the *Indian Act* (Canada)). Currently, the OEFC holds these assets. Under the terms of the transfer orders, the Company is required to manage these assets until it has obtained all consents necessary to complete the transfer of title of these assets to itself. The Company cannot predict the aggregate amount that it may have to pay, either on an annual or one-time basis, to obtain the required consents. In 2015, the Company paid approximately $1 million (2014 – $1 million) in respect of consents obtained. If the Company cannot obtain the required consents, the OEFC will continue to hold these assets for an indefinite period of time. If the Company cannot reach a satisfactory settlement, it may have to relocate these assets to other locations at a cost that could be substantial or, in a limited number of cases, to abandon a line and replace it with diesel-generation facilities. The costs relating to these assets could have a material adverse effect on the Company's results of operations if the Company is not able to recover them in future rate orders.

26. COMMITMENTS

Outsourcing Agreements

Inergi LP (Inergi), an affiliate of Capgemini Canada Inc., provides services to Hydro One, including settlements, source to pay services, pay operations services, information technology, finance and accounting services. The agreement with Inergi for these services expires in December 2019. In addition, Inergi provides customer service operations outsourcing services to Hydro One. The agreement for these services expires in February 2018.

Brookfield Global Integrated Solutions (formerly Brookfield Johnson Controls Canada LP) (Brookfield) provides services to Hydro One, including facilities management and execution of certain capital projects as deemed required by the Company. The current agreement with Brookfield expires in December 2024.

At December 31, 2015, the annual commitments under the outsourcing agreements were as follows: 2016 – $167 million; 2017 – $138 million; 2018 – $106 million; 2019 – $99 million; 2020 – $2 million; and thereafter – $11 million.

Trilliant Agreement

In December 2015, Hydro One entered into an agreement with Trilliant Holdings Inc. and Trilliant Networks (Canada) Inc. (Trilliant) for the supply, maintenance and support services for smart meters and related hardware and software, including additional software licenses, as well as certain professional services. This agreement is for a term of ten years, from December 31, 2015 to December 31, 2025, with the option to renew for an additional term of five years at Hydro One's sole discretion. At December 31, 2015, the annual commitments under the agreement were as follows: 2016 – $17 million; 2017 – $17 million; 2018 – $17 million; 2019 – $17 million; 2020 – $16 million; and thereafter – $6 million.

Prudential Support

Purchasers of electricity in Ontario, through the IESO, are required to provide security to mitigate the risk of their default based on their expected activity in the market. As at December 31, 2015, Hydro One provided prudential support to the IESO on behalf of its subsidiaries using parental guarantees of $329 million (2014 – $330 million), and on behalf of a distributor using guarantees of $1 million (2014 – $1 million). In addition, as at December 31, 2015, Hydro One has provided letters of credit in the amount of $15 million (2014 – $8 million) to the IESO. The IESO could draw on these guarantees and/or letters of credit if these subsidiaries or distributor fail to make a payment required by a default notice issued by the IESO. The maximum potential payment is the face value of any letters of credit plus the amount of the parental guarantees.

Retirement Compensation Arrangements

Bank letters of credit have been issued to provide security for the Company's liability under the terms of a trust fund established pursuant to the supplementary pension plan for eligible employees of Hydro One. The supplementary pension plan trustee is required to draw upon these letters of credit if Hydro One is in default of its obligations under the terms of this plan. Such obligations include the requirement to provide the trustee with an annual actuarial report as well as letters of credit sufficient to secure the Company's liability under the plan, to pay benefits payable under the plan and to pay the letter of credit fee. The maximum potential payment is the face value of the letters of credit. At December 31, 2015, Hydro One had letters of credit of $139 million (2014 – $126 million) outstanding relating to retirement compensation arrangements.

Operating Leases

Hydro One is committed as lessee to irrevocable operating lease contracts for buildings used in administrative and service-related functions. These leases have typical terms of between three and five years, but several leases have lesser or greater terms to address special circumstances and/or opportunities. Renewal options, which are generally prevalent in most leases, have similar terms of three to five years. All leases include a clause to enable upward revision of the rental charge on an annual basis or on renewal according to prevailing market conditions or pre-established rents. There are no restrictions placed upon Hydro One by entering into these leases.

During the year ended December 31, 2015, the Company made lease payments totaling $6 million (2014 – $11 million). At December 31, 2015, the future minimum lease payments under non-cancellable operating leases were as follows; 2016 – $10 million; 2017 – $9 million; 2018 – $7 million; 2019 – $2 million; 2020 – $7 million; and thereafter – $3 million.

27. SEGMENTED REPORTING

Hydro One has three reportable segments:

- The Transmission Business, which comprises the core business of transmitting high voltage electricity across the province, interconnecting more than 70 local distribution companies and certain large directly connected industrial customers throughout the Ontario electricity grid;
- The Distribution Business, which comprises the core business of delivering electricity to end customers and certain other municipal electricity distributors; and

- Other Business, which includes certain corporate activities, and the operations of the Company's telecommunications business up to November 6, 2015. See Note 4 – Business Combinations for details of Hydro One Telecom spin-off.

The designation of segments has been based on a combination of regulatory status and the nature of the products and services provided. Operating segments of the Company are determined based on information used by the chief operating decision maker in deciding how to allocate resources and evaluate the performance of each of the segments. The Company evaluates segment performance based on income before financing charges and income taxes from continuing operations (excluding certain allocated corporate governance costs).

The accounting policies followed by the segments are the same as those described in the summary of significant accounting policies (see Note 2 – Significant Accounting Policies). Segment information on the above basis is as follows:

Year ended December 31, 2015 *(millions of Canadian dollars)*	**Transmission**	**Distribution**	**Other**	**Consolidated**
Revenues	1,536	4,949	44	6,529
Purchased power	–	3,450	–	3,450
Operation, maintenance and administration	426	633	71	1,130
Depreciation and amortization	374	380	3	757
Income (loss) before financing charges and income taxes	736	486	(30)	1,192
Capital investments	943	711	8	1,662

Year ended December 31, 2014 *(millions of Canadian dollars)*	**Transmission**	**Distribution**	**Other**	**Consolidated**
Revenues	1,588	4,903	57	6,548
Purchased power	–	3,419	–	3,419
Operation, maintenance and administration	394	742	56	1,192
Depreciation and amortization	346	367	9	722
Income (loss) before financing charges and income taxes	848	375	(8)	1,215
Capital investments	845	680	5	1,530

Total Assets by Segment:

December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Transmission	12,066	12,540
Distribution	9,213	9,805
Other	2,924	205
Total assets	24,203	22,550

All revenues, costs and assets, as the case may be, are earned, incurred or held in Canada.

28. SUBSEQUENT EVENTS

Dividends and Return of Stated Capital

On February 11, 2016, common share dividends in the amount of $2 million were declared, and a return of stated capital in the amount of $225 million was approved.

Great Lakes Power Transmission Purchase Agreement

On January 28, 2016, Hydro One reached an agreement to acquire from Brookfield Infrastructure various entities that own and control Great Lakes Power Transmission LP, an Ontario regulated electricity transmission business operating along the eastern shore of Lake Superior, north and east of Sault Ste. Marie, Ontario, for $222 million in cash, subject to customary adjustments, plus the assumption of approximately $151 million in outstanding indebtedness. The acquisition is pending a *Competition Act* approval as well as regulatory approval from the OEB.

HYDRO ONE INC.
MANAGEMENT'S REPORT

The Consolidated Financial Statements, Management's Discussion and Analysis (MD&A) and related financial information have been prepared by the management of Hydro One Inc. (Hydro One or the Company). Management is responsible for the integrity, consistency and reliability of all such information presented. The Consolidated Financial Statements have been prepared in accordance with United States Generally Accepted Accounting Principles and applicable securities legislation. The MD&A has been prepared in accordance with National Instrument 51-102.

The preparation of the Consolidated Financial Statements and information in the MD&A involves the use of estimates and assumptions based on management's judgment, particularly when transactions affecting the current accounting period cannot be finalized with certainty until future periods. Estimates and assumptions are based on historical experience, current conditions and various other assumptions believed to be reasonable in the circumstances, with critical analysis of the significant accounting policies followed by the Company as described in Note 2 to the Consolidated Financial Statements. The preparation of the Consolidated Financial Statements and the MD&A includes information regarding the estimated impact of future events and transactions. The MD&A also includes information regarding sources of liquidity and capital resources, operating trends, risks and uncertainties. Actual results in the future may differ materially from the present assessment of this information because future events and circumstances may not occur as expected. The Consolidated Financial Statements and MD&A have been properly prepared within reasonable limits of materiality and in light of information up to February 11, 2015.

Management is responsible for establishing and maintaining adequate internal control over financial reporting for the Company. In meeting its responsibility for the reliability of financial information, management maintains and relies on a comprehensive system of internal control and internal audit. The system of internal control includes a written corporate conduct policy; implementation of a risk management framework; effective segregation of duties and delegation of authorities; and sound and conservative accounting policies that are regularly reviewed. This structure is designed to provide reasonable assurance that assets are safeguarded and that reliable information is available on a timely basis. In addition, management has assessed the design and operating effectiveness of the Company's internal control over financial reporting in accordance with the criteria set forth in Internal Control – Integrated Framework (2013), issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this assessment, management concluded that the Company maintained effective internal control over financial reporting as of December 31, 2014. The effectiveness of these internal controls is reported to the Audit, Finance and Pension Investment Committee of the Hydro One Board of Directors, as required.

The Consolidated Financial Statements have been audited by KPMG LLP, independent external auditors appointed by the Shareholder. The external auditors' responsibility is to express their opinion on whether the Consolidated Financial Statements are fairly presented in accordance with United States Generally Accepted Accounting Principles. The Independent Auditors' Report outlines the scope of their examination and their opinion.

The Hydro One Board of Directors, through its Audit, Finance and Pension Investment Committee, is responsible for ensuring that management fulfills its responsibilities for financial reporting and internal controls. The Audit, Finance and Pension Investment Committee of Hydro One met periodically with management, the internal auditors and the external auditors to satisfy itself that each group had properly discharged its respective responsibility and to review the Consolidated Financial Statements before recommending approval by the Board of Directors. The external auditors had direct and full access to the Audit, Finance and Pension Investment Committee, with and without the presence of management, to discuss their audit findings, if any.

The President and Chief Executive Officer and the Chief Financial Officer (Acting) have certified Hydro One's annual Consolidated Financial Statements and annual MD&A, related disclosure controls and procedures and the design and effectiveness of related internal controls over financial reporting.

On behalf of Hydro One Inc.'s management:

Carmine Marcello	Ali R. Suleman
President and Chief Executive Officer	Chief Financial Officer (Acting)

HYDRO ONE INC.
INDEPENDENT AUDITORS' REPORT

To the Shareholder of Hydro One Inc.

We have audited the accompanying Consolidated Financial Statements of Hydro One Inc., which comprise the consolidated balance sheets as at December 31, 2014 and December 31, 2013, the consolidated statements of operations and comprehensive income, changes in equity and cash flows for the years 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 United States Generally Accepted Accounting Principles, 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 audits. We conducted our audits 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 in our audits 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 consolidated financial position of Hydro One Inc. as at December 31, 2014 and December 31, 2013, and its consolidated results of operations and its consolidated cash flows for the years then ended in accordance with United States Generally Accepted Accounting Principles.

KPMG LLP

Chartered Professional Accountants, Licensed Public Accountants

Toronto, Canada
February 11, 2015

HYDRO ONE INC.
CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME
For the years ended December 31, 2014 and 2013

Year ended December 31 (millions of Canadian dollars, except per share amounts)	**2014**	**2013**
Revenues		
Distribution (includes $159 related party revenues; 2013 – $160) *(Note 20)*	4,903	4,484
Transmission (includes $1,567 related party revenues; 2013 – $1,517) *(Note 20)*	1,588	1,529
Other	57	61
	6,548	6,074
Costs		
Purchased power (includes $2,633 related party costs; 2013 – $2,500) *(Note 20)*	3,419	3,020
Operation, maintenance and administration *(Note 20)*	1,192	1,106
Depreciation and amortization *(Note 5)*	722	676
	5,333	4,802
Income before financing charges and provision for payments in lieu of corporate income taxes	1,215	1,272
Financing charges *(Note 6)*	379	360
Income before provision for payments in lieu of corporate income taxes	836	912
Provision for payments in lieu of corporate income taxes *(Notes 7, 20)*	89	109
Net income	747	803
Net income (loss) attributable to noncontrolling interest *(Note 4)*	(2)	–
Net income attributable to the Shareholder of Hydro One Inc.	**749**	**803**
Other comprehensive income	–	–
Comprehensive income	**747**	**803**
Comprehensive income (loss) attributable to noncontrolling interest *(Note 4)*	(2)	–
Comprehensive income attributable to the Shareholder of Hydro One Inc.	**749**	**803**
Basic and fully diluted earnings per common share *(dollars) (Note 18)*	7,319	7,850
Dividends per common share declared *(dollars) (Note 19)*	2,696	2,000

See accompanying notes to Consolidated Financial Statements.

HYDRO ONE INC.
CONSOLIDATED BALANCE SHEETS
At December 31, 2014 and 2013

December 31 (millions of Canadian dollars)	**2014**	**2013**
Assets		
Current assets:		
Cash and cash equivalents *(Note 13)*	100	565
Accounts receivable (net of allowance for doubtful accounts – $66; 2013 – $36) *(Note 8)*	1,016	923
Due from related parties *(Note 20)*	224	197
Regulatory assets *(Note 11)*	31	47
Materials and supplies	23	23
Deferred income tax assets *(Note 7)*	19	18
Derivative instruments *(Note 13)*	2	6
Investment *(Notes 13, 20)*	–	251
Prepaid expenses and other assets	35	28
	1,450	2,058
Property, plant and equipment *(Note 9)*:		
Property, plant and equipment in service	25,356	23,820
Less: accumulated depreciation	9,134	8,615
	16,222	15,205
Construction in progress	1,025	1,078
Future use land, components and spares	154	148
	17,401	16,431
Other long-term assets:		
Regulatory assets *(Note 11)*	3,200	2,636
Intangible assets (net of accumulated amortization – $305; 2013 – $252) *(Note 10)*	276	313
Goodwill *(Note 4)*	173	133
Deferred debt issuance costs	36	36
Deferred income tax assets *(Note 7)*	7	11
Derivative instruments *(Note 13)*	–	6
Other	7	1
	3,699	3,136
Total assets	**22,550**	**21,625**

See accompanying notes to Consolidated Financial Statements.

HYDRO ONE INC.
CONSOLIDATED BALANCE SHEETS (continued)
At December 31, 2014 and 2013

December 31 (millions of Canadian dollars, except number of shares)	**2014**	**2013**
Liabilities		
Current liabilities:		
Bank indebtedness *(Note 13)*	2	31
Accounts payable	173	135
Accrued liabilities *(Notes 15, 16)*	611	654
Due to related parties *(Note 20)*	227	230
Accrued interest	100	100
Regulatory liabilities *(Note 11)*	47	85
Derivative instruments *(Note 13)*	3	–
Long-term debt payable within one year (includes $252 measured at fair value; 2013 – $506) *(Notes 12, 13)*	552	756
	1,715	1,991
Long-term debt (includes $nil measured at fair value; 2013 – $256) *(Notes 12, 13)*	8,373	8,301
Other long-term liabilities:		
Post-retirement and post-employment benefit liability *(Note 15)*	1,533	1,488
Deferred income tax liabilities *(Note 7)*	1,313	1,129
Pension benefit liability *(Note 15)*	1,236	845
Environmental liabilities *(Note 16)*	221	239
Regulatory liabilities *(Note 11)*	168	163
Net unamortized debt premiums	18	20
Asset retirement obligations *(Note 17)*	9	14
Long-term accounts payable and other liabilities	17	20
	4,515	3,918
Total liabilities	**14,603**	**14,210**
Contingencies and commitments (Notes 22, 23)		
Subsequent Event (Note 25)		
Preferred shares (authorized: unlimited; issued: 12,920,000) *(Notes 18, 19)*	323	323
Noncontrolling interest subject to redemption *(Note 4)*	21	–
Equity		
Common shares (authorized: unlimited; issued: 100,000) *(Notes 18, 19)*	3,314	3,314
Retained earnings	4,249	3,787
Accumulated other comprehensive loss	(9)	(9)
Noncontrolling interest *(Note 4)*	49	–
Total equity	**7,603**	**7,092**
	22,550	**21,625**

See accompanying notes to Consolidated Financial Statements.

On behalf of the Board of Directors:

Sandra Pupatello
Chair

George L. Cooke
Chair, Audit, Finance and Pension Investment Committee

HYDRO ONE INC.
CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY
For the years ended December 31, 2014 and 2013

Year ended December 31, 2014 *(millions of Canadian dollars)*	**Common Shares**	**Retained Earnings**	**Accumulated Other Comprehensive Loss**	**Noncontrolling Interest**	**Total Equity**
January 1, 2014	3,314	3,787	(9)	–	7,092
Net income	–	749	–	(1)	748
Other comprehensive income	–	–	–	–	–
Amount contributed by noncontrolling interest	–	–	–	50	50
Dividends on preferred shares	–	(18)	–	–	(18)
Dividends on common shares	–	(269)	–	–	(269)
December 31, 2014	3,314	4,249	(9)	(49)	7,603

Year ended December 31, 2013 *(millions of Canadian dollars)*	**Common Shares**	**Retained Earnings**	**Accumulated Other Comprehensive Loss**	**Noncontrolling Interest**	**Total Equity**
January 1, 2013	3,314	3,202	(9)	–	6,507
Net income	–	803	–	–	803
Other comprehensive income	–	–	–	–	–
Dividends on preferred shares	–	(18)	–	–	(18)
Dividends on common shares	–	(200)	–	–	(200)
December 31, 2013	3,314	3,787	(9)	–	7,092

See accompanying notes to Consolidated Financial Statements.

HYDRO ONE INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
For the years ended December 31, 2014 and 2013

Year ended December 31 (millions of Canadian dollars)	**2014**	**2013**
Operating activities		
Net income	747	803
Environmental expenditures	(18)	(16)
Adjustments for non-cash items:		
Depreciation and amortization (excluding removal costs)	641	597
Regulatory assets and liabilities	(69)	3
Deferred income taxes	10	(2)
Other	–	8
Changes in non-cash balances related to operations *(Note 21)*	(55)	11
Net cash from operating activities	1,256	1,404
Financing activities		
Long-term debt issued	628	1,185
Long-term debt retired	(776)	(600)
Amount contributed by noncontrolling interest *(Note 4)*	72	–
Dividends paid	(287)	(218)
Change in bank indebtedness	(29)	(11)
Other	(3)	(5)
Net cash from (used in) financing activities	(395)	351
Investing activities		
Capital expenditures *(Note 21)*		
Property, plant and equipment	(1,481)	(1,308)
Intangible assets	(23)	(79)
Acquisition of Norfolk Power Inc. *(Note 4)*	(66)	–
Proceeds from investment	250	–
Other	(6)	2
Net cash used in investing activities	(1,326)	(1,385)
Net change in cash and cash equivalents	(465)	370
Cash and cash equivalents, beginning of year	565	195
Cash and cash equivalents, end of year	**100**	**565**

See accompanying notes to Consolidated Financial Statements.

HYDRO ONE INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
For the years ended December 31, 2014 and 2013

1. DESCRIPTION OF THE BUSINESS

Hydro One Inc. (Hydro One or the Company) was incorporated on December 1, 1998, under the *Business Corporations Act* (Ontario) and is wholly owned by the Province of Ontario (Province). The principal businesses of Hydro One are the transmission and distribution of electricity to customers within Ontario. The electricity rates of these businesses are regulated by the Ontario Energy Board (OEB).

2. SIGNIFICANT ACCOUNTING POLICIES

Basis of Consolidation

These Consolidated Financial Statements include the accounts of the Company and its wholly owned subsidiaries: Hydro One Networks Inc. (Hydro One Networks), Hydro One Remote Communities Inc. (Hydro One Remote Communities), Hydro One Brampton Networks Inc. (Hydro One Brampton Networks), Hydro One Telecom Inc. (Hydro One Telecom), Hydro One Lake Erie Link Management Inc., Hydro One Lake Erie Link Company Inc., Norfolk Power Inc. (Norfolk Power), and Hydro One B2M Holdings. Intercompany transactions and balances have been eliminated.

Basis of Accounting

These Consolidated Financial Statements are prepared and presented in accordance with United States (US) Generally Accepted Accounting Principles (GAAP) and in Canadian dollars.

Hydro One performed an evaluation of subsequent events through to February 11, 2015, the date these Consolidated Financial Statements were issued, to determine whether any events or transactions warranted recognition and disclosure in these Consolidated Financial Statements. See Note 25 – Subsequent Event.

Use of Management Estimates

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues, expenses, gains and losses during the reporting periods. Management evaluates these estimates on an ongoing basis based upon historical experience, current conditions, and assumptions believed to be reasonable at the time the assumptions are made, with any adjustments being recognized in results of operations in the period they arise. Significant estimates relate to regulatory assets and regulatory liabilities, environmental liabilities, pension benefits, post-retirement and post-employment benefits, asset retirement obligations (AROs), goodwill and asset impairments, contingencies, unbilled revenues, allowance for doubtful accounts, derivative instruments, and deferred income tax assets and liabilities. Actual results may differ significantly from these estimates, which may be impacted by future decisions made by the OEB or the Province.

Rate Setting

The Company's Transmission Business includes the separately regulated transmission businesses of Hydro One Networks and B2M Limited Partnership (B2M LP). The Company's consolidated Distribution Business includes the separately regulated distribution businesses of Hydro One Networks and the newly acquired Norfolk Power, as well as the subsidiaries Hydro One Brampton Networks and Hydro One Remote Communities.

The OEB has approved the use of US GAAP for rate setting and regulatory accounting and reporting by Hydro One Networks' transmission and distribution businesses, as well as by Hydro One Remote Communities, beginning with the year 2012. Up to the year ended December 31, 2014, Hydro One Brampton Networks used Canadian GAAP (Part V) for its distribution rate-setting purposes, and has transitioned to International Financial Reporting Standards beginning on January 1, 2015.

Transmission

In May 2012, Hydro One Networks filed a cost-of-service application with the OEB for 2013 and 2014 transmission rates. In December 2012, the OEB approved the 2013 and 2014 revenue requirement of $1,438 million and $1,528 million, respectively.

In December 2013, Hydro One Networks filed a draft Rate Order with the OEB for 2014 transmission rates. The 2014 transmission revenue requirement was increased to $1,535 million from the originally-approved revenue requirement of $1,528 million, primarily due to changes in the cost of capital parameters for 2014 released by the OEB in November 2013. On January 9, 2014, the OEB approved the draft Rate Order for 2014 transmission rates as filed.

Distribution

In June 2012, Hydro One Networks filed an Incentive Regulation Mechanism (IRM) application with the OEB for 2013 distribution rates, to be effective January 1, 2013. In December 2012, the OEB issued its final Decision, which resulted in an increase in distribution rates of approximately 1.3% in 2013, or 0.4% when considering total bill impact, for a typical residential customer consuming 800 kWh per month. In April 2013, Hydro One Networks filed an IRM application with the OEB for 2014 distribution rates, to be effective January 1, 2014. In December 2013, the OEB issued its final Decision, which resulted in an increase in distribution rates of approximately 2.4% in 2014, or 0.85% when considering total bill impact, for a typical residential customer consuming 800 kWh per month.

In August 2012, Hydro One Brampton Networks filed an IRM application with the OEB for 2013 distribution rates, to be effective January 1, 2013. In December 2012, the OEB issued its final Decision, which resulted in an increase in distribution rates of approximately 0.3% in 2013, or less than 0.1% when considering total bill impact, for a typical residential customer consuming 800 kWh per month. In August 2013, Hydro One Brampton Networks filed an IRM application with the OEB for 2014 distribution rates, to be effective January 1, 2014. In December 2013, the OEB issued its final Decision, which resulted in a reduction in distribution rates of approximately 2.3% in 2014, or 0.5% when considering total bill impact, for a typical residential customer consuming 800 kWh per month.

In September 2012, Hydro One Remote Communities filed a cost-of-service application with the OEB for 2013 rates, seeking approval for a 2013 revenue requirement of $53 million. In June 2013, the OEB approved a revenue requirement of $51 million for 2013. In October 2013, Hydro One Remote Communities filed an IRM application with the OEB for 2014 rates, seeking approval for a rate increase of approximately 0.5%. In March 2014, the OEB approved an increase of approximately 1.7% to basic rates for the distribution and generation of electricity, with an effective date of May 1, 2014. The final rate increase was adjusted by the OEB's updated rate adjustment parameters and Hydro One Remote Communities' IRM stretch factor.

Regulatory Accounting

The OEB has the general power to include or exclude revenues, costs, gains or losses in the rates of a specific period, resulting in a change in the timing of accounting recognition from that which would have been applied in an unregulated company. Such change in timing involves the application of rate-regulated accounting, giving rise to the recognition of regulatory assets and liabilities. The Company's regulatory assets represent certain amounts receivable from future customers and costs that have been deferred for accounting purposes because it is probable that they will be recovered in future rates. In addition, the Company has recorded regulatory liabilities that generally represent amounts that are refundable to future customers. The Company continually assesses the likelihood of recovery of each of its regulatory assets and continues to believe that it is probable that the OEB will factor its regulatory assets and liabilities into the setting of future rates. If, at some future date, the Company judges that it is no longer probable that the OEB will include a regulatory asset or liability in setting future rates, the appropriate carrying amount will be reflected in results of operations in the period that the assessment is made.

Cash and Cash Equivalents

Cash and cash equivalents include cash and short-term investments with an original maturity of three months or less.

Revenue Recognition

Transmission revenues are collected through OEB-approved rates, which are based on an approved revenue requirement that includes a rate of return. Such revenue is recognized as electricity is transmitted and delivered to customers.

Distribution revenues are recognized on an accrual basis and include billed and unbilled revenues. Distribution revenues attributable to the delivery of electricity are based on OEB-approved distribution rates and are recognized as electricity is delivered to customers. The Company estimates monthly revenue for a period based on wholesale electricity purchases because customer meters are not generally read at the end of each month. At the end of each month, the electricity delivered to customers, but not billed, is estimated and revenue is recognized. The unbilled revenue estimate is affected by energy demand, weather, line losses and changes in the composition of customer classes.

Distribution revenue also includes an amount relating to rate protection for rural, residential and remote customers, which is received from the Independent Electricity System Operator (IESO) based on a standardized customer rate that is approved by the OEB. Current legislation provides rate protection for prescribed classes of rural, residential and remote consumers by reducing the electricity rates that would otherwise apply.

Revenues also include amounts related to sales of other services and equipment. Such revenue is recognized as services are rendered or as equipment is delivered.

Revenues are recorded net of indirect taxes.

Accounts Receivable and Allowance for Doubtful Accounts

Billed accounts receivable are recorded at the invoiced amount, net of allowance for doubtful accounts. Unbilled accounts receivable are estimated and recorded based on wholesale electricity purchases. Overdue amounts related to regulated billings bear interest at OEB-approved rates. The allowance for doubtful accounts reflects the Company's best estimate of losses on billed accounts receivable balances. The allowance is based on accounts receivable aging, historical experience and other currently available information. The Company estimates the allowance for doubtful accounts on customer receivables by applying internally developed loss rates to the outstanding receivable balances by risk segment. Risk segments represent groups of customers with similar credit quality indicators and are computed based on various attributes, including number of days receivables are past due, delinquency of balances and payment history. Loss rates applied to the accounts receivable balances are based on historical average write-offs as a percentage of accounts receivable in each risk segment. An account is considered delinquent if the final amount billed is not received within 110 days of the invoiced date. Accounts receivable are written off against the allowance when they are deemed uncollectible. The existing allowance for uncollectible accounts will continue to be affected by changes in volume, prices and economic conditions.

Noncontrolling interest

Noncontrolling interest represents the portion of equity ownership in subsidiaries that is not attributable to the Shareholder of the parent company. Noncontrolling interest is initially recorded at fair value and subsequently the amount is adjusted for the proportionate share of net income (loss) and other comprehensive income (loss) attributable to the noncontrolling interest and any dividends or distributions paid to the noncontrolling interest.

If a transaction results in the acquisition of all, or part, of a noncontrolling interest in a subsidiary, the acquisition of the noncontrolling interest is accounted for as an equity transaction. No gain or loss is recognized in consolidated net income or comprehensive income as a result of changes in the noncontrolling interest, unless a change results in the loss of control by the Company.

Corporate Income Taxes

Under the *Electricity Act, 1998*, Hydro One is required to make payments in lieu of corporate income taxes (PILs) to the Ontario Electricity Financial Corporation (OEFC). These payments are calculated in accordance with the rules for computing income and other relevant amounts contained in the *Income Tax Act* (Canada) and the *Taxation Act, 2007* (Ontario) as modified by the *Electricity Act, 1998* and related regulations.

Current and deferred income taxes are computed based on the tax rates and tax laws enacted at the balance sheet date. Tax benefits associated with income tax positions taken, or expected to be taken, in a tax return are recorded only when the "more-likely-than-not" recognition threshold is satisfied and are measured at the largest amount of benefit that has a greater than 50% likelihood of being realized upon settlement. Management evaluates each position based solely on the technical merits and facts and circumstances of the position, assuming the position will be examined by a taxing authority having full knowledge of all relevant information. Significant management judgment is required to determine recognition thresholds and the related amount of tax benefits to be recognized in the Consolidated Financial Statements. Management re-evaluates tax positions each period in which new information about recognition or measurement becomes available.

Current Income Taxes

The provision for current taxes and the assets and liabilities recognized for the current and prior periods are measured at the amounts receivable from, or payable to, the OEFC.

Deferred Income Taxes

Deferred income taxes are provided for using the liability method. Deferred income taxes are recognized based on the estimated future tax consequences attributable to temporary differences between the carrying amount of assets and liabilities in the Consolidated Financial Statements and their corresponding tax bases.

Deferred income tax liabilities are generally recognized on all taxable temporary differences. Deferred tax assets are recognized to the extent that it is more-likely-than-not that these assets will be realized from taxable income available against which deductible temporary differences can be utilized.

Deferred income taxes are calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realized, based on the tax rates and tax laws that have been enacted at the balance sheet date. Deferred income taxes that are not included in the rate-setting process are charged or credited to the Consolidated Statements of Operations and Comprehensive Income.

If management determines that it is more-likely-than-not that some or all of a deferred income tax asset will not be realized, a valuation allowance is recorded against the deferred income tax asset to report the net balance at the amount expected to be realized. Previously unrecognized deferred income tax assets are reassessed at each balance sheet date and are recognized to the extent that it has become more-likely-than-not that the tax benefit will be realized.

The Company records regulatory assets and liabilities associated with deferred income taxes that will be included in the rate-setting process.

The Company uses the flow-through method to account for investment tax credits (ITCs) earned on eligible scientific research and experimental development expenditures, and apprenticeship job creation. Under this method, only non-refundable ITCs are recognized as a reduction to income tax expense.

Materials and Supplies

Materials and supplies represent consumables, small spare parts and construction materials held for internal construction and maintenance of property, plant and equipment. These assets are carried at average cost less any impairments recorded.

Property, Plant and Equipment

Property, plant and equipment is recorded at original cost, net of customer contributions received in aid of construction and any accumulated impairment losses. The cost of additions, including betterments and replacement asset components, is included on the Consolidated Balance Sheets as property, plant and equipment.

The original cost of property, plant and equipment includes direct materials, direct labour (including employee benefits), contracted services, attributable capitalized financing costs, asset retirement costs, and direct and indirect overheads that are related to the capital project or program. Indirect overheads include a portion of corporate costs such as finance, treasury,

human resources, information technology and executive costs. Overhead costs, including corporate functions and field services costs, are capitalized on a fully allocated basis, consistent with an OEB-approved methodology.

Property, plant and equipment in service consists of transmission, distribution, communication, administration and service assets and land easements. Property, plant and equipment also includes future use assets, such as land, major components and spare parts, and capitalized project development costs associated with deferred capital projects.

Transmission

Transmission assets include assets used for the transmission of high-voltage electricity, such as transmission lines, support structures, foundations, insulators, connecting hardware and grounding systems, and assets used to step up the voltage of electricity from generating stations for transmission and to step down voltages for distribution, including transformers, circuit breakers and switches.

Distribution

Distribution assets include assets related to the distribution of low-voltage electricity, including lines, poles, switches, transformers, protective devices and metering systems.

Communication

Communication assets include the fibre optic and microwave radio system, optical ground wire, towers, telephone equipment and associated buildings.

Administration and Service

Administration and service assets include administrative buildings, personal computers, transport and work equipment, tools and other minor assets.

Easements

Easements include statutory rights of use for transmission corridors and abutting lands granted under the *Reliable Energy and Consumer Protection Act, 2002*, as well as other land access rights.

Intangible Assets

Intangible assets separately acquired or internally developed are measured on initial recognition at cost, which comprises purchased software, direct labour (including employee benefits), consulting, engineering, overheads and attributable capitalized financing charges. Following initial recognition, intangible assets are carried at cost, net of any accumulated amortization and accumulated impairment losses. The Company’s intangible assets primarily represent major company-wide computer applications.

Capitalized Financing Costs

Capitalized financing costs represent interest costs attributable to the construction of property, plant and equipment or development of intangible assets. The financing cost of attributable borrowed funds is capitalized as part of the acquisition cost of such assets. The capitalized portion of financing costs is a reduction to financing charges recognized in the Consolidated Statements of Operations and Comprehensive Income. Capitalized financing costs are calculated using the Company’s weighted average effective cost of debt.

Construction and Development in Progress

Construction and development in progress consists of the capitalized cost of constructed assets that are not yet complete and which have not yet been placed in service.

Depreciation and Amortization

The cost of property, plant and equipment and intangible assets is depreciated or amortized on a straight-line basis based on the estimated remaining service life of each asset category, except for transport and work equipment, which is depreciated on a declining balance basis.

The Company periodically initiates an external independent review of its property, plant and equipment and intangible asset depreciation and amortization rates, as required by the OEB. Any changes arising from OEB approval of such a review are implemented on a remaining service life basis, consistent with their inclusion in electricity rates. The last review resulted in changes to rates effective January 1, 2013. A summary of average service lives and depreciation and amortization rates for the various classes of assets is included below:

	Average	Rate	
	Service Life	Range	Average
Transmission	57 years	1% – 2%	2%
Distribution	42 years	1% – 20%	2%
Communication	19 years	1% – 15%	4%
Administration and service	15 years	3% – 20%	7%

The cost of intangible assets is included primarily within the administration and service classification above. Amortization rates for computer applications software and other intangible assets range from 9% to 20%.

In accordance with group depreciation practices, the original cost of property, plant and equipment, or major components thereof, and intangible assets that are normally retired, is charged to accumulated depreciation, with no gain or loss being reflected in results of operations. Where a disposition of property, plant and equipment occurs through sale, a gain or loss is calculated based on proceeds and such gain or loss is included in depreciation expense. Depreciation expense also includes the costs incurred to remove property, plant and equipment where no ARO has been recorded.

Goodwill

Goodwill represents the cost of acquired local distribution companies that is in excess of the fair value of the net identifiable assets acquired at the acquisition date. Goodwill is not included in rate base.

Goodwill is evaluated for impairment on an annual basis, or more frequently if circumstances require. The Company performs a qualitative assessment to determine whether it is more-likely-than-not that the fair value of the applicable reporting unit is less than its carrying amount. If the Company determines, as a result of its qualitative assessment, that it is not more-likely-than-not that the fair value of the applicable reporting unit is less than its carrying amount, no further testing is required. If the Company determines, as a result of its qualitative assessment, that it is more-likely-than-not that the fair value of the applicable reporting unit is less than its carrying amount, a goodwill impairment assessment is performed using a two-step, fair value-based test. The first step compares the fair value of the applicable reporting unit to its carrying amount, including goodwill. If the carrying amount of the applicable reporting unit exceeds its fair value, a second step is performed. The second step requires an allocation of fair value to the individual assets and liabilities using purchase price allocation in order to determine the implied fair value of goodwill. If the implied fair value of goodwill is less than the carrying amount, an impairment loss is recorded as a reduction to goodwill and as a charge to results of operations.

For the year ended December 31, 2014, based on the qualitative assessment performed as at September 30, 2014, the Company has determined that it is not more-likely-than-not that the fair value of each applicable reporting unit assessed is less than its carrying amount. As a result, no further testing was performed, and the Company has concluded that goodwill was not impaired at December 31, 2014.

Long-Lived Asset Impairment

When circumstances indicate the carrying value of long-lived assets may not be recoverable, the Company evaluates whether the carrying value of such assets, excluding goodwill, has been impaired. For such long-lived assets, impairment exists when the carrying value exceeds the sum of the future estimated undiscounted cash flows expected to result from the use and

eventual disposition of the asset. When alternative courses of action to recover the carrying amount of a long-lived asset are under consideration, a probability-weighted approach is used to develop estimates of future undiscounted cash flows. If the carrying value of the long-lived asset is not recoverable based on the estimated future undiscounted cash flows, an impairment loss is recorded, measured as the excess of the carrying value of the asset over its fair value. As a result, the asset's carrying value is adjusted to its estimated fair value.

