RESULTS OF OPERATIONS

As used in this section, references to increases and decreases, whether in terms of amounts or percentages, are made by comparison of the three months ended March 31, 2009 to the three months ended March 31, 2008.

Revenues

Three months ended March 31 (Canadian dollars in millions)	**2009**	**2008**	**$ Change**	**% Change**
Transmission	302	304	(2)	(1)
Distribution	986	908	78	9
Other	15	10	5	50
	1,303	1,222	81	7
Average Ontario 60-minute peak demand *(MW)* [1]	22,186	22,275	(89)	-
Distribution - units distributed to customers *(TWh)* [1]	8.4	8.5	(.1)	(1)

[1]System-related statistics are preliminary

The demand for electricity generally follows normal weather-related variations, and therefore our energy-related revenues, all other things being equal, will tend to be higher in the first and third quarters than in the second and fourth quarters.

Transmission

Transmission revenues predominantly consist of our transmission tariff, which is based on the monthly peak demand for electricity across our high-voltage network. The tariff is designed to recover revenues necessary to support a transmission system with sufficient capacity to accommodate the maximum expected demand. Demand is primarily influenced by weather and economic conditions. Transmission revenues also include minor amounts of ancillary revenues which are primarily attributable to maintenance services provided to generators and secondary use of our land rights-of-way.

Our transmission revenues were lower by $2 million, or 1% in the first quarter of 2009 compared to the same period last year. The average peak demand was slightly lower than the same period last year, resulting in a marginal effect on our transmission revenues.

Distribution

Distribution revenues include our distribution tariff, which is based on OEB (Ontario Energy Board) approved rates, as well as amounts to recover the cost of purchased power used by our customers. Accordingly, distribution revenues are primarily influenced by our distribution rates, the amount of electricity we distribute, and the cost of purchased power. Distribution revenues also include a minor amount of ancillary distribution services revenues, such as fees related to the use of our poles by the telecommunications and cable television industries, and miscellaneous charges such as those for late payments.

Distribution revenues increased by $78 million, or 9%, in the first quarter of 2009 compared to the same period last year. This change includes the recovery of higher purchased power costs of $70 million as described below under "Purchased Power." In addition, the OEB approved increases in the distribution tariff rates for our subsidiary, Hydro One Networks Inc. (Hydro One Networks), on December 18, 2008. These tariff rate increases, which support the maintenance and investment requirements of our distribution system, enabling the safe and reliable delivery of electricity to our customers throughout Ontario, were implemented on February 1, 2009, and resulted in higher distribution revenues of $12 million during the first quarter of 2009. In addition, higher energy consumption, resulting primarily from the colder weather experienced in January this year, increased our distribution revenues by a further $2 million for the first quarter. These increases were partially offset by reduced revenues of $5 million associated with the recovery of a distribution-related regulatory account which ceased March 31, 2008, and lower other revenues of $1 million as compared to the same period last year.

Purchased Power

Purchased power costs incurred by our Distribution Business represent the cost of electricity delivered to customers within our distribution service territory and consist of the wholesale commodity cost of energy, the Independent Electricity System Operator's (IESO's) wholesale market service charges, and transmission charges levied by the IESO. The commodity cost of energy for certain low-volume and designated customers is based on the OEB's Regulated Price Plan (RPP), which consists of a two-tiered pricing structure with threshold amounts adjusted twice annually. Customers who are not eligible for the RPP pay the market price for electricity, adjusted for the difference between market prices and the prices paid to generators under the *Electricity Restructuring Act, 2004*. A summary of the RPP impacting the reporting period is provided below.

	Tier Threshold (kWh/month)		Tier Rates (cents/kWh)	
Effective Date	**Residential**	**Non-Residential**	**First Tier**	**Second Tier**
November 1, 2007	1,000	750	5.0	5.9
May 1, 2008	600	750	5.0	5.9
November 1, 2008	1,000	750	5.6	6.5

Purchased power costs increased in 2009 by $70 million, or 12%, to $666 million compared to last year. The increase in our purchased power costs was primarily due to higher costs associated with the OEB's RPP for residential and other eligible customers of $56 million, the impact of higher charges levied by the IESO of $9 million, including transmission charges due to the OEB's August 16, 2007 transmission rate decision and wholesale market service charges, and higher purchased power costs for customers who are not eligible for the RPP of $5 million.

Operation, Maintenance and Administration

Our operation, maintenance and administration costs are comprised primarily of labour, material, equipment and purchased services in support of the operation and maintenance of the transmission and distribution systems. These costs also include property taxes and payments in lieu thereof on our transmission and distribution lines, stations and buildings.