Within its regulated business, the carrying costs of most of Hydro One's long-lived assets are included in rate base where they earn an OEB-approved rate of return. Asset carrying values and the related return are recovered through approved rates. As a result, such assets are only tested for impairment in the event that the OEB disallows recovery, in whole or in part, or if such a disallowance is judged to be probable.

Hydro One regularly monitors the assets of its unregulated Hydro One Telecom subsidiary for indications of impairment. Management assesses the fair value of such long-lived assets using commonly accepted techniques, and may use more than one. Techniques used to determine fair value include, but are not limited to, the use of recent third party comparable sales for reference and internally developed discounted cash flow analysis. Significant changes in market conditions, changes to the condition of an asset, or a change in management's intent to utilize the asset are generally viewed by management as triggering events to reassess the cash flows related to these long-lived assets. As at December 31, 2014, no asset impairment had been recorded for assets within either the Company's regulated or unregulated businesses.

Costs of Arranging Debt Financing

For financial liabilities classified as other than held-for-trading, the Company defers the external transaction costs related to obtaining debt financing and presents such amounts as deferred debt issuance costs on the Consolidated Balance Sheets. Deferred debt issuance costs are amortized over the contractual life of the related debt on an effective-interest basis and the amortization is included within financing charges in the Consolidated Statements of Operations and Comprehensive Income. Transaction costs for items classified as held-for-trading are expensed immediately.

Comprehensive Income

Comprehensive income is comprised of net income and other comprehensive income (OCI). Hydro One presents net income and OCI in a single continuous Consolidated Statement of Operations and Comprehensive Income.

Financial Assets and Liabilities

All financial assets and liabilities are classified into one of the following five categories: held-to-maturity; loans and receivables; held-for-trading; other liabilities; or available-for-sale. Financial assets and liabilities classified as held-for-trading are measured at fair value. All other financial assets and liabilities are measured at amortized cost, except accounts receivable and amounts due from related parties, which are measured at the lower of cost or fair value. Accounts receivable and amounts due from related parties are classified as loans and receivables. The Company considers the carrying amounts of accounts receivable and amounts due from related parties to be reasonable estimates of fair value because of the short time to maturity of these instruments. Provisions for impaired accounts receivable are recognized as adjustments to the allowance for doubtful accounts and are recognized when there is objective evidence that the Company will not be able to collect amounts according to the original terms. All financial instrument transactions are recorded at trade date.

Derivative instruments are measured at fair value. Gains and losses from fair valuation are included within financing charges in the period in which they arise. The Company determines the classification of its financial assets and liabilities at the date of initial recognition. The Company designates certain of its financial assets and liabilities to be held at fair value, when it is consistent with the Company's risk management policy disclosed in Note 13 – Fair Value of Financial Instruments and Risk Management.

Derivative Instruments and Hedge Accounting

The Company closely monitors the risks associated with changes in interest rates on its operations and, where appropriate, uses various instruments to hedge these risks. Certain of these derivative instruments qualify for hedge accounting and are

designated as accounting hedges, while others either do not qualify as hedges or have not been designated as hedges (hereinafter referred to as undesignated contracts) as they are part of economic hedging relationships.

The accounting guidance for derivative instruments requires the recognition of all derivative instruments not identified as meeting the normal purchase and sale exemption as either assets or liabilities recorded at fair value on the Consolidated Balance Sheets. For derivative instruments that qualify for hedge accounting, the Company may elect to designate such derivative instruments as either cash flow hedges or fair value hedges. The Company offsets fair value amounts recognized on its Consolidated Balance Sheets related to derivative instruments executed with the same counterparty under the same master netting agreement.

For derivative instruments that qualify for hedge accounting and which are designated as cash flow hedges, the effective portion of any gain or loss, net of tax, is reported as a component of accumulated OCI (AOCI) and is reclassified to results of operations in the same period or periods during which the hedged transaction affects results of operations. Any gains or losses on the derivative instrument that represent either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness are recognized in results of operations. For fair value hedges, changes in fair value of both the derivative instrument and the underlying hedged exposure are recognized in the Consolidated Statements of Operations and Comprehensive Income in the current period. The gain or loss on the derivative instrument is included in the same line item as the offsetting gain or loss on the hedged item in the Consolidated Statements of Operations and Comprehensive Income. Additionally, the Company enters into derivative agreements that are economic hedges which either do not qualify for hedge accounting or have not been designated as hedges. The changes in fair value of these undesignated derivative instruments are reflected in results of operations.

Embedded derivative instruments are separated from their host contracts and carried at fair value on the Consolidated Balance Sheets when: (a) the economic characteristics and risks of the embedded derivative are not clearly and closely related to the economic characteristics and risks of the host contract; (b) the hybrid instrument is not measured at fair value, with changes in fair value recognized in results of operations each period; and (c) the embedded derivative itself meets the definition of a derivative. The Company does not engage in derivative trading or speculative activities and had no embedded derivatives at December 31, 2014 or 2013.

Hydro One periodically develops hedging strategies taking into account risk management objectives. At the inception of a hedging relationship where the Company has elected to apply hedge accounting, Hydro One formally documents the relationship between the hedged item and the hedging instrument, the related risk management objective, the nature of the specific risk exposure being hedged, and the method for assessing the effectiveness of the hedging relationship. The Company also assesses, both at the inception of the hedge and on a quarterly basis, whether the hedging instruments are effective in offsetting changes in fair values or cash flows of the hedged items.

Employee Future Benefits

Employee future benefits provided by Hydro One include pension, post-retirement and post-employment benefits. The costs of the Company’s pension, post-retirement and post-employment benefit plans are recorded over the periods during which employees render service.

The Company recognizes the funded status of its pension, post-retirement and post-employment plans on its Consolidated Balance Sheets and subsequently recognizes the changes in funded status at the end of each reporting year. Pension, post-retirement and post-employment plans are considered to be underfunded when the projected benefit obligation exceeds the fair value of the plan assets. Liabilities are recognized on the Consolidated Balance Sheets for any net underfunded projected benefit obligation. The net underfunded projected benefit obligation may be disclosed as a current liability, long-term liability, or both. The current portion is the amount by which the actuarial present value of benefits included in the benefit obligation payable in the next 12 months exceeds the fair value of plan assets. If the fair value of plan assets exceeds the projected benefit obligation of the plan, an asset is recognized equal to the net overfunded projected benefit obligation. The post-retirement and post-employment benefit plans are unfunded because there are no related plan assets.

Pension benefits

In accordance with the OEB's rate orders, pension costs are recorded on a cash basis as employer contributions are paid to the pension fund in accordance with the *Pension Benefits Act* (Ontario). Pension costs are recorded on an accrual basis for financial reporting purposes. Pension costs are actuarially determined using the projected benefit method prorated on service and are based on assumptions that reflect management's best estimate of the effect of future events, including future compensation increases. Past service costs from plan amendments and all actuarial gains and losses are amortized on a straight-line basis over the expected average remaining service period of active employees in the plan, and over the estimated remaining life expectancy of inactive employees in the plan. Pension plan assets, consisting primarily of listed equity securities as well as corporate and government debt securities, are fair valued at the end of each year.

Hydro One records a regulatory asset equal to the net underfunded projected benefit obligation for its pension plan. The regulatory asset for the net underfunded projected benefit obligation for the pension plan, in the absence of regulatory accounting, would be recognized in AOCI. A regulatory asset is recognized because management considers it to be probable that pension benefit costs will be recovered in the future through the rate-setting process. The pension regulatory assets are remeasured at the end of each year based on the current status of the pension plan.

All future pension benefit costs are attributed to labour and are either charged to results of operations or capitalized as part of the cost of property, plant and equipment and intangible assets.

Post-retirement and post-employment benefits

Post-retirement and post-employment benefits are recorded and included in rates on an accrual basis. Costs are determined by independent actuaries using the projected benefit method prorated on service and based on assumptions that reflect management's best estimates. Past service costs from plan amendments are amortized to results of operations based on the expected average remaining service period.

Hydro One records a regulatory asset equal to the incremental net unfunded projected benefit obligation for post-retirement and post-employment plans recorded at each year end based on annual actuarial reports. The regulatory asset for the incremental net unfunded projected benefit obligation for post-retirement and post-employment plans, in the absence of regulatory accounting, would be recognized in AOCI. A regulatory asset is recognized because management considers it to be probable that post-retirement and post-employment benefit costs will be recovered in the future through the rate-setting process.

For post-retirement benefits, all actuarial gains or losses are deferred using the "corridor" approach. The amount calculated above the "corridor" is amortized to results of operations on a straight-line basis over the expected average remaining service life of active employees in the plan and over the remaining life expectancy of inactive employees in the plan. The post-retirement benefit obligation is remeasured to its fair value at each year end based on an annual actuarial report, with an offset to the associated regulatory asset, to the extent of the remeasurement adjustment.

For post-employment obligations, the associated regulatory liabilities representing actuarial gains on transition to US GAAP are amortized to results of operations based on the "corridor" approach. Post transition, the actuarial gains and losses on post-employment obligations that are incurred during the year are recognized immediately to results of operations. The post-employment benefit obligation is remeasured to its fair value at each year end based on an annual actuarial report, with an offset to the associated regulatory asset, to the extent of the remeasurement adjustment.

All post-retirement and post-employment future benefit costs are attributed to labour and are either charged to results of operations or capitalized as part of the cost of property, plant and equipment and intangible assets.

Multiemployer Pension Plan

Employees of Hydro One Brampton Networks and the newly acquired Norfolk Power participate in the Ontario Municipal Employees Retirement System Fund (OMERS), a multiemployer, contributory, defined benefit public sector pension fund. OMERS provides retirement pension payments based on members' length of service and salary. Both the participating employers and members are required to make plan contributions. The OMERS plan assets are pooled together to provide

benefits to all plan participants and the plan assets are not segregated by member entity. OMERS is registered with the Financial Services Commission of Ontario under Registration #0345983. At December 31, 2013, OMERS had approximately 440,000 members, with approximately 335 members being current employees of Hydro One Brampton Networks and Norfolk Power.

The OMERS plan is accounted for as a defined contribution plan by Hydro One because it is not practicable to determine the present value of the Company's obligation, the fair value of plan assets or the related current service cost applicable to Hydro One Brampton Networks and Norfolk Power employees. Hydro One recognizes its contributions to the OMERS plan as pension expense, with a portion being capitalized. The expensed amount is included in operation, maintenance and administration costs in the Consolidated Statements of Operations and Comprehensive Income.

Loss Contingencies

Hydro One is involved in certain legal and environmental matters that arise in the normal course of business. In the preparation of its Consolidated Financial Statements, management makes judgments regarding the future outcome of contingent events and records a loss for a contingency based on its best estimate when it is determined that such loss is probable and the amount of the loss can be reasonably estimated. Where the loss amount is recoverable in future rates, a regulatory asset is also recorded. When a range estimate for the probable loss exists and no amount within the range is a better estimate than any other amount, the Company records a loss at the minimum amount within the range.

Management regularly reviews current information available to determine whether recorded provisions should be adjusted and whether new provisions are required. Estimating probable losses may require analysis of multiple forecasts and scenarios that often depend on judgments about potential actions by third parties, such as federal, provincial and local courts or regulators. Contingent liabilities are often resolved over long periods of time. Amounts recorded in the Consolidated Financial Statements may differ from the actual outcome once the contingency is resolved. Such differences could have a material impact on future results of operations, financial position and cash flows of the Company.

Provisions are based upon current estimates and are subject to greater uncertainty where the projection period is lengthy. A significant upward or downward trend in the number of claims filed, the nature of the alleged injuries, and the average cost of resolving each claim could change the estimated provision, as could any substantial adverse or favourable verdict at trial. A federal or provincial legislative outcome or structured settlement could also change the estimated liability. Legal fees are expensed as incurred.

Environmental Liabilities

Environmental liabilities are recorded in respect of past contamination when it is determined that future environmental remediation expenditures are probable under existing statute or regulation and the amount of the future expenditures can be reasonably estimated. Hydro One records a liability for the estimated future expenditures associated with the contaminated land assessment and remediation (LAR) and for the phase-out and destruction of polychlorinated biphenyl (PCB)-contaminated mineral oil removed from electrical equipment, based on the present value of these estimated future expenditures. The Company determines the present value with a discount rate equal to its credit-adjusted risk-free interest rate on financial instruments with comparable maturities to the pattern of future environmental expenditures. As the Company anticipates that the future expenditures will continue to be recoverable in future rates, an offsetting regulatory asset has been recorded to reflect the future recovery of these environmental expenditures from customers. Hydro One reviews its estimates of future environmental expenditures annually, or more frequently if there are indications that circumstances have changed.

Asset Retirement Obligations

AROs are recorded for legal obligations associated with the future removal and disposal of long-lived assets. Such obligations may result from the acquisition, construction, development and/or normal use of the asset. Conditional AROs are recorded when there is a legal obligation to perform a future asset retirement activity but where the timing and/or method of settlement are conditional on a future event that may or may not be within the control of the Company. In such a case, the obligation to perform the asset retirement activity is unconditional even though uncertainty exists about the timing and/or method of settlement.

When recording an ARO, the present value of the estimated future expenditures required to complete the asset retirement activity is recorded in the period in which the obligation is incurred, if a reasonable estimate can be made. In general, the present value of the estimated future expenditures is added to the carrying amount of the associated asset and the resulting asset retirement cost is depreciated over the estimated useful life of the asset. Where an asset is no longer in service when an ARO is recorded, the asset retirement cost is recorded in results of operations.

Some of the Company's transmission and distribution assets, particularly those located on unowned easements and rights-of-way, may have AROs, conditional or otherwise. The majority of the Company's easements and rights-of-way are either of perpetual duration or are automatically renewed annually. Land rights with finite terms are generally subject to extension or renewal. As the Company expects to use the majority of its facilities in perpetuity, no ARO currently exists for these assets. If, at some future date, a particular facility is shown not to meet the perpetuity assumption, it will be reviewed to determine whether an estimable ARO exists. In such a case, an ARO would be recorded at that time.

The Company's AROs recorded to date relate to estimated future expenditures associated with the removal and disposal of asbestos-containing materials installed in some of its facilities and with the decommissioning of specific switching stations located on unowned sites.

3. NEW ACCOUNTING PRONOUNCEMENTS

Recently Adopted Accounting Pronouncements

In July 2013, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2013-11, Income Taxes (Topic 740): Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists. This ASU provides guidance on the presentation of unrecognized tax benefits. This ASU is effective for fiscal years, and interim periods within those years, beginning after December 15, 2013, and should be applied prospectively to all unrecognized tax benefits that exist at the effective date. The adoption of this ASU did not have a significant impact on the Company's consolidated financial statements.

Recent Accounting Guidance Not Yet Adopted

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers (Topic 606). This ASU provides guidance on revenue recognition that depicts the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods and services. This ASU is required to be applied retrospectively and is effective for fiscal years, and interim periods within those years, beginning after December 15, 2016. The Company is currently assessing the impact of adoption of ASU 2014-09 on its consolidated financial statements.

In August 2014, the FASB issued ASU 2014-15, Presentation of Financial Statements – Going Concern (Subtopic 205-40): Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern. This ASU provides guidance about management's responsibility to evaluate whether there is substantial doubt about an entity's ability to continue as a going concern and related disclosures. This ASU is effective for the annual period ending December 31, 2016, and for annual and interim periods thereafter. The adoption of this ASU is not anticipated to have a significant impact on the Company's consolidated financial statements.

In November 2014, the FASB issued ASU 2014-16, Derivatives and Hedging (Topic 815). This ASU provides guidance on accounting for hybrid financial instruments issued in the form of a share. This ASU is effective for fiscal years, and interim periods within those years, beginning after December 15, 2015. The Company is currently assessing the impact of adoption of ASU 2014-16 on its consolidated financial statements.

4. BUSINESS COMBINATIONS

B2M Limited Partnership

In 2012, Hydro One entered into an agreement with the Chippewas of Nawash First Nation and the Chippewas of Saugeen First Nation, collectively referred to as the Saugeen Ojibway Nation (SON), where a noncontrolling equity interest in Hydro One's new limited partnership, B2M LP, would be made available for purchase at fair value by the SON. B2M LP was formed by Hydro One in 2013 to hold most of the transmission lines and a licence to use the related land. These assets are associated with Hydro One's Bruce to Milton Transmission Reinforcement Project, an electricity transmission line (Bruce to Milton Line) in southwestern Ontario, from the Bruce Power facility in Kincardine to Hydro One's Milton Switching Station in the Town of Milton. Hydro One Networks will maintain and operate the Bruce to Milton Line in accordance with an operation and management services agreement. In November 2013, the OEB issued a Decision and Order granting B2M LP a transmission licence and granting Hydro One Networks leave to sell the relevant Bruce to Milton Line transmission assets to B2M LP.

On December 16, 2014, the relevant Bruce to Milton Line transmission assets totalling $526 million were transferred from Hydro One Networks to B2M LP. This was financed by 60% debt ($316 million) and 40% equity ($210 million). On December 17, 2014, the SON acquired a 34.2% equity interest in B2M LP for consideration of $72 million, representing the fair value of the equity interest acquired.

Part of the SON's equity interest in B2M LP is in Class B units of B2M LP that have a mandatory put option. The put option requires that upon the occurrence of an enforcement event (i.e. an event of default such as a debt default by the SON or insolvency event), the SON has the ability to require Hydro One to purchase the Class B units of B2M LP for net book value on the redemption date.

The noncontrolling interest relating to the Class B units is classified on the Consolidated Balance Sheet as temporary equity because the redemption feature is outside the control of the Company. The balance of the noncontrolling interest is classified within equity. At December 31, 2014, the total noncontrolling interest was reduced by the 2014 net loss attributable to noncontrolling interest totalling $2 million, including $1 million relating to noncontrolling interest subject to redemption.

Acquisition of Norfolk Power

On August 29, 2014, Hydro One acquired 100% of the common shares of Norfolk Power, an electricity distribution and telecom company located in southwestern Ontario. The total purchase price for Norfolk Power, net of the long-term debt assumed and adjusted for preliminary working capital and other closing adjustments, is approximately $68 million.

The following table summarizes the preliminary determination of the fair value of the assets acquired and liabilities assumed:

(millions of Canadian dollars)	
Working capital	6
Property, plant and equipment	56
Deferred income tax assets	1
Goodwill	40
Bank indebtedness	(3)
Derivative instruments	(3)
Long-term debt	(26)
Post-retirement and post-employment benefit liability	(1)
Environmental liability	(1)
Long-term accounts payable and other liabilities	(1)
	68

The determination of the fair values of assets acquired and liabilities assumed has been based upon management's estimates and certain assumptions with respect to the fair values of the assets acquired and liabilities assumed. The purchase agreement provides for final purchase price adjustments based on agreed working capital and other balances at the acquisition date which have not yet been finalized. The Company will continue to review information and perform further analysis prior to finalizing

the total purchase price and therefore the actual total purchase price and the consequent impact on goodwill may differ from the amounts above.

Goodwill of approximately $40 million arising from the Norfolk Power acquisition consists largely of the synergies and economies of scale expected from combining the operations of Hydro One and Norfolk Power. All of the goodwill was assigned to Hydro One's Distribution Business segment. None of the goodwill recognized is expected to be deductible for income tax purposes.

Norfolk Power contributed revenues of $18 million and net income of less than $1 million to the Company's consolidated financial results for the year ended December 31, 2014.

All costs related to the acquisition have been expensed through the Consolidated Statements of Operations and Comprehensive Income. The disclosure of Norfolk Power's pro forma information is immaterial to the Company's consolidated financial results for the year ended December 31, 2014.

Woodstock Hydro Purchase Agreement

On May 21, 2014, Hydro One reached an agreement with the City of Woodstock to acquire 100% of the common shares of Woodstock Hydro Holdings Inc. (Woodstock Hydro), an electricity distribution company located in southwestern Ontario. The acquisition is pending a regulatory decision from the OEB. The purchase price for Woodstock Hydro will be approximately $29 million, subject to final closing adjustments. The transaction is anticipated to be completed in 2015. In anticipation of the Woodstock Hydro acquisition, the Company made a refundable deposit totalling $2 million, which is recorded in prepaid expenses and other assets on the Consolidated Balance Sheet.

Haldimand Hydro Purchase Agreement

On June 10, 2014, Hydro One reached an agreement with Haldimand County to acquire 100% of the common shares of Haldimand County Utilities Inc. (Haldimand Hydro), an electricity distribution and telecom company located in southwestern Ontario. The acquisition is pending a regulatory decision from the OEB. The purchase price for Haldimand Hydro will be approximately $65 million, subject to final closing adjustments. The transaction is anticipated to be completed in 2015. In anticipation of the Haldimand Hydro acquisition, the Company made a refundable deposit totalling $3 million, which is recorded in prepaid expenses and other assets on the Consolidated Balance Sheet.

5. DEPRECIATION AND AMORTIZATION

Year ended December 31 (millions of Canadian dollars)	**2014**	**2013**
Depreciation of property, plant and equipment	565	533
Amortization of intangible assets	53	48
Asset removal costs	81	79
Amortization of regulatory assets	23	16
	722	676

6. FINANCING CHARGES

Year ended December 31 (millions of Canadian dollars)	**2014**	**2013**
Interest on long-term debt	432	416
Other	12	9
Less: Interest capitalized on construction and development in progress	(49)	(51)
Gain on interest-rate swap agreements	(10)	(11)
Interest earned on investments	(6)	(3)
	379	360

7. PROVISION FOR PAYMENTS IN LIEU OF CORPORATE INCOME TAXES

The provision for PILs differs from the amount that would have been recorded using the combined Canadian federal and Ontario statutory income tax rate. The reconciliation between the statutory and the effective tax rates is provided as follows:

Year ended December 31 (millions of Canadian dollars)	**2014**	**2013**
Income before provision for PILs	836	912
Canadian federal and Ontario statutory income tax rate	26.50%	26.50%
Provision for PILs at statutory rate	222	242
Increase (decrease) resulting from:		
Net temporary differences included in amounts charged to customers:		
Capital cost allowance in excess of depreciation and amortization	(72)	(72)
Pension contributions in excess of pension expense	(24)	(23)
Overheads capitalized for accounting but deducted for tax purposes	(15)	(14)
Interest capitalized for accounting but deducted for tax purposes	(13)	(13)
Environmental expenditures	(5)	(4)
Prior year's adjustments	(4)	(8)
Non-refundable investment tax credits	(3)	(4)
Post-retirement and post-employment benefit expense in excess of cash payments	3	4
Other	(1)	(1)
Net temporary differences	(134)	(135)
Net permanent differences	1	2
Total provision for PILs	89	109

The major components of income tax expense are as follows:

Year ended December 31 (millions of Canadian dollars)	**2014**	**2013**
Current provision for PILs	79	111
Deferred provision (recovery) for PILs	10	(2)
Total provision for PILs	89	109
Effective income tax rate	10.63%	11.98%

The current provision for PILs is remitted to, or received from, the OEFC. At December 31, 2014, $39 million due from the OEFC was included in due from related parties on the Consolidated Balance Sheet (2013 – $29 million).

At December 31, 2014, the total provision for PILs includes deferred provision for PILs of $10 million (2013 – deferred recovery of $2 million) that is not included in the rate-setting process, using the liability method of accounting. Deferred PILs balances expected to be included in the rate-setting process are offset by regulatory assets and liabilities to reflect the anticipated recovery or disposition of these balances within future electricity rates.

Deferred Income Tax Assets and Liabilities

Deferred income tax assets and liabilities arise from differences between the carrying amounts and tax basis of the Company's assets and liabilities. At December 31, 2014 and 2013, deferred income tax assets and liabilities consisted of the following:

December 31 (millions of Canadian dollars)	**2014**	**2013**
Deferred income tax assets		
Post-retirement and post-employment benefits expense in excess of cash payments	8	7
Environmental expenditures	4	5
Depreciation and amortization in excess of capital cost allowance	(4)	–
Other	(1)	(1)
Total deferred income tax assets	7	11
Less: current portion	–	–
	7	11

December 31 (millions of Canadian dollars)	**2014**	**2013**
Deferred income tax liabilities		
Capital cost allowance in excess of depreciation and amortization	(1,713)	(1,556)
Regulatory amounts that are not recognized for tax purposes	(140)	(144)
Partnership interest	(38)	–
Goodwill	(21)	(20)
Post-retirement and post-employment benefits expense in excess of cash payments	559	542
Environmental expenditures	59	66
Other	–	1
Total deferred income tax liabilities	(1,294)	(1,111)
Less: current portion	19	18
	(1,313)	(1,129)

During 2014 and 2013, there were no changes in the rate applicable to future taxes.

8. ACCOUNTS RECEIVABLE

December 31 (millions of Canadian dollars)	**2014**	**2013**
Accounts receivable – billed	496	268
Accounts receivable – unbilled	586	691
Accounts receivable, gross	1,082	959
Allowance for doubtful accounts	(66)	(36)
Accounts receivable, net	1,016	923

The following table shows the movements in the allowance for doubtful accounts for the years ended December 31, 2014 and 2013:

Year ended December 31 (millions of Canadian dollars)	**2014**	**2013**
Allowance for doubtful accounts – January 1	(36)	(23)
Write-offs	24	24
Additions to allowance for doubtful accounts	(54)	(37)
Allowance for doubtful accounts – December 31	(66)	(36)

9. PROPERTY, PLANT AND EQUIPMENT

December 31, 2014 (millions of Canadian dollars)	Property, Plant and Equipment	Accumulated Depreciation	Construction in Progress	Total
Transmission	13,209	4,416	626	9,419
Distribution	9,076	3,225	320	6,171
Communication	1,100	615	56	541
Administration and Service	1,502	793	23	732
Easements	623	85	–	538
	25,510	9,134	1,025	17,401

December 31, 2013 (millions of Canadian dollars)	Property, Plant and Equipment	Accumulated Depreciation	Construction in Progress	Total
Transmission	12,413	4,215	671	8,869
Distribution	8,498	3,046	316	5,768
Communication	1,060	560	53	553
Administration and Service	1,380	716	38	702
Easements	617	78	–	539
	23,968	8,615	1,078	16,431

Financing charges capitalized on property, plant and equipment under construction were $48 million in 2014 (2013 – $48 million).

10. INTANGIBLE ASSETS

December 31, 2014 (millions of Canadian dollars)	Intangible Assets	Accumulated Amortization	Development in Progress	Total
Computer applications software	573	303	3	273
Other	5	2	–	3
	578	305	3	276

December 31, 2013 (millions of Canadian dollars)	Intangible Assets	Accumulated Amortization	Development in Progress	Total
Computer applications software	557	249	3	311
Other	5	3	–	2
	562	252	3	313

Financing charges capitalized on intangible assets under development were $1 million in 2014 (2013 – $3 million). The estimated annual amortization expense for intangible assets is as follows: 2015 – $53 million; 2016 – $53 million; 2017 – $53 million; 2018 – $45 million; and 2019 – $31 million.

11. REGULATORY ASSETS AND LIABILITIES

Regulatory assets and liabilities arise as a result of the rate-setting process. Hydro One has recorded the following regulatory assets and liabilities:

December 31 (millions of Canadian dollars)	**2014**	**2013**
Regulatory assets:		
Deferred income tax regulatory asset	1,327	1,145
Pension benefit regulatory asset	1,236	845
Post-retirement and post-employment benefits	273	308
Environmental	239	266
Pension cost variance	90	80
DSC exemption	16	7
OEB cost assessment differential	12	9
Retail settlement variance accounts	11	–
Long-term project development costs	–	5
Other	27	18
Total regulatory assets	3,231	2,683
Less: current portion	31	47
	3,200	2,636
Regulatory liabilities:		
Rider 11	83	55
External revenue variance	54	81
CDM deferral variance account	25	–
Deferred income tax regulatory liability	21	19
PST savings deferral	19	17
Hydro One Brampton Networks rider	2	8
Retail settlement variance accounts	–	35
Rider 9	–	19
Other	11	14
Total regulatory liabilities	215	248
Less: current portion	47	85
	168	163

Deferred Income Tax Regulatory Asset and Liability

Deferred income taxes are recognized on temporary differences between the carrying amount of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit. The Company has recognized regulatory assets and liabilities that correspond to deferred income taxes that flow through the rate-setting process. In the absence of rate-regulated accounting, the Company's provision for PILs would have been recognized using the liability method and there would be no regulatory accounts established for taxes to be recovered through future rates. As a result, the 2014 provision for PILs would have been higher by approximately $132 million (2013 – $139 million).

Pension Benefit Regulatory Asset

The Company recognizes the net unfunded status of pension obligations on the Consolidated Balance Sheets with an offset to the associated regulatory asset. A regulatory asset is recognized because management considers it to be probable that pension benefit costs will be recovered in the future through the rate-setting process. The pension benefit obligation is remeasured to its fair value at each year end based on an annual actuarial report, with an offset to the associated regulatory asset, to the extent of the remeasurement adjustment. In the absence of rate-regulated accounting, 2014 OCI would have been lower by $391 million (2013 – higher by $670 million).

Post-Retirement and Post-Employment Benefits

The Company recognizes the net unfunded status of post-retirement and post-employment obligations on the Consolidated Balance Sheets with an incremental offset to the associated regulatory assets. A regulatory asset is recognized because management considers it to be probable that post-retirement and post-employment benefit costs will be recovered in the future through the rate-setting process. The post-retirement and post-employment benefit obligation is remeasured to its fair value at each year end based on an annual actuarial report, with an offset to the associated regulatory asset, to the extent of the remeasurement adjustment. In the absence of rate-regulated accounting, 2014 OCI would have been higher by $35 million (2013 – $12 million).

Environmental

Hydro One records a liability for the estimated future expenditures required to remediate environmental contamination. Because such expenditures are expected to be recoverable in future rates, the Company has recorded an equivalent amount as a regulatory asset. In 2014, the environmental regulatory asset decreased by $33 million (2013 – $3 million) to reflect related changes in the Company's PCB liability, and increased by $13 million (2013 – $26 million) due to changes in the LAR liability. The environmental regulatory asset is amortized to results of operations based on the pattern of actual expenditures incurred and charged to environmental liabilities. The OEB has the discretion to examine and assess the prudency and the timing of recovery of all of Hydro One's actual environmental expenditures. In the absence of rate-regulated accounting, 2014 operation, maintenance and administration expenses would have been lower by $20 million (2013 – higher by $23 million). In addition, 2014 amortization expense would have been lower by $18 million (2013 – $16 million), and 2014 financing charges would have been higher by $11 million (2013 – $10 million).

Pension Cost Variance

A pension cost variance account was established for Hydro One Networks' transmission and distribution businesses to track the difference between the actual pension expenses incurred and estimated pension costs approved by the OEB. The balance in this regulatory account reflects the excess of pension costs paid as compared to OEB-approved amounts. In the absence of rate-regulated accounting, 2014 revenue would have been lower by $10 million (2013 – $19 million).

DSC Exemption

In June 2010, Hydro One Networks filed an application with the OEB regarding the OEB's new cost responsibility rules contained in the OEB's October 2009 Notice of Amendment to the Distribution System Code (DSC), with respect to the connection of certain renewable generators that were already connected or that had received a connection impact assessment prior to October 21, 2009. The application sought approval to record and defer the unanticipated costs incurred by Hydro One Networks that resulted from the connection of certain renewable generation facilities. The OEB ruled that identified specific expenditures can be recorded in a deferral account subject to the OEB's review until the next Hydro One Networks' distribution cost-of-service application. This program effectively ended at the end of 2014 with no new principal to be recorded in 2015.

OEB Cost Assessment Differential

In April 2010, the OEB issued its Decision regarding Hydro One Networks' distribution rate application for 2010 and 2011. As part of this decision, the OEB also approved the distribution-related OEB Cost Assessment Differential Account to record the difference between the amounts approved in rates and actual expenditures with respect to the OEB's cost assessments. This continued for 2012-2014 until the next Hydro One Networks' distribution cost-of-service application, which was submitted in 2014. This program effectively ended at the end of 2014 with no new activity to be recorded in 2015.

Retail Settlement Variance Accounts (RSVAs)

Hydro One has deferred certain retail settlement variance amounts under the provisions of Article 490 of the OEB's Accounting Procedures Handbook. In December 2012, the OEB approved the disposition of the total RSVA balance accumulated from January 2010 to December 2011, including accrued interest, to be disposed over a 24-month period from January 1, 2013 to December 31, 2014. At December 31, 2014, the RSVA was in a net asset position due to a change in global adjustment.

Long-Term Project Development Costs

In May 2009, the OEB approved the creation of a deferral account to record Hydro One Networks' costs of preliminary work to advance certain transmission projects identified in the Company's 2009 and 2010 transmission rate applications. In March 2010, the OEB issued a decision amending the scope of the account to include the 20 major transmission projects identified in the September 2009 request from the Ministry of Energy and Infrastructure. In December 2012, the OEB approved the recovery of the December 31, 2012 balance, including accrued interest, to be recovered over a one-year period from January 1, 2014 to December 31, 2014.

Rider 11

In April 2010, the OEB requested the establishment of deferral accounts which capture the difference between the revenue recorded on the basis of Green Energy Plan expenditures incurred and the actual recoveries received. Rider 11 includes amounts previously included as Rider 8.

External Revenue Variance

In May 2009, the OEB approved forecasted amounts related to export service revenue, external revenue from secondary land use, and external revenue from station maintenance and engineering and construction work. In November 2012, the OEB again approved forecasted amounts related to these revenue categories and extended the scope to encompass all other external revenues. The external revenue variance account balance reflects the excess of actual external revenues compared to the OEB-approved forecasted amounts.

CDM Deferral Variance Account

As part of Hydro One Networks' application for 2013 and 2014 transmission rates, Hydro One agreed to establish a new regulatory deferral variance account to track the impact of actual Conservation and Demand Management (CDM) and demand response results on the load forecast compared to the estimated load forecast included in the revenue requirement. The balance in the CDM deferral variance account relates to the actual 2013 CDM compared to the amounts included in 2013 revenue requirement. The OEB rate order specifically states that the Ontario Power Authority (OPA) data used to calculate the difference between forecasted and actual savings will be provided one year in arrears, and as a result, no amount should be recorded in advance of notification from the OPA of actual results. This notification from the OPA typically occurs in September of each year.

PST Savings Deferral Account

The provincial sales tax (PST) and goods and services tax (GST) were harmonized in July 2010. Unlike the GST, the PST was included in operation, maintenance and administration expenses or capital expenditures for past revenue requirements approved during a full cost-of-service hearing. Under the harmonized sales tax (HST) regime, the HST included in operation, maintenance and administration expenses or capital expenditures is not a cost ultimately borne by the Company and as such, a refund of the prior PST element in the approved revenue requirement is applicable, and calculations for tracking and refund were requested by the OEB. For Hydro One Networks' transmission revenue requirement, PST was included between July 1, 2010 and December 31, 2010 and recorded in a deferral account, per direction from the OEB. For Hydro One Networks' distribution revenue requirement, PST was included between July 1, 2010 and December 31, 2014 and recorded in a deferral account, per direction from the OEB.

Hydro One Brampton Networks Rider

In December 2013, the OEB issued a decision for Hydro One Brampton Networks' 2014 distribution rates. Included in the OEB's decision was the approval of certain deferral account balances, primarily RSVAs. The OEB ordered that the approved balances be aggregated into a single regulatory account and disposed of through a rate rider over a two-year period from January 1, 2014 to December 31, 2015.

Rider 9

In December 2012, as part of Hydro One Networks' 2013 IRM distribution rate application, the OEB approved for disposition certain distribution-related deferral account balances, including RSVA amounts and balances of Rider 2 and Rider 3, accumulated up to December 2011, including accrued interest, to be disposed over a 24-month period from January 1, 2013 to December 31, 2014.

12. DEBT AND CREDIT AGREEMENTS

Short-Term Notes

Hydro One meets its short-term liquidity requirements in part through the issuance of commercial paper under its Commercial Paper Program which has a maximum authorized amount of $1,000 million. These short-term notes are denominated in Canadian dollars with varying maturities not exceeding 365 days. Hydro One had no commercial paper borrowings outstanding as at December 31, 2014 and 2013.

Hydro One has a $1,500 million committed and unused revolving standby credit facility with a syndicate of banks, maturing in June 2019. If used, interest on the facility would apply based on Canadian benchmark rates. This credit facility is unsecured and supports the Company's Commercial Paper Program. The Company may use the credit facility for general corporate purposes, including meeting short-term funding requirements. The obligation of each lender to make any credit extension to the Company under its credit facility is subject to various conditions including, among other things, that no event of default has occurred or would result from such credit extension.

Long-Term Debt

The Company issues notes for long-term financing under its Medium-Term Note (MTN) Program. The maximum authorized principal amount of notes issuable under this program is $3,000 million. At December 31, 2014, $1,187 million remained available for issuance until October 2015.

The following table presents the outstanding long-term debt at December 31, 2014 and 2013:

December 31 (millions of Canadian dollars)	**2014**	**2013**
3.13% Series 19 notes due 2014[1]	–	750
2.95% Series 21 notes due 2015[1]	500	500
Floating-rate Series 22 notes due 2015[2]	50	50
4.64% Series 10 notes due 2016	450	450
Floating-rate Series 27 notes due 2016[2]	50	50
5.18% Series 13 notes due 2017	600	600
2.78% Series 28 notes due 2018	750	750
Floating-rate Series 31 notes due 2019[2]	228	–
4.40% Series 20 notes due 2020	300	300
3.20% Series 25 notes due 2022	600	600
7.35% Debentures due 2030	400	400
6.93% Series 2 notes due 2032	500	500
6.35% Series 4 notes due 2034	385	385
5.36% Series 9 notes due 2036	600	600
4.89% Series 12 notes due 2037	400	400
6.03% Series 17 notes due 2039	300	300
5.49% Series 18 notes due 2040	500	500
4.39% Series 23 notes due 2041	300	300
6.59% Series 5 notes due 2043	315	315
4.59% Series 29 notes due 2043	435	435
4.17% Series 32 notes due 2044	350	–
5.00% Series 11 notes due 2046	325	325
4.00% Series 24 notes due 2051	225	225
3.79% Series 26 notes due 2062	310	310
4.29% Series 30 notes due 2064	50	–
	8,923	9,045
Add: Unrealized mark-to-market loss[1]	2	12
Less: Long-term debt payable within one year	(552)	(756)
Long-term debt	8,373	8,301

[1] The unrealized mark-to-market loss relates to $250 million of the Series 21 notes due 2015 (2013 – $500 million of the Series 19 notes due 2014, and $250 million of the Series 21 notes due 2015). The unrealized mark-to-market loss is offset by a $2 million (2013 – $12 million) unrealized mark-to-market gain on the related fixed-to-floating interest-rate swap agreements, which are accounted for as fair value hedges. See Note 13 – Fair Value of Financial Instruments and Risk Management for details of fair value hedges.

[2] The interest rates of the floating-rate notes are referenced to the 3-month Canadian dollar bankers' acceptance rate, plus a margin.

In 2014, Hydro One issued $628 million (2013 – $1,185 million) of long-term debt under the MTN Program, and repaid the $750 million MTN Series 19 notes (2013 – repaid $600 million MTN Series 15 notes). In addition, the Company repaid long-term debt totalling $26 million assumed on the Norfolk Power acquisition.

The long-term debt is unsecured and denominated in Canadian dollars. The long-term debt is summarized by the number of years to maturity in Note 13 – Fair Value of Financial Instruments and Risk Management.

13. FAIR VALUE OF FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

Fair value is considered to be the exchange price in an orderly transaction between market participants to sell an asset or transfer a liability at the measurement date. The fair value definition focuses on an exit price, which is the price that would be received in the sale of an asset or the amount that would be paid to transfer a liability.

Hydro One classifies its fair value measurements based on the following hierarchy, as prescribed by the accounting guidance for fair value, which prioritizes the inputs to valuation techniques used to measure fair value into three levels:

Level 1 inputs are unadjusted quoted prices in active markets for identical assets or liabilities that Hydro One has the ability to access. An active market for the asset or liability is one in which transactions for the asset or liability occur with sufficient frequency and volume to provide ongoing pricing information.

Level 2 inputs are those other than quoted market prices that are observable, either directly or indirectly, for an asset or liability. Level 2 inputs include, but are not limited to, quoted prices for similar assets or liabilities in an active market, quoted prices for identical or similar assets or liabilities in markets that are not active and inputs other than quoted market prices that are observable for the asset or liability, such as interest-rate curves and yield curves observable at commonly quoted intervals, volatilities, credit risk and default rates. A Level 2 measurement cannot have more than an insignificant portion of the valuation based on unobservable inputs.

Level 3 inputs are any fair value measurements that include unobservable inputs for the asset or liability for more than an insignificant portion of the valuation. A Level 3 measurement may be based primarily on Level 2 inputs.

Non-Derivative Financial Assets and Liabilities

At December 31, 2014 and 2013, the Company's carrying amounts of accounts receivable, due from related parties, cash and cash equivalents, bank indebtedness, accounts payable, and due to related parties are representative of fair value because of the short-term nature of these instruments.

Fair Value Measurements of Long-Term Debt

The fair values and carrying values of the Company's long-term debt at December 31, 2014 and 2013 are as follows:

December 31 (millions of Canadian dollars)	2014 Carrying Value	2014 Fair Value	2013 Carrying Value	2013 Fair Value
Long-term debt				
$500 million of MTN Series 19 notes[1]	–	–	506	506
$250 million of MTN Series 21 notes[1]	252	252	256	256
Other notes and debentures[2]	8,673	10,159	8,295	9,018
	8,925	10,411	9,057	9,780

[1] The fair value of $500 million of the MTN Series 19 notes and of $250 million of the MTN Series 21 notes subject to hedging is primarily based on changes in the present value of future cash flows due to a change in the yield in the swap market for the related swap (hedged risk).

[2] The fair value of other notes and debentures, and the portions of the MTN Series 19 notes and the MTN Series 21 notes that are not subject to hedging, represents the market value of the notes and debentures and is based on unadjusted period-end market prices for the same or similar debt of the same remaining maturities.

Fair Value Measurements of Derivative Instruments

At December 31, 2014, the Company had interest-rate swaps totalling $250 million (2013 – $750 million) that were used to convert fixed-rate debt to floating-rate debt. These swaps are classified as fair value hedges. The Company's fair value hedge exposure was equal to about 3% (2013 – 8%) of its total long-term debt of $8,925 million (2013 – $9,057 million). At December 31, 2014, the Company had the following interest-rate swaps designated as fair value hedges:

(a) two $125 million fixed-to-floating interest-rate swap agreements to convert $250 million of the $500 million MTN Series 21 notes maturing September 11, 2015 into three-month variable-rate debt.

At December 31, 2014, the Company also had interest-rate swaps with a total notional value of $409 million (2013 – $900 million) classified as undesignated contracts. The undesignated contracts consist of the following interest-rate swaps:

(b) a $150 million floating-to-fixed interest-rate swap agreement that locks in the floating rate the Company pays on a portion of the above fixed-to-floating interest-rate swaps from December 11, 2014 to September 11, 2015;
(c) a $50 million floating-to-fixed interest-rate swap agreement that locks in the floating rate the Company pays on the $50 million floating-rate MTN Series 22 notes from January 24, 2014 to January 24, 2015;

(d) a $137 million floating-to-fixed interest-rate swap agreement that locks in the floating rate the Company pays on the $228 million floating-rate MTN Series 31 notes from December 22, 2014 to December 21, 2015;

(e) a $30 million floating-to-fixed interest-rate swap agreement that locks in the floating rate the Company pays on the $50 million floating-rate MTN Series 27 notes from March 3, 2015 to December 3, 2015;

(f) a $30 million floating-to-fixed interest-rate swap agreement that locks in the floating rate the Company pays on the $50 million floating-rate MTN Series 22 notes from January 26, 2015 to July 24, 2015; and

(g) three interest-rate swaps with a total notional value of $12 million that were assumed as part of the Norfolk Power acquisition. These swaps consist of $8 million and $2 million floating-to-fixed interest-rate swap agreements maturing on September 20, 2029, and a $2 million floating-to-fixed interest-rate swap agreement maturing on September 20, 2019.

Fair Value Hierarchy

The fair value hierarchy of financial assets and liabilities at December 31, 2014 and 2013 is as follows:

December 31, 2014 (millions of Canadian dollars)	Carrying Value	Fair Value	Level 1	Level 2	Level 3
Assets:					
Cash and cash equivalents	100	100	100	–	–
Derivative instruments					
Fair value hedges – interest-rate swaps	2	2	–	2	–
	102	102	100	2	–
Liabilities:					
Bank indebtedness	2	2	2	–	–
Derivative instruments					
Undesignated contracts – interest-rate swaps	3	3	–	3	–
Long-term debt	8,925	10,411	–	10,411	–
	8,930	10,416	2	10,414	–

December 31, 2013 (millions of Canadian dollars)	Carrying Value	Fair Value	Level 1	Level 2	Level 3
Assets:					
Cash and cash equivalents	565	565	565	–	–
Investment	251	251	–	251	–
Derivative instruments					
Fair value hedges – interest-rate swaps	12	12	–	12	–
	828	828	565	263	–
Liabilities:					
Bank indebtedness	31	31	31	–	–
Long-term debt	9,057	9,780	–	9,780	–
	9,088	9,811	31	9,780	–

Cash and cash equivalents include cash and short-term investments. At December 31, 2014, short-term investments consisted of bankers' acceptances and money market funds totalling $nil (2013 – $515 million). The carrying values are representative of fair value because of the short-term nature of these instruments.

The investment at December 31, 2013 represented the Province of Ontario Floating-Rate Notes that matured in November 2014. The fair value of the investment was determined using inputs other than quoted prices that are observable for the asset, with unrecognized gains or losses recognized in financing charges. The Company obtained quotes from an independent third party for the fair value of the investment, who uses the market price of similar securities adjusted for changes in observable inputs such as maturity dates and interest rates.

The fair value of the derivative instruments is determined using inputs other than quoted prices that are observable for these assets. The fair value is primarily based on the present value of future cash flows using a swap yield curve to determine the assumptions for interest rates.

The fair value of the hedged portion of the long-term debt is primarily based on the present value of future cash flows using a swap yield curve to determine the assumption for interest rates. The fair value of the unhedged portion of the long-term debt is based on unadjusted period-end market prices for the same or similar debt of the same remaining maturities.

There were no significant transfers between any of the fair value levels during the years ended December 31, 2014 and 2013.

Risk Management

Exposure to market risk, credit risk and liquidity risk arises in the normal course of the Company's business.

Market Risk

Market risk refers primarily to the risk of loss that results from changes in commodity prices, foreign exchange rates and interest rates. The Company does not have commodity risk. The Company does have foreign exchange risk as it enters into agreements to purchase materials and equipment associated with capital programs and projects that are settled in foreign currencies. This foreign exchange risk is not material, although the Company could in the future decide to issue foreign currency-denominated debt which would be hedged back to Canadian dollars consistent with its risk management policy. Hydro One is exposed to fluctuations in interest rates as the regulated rate of return for the Company's Transmission and Distribution Businesses is derived using a formulaic approach that is based on the forecast for long-term Government of Canada bond yields and the spread in 30-year "A"-rated Canadian utility bonds over the 30-year benchmark Government of Canada bond yield. The Company estimates that a 1% decrease in the forecasted long-term Government of Canada bond yield or the "A"-rated Canadian utility spread used in determining the Company's rate of return would reduce the Transmission Business' 2014 annual results of operations by approximately $20 million (2013 – $19 million) and Hydro One Networks' distribution business' 2014 annual results of operations by approximately $10 million (2013 – $10 million).

The Company uses a combination of fixed and variable-rate debt to manage the mix of its debt portfolio. The Company also uses derivative financial instruments to manage interest-rate risk. The Company utilizes interest-rate swaps, which are typically designated as fair value hedges, as a means to manage its interest rate exposure to achieve a lower cost of debt. In addition, the Company may utilize interest-rate derivative instruments to lock in interest-rate levels in anticipation of future financing. Hydro One may also enter into derivative agreements such as forward-starting pay fixed-interest-rate swap agreements to hedge against the effect of future interest-rate movements on long-term fixed-rate borrowing requirements. Such arrangements are typically designated as cash flow hedges. No cash flow hedge agreements were in existence as at December 31, 2014 or 2013.

A hypothetical 10% increase in the interest rates associated with variable-rate debt would not have resulted in a significant decrease in Hydro One's results of operations for the years ended December 31, 2014 or 2013.

Fair Value Hedges

For derivative instruments that are designated and qualify as fair value hedges, the gain or loss on the derivative as well as the offsetting loss or gain on the hedged item attributable to the hedged risk are recognized in the Consolidated Statements of

Operations and Comprehensive Income. The net unrealized loss (gain) on the hedged debt and the related interest-rate swaps for the years ended December 31, 2014 and 2013 are included in financing charges as follows:

Year ended December 31 (millions of Canadian dollars)	**2014**	**2013**
Unrealized loss (gain) on hedged debt	(3)	(8)
Unrealized loss (gain) on fair value interest-rate swaps	3	8
Net unrealized loss (gain)	–	–

At December 31, 2014, Hydro One had $250 million (2013 – $750 million) of notional amounts of fair value hedges outstanding related to interest-rate swaps, with assets at fair value of $2 million (2013 – $12 million). During the years ended December 31, 2014 and 2013, there was no significant impact on the results of operations as a result of any ineffectiveness attributable to fair value hedges.

Credit Risk

Financial assets create a risk that a counterparty will fail to discharge an obligation, causing a financial loss. At December 31, 2014 and 2013, there were no significant concentrations of credit risk with respect to any class of financial assets. The Company's revenue is earned from a broad base of customers. As a result, Hydro One did not earn a significant amount of revenue from any single customer. At December 31, 2014 and 2013, there was no significant accounts receivable balance due from any single customer.

At December 31, 2014, the Company's provision for bad debts was $66 million (2013 – $36 million). Adjustments and write-offs were determined on the basis of a review of overdue accounts, taking into consideration historical experience. At December 31, 2014, approximately 6% of the Company's net accounts receivable were aged more than 60 days (2013 – 4%).

Hydro One manages its counterparty credit risk through various techniques including: entering into transactions with highly-rated counterparties; limiting total exposure levels with individual counterparties consistent with the Company's Board-approved Credit Risk Policy; entering into master agreements which enable net settlement and the contractual right of offset; and monitoring the financial condition of counterparties. In addition to payment netting language in master agreements, the Company establishes credit limits, margining thresholds and collateral requirements for each counterparty. Counterparty credit limits are based on an internal credit review that considers a variety of factors, including the results of a scoring model, leverage, liquidity, profitability, credit ratings and risk management capabilities. The determination of credit exposure for a particular counterparty is the sum of current exposure plus the potential future exposure with that counterparty. The current exposure is calculated as the sum of the principal value of money market exposures and the market value of all contracts that have a positive mark-to-market position on the measurement date. The Company would offset the positive market values against negative values with the same counterparty only where permitted by the existence of a legal netting agreement such as an International Swap Dealers Association master agreement. The potential future exposure represents a safety margin to protect against future fluctuations of interest rates, currencies, equities, and commodities. It is calculated based on factors developed by the Bank of International Settlements, following extensive historical analysis of random fluctuations of interest rates and currencies. To the extent that a counterparty's margining thresholds are exceeded, the counterparty is required to post collateral with the Company as specified in each agreement. The Company monitors current and forward credit exposure to counterparties both on an individual and an aggregate basis. The Company's credit risk for accounts receivable is limited to the carrying amounts on the Consolidated Balance Sheets.

Derivative financial instruments result in exposure to credit risk since there is a risk of counterparty default. The credit exposure of derivative contracts, before collateral, is represented by the fair value of contracts at the reporting date. At December 31, 2014, the counterparty credit risk exposure on the fair value of these interest-rate swap contracts was $3 million (2013 – $14 million). At December 31, 2014, Hydro One's credit exposure for all derivative instruments, and applicable payables and receivables, had a credit rating of investment grade, with five financial institutions as the counterparties. The credit exposure of three of the five counterparties accounted for more than 10% of the total credit exposure of derivative contracts.

Liquidity Risk

Liquidity risk refers to the Company's ability to meet its financial obligations as they come due. Hydro One meets its short-term liquidity requirements using cash and cash equivalents on hand, funds from operations, the issuance of commercial paper, and the revolving standby credit facility of $1,500 million. The short-term liquidity under the Commercial Paper Program, and anticipated levels of funds from operations should be sufficient to fund normal operating requirements.

At December 31, 2014, accounts payable and accrued liabilities in the amount of $784 million (2013 – $789 million) were expected to be settled in cash at their carrying amounts within the next 12 months.

At December 31, 2014, Hydro One had issued long-term debt in the principal amount of $8,923 million (2013 – $9,045 million). Principal repayments, interest payments and related weighted average interest rates are summarized by the number of years to maturity in the following table:

Years to Maturity	Long-term Debt Principal Repayments *(millions of Canadian dollars)*	Interest Payments *(millions of Canadian dollars)*	Weighted Average Interest Rate *(%)*
1 year	550	419	2.8
2 years	500	393	4.3
3 years	600	381	5.2
4 years	750	350	2.8
5 years	228	327	1.6
	2,628	1,870	3.5
6 – 10 years	900	1,522	3.6
Over 10 years	5,395	4,373	5.4
	8,923	7,765	4.7

14. CAPITAL MANAGEMENT

The Company's objectives with respect to its capital structure are to maintain effective access to capital on a long-term basis at reasonable rates, and to deliver appropriate financial returns. In order to ensure ongoing effective access to capital, the Company targets to maintain an "A" category long-term credit rating.

The Company considers its capital structure to consist of Shareholder's equity, preferred shares, long-term debt, and cash and cash equivalents. At December 31, 2014 and 2013, the Company's capital structure was as follows:

December 31 (millions of Canadian dollars)	**2014**	**2013**
Long-term debt payable within one year	552	756
Less: cash and cash equivalents	100	565
	452	191
Long-term debt	8,373	8,301
Preferred shares	323	323
Common shares	3,314	3,314
Retained earnings	4,249	3,787
	7,563	7,101
Total capital	16,711	15,916

The Company has customary covenants typically associated with long-term debt. Among other things, Hydro One's long-term debt and credit facility covenants limit the permissible debt to 75% of the Company's total capitalization, limit the

ability to sell assets and impose a negative pledge provision, subject to customary exceptions. At December 31, 2014 and 2013, Hydro One was in compliance with all of these covenants and limitations.

15. PENSION AND POST-RETIREMENT AND POST-EMPLOYMENT BENEFITS

Hydro One has a defined benefit pension plan, a supplementary pension plan, and post-retirement and post-employment benefit plans. The defined benefit pension plan (Pension Plan) is contributory and covers all regular employees of Hydro One and its subsidiaries, except employees of Hydro One Brampton Networks and Norfolk Power. Employees of Hydro One Brampton Networks and Norfolk Power participate in the OMERS plan. The supplementary pension plan provides members of the Pension Plan with benefits that would have been earned and payable under the Pension Plan but for the limitations imposed by the *Income Tax Act* (Canada). The supplementary pension plan obligation is included with other post-retirement and post-employment benefit obligations on the Consolidated Balance Sheets.

The OMERS Plan

Hydro One contributions to the OMERS plan for the year ended December 31, 2014 were $2 million (2013 – $2 million). Company contributions payable at December 31, 2014 and included in accrued liabilities on the Consolidated Balance Sheets were less than $1 million (2013 – less than $1 million). Hydro One contributions do not represent more than 5% of total contributions to the OMERS plan, as indicated in OMERS' most recently available annual report for the year ended December 31, 2013.

At December 31, 2013, the OMERS plan was 88.2% funded, with an unfunded liability of $8,641 million. This unfunded liability could result in future payments by participating employers and members. Hydro One future contributions could be increased substantially if other entities withdraw from the plan.

Pension Plan, Post-Retirement and Post-Employment Plans

The Pension Plan provides benefits based on highest three-year average pensionable earnings. For new management employees who commenced employment on or after January 1, 2004, and for new Society of Energy Professionals-represented staff hired after November 17, 2005, benefits are based on highest five-year average pensionable earnings. After retirement, pensions are indexed to inflation.

Company and employee contributions to the Pension Plan are based on actuarial valuations performed at least every three years. Annual Pension Plan contributions for 2014 of $174 million (2013 – $160 million) were based on an actuarial valuation effective December 31, 2013 (2013 – effective December 31, 2011) and the expected level of pensionable earnings. Estimated annual Pension Plan contributions for 2015 and 2016 are approximately $174 million and $175 million, respectively, based on the actuarial valuation as at December 31, 2013 and projected levels of pensionable earnings. Future minimum contributions beyond 2016 will be based on an actuarial valuation effective no later than December 31, 2016. Contributions are payable one month in arrears. All of the contributions are expected to be in the form of cash.

Hydro One recognizes the overfunded or underfunded status of the Pension Plan, and post-retirement and post-employment benefit plans (Plans) as an asset or liability on its Consolidated Balance Sheets, with offsetting regulatory assets and liabilities as appropriate. The underfunded benefit obligations for the Plans, in the absence of regulatory accounting, would be recognized in AOCI. The impact of changes in assumptions used to measure pension, post-retirement and post-employment benefit obligations is generally recognized over the expected average remaining service period of the employees. The measurement date for the Plans is December 31.

	Pension Benefits		Post-Retirement and Post-Employment Benefits	
Year ended December 31 (millions of Canadian dollars)	**2014**	**2013**	**2014**	**2013**
Change in projected benefit obligation				
Projected benefit obligation, beginning of year	6,576	6,507	1,531	1,459
Current service cost	145	170	41	40
Interest cost	312	278	73	63
Reciprocal transfers	–	1	–	–
Benefits paid	(319)	(317)	(45)	(44)
Net actuarial loss (gain)	821	(63)	(18)	13
Projected benefit obligation, end of year	7,535	6,576	1,582	1,531
Change in plan assets				
Fair value of plan assets, beginning of year	5,731	4,992	–	–
Actual return on plan assets	703	887	–	–
Reciprocal transfers	–	1	–	–
Benefits paid	(319)	(317)	–	–
Employer contributions	174	160	–	–
Employee contributions	35	30	–	–
Administrative expenses	(25)	(22)	–	–
Fair value of plan assets, end of year	6,299	5,731	–	–
Unfunded status	1,236	845	1,582	1,531

Hydro One presents its benefit obligations and plan assets net on its Consolidated Balance Sheets within the following line items:

	Pension Benefits		Post-Retirement and Post-Employment Benefits	
December 31 (millions of Canadian dollars)	**2014**	**2013**	**2014**	**2013**
Accrued liabilities	–	–	49	43
Pension benefit liability	1,236	845	–	–
Post-retirement and post-employment benefit liability	–	–	1,533	1,488
Unfunded status	1,236	845	1,582	1,531

The funded or unfunded status of the pension, post-retirement and post-employment benefit plans refers to the difference between the fair value of plan assets and the projected benefit obligations for the Plans. The funded/unfunded status changes over time due to several factors, including contribution levels, assumed discount rates and actual returns on plan assets.

The following table provides the projected benefit obligation (PBO), accumulated benefit obligation (ABO) and fair value of plan assets for the Pension Plan:

December 31 (millions of Canadian dollars)	**2014**	**2013**
PBO	7,535	6,576
ABO	6,887	5,998
Fair value of plan assets	6,299	5,731

On an ABO basis, the Pension Plan was funded at 91% at December 31, 2014 (2013 – 96%). On a PBO basis, the Pension Plan was funded at 84% at December 31, 2014 (2013 – 87%). The ABO differs from the PBO in that the ABO includes no assumption about future compensation levels.

Components of Net Periodic Benefit Costs

The following table provides the components of the net periodic benefit costs for the years ended December 31, 2014 and 2013 for the Pension Plan:

Year ended December 31 (millions of Canadian dollars)	**2014**	**2013**
Current service cost, net of employee contributions	110	141
Interest cost	312	278
Expected return on plan assets, net of expenses	(369)	(309)
Actuarial loss amortization	103	175
Prior service cost amortization	2	2
Net periodic benefit costs	158	287
Charged to results of operations[1]	81	72

[1] The Company follows the cash basis of accounting consistent with the inclusion of pension costs in OEB-approved rates. During the year ended December 31, 2014, pension costs of $174 million (2013 – $160 million) were attributed to labour, of which $81 million (2013 – $72 million) was charged to operations, and $93 million (2013 – $88 million) was capitalized as part of the cost of property, plant and equipment and intangible assets.

The following table provides the components of the net periodic benefit costs for the years ended December 31, 2014 and 2013 for the post-retirement and post-employment benefit plans:

Year ended December 31 (millions of Canadian dollars)	**2014**	**2013**
Current service cost, net of employee contributions	41	40
Interest cost	73	63
Actuarial loss amortization	18	27
Prior service cost amortization	2	3
Net periodic benefit costs	134	133
Charged to results of operations	62	58

Assumptions

The measurement of the obligations of the Plans and the costs of providing benefits under the Plans involves various factors, including the development of valuation assumptions and accounting policy elections. When developing the required assumptions, the Company considers historical information as well as future expectations. The measurement of benefit obligations and costs is impacted by several assumptions including the discount rate applied to benefit obligations, the long-term expected rate of return on plan assets, Hydro One's expected level of contributions to the Plans, the incidence of mortality, the expected remaining service period of plan participants, the level of compensation and rate of compensation increases, employee age, length of service, and the anticipated rate of increase of health care costs, among other factors. The impact of changes in assumptions used to measure the obligations of the Plans is generally recognized over the expected average remaining service period of the plan participants. In selecting the expected rate of return on plan assets, Hydro One considers historical economic indicators that impact asset returns, as well as expectations regarding future long-term capital market performance, weighted by target asset class allocations. In general, equity securities, real estate and private equity investments are forecasted to have higher returns than fixed-income securities.

The following weighted average assumptions were used to determine the benefit obligations at December 31, 2014 and 2013:

	Pension Benefits		Post-Retirement and Post-Employment Benefits	
Year ended December 31	**2014**	**2013**	**2014**	**2013**
Significant assumptions:				
Weighted average discount rate	4.00%	4.75%	4.00%	4.75%
Rate of compensation scale escalation (without merit)	2.50%	2.50%	2.50%	2.50%
Rate of cost of living increase	2.00%	2.00%	2.00%	2.00%
Rate of increase in health care cost trends[1]	–	–	4.36%	4.39%

[1] 6.52% per annum in 2015, grading down to 4.36% per annum in and after 2031 (2013 – 6.81% in 2014, grading down to 4.39% per annum in and after 2031)

The following weighted average assumptions were used to determine the net periodic benefit costs for the years ended December 31, 2014 and 2013. Assumptions used to determine current year-end benefit obligations are the assumptions used to estimate the subsequent year's net periodic benefit costs.

Year ended December 31	**2014**	**2013**
Pension Benefits:		
Weighted average expected rate of return on plan assets	6.50%	6.25%
Weighted average discount rate	4.75%	4.25%
Rate of compensation scale escalation (without merit)	2.50%	2.50%
Rate of cost of living increase	2.00%	2.00%
Average remaining service life of employees *(years)*	11	11
Post-Retirement and Post-Employment Benefits:		
Weighted average discount rate	4.75%	4.25%
Rate of compensation scale escalation (without merit)	2.50%	2.50%
Rate of cost of living increase	2.00%	2.00%
Average remaining service life of employees *(years)*	12	12
Rate of increase in health care cost trends[1]	4.39%	4.39%

[1] 6.81% per annum in 2014, grading down to 4.39% per annum in and after 2031 (2013 – 6.91% in 2013, grading down to 4.39% per annum in and after 2031)

The discount rate used to determine the current year pension obligation and the subsequent year's net periodic benefit costs is based on a yield curve approach. Under the yield curve approach, expected future benefit payments for each plan are discounted by a rate on a third party bond yield curve corresponding to each duration. The yield curve is based on "AA" long-term corporate bonds. A single discount rate is calculated that would yield the same present value as the sum of the discounted cash flows.

The effect of a 1% change in health care cost trends on the projected benefit obligation for the post-retirement and post-employment benefits at December 31, 2014 and 2013 is as follows:

December 31 (millions of Canadian dollars)	**2014**	**2013**
Projected benefit obligation:		
Effect of a 1% increase in health care cost trends	248	258
Effect of a 1% decrease in health care cost trends	(193)	(200)

The effect of a 1% change in health care cost trends on the service cost and interest cost for the post-retirement and post-employment benefits for the years ended December 31, 2014 and 2013 is as follows:

Year ended December 31 (millions of Canadian dollars)	**2014**	**2013**
Service cost and interest cost:		
Effect of a 1% increase in health care cost trends	23	21
Effect of a 1% decrease in health care cost trends	(17)	(16)

The following approximate life expectancies were used in the mortality assumptions to determine the projected benefit obligations for the pension and post-retirement and post-employment plans at December 31, 2014 and 2013:

December 31, 2014				**December 31, 2013**			
Life expectancy at 65 for a member currently at				**Life expectancy at 65 for a member currently at**			
Age 65		**Age 45**		**Age 65**		**Age 45**	
Male	Female	Male	Female	Male	Female	Male	Female
23	25	24	26	23	25	24	26

Estimated Future Benefit Payments

At December 31, 2014, estimated future benefit payments to the participants of the Plans were:

(millions of Canadian dollars)	Pension Benefits	Post-Retirement and Post-Employment Benefits
2015	305	50
2016	316	52
2017	328	54
2018	339	56
2019	350	59
2020 through to 2024	1,889	332
Total estimated future benefit payments through to 2024	3,527	603

Components of Regulatory Assets

A portion of actuarial gains and losses and prior service costs is recorded within regulatory assets on Hydro One's Consolidated Balance Sheets to reflect the expected regulatory inclusion of these amounts in future rates, which would otherwise be recorded in OCI. The following table provides the actuarial gains and losses and prior service costs recorded within regulatory assets:

Year ended December 31 (millions of Canadian dollars)	**2014**	**2013**
Pension Benefits:		
Actuarial loss (gain) for the year	511	(619)
Actuarial loss amortization	(103)	(175)
Prior service cost amortization	(2)	(2)
	406	(796)
Post-Retirement and Post-Employment Benefits:		
Actuarial loss (gain) for the year	(18)	13
Actuarial loss amortization	(18)	(27)
Prior service cost amortization	(2)	(3)
	(38)	(17)

The following table provides the components of regulatory assets that have not been recognized as components of net periodic benefit costs for the years ended December 31, 2014 and 2013:

Year ended December 31 (millions of Canadian dollars)	**2014**	**2013**
Pension Benefits:		
Prior service cost	2	3
Actuarial loss	1,234	842
	1,236	845
Post-Retirement and Post-Employment Benefits:		
Prior service cost	–	2
Actuarial loss	273	306
	273	308

The following table provides the components of regulatory assets at December 31 that are expected to be amortized as components of net periodic benefit costs in the following year:

	Pension Benefits		Post-Retirement and Post-Employment Benefits	
December 31 (millions of Canadian dollars)	**2014**	**2013**	**2014**	**2013**
Prior service cost	2	2	–	2
Actuarial loss	119	103	10	15
	121	105	10	17

Pension Plan Assets

Investment Strategy

On a regular basis, Hydro One evaluates its investment strategy to ensure that Pension Plan assets will be sufficient to pay Pension Plan benefits when due. As part of this ongoing evaluation, Hydro One may make changes to its targeted asset allocation and investment strategy. The Pension Plan is managed at a net asset level. The main objective of the Pension Plan is to sustain a certain level of net assets in order to meet the pension obligations of the Company. The Pension Plan fulfills its primary objective by adhering to specific investment policies outlined in its Summary of Investment Policies and Procedures (SIPP), which is reviewed and approved by the Audit, Finance and Pension Investment Committee of Hydro One's Board of Directors. The Company manages net assets by engaging knowledgeable external investment managers who are charged with the responsibility of investing existing funds and new funds (current year's employee and employer contributions) in accordance with the approved SIPP. The performance of the managers is monitored through a governance structure. Increases in net assets are a direct result of investment income generated by investments held by the Pension Plan and contributions to the Pension Plan by eligible employees and by the Company. The main use of net assets is for benefit payments to eligible Pension Plan members.

Pension Plan Asset Mix

At December 31, 2014, the Pension Plan target asset allocations and weighted average asset allocations were as follows:

	Target Allocation (%)	Pension Plan Assets (%)
Equity securities	60.0	60.9
Debt securities	35.0	35.9
Other[1]	5.0	3.2
	100.0	100.0

[1] Other investments include real estate and infrastructure investments.

At December 31, 2014, the Pension Plan held no Hydro One corporate bonds (2013 – $15 million) and $340 million of debt securities of the Province (2013 – $217 million).

Concentrations of Credit Risk

Hydro One evaluated its Pension Plan's asset portfolio for the existence of significant concentrations of credit risk as at December 31, 2014 and 2013. Concentrations that were evaluated include, but are not limited to, investment concentrations in a single entity, concentrations in a type of industry, and concentrations in individual funds. At December 31, 2014 and 2013, there were no significant concentrations (defined as greater than 10% of plan assets) of risk in the Pension Plan's assets.

The Pension Plan manages its counterparty credit risk with respect to bonds by investing in investment-grade and government bonds and with respect to derivative instruments by transacting only with financial institutions rated at least "A+" by Standard and Poor's Rating Services Inc., DBRS Limited, and Fitch Ratings Inc., and "A1" by Moody's Investors Service Inc., and also by utilizing exposure limits to each counterparty and ensuring that exposure is diversified across counterparties. The risk of default on transactions in listed securities is considered minimal, as the trade will fail if either party to the transaction does not meet its obligation.

Fair Value Measurements

The following tables present the Pension Plan assets measured and recorded at fair value on a recurring basis and their level within the fair value hierarchy at December 31, 2014 and 2013:

December 31, 2014 (millions of Canadian dollars)	**Level 1**	**Level 2**	**Level 3**	**Total**
Pooled funds	–	18	142	160
Cash and cash equivalents	166	–	–	166
Short-term securities	–	176	–	176
Real estate	–	–	2	2
Corporate shares – Canadian	1,008	–	–	1,008
Corporate shares – Foreign	2,766	–	–	2,766
Bonds and debentures – Canadian	–	1,799	–	1,799
Bonds and debentures – Foreign	–	211	–	211
Total fair value of plan assets[1]	3,940	2,204	144	6,288

[1] At December 31, 2014, the total fair value of Pension Plan assets excludes $18 million of interest and dividends receivable, and $7 million relating to accruals for pension administration expense.

December 31, 2013 (millions of Canadian dollars)	**Level 1**	**Level 2**	**Level 3**	**Total**
Pooled funds	1	16	117	134
Cash and cash equivalents	150	–	–	150
Short-term securities	–	180	–	180
Real estate	–	–	2	2
Corporate shares – Canadian	943	–	–	943
Corporate shares – Foreign	2,708	–	–	2,708
Bonds and debentures – Canadian	–	1,416	–	1,416
Bonds and debentures – Foreign	–	186	–	186
Total fair value of plan assets[1]	3,802	1,798	119	5,719

[1] At December 31, 2013, the total fair value of Pension Plan assets excludes $19 million of interest and dividends receivable, and $7 million relating to accruals for pension administration expense.

See Note 13 – Fair Value of Financial Instruments and Risk Management for a description of levels within the fair value hierarchy.

Changes in the Fair Value of Financial Instruments Classified in Level 3

The following table summarizes the changes in fair value of financial instruments classified in Level 3 for the years ended December 31, 2014 and 2013. The Pension Plan classifies financial instruments as Level 3 when the fair value is measured based on at least one significant input that is not observable in the markets or due to lack of liquidity in certain markets. The

gains and losses presented in the table below may include changes in fair value based on both observable and unobservable inputs.

Year ended December 31 (millions of Canadian dollars)	**2014**	**2013**
Fair value, beginning of year	119	106
Realized and unrealized gains	30	23
Purchases	23	–
Sales and disbursements	(28)	(10)
Fair value, end of year	144	119

There were no significant transfers between any of the fair value levels during the years ended December 31, 2014 and 2013.

The Company performs sensitivity analysis for fair value measurements classified in Level 3, substituting the unobservable inputs with one or more reasonably possible alternative assumptions. These sensitivity analyses resulted in negligible changes in the fair value of financial instruments classified in this level.

Valuation Techniques Used to Determine Fair Value

Pooled Funds

The pooled fund category mainly consists of private equity and infrastructure investments. Private equity investments represent private equity funds that invest in operating companies that are not publicly traded on a stock exchange. Investment strategies in private equity include limited partnerships in businesses that are characterized by high internal growth and operational efficiencies, venture capital, leveraged buyouts and special situations such as distressed investments. Infrastructure investments represent infrastructure funds that invest in real assets which are not publicly traded on a stock exchange. Investment strategies in infrastructure include limited partnerships in core infrastructure assets focusing on assets that generate stable, long-term cash flows and deliver incremental returns relative to conventional fixed-income investments. Private equity and infrastructure valuations are reported by the fund manager and are based on the valuation of the underlying investments which includes inputs such as cost, operating results, discounted future cash flows and market-based comparable data. Since these valuation inputs are not highly observable, private equity and infrastructure investments have been categorized as Level 3 within pooled funds.

Cash Equivalents

Demand cash deposits held with banks and cash held by the investment managers are considered cash equivalents and are included in the fair value measurements hierarchy as Level 1.

Short-Term Securities

Short-term securities are valued at cost plus accrued interest, which approximates fair value due to their short-term nature. Short-term securities have been categorized as Level 2.