Operation, maintenance and administration costs for each of our three business segments were as follows:

Three months ended March 31 (Canadian dollars in millions)	**2009**	**2008**	**$ Change**	**% Change**
Transmission	103	97	6	6
Distribution	127	115	12	10
Other	13	9	4	44
	243	221	22	10

Transmission

Operation, maintenance and administration expenditures incurred to sustain our high-voltage transmission stations, lines and rights-of-way increased by $6 million, or 6%, in the first quarter compared to last year. This increase was primarily attributable to an increase of $10 million in our expenditures incurred in support of the transmission system. This was mainly attributable to a one-time settlement credit in 2008 associated with the transfer of assets to the Inergi LP (Inergi) pension plan following approval from the Financial Services Commission of Ontario (FSCO). The increase in support expenditures was partially offset by marginally lower expenditures within our work programs. Our work program expenditures were lower by $4 million compared to the same period in the prior year. These reductions were primarily attributable to lower expenditures on unplanned corrective station maintenance, particularly for power equipment, lower expenditures within our planned line maintenance programs and lower forestry expenditures.

Distribution

Operation, maintenance and administration expenditures necessary to maintain our low-voltage distribution system increased by $12 million, or 10%, compared to last year. Our work program expenditures remained consistent. The increase in our operation, maintenance and administration expenditures was due to higher support costs of $12 million reflecting a one-time settlement credit in 2008 associated with the transfer of pension assets to the Inergi pension plan.

Depreciation and Amortization

Depreciation and amortization expense for the first three months of the year decreased by $6 million, or 5%, to $124 million relative to the comparative period. This decrease was mainly attributable to the full recovery and therefore the completion of amortization associated with two regulatory accounts, one related to past service costs for employee future benefits other than pension and the second related to a distribution deferral account. These decreases were partially offset by higher depreciation from new assets placed in service.

Financing Charges

Financing charges increased by $3 million, or 4%, to $72 million in the quarter compared to the same period last year. This increase was primarily due to a $6 million interest credit in the first quarter of 2008 related to the Inergi pension asset transfer settlement and a net increase in interest expense reflecting a higher average level of debt partially offset by a lower average effective interest rate. These increases were partially offset by an increase in interest capitalization on capital reflecting higher construction in progress levels.

Provision for Payments in Lieu of Corporate Income Taxes

The provision for payments in lieu of corporate income taxes decreased by $28 million, or 57%, to $21 million in the first quarter compared to the same period last year. This decrease primarily reflects the impact of increased temporary differences relating to higher capital cost allowance deductions being available on our information system and smart meter investments in excess of depreciation and net temporary differences associated with certain regulatory accounts partially offset by an increase to the provision for payments in lieu relating to future taxes.

Net Income

Net income of $177 million was higher by $20 million, or 13%, compared to 2008 first quarter results. This year over year increase was primarily due to a reduction in our payments in lieu of corporate income taxes primarily resulting from higher capital cost allowance deductions being available on our information system and smart meter investments in excess of depreciation. In addition, we experienced higher distribution tariff revenue associated with a December 18, 2008 Ontario Energy Board decision. These increases were partially offset by the impact of a one-time settlement credit in 2008 associated with the transfer of pension assets to the Inergi pension plan following approval from the FSCO.

QUARTERLY RESULTS OF OPERATIONS

The following table sets forth unaudited quarterly information for each of the eight quarters from June 30, 2007 through March 31, 2009. This information has been derived from our unaudited interim Consolidated Financial Statements which, in the opinion of our management, have been prepared on a basis consistent with the audited annual Consolidated Financial Statements and which include all adjustments, consisting only of normal recurring adjustments, necessary for fair presentation of our financial position and results of operations for those periods. These operating results are not necessarily indicative of results for any future period and should not be relied upon to predict our future performance.

(Canadian dollars in millions)	**2009**		**2008**				**2007**	
Quarter ended	**Mar. 31**	**Dec. 31**[3]	**Sep. 30**	**Jun. 30**	**Mar. 31**	**Dec. 31**	**Sep. 30**[2]	**Jun. 30**
Total revenue[1]	1,303	1,194	1,126	1,055	1,222	1,129	1,128	1,120
Net income[1]	177	131	112	98	157	90	67	93
Net income to common shareholder[1]	173	126	108	93	153	85	63	88

[1] The demand for electricity generally follows normal weather-related variations, and therefore our electricity-related revenues and profit, all other things being equal, would tend to be higher in the first and third quarters than in the second and fourth quarters.