Real Estate

Real estate investments represent private equity investments in holding companies that invest in real estate properties. The investments in the holding companies are valued using net asset values reported by the fund manager. Real estate investments are categorized as Level 3.

Corporate Shares

Corporate shares are valued based on quoted prices in active markets and are categorized as Level 1. Investments denominated in foreign currencies are translated into Canadian currency at year-end rates of exchange.

Bonds and Debentures

Bonds and debentures are presented at published closing trade quotations, and are categorized as Level 2.

16. ENVIRONMENTAL LIABILITIES

The following tables show the movements in environmental liabilities for the years ended December 31, 2014 and 2013:

Year ended December 31, 2014 (millions of Canadian dollars)	**PCB**	**LAR**	**Total**
Environmental liabilities, January 1	201	65	266
Interest accretion	9	2	11
Expenditures	(5)	(13)	(18)
Revaluation adjustment	(33)	13	(20)
Environmental liabilities, December 31	172	67	239
Less: current portion	8	10	18
	164	57	221

Year ended December 31, 2013 (millions of Canadian dollars)	**PCB**	**LAR**	**Total**
Environmental liabilities, January 1	197	52	249
Interest accretion	9	1	10
Expenditures	(2)	(14)	(16)
Revaluation adjustment	(3)	26	23
Environmental liabilities, December 31	201	65	266
Less: current portion	15	12	27
	186	53	239

The following tables show the reconciliation between the undiscounted basis of the environmental liabilities and the amount recognized on the Consolidated Balance Sheets after factoring in the discount rate:

December 31, 2014 (millions of Canadian dollars)	**PCB**	**LAR**	**Total**
Undiscounted environmental liabilities	195	70	265
Less: discounting accumulated liabilities to present value	23	3	26
Discounted environmental liabilities	172	67	239

December 31, 2013 (millions of Canadian dollars)	**PCB**	**LAR**	**Total**
Undiscounted environmental liabilities	237	68	305
Less: discounting accumulated liabilities to present value	36	3	39
Discounted environmental liabilities	201	65	266

At December 31, 2014, the estimated future environmental expenditures were as follows:

(millions of Canadian dollars)	
2015	18
2016	37
2017	36
2018	35
2019	33
Thereafter	106
	265

At December 31, 2014, of the total estimated future environmental expenditures, $195 million relates to PCBs (2013 – $237 million) and $70 million relates to LAR (2013 – $68 million).

Hydro One records a liability for the estimated future expenditures for the contaminated LAR and for the phase-out and destruction of PCB-contaminated mineral oil removed from electrical equipment when it is determined that future environmental remediation expenditures are probable under existing statute or regulation and the amount of the future expenditures can be reasonably estimated.

There are uncertainties in estimating future environmental costs due to potential external events such as changes in legislation or regulations, and advances in remediation technologies. In determining the amounts to be recorded as environmental liabilities, the Company estimates the current cost of completing required work and makes assumptions as to when the future expenditures will actually be incurred, in order to generate future cash flow information. A long-term inflation rate assumption of approximately 2% has been used to express these current cost estimates as estimated future expenditures. Future expenditures have been discounted using factors ranging from approximately 2.3% to 6.3%, depending on the appropriate rate for the period when expenditures are expected to be incurred. All factors used in estimating the Company's environmental liabilities represent management's best estimates of the present value of costs required to meet existing legislation or regulations. However, it is reasonably possible that numbers or volumes of contaminated assets, cost estimates to perform work, inflation assumptions and the assumed pattern of annual cash flows may differ significantly from the Company's current assumptions. In addition, with respect to the PCB environmental liability, the availability of critical resources such as skilled labour and replacement assets and the ability to take maintenance outages in critical facilities may influence the timing of expenditures.

PCBs

The Environment Canada regulations, enacted under the *Canadian Environmental Protection Act,* 1999, govern the management, storage and disposal of PCBs based on certain criteria, including type of equipment, in-use status, and PCB-contamination thresholds. Under current regulations, Hydro One's PCBs have to be disposed of by the end of 2025, with the exception of specifically exempted equipment. Contaminated equipment will generally be replaced, or will be decontaminated by removing PCB-contaminated insulating oil and retro filling with replacement oil that contains PCBs in concentrations of less than 2 ppm.

The Company's best estimate of the total estimated future expenditures to comply with current PCB regulations is $195 million. These expenditures are expected to be incurred over the period from 2015 to 2025. As a result of its annual review of environmental liabilities, the Company recorded a revaluation adjustment in 2014 to reduce the PCB environmental liability by $33 million (2013 – $3 million).

LAR

The Company's best estimate of the total estimated future expenditures to complete its LAR program is $70 million. These expenditures are expected to be incurred over the period from 2015 to 2023. As a result of its annual review of environmental liabilities, the Company recorded a revaluation adjustment in 2014 to increase the LAR environmental liability by $13 million (2013 – $26 million).

17. ASSET RETIREMENT OBLIGATIONS

Hydro One records a liability for the estimated future expenditures for the removal and disposal of asbestos-containing materials installed in some of its facilities and for the decommissioning of specific switching stations located on unowned sites. AROs, which represent legal obligations associated with the retirement of certain tangible long-lived assets, are computed as the present value of the projected expenditures for the future retirement of specific assets and are recognized in the period in which the liability is incurred, if a reasonable estimate of fair value can be made. If the asset remains in service at the recognition date, the present value of the liability is added to the carrying amount of the associated asset in the period the liability is incurred and this additional carrying amount is depreciated over the remaining life of the asset. If an ARO is recorded in respect of an out-of-service asset, the asset retirement cost is charged to results of operations. Subsequent to the initial recognition, the liability is adjusted for any revisions to the estimated future cash flows associated with the ARO, which can occur due to a number of factors including, but not limited to, cost escalation, changes in technology applicable to the assets to be retired, changes in legislation or regulations, as well as for accretion of the liability due to the passage of time

until the obligation is settled. Depreciation expense is adjusted prospectively for any increases or decreases to the carrying amount of the associated asset.

In determining the amounts to be recorded as AROs, the Company estimates the current fair value for completing required work and makes assumptions as to when the future expenditures will actually be incurred, in order to generate future cash flow information. A long-term inflation assumption of approximately 2% has been used to express these current cost estimates as estimated future expenditures. Future expenditures have been discounted using factors ranging from approximately 3.0% to 5.0%, depending on the appropriate rate for the period when expenditures are expected to be incurred. All factors used in estimating the Company's AROs represent management's best estimates of the cost required to meet existing legislation or regulations. However, it is reasonably possible that numbers or volumes of contaminated assets, cost estimates to perform work, inflation assumptions and the assumed pattern of annual cash flows may differ significantly from the Company's current assumptions. AROs are reviewed annually or more frequently if significant changes in regulations or other relevant factors occur. Estimate changes are accounted for prospectively.

At December 31, 2014, Hydro One had recorded AROs of $9 million (2013 – $14 million), consisting of $8 million (2013 – $7 million) related to the estimated future expenditures associated with the removal and disposal of asbestos-containing materials installed in some of its facilities, as well as $1 million (2013 – $7 million) related to the future decommissioning and removal of two switching stations. The amount of interest recorded is nominal.

18. SHARE CAPITAL

Preferred Shares

The Company has 12,920,000 issued and outstanding 5.5% cumulative preferred shares with a redemption value of $25 per share or $323 million total value. The Company is authorized to issue an unlimited number of preferred shares.

The Company's preferred shares are entitled to an annual cumulative dividend of $18 million, or $1.375 per share, which is payable on a quarterly basis. The preferred shares are not subject to mandatory redemption (except on liquidation) but are redeemable in certain circumstances. The shares are redeemable at the option of the Province at the redemption value, plus any accrued and unpaid dividends, if the Province sells a number of the common shares which it owns to the public such that the Province's holdings are reduced to less than 50% of the common shares of the Company. Hydro One may elect, without condition, to pay all or part of the redemption price by issuing additional common shares to the Province. If the Province does not exercise its redemption right, the Company would have the ability to adjust the dividend on the preferred shares to produce a yield that is 0.50% less than the then-current dividend market yield for similarly rated preferred shares. The preferred shares do not carry voting rights, except in limited circumstances, and would rank in priority over the common shares upon liquidation.

These preferred shares have conditions for their redemption that are outside the control of the Company because the Province can exercise its right to redeem in the event of change in ownership without approval of the Company's Board of Directors. Because the conditional redemption feature is outside the control of the Company, the preferred shares are classified outside of equity on the Consolidated Balance Sheets. Management believes that it is not probable that the preferred shares will become redeemable. No adjustment to the carrying value of the preferred shares has been recognized at December 31, 2014. If it becomes probable in the future that the preferred shares will be redeemed, the redemption value would be adjusted.

Common Shares

The Company has 100,000 issued and outstanding common shares. The Company is authorized to issue an unlimited number of common shares.

Common share dividends are declared at the sole discretion of the Hydro One Board of Directors, and are recommended by management based on results of operations, maintenance of the deemed regulatory capital structure, financial conditions, cash requirements, and other relevant factors, such as industry practice and Shareholder expectations.

Earnings per Share

Basic and diluted earnings per share have been calculated on the basis of net income attributable to the Shareholder of Hydro One and the weighted average number of common shares outstanding during the year.

19. DIVIDENDS

In 2014, preferred share dividends in the amount of $18 million (2013 – $18 million) and common share dividends in the amount of $269 million (2013 – $200 million) were declared.

20. RELATED PARTY TRANSACTIONS

Hydro One is owned by the Province. The OEFC, IESO, OPA, Ontario Power Generation Inc. (OPG) and the OEB are related parties to Hydro One because they are controlled or significantly influenced by the Province.

The Province

During 2014, Hydro One paid dividends to the Province totalling $287 million (2013 – $218 million).

In November 2014, the Company redeemed the $250 million Province of Ontario Floating-Rate Notes held as a long-term investment. These notes were originally purchased in January 2010 with a maturity date of November 19, 2014.

IESO

In 2014, Hydro One purchased power in the amount of $2,601 million (2013 – $2,477 million) from the IESO-administered electricity market.

Hydro One receives revenues for transmission services from the IESO, based on OEB-approved uniform transmission rates. Transmission revenues for 2014 include $1,556 million (2013 – $1,509 million) related to these services.

Hydro One receives amounts for rural rate protection from the IESO. Distribution revenues for 2014 include $127 million (2013 – $127 million) related to this program.

Hydro One also receives revenues related to the supply of electricity to remote northern communities from the IESO. Distribution revenues for 2014 include $32 million (2013 – $33 million) related to these services.

OPA

The OPA funds substantially all of the Company’s conservation and demand management programs. The funding includes program costs, incentives, and management fees. In 2014, Hydro One received $33 million (2013 – $34 million) from the OPA related to these programs.

OPG

In 2014, Hydro One purchased power in the amount of $23 million (2013 – $15 million) from OPG.

Hydro One has service level agreements with OPG. These services include field, engineering, logistics and telecommunications services. In 2014, revenues related to the provision of construction and equipment maintenance services with respect to these service level agreements were $12 million (2013 – $9 million), primarily for the Transmission Business. Operation, maintenance and administration costs in 2014 related to the purchase of services with respect to these service level agreements were $1 million (2013 – $1 million).

OEFC

In 2014, Hydro One made payments in lieu of corporate income taxes to the OEFC totalling $86 million (2013 – $138 million).

In 2014, Hydro One purchased power in the amount of $9 million (2013 – $8 million) from power contracts administered by the OEFC.

Hydro One pays a $5 million annual fee to the OEFC for indemnification against adverse claims in excess of $10 million paid by the OEFC with respect to certain of Ontario Hydro's businesses transferred to Hydro One on April 1, 1999.

PILs and payments in lieu of property taxes are paid to the OEFC.

OEB

Under the *Ontario Energy Board Act, 1998*, the OEB is required to recover all of its annual operating costs from gas and electricity distributors and transmitters. In 2014, Hydro One incurred $12 million (2013 – $12 million) in OEB fees.

Sales to and purchases from related parties occur at normal market prices or at a proxy for fair value based on the requirements of the OEB's Affiliate Relationships Code. Outstanding balances at period end are interest free and settled in cash.

The amounts due to and from related parties as a result of the transactions referred to above are as follows:

December 31 (millions of Canadian dollars)	**2014**	**2013**
Due from related parties	224	197
Due to related parties[1]	(227)	(230)
Investment	–	251

[1] Included in due to related parties at December 31, 2014 are amounts owing to the IESO in respect of power purchases of $214 million (2013 – $217 million).

21. CONSOLIDATED STATEMENTS OF CASH FLOWS

The changes in non-cash balances related to operations consist of the following:

Year ended December 31 (millions of Canadian dollars)	**2014**	**2013**
Accounts receivable	(93)	(78)
Due from related parties	(27)	(43)
Prepaid expenses and other assets	(13)	(5)
Accounts payable	39	13
Accrued liabilities	(35)	71
Due to related parties	(3)	(31)
Accrued interest	–	5
Long-term accounts payable and other liabilities	(3)	(5)
Post-retirement and post-employment benefit liability	80	84
	(55)	11

Capital Expenditures

The following table illustrates the reconciliation between investments in property, plant and equipment and the amount presented in the Consolidated Statements of Cash Flows after factoring in capitalized depreciation and the net change in related accruals:

Year ended December 31 (millions of Canadian dollars)	**2014**	**2013**
Capital investments in property, plant and equipment	(1,511)	(1,312)
Capitalized depreciation and net change in accruals included in capital investments in property, plant and equipment	30	4
Capital expenditures – property, plant and equipment	(1,481)	(1,308)

The following table illustrates the reconciliation between investments in intangible assets and the amount presented in the Consolidated Statements of Cash Flows after factoring in the net change in related accruals:

Year ended December 31 (millions of Canadian dollars)	**2014**	**2013**
Capital investments in intangible assets	(19)	(82)
Net change in accruals included in capital investments in intangible assets	(4)	3
Capital expenditures – intangible assets	(23)	(79)

Supplementary Information

Year ended December 31 (millions of Canadian dollars)	**2014**	**2013**
Net interest paid	412	395
PILs	86	138

22. CONTINGENCIES

Legal Proceedings

Hydro One is involved in various lawsuits, claims and regulatory proceedings in the normal course of business. In the opinion of management, the outcome of such matters will not have a material adverse effect on the Company's consolidated financial position, results of operations or cash flows.

Transfer of Assets

The transfer orders by which the Company acquired certain of Ontario Hydro's businesses as of April 1, 1999 did not transfer title to some assets located on Reserves (as defined in the *Indian Act* (Canada)). Currently, the OEFC holds these assets. Under the terms of the transfer orders, the Company is required to manage these assets until it has obtained all consents necessary to complete the transfer of title of these assets to itself. The Company cannot predict the aggregate amount that it may have to pay, either on an annual or one-time basis, to obtain the required consents. In 2014, the Company paid approximately $1 million (2013 – $2 million) in respect of these consents. If the Company cannot obtain the required consents, the OEFC will continue to hold these assets for an indefinite period of time. If the Company cannot reach a satisfactory settlement, it may have to relocate these assets to other locations at a cost that could be substantial or, in a limited number of cases, to abandon a line and replace it with diesel-generation facilities. The costs relating to these assets could have a material adverse effect on the Company's results of operations if the Company is not able to recover them in future rate orders.

23. COMMITMENTS

Outsourcing Agreements

The current agreement with Inergi LP (Inergi), an affiliate of Capgemini Canada Inc., expires on February 28, 2015. On November 28, 2014, Hydro One entered into an agreement with Inergi (Inergi Agreement), the service provider selected through a competitive procurement process which began in 2013, for second-generation back office and IT outsourcing services for a term of 58 months, commencing March 1, 2015 to December 31, 2019. Under the agreement, Inergi will provide Hydro One with settlements, source to pay services, pay operations services, information technology and finance and accounting services. Coincident with the conclusion of negotiations on the Inergi Agreement, Hydro One reached agreement with Inergi for the provision of second-generation customer service operations outsourcing services for a fixed period of three years beginning March 1, 2015 to February 28, 2018.

In September 2014, Hydro One entered into an agreement with Brookfield Johnson Controls Canada LP (Brookfield) for facilities management services for a term of ten years, from January 1, 2015 to December 31, 2024, with the option to renew for an additional term of three years. Under the agreement, Brookfield will provide us with facilities management and execution of certain capital projects as deemed required by the Company. The Brookfield Agreement has a value of up to approximately $658 million over the ten-year term of the agreement, including the facilities management portion of the contract, plus a variable amount of capital work depending on the needs that may arise as determined by the Company, with no minimum capital work guarantee. The agreement also includes a fixed management fee of approximately $2 million for each year of the term.

At December 31, 2014, the annual commitments under the outsourcing agreements were as follows: 2015 – $179 million; 2016 – $146 million; 2017 – $145 million; 2018 – $113 million; 2019 – $105 million; and thereafter – $13 million.

Prudential Support

Purchasers of electricity in Ontario, through the IESO, are required to provide security to mitigate the risk of their default based on their expected activity in the market. As at December 31, 2014, the Company provided prudential support to the IESO on behalf of its subsidiaries using parental guarantees of $330 million (2013 – $325 million), and on behalf of two distributors using guarantees of $1 million (2013 – $1 million). In addition, as at December 31, 2014, the Company has provided letters of credit in the amount of $8 million (2013 – $21 million) to the IESO. The IESO could draw on these guarantees and/or letters of credit if these subsidiaries or distributors fail to make a payment required by a default notice issued by the IESO. The maximum potential payment is the face value of any letters of credit plus the amount of the parental guarantees.

Retirement Compensation Arrangements

Bank letters of credit have been issued to provide security for the Company's liability under the terms of a trust fund established pursuant to the supplementary pension plan for eligible employees of Hydro One. The supplementary pension plan trustee is required to draw upon these letters of credit if Hydro One is in default of its obligations under the terms of this plan. Such obligations include the requirement to provide the trustee with an annual actuarial report as well as letters of credit sufficient to secure the Company's liability under the plan, to pay benefits payable under the plan and to pay the letter of credit fee. The maximum potential payment is the face value of the letters of credit. At December 31, 2014, Hydro One had letters of credit of $126 million (2013 – $127 million) outstanding relating to retirement compensation arrangements.

Operating Leases

Hydro One is committed as lessee to irrevocable operating lease contracts for buildings used in administrative and service-related functions and storing telecommunications equipment. These leases have a typical term of between three and five years, but several leases have lesser or greater terms to address special circumstances and/or opportunities. Renewal options, which are generally prevalent in most leases, have similar terms of three to five years. All leases include a clause to enable upward revision of the rental charge on an annual basis or on renewal according to prevailing market conditions or pre-established rents. There are no restrictions placed upon Hydro One by entering into these leases. Hydro One Networks and Hydro One Telecom are the principal entities concerned.

During the year ended December 31, 2014, the Company made lease payments totalling $11 million (2013 – $11 million). At December 31, 2014, the future minimum lease payments under non-cancellable operating leases were as follows: 2015 – $7 million; 2016 – $10 million; 2017 – $9 million; 2018 – $7 million; 2019 – $3 million; and thereafter – $9 million.

24. SEGMENTED REPORTING

Hydro One has three reportable segments:

- The Transmission Business, which comprises the core business of providing electricity transportation and connection services, is responsible for transmitting electricity throughout the Ontario electricity grid;
- The Distribution Business, which comprises the core business of delivering and selling electricity to customers; and
- Other, which includes certain corporate activities and the operations of the telecommunications business.

The designation of segments has been based on a combination of regulatory status and the nature of the products and services provided. Operating segments of the Company are determined based on information used by the chief operating decision maker in deciding how to allocate resources and evaluate the performance of each of the segments. The Company evaluates segment performance based on income before financing charges and provision for PILs from continuing operations (excluding certain allocated corporate governance costs).

The accounting policies followed by the segments are the same as those described in the summary of significant accounting policies (see Note 2 – Significant Accounting Policies). Segment information on the above basis is as follows:

Year ended December 31, 2014 (millions of Canadian dollars)	**Transmission**	**Distribution**	**Other**	**Consolidated**
Revenues	1,588	4,903	57	6,548
Purchased power	–	3,419	–	3,419
Operation, maintenance and administration	394	742	56	1,192
Depreciation and amortization	346	367	9	722
Income (loss) before financing charges and provision for PILs	848	375	(8)	1,215
Capital investments	845	680	5	1,530

Year ended December 31, 2013 (millions of Canadian dollars)	**Transmission**	**Distribution**	**Other**	**Consolidated**
Revenues	1,529	4,484	61	6,074
Purchased power	–	3,020	–	3,020
Operation, maintenance and administration	375	672	59	1,106
Depreciation and amortization	327	340	9	676
Income (loss) before financing charges and provision for PILs	827	452	(7)	1,272
Capital investments	714	673	7	1,394

Total Assets by Segment:

December 31 (millions of Canadian dollars)	**2014**	**2013**
Transmission	12,540	11,846
Distribution	9,805	8,805
Other	205	974
Total assets	22,550	21,625

All revenues, costs and assets, as the case may be, are earned, incurred or held in Canada.

25. SUBSEQUENT EVENT

On February 11, 2015, preferred share dividends in the amount of $4 million and common share dividends in the amount of $25 million were declared.

HYDRO ONE NETWORKS INC.

DISTRIBUTION BUSINESS

FINANCIAL STATEMENTS

DECEMBER 31, 2015

HYDRO ONE NETWORKS INC.
DISTRIBUTION BUSINESS
INDEPENDENT AUDITORS' REPORT

To the Directors of Hydro One Networks Inc.

We have audited the accompanying carve-out financial statements of the Distribution Business (a business of Hydro One Networks Inc.), which comprise the carve-out balance sheet as at December 31, 2015, the carve-out statements of operations and comprehensive income, and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information. The carve-out financial statements have been prepared by management in accordance with the basis of accounting in Note 2 to the carve-out financial statements.

Management's Responsibility for the Carve-out Financial Statements

Management of Hydro One Networks Inc. is responsible for the preparation of these carve-out financial statements in accordance with the basis of accounting in Note 2 to the carve-out financial statements; this includes determining that the basis of accounting is an acceptable basis for the preparation of these carve-out financial statements in the circumstances, and for such internal control as management determines is necessary to enable the preparation of carve-out 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 carve-out 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 carve-out financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the carve-out financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the carve-out financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation of the carve-out 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 carve-out 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 carve-out financial statements as at and for the year ended December 31, 2015 are prepared, in all material respects, in accordance with the basis of accounting in Note 2 to the carve-out financial statements.

Basis of Accounting and Restriction of Use

Without modifying our opinion, we draw attention to Note 2 to the carve-out financial statements, which describe the basis of preparation used in these carve-out financial statements. In particular, in preparing the carve-out financial statements, long-term debt, shared functions and service costs, and income taxes have been allocated to the Distribution Business (a business of Hydro One Networks Inc.) using the method of allocation described in Note 2 to the carve-out financial statements. As a result, the carve-out financial statements may not necessarily be identical to the balance sheet, results of operations and cash flows that would have resulted had the Distribution Business (a business of Hydro One Networks Inc.) historically operated on a stand-alone basis. The carve-out financial statements are prepared to assist Hydro One Networks Inc. to comply with its reporting requirements of the Ontario Energy Board. As a result, the carve-out financial statements may not be suitable for another purpose.

Our report is intended solely for the Directors of Hydro One Networks Inc. and the Ontario Energy Board and should not be used by parties other than Hydro One Networks Inc. or the Ontario Energy Board.

KPMG LLP

Chartered Professional Accountants, Licensed Public Accountants

Toronto, Canada
April 26, 2016

HYDRO ONE NETWORKS INC.
DISTRIBUTION BUSINESS
STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME
For the years ended December 31, 2015 and 2014

Year ended December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Revenues		
Energy sales	4,305	4,176
Rural rate protection *(Note 20)*	125	126
Other	45	38
	4,475	4,340
Costs		
Purchased power *(Note 20)*	3,087	2,979
Operation, maintenance and administration *(Note 20)*	574	675
Depreciation and amortization *(Note 5)*	360	347
	4,021	4,001
Income before financing charges and income taxes	**454**	**339**
Financing charges *(Notes 6, 20)*	146	147
Income before income taxes	**308**	**192**
Income taxes *(Notes 7, 20)*	51	3
Net income	**257**	**189**
Other comprehensive income	–	–
Comprehensive income	**257**	**189**

See accompanying notes to Financial Statements.

HYDRO ONE NETWORKS INC.
DISTRIBUTION BUSINESS
BALANCE SHEETS
At December 31, 2015 and 2014

December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Assets		
Current assets:		
Accounts receivable (net of allowance for doubtful accounts – $59; 2014 – $64) *(Notes 8, 20)*	776	985
Regulatory assets *(Note 11)*	28	11
Materials and supplies	4	7
Deferred income tax assets *(Note 7)*	10	9
Derivative instruments *(Note 13)*	–	1
Other	8	13
	826	1,026
Property, plant and equipment *(Note 9)*:		
Property, plant and equipment in service	10,150	9,426
Less: accumulated depreciation	3,794	3,503
	6,356	5,923
Construction in progress	254	326
Future use land, components and spares	53	49
	6,663	6,298
Other long-term assets:		
Regulatory assets *(Note 11)*	829	789
Intangible assets (net of accumulated amortization – $147; 2014 – $179) *(Note 10)*	257	197
Goodwill	113	73
Deferred debt costs	13	13
Other	1	3
	1,213	1,075
Total assets	**8,702**	**8,399**

See accompanying notes to Financial Statements.

HYDRO ONE NETWORKS INC.
DISTRIBUTION BUSINESS
BALANCE SHEETS (continued)
At December 31, 2015 and 2014

December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Liabilities		
Current liabilities:		
Inter-company demand facility *(Notes 13, 14, 20)*	640	225
Accounts payable	59	65
Accrued liabilities *(Notes 7, 15, 16, 20)*	597	605
Accrued interest *(Note 20)*	36	38
Regulatory liabilities *(Note 11)*	10	8
Long-term debt payable within one year *(Notes 12, 13, 14, 20)*	200	221
	1,542	1,162
Long-term debt *(Notes 12, 13, 14, 20)*	2,991	3,161
Other long-term liabilities:		
Post-retirement and post-employment benefit liability *(Note 15)*	862	844
Deferred income tax liabilities *(Note 7)*	426	388
Environmental liabilities *(Note 16)*	99	124
Regulatory liabilities *(Note 11)*	83	110
Net unamortized debt premiums	9	10
Asset retirement obligations *(Note 17)*	4	4
Long-term accounts payable and other liabilities	7	1
	1,490	1,481
Total liabilities	**6,023**	**5,804**
Contingencies and commitments (Notes 22, 23)		
Subsequent Events (Note 24)		
Excess of assets over liabilities *(Notes 14, 18)*	2,679	2,595
Total liabilities and excess of assets over liabilities	**8,702**	**8,399**

See accompanying notes to Financial Statements.

On behalf of the Board of Directors:

George Cooke
Director

Mayo Schmidt
Director

HYDRO ONE NETWORKS INC.
DISTRIBUTION BUSINESS
STATEMENTS OF CASH FLOWS
For the years ended December 31, 2015 and 2014

Year ended December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Operating activities		
Net income	257	189
Environmental expenditures	(11)	(10)
Adjustments for non-cash items:		
Depreciation and amortization (excluding removal costs)	301	295
Regulatory assets and liabilities	(70)	(58)
Deferred income taxes	(12)	15
Other	3	1
Changes in non-cash balances related to operations *(Note 21)*	240	(80)
Net cash from operating activities	708	352
Financing activities		
Long-term debt issued	30	243
Long-term debt retired	(220)	(175)
Payments to Hydro One Inc. to finance dividends	(240)	(59)
Other	(3)	(1)
Net cash from (used in) financing activities	(433)	8
Investing activities		
Capital expenditures *(Note 21)*		
Property, plant and equipment	(634)	(614)
Intangible assets	(24)	(14)
Transfer of Norfolk Power	(33)	–
Other	1	(4)
Net cash used in investing activities	(690)	(632)
Net change in inter-company demand facility	(415)	(272)
Inter-company demand facility, beginning of year	(225)	47
Inter-company demand facility, end of year	**(640)**	**(225)**

See accompanying notes to Financial Statements.

1. DESCRIPTION OF THE BUSINESS

Hydro One Inc. (Hydro One) was incorporated on December 1, 1998, under the Business Corporations Act (Ontario) and was wholly owned by the Province of Ontario (the Province) until October 31, 2015. On October 31, 2015, Hydro One Limited, a wholly owned subsidiary of the Province, acquired all issued and outstanding shares of Hydro One from the Province. The principal businesses of Hydro One are the transmission and distribution of electricity to customers within Ontario.

Hydro One Networks Inc. (Hydro One Networks or the Company) was incorporated on March 4, 1999 under the *Business Corporations Act* (Ontario) and is a wholly-owned subsidiary of Hydro One. The Company owns and operates Hydro One's regulated transmission and distribution businesses. The regulated distribution business (Distribution Business) operates a low-voltage electrical distribution network that distributes electricity from the transmission system, or directly from generators, to customers within Ontario. The Distribution Business is regulated by the Ontario Energy Board (OEB).

2. SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting

These Financial Statements are prepared and presented in accordance with the accounting policies summarized below and in Canadian dollars. These policies are consistent with United States (US) Generally Accepted Accounting Principles (GAAP), with the exception that business combinations of entities under common control have been accounted for as of the date of the transfer, such that (1) the Financial Statements were not prepared as though the transfer of entities under common control had occurred at the beginning of the year in which the transfer occurred and (2) the comparative year information has not been retrospectively adjusted.

These Financial Statements have been prepared for the specific use of the OEB. As a result, the financial statements may not be suitable for any other purpose. Consolidated Financial Statements of Hydro One for the year ended December 31, 2015 have been prepared and are publicly available.

These Financial Statements have been prepared on a carve-out basis to provide the financial position, results of operations and cash flows of the Company's regulated Distribution Business on a basis approved by the OEB. The Financial Statements are considered by management to be a reasonable representation, prepared on a rational, systematic and consistent basis, of the financial results of the Company's Distribution Business. As a result of this basis of accounting, these Financial Statements may not necessarily be identical to the financial position and results of operations that would have resulted had the Distribution Business historically operated on a stand-alone basis.

The Financial Statements have been constructed primarily through specific identification of assets, liabilities (other than debt), revenues and expenses that relate to the Distribution Business. The Company's long-term debt is allocated based on the respective borrowing requirements of the Company's transmission and distribution businesses. A portion of the Company's shared functions and services costs is allocated to the Distribution Business on a fully allocated-cost basis, consistent with OEB-approved independent studies. Income tax expense has been recorded at effective rates based on income taxes as reported in the Statements of Operations and Comprehensive Income as though the Distribution Business was a separate taxpaying entity. However, income taxes paid and the deferred tax asset recognized by the Company in relation to the Company losing its exemption from tax under the Federal Tax Regime have been excluded as they represent transactions that are not included in the rate-setting process of the Distribution Business. Certain other amounts presented in these Financial Statements represent allocations subject to review and approval by the OEB.

Hydro One Networks performed an evaluation of subsequent events through to April 26, 2016, the date these Financial Statements were available to be issued, to determine whether any events or transactions warranted recognition and disclosure in these financial statements. See Note 24 – Subsequent Events.

Use of Management Estimates

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues, expenses, gains and losses during the reporting periods. Management evaluates these estimates on an ongoing basis based upon historical experience, current conditions, and assumptions believed to be reasonable at the time the assumptions are made with any adjustments being recognized in results of operations in the period they arise. Significant estimates relate to regulatory assets and regulatory liabilities, environmental liabilities, post-retirement and post-employment benefits, asset retirement obligations (AROs), goodwill and asset impairments, contingencies, unbilled revenues, allowance for doubtful accounts, derivative instruments, and deferred income tax assets and liabilities. Actual results may differ significantly from these estimates, which may be impacted by future decisions made by the OEB.

Rate Setting

The OEB has approved the use of US GAAP for rate setting and regulatory accounting and reporting by Hydro One Networks' Distribution Business.

On March 12, 2015, the OEB issued a Decision and Rate Order approving a revenue requirement of $1,326 million for 2015, $1,430 million for 2016 and $1,486 million for 2017. The revenue requirements for 2016 and 2017 are estimates that may change based on 2016 and 2017 Rate Orders. On April 23, 2015, the Final Rate Order for 2015 rates was approved by the OEB.

Regulatory Accounting

The OEB has the general power to include or exclude revenues, costs, gains or losses in the rates of a specific period, resulting in a change in the timing of accounting recognition from that which would have been applied in an unregulated company. Such change in timing involves the application of rate-regulated accounting, giving rise to the recognition of regulatory assets and liabilities. The Distribution Business' regulatory assets represent certain amounts receivable from future customers and costs that have been deferred for accounting purposes because it is probable that they will be recovered in future rates. In addition, the Distribution Business has recorded regulatory liabilities that generally represent amounts that are refundable to future customers. The Distribution Business continually assesses the likelihood of recovery of each of its regulatory assets and continues to believe that it is probable that the OEB will factor its regulatory assets and liabilities into the setting of future rates. If, at some future date, the Distribution Business judges that it is no longer probable that the OEB will include a regulatory asset or liability in setting future rates, the appropriate carrying amount will be reflected in results of operations in the period that the assessment is made.

Revenue Recognition

Distribution revenues attributable to the delivery of electricity are based on OEB-approved distribution rates and are recognized on an accrual basis and include billed and unbilled revenues. Billed revenues are based on electricity delivered as measured from customer meters. Unbilled revenues are based on an estimate of electricity delivered determined by historical trends of consumption and are estimated at the end of each month. The unbilled revenue estimate is affected by energy consumption, weather, and changes in the composition of customer classes. Distribution revenue also includes an amount relating to rate protection for rural, residential and remote customers, which is received from the Independent Electricity System Operator (IESO) based on a standardized customer rate that is approved by the OEB. Revenues are recorded net of indirect taxes.

Accounts Receivable and Allowance for Doubtful Accounts

Billed accounts receivable are recorded at the invoiced amount, net of allowance for doubtful accounts. Unbilled accounts receivable are recorded at their estimated value. Overdue amounts related to regulated billings bear interest at OEB-approved rates. The allowance for doubtful accounts reflects the Distribution Business' best estimate of losses on billed accounts receivable balances. The Distribution Business estimates the allowance for doubtful accounts on customer receivables by applying internally developed loss rates to the outstanding receivable balances by aging category. Loss rates applied to the accounts receivable balances are based on historical overdue balances, customer payments and write-offs. Accounts receivable are written-off against the allowance when they are deemed uncollectible. The existing allowance for doubtful accounts will continue to be affected by changes in volume, prices and economic conditions.

Income Taxes

On October 31, 2015, Hydro One Networks ceased to be exempt from tax under the *Income Tax Act* (Canada) and the *Taxation Act*, 2007 (Ontario) (Federal Tax Regime). Prior to that date, Hydro One Networks was required to make payments in lieu of corporate income taxes (PILs) to the Ontario Electricity Financial Corporation (OEFC) under the *Electricity Act*, 1998 (Ontario) (PILs Regime). These payments were calculated in accordance with the rules for computing income and other relevant amounts contained in the *Income Tax Act* (Canada) and the *Taxation Act, 2007* (Ontario), as modified by the *Electricity Act, 1998*, and related regulations. Upon exiting the PILs Regime, Hydro One is required to make corporate income tax payments to the Canada Revenue Agency (CRA) under the Federal Tax Regime.

Current and deferred income taxes are computed based on the tax rates and tax laws enacted as at the balance sheet date. Tax benefits associated with income tax positions taken, or expected to be taken, in a tax return are recorded only when the "more-likely-than-not" recognition threshold is satisfied and are measured at the largest amount of benefit that has a greater than 50% likelihood of being realized upon settlement. Management evaluates each position based solely on the technical merits and facts and circumstances of the position, assuming the position will be examined by a taxing authority having full knowledge of all relevant information. Significant management judgment is required to determine recognition thresholds and the related amount of tax benefits to be recognized in the Financial Statements. Management re-evaluates tax positions each period in which new information about recognition or measurement becomes available.

Deferred Income Taxes

Deferred income taxes are provided for using the liability method. Deferred income taxes are recognized based on the estimated future tax consequences attributable to temporary differences between the carrying amount of assets and liabilities in the Financial Statements and their corresponding tax bases.

Deferred income tax liabilities are generally recognized on all taxable temporary differences. Deferred tax assets are recognized to the extent that it is more-likely-than-not that these assets will be realized from taxable income available against which deductible temporary differences can be utilized.

Deferred income taxes are calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realized, based on the tax rates and tax laws that have been enacted as at the balance sheet date. Deferred income taxes that are not included in the rate-setting process are charged or credited to the Statements of Operations and Comprehensive Income.

If management determines that it is more-likely-than-not that some or all of a deferred income tax asset will not be realized, a valuation allowance is recorded against the deferred income tax asset to report the net balance at the amount expected to be realized. Previously unrecognized deferred income tax assets are reassessed at each balance sheet date and are recognized to the extent that it has become more-likely-than-not that the tax benefit will be realized.

The Company records regulatory assets and liabilities associated with deferred income taxes that will be included in the rate-setting process.

The Company uses the flow-through method to account for investment tax credits (ITCs) earned on eligible scientific research and experimental development expenditures, and apprenticeship job creation. Under this method, only non-refundable ITCs are recognized as a reduction to income tax expense.

Inter-company Demand Facility

Hydro One maintains pooled bank accounts for its use and for the use of its subsidiaries, and implicitly, by the regulated businesses of its subsidiaries. The balance in the inter-company demand facility represents the cumulative net effect of all deposits and withdrawals made by the Distribution Business to and from the pooled bank accounts. Interest is earned on positive inter-company balances based on the average of the bankers' acceptance rate at the beginning and end of the month, less 0.02%. Interest is charged on overdraft inter-company balances based on the same bankers' acceptance rate, plus 0.15%.

Materials and Supplies

Materials and supplies represent consumables, small spare parts and construction materials held for internal construction and maintenance of property, plant and equipment. These assets are carried at average cost less any impairments recorded.

Property, Plant and Equipment

Property, plant and equipment is recorded at original cost, net of customer contributions, and any accumulated impairment losses. The cost of additions, including betterments and replacement asset components, is included on the Balance Sheets as property, plant and equipment.

The original cost of property, plant and equipment includes direct materials, direct labour (including employee benefits), contracted services, attributable capitalized financing costs, asset retirement costs, and direct and indirect overheads that are related to the capital project or program. Indirect overheads include a portion of corporate costs such as finance, treasury, human resources, information technology and executive costs. Overhead costs, including corporate functions and field services costs, are capitalized on a fully allocated basis, consistent with an OEB-approved methodology.

Property, plant and equipment in service consists of distribution, communication, administration and service assets and land easements. Property, plant and equipment also includes future use assets, such as land, major components and spare parts, and capitalized project development costs associated with deferred capital projects.

Distribution

Distribution assets include assets related to the distribution of low-voltage electricity, including lines, poles, switches, transformers, protective devices and metering systems.

Communication

Communication assets include fibre optic and microwave radio systems, optical ground wire, towers, telephone equipment and associated buildings.

Administration and Service

Administration and service assets include administrative buildings, personal computers, transport and work equipment, tools and other minor assets.

Intangible Assets

Intangible assets separately acquired or internally developed are measured on initial recognition at cost, which comprises purchased software, direct labour (including employee benefits), consulting, engineering, overheads and attributable capitalized financing charges. Following initial recognition, intangible assets are carried at cost, net of any accumulated amortization and accumulated impairment losses. The Distribution Business' intangible assets primarily represent major administrative computer applications.

Capitalized Financing Costs

Capitalized financing costs represent interest costs attributable to the construction of property, plant and equipment or development of intangible assets. The financing cost of attributable borrowed funds is capitalized as part of the acquisition cost of such assets. The capitalized portion of financing costs is a reduction to financing charges recognized in the Statements of Operations and Comprehensive Income. Capitalized financing costs are calculated using the Company's weighted average effective cost of debt.

Construction and Development in Progress

Construction and development in progress consists of the capitalized cost of constructed assets that are not yet complete and which have not yet been placed in service.

Depreciation and Amortization

The cost of property, plant and equipment and intangible assets is depreciated or amortized on a straight-line basis based on the estimated remaining service life of each asset category, except for transport and work equipment, which is depreciated on a declining balance basis.

Hydro One periodically initiates an external independent review of its property, plant and equipment and intangible asset depreciation and amortization rates, as required by the OEB. Any changes arising from OEB approval of such a review are implemented on a remaining service life basis, consistent with their inclusion in electricity rates. The last review resulted in

changes to rates effective January 1, 2015. A summary of average service lives and depreciation and amortization rates for the various classes of assets is included below:

	Average	Rate (%)	
	Service Life	Range	Average
Distribution	47 years	1% – 2%	2%
Communication	8 years	1% – 15%	12%
Administration and service	18 years	1% – 7%	6%

The cost of intangible assets is included primarily within the administration and service classification above. Amortization rate for computer applications software assets is 10%.

In accordance with group depreciation practices, the original cost of property, plant and equipment, or major components thereof, and intangible assets that are normally retired, is charged to accumulated depreciation and amortization, with no gain or loss being reflected in results of operations. Where a disposition of property, plant and equipment occurs through sale, a gain or loss is calculated based on proceeds and such gain or loss is included in depreciation expense. Depreciation expense also includes the costs incurred to remove property, plant and equipment where no ARO has been recorded.

Goodwill

Goodwill represents the cost of acquired local distribution companies that is in excess of the fair value of the net identifiable assets acquired at the acquisition date. Goodwill is not included in rate base.

Goodwill is evaluated for impairment on an annual basis, or more frequently if circumstances require. The Company performs a qualitative assessment to determine whether it is more-likely-than-not that the fair value of the applicable reporting unit is less than its carrying amount. If the Company determines, as a result of its qualitative assessment, that it is not more-likely-than-not that the fair value of the applicable reporting unit is less than its carrying amount, no further testing is required. If the Company determines, as a result of its qualitative assessment, that it is more-likely-than-not that the fair value of the applicable reporting unit is less than its carrying amount, a goodwill impairment assessment is performed using a two-step, fair value-based test. The first step compares the fair value of the applicable reporting unit to its carrying amount, including goodwill. If the carrying amount of the applicable reporting unit exceeds its fair value, a second step is performed. The second step requires an allocation of fair value to the individual assets and liabilities using purchase price allocation in order to determine the implied fair value of goodwill. If the implied fair value of goodwill is less than the carrying amount, an impairment loss is recorded as a reduction to goodwill and as a charge to results of operations.

For the year ended December 31, 2015, based on the qualitative assessment performed as at September 30, 2015, the Company has determined that it is not more-likely-than-not that the fair value of each applicable reporting unit assessed is less than its carrying amount. As a result, no further testing was performed, and the Company has concluded that goodwill was not impaired at December 31, 2015.

Long-Lived Asset Impairment

When circumstances indicate the carrying value of long-lived assets may not be recoverable, the Company evaluates whether the carrying value of such assets, excluding goodwill, has been impaired. For such long-lived assets, the Company evaluates whether impairment may exist by estimating future estimated undiscounted cash flows expected to result from the use and eventual disposition of the asset. When alternative courses of action to recover the carrying amount of a long-lived asset are under consideration, a probability-weighted approach is used to develop estimates of future undiscounted cash flows. If the carrying value of the long-lived asset is not recoverable based on the estimated future undiscounted cash flows, an impairment loss is recorded, measured as the excess of the carrying value of the asset over its fair value. As a result, the asset's carrying value is adjusted to its estimated fair value.

The carrying costs of most of the Distribution Business' long-lived assets are included in rate base where they earn an OEB-approved rate of return. Asset carrying values and the related return are recovered through approved rates. As a result, such assets are only tested for impairment in the event that the OEB disallows recovery, in whole or in part, or if such a disallowance is judged to be probable. As at December 31, 2015 and 2014, no asset impairment had been recorded.

Costs of Arranging Debt Financing

For financial liabilities classified as other than held-for-trading, the Company defers its proportionate share of the relevant Hydro One external transaction costs related to obtaining debt financing and presents such amounts as deferred debt costs on the Balance Sheets. Deferred debt costs are amortized over the contractual life of the related debt on an effective-interest basis and the amortization is included within financing charges in the Statements of Operations and Comprehensive Income. Transaction costs for items classified as held-for-trading are expensed immediately.

Comprehensive Income

Comprehensive income is comprised of net income and other comprehensive income (OCI). OCI and net income are presented in a single continuous Statement of Operations and Comprehensive Income.

Financial Assets and Liabilities

All financial assets and liabilities are classified into one of the following five categories: held-to-maturity investments; loans and receivables; held-for-trading; other liabilities; or available-for-sale. Financial assets and liabilities classified as held-for-trading are measured at fair value. All other financial assets and liabilities are measured at amortized cost, except accounts receivable which are measured at the lower of cost or fair value. Accounts receivable are classified as loans and receivables. The Company considers the carrying amount of accounts receivable to be a reasonable estimate of fair value because of the short time to maturity of these instruments. Provisions for impaired accounts receivable are recognized as adjustments to the allowance for doubtful accounts and are recognized when there is objective evidence that the Company will not be able to collect amounts according to the original terms. All financial instrument transactions are recorded at trade date.

Derivative instruments are measured at fair value. Gains and losses from fair valuation are included within financing charges in the period in which they arise. Hydro One Networks determines the classification of its financial assets and liabilities at the date of initial recognition. The Company designates certain of its financial assets and liabilities to be held at fair value, when it is consistent with its risk management policy disclosed in Note 13 – Fair Value of Financial Instruments and Risk Management.

Derivative Instruments and Hedge Accounting

Hydro One closely monitors the risks associated with changes in interest rates on its operations and, where appropriate, uses various derivative instruments to hedge these risks. Certain of these derivative instruments qualify for hedge accounting and are designated as accounting hedges, while others either do not qualify as hedges or have not been designated as hedges (hereinafter referred to as undesignated contracts) as they are part of economic hedge relationships. Hydro One's derivative instruments, or portions thereof, are mirrored down to Hydro One Networks, and are allocated between the Company's transmission and distribution businesses. The derivative instruments are classified as fair value hedges or undesignated contracts, consistent with Hydro One's derivative instruments classification.

The accounting guidance for derivative instruments requires the recognition of all derivative instruments not identified as meeting the normal purchase and sale exemption as either assets or liabilities recorded at fair value on the Balance Sheets. For derivative instruments that qualify for hedge accounting, Hydro One may elect to designate such derivative instruments as either cash flow hedges or fair value hedges. Hydro One offsets fair value amounts recognized in its Balance Sheets related to derivative instruments executed with the same counterparty under the same master netting agreement.

For derivative instruments that qualify for hedge accounting and which are designated as cash flow hedges, the effective portion of any gain or loss, net of tax, is reported as a component of accumulated OCI (AOCI) and is reclassified to results of operations in the same period or periods during which the hedged transaction affects results of operations. Any gains or losses on the derivative instrument that represent either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness are recognized in results of operations. For fair value hedges, changes in fair value of both the derivative instrument and the underlying hedged exposure are recognized in the Statement of Operations and Comprehensive Income in the current period. The gain or loss on the derivative instrument is included in the same line item as the offsetting gain or loss on the hedged item in the Statements of Operations and Comprehensive Income. Additionally, Hydro One enters into derivative agreements that are economic hedges that either do not qualify for hedge accounting or have not been designated as hedges. The changes in fair value of these undesignated derivative instruments are reflected in results of operations.

Embedded derivative instruments are separated from their host contracts and carried at fair value on the Balance Sheets when: (a) the economic characteristics and risks of the embedded derivative are not clearly and closely related to the economic characteristics and risks of the host contract; (b) the hybrid instrument is not measured at fair value, with changes in fair value recognized in results of operations each period; and (c) the embedded derivative itself meets the definition of a derivative. Hydro One does not engage in derivative trading or speculative activities and had no embedded derivatives at December 31, 2015 or 2014.

Hydro One periodically develops hedging strategies taking into account risk management objectives. At the inception of a hedging relationship where Hydro One has elected to apply hedge accounting, Hydro One formally documents the relationship between the hedged item and the hedging instrument, the related risk management objective, the nature of the specific risk exposure being hedged, and the method for assessing the effectiveness of the hedging relationship. Hydro One also assesses, both at the inception of the hedge and on a quarterly basis, whether the hedging instruments are effective in offsetting changes in fair values or cash flows of the hedged items.

Employee Future Benefits

Employee future benefits provided by Hydro One include pension, post-retirement and post-employment benefits. The costs of the pension, post-retirement and post-employment benefit plans are recorded over the periods during which employees render service.

Hydro One recognizes the funded status of its defined benefit pension, post-retirement and post-employment plans on its Consolidated Balance Sheets and subsequently recognizes the changes in funded status at the end of each reporting year. Defined benefit pension, post-retirement and post-employment plans are considered to be underfunded when the projected benefit obligation exceeds the fair value of the plan assets. Liabilities are recognized on the Consolidated Balance Sheets of Hydro One for any net underfunded projected benefit obligation. The net underfunded projected benefit obligation may be disclosed as a current liability, long-term liability, or both. The current portion is the amount by which the actuarial present value of benefits included in the benefit obligation payable in the next 12 months exceeds the fair value of plan assets. If the fair value of plan assets exceeds the projected benefit obligation of the plan, an asset is recognized equal to the net overfunded projected benefit obligation. The post-retirement and post-employment benefit plans are unfunded because there are no related plan assets.

Pension benefits

Hydro One has a contributory defined benefit pension plan covering most regular employees of Hydro One and its subsidiaries, including Hydro One Networks. The Hydro One pension plan does not segregate assets in a separate account for individual subsidiaries, nor is the obligation of the pension plan allocated to, or funded separately by, entities within the consolidated group. Accordingly, for purposes of these Financial Statements, the pension plan is accounted for as a defined contribution plan and no pension benefit asset or liability is recorded.

A detailed description of Hydro One pension benefits is provided in Note 15 – Pension and Post-Retirement and Post-Employment Benefits, to the Consolidated Financial Statements of Hydro One for the year ended December 31, 2015.

Post-retirement and post-employment benefits

Hydro One has post-retirement and post-employment benefit plans covering all regular employees of Hydro One and its subsidiaries, including Hydro One Networks. The benefit obligations of these post-retirement and post-employment benefit plans are not segregated, or funded separately, for Hydro One Networks. Accordingly, for purposes of these Financial Statements, the post-retirement and post-employment benefit obligations are allocated to the Company based on base pensionable earnings.

The Company records a regulatory asset equal to its allocated share of Hydro One's incremental net unfunded projected benefit obligation for post-retirement and post-employment plans at each year end based on annual actuarial reports. The regulatory asset for the incremental net unfunded projected benefit obligation for post-retirement and post-employment plans, in absence of regulatory accounting, would be recognized in accumulated OCI (AOCI). A regulatory asset is recognized because management considers it to be probable that post-retirement and post-employment benefit costs will be recovered in the future through the rate-setting process.

Post-retirement and post-employment benefits are recorded and included in rates on an accrual basis. Costs are determined by independent actuaries using the projected benefit method prorated on service and based on assumptions that reflect

management's best estimates. Past service costs from plan amendments are amortized to results of operations based on the expected average remaining service period.

For post-retirement benefits, all actuarial gains or losses are deferred using the "corridor" approach. The amount calculated above the "corridor" is amortized to results of operations on a straight-line basis over the expected average remaining service lives of active Hydro One employees in the plan and over the remaining life expectancy of inactive Hydro One employees in the plan. The post-retirement benefit obligation is remeasured to its fair value at each year end based on an annual actuarial report, with an offset to associated regulatory asset, to the extent of the remeasurement adjustment.

For post-employment obligations, the actuarial gains and losses that are incurred during the year are recognized immediately to results of operations. The post-employment benefit obligation is remeasured to its fair value at each year end based on an annual actuarial report, with an offset to associated regulatory asset, to the extent of the remeasurement adjustment.

All post-retirement and post-employment future benefit costs are attributed to labour and are either charged to results of operations or capitalized as part of the cost of property, plant and equipment and intangible assets.

A detailed description of Hydro One post-retirement and post-employment benefits is provided in Note 15 – Pension and Post-Retirement and Post-Employment Benefits, to the Consolidated Financial Statements of Hydro One for the year ended December 31, 2015.

Stock-Based Compensation

Hydro One measures share grant plans based on fair value of share grants as estimated based on the grant date Hydro One Limited share price. The costs are recognized in the financial statements using the graded-vesting attribution method for share grant plans that have both a performance condition and a service condition. The Company records a regulatory asset equal to the accrued costs of share grant plans recognized in each period, as management considers it to be probable that such costs will be recovered in the future through the rate-setting process.

Loss Contingencies

Hydro One and its subsidiaries are involved in certain legal and environmental matters that arise in the normal course of business. In the preparation of the Distribution Business' Financial Statements, management makes judgments regarding the future outcome of contingent events and records a loss for a contingency based on its best estimate when it is determined that such loss is probable and the amount of the loss can be reasonably estimated. Where the loss amount is recoverable in future rates, a regulatory asset is also recorded. When a range estimate for the probable loss exists and no amount within the range is a better estimate than any other amount, the Distribution Business records a loss at the minimum amount within the range.

Management regularly reviews current information available to determine whether recorded provisions should be adjusted and whether new provisions are required. Estimating probable losses may require analysis of multiple forecasts and scenarios that often depend on judgments about potential actions by third parties, such as federal, provincial and local courts or regulators. Contingent liabilities are often resolved over long periods of time. Amounts recorded in the Financial Statements may differ from the actual outcome once the contingency is resolved. Such differences could have a material impact on future results of operations, financial position and cash flows of the Distribution Business.

Provisions are based upon current estimates and are subject to greater uncertainty where the projection period is lengthy. A significant upward or downward trend in the number of claims filed, the nature of the alleged injuries, and the average cost of resolving each claim could change the estimated provision, as could any substantial adverse or favorable verdict at trial. A federal or provincial legislative outcome or structured settlement could also change the estimated liability. Legal fees are expensed as incurred.

Environmental Liabilities

Environmental liabilities are recorded in respect of past contamination when it is determined that future environmental remediation expenditures are probable under existing statute or regulation and the amount of the future expenditures can be reasonably estimated. The Distribution Business records a liability for the estimated future expenditures associated with contaminated land assessment (LAR) and remediation and for the phase-out and destruction of polychlorinated biphenyl (PCB)-contaminated mineral oil removed from electrical equipment, based on the present value of these estimated future expenditures. The Company determines the present value with a discount rate equal to its credit-adjusted risk-free interest rate on financial instruments with comparable maturities to the pattern of future environmental expenditures. As the

Company anticipates that the future expenditures will continue to be recoverable in future rates, an offsetting regulatory asset has been recorded to reflect the future recovery of these environmental expenditures from customers. The Company reviews its estimates of future environmental expenditures annually, or more frequently if there are indications that circumstances have changed.

Asset Retirement Obligations

Asset retirement obligations are recorded for legal obligations associated with the future removal and disposal of long-lived assets. Such obligations may result from the acquisition, construction, development and/or normal use of the asset. Conditional asset retirement obligations are recorded when there is a legal obligation to perform a future asset retirement activity but where the timing and/or method of settlement are conditional on a future event that may or may not be within the control of the Company. In such a case, the obligation to perform the asset retirement activity is unconditional even though uncertainty exists about the timing and/or method of settlement.

When recording an asset retirement obligation, the present value of the estimated future expenditures required to complete the asset retirement activity is recorded in the period in which the obligation is incurred, if a reasonable estimate can be made. In general, the present value of the estimated future expenditures is added to the carrying amount of the associated asset and the resulting asset retirement cost is depreciated over the estimated useful life of the asset. Where an asset is no longer in service when an asset retirement obligation is recorded, the asset retirement cost is recorded in results of operations.

Some of the Company’s distribution assets, particularly those located on unowned easements and rights-of-way, may have asset retirement obligations, conditional or otherwise. The majority of the Company’s easements and rights-of-way are either of perpetual duration or are automatically renewed annually. Land rights with finite terms are generally subject to extension or renewal. As the Distribution Business expects to use the majority of its facilities in perpetuity, no asset retirement obligations currently exist for these assets. If, at some future date, a particular facility is shown not to meet the perpetuity assumption, it will be reviewed to determine whether an estimable ARO exists. In such a case, an ARO would be recorded at that time.

The Distribution Business’ AROs recorded to date relate to estimated future expenditures associated with the removal and disposal of asbestos-containing materials installed in some of its facilities and with the decommissioning of certain assets.

3. NEW ACCOUNTING PRONOUNCEMENTS

Recent Accounting Guidance Not Yet Adopted

In January 2015, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2015-01, Income Statement – Extraordinary and Unusual Items (Subtopic 225-20): Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Items. This ASU eliminates the requirements for reporting entities to consider whether an underlying event or transaction is extraordinary and to show the item separately in the income statement. This ASU is effective for fiscal years, and interim periods within these years, beginning after December 15, 2015. The adoption of this ASU is not anticipated to have an impact on the Distribution Business’ financial statements.

In April 2015, the FASB issued ASU 2015-03, Interest – Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs. This ASU requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability. The recognition and measurement guidance for debt issuance costs are not affected. This ASU is effective for fiscal years, and interim periods within those years, beginning after December 15, 2015. Upon adoption of this ASU in the first quarter of 2016, the Distribution Business’ deferred debt issuance costs that are currently presented under other long-term assets will be reclassified as a deduction from the carrying amount of long-term debt.

In April 2015, the FASB issued ASU 2015-05, Intangibles – Goodwill and Other – Internal-Use Software (Subtopic 350-40): Customer’s Accounting for Fees Paid in a Cloud Computing Arrangement. This ASU provides guidance to customers about whether a cloud computing arrangement includes a software license, as well as the related accounting for the arrangement. This ASU is effective for fiscal years, and interim periods within these years, beginning after December 15, 2015. The Distribution Business is currently assessing the impact of adoption of this ASU on its financial statements.

In August 2015, the FASB issued ASU 2015-14, Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date. This ASU defers by one year the effective date of ASU 2014-09, Revenue from Contracts with Customers (Topic 606) issued by the FASB in May 2014. ASU 2014-09 provides guidance on revenue recognition that depicts the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods and services. The guidance in ASU 2014-09 is now effective for fiscal years, and interim periods within those years, beginning after December 15, 2017. The Distribution Business is currently assessing the impact of adoption of ASU 2014-09 on its financial statements.

In November 2015, the FASB issued ASU 2015-17, Income Taxes (Topic 740): Balance Sheet Classification of Deferred Taxes. The amendments in this ASU require that all deferred tax assets and liabilities be classified as noncurrent on the balance sheet. This ASU is effective for fiscal years, and interim periods within those years, beginning after December 15, 2016. Upon adoption of this ASU in the first quarter of 2017, the current portions of the Distribution Business' deferred income tax assets and liabilities will be reclassified as noncurrent assets and liabilities on the Balance Sheets.

4. NORFOLK POWER TRANSFER

On August 31, 2015, the common shares of Norfolk Power Distribution Inc. (Norfolk Power) were transferred to Hydro One Networks by Hydro One. The transfer was accounted as a non-monetary transfer, based on Norfolk Power's carrying values at August 31, 2015. On September 1, 2015, Norfolk Power started dissolution proceedings and, as a result, its net assets were transferred to Hydro One Networks.

The following table summarizes the assets and liabilities that were transferred to Hydro One Networks' Distribution Business at September 1, 2015:

(millions of Canadian dollars)	
Property, plant and equipment	55
Goodwill	40
Working capital	9
Other assets	1
Inter-company demand facility	(33)
Derivative instruments	(3)
Other liabilities	(2)
	67

5. DEPRECIATION AND AMORTIZATION

Year ended December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Depreciation of property, plant and equipment	254	250
Amortization of intangible assets	36	34
Asset removal costs	59	52
Amortization of regulatory assets	11	11
	360	347

6. FINANCING CHARGES

Year ended December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Interest on long-term debt *(Note 20)*	154	158
Interest on inter-company demand facility *(Note 20)*	3	1
Other	4	6
Less: Interest capitalized on construction and development in progress	(14)	(15)
Gain on interest-rate swap agreements	(1)	(3)
	146	147

7. INCOME TAXES

Income taxes / provision for PILs differ from the amount that would have been recorded using the combined Canadian federal and Ontario statutory income tax rate. The reconciliation between the statutory and the effective tax rates is provided as follows:

Year ended December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Income taxes / provision for PILs at statutory rate	82	51
Increase (decrease) resulting from:		
Net temporary differences included in amounts charged to customers:		
Pension contributions in excess of pension expense	(13)	(12)
Overheads capitalized for accounting but deducted for tax purposes	(6)	(6)
Capital cost allowance in excess of depreciation and amortization	(4)	(25)
Interest capitalized for accounting but deducted for tax purposes	(4)	(4)
Environmental expenditures	(3)	(3)
Non-refundable ITCs	(1)	(2)
Post-retirement and post-employment benefit expense in excess of cash payments	–	2
Other	(1)	1
Net temporary differences	(32)	(49)
Net permanent differences	1	1
Total income taxes / provision for PILs	51	3
Current income taxes / provision for (recovery of) PILs	63	(12)
Deferred income taxes / provision for PILs	(12)	15
Total income taxes / provision for PILs	51	3
Effective income tax rate	16.6%	1.6%

The provision for PILs / current income taxes is remitted to, or received from, the OEFC (PILs Regime) and the CRA (Federal Tax Regime). At December 31, 2015, $10 million (2014 – $49 million) due from the OEFC and $1 million due from the CRA were included in accounts receivable (2014 – $nil).

At December 31, 2015, the total income taxes / provision for PILs includes deferred income taxes / recovery of PILs of $12 million (2014 – deferred provision of $15 million) that is not included in the rate-setting process, using the balance sheet liability method of accounting. Deferred PILs balances expected to be included in the rate-setting process are offset by regulatory assets and liabilities to reflect the anticipated recovery or disposition of these balances within future electricity rates.

Deferred Income Tax Assets and Liabilities

Deferred income tax assets and liabilities arise from differences between the carrying amounts and tax basis of the Company's assets and liabilities. At December 31, 2015 and 2014, deferred income tax assets and liabilities consisted of the following:

December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Deferred income tax liabilities		
Capital cost allowance in excess of depreciation and amortization	(686)	(626)
Regulatory amounts not recognized for tax	(112)	(93)
Goodwill	(9)	(9)
Post-retirement and post-employment benefits expense in excess of cash payments	319	312
Environmental expenses	41	36
Non-capital losses	31	–
Other	–	1
Total deferred income tax liabilities	(416)	(379)
Less: current portion	10	9
	(426)	(388)

During 2015 and 2014, there were no changes in the rate applicable to future taxes.

8. ACCOUNTS RECEIVABLE

Year ended December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Accounts receivable – billed	384	474
Accounts receivable – unbilled	451	575
Accounts receivable, gross	835	1,049
Allowance for doubtful accounts	(59)	(64)
Accounts receivable, net	776	985

The following table shows the movements in the allowance for doubtful accounts for the years ended December 31, 2015 and 2014.

Year ended December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Allowance for doubtful accounts – January 1	(64)	(32)
Write-offs	37	24
Additions to allowance for doubtful accounts	(32)	(56)
Allowance for doubtful accounts – December 31	(59)	(64)

9. PROPERTY, PLANT AND EQUIPMENT

December 31, 2015 *(millions of Canadian dollars)*	**Property, Plant and Equipment**	**Accumulated Depreciation**	**Construction in Progress**	**Total**
Distribution	9,083	3,155	236	6,164
Communication	124	65	–	59
Administration and Service	996	574	18	440
	10,203	3,794	254	6,663

December 31, 2014 *(millions of Canadian dollars)*	**Property, Plant and Equipment**	**Accumulated Depreciation**	**Construction in Progress**	**Total**
Distribution	8,431	2,933	313	5,811
Communication	109	37	3	75
Administration and Service	935	533	10	412
	9,475	3,503	326	6,298

Financing charges capitalized on property, plant and equipment under construction were $14 million (2014 – $14 million).

10. INTANGIBLE ASSETS

December 31, 2015 *(millions of Canadian dollars)*	**Intangible Assets**	**Accumulated Amortization**	**Development in Progress**	**Total**
Computer applications software	352	141	17	228
Other	35	6	–	29
	387	147	17	257

December 31, 2014 *(millions of Canadian dollars)*	**Intangible Assets**	**Accumulated Amortization**	**Development in Progress**	**Total**
Computer applications software	356	178	19	197
Other	1	1	–	–
	357	179	19	197

Financing charges capitalized on intangible assets under development were $1 million (2014 – $1 million). The estimated annual amortization expense for intangible assets is as follows: 2016 – $36 million; 2017 – $36 million; 2018 – $36 million; and 2019 – $32 million; and 2020 – $24 million.

11. REGULATORY ASSETS AND LIABILITIES

Regulatory assets and liabilities arise as a result of the rate-making process. The Distribution Business has recorded the following regulatory assets and liabilities:

December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Regulatory assets:		
Deferred income tax regulatory asset	431	378
Post-retirement and post-employment benefits	134	154
Environmental	114	135
Retail settlement variance accounts	113	7
Pension cost variance	23	79
2015-2017 rate rider	20	–
DSC exemption	10	16
Share-based compensation	5	–
OEB cost assessment differential	–	12
Other	7	19
Total regulatory assets	857	800
Less: current portion	28	11
	829	789

December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Regulatory liabilities:		
Green Energy expenditure variance	76	83
Deferred income tax regulatory liability	9	8
PST savings deferral	4	19
Other	4	8
Total regulatory liabilities	93	118
Less: current portion	10	8
	83	110

Deferred Income Tax Regulatory Asset and Liability

Deferred income taxes are recognized on temporary differences between the carrying amount of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable income. The Distribution Business has recognized regulatory assets and liabilities that correspond to deferred income taxes that flow through the rate-setting process. In the absence of rate-regulated accounting, the Distribution Business' income tax expense would have been recognized using the liability method and there would be no regulatory accounts established for taxes to be recovered through future rates. As a result, the 2015 income tax expense would have been higher by approximately $32 million (2014 – $49 million).

Post-Retirement and Post-Employment Benefits

The Distribution Business recognizes the net unfunded status of post-retirement and post-employment obligations on the Balance Sheets with an incremental offset to the associated regulatory assets. A regulatory asset is recognized because management considers it to be probable that post-retirement and post-employment benefit costs will be recovered in the future through the rate-setting process. The post-retirement and post-employment benefit obligation is remeasured to its fair value at each year end based on an annual actuarial report, with an offset to the associated regulatory asset, to the extent of the remeasurement adjustment. In the absence of rate-regulated accounting, 2015 OCI would have been higher by $20 million (2014 – $18 million).

Environmental

The Distribution Business records a liability for the estimated future expenditures required to remediate past environmental contamination. Because such expenditures are expected to be recoverable in future rates, an equivalent amount was recorded as a regulatory asset. In 2015, the environmental regulatory asset decreased by $17 million (2014 – $25 million) to reflect related changes in the PCB liability, and increased by $2 million (2014 – $12 million) due to changes in the LAR liability. The environmental regulatory asset is amortized to results of operations based on the pattern of actual expenditures incurred and charged to environmental liabilities. The OEB has the discretion to examine and assess the prudency and the timing of recovery of all of the Distribution Business' actual environmental expenditures. In the absence of rate-regulated accounting, 2015 operation, maintenance and administration expenses would have been lower by $15 million (2014 – $13 million). In addition, 2015 amortization expense would have been lower by $11 million (2014 – $10 million), and 2015 financing charges would have been higher by $5 million (2014 – $6 million).

Retail Settlement Variance Accounts (RSVA)

Hydro One has deferred certain retail settlement variance amounts (RSVA) under the provisions of Article 490 of the OEB's Accounting Procedures Handbook. RSVA primarily includes variances relating to Power, Global Adjustment, Wholesale Market Service Charge and Transmission Network and Transmission Connection Services. In March 2015, the OEB approved the disposition of the total RSVA balance accumulated from January 2012 to December 2013, including accrued interest, to be recovered through the 2015-2017 Rate Rider. In 2015, the Company revised its method to estimate the unbilled accounts receivable based on new technology implemented to improve the accuracy of the estimation process. This revised method is also in compliance with OEB guidance. At December 31, 2015, the change in estimate reduced unbilled accounts receivable by approximately $121 million, with a corresponding offset to various components of RSVA. The change in estimate had no significant impact on 2015 net income.

Pension Cost Variance

A pension cost variance account was established for the Distribution Business to track the difference between the actual pension expense incurred and estimated pension costs approved by the OEB. The balance in this regulatory account reflects the excess of pension costs paid as compared to OEB-approved amounts. In the absence of rate-regulated accounting, 2015 revenue would have been higher by $3 million (2014 – lower by $20 million).

2015-2017 Rate Rider

In March 2015, as part of its decision on Hydro One Networks' Distribution rate application for 2015-2019 the OEB approved the disposition of certain deferral and variance accounts, including RSVAs and accrued interest. The 2015-2017 Rate Rider account includes the balances approved for disposition by the OEB and will be disposed over a 32-month period in accordance with the OEB decision.

DSC Exemption

In June 2010, Hydro One Networks filed an application with the OEB regarding the OEB's new cost responsibility rules contained in the OEB's October 2009 Notice of Amendment to the Distribution System Code (DSC), with respect to the connection of certain renewable generators that were already connected or that had received a connection impact assessment prior to October 21, 2009. The application sought approval to record and defer the unanticipated costs incurred by Hydro One Networks that resulted from the connection of certain renewable generation facilities. The OEB ruled that identified specific expenditures can be recorded in a deferral account subject to the OEB's review in subsequent Hydro One Network distribution applications. In March 2015, the OEB approved the disposition of the DSC exemption deferral account at December 31, 2013, including accrued interest, which will be recovered through the 2015-2017 Rate Rider. In addition, the OEB also approved Hydro One's request to discontinue this deferral account, and there were no additions to this regulatory account in 2015.

Share-based Compensation

The Distribution Business recognizes costs associated with stock-based compensation in a regulatory asset as management considers it probable that stock-based compensation costs will be recovered in the future through the rate-setting process. At December 31, 2015, the stock-based compensation costs related to the share grant plans are measured at fair value estimated based on grant date Hydro One Limited share price and recognized using the graded-vesting attribution method. In the absence of rate-regulated accounting, 2015 operation, maintenance and administration expenses would have been higher by $2 million (2014 – $nil).

OEB Cost Assessment Differential

In April 2010, the OEB issued its Decision regarding Hydro One Networks' distribution rate application for 2010 and 2011. As part of this decision, the OEB also approved the distribution-related OEB Cost Assessment Differential Account to record the difference between the amounts approved in rates and actual expenditures with respect to the OEB's cost assessments. In March 2015, the OEB approved the disposition of the OEB Cost Assessment Differential Account at December 31, 2013, including accrued interest, which will be recovered through the 2015-2017 Rate Rider. In addition, the OEB also approved Hydro One's request to discontinue this deferral account, and there were no additions to this regulatory account in 2015.

Green Energy Expenditure Variance

In April 2010, the OEB requested the establishment of deferral accounts which capture the difference between the revenue recorded on the basis of Green Energy Plan expenditures incurred and the actual recoveries received.

PST Savings Deferral Account

The provincial sales tax (PST) and goods and services tax (GST) were harmonized in July 2010. Unlike the GST, the PST was included in operation, maintenance and administration expenses or capital expenditures for past revenue requirements approved during a full cost-of-service hearing. Under the harmonized sales tax (HST) regime, the HST included in operation, maintenance and administration expenses or capital expenditures is not a cost ultimately borne by the Company and as such, a refund of the prior PST element in the approved revenue requirement is applicable, and calculations for tracking and refund were requested by the OEB. For Hydro One Networks' distribution revenue requirement, PST was included between July 1,

2010 and December 31, 2015 and recorded in a deferral account, as directed by the OEB. In March 2015, the OEB approved the disposition of the PST Savings Deferral account at December 31, 2013, including accrued interest, which will be recovered through the 2015-2017 Rate Rider.

12. DEBT

Hydro One issues notes for long-term financing under its Medium-Term Note (MTN) Program. The terms of certain issuances are mirrored down to Hydro One Networks through the issuance of inter-company debt, which is then allocated between the Company's transmission and distribution businesses.

The following table presents the outstanding long-term debt of the Distribution Business as at December 31, 2015 and 2014:

December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Long-term debt	3,191	3,381
Add: Unrealized marked-to-market loss[1]	–	1
Less: Long-term debt payable within one year	(200)	(221)
Long-term debt	2,991	3,161

[1] At December 31, 2014, the unrealized marked-to-market loss related to $100 million of Distribution Business' $200 million note due 2015. This loss was offset by $1 million unrealized marked-to-market gain on the related fixed-to-floating interest-rate swap agreements, which are accounted for as fair value hedges.

The long-term debt is unsecured and denominated in Canadian dollars. The long-term debt is summarized by the number of years to maturity in Note 13 – Fair Value of Financial Instruments and Risk Management.

13. FAIR VALUE OF FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

Fair value is considered to be the exchange price in an orderly transaction between market participants to sell an asset or transfer a liability at the measurement date. The fair value definition focuses on an exit price, which is the price that would be received in the sale of an asset or the amount that would be paid to transfer a liability.

The Company classifies its fair value measurements based on the following hierarchy, as prescribed by the accounting guidance for fair value, which prioritizes the inputs to valuation techniques used to measure fair value into three levels:

Level 1 inputs are unadjusted quoted prices in active markets for identical assets or liabilities that Hydro One has the ability to access. An active market for the asset or liability is one in which transactions for the asset or liability occurs with sufficient frequency and volume to provide ongoing pricing information.