[2] As a result of the OEB's August 16, 2007 decision on Hydro One Networks' Transmission rate application that was effective January 1, 2007, revenues reflect a reduced revenue requirement based on the approved rate of return of 8.35%. Previously, the rate of return was 9.88%. Revenues in the third quarter of 2007 reflect a $38 million reduction to revenues in respect of the period January 1, 2007 to August 16, 2007 and reflect the OEB's decision to reduce the rate of return and revise the capital structure of our Transmission Business.

[3] As a result of the OEB's December 18, 2008 decision on Hydro One Network's distribution rate application that was effective May 1, 2008, revenues in the fourth quarter of 2008 reflect a $25 million increase in respect of the period May 1, 2008 to December 31, 2008, reflecting growth in the work program requirements and investment in capital infrastructure.

LIQUIDITY AND CAPITAL RESOURCES

Our primary sources of liquidity and capital resources are funds generated from operations, debt capital market borrowings and bank financing. These resources will be used to satisfy our capital resource requirements, which continue to include capital expenditures, servicing and repayment of our debt, payments related to our outsourcing arrangements, investing activities, and dividends.

Summary of Sources and Uses of Cash

Three months ended March 31 (Canadian dollars in millions)	**2009**	**2008**
Operating activities	185	229
Financing activities		
Long-term debt issued	600	550
Long-term debt retired	(400)	-
Short-term notes	150	-
Dividends paid	(108)	(41)
Investing activities		
Capital expenditures	(336)	(211)
Other financing and investing activities	13	11
Net change in cash and cash equivalents	104	538

Operating Activities

Net cash from operating activities decreased by $44 million, to $185 million, compared to 2008 results. The reduction is a result of higher working capital requirements in the quarter compared to the same period last year, primarily related to increases in both our levels of revenue and to our work programs, and to amounts recorded in certain regulatory accounts, primarily the regulatory liability refund account. These reductions were partially offset by the repayment to customers in 2008 of amounts recorded in the revenue difference deferral account following the 2007 transmission rate decision as well as by higher net income.

Financing Activities

Short-term liquidity is provided through funds from operations and our Commercial Paper Program, under which we are authorized to issue up to $1,000 million in short-term notes with a term to maturity of less than 365 days. At March 31, 2009, we had $150 million of short-term notes outstanding. Our Commercial Paper Program is supported by a $1,000 million committed revolving credit facility with a syndicate of banks maturing August 10, 2010. The short-term liquidity under this program and anticipated levels of funds from operations should be sufficient to fund our normal operating requirements. At March 31, 2009, we had $6,325 million in long-term debt outstanding, which was all long-term. Our notes and debentures mature between 2010 and 2046. Long-term financing is provided by our access to the debt markets, primarily through our Medium-Term Note Program. The maximum authorized principal amount of medium-term notes issuable under this program until July 2009 is $2,500 million, of which $550 million was remaining and available as at March 31, 2009.

	Rating	
Rating Agency	**Short-term Debt**	**Long-term Debt**
DBRS Limited	R-1 (middle)	A (high)
Moody's Investors Service Inc.	Prime-1	Aa3
S&P	A-1	A+

We have the customary covenants normally associated with long-term debt. Among other things, our long-term debt covenants limit our permissible debt as a percentage of our total capitalization, limit our ability to sell assets and impose a negative pledge provision, subject to customary exceptions. The credit agreement related to our $1,000 million credit facility has no material adverse change clauses that could trigger default. However, the credit agreement requires that we provide notice to the lenders of any material adverse change within three business days of the occurrence. The agreement also provides limitations that debt cannot exceed 75% of total capitalization and that debt issued by our subsidiaries cannot exceed 10% of the total book value of our assets. We are in compliance with all of these covenants and limitations.

During the first quarter of 2009, we issued $600 million in long-term debt under our Medium-Term Note Program. We also repaid $400 million in maturing long-term debt. In comparison, during the first quarter of 2008 we issued $550 million in long-term debt under our Medium-Term Note Program and had no debt maturities in the first quarter. In the first quarter of 2009, the amount of short term notes increased by $150 million year-over-year. For the first quarter of 2008, we had no change in our short-term notes outstanding.

In the first three months of 2009, we paid dividends to the Province in the amount of $108 million, consisting of $104 million in common dividends and $4 million in preferred dividends. In the comparative period, we paid common dividends of $37 million and preferred dividends of $4 million.

Common dividends are declared at the sole discretion of our Board of Directors, and are recommended by management based on results of operations, financial condition, cash requirements and other relevant factors such as industry practice, shareholder expectations and maintenance of the deemed regulatory capital structure. Common dividends pertaining to the quarterly financial results are generally declared and paid in the immediately following quarter.