Level 2 inputs are those other than quoted market prices that are observable, either directly or indirectly, for an asset or liability. Level 2 inputs include, but are not limited to, quoted prices for similar assets or liabilities in an active market, quoted prices for identical or similar assets or liabilities in markets that are not active and inputs other than quoted market prices that are observable for the asset or liability, such as interest rate curves and yield curves observable at commonly quoted intervals, volatilities, credit risk and default rates. A Level 2 measurement cannot have more than an insignificant portion of the valuation based on unobservable inputs.

Level 3 inputs are any fair value measurements that include unobservable inputs for the asset or liability for more than an insignificant portion of the valuation. A Level 3 measurement may be based primarily on Level 2 inputs.

Non−Derivative Financial Assets and Liabilities

At December 31, 2015 and 2014, the carrying amounts of accounts receivable, inter-company demand facility, and accounts payable are representative of fair value because of the short-term nature of these instruments.

Fair Value Measurements of Long-Term Debt

The fair values and carrying values of the Distribution Business' long-term debt at December 31, 2015 and 2014 are as follows:

December 31 *(millions of Canadian dollars)*	**2015 Carrying Value**	**2015 Fair Value**	**2014 Carrying Value**	**2014 Fair Value**
Long-term debt				
$30 million notes due 2020[1]	30	30	–	–
$100 million of $200 million notes due 2015[1]	–	–	101	101
Other notes and debentures[2]	3,161	3,623	3,281	3,820
	3,191	3,653	3,382	3,921

[1] The fair value of Distribution Business' $30 million notes due 2020 (2014 – $100 million of Distribution Business' $200 million notes due 2015) subject to hedging is primarily based on changes in the present value of future cash flows due to a change in the yield in the swap market for the related swap (hedged risk).

[2] The fair value of other notes and debentures, and the portions of Distribution Business' notes that are not subject to hedging, represents the market value of the notes and debentures and is based on unadjusted period-end market prices for the same or similar debt of the same remaining maturities.

Fair Value Measurements of Derivative Instruments

Hydro One enters into interest-rate swaps agreements with respect to its long-term debt. The terms of these interest-rate swap agreements are mirrored down to Hydro One Networks, and are then allocated between the Company's transmission and distribution businesses.

At December 31, 2015, the Distribution Business' share of the Company's derivative instruments include $30 million (2014 – $100 million) of interest-rate swaps that were used to convert fixed-rate debt to floating-rate debt. These interest-rate swaps are classified as fair value hedges. The Distribution Business' fair value hedge exposure was equal to about 1% (2014 – 3%) of its long-term debt. At December 31, 2015, the Distribution Business' interest-rate swaps designated as fair value hedges were as follows:

- $30 million fixed-to-floating interest-rate swap agreements to convert $30 million notes maturing on April 30, 2020 into three-month variable rate debt.

At December 31, 2015, the Distribution Business' had no interest-rate swaps classified as undesignated contracts (2014 – $20 million).

Fair Value Hierarchy

Fair value hierarchy information for financial assets and liabilities at December 31, 2015 and 2014 was as follows:

December 31, 2015 *(millions of Canadian dollars)*	**Carrying Value**	**Fair Value**	**Level 1**	**Level 2**	**Level 3**
Liabilities:					
Inter-company demand facility	640	640	640	–	–
Long-term debt	3,191	3,653	–	3,653	–
	3,831	4,293	640	3,653	

December 31, 2014 *(millions of Canadian dollars)*	**Carrying Value**	**Fair Value**	**Level 1**	**Level 2**	**Level 3**
Assets:					
Derivative instruments					
Fair value hedges – interest-rate swaps	1	1	–	1	–
	1	1	–	1	–
Liabilities:					
Inter-company demand facility	225	225	225	–	–
Long-term debt	3,382	3,921	–	3,921	–
	3,607	4,146	225	3,921	–

The fair value of the derivative instruments is determined using inputs other than quoted prices that are observable for these assets. The fair value is primarily based on the present value of future cash flows using a swap yield curve to determine the assumptions for interest rates.

The fair value of the hedged portion of the long-term debt is primarily based on the present value of future cash flows using a swap yield curve to determine the assumption for interest rates. The fair value of the un-hedged portion of the long-term debt is based on unadjusted period-end market prices for the same or similar debt of the same remaining maturities.

There were no significant transfers between any of the levels during the years ended December 31, 2015 and 2014.

Risk Management

Exposure to market risk, credit risk and liquidity risk arises in the normal course of the Company's business.

Market Risk

Market risk refers primarily to the risk of loss that results from changes in costs, foreign exchange rates and interest rates. The Company is exposed to fluctuations in interest rates as its regulated return on equity is derived using a formulaic approach that takes into account anticipated interest rates, but is not currently exposed to material commodity price risk or material foreign exchange risk.

The OEB-approved adjustment formula for calculating return on equity in a deemed regulatory capital structure of 60% debt and 40% equity provides for increases and decreases depending on changes in benchmark rates of return for Government of Canada debt. The Company estimates that a 1% decrease in the forecasted long-term Government of Canada bond yield used in determining the Distribution Business' rate of return would reduce the Distribution Business' 2015 net income by approximately $13 million (2014 – $10 million).

Hydro One uses a combination of fixed and variable-rate debt to manage the mix of its debt portfolio. Hydro One also uses derivative financial instruments to manage interest-rate risk. Hydro One utilizes interest-rate swaps, which are typically designated as fair value hedges, as a means to manage its interest rate exposure to achieve a lower cost of debt. In addition, the Company may utilize interest-rate derivative instruments to lock in interest-rate levels in anticipation of future financing.

A hypothetical 10% increase in the interest rates associated with variable-rate debt would not have resulted in a significant decrease in Hydro One's net income for the years ended December 31, 2015 or 2014.

Fair Value Hedges
For derivative instruments that are designated and qualify as fair value hedges, the gain or loss on the derivative instruments as well as the offsetting loss or gain on the hedged item attributable to the hedged risk are recognized in the Statements of Operations and Comprehensive Income. The Distribution Business' net unrealized loss (gain) on the hedged debt and the related interest-rate swaps for the years ended December 31, 2015 and 2014 are included in financing charges as follows:

Year ended December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Unrealized loss (gain) on hedged debt	(1)	(1)
Unrealized loss (gain) on fair value interest-rate swaps	1	1
Net unrealized loss (gain)	–	–

At December 31, 2015, the amount of the Distribution Business' fair value hedges outstanding related to interest-rate swaps was $30 million (2014 – $100 million), with assets at fair value of $nil (2014 – $1 million). During the years ended December 31, 2015 and 2014, there was no significant impact on the Distribution Business' results of operations as a result of any ineffectiveness attributable to fair value hedges.

Credit Risk

Financial assets create a risk that a counterparty will fail to discharge an obligation, causing a financial loss. At December 31, 2015 and 2014, there were no significant concentrations of credit risk with respect to any class of financial assets. The Distribution Business did not earn a significant amount of revenue from any individual customer. At December 31, 2015 and 2014, there was no significant accounts receivable balance due from any single customer.

At December 31, 2015, the Distribution Business' allowance for doubtful accounts was $59 million (2014 – $64 million). Adjustments and write-offs are determined on the basis of a review of overdue accounts, taking into consideration historical

experience. At December 31, 2015, approximately 5% of the Distribution Business' net accounts receivable were aged more than 60 days (2014 – 6%).

Hydro One manages its counterparty credit risk through various techniques including: entering into transactions with highly-rated counterparties; limiting total exposure levels with individual counterparties consistent with the Hydro One's Board-approved Credit Risk Policy; entering into master agreements which enable net settlement and the contractual right of offset; and monitoring the financial condition of counterparties. In addition to payment netting language in master agreements, Hydro One establishes credit limits, margining thresholds and collateral requirements for each counterparty. Counterparty credit limits are based on an internal credit review that considers a variety of factors, including the results of a scoring model, leverage, liquidity, profitability, credit ratings and risk management capabilities. The determination of credit exposure for a particular counterparty is the sum of current exposure plus the potential future exposure with that counterparty. The current exposure is calculated as the sum of the principal value of money market exposures and the market value of all contracts that have a positive mark-to-market position on the measurement date. Hydro One would only offset the positive market values against negative values with the same counterparty where permitted by the existence of a legal netting agreement such as an International Swap Dealers Association master agreement. The potential future exposure represents a safety margin to protect against future fluctuations of interest rates, currencies, equities, and commodities. It is calculated based on factors developed by the Bank of International Settlements, following extensive historical analysis of random fluctuations of interest rates and currencies. To the extent that a counterparty's margining thresholds are exceeded, the counterparty is required to post collateral with Hydro One as specified in each agreement. Hydro One monitors current and forward credit exposure to counterparties both on an individual and an aggregate basis. The Company's counterparty credit risk policy is consistent with Hydro One. The Distribution Business' credit risk for accounts receivable is limited to the carrying amounts on its Balance Sheets.

Liquidity Risk

Liquidity risk refers to the Company's ability to meet its financial obligations as they come due. The Company meets its short-term liquidity requirements through the inter-company demand facility with Hydro One and funds from operations. The short-term liquidity available to the Company should be sufficient to fund normal operating requirements.

At December 31, 2015, accounts payable and accrued liabilities in the amount of $656 million (2014 – $670 million) were expected to be settled in cash at their carrying amounts within the next 12 months.

At December 31, 2015, the principal amount of the Distribution Business' long-term debt was $3,191 million (2014 – $3,381 million). Principal repayments and related weighted average interest rates are summarized by the number of years to maturity in the following table:

Years to Maturity	Long-term Debt Principal Repayments *(millions of Canadian dollars)*	Weighted Average Interest Rate *(%)*
1 year	200	4.3
2 years	195	5.2
3 years	338	2.8
4 years	91	1.2
5 years	150	3.9
	974	3.6
6 – 10 years	261	3.2
Over 10 years	1,956	5.4
	3,191	4.7

Interest payments on long-term debt are summarized by year in the following table:

Year	Interest Payments *(millions of Canadian dollars)*
2016	146
2017	141
2018	131
2019	121
2020	118
	657
2021-2025	544
2026 +	1,523
	2,724

14. CAPITAL MANAGEMENT

The Distribution Business' objective is to manage its capital structure consistent with the deemed capital structure for rate-setting purposes as prescribed by the OEB.

The Distribution Business considers its capital structure to consist of excess of assets over liabilities, long-term debt, and the inter-company demand facility. The following table summarizes this capital structure:

December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Long-term debt payable within one year	200	221
Inter-company demand facility	640	225
	840	446
Long-term debt	2,991	3,161
Excess of assets over liabilities	2,679	2,595
Total capital	6,510	6,202

The following table shows the movements in the excess of assets over liabilities for the years ended December 31, 2015 and 2014:

December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Excess of assets over liabilities, January 1	2,595	2,465
Net income	257	189
Payments to Hydro One to finance dividends	(240)	(59)
Transfer of Norfolk Power	67	–
Excess of assets over liabilities, December 31	2,679	2,595

15. PENSION AND POST-RETIREMENT AND POST-EMPLOYMENT BENEFITS

Hydro One has a defined benefit pension plan, a supplementary pension plan, and post-retirement and post-employment benefit plans. The defined benefit pension plan (Pension Plan) is contributory and covers most regular employees of Hydro One and its subsidiaries. The supplementary pension plan provides members of the Pension Plan with benefits that would have been earned and payable under the Pension Plan but for the limitations imposed by the *Income Tax Act* (Canada). The supplementary pension plan obligation is included with other post-retirement and post-employment benefit obligations on the Balance Sheets.

Pension Benefits

The Pension Plan provides benefits based on highest three-year average pensionable earnings. For new management employees who commenced employment on or after January 1, 2004, and for new Society of Energy Professionals

represented staff hired after November 17, 2005, benefits are based on highest five-year average pensionable earnings. After retirement, pensions are indexed to inflation.

Hydro One and employee contributions to the Pension Plan are based on actuarial valuations performed at least every three years. Hydro One's annual Pension Plan contributions for 2015 of $177 million (2014 – $174 million) were based on an actuarial valuation effective December 31, 2013 and the level of pensionable earnings. Estimated annual Pension Plan contributions for 2016 are approximately $180 million, based on the actuarial valuation as at December 31, 2013 and projected levels of pensionable earnings. Future minimum contributions beyond 2016 will be based on an actuarial valuation effective no later than December 31, 2016. Contributions are payable one month in arrears. All of the contributions are expected to be in the form of cash.

At December 31, 2015, based on the December 31, 2013 actuarial valuation, the present value of Hydro One's projected pension benefit obligation was estimated to be $7,683 million (2014 – $7,535 million). The fair value of pension plan assets available for these benefits was $6,731 million (2014 – $6,299 million).

Post-Retirement and Post-Employment Benefits

During the year ended December 31, 2015, the Distribution Business charged $31 million (2014 – $33 million) of post-retirement and post-employment benefit costs to operations, and capitalized $35 million (2014 – $34 million) as part of the cost of property, plant and equipment and intangible assets. Benefits paid in 2015 were $27 million (2014 – $26 million). In addition, the associated post-retirement and post-employment benefits regulatory asset decreased by $20 million (2014 – $18 million).

The Distribution Business presents its post-retirement and post-employment benefit liabilities on its Balance Sheets within the following line items:

December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Accrued liabilities	26	25
Post-retirement and post-employment benefit liability	862	844
	888	869

16. ENVIRONMENTAL LIABILITIES

The following tables show the movements in environmental liabilities for the years ended December 31, 2015 and 2014:

Year ended December 31, 2015 *(millions of Canadian dollars)*	**PCB**	**LAR**	**Total**
Environmental liabilities, January 1	95	40	135
Interest accretion	4	1	5
Expenditures	(5)	(6)	(11)
Revaluation adjustment	(17)	2	(15)
Environmental liabilities, December 31	77	37	114
Less: current portion	10	5	15
	67	32	99

Year ended December 31, 2014 *(millions of Canadian dollars)*	**PCB**	**LAR**	**Total**
Environmental liabilities, January 1	117	35	152
Interest accretion	5	1	6
Expenditures	(2)	(8)	(10)
Revaluation adjustment	(25)	12	(13)
Environmental liabilities, December 31	95	40	135
Less: current portion	6	5	11
	89	35	124

The following tables show the reconciliation between the undiscounted basis of the environmental liabilities and the amount recognized on the Balance Sheets after factoring in the discount rate:

December 31, 2015 *(millions of Canadian dollars)*	**PCB**	**LAR**	**Total**
Undiscounted environmental liabilities	87	38	125
Less: discounting accumulated liabilities to present value	10	1	11
Discounted environmental liabilities	77	37	114

December 31, 2014 *(millions of Canadian dollars)*	**PCB**	**LAR**	**Total**
Undiscounted environmental liabilities	108	42	150
Less: discounting accumulated liabilities to present value	13	2	15
Discounted environmental liabilities	95	40	135

At December 31, 2015, the estimated future environmental expenditures were as follows:

(millions of Canadian dollars)	
2016	15
2017	16
2018	16
2019	17
2020	17
Thereafter	44
	125

The Distribution Business records a liability for the estimated future expenditures for the contaminated LAR and for the phase-out and destruction of PCB-contaminated mineral oil removed from electrical equipment when it is determined that future environmental remediation expenditures are probable under existing statute or regulation and the amount of the future expenditures can be reasonably estimated.

There are uncertainties in estimating future environmental costs due to potential external events such as changes in legislation or regulations, and advances in remediation technologies. In determining the amounts to be recorded as environmental liabilities, the Company estimates the current cost of completing required work and makes assumptions as to when the future expenditures will actually be incurred, in order to generate future cash flow information. A long-term inflation rate assumption of approximately 2% has been used to express these current cost estimates as estimated future expenditures. Future expenditures have been discounted using factors ranging from approximately 2.4% to 6.3%, depending on the appropriate rate for the period when expenditures are expected to be incurred. All factors used in estimating the Distribution Business' environmental liabilities represent management's best estimates of the present value of costs required to meet existing legislation or regulations. However, it is reasonably possible that numbers or volumes of contaminated assets, cost estimates to perform work, inflation assumptions and the assumed pattern of annual cash flows may differ significantly from the Company's current assumptions. In addition, with respect to the PCB environmental liability, the availability of critical resources such as skilled labour and replacement assets and the ability to take maintenance outages in critical facilities may influence the timing of expenditures.

PCBs

The Environment Canada regulations, enacted under the *Canadian Environmental Protection Act,* 1999, govern the management, storage and disposal of PCBs based on certain criteria, including type of equipment, in-use status, and PCB-contamination thresholds. Under current regulations, the Company's PCBs have to be disposed of by the end of 2025, with the exception of specifically exempted equipment. Contaminated equipment will generally be replaced, or will be decontaminated by removing PCB-contaminated insulating oil and retro filling with replacement oil that contains PCBs in concentrations of less than 2 ppm.

The Distribution Business' best estimate of the total estimated future expenditures to comply with current PCB regulations is $87 million. These expenditures are expected to be incurred over the period from 2016 to 2025. As a result of its annual review of environmental liabilities, the Distribution Business recorded a revaluation adjustment in 2015 to reduce the PCB environmental liability by $17 million (2014 – $25 million).

LAR

The Distribution Business' best estimate of the total estimated future expenditures to complete its LAR program is $38 million. These expenditures are expected to be incurred over the period from 2016 to 2023. As a result of its annual review of environmental liabilities, the Distribution Business recorded a revaluation adjustment in 2015 to increase the LAR environmental liability by $2 million (2014 – $12 million).

17. ASSET RETIREMENT OBLIGATIONS

The Company records a liability for the estimated future expenditures for the removal and disposal of asbestos-containing materials installed in some of its facilities and for the decommissioning of specific switching stations located on unowned sites. AROs, which represent legal obligations associated with the retirement of certain tangible long-lived assets, are computed as the present value of the projected expenditures for the future retirement of specific assets and are recognized in the period in which the liability is incurred, if a reasonable estimate of fair value can be made. If the asset remains in service at the recognition date, the present value of the liability is added to the carrying amount of the associated asset in the period the liability is incurred and this additional carrying amount is depreciated over the remaining life of the asset. If an ARO is recorded in respect of an out-of-service asset, the asset retirement cost is charged to results of operations. Subsequent to the initial recognition, the liability is adjusted for any revisions to the estimated future cash flows associated with the ARO, which can occur due to a number of factors including, but not limited to, cost escalation, changes in technology applicable to the assets to be retired, changes in legislation or regulations, as well as for accretion of the liability due to the passage of time until the obligation is settled. Depreciation expense is adjusted prospectively for any increases or decreases to the carrying amount of the associated asset.

In determining the amounts to be recorded as AROs, the Company estimates the current fair value for completing required work and makes assumptions as to when the future expenditures will actually be incurred, in order to generate future cash flow information. A long-term inflation assumption of approximately 2% has been used to express these current cost estimates as estimated future expenditures. Future expenditures have been discounted using factors ranging from approximately 3.0% to 5.0%, depending on the appropriate rate for the period when expenditures are expected to be incurred. All factors used in estimating the Distribution Business' AROs represent management's best estimates of the cost required to meet existing legislation or regulations. However, it is reasonably possible that numbers or volumes of contaminated assets, cost estimates to perform work, inflation assumptions and the assumed pattern of annual cash flows may differ significantly from the Company's current assumptions. AROs are reviewed annually or more frequently if significant changes in regulations or other relevant factors occur. Estimate changes are accounted for prospectively.

At December 31, 2015, the Company had recorded AROs of $4 million (2014 – $4 million), related to its Distribution Business, consisting of the estimated future expenditures associated with the removal and disposal of asbestos-containing materials installed in some of its facilities. The amount of interest recorded is nominal.

18. HYDRO ONE NETWORKS' SHARE CAPITAL

Hydro One Networks is authorized to issue an unlimited number of common and preferred shares. At December 31, 2015, Hydro One Networks had 207,577,181 common shares issued and outstanding and no preferred shares issued and outstanding.

During 2015, Hydro One Networks declared preferred share dividends in the amount of $16 million (2014 – $20 million) and common share dividends in the amount of $875 million (2014 – $724 million) to Hydro One. The amount allocated to and paid by the Distribution Business to finance these dividends was $240 million (2014 – $59 million).

19. STOCK-BASED COMPENSATION

The following compensation plans were established by Hydro One Limited, however they represent components of compensation costs of Hydro One and its subsidiaries, including Hydro One Networks, in current and future periods.

Share Grant Plans

At December 31, 2015, Hydro One Limited had two share grant plans, one for the benefit of certain members of the Power Workers' Union (the PWU Share Grant Plan) and one for the benefit of certain members of The Society of Energy Professionals (the Society Share Grant Plan). These plans are part of the Company's overall compensation strategy. Hydro One and Hydro One Limited entered into an intercompany agreement, such that Hydro One will pay Hydro One Limited for the compensation costs associated with these plans. The agreement requires Hydro One Networks to reimburse Hydro One for the value of shares granted to the Company's eligible employees relating to these plans.

The PWU Share Grant Plan provides for the issuance of common shares of Hydro One Limited from treasury to certain eligible members of the Power Workers' Union annually, commencing on April 1, 2017 and continuing until the earlier of April 1, 2028 or the date an eligible employee no longer meets the eligibility criteria of the PWU Share Grant Plan. To be eligible, an employee must be a member of the Pension Plan on April 1, 2015, be employed on the date annual share issuance occurs and continue to have under 35 years of service. The requisite service period for the PWU share grant plan begins on July 3, 2015, which is the date the share grant plans were ratified by the PWU. The number of common shares issued annually to each eligible employee will be equal to 2.7% of such eligible employee's salary as at April 1, 2015, divided by $20.50, being the price of the common shares of Hydro One Limited in the IPO. The aggregate number of Hydro One Limited common shares issuable under the PWU Share Grant Plan shall not exceed 3,981,763 common shares. In 2015, 2,152,519 Hydro One Limited common shares were granted under the PWU Share Grant Plan relevant to the total share based compensation recognized by the Distribution Business.

The Society Share Grant Plan provides for the issuance of common shares of Hydro One Limited from treasury to certain eligible members of The Society of Energy Professionals annually, commencing on April 1, 2018 and continuing until the earlier of April 1, 2029 or the date an eligible employee no longer meets the eligibility criteria of the Society Share Grant Plan. To be eligible, an employee must be a member of the Pension Plan on September 1, 2015, be employed on the date annual share issuance occurs and continue to have under 35 years of service. Therefore the requisite service period for the Society Share Grant Plan begins on September 1, 2015. The number of common shares issued annually to each eligible employee will be equal to 2.0% of such eligible employee's salary as at September 1, 2015, divided by $20.50, being the price of the common shares of Hydro One Limited in the IPO. The aggregate number of Hydro One Limited common shares issuable under the Society Share Grant Plan shall not exceed 1,434,686 common shares. In 2015, 743,877 Hydro One Limited common shares were granted under the Society Share Grant Plan relevant to the total share based compensation recognized by the Distribution Business.

The fair value of the Hydro One Limited share grants is estimated based on the grant date Hydro One Limited share price of $20.50 and is recognized using the graded-vesting attribution method as the share grant plans have both a performance condition and a service condition. Total fair value of shares granted to employees of Hydro One Networks' Distribution Business in 2015 is $59 million (2014 – $nil). Total share based compensation recognized during 2015 by Hydro One Networks' Distribution Business was $5 million (2014 – $nil) and was recorded as a regulatory asset. The historical turnover rate relating to members of the Power Workers' Union and The Society of Energy Professionals is not believed to be reflective of a future turnover rate due to benefits conferred by the share grant plans. At December 31, 2015, the Company expects all eligible employees to receive the share grants until such time that they no longer meet the eligibility criteria and therefore, a forfeiture rate of 0% is assumed in amounts recognized during 2015. The Company will reevaluate this assumption in subsequent periods based on actual experience.

A summary of the Distribution Business' share grant activity under the Share Grant Plans as of December 31, 2015 is presented below:

Years ended December 31, 2015	Share Grants *(Number)*	Weighted-Average Price
Outstanding – beginning of year	–	–
Granted (non-vested)	2,896,396	$20.50
Outstanding – end of year	2,896,396	–

Employee Share Ownership Plan

Effective December 15, 2015, Hydro One Limited established an Employee Share Ownership Plan (ESOP). Under the ESOP, certain eligible management and non-represented employees may contribute between 1% and 6% of their base salary towards

purchasing common shares of Hydro One Limited. Hydro One Networks will match 50% of the employee's contributions, up to a maximum Company contribution of $25,000 per calendar year. No contributions were made under the ESOP during 2015.

Long-term Incentive Plan

Effective August 31, 2015, the Board of Directors of Hydro One Limited adopted a Long-term Incentive Plan (LTIP). Under the LTIP, long-term incentives will be granted to certain executive and management employees of Hydro One Limited and its subsidiaries, and all equity-based awards will be settled in newly-issued shares of Hydro One Limited from treasury, consistent with the provisions of the plan. The aggregate number of shares issuable under the LTIP shall not exceed 11,900,000 shares of Hydro One Limited.

The LTIP provides flexibility to award a range of vehicles, including restricted share units, performance share units, stock options, share appreciation rights, restricted shares, deferred share units and other share-based awards. The mix of vehicles is intended to vary by role to recognize the level of executive accountability for overall business performance. No long-term incentives were awarded during 2015.

20. RELATED PARTY TRANSACTIONS

The Distribution Business is a separately regulated business of Hydro One Networks which is a subsidiary of Hydro One. Hydro One is owned by Hydro One Limited, and the Province is the majority shareholder of Hydro One Limited. The OEFC, IESO, Ontario Power Generation Inc. (OPG), the OEB, and Hydro One Brampton are related parties to Hydro One Networks because they are controlled or significantly influenced by the Province. Transactions between these parties and the Distribution Business are described below.

IESO

- In 2015, the Distribution Business purchased power in the amount of $1,963 million (2014 – $2,172 million) from the IESO-administered electricity market.
- The Distribution Business receives amounts for rural rate protection from the IESO. Revenues in 2015 include $125 million (2014 – $125 million) related to this program.
- The IESO funds substantially all of the Company's conservation and demand management programs. The funding includes program costs, incentives, and management fees. In 2015, the Distribution Business received $63 million (2014 – $28 million) related to these programs.

OPG

- In 2015, the Distribution Business purchased power in the amount of $11 million (2014 – $23 million) from OPG.
- The Company has service level agreements with OPG. These services include field and engineering, logistics, corporate, telecommunications and information technology services. Operation, maintenance and administration costs of the Distribution Business in 2015 and 2014 related to the purchase of services with respect to these service level agreements were not significant.

OEFC

- In 2015, the Distribution Business purchased power in the amount of $6 million (2014 – $10 million) from power contracts administered by the OEFC.
- During 2015, Hydro One paid a $8 million (2014 – $5 million) fee to the OEFC for indemnification against adverse claims in excess of $10 million paid by the OEFC with respect to certain of Ontario Hydro's businesses transferred to Hydro One on April 1, 1999. Hydro One has not made any claims under the indemnity since it was put in place in 1999. Hydro One and the OEFC, with the consent of the Minister of Finance, terminated the indemnity fee effective October 31, 2015. The Distribution Business' allocation of this fee was $1 million.
- PILs and payments in lieu of property taxes were paid to the OEFC.

OEB

- Under the *Ontario Energy Board Act,* 1998, the OEB is required to recover all of its annual operating costs from gas and electricity distributors and transmitters. In 2015, the Distribution Business incurred $7 million (2014 – $6 million) in OEB fees.

Hydro One Brampton

- Effective August 31, 2015, Hydro One Brampton is no longer a subsidiary of Hydro One, but is indirectly owned by the Province.

  Subsequent to August 31, 2015, the Distribution Business continues to provide certain management, administrative and smart meter network services to Hydro One Brampton pursuant to certain service level agreements, which are provided at market rates. These agreements will continue until the end of 2016 (except in the case of smart meter network services, which will continue until the end of 2017). Hydro One Brampton has the right to renew these agreements (other than smart meter network services) for additional one-year terms to end no later than December 31, 2019. These agreements will terminate if the Province disposes of its interest in Hydro One Brampton, except in the case of the smart meter network services agreement, which is anticipated to continue for a transition period after the Province disposes of its interest in Hydro One Brampton. From September 1 to December 31, 2015, revenues related to the provision of services with respect to these service level agreements were $1 million.

The amounts due to and from related parties as a result of the transactions referred to above are as follows:

December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Accounts receivable	60	98
Accrued liabilities[1]	(128)	(180)

[1] Included in accrued liabilities at December 31, 2015 are amounts owing to the IESO in respect of power purchases of $127 million (2014 – $176 million).

Hydro One Limited and Subsidiaries

- The Distribution Business provides services to, and receives services from, Hydro One Limited and its subsidiaries. Amounts due to and from Hydro One Limited and its subsidiaries are settled through the inter-company demand facility.

  The Company has entered into various agreements with Hydro One Limited and its other subsidiaries related to the provision of shared corporate functions and services, including legal, financial and human resources services, and operational services, including environmental, forestry, and line services. 2015 revenues of the Distribution Business include $4 million (2014 – $2 million) related to the provision of services to Hydro One and its subsidiaries. In 2015, services were purchased from Hydro One Limited and its other subsidiaries totalling $16 million (2014 – $12 million), of which $16 million (2014 – $11 million) was expensed and less than $1 million (2014 – $1 million) was capitalized.
- The Distribution Business' long-term debt is due to Hydro One. In addition, balances payable or receivable under the inter-company demand facility are due to or due from Hydro One Limited. Financing charges include interest expense on the long-term debt in the amount of $154 million (2014 – $158 million), and interest expense on the inter-company demand facility in the amount of $3 million (2014 – $1 million). At December 31, 2015, the Distribution Business had accrued interest payable to Hydro One totaling $36 million (2014 – $38 million).
- During 2015, Hydro One Networks declared preferred share dividends in the amount of $16 million (2014 – $20 million) and common share dividends in the amount of $875 million (2014 – $724 million) to Hydro One. The amount allocated to the Distribution Business to finance these dividends was $240 million (2014 – $59 million). The entire amount was paid in 2015 (2014 – entire amount was paid in 2014).
- In 2015, Hydro One Limited established certain stock-based compensation plans, however they represent components of costs of Hydro One and its subsidiaries, including Hydro One Networks in current and future periods. Hydro One and Hydro One Limited entered into an intercompany agreement, such that Hydro One will pay Hydro One Limited for the compensation costs associated with the share grant plans. The agreement requires Hydro One Networks to reimburse Hydro One for the value of shares granted to the Company's eligible employees relating to these plans. At December 31, 2015, Hydro One Networks' Distribution Business had a payable of $5 million (2014 – $nil) to Hydro One associated with these plans. See Note 19 – Stock-based Compensation.

- On August 31, 2015, the common shares of Norfolk Power were transferred to Hydro One Networks by Hydro One. On September 1, 2015, Norfolk Power started dissolution proceedings and, as a result, its assets were transferred to Hydro One Networks. For details, see Note 4 – Norfolk Power Transfer.

21. STATEMENTS OF CASH FLOWS

The changes in non-cash balances related to operations consist of the following:

Year ended December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Accounts receivable	209	(132)
Materials and supplies	3	(1)
Other assets	7	(5)
Accounts payable	(10)	4
Accrued liabilities	(11)	16
Accrued interest	(2)	–
Long-term accounts payable and other liabilities	6	–
Post-retirement and post-employment benefit liability	38	38
	240	(80)

Capital Expenditures

The following table illustrates the reconciliation between investments in property, plant and equipment and the amount presented in the Statements of Cash Flows after factoring in capitalized depreciation and the net change in related accruals:

Year ended December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Capital investments in property, plant and equipment	(653)	(633)
Capitalized depreciation and net change in accruals included in capital investments in property, plant and equipment	19	19
Capital expenditures – property, plant and equipment	(634)	(614)

The following table illustrates the reconciliation between investments in intangible assets and the amount presented in the Statements of Cash Flows after factoring in the net change in related accruals:

Year ended December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Capital investments in intangible assets	(26)	(14)
Net change in accruals included in capital investments in intangible assets	2	–
Capital expenditures – intangible assets	(24)	(14)

Supplementary Information

Year ended December 31 *(millions of Canadian dollars)*	**2015**	**2014**
Net interest paid	156	155
Income taxes / PILs paid	21	15

22. CONTINGENCIES

In September 2015, Hydro One and three of its subsidiaries, including Hydro One Networks, were served with a class action suit in which the representative plaintiff is seeking up to $125 million in damages related to allegations of improper billing practices. Hydro One intends to defend the action. Due to the preliminary stage of legal proceedings, an estimate of a possible loss related to this claim cannot be made.

The Company is a wholly-owned subsidiary of Hydro One. As such, the assets of the Distribution Business are available to satisfy the debts, contingent liabilities and commitments of both the Company and Hydro One

23. COMMITMENTS

The Company and Hydro One have numerous commitments. These commitments have not been specifically allocated to the Distribution Business. However, the assets of the Distribution Business are available to satisfy the commitments of both the Company and Hydro One.

24. SUBSEQUENT EVENTS

Long-term Debt

On February 24, 2016, Hydro One issued the following notes under its MTN Program:

- $500 million notes with a maturity date of February 24, 2021 and a coupon rate of 1.84%. This issuance was mirrored down to Hydro One Networks through the issuance of inter-company debt with a coupon rate of 1.86%, of which $250 million was allocated to the Company's Distribution Business;
- $500 million notes with a maturity date of February 24, 2026 and a coupon rate of 2.77%. $490 million of this issuance was mirrored down to Hydro One Networks through the issuance of inter-company debt with a coupon rate of 2.79%, of which $245 million was allocated to the Company's Distribution Business; and
- $350 million notes with a maturity date of February 23, 2046 and a coupon rate of 3.91%. This issuance was mirrored down to Hydro One Networks through the issuance of inter-company debt with a coupon rate of 3.93%, of which $175 million was allocated to the Company's Distribution Business.

On March 3, 2016, Hydro One repaid $450 million of maturing long-term debt notes under its MTN Program. On the same date, Hydro One Networks repaid inter-company debt of $450 million to Hydro One, of which $180 million was allocated to the Company's Distribution Business.

Payments to Finance Dividends

On February 11, 2016, Hydro One Networks declared common share dividends in the amount of $2 million, and a return of stated capital in the amount of $225 million was approved. The amount allocated to the Distribution Business to finance these payments was $114 million, of which $12 million was paid on February 22, 2016.

HYDRO ONE NETWORKS INC.

DISTRIBUTION BUSINESS

FINANCIAL STATEMENTS

DECEMBER 31, 2014

HYDRO ONE NETWORKS INC.
DISTRIBUTION BUSINESS
INDEPENDENT AUDITORS' REPORT

To the Directors of Hydro One Networks Inc.

We have audited the accompanying carve-out financial statements of the Distribution Business (a business of Hydro One Networks Inc.), which comprise the carve-out balance sheet as at December 31, 2014, the carve-out statements of operations and comprehensive income, and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information. The carve-out financial statements have been prepared by management in accordance with the basis of accounting in Note 2 to the carve-out financial statements.

Management's Responsibility for the Carve-out Financial Statements

Management of Hydro One Networks Inc. is responsible for the preparation of these carve-out financial statements in accordance with the basis of accounting in Note 2 to the carve-out financial statements; this includes determining that the basis of accounting is an acceptable basis for the preparation of these carve-out financial statements in the circumstances, and for such internal control as management determines is necessary to enable the preparation of carve-out 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 carve-out 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 carve-out financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the carve-out financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the carve-out financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation of the carve-out 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 carve-out 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 carve-out financial statements as at and for the year ended December 31, 2014 are prepared, in all material respects, in accordance with the basis of accounting in Note 2 to the carve-out financial statements.

Basis of Accounting and Restriction of Use

Without modifying our opinion, we draw attention to Note 2 to the carve-out financial statements, which describes the basis of preparation used in these carve-out financial statements. In particular, in preparing the carve-out financial statements, long-term debt, shared functions and service costs, and payments in lieu of corporate income taxes have been allocated to the Distribution Business (a business of Hydro One Networks Inc.) using the method of allocation described in Note 2 to the carve-out financial statements. As a result, the carve-out financial statements may not necessarily be identical to the balance sheet, results of operations and cash flows that would have resulted had the Distribution Business (a business of Hydro One Networks Inc.) historically operated on a stand-alone basis. The carve-out financial statements are prepared to assist Hydro One Networks Inc. to comply with its reporting requirements of the Ontario Energy Board. As a result, the carve-out financial statements may not be suitable for another purpose.

Our report is intended solely for the Directors of Hydro One Networks Inc. and the Ontario Energy Board and should not be used by parties other than Hydro One Networks Inc. or the Ontario Energy Board.