Investing Activities

Cash used for investing activities primarily represents capital expenditures for each of our three business segments as follows:

Three months ended March 31 (Canadian dollars in millions)	**2009**	**2008**	**$ Change**	**% Change**
Transmission	187	107	80	75
Distribution	148	102	46	45
Other	1	2	(1)	(50)
	336	211	125	59

Transmission

Transmission capital expenditures increased by $80 million in the first quarter of 2009 to $187 million, compared to the same period in 2008.

Expenditures to expand and reinforce the transmission system were $87 million, representing an increase of $40 million over last year. The increase is primarily attributable to a number of significant inter-area network upgrade projects to increase generation. These were slightly offset by some local area supply projects as well as some load and generation projects that were completed or nearing completion last year.

Inter-area network upgrades with increased expenditures in the first quarter of 2009 include the Bruce to Milton Transmission Reinforcement Project to connect redeveloped nuclear and new wind generation sources in the Huron-Grey-Bruce area, the South Western Ontario Capacitor Banks Project, which will expand transmission capacity in the Bruce area to enable the delivery of additional generation from the Bruce “A” nuclear plant and committed wind generation, and the Cherrywood Transformer Station to Claireville Transformer Station connection project which will enable greater transfer capability across the Greater Toronto Area. These increases are minimally offset by the substantial completion in the first part of 2008 of our construction phase of an interconnection project with Québec that will increase access to emission-free hydroelectric power.

Local area supply projects with significant expenditures in the first quarter of 2009 include our Greater Toronto Area (GTA) West Transmission Reinforcement Project, which will increase capacity in the Western GTA to ensure supply reliability in the area and our Essa Transformer Station to Stayner Transformer Station connection, which will improve the adequacy and reliability of supply to the Southern Georgian Bay region in recognition of the growing needs of our customers. The final completion of our Niagara Reinforcement Project continues to be delayed by the aboriginal land dispute in the Caledonia area. Discussions related to the Niagara Reinforcement Project continue between the aboriginal peoples involved and various government entities and we expect to complete this project when site access becomes available.

Expenditures to sustain our existing transmission system were $64 million, representing an increase of $25 million compared to 2008. This increase was due to refurbishment and replacement of end-of-life equipment associated with various projects including our Claireville Transformer Station project to improve reliability and to meet growing demand, and to the timing of expenditures within our spare transformer purchase program.

Our other transmission capital expenditures were $36 million in the first quarter of 2009, representing an increase of $15 million from the same period in the prior year. This increase was attributable to higher information technology expenditures primarily related to an entity-wide information system replacement and improvement project to replace end-of-life systems and improve productivity, for which we are nearing the completion of the second phase. In addition, we incurred higher expenditures associated with information security enhancements at our Ontario Grid Control Centre.

Distribution

Distribution capital expenditures increased by $46 million to $148 million in the first quarter of 2009, compared to the prior year.

Capital expenditures to expand and reinforce our distribution network were $85 million, an increase of $44 million compared to last year. These increases primarily reflect ongoing investments in our Smart Meter Program. We have also initiated some programs to support the development of a smart grid that would transform the distribution network. During the quarter, we installed approximately 111,000 smart meters, bringing our cumulative program total to about 895,000 meters.

Expenditures to sustain our distribution system were $46 million, an increase of $1 million from 2008. This increase was primarily a result of increased engineering and construction work to upgrade or replace wholesale meters offset by lower storm-recovery expenditures and planned replacement of end-of-life wood poles on our lines. Our other distribution capital expenditures were $17 million in 2009, representing an increase of $1 million from last year. This increase reflects expenditures on our entity-wide information system replacement and improvement project.

Future Capital Expenditures

Our capital expenditures for 2009 are budgeted at $1.6 billion. The 2009 capital budgets for our transmission and distribution businesses are approximately $950 million and $650 million, respectively. Capital expenditures are expected to exceed $1.7 billion in 2010 and $1.5 billion in 2011, primarily reflecting investments to expand, refurbish or replace transmission infrastructure, consistent with government policy, Ontario Power Authority (OPA) planning information including the Integrated Power System Plan (IPSP), local area supply requirements and the preventive and corrective maintenance needs to manage aging assets. These investments will facilitate an adequate and reliable supply of electricity in the public interest. These investment levels also reflect the continued mass deployment of smart meters within our distribution businesses that began in 2007 and which will be completed by the end of 2010. The replacement of critical information technology systems is also underway. Capital expenditures of our other business segment are budgeted at about $7 million in 2009, reflecting sustainment of the fibre optic network.