KPMG LLP

Chartered Professional Accountants, Licensed Public Accountants
Toronto, Canada
March 24, 2015

HYDRO ONE NETWORKS INC.
DISTRIBUTION BUSINESS
STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME
For the years ended December 31, 2014 and 2013

Year ended December 31 (millions of Canadian dollars)	**2014**	**2013**
Revenues		
Energy sales	4,176	3,806
Rural rate protection *(Note 18)*	126	125
Other	38	40
	4,340	3,971
Costs		
Purchased power *(Note 18)*	2,979	2,620
Operation, maintenance and administration *(Note 18)*	675	611
Depreciation and amortization *(Note 4)*	347	321
	4,001	3,552
Income before financing charges and provision for payments in lieu of corporate income taxes	339	419
Financing charges *(Notes 5, 18)*	147	137
Income before provision for payments in lieu of corporate income taxes	192	282
Provision for payments in lieu of corporate income taxes *(Notes 6, 18)*	3	24
Net income	189	258
Other comprehensive income	–	–
Comprehensive income	189	258

See accompanying notes to Financial Statements.

HYDRO ONE NETWORKS INC.
DISTRIBUTION BUSINESS
BALANCE SHEETS
At December 31, 2014 and 2013

December 31 (millions of Canadian dollars)	**2014**	**2013**
Assets		
Current assets:		
Inter-company demand facility *(Notes 12, 13, 18)*	–	47
Accounts receivable (net of allowance for doubtful accounts – $64; 2013 – $32) *(Notes 7,18)*	985	853
Regulatory assets *(Note 10)*	11	15
Materials and supplies	7	6
Deferred income tax assets *(Note 6)*	9	8
Derivative instruments *(Note 12)*	1	1
Other	13	11
	1,026	941
Property, plant and equipment *(Note 8)*:		
Property, plant and equipment in service	9,426	8,864
Less: accumulated depreciation	3,503	3,279
	5,923	5,585
Construction in progress	326	323
Future use land, components and spares	49	45
	6,298	5,953
Other long-term assets:		
Regulatory assets *(Note 10)*	789	705
Intangible assets (net of accumulated amortization – $179; 2013 – $145) *(Note 9)*	197	204
Goodwill	73	73
Deferred debt costs	13	13
Derivative instruments *(Note 12)*	–	2
Other	3	–
	1,075	997
Total assets	8,399	7,891

See accompanying notes to Financial Statements.

HYDRO ONE NETWORKS INC.
DISTRIBUTION BUSINESS
BALANCE SHEETS (continued)
At December 31, 2014 and 2013

December 31 (millions of Canadian dollars)	**2014**	**2013**
Liabilities		
Current liabilities:		
Inter-company demand facility	225	–
Accounts payable	65	59
Accrued liabilities *(Notes 6, 14, 15, 18)*	605	592
Accrued interest *(Note 18)*	38	38
Regulatory liabilities *(Note 10)*	8	26
Long-term debt payable within one year *(Notes 11, 12, 13, 18)*	221	176
	1,162	891
Long-term debt *(Notes 11, 12, 13, 18)*	3,161	3,140
Other long-term liabilities:		
Post-retirement and post-employment benefit liability *(Note 14)*	844	824
Deferred income tax liabilities *(Note 6)*	388	306
Environmental liabilities *(Note 15)*	124	139
Regulatory liabilities *(Note 10)*	110	110
Net unamortized debt premiums	10	11
Asset retirement obligations *(Note 16)*	4	4
Long-term accounts payable and other liabilities	1	1
	1,481	1,395
Total liabilities	5,804	5,426
Contingencies and commitments (Notes 20, 21)		
Excess of assets over liabilities *(Notes 13, 17)*	2,595	2,465
Total liabilities and excess of assets over liabilities	8,399	7,891

See accompanying notes to Financial Statements.

On behalf of the Board of Directors:

Carmine Marcello
Chair

Ali R. Suleman
Director

HYDRO ONE NETWORKS INC.
DISTRIBUTION BUSINESS
STATEMENTS OF CASH FLOWS
For the years ended December 31, 2014 and 2013

Year ended December 31 (millions of Canadian dollars)	**2014**	**2013**
Operating activities		
Net income	189	258
Environmental expenditures	(10)	(9)
Adjustments for non-cash items:		
Depreciation and amortization (excluding removal costs)	295	270
Regulatory assets and liabilities	(58)	(12)
Deferred income taxes	15	3
Other	1	2
Changes in non-cash balances related to operations *(Note 19)*	(80)	(30)
Net cash from operating activities	352	482
Financing activities		
Long-term debt issued	243	533
Long-term debt retired	(175)	(230)
Payments to Hydro One Inc. to finance dividends	(59)	(112)
Other	(1)	(2)
Net cash from financing activities	8	189
Investing activities		
Capital expenditures *(Note 19)*		
Property, plant and equipment	(614)	(563)
Intangible assets	(14)	(66)
Other	(4)	–
Net cash used in investing activities	(632)	(629)
Net change in inter-company demand facility	(272)	42
Inter-company demand facility, beginning of year	47	5
Inter-company demand facility, end of year	(225)	47

See accompanying notes to Financial Statements.

1. DESCRIPTION OF THE BUSINESS

Hydro One Inc. (Hydro One) was incorporated on December 1, 1998, under the *Business Corporations Act* (Ontario) and is wholly owned by the Province of Ontario (Province). The principal businesses of Hydro One are the transmission and distribution of electricity to customers within Ontario.

Hydro One Networks Inc. (Hydro One Networks or the Company) was incorporated on March 4, 1999 under the *Business Corporations Act* (Ontario) and is a wholly-owned subsidiary of Hydro One. The Company owns and operates Hydro One's regulated transmission and distribution businesses. The regulated distribution business (Distribution Business) operates a low-voltage electrical distribution network that distributes electricity from the transmission system, or directly from generators, to customers within Ontario. The Distribution Business is regulated by the Ontario Energy Board (OEB).

2. SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting

These Financial Statements are prepared and presented in accordance with the accounting policies summarized below and in Canadian dollars. These policies are consistent with United States (US) Generally Accepted Accounting Principles (GAAP). These Financial Statements have been prepared for the specific use of the OEB. Consolidated Financial Statements of Hydro One for the year ended December 31, 2014 have been prepared and are publicly available.

These Financial Statements have been prepared on a carve-out basis to provide the financial position, results of operations and cash flows of the Company's regulated Distribution Business on a basis approved by the OEB. The Financial Statements are considered by management to be a reasonable representation, prepared on a rational, systematic and consistent basis, of the financial results of the Company's Distribution Business. As a result of this basis of accounting, these Financial Statements may not necessarily be identical to the financial position and results of operations that would have resulted had the Distribution Business historically operated on a stand-alone basis.

The Financial Statements have been constructed primarily through specific identification of assets, liabilities (other than debt), revenues and expenses that relate to the Distribution Business. The Company's long-term debt is allocated based on the respective borrowing requirements of the Company's transmission and distribution businesses. A portion of the Company's shared functions and services costs is allocated to the Distribution Business on a fully allocated-cost basis, consistent with OEB-approved independent studies. Payments in lieu of corporate income taxes (PILs) have been recorded at effective rates based on income taxes as reported in the Statements of Operations and Comprehensive Income as though the Distribution Business was a separate taxpaying entity. Certain other amounts presented in these Financial Statements represent allocations subject to review and approval by the OEB.

Hydro One Networks performed an evaluation of subsequent events through to March 24, 2015, the date these Financial Statements were available to be issued, to determine whether any events or transactions warranted recognition and disclosure in these financial statements. See Note 22 – Subsequent Event.

Use of Management Estimates

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues, expenses, gains and losses during the reporting periods. Management evaluates these estimates on an on-going basis based upon: historical experience; current conditions; and assumptions believed to be reasonable at the time the assumptions are made with any adjustments being recognized in results of operations in the period they arise. Significant estimates relate to regulatory assets and regulatory liabilities, environmental liabilities, post-retirement and post-employment benefits, asset retirement obligations (AROs), goodwill and asset impairments, contingencies, unbilled revenues, allowance for doubtful accounts, derivative instruments, and deferred income tax assets and liabilities. Actual results may differ significantly from these estimates, which may be impacted by future decisions made by the OEB or the Province.

Rate Setting

The OEB has approved the use of US GAAP for rate setting and regulatory accounting and reporting by the Company's Distribution Business beginning with the year 2012.

In June 2012, Hydro One Networks filed an Incentive Regulation Mechanism (IRM) application with the OEB for 2013 distribution rates, to be effective January 1, 2013. In December 2012, the OEB issued its final Decision, which resulted in an increase in distribution rates of approximately 1.3% in 2013, or 0.4% when considering total bill impact, for a typical residential customer consuming 800 kWh per month. In April 2013, Hydro One Networks filed an IRM application with the OEB for 2014 distribution rates, to be effective January 1, 2014. In December 2013, the OEB issued its final Decision, which resulted in an increase in distribution rates of approximately 2.4% in 2014, or 0.85% when considering total bill impact, for a typical residential customer consuming 800 kWh per month.

Regulatory Accounting

The OEB has the general power to include or exclude revenues, costs, gains or losses in the rates of a specific period, resulting in a change in the timing of accounting recognition from that which would have applied in an unregulated company. Such change in timing involves the application of rate-regulated accounting, giving rise to the recognition of regulatory assets and liabilities. The Distribution Business' regulatory assets represent certain amounts receivable from future customers and costs that have been deferred for accounting purposes because it is probable that they will be recovered in future rates. In addition, the Distribution Business has recorded regulatory liabilities that generally represent amounts that are refundable to future customers. The Distribution Business continually assesses the likelihood of recovery of each of its regulatory assets and continues to believe that it is probable that the OEB will factor its regulatory assets and liabilities into the setting of future rates. If, at some future date, the Distribution Business judges that it is no longer probable that the OEB will include a regulatory asset or liability in setting future rates, the appropriate carrying amount will be reflected in results of operations in the period that the assessment is made.

Revenue Recognition

Distribution revenues are recognized on an accrual basis and include billed and unbilled revenues. Distribution revenues attributable to the delivery of electricity are based on OEB-approved distribution rates and are recognized as electricity is delivered to customers. The Company estimates monthly revenue for a period based on wholesale electricity purchases because customer meters are not generally read at the end of each month. At the end of each month, the electricity delivered to customers, but not billed, is estimated and revenue is recognized. The unbilled revenue estimate is affected by energy demand, weather, line losses and changes in the composition of customer classes. Distribution revenue also includes an amount relating to rate protection for rural, residential and remote customers, which is received from the Independent Electricity System Operator (IESO) based on a standardized customer rate that is approved by the OEB. Current legislation provides rate protection for prescribed classes of rural, residential and remote consumers by reducing the electricity rates that would otherwise apply. Revenues are recorded net of indirect taxes.

Accounts Receivable and Allowance for Doubtful Accounts

Billed accounts receivable are recorded at the invoiced amount, net of allowance for doubtful accounts. Unbilled accounts receivable are estimated and recorded based on wholesale electricity purchases. Overdue amounts related to regulated billings bear interest at OEB-approved rates. The allowance for doubtful accounts reflects the Distribution Business' best estimate of losses on billed accounts receivable balances. The allowance is based on accounts receivable aging, historical experience and other currently available information. The Distribution Business estimates the allowance for doubtful accounts on customer receivables by applying internally developed loss rates to the outstanding receivable balances by risk segment. Risk segments represent groups of customers with similar credit quality indicators and are computed based on various attributes, including number of days receivables are past due, delinquency of balances and payment history. Loss rates applied to the accounts receivable balances are based on historical average write-offs as a percentage of accounts receivable in each risk segment. An account is considered delinquent if the amount billed is not received within 110 days of the invoiced date. Accounts receivable are written off against the allowance when they are deemed uncollectible. The existing allowance for uncollectible accounts will continue to be affected by changes in volume, prices and economic conditions.

Corporate Income Taxes

Under the *Electricity Act, 1998*, Hydro One Networks is required to remit PILs to the Ontario Electricity Financial Corporation (OEFC). These payments are calculated in accordance with the rules for computing income and other relevant amounts contained in the *Income Tax Act* (Canada) and the *Taxation Act, 2007* (Ontario) as modified by the *Electricity Act, 1998* and related regulations.

Current and deferred income taxes are computed based on the tax rates and tax laws enacted at the balance sheet date. Tax benefits associated with income tax positions taken, or expected to be taken, in a tax return are recorded only when the "more-likely-than-not" recognition threshold is satisfied and are measured at the largest amount of benefit that has a greater than 50% likelihood of being realized upon settlement. Management evaluates each position based solely on the technical merits and facts and circumstances of the position, assuming the position will be examined by a taxing authority having full knowledge of all relevant information. Significant management judgment is required to determine recognition thresholds and the related amount of tax benefits to be recognized in the Financial Statements. Management re-evaluates tax positions each period in which new information about recognition or measurement becomes available.

Current Income Taxes

The provision for current taxes and the assets and liabilities recognized for the current and prior periods are measured at the amounts receivable from, or payable to, the OEFC.

Deferred Income Taxes

Deferred income taxes are provided for using the liability method. Deferred income taxes are recognized based on the estimated future tax consequences attributable to temporary differences between the carrying amount of assets and liabilities in the Financial Statements and their corresponding tax bases.

Deferred income tax liabilities are generally recognized on all taxable temporary differences. Deferred tax assets are recognized to the extent that it is more-likely-than-not that these assets will be realized from taxable income available against which deductible temporary differences can be utilized.

Deferred income taxes are calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realized, based on the tax rates and tax laws that have been enacted at the balance sheet date. Deferred income taxes that are not included in the rate-setting process are charged or credited to the Statements of Operations and Comprehensive Income.

If management determines that it is more-likely-than-not that some or all of a deferred income tax asset will not be realized, a valuation allowance is recorded against the deferred income tax asset to report the net asset balance at the amount expected to be realized. Previously unrecognized deferred income tax assets are reassessed at each balance sheet date and are recognized to the extent that it has become more-likely-than-not that the tax benefit will be realized.

The Distribution Business has recognized regulatory assets and liabilities associated with deferred income taxes that will be included in the rate-setting process.

The Distribution Business uses the flow-through method to account for investment tax credits (ITCs) earned on eligible scientific research and experimental development expenditures, and apprenticeship job creation. Under this method, only non-refundable ITCs are recognized as a reduction to income tax expense.

Inter-company Demand Facility

Hydro One maintains pooled bank accounts for its use and for the use of its subsidiaries, and implicitly, by the regulated businesses of its subsidiaries. The balance in the inter-company demand facility represents the cumulative net effect of all deposits and withdrawals made by the Distribution Business to and from the pooled bank accounts. Interest is earned on

positive inter-company balances based on the average of the bankers' acceptance rate at the beginning and end of the month, less 0.02%. Interest is charged on overdraft inter-company balances based on the same bankers' acceptance rate, plus 0.15%.

Materials and Supplies

Materials and supplies represent consumables, small spare parts and construction materials held for internal construction and maintenance of property, plant and equipment. These assets are carried at average cost less any impairments recorded.

Property, Plant and Equipment

Property, plant and equipment is recorded at original cost, net of customer contributions received in aid of construction and any accumulated impairment losses. The cost of additions, including betterments and replacements of asset components, is included on the Balance Sheets as property, plant and equipment.

The original cost of property, plant and equipment includes direct materials, direct labour (including employee benefits), contracted services, attributable capitalized financing costs, asset retirement costs, and direct and indirect overheads that are related to the capital project or program. Indirect overhead includes a portion of corporate costs such as finance, treasury, human resources, information technology and executive costs. Overhead costs, including corporate functions and field services costs, are capitalized on a fully allocated basis, consistent with an OEB-approved methodology.

Property, plant and equipment in service consists of distribution, communication, administration and service assets and land easements. Property, plant and equipment also includes future use assets, such as land, major components and spare parts, and capitalized project development costs associated with deferred capital projects.

Distribution

Distribution assets include assets related to the distribution of low-voltage electricity, including lines, poles, switches, transformers, protective devices and metering systems.

Communication

Communication assets include the fibre-optic and microwave radio system, optical ground wire, towers, telephone equipment and associated buildings.

Administration and Service

Administration and service assets include administrative buildings, personal computers, transport and work equipment, tools and other minor assets.

Easements

Easements include amounts incurred to acquire land rights and other access rights.

Intangible Assets

Intangible assets separately acquired or internally developed are measured on initial recognition at cost, which comprises purchased software, direct labour (including employee benefits), consulting, engineering, overheads and attributable capitalized financing charges. Following initial recognition, intangible assets are carried at cost, net of any accumulated amortization and accumulated impairment losses. The Distribution Business' intangible assets primarily represent major administrative computer applications.

Capitalized Financing Costs

Capitalized financing costs represent interest costs attributable to the construction of property, plant and equipment or development of intangible assets. The financing cost of attributable borrowed funds is capitalized as part of the acquisition cost of such assets. The capitalized portion of financing costs is a reduction to financing charges recognized in the Statements of Operations and Comprehensive Income. Capitalized financing costs are calculated using the Company's weighted average effective cost of debt.

Construction and Development in Progress

Construction and development in progress consists of the capitalized cost of constructed assets that are not yet complete and which have not yet been placed in service.

Depreciation and Amortization

The cost of property, plant and equipment and intangible assets is depreciated or amortized on a straight-line basis based on the estimated remaining service life of each asset category, except for transport and work equipment, which is depreciated on a declining balance basis.

Hydro One periodically initiates an external independent review of its property, plant and equipment and intangible asset depreciation and amortization rates, as required by the OEB. Any changes arising from OEB approval of such a review are implemented on a remaining service life basis, consistent with their inclusion in electricity rates. The last review resulted in changes to rates effective January 1, 2013. A summary of average service lives and depreciation and amortization rates for the various classes of assets is included below:

	Average Service Life	Rate (%) Range	Rate (%) Average
Distribution	43 years	1% – 20%	2%
Communication	13 years	1% – 9%	5%
Administration and service	15 years	3% – 20%	8%

The cost of intangible assets is included primarily within the administration and service classification above. Amortization rates for computer applications software assets range from 9% to 10%.

In accordance with group depreciation practices, the original cost of property, plant and equipment, or major components thereof, and intangible assets that are normally retired, is charged to accumulated depreciation and amortization, with no gain or loss being reflected in results of operations. Where a disposition of property, plant and equipment occurs through sale, a gain or loss is calculated based on proceeds and such gain or loss is included in depreciation expense. Depreciation expense also includes the costs incurred to remove property, plant and equipment where no ARO has been recorded.

Goodwill

Goodwill represents the cost of acquired local distribution companies that is in excess of the fair value of the net identifiable assets acquired at the acquisition date. Goodwill is not included in rate base.

Goodwill is evaluated for impairment on an annual basis, or more frequently if circumstances require. The Company performs a qualitative assessment to determine whether it is more-likely-than-not that the fair value of the applicable reporting unit is less than its carrying amount. If the Company determines, as a result of its qualitative assessment, that it is not more-likely-than-not that the fair value of the applicable reporting unit is less than its carrying amount, no further testing is required. If the Company determines, as a result of its qualitative assessment, that it is more-likely-than-not that the fair value of the applicable reporting unit is less than its carrying amount, a goodwill impairment assessment is performed using a two-step, fair value-based test. The first step compares the fair value of the applicable reporting unit to its carrying amount, including goodwill. If the carrying amount of the applicable reporting unit exceeds its fair value, a second step is performed. The second step requires an allocation of fair value to the individual assets and liabilities using purchase price allocation in

order to determine the implied fair value of goodwill. If the implied fair value of goodwill is less than the carrying amount, an impairment loss is recorded as a reduction to goodwill and as a charge to results of operations.

For the year ended December 31, 2014, based on the qualitative assessment performed as at September 30, 2014, the Company has determined that it is not more-likely-than-not that the fair value of each applicable reporting unit assessed is less than its carrying amount. As a result, no further testing was performed, and the Company has concluded that goodwill was not impaired at December 31, 2014.

Long-Lived Asset Impairment

When circumstances indicate the carrying value of long-lived assets may not be recoverable, the Company evaluates whether the carrying value of such assets, excluding goodwill, has been impaired. For such long-lived assets, impairment exists when the carrying value exceeds the sum of the future estimated undiscounted cash flows expected to result from the use and eventual disposition of the asset. When alternative courses of action to recover the carrying amount of a long-lived asset are under consideration, a probability-weighted approach is used to develop estimates of future undiscounted cash flows. If the carrying value of the long-lived asset is not recoverable based on the estimated future undiscounted cash flows, an impairment loss is recorded, measured as the excess of the carrying value of the asset over its fair value. As a result, the asset’s carrying value is adjusted to its estimated fair value.

The carrying costs of most of the Distribution Business’ long-lived assets are included in rate base where they earn an OEB-approved rate of return. Asset carrying values and the return are recovered through approved rates. As a result, such assets are only tested for impairment in the event that the OEB disallows recovery, in whole or in part, or if such a disallowance is judged to be probable. As at December 31, 2014, no asset impairment had been recorded.

Costs of Arranging Debt Financing

For financial liabilities classified as other than held-for-trading, the Company defers its proportionate share of the relevant Hydro One external transaction costs related to obtaining debt financing and presents such amounts as deferred debt costs on the Balance Sheets. Deferred debt costs are amortized over the contractual life of the related debt on an effective-interest basis and the amortization is included within financing charges in the Statements of Operations and Comprehensive Income. Transaction costs for items classified as held-for-trading are expensed immediately.

Comprehensive Income

Comprehensive income is comprised of net income and other comprehensive income (OCI). OCI and net income are presented in a single continuous Statement of Operations and Comprehensive Income.

Financial Assets and Liabilities

All financial assets and liabilities are classified into one of the following five categories: held-to-maturity investments; loans and receivables; held-for-trading; other liabilities; or available-for-sale. Financial assets and liabilities classified as held-for-trading are measured at fair value. All other financial assets and liabilities are measured at amortized cost, except accounts receivable which are measured at the lower of cost or fair value. Accounts receivable are classified as loans and receivables. The Company considers the carrying amount of accounts receivable to be a reasonable estimate of fair value because of the short time to maturity of these instruments. Provisions for impaired accounts receivable are recognized as adjustments to the allowance for doubtful accounts and are recognized when there is objective evidence that the Company will not be able to collect amounts according to the original terms. All financial instrument transactions are recorded at trade date.

Derivative instruments are measured at fair value. Gains and losses from fair valuation are included within financing charges in the period in which they arise. Hydro One Networks determines the classification of its financial assets and liabilities at the date of initial recognition. The Company designates certain of its financial assets and liabilities to be held at fair value, when it is consistent with its risk management policy disclosed in Note 12 – Fair Value of Financial Instruments and Risk Management.

Derivative Instruments and Hedge Accounting

Hydro One closely monitors the risks associated with changes in interest rates on its operations and, where appropriate, uses various derivative instruments to hedge these risks. Certain of these derivative instruments qualify for hedge accounting and are designated as accounting hedges, while others either do not qualify as hedges or have not been designated as hedges (hereinafter referred to as undesignated contracts) as they are part of economic hedge relationships. Hydro One's derivative instruments, or portions thereof, are mirrored down to Hydro One Networks, and are allocated between the Company's transmission and distribution businesses. The derivative instruments are classified as fair value hedges or undesignated contracts, consistent with Hydro One's derivative instruments classification.

The accounting guidance for derivative instruments requires the recognition of all derivative instruments not identified as meeting the normal purchase and sale exemption as either assets or liabilities recorded at fair value on the Balance Sheets. For derivative instruments that qualify for hedge accounting, Hydro One may elect to designate such derivative instruments as either cash flow hedges or fair value hedges. Hydro One offsets fair value amounts recognized in its Balance Sheets related to derivative instruments executed with the same counterparty under the same master netting agreement.

For derivative instruments that qualify for hedge accounting and which are designated as cash flow hedges, the effective portion of any gain or loss, net of tax, is reported as a component of accumulated OCI (AOCI) and is reclassified to results of operations in the same period or periods during which the hedged transaction affects results of operations. Any gains or losses on the derivative instrument that represent either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness are recognized in results of operations. For fair value hedges, changes in fair value of both the derivative instrument and the underlying hedged exposure are recognized in the Statement of Operations and Comprehensive Income in the current period. The gain or loss on the derivative instrument is included in the same line item as the offsetting gain or loss on the hedged item in the Statements of Operations and Comprehensive Income. Additionally, Hydro One enters into derivative agreements that are economic hedges that either do not qualify for hedge accounting or have not been designated as hedges. The changes in fair value of these undesignated derivative instruments are reflected in results of operations.

Embedded derivative instruments are separated from their host contracts and carried at fair value on the Balance Sheets when: (a) the economic characteristics and risks of the embedded derivative are not clearly and closely related to the economic characteristics and risks of the host contract; (b) the hybrid instrument is not measured at fair value, with changes in fair value recognized in results of operations each period; and (c) the embedded derivative itself meets the definition of a derivative. Hydro One does not engage in derivative trading or speculative activities and had no embedded derivatives at December 31, 2014.

Hydro One periodically develops hedging strategies taking into account risk management objectives. At the inception of a hedging relationship where Hydro One has elected to apply hedge accounting, Hydro One formally documents the relationship between the hedged item and the hedging instrument, the related risk management objective, the nature of the specific risk exposure being hedged, and the method for assessing the effectiveness of the hedging relationship. Hydro One also assesses, both at the inception of the hedge and on a quarterly basis, whether the hedging instruments are effective in offsetting changes in fair values or cash flows of the hedged items.

Employee Future Benefits

Employee future benefits provided by Hydro One include pension, post-retirement and post-employment benefits. The costs of the pension, post-retirement and post-employment benefit plans are recorded over the periods during which employees render service.

Hydro One recognizes the funded status of its pension, post-retirement and post-employment plans on its Consolidated Balance Sheets and subsequently recognizes the changes in funded status at the end of each reporting year. Pension, post-retirement and post-employment funds are considered to be underfunded when the projected benefit obligation exceeds the fair value of the plan assets. Liabilities are recognized on the Consolidated Balance Sheets of Hydro One for any net underfunded projected benefit obligation. The net underfunded projected benefit obligation may be disclosed as a current liability, long-term liability, or both. The current portion is the amount by which the actuarial present value of benefits

included in the benefit obligation payable in the next 12 months exceeds the fair value of plan assets. If the fair value of plan assets exceeds the projected benefit obligation of the plan, an asset is recognized equal to the net overfunded projected benefit obligation. The post-retirement and post-employment benefit plans are unfunded because there are no related plan assets. For the year ended December 31, 2014, the measurement date for the Plans was December 31.

Pension benefits

Hydro One has a contributory defined benefit pension plan covering all regular employees of Hydro One and its subsidiaries, except Hydro One Brampton Networks Inc. The Hydro One pension plan does not segregate assets in a separate account for individual subsidiaries, nor is the accrual cost of the pension plan allocated to, or funded separately by, entities within the consolidated group. Consequently, for purposes of these financial statements, the pension plan is accounted for as a defined contribution plan and no deferred pension asset or liability is recorded.

A detailed description of Hydro One pension benefits is provided in Note 15 – Pension and Post-Retirement and Post-Employment Benefits, to the Consolidated Financial Statements of Hydro One for the year ended December 31, 2014.

Post-retirement and post-employment benefits

Post-retirement and post-employment benefits are recorded and included in rates on an accrual basis. Costs are determined by independent actuaries using the projected benefit method prorated on service and based on assumptions that reflect management's best estimates. Past service costs from plan amendments are amortized to results of operations based on the expected average remaining service period.

The Company records a regulatory asset equal to the incremental net unfunded projected benefit obligation for post-retirement and post-employment plans at each year end based on annual actuarial reports. The regulatory asset for the incremental net unfunded projected benefit obligation for post-retirement and post-employment plans, in absence of regulatory accounting, would be recognized in AOCI. A regulatory asset is recognized because management considers it to be probable that post-retirement and post-employment benefit costs will be recovered in the future through the rate-setting process.

For post-retirement benefits, all actuarial gains or losses are deferred using the "corridor" approach. The amount calculated above the "corridor" is amortized to results of operations on a straight-line basis over the expected average remaining service life of active employees in the plan and over the remaining life expectancy of inactive employees in the plan. The post-retirement benefit obligation is remeasured to its fair value at each year end based on an annual actuarial report, with an offset to associated regulatory asset, to the extent of the remeasurement adjustment.

For post-employment obligations, the actuarial gains and losses that are incurred during the year are recognized immediately to results of operations. The post-employment benefit obligation is remeasured to its fair value at each year end based on an annual actuarial report, with an offset to associated regulatory asset, to the extent of the remeasurement adjustment.

All post-retirement and post-employment future benefit costs are attributed to labour and are either charged to results of operations or capitalized as part of the cost of property, plant and equipment and intangible assets.

A detailed description of Hydro One post-retirement and post-employment benefits is provided in Note 15 – Pension and Post-Retirement and Post-Employment Benefits, to the Consolidated Financial Statements of Hydro One for the year ended December 31, 2014.

Loss Contingencies

Hydro One and its subsidiaries are involved in certain legal and environmental matters that arise in the normal course of business. In the preparation of the Distribution Business' Financial Statements, management makes judgments regarding the future outcome of contingent events and records a loss for a contingency based on its best estimate when it is determined that such loss is probable and the amount of the loss can be reasonably estimated. Where the loss amount is recoverable in future

rates, a regulatory asset is also recorded. When a range estimate for the probable loss exists and no amount within the range is a better estimate than any other amount, the Distribution Business records a loss at the minimum amount within the range.

Management regularly reviews current information available to determine whether recorded provisions should be adjusted and whether new provisions are required. Estimating probable losses may require analysis of multiple forecasts and scenarios that often depend on judgments about potential actions by third parties, such as federal, provincial and local courts or regulators. Contingent liabilities are often resolved over long periods of time. Amounts recorded in the Financial Statements may differ from the actual outcome once the contingency is resolved. Such differences could have a material impact on future results of operations, financial position and cash flows of the Distribution Business.

Provisions are based upon current estimates and are subject to greater uncertainty where the projection period is lengthy. A significant upward or downward trend in the number of claims filed, the nature of the alleged injuries, and the average cost of resolving each claim could change the estimated provision, as could any substantial adverse or favorable verdict at trial. A federal or provincial legislative outcome or structured settlement could also change the estimated liability. Legal fees are expensed as incurred.

Environmental Liabilities

Environmental liabilities are recorded in respect of past contamination when it is determined that future environmental remediation expenditures are probable under existing statute or regulation and the amount of the future expenditures can be reasonably estimated. The Distribution Business records a liability for the estimated future expenditures associated with the contaminated land assessment and remediation (LAR) and for the phase-out and destruction of polychlorinated biphenyl (PCB)-contaminated mineral oil removed from electrical equipment, based on the present value of these estimated future expenditures. The present value is determined with a discount rate equal to its credit-adjusted risk-free interest rate on financial instruments with comparable maturities to the pattern of future environmental expenditures. As it is anticipated that the future expenditures will continue to be recoverable in future rates, an offsetting regulatory asset has been recorded to reflect the future recovery of these environmental expenditures from customers. The estimates of future environmental expenditures are reviewed annually or more frequently if there are indications that circumstances have changed.

Asset Retirement Obligations

AROs are recorded for legal obligations associated with the future removal and disposal of long-lived assets. Such obligations may result from the acquisition, construction, development and/or normal use of the asset. Conditional AROs are recorded when there is a legal obligation to perform a future asset retirement activity but where the timing and/or method of settlement are conditional on a future event that may or may not be within the control of the Company. In such a case, the obligation to perform the asset retirement activity is unconditional even though uncertainty exists about the timing and/or method of settlement.

When recording an ARO, the present value of the estimated future expenditures required to complete the asset retirement activity is recorded in the period in which the obligation is incurred, if a reasonable estimate can be made. In general, the present value of the estimated future expenditures is added to the carrying amount of the associated asset and the resulting asset retirement cost is depreciated over the estimated useful life of the asset. Where an asset is no longer in-service when an ARO is recorded, the asset retirement cost is recorded in results of operations.

Some distribution assets, particularly those located on unowned easements and rights-of-way, may have AROs, conditional or otherwise. The majority of the Company's easements and rights-of-way are either of perpetual duration or are automatically renewed annually. Land rights with finite terms are generally subject to extension or renewal. As the Distribution Business expects to use the majority of its facilities in perpetuity, no ARO currently exists for these assets. If, at some future date, a particular facility is shown not to meet the perpetuity assumption, it will be reviewed to determine whether an estimable ARO exists. In such case, an ARO would be recorded at that time.

The Distribution Business' AROs recorded to date relate to estimated future expenditures associated with the removal and disposal of asbestos-containing materials installed in some of its facilities and with the decommissioning of specific switching stations located on unowned sites.

3. NEW ACCOUNTING PRONOUNCEMENTS

Recently Adopted Accounting Pronouncements

In July 2013, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2013-11, Income Taxes (Topic 740): Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists. This ASU provides guidance on the presentation of unrecognized tax benefits. This ASU is effective for fiscal years, and interim periods within those years, beginning after December 15, 2013, and should be applied prospectively to all unrecognized tax benefits that exist at the effective date. The adoption of this ASU did not have a significant impact on the Distribution Business' financial statements.

Recent Accounting Guidance Not Yet Adopted

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers (Topic 606). This ASU provides guidance on revenue recognition that depicts the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods and services. This ASU is required to be applied retrospectively and is effective for fiscal years, and interim periods within those years, beginning after December 15, 2016. The Distribution Business is currently assessing the impact of adoption of ASU 2014-09 on its financial statements.

In August 2014, the FASB issued ASU 2014-15, Presentation of Financial Statements – Going Concern (Subtopic 205-40): Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern. This ASU provides guidance about management's responsibility to evaluate whether there is substantial doubt about an entity's ability to continue as a going concern and related disclosures. This ASU is effective for the annual period ending December 31, 2016, and for annual and interim periods thereafter. The adoption of this ASU is not anticipated to have a significant impact on the Distribution Business' financial statements.

4. DEPRECIATION AND AMORTIZATION

Year ended December 31 (millions of Canadian dollars)	**2014**	**2013**
Depreciation of property, plant and equipment	250	235
Amortization of intangible assets	34	26
Asset removal costs	52	51
Amortization of regulatory assets	11	9
	347	321

5. FINANCING CHARGES

Year ended December 31 (millions of Canadian dollars)	**2014**	**2013**
Interest on long-term debt *(Note 18)*	158	150
Other	6	5
Interest on inter-company demand facility *(Note 18)*	1	1
Less: Interest capitalized on construction and development in progress	(15)	(16)
Gain on interest-rate swap agreements	(3)	(3)
	147	137

6. PROVISION FOR PAYMENTS IN LIEU OF CORPORATE INCOME TAXES

The provision for PILs differs from the amount that would have been recorded using the combined Canadian Federal and Ontario statutory income tax rate. The reconciliation between the statutory and the effective tax rates is provided as follows:

Year ended December 31 (millions of Canadian dollars)	**2014**	**2013**
Income before provision for PILs	192	282
Canadian Federal and Ontario statutory income tax rate	26.50%	26.50%
Provision for PILs at statutory rate	51	75
Increase (decrease) resulting from:		
Net temporary differences included in amounts charged to customers:		
Capital cost allowance in excess of depreciation and amortization	(25)	(28)
Pension contributions in excess of pension expense	(12)	(10)
Overheads capitalized for accounting but deducted for tax purposes	(6)	(6)
Prior year's adjustment	–	(5)
Interest capitalized for accounting but deducted for tax purposes	(4)	(4)
Environmental expenditures	(3)	(2)
Non-refundable ITCs	(2)	(2)
Post-retirement and post-employment benefit expense in excess of cash payments	2	3
Other	1	2
Net temporary differences	(49)	(52)
Net permanent differences	1	1
Total provision for PILs	3	24
Current provision for (recovery of) PILs	(12)	21
Deferred provision for PILs	15	3
Total provision for PILs	3	24
Effective income tax rate	1.58%	8.51%

The current provision for PILs is remitted to, or received from, the OEFC. At December 31, 2014, $49 million receivable from the OEFC was included in accounts receivable on the Balance Sheet (2013 –$19 million).

The total provision for PILs includes deferred provision for PILs of $15 million (2013 – $3 million) that is not included in the rate-setting process, using the balance sheet liability method of accounting. Deferred PILs balances expected to be included in the rate-setting process are offset by regulatory assets and liabilities to reflect the anticipated recovery or disposition of these balances within future electricity rates.

Deferred Income Tax Assets and Liabilities

Deferred income tax assets and liabilities arise from differences between the carrying amounts and tax bases of the Company's assets and liabilities. At December 31, deferred income tax assets and liabilities consisted of the following:

December 31 (millions of Canadian dollars)	**2014**	**2013**
Deferred income tax liabilities		
Capital cost allowance in excess of depreciation and amortization	(626)	(547)
Regulatory amounts not recognized for tax	(93)	(87)
Goodwill	(9)	(8)
Post-retirement and post-employment benefits expense in excess of cash payments	312	304
Environmental expenses	36	39
Other	1	1
Total deferred income tax liabilities	(379)	(298)
Less: current portion	9	8
	(388)	(306)

During 2014 and 2013, there was no change in the rate applicable to future taxes.

7. ACCOUNTS RECEIVABLE

Year ended December 31 (millions of Canadian dollars)	**2014**	**2013**
Accounts receivable – billed	474	238
Accounts receivable – unbilled	575	647
Accounts receivable, gross	1,049	885
Allowance for doubtful accounts	(64)	(32)
Accounts receivable, net	985	853

The following table shows the movements in the allowance for doubtful accounts for the years ended December 31, 2014 and 2013.

Year ended December 31 (millions of Canadian dollars)	**2014**	**2013**
Allowance for doubtful accounts – January 1	(32)	(20)
Write-offs	24	23
Additions to allowance for doubtful accounts	(56)	(35)
Allowance for doubtful accounts – December 31	(64)	(32)

8. PROPERTY, PLANT AND EQUIPMENT

December 31, 2014 (millions of Canadian dollars)	Property, Plant and Equipment	Accumulated Depreciation	Construction in Progress	Total
Distribution	8,422	2,929	313	5,806
Communication	109	37	3	75
Administration and Service	935	533	10	412
Easements	9	4	–	5
	9,475	3,503	326	6,298

December 31, 2013 (millions of Canadian dollars)	Property, Plant and Equipment	Accumulated Depreciation	Construction in Progress	Total
Distribution	7,939	2,763	307	5,483
Communication	106	29	–	77
Administration and Service	855	483	16	388
Easements	9	4	–	5
	8,909	3,279	323	5,953

Financing charges capitalized on property, plant and equipment under construction were $14 million (2013 – $13 million).

9. INTANGIBLE ASSETS

December 31, 2014 (millions of Canadian dollars)	Intangible Assets	Accumulated Amortization	Development in Progress	Total
Computer applications software	356	178	19	197
Other	1	1	–	–
	357	179	19	197

December 31, 2013 (millions of Canadian dollars)	Intangible Assets	Accumulated Amortization	Development in Progress	Total
Computer applications software	347	144	1	204
Other	1	1	–	–
	348	145	1	204

Financing charges capitalized on intangible assets under development were $1 million (2013 – $3 million). The estimated annual amortization expense for intangible assets is as follows: 2015 – $33 million; 2016 – $33 million; 2017 – $33 million; 2018 – $29 million; and 2019 – $23 million.

10. REGULATORY ASSETS AND LIABILITIES

Regulatory assets and liabilities arise as a result of the rate-making process. The Distribution Business has recorded the following regulatory assets and liabilities:

December 31 (millions of Canadian dollars)	**2014**	**2013**
Regulatory assets:		
Deferred income tax regulatory asset	378	310
Post-retirement and post-employment benefits	154	172
Environmental	135	152
Pension cost variance	79	59
DSC exemption	16	7
OEB cost assessment differential	12	9
Retail settlement variance accounts	7	–
Other	19	11
Total regulatory assets	800	720
Less: current portion	11	15
	789	705

December 31 (millions of Canadian dollars)	**2014**	**2013**
Regulatory liabilities:		
Rider 11	83	54
PST savings deferral	19	14
Deferred income tax regulatory liability	8	7
Retail settlement variance accounts	–	35
Rider 9	–	19
Other	8	7
Total regulatory liabilities	118	136
Less: current portion	8	26
	110	110

Deferred Income Tax Regulatory Asset and Liability

Deferred income taxes are recognized on temporary differences between the carrying amount of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit. The Distribution Business has recognized regulatory assets and liabilities that correspond to deferred income taxes that flow through the rate-setting process. In the absence of rate-regulated accounting, the Distribution Business' provision for PILs would have been recognized using the liability method and there would be no regulatory accounts established for taxes to be reflected in future rates. As a result, the 2014 provision for PILs would have been higher by approximately $48 million (2013 – $53 million).

Post-Retirement and Post-Employment Benefits

The Distribution Business recognizes the net unfunded status of post-retirement and post-employment obligations on the Balance Sheets with an incremental offset to the associated regulatory assets. A regulatory asset is recognized because management considers it to be probable that post-retirement and post-employment benefit costs will be recovered in the future through the rate-setting process. The post-retirement and post-employment benefit obligation is remeasured to its fair value at each year end based on an annual actuarial report, with an offset to the associated regulatory asset, to the extent of the remeasurement adjustment. In the absence of rate-regulated accounting, 2014 OCI would have been higher by $18 million (2013 – $8 million).

Environmental

The Distribution Business records a liability for the estimated future expenditures required to remediate past environmental contamination. Because such expenditures are expected to be recoverable in future rates, an equivalent amount was recorded as a regulatory asset. In 2014, the environmental regulatory asset decreased by $25 million (2013 – $3 million) to reflect related changes in the PCB liability, and increased by $12 million (2013 – $18 million) due to changes in the LAR liability. The environmental regulatory asset is amortized to results of operations based on the pattern of actual expenditures incurred and charged to environmental liabilities. The OEB has the discretion to examine and assess the prudency and the timing of recovery of all of the Distribution Business' actual environmental expenditures. In the absence of rate-regulated accounting, 2014 operation, maintenance and administration expenses would have been lower by 13 million (2013 – higher by 15 million). In addition, 2014 amortization expense would have been lower by $10 million (2013 – $9 million), and 2014 financing charges would have been higher by $6 million (2013 – $6 million).

Pension Cost Variance

A pension cost variance account was established for the Distribution Business to track the difference between the actual pension expense incurred and estimated pension costs approved by the OEB. The balance in this regulatory account reflects the excess of pension costs paid as compared to OEB-approved amounts. In the absence of rate-regulated accounting, 2014 revenue would have been lower by $20 million (2013 – $13 million).

DSC Exemption

In June 2010, Hydro One Networks filed an application with the OEB regarding the OEB's new cost responsibility rules contained in the OEB's October 2009 Notice of Amendment to the Distribution System Code (DSC), with respect to the connection of certain renewable generators that were already connected or that had received a connection impact assessment prior to October 21, 2009. The application sought approval to record and defer the unanticipated costs incurred by Hydro One Networks that resulted from the connection of certain renewable generation facilities. The OEB ruled that identified specific expenditures can be recorded in a deferral account subject to the OEB's review until the next Hydro One Networks' distribution cost-of-service application. This program effectively ended at the end of 2014 with no new principal to be recorded in 2015.

OEB Cost Assessment Differential

In April 2010, the OEB announced its decision regarding the Distribution Business' rate application for 2010 and 2011. As part of this decision, the OEB also approved the distribution-related OEB Cost Assessment Differential Account to record the difference between the amounts approved in rates and actual expenditures with respect to the OEB's cost assessments.

Retail Settlement Variance Accounts (RSVA)

Hydro One Networks has deferred certain retail settlement variance amounts under the provisions of Article 490 of the OEB's Accounting Procedures Handbook. In December 2012, the OEB approved the disposition of the total RSVA balance accumulated from January 2010 to December 2011, including accrued interest, to be disposed over a 24-month period from January 1, 2013 to December 31, 2014. At December 31, 2014, the RSVA was in a net asset position due to a change in global adjustment.

Rider 11

In April 2010, the OEB requested the establishment of deferral accounts which capture the difference between the revenue recorded on the basis of Green Energy Plan expenditures incurred and the actual recoveries received. Rider 11 includes amounts previously included as Rider 8.

PST Savings Deferral Account

The provincial sales tax (PST) and goods and services tax (GST) were harmonized in July 2010. Unlike the GST, the PST was included in operation, maintenance and administration expenses or capital expenditures for past revenue requirements

approved during a full cost-of-service hearing. Under the harmonized sales tax (HST) regime, the HST included in operation, maintenance and administration expenses or capital expenditures is not a cost ultimately borne by the Company and as such, a refund of the prior PST element in the approved revenue requirement is applicable, and calculations for tracking and refund were requested by the OEB. For the Distribution Business, PST was included in rates between July 1, 2010 and December 31, 2014 and recorded in a deferral account per direction from the OEB.

Rider 9

In December 2012, as part of Hydro One Networks' 2013 IRM distribution rate application, the OEB approved for disposition certain distribution-related deferral account balances, including RSVA amounts and balances of Rider 2 and Rider 3, accumulated up to December 2011, including accrued interest, to be disposed over a 24-month period from January 1, 2013 to December 31, 2014.

11. DEBT

Hydro One issues notes for long-term financing under its Medium-Term Note (MTN) Program. The terms of certain issuances are mirrored down to Hydro One Networks through the issuance of inter-company debt, which is then allocated between the Company's transmission and distribution businesses.

The following table presents the outstanding long-term debt of the Distribution Business as at December 31, 2014 and 2013:

December 31 (millions of Canadian dollars)	**2014**	**2013**
Long-term debt	3,381	3,313
Add: Unrealized marked-to-market loss[1]	1	3
Less: Long-term debt payable within one year	(221)	(176)
Long-term debt	3,161	3,140

[1] The unrealized marked-to-market loss relates to $100 million of Distribution Business' $200 million note due 2015 (2013 – $100 million of Distribution Business' $175 million note due 2014 and $100 million of Distribution Business' $200 million note due 2015). The unrealized marked-to-market loss is offset by a $1 million (2013 – $5 million) unrealized marked-to-market gain on the related fixed-to-floating interest-rate swap agreements, which are accounted for as fair value hedges. See Note 12 – Fair Value of Financial Instruments and Risk Management for details of fair value hedges.

The long-term debt is unsecured and denominated in Canadian dollars. The long-term debt is summarized by the number of years to maturity in Note 12 – Fair Value of Financial Instruments and Risk Management.

12. FAIR VALUE OF FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

Fair value is considered to be the exchange price in an orderly transaction between market participants to sell an asset or transfer a liability at the measurement date. The fair value definition focuses on an exit price, which is the price that would be received in the sale of an asset or the amount that would be paid to transfer a liability.

The Company classifies its fair value measurements based on the following hierarchy, as prescribed by the accounting guidance for fair value, which prioritizes the inputs to valuation techniques used to measure fair value into three levels:

Level 1 inputs are unadjusted quoted prices in active markets for identical assets or liabilities that Hydro One has the ability to access. An active market for the asset or liability is one in which transactions for the asset or liability occurs with sufficient frequency and volume to provide ongoing pricing information.

Level 2 inputs are those other than quoted market prices that are observable, either directly or indirectly, for an asset or liability. Level 2 inputs include, but are not limited to, quoted prices for similar assets or liabilities in an active market, quoted prices for identical or similar assets or liabilities in markets that are not active and inputs other than quoted market prices that are observable for the asset or liability, such as interest rate curves and yield curves observable at commonly

quoted intervals, volatilities, credit risk and default rates. A Level 2 measurement cannot have more than an insignificant portion of the valuation based on unobservable inputs.

Level 3 inputs are any fair value measurements that include unobservable inputs for the asset or liability for more than an insignificant portion of the valuation. A Level 3 measurement may be based primarily on Level 2 inputs.

Non−Derivative Financial Assets and Liabilities

At December 31, 2014 and 2013, the carrying amounts of accounts receivable, inter-company demand facility, and accounts payable are representative of fair value because of the short-term nature of these instruments.

Fair Value Measurements of Long-Term Debt

The fair values and carrying values of the Distribution Business' long-term debt at December 31, 2014 and 2013 are as follows:

December 31 (millions of Canadian dollars)	2014 Carrying Value	2014 Fair Value	2013 Carrying Value	2013 Fair Value
Long-term debt				
$100 million of $175 million notes due 2014[1]	–	–	101	101
$100 million of $200 million notes due 2015[1]	101	101	102	102
Other notes and debentures[2]	3,281	3,820	3,113	3,370
	3,382	3,921	3,316	3,573

[1] The fair value of $100 million of Distribution Business' $175 million notes due 2014 and $100 million of Distribution Business' $200 million notes due 2015 subject to hedging is primarily based on changes in the present value of future cash flows due to a change in the yield in the swap market for the related swap (hedged risk).

[2] The fair value of other notes and debentures, and the portions of Distribution Business' $175 million and $200 million notes that are not subject to hedging, represents the market value of the notes and debentures and is based on unadjusted period-end market prices for the same or similar debt of the same remaining maturities.

Fair Value Measurements of Derivative Instruments

Hydro One enters into interest-rate swaps agreements with respect to its long-term debt. The terms of these interest-rate swap agreements are mirrored down to Hydro One Networks, and are then allocated between the Company's transmission and distribution businesses.

At December 31, 2014, the Distribution Business' share of the Company's derivative instruments include $100 million (2013 – $200 million) of interest-rate swaps that were used to convert fixed-rate debt to floating-rate debt. These interest-rate swaps are classified as fair value hedges. The Distribution Business' fair value hedge exposure was equal to about 3% (2013 – 6%) of its long-term debt. At December 31, 2014, the Distribution Business' interest-rate swaps designated as fair value hedges were as follows:

- two $50 million fixed-to-floating interest-rate swap agreements to convert $100 million of the $200 million notes maturing September 11, 2015 into three-month variable rate debt.

At December 31, 2014, the Distribution Business' share of interest-rate swaps classified as undesignated contracts consisted of the following:

- a $20 million floating-to-fixed interest-rate swap agreement that locks in the floating rate the Company pays on the $20 million floating-rate MTN Series 22 notes from January 24, 2014 to January 24, 2015.

Fair Value Hierarchy

Fair value hierarchy information for financial assets and liabilities at December 31, 2014 and 2013 was as follows:

December 31, 2014 (millions of Canadian dollars)	Carrying Value	Fair Value	Level 1	Level 2	Level 3
Assets:					
Derivative instruments					
Fair value hedges – interest-rate swaps	1	1	–	1	–
	1	1	–	1	–
Liabilities:					
Inter-company demand facility	225	225	225	–	–
Long-term debt	3,382	3,921	–	3,921	–
	3,607	4,146	225	3,921	–

December 31, 2013 (millions of dollars)	Carrying Value	Fair Value	Level 1	Level 2	Level 3
Assets:					
Inter-company demand facility	47	47	47	–	–
Derivative instruments					
Fair value hedges – interest-rate swaps	3	3	–	3	–
	50	50	47	3	–
Liabilities:					
Long-term debt	3,316	3,573	–	3,573	–
	3,316	3,573	–	3,573	–

The fair value of the derivative instruments is determined using inputs other than quoted prices that are observable for these assets. The fair value is primarily based on the present value of future cash flows using a swap yield curve to determine the assumptions for interest rates.

The fair value of the hedged portion of the long-term debt is primarily based on the present value of future cash flows using a swap yield curve to determine the assumption for interest rates. The fair value of the un-hedged portion of the long-term debt is based on unadjusted period-end market prices for the same or similar debt of the same remaining maturities.

There were no significant transfers between any of the levels during the years ended December 31, 2014 and 2013.

Risk Management

Exposure to market risk, credit risk and liquidity risk arises in the normal course of the Company's business.

Market Risk

Market risk refers primarily to the risk of loss that results from changes in commodity prices, foreign exchange rates and interest rates. The Company does not have commodity risk. The Company does have foreign exchange risk as it enters into agreements to purchase materials and equipment associated with capital programs and projects that are settled in foreign currencies. This foreign exchange risk is not material, although Hydro One could in the future decide to issue foreign currency-denominated debt which would be hedged back to Canadian dollars consistent with its risk management policy. This could be mirrored in the Company. The Company is exposed to fluctuations in interest rates as the regulated rate of return for its Distribution Business is derived using a formulaic approach that is based on the forecast for long-term Government of Canada bond yields and the spread in 30-year "A"-rated Canadian utility bonds over the 30-year benchmark Government of Canada bond yield. The Company estimates that a 1% decrease in the forecasted long-term Government of

Canada bond yield or the "A"-rated Canadian utility spread used in determining the Distribution Business' rate of return would reduce the Distribution Business' 2014 results of operations by approximately $10 million (2013 – $10 million).

Hydro One uses a combination of fixed and variable-rate debt to manage the mix of its debt portfolio. Hydro One also uses derivative financial instruments to manage interest-rate risk. Hydro One utilizes interest-rate swaps, which are typically designated as fair value hedges, as a means to manage its interest rate exposure to achieve a lower cost of debt. In addition, Hydro One may utilize interest-rate derivative instruments to lock in interest rate levels in anticipation of future financing. Hydro One may also enter into derivative agreements such as forward-starting pay fixed-interest-rate swap agreements to hedge against the effect of future interest rate movements on long-term fixed-rate borrowing requirements. Such arrangements are typically designated as cash flow hedges. The Company's derivative instrument policy is consistent with Hydro One. No cash flow hedge agreements were outstanding as at December 31, 2014 or 2013.

A hypothetical 10% increase in the interest rates associated with variable-rate debt would not have resulted in a significant decrease in the Distribution Business' results of operations for the years ended December 31, 2014 or 2013.

Fair Value Hedges

For derivative instruments that are designated and qualify as fair value hedges, the gain or loss on the derivative instruments as well as the offsetting loss or gain on the hedged item attributable to the hedged risk are recognized in the Statements of Operations and Comprehensive Income. The Distribution Business' net unrealized loss (gain) on the hedged debt and the related interest-rate swaps for the years ended December 31, 2014 and 2013 are included in financing charges as follows:

Year ended December 31 (millions of Canadian dollars)	**2014**	**2013**
Unrealized loss (gain) on hedged debt	(1)	(2)
Unrealized loss (gain) on fair value interest-rate swaps	1	2
Net unrealized loss (gain)	–	–

At December 31, 2014, the amount of the Distribution Business' fair value hedges outstanding related to interest-rate swaps was $100 million (2013 – $200 million), with assets at fair value of $1 million (2013 – $3 million). During the years ended December 31, 2014 and 2013, there was no significant impact on the Distribution Business' results of operations as a result of any ineffectiveness attributable to fair value hedges.

Credit Risk

Financial assets create a risk that a counterparty will fail to discharge an obligation, causing a financial loss. At December 31, 2014 and 2013, there were no significant concentrations of credit risk with respect to any class of financial assets. The Distribution Business did not earn a significant amount of revenue from any individual customer. At December 31, 2014 and 2013, there was no significant accounts receivable balance due from any single customer.

At December 31, 2014, the Distribution Business' allowance for doubtful accounts was $64 million (2013 – $32 million). Adjustments and write-offs are determined on the basis of a review of overdue accounts, taking into consideration historical experience. At December 31, 2014, approximately 6% of the Distribution Business' net accounts receivable were aged more than 60 days (2013 – 4%).

Hydro One manages its counterparty credit risk through various techniques including: entering into transactions with highly-rated counterparties; limiting total exposure levels with individual counterparties consistent with the Hydro One's Board-approved Credit Risk Policy; entering into master agreements which enable net settlement and the contractual right of offset; and monitoring the financial condition of counterparties. In addition to payment netting language in master agreements, Hydro One establishes credit limits, margining thresholds and collateral requirements for each counterparty. Counterparty credit limits are based on an internal credit review that considers a variety of factors, including the results of a scoring model, leverage, liquidity, profitability, credit ratings and risk management capabilities. The determination of credit exposure for a particular counterparty is the sum of current exposure plus the potential future exposure with that counterparty. The current exposure is calculated as the sum of the principal value of money market exposures and the market value of all contracts that have a positive mark-to-market position on the measurement date. Hydro One would only offset the positive market values

against negative values with the same counterparty where permitted by the existence of a legal netting agreement such as an International Swap Dealers Association master agreement. The potential future exposure represents a safety margin to protect against future fluctuations of interest rates, currencies, equities, and commodities. It is calculated based on factors developed by the Bank of International Settlements, following extensive historical analysis of random fluctuations of interest rates and currencies. To the extent that a counterparty's margining thresholds are exceeded, the counterparty is required to post collateral with Hydro One as specified in each agreement. Hydro One monitors current and forward credit exposure to counterparties both on an individual and an aggregate basis. The Company's counterparty credit risk policy is consistent with Hydro One. The Distribution Business' credit risk for accounts receivable is limited to the carrying amounts on its Balance Sheets.

Liquidity Risk

Liquidity risk refers to the Company's ability to meet its financial obligations as they come due. The Company meets its short-term liquidity requirements through the inter-company demand facility with Hydro One and funds from operations. The short-term liquidity available to the Company should be sufficient to fund normal operating requirements.

At December 31, 2014, accounts payable and accrued liabilities in the amount of $670 million (2013 – $651 million) were expected to be settled in cash at their carrying amounts within the next year.

At December 31, 2014, the principal amount of the Distribution Business' long-term debt was $3,381million (2013 – $3,313 million). Principal outstanding, interest payments and related weighted average interest rates are summarized by the number of years to maturity in the following table:

Years to Maturity	**Principal Outstanding on Long-term Debt** *(millions of Canadian dollars)*	**Interest Payments** *(millions of Canadian dollars)*	**Weighted Average Interest Rate** *(%)*
1 year	220	156	2.9
2 years	200	146	4.4
3 years	195	141	5.2
4 years	338	131	2.8
5 years	91	121	1.7
	1,044	695	3.5
6 – 10 years	381	555	3.6
Over 10 years	1,956	1,630	5.4
	3,381	2,880	4.6

13. CAPITAL MANAGEMENT

The Distribution Business' objective is to manage its capital structure consistent with the deemed capital structure for rate-setting purposes as prescribed by the OEB.

The Distribution Business considers its capital structure to consist of excess of assets over liabilities, long-term debt, and the inter-company demand facility. The following table summarizes this capital structure:

December 31 (millions of Canadian dollars)	**2014**	**2013**
Long-term debt payable within one year	221	176
Inter-company demand facility	225	(47)
	446	129
Long-term debt	3,161	3,140
Excess of assets over liabilities	2,595	2,465
Total capital	6,202	5,734

The following table shows the movements in the excess of assets over liabilities for the years ended December 31, 2014 and 2013:

December 31 (millions of Canadian dollars)	**2014**	**2013**
Excess of assets over liabilities, January 1	2,465	2,319
Net income	189	258
Payments to Hydro One to finance dividends	(59)	(112)
Excess of assets over liabilities, December 31	2,595	2,465

14. PENSION AND POST-RETIREMENT AND POST-EMPLOYMENT BENEFITS

Hydro One has a defined benefit pension plan, a supplementary pension plan, and post-retirement and post-employment benefit plans. The defined benefit pension plan (Pension Plan) is contributory and covers all regular employees of Hydro One and its subsidiaries, except Hydro One Brampton Networks Inc. The supplementary pension plan provides members of the Pension Plan with benefits that would have been earned and payable under the Pension Plan but for the limitations imposed by the *Income Tax Act* (Canada). The supplementary pension plan obligation is included in post-retirement and post-employment benefit liability on the Balance Sheets.

Pension Benefits

The Pension Plan provides benefits based on highest three-year average pensionable earnings. For new management employees who commenced employment on or after January 1, 2004, and for new Society of Energy Professionals-represented staff hired after November 17, 2005, benefits are based on highest five-year average pensionable earnings. After retirement, pensions are indexed to inflation.

Hydro One and employee contributions to the Pension Plan are based on actuarial valuations performed at least every three years. Hydro One's annual Pension Plan contributions for 2014 of $174 million (2013 – $160 million) were based on an actuarial valuation effective December 31, 2013 (2013 – effective December 31, 2011) and the level of 2014 pensionable earnings. Estimated annual Pension Plan contributions for 2015 and 2016 are approximately $174 million and $175 million, respectively, based on an actuarial valuation as at December 31, 2013 and projected levels of pensionable earnings. Future minimum contributions beyond 2016 will be based on an actuarial valuation effective no later than December 31, 2016. Contributions are payable one month in arrears. All of the contributions are expected to be in the form of cash.

At December 31, 2014, based on the December 31, 2013 actuarial valuation, the present value of Hydro One's projected pension benefit obligation was estimated to be $7,535 million (2013 – $6,576 million). The fair value of pension plan assets available for these benefits was $6,299 million (2013 – $5,731 million).

Post-Retirement and Post-Employment Benefits

During the year ended December 31, 2014, the Distribution Business charged $33 million (2013 – $36 million) of post-retirement and post-employment benefit costs to operations, and capitalized $34 million (2013 – $35 million) as part of the cost of property, plant and equipment and intangible assets. Benefits paid in 2014 were $26 million (2013 – $24 million). In addition, the associated post-retirement and post-employment benefits regulatory asset decreased by $18 million (2013 – $8 million).

The Distribution Business presents its post-retirement and post-employment benefit liabilities on its Balance Sheets within the following line items:

December 31 (millions of Canadian dollars)	**2014**	**2013**
Accrued liabilities	25	22
Post-retirement and post-employment benefit liability	844	824
	869	846

15. ENVIRONMENTAL LIABILITIES

The following tables show the movements in environmental liabilities for the years ended December 31, 2014 and 2013:

Year ended December 31, 2014 (millions of Canadian dollars)	**PCB**	**LAR**	**Total**
Environmental liabilities, January 1	117	35	152
Interest accretion	5	1	6
Expenditures	(2)	(8)	(10)
Revaluation adjustment	(25)	12	(13)
Environmental liabilities, December 31	95	40	135
Less: current portion	6	5	11
	89	35	124

Year ended December 31, 2013 (millions of Canadian dollars)	**PCB**	**LAR**	**Total**
Environmental liabilities, January 1	116	24	140
Interest accretion	6	–	6
Expenditures	(2)	(7)	(9)
Revaluation adjustment	(3)	18	15
Environmental liabilities, December 31	117	35	152
Less: current portion	7	6	13
	110	29	139

The following tables show the reconciliation between the undiscounted basis of the environmental liabilities and the amount recognized on the Balance Sheets after factoring in the discount rate:

December 31, 2014 (millions of Canadian dollars)	**PCB**	**LAR**	**Total**
Undiscounted environmental liabilities	108	42	150
Less: discounting accumulated liabilities to present value	13	2	15
Discounted environmental liabilities	95	40	135

December 31, 2013 (millions of Canadian dollars)	**PCB**	**LAR**	**Total**
Undiscounted environmental liabilities	136	37	173
Less: discounting accumulated liabilities to present value	19	2	21
Discounted environmental liabilities	117	35	152

At December 31, 2014, the estimated future environmental expenditures were as follows:

(millions of Canadian dollars)	
2015	11
2016	19
2017	19
2018	19
2019	18
Thereafter	64
	150

At December 31, 2014, of the total estimated future environmental expenditures, $108 million relates to PCBs (2013 – $136 million) and $42 million relates to LAR (2013 – $37 million).

The Distribution Business records a liability for the estimated future expenditures for the contaminated LAR and for the phase-out and destruction of PCB-contaminated mineral oil removed from electrical equipment when it is determined that future environmental remediation expenditures are probable under existing statute or regulation and the amount of the future expenditures can be reasonably estimated.

There are uncertainties in estimating future environmental costs due to potential external events such as changes in legislation or regulations, and advances in remediation technologies. In determining the amounts to be recorded as environmental liabilities, the Company estimates the current cost of completing required work and makes assumptions as to when the future expenditures will actually be incurred, in order to generate future cash flow information. A long-term inflation rate assumption of approximately 2% has been used to express these current cost estimates as estimated future expenditures. Future expenditures have been discounted using factors ranging from approximately 2.3% to 6.3%, depending on the appropriate rate for the period when expenditures are expected to be incurred. All factors used in estimating the Distribution Business' environmental liabilities represent management's best estimates of the present value of costs required to meet existing legislation or regulations. However, it is reasonably possible that numbers or volumes of contaminated assets, cost estimates to perform work, inflation assumptions and the assumed pattern of annual cash flows may differ significantly from the Company's current assumptions. In addition, with respect to the PCB environmental liability, the availability of critical resources such as skilled labour and replacement assets and the ability to take maintenance outages in critical facilities may influence the timing of expenditures.

PCBs

The Environment Canada regulations, enacted under the *Canadian Environmental Protection Act,* 1999, govern the management, storage and disposal of PCBs based on certain criteria, including type of equipment, in-use status, and PCB-contamination thresholds. Under current regulations, the Company's PCBs have to be disposed of by the end of 2025, with the exception of specifically exempted equipment. Contaminated equipment will generally be replaced, or will be

decontaminated by removing PCB-contaminated insulating oil and retro filling with replacement oil that contains PCBs in concentrations of less than 2 ppm.

The Distribution Business' best estimate of the total estimated future expenditures to comply with current PCB regulations is $108 million. These expenditures are expected to be incurred over the period from 2015 to 2025. As a result of its annual review of environmental liabilities, the Distribution Business recorded a revaluation adjustment in 2014 to reduce the PCB environmental liability by $25 million (2013 – $3 million).

LAR

The Distribution Business' best estimate of the total estimated future expenditures to complete its LAR program is $42 million. These expenditures are expected to be incurred over the period from 2015 to 2023. As a result of its annual review of environmental liabilities, the Distribution Business recorded a revaluation adjustment in 2014 to increase the LAR environmental liability by $12 million (2013 – $18 million).

16. ASSET RETIREMENT OBLIGATIONS

The Company records a liability for the estimated future expenditures for the removal and disposal of asbestos-containing materials installed in some of its facilities and for the decommissioning of specific switching stations located on unowned sites. AROs, which represent legal obligations associated with the retirement of certain tangible long-lived assets, are computed as the present value of the projected expenditures for the future retirement of specific assets and are recognized in the period in which the liability is incurred, if a reasonable estimate of fair value can be made. If the asset remains in service at the recognition date, the present value of the liability is added to the carrying amount of the associated asset in the period the liability is incurred and this additional carrying amount is depreciated over the remaining life of the asset. If an ARO is recorded in respect of an out-of-service asset, the asset retirement cost is charged to results of operations. Subsequent to the initial recognition, the liability is adjusted for any revisions to the estimated future cash flows associated with the ARO, which can occur due to a number of factors including, but not limited to, cost escalation, changes in technology applicable to the assets to be retired, changes in legislation or regulations, as well as for accretion of the liability due to the passage of time until the obligation is settled. Depreciation expense is adjusted prospectively for any increases or decreases to the carrying amount of the associated asset.

In determining the amounts to be recorded as AROs, the Company estimates the current fair value for completing required work and makes assumptions as to when the future expenditures will actually be incurred, in order to generate future cash flow information. A long-term inflation assumption of approximately 2% has been used to express these current cost estimates as estimated future expenditures. Future expenditures have been discounted using factors ranging from approximately 3.0% to 5.0%, depending on the appropriate rate for the period when expenditures are expected to be incurred. All factors used in estimating the Distribution Business' AROs represent management's best estimates of the cost required to meet existing legislation or regulations. However, it is reasonably possible that numbers or volumes of contaminated assets, cost estimates to perform work, inflation assumptions and the assumed pattern of annual cash flows may differ significantly from the Company's current assumptions. AROs are reviewed annually or more frequently if significant changes in regulations or other relevant factors occur. Estimate changes are accounted for prospectively.

At December 31, 2014, the Company had recorded AROs of $4 million (2013 – $4 million), related to its Distribution Business, consisting of the estimated future expenditures associated with the removal and disposal of asbestos-containing materials installed in some of its facilities. The amount of interest recorded is nominal.

17. HYDRO ONE NETWORKS' SHARE CAPITAL

Hydro One Networks has 14,875,720 issued and outstanding cumulative preferred shares and 148,821,741 issued and outstanding common shares. The Company is authorized to issue an unlimited number of preferred shares and common shares.

Hydro One Networks makes common share and preferred share dividend payments to Hydro One. The Distribution Business makes payments to finance its share of the Company's common share and preferred share dividends. During 2014, the Distribution Business' payments to finance these dividends totaled $59 million (2013 – $112 million).

18. RELATED PARTY TRANSACTIONS

The Distribution Business is a separately regulated business of Hydro One Networks which is a subsidiary of Hydro One, and Hydro One is owned by the Province. The OEFC, IESO, Ontario Power Authority (OPA), Ontario Power Generation Inc. (OPG) and the OEB are related parties to the Distribution Business because they are controlled or significantly influenced by the Province. Transactions between these parties and the Distribution Business are described below.

IESO

In 2014, the Distribution Business purchased power in the amount of $2,172 million (2013 – $2,077 million) from the IESO-administered electricity market.

The Distribution Business receives amounts for rural rate protection from the IESO. 2014 revenues include $125 million (2013 – $125 million) related to this program.

OPA

The OPA funds substantially all of the Company's conservation and demand management programs. The funding includes program costs, incentives, and management fees. In 2014, the Distribution Business received $28 million (2013 – $26 million) from the OPA related to these programs.

OPG

In 2014, the Distribution Business purchased power in the amount of $23 million (2013 – $15 million) from OPG.

The Company has service level agreements with OPG. These services include field and engineering, logistics, corporate, telecommunications and information technology services. Operation, maintenance and administration costs of the Distribution Business related to the purchase of services with respect to these service level agreements were less than $1 million in both 2014 and 2013.

OEFC

In 2014, the Distribution Business purchased power in the amount of $10 million (2013 – $8 million) from power contracts administered by the OEFC.

Hydro One pays a $5 million annual fee to the OEFC for indemnification against adverse claims in excess of $10 million paid by the OEFC with respect to certain of Ontario Hydro's businesses transferred to Hydro One on April 1, 1999. The Distribution Business' allocation of this fee is $1 million.

PILs and payments in lieu of property taxes were paid or payable to the OEFC.

OEB

Under the *Ontario Energy Board Act, 1998*, the OEB is required to recover all of its annual operating costs from gas and electricity distributors and transmitters. In 2014, the Distribution Business incurred $6 million (2013 – $6 million) in OEB fees.

The amounts due to and from related parties as a result of the transactions referred to above are as follows:

December 31 (millions of Canadian dollars)	**2014**	**2013**
Accounts receivable	98	56
Accrued liabilities[1]	(180)	(189)

[1] Included in accrued liabilities at December 31, 2014 are amounts owing to the IESO in respect of power purchases of $176 million (2013 – $185 million).

Hydro One and Subsidiaries

The Distribution Business provides services to, and receives services from, Hydro One and its subsidiaries. Amounts due to and from Hydro One and its subsidiaries are settled through the inter-company demand facility.

The Company has entered into various agreements with Hydro One and its other subsidiaries related to the provision of shared corporate functions and services, such as legal, financial and human resources services, and operational services, such as environmental, forestry, and line services. 2014 revenues of the Distribution Business include $2 million (2013 – $3 million) related to the provision of services to Hydro One and its subsidiaries. During year ended December 31, 2014, the Distribution Business provided services to Hydro One and its other subsidiaries totalling $12 million (2013 – $12 million), of which $11 million (2013 – $12 million) was charged to operation, maintenance and administration costs, and $1 million (2013 – $nil) was capitalized.

The Distribution Business' long-term debt is due to Hydro One. In addition, balances payable or receivable under the inter-company demand facility are due to or due from Hydro One. Financing charges include interest expense on the long-term debt in the amount of $158 million (2013 – $150 million), and interest expense on the inter-company demand facility in the amount of $1 million (2013 – $1 million). At December 31, 2014, the Distribution Business had accrued interest payable to Hydro One totalling $38 million (2013 – $38 million).

During 2014, Hydro One Networks paid preferred share dividends in the amount of $20 million (2013 – $20 million) and common share dividends in the amount of $724 million (2013 – $200 million) to Hydro One. The amount allocated to the Distribution Business to finance these dividends was $59 million (2013 – $112 million).

19. STATEMENTS OF CASH FLOWS

The changes in non-cash balances related to operations consist of the following:

Year ended December 31 (millions of Canadian dollars)	**2014**	**2013**
Accounts receivable	(132)	(75)
Materials and supplies	(1)	1
Other assets	(5)	1
Accounts payable	4	9
Accrued liabilities	16	(4)
Accrued interest	–	3
Long-term accounts payable and other liabilities	–	(12)
Post-retirement and post-employment benefit liability	38	47
	(80)	(30)

Capital Expenditures

The following table illustrates the reconciliation between investments in property, plant and equipment and the amount presented in the Statements of Cash Flows after factoring in capitalized depreciation and the net change in related accruals:

Year ended December 31 (millions of Canadian dollars)	**2014**	**2013**
Capital investments in property, plant and equipment	(633)	(572)
Capitalized depreciation and net change in accruals included in capital investments in property, plant and equipment	19	9
Capital expenditures – property, plant and equipment	(614)	(563)

The following table illustrates the reconciliation between investments in intangible assets and the amount presented in the Statements of Cash Flows after factoring in the net change in related accruals:

Year ended December 31 (millions of Canadian dollars)	**2014**	**2013**
Capital investments in intangible assets	(14)	(65)
Net change in accruals included in capital investments in intangible assets	–	(1)
Capital expenditures – intangible assets	(14)	(66)

Supplementary Information

Year ended December 31 (millions of Canadian dollars)	**2014**	**2013**
Net interest paid	155	144
PILs	15	41

20. CONTINGENCIES

The Company is a wholly-owned subsidiary of Hydro One. As such, the assets of the Distribution Business are available for the satisfaction of the debts, contingent liabilities and commitments of both the Company and Hydro One.

21. COMMITMENTS

The Company and Hydro One have numerous commitments. These commitments have not been specifically allocated to the Distribution Business. However, the net assets of the Distribution Business are available to satisfy the commitments of both the Company and Hydro One.

22. SUBSEQUENT EVENT

On February 11, 2015, Hydro One Networks declared preferred share dividends in the amount of $5 million and common share dividends in the amount of $25 million. The amount allocated to the Distribution Business to finance these dividends was $2 million.