The proposed *Green Energy and Green Economy Act, 2009* (Act) (see Recent Developments), if passed, would be expected to lead to additional investments in the electricity system to facilitate renewable generation, and higher investments through advanced technologies to increase functionality and reliability of the electricity grid. These additional investments will depend, to some extent, on which investments are determined by the government and the OEB to be appropriate system investments to be borne by the rate base, and which are assigned to connecting generators. Investments in advanced technologies will build on the investment already planned for, and underway, in smart meters and the associated communications and data processing capacity. The determination of the precise nature and volume of incremental investments to facilitate the connection of renewable generation, to enable a smart grid and to comply with other parts of the Act will be an ongoing part of our investment planning process.

Summary of Contractual Obligations and Other Commercial Commitments

The following table presents a summary of our debt and other major contractual obligations as well as other major commercial commitments.

March 31, 2009 (Canadian dollars in millions)	**Total**	**2009**[1]	**2010/2011**	**2012/2013**	**After 2013**
Contractual Obligations *(due by year)*					
Short-term notes payable	150	150	-	-	-
Long-term debt – principal repayments	6,325	-	1,100	1,200	4,025
Long-term debt – interest payments	5,732	315	668	564	4,185
Inergi outsourcing agreement[2]	274	74	184	16	-
Operating lease commitments	60	5	11	12	32
Total Contractual Obligations	12,541	544	1,963	1,792	8,242

March 31, 2009 (Canadian dollars in millions)	**Total**	**2009**[1]	**2010/2011**	**2012/2013**	**After 2013**
Other Commercial Commitments *(by year of expiry)*					
Bank line[3]	1,000	-	1,000	-	-
Letters of credit[4]	121	111	10	-	-
Guarantees[4]	325	325	-	-	-
Pension[5]	84	76	8	-	-
Total Other Commercial Commitments	1,530	512	1,018	-	-

[1] The amounts disclosed represent the balances due over the period April 1, 2009 to December 31, 2009.

[2] On March 1, 2002, Inergi began providing a range of services to us for a 10-year period, including information technology, customer care, supply chain and certain human resources and finance services. The agreement expires on February 29, 2012. Given the complexities involved, we have begun developing a plan of action for end-of-term.

[3] As a backstop to our commercial paper program, we have a $1,000 million revolving standby credit facility with a syndicate of banks which matures in August 2010.

[4] We currently have bank letters of credit of $107 million outstanding relating to retirement compensation arrangements. The other $14 million included in letters of credit pertains to operating letters of credit and to surety bonds. We have also provided prudential support to the IESO on behalf of our subsidiaries as required by the Market Rules using guarantees of up to a maximum of $325 million and on behalf of a distributor using a guarantee of up to a maximum of $335 thousand. Although no letters of credit are required for prudential support, we would have to resume providing bank letters of credit if our credit rating deteriorated to below the "Aa" category. In January 2009, we issued an additional letter of credit in the amount of $10 million relating to an agreement to purchase goods.

[5] Contributions to the pension fund are made one month in arrears. Contributions for 2009 are based on an actuarial valuation filed in September 2007 and effective December 31, 2006. Our annual pension contributions for 2009 will be about $105 million. Contributions beyond 2009 will be based on an actuarial valuation effective no later than December 31, 2009 and will depend on future investment returns, changes in benefits or actuarial assumptions. Pension contributions beyond 2009 are not estimable at this time.

The amounts in the above table under long-term debt – principal repayments, are not charged to our results of operations, but are reflected on our Balance Sheet and Statement of Cash Flows. Interest associated with this debt is recorded under financing charges on our Statement of Operations or in our capital programs. Payments in respect of operating leases and our outsourcing agreement with Inergi are recorded under operation, maintenance and administration costs on our Statement of Operations or within our capital expenditures.

RELATED PARTY TRANSACTIONS

Related party transactions primarily consist of our transmission revenues received from, and our power purchases payments made to the IESO, which is a related party by virtue of its status as an agency of our shareholder, the Province. The year-over-year changes related to these amounts are described more fully in our discussion of our transmission revenues and purchased power costs. Other significant related party transactions include our dividends which are paid to the Province and our payments in lieu of corporate income taxes which are paid or payable to the Ontario Electricity Financial Corporation.

CONSIDERATIONS OF CURRENT ECONOMIC CONDITIONS

Pension

During the first three months of 2009, the deferred pension asset reported on our balance sheet decreased by $3 million to $438 million. We have contributed $29 million into our pension plan in 2009 and incurred $32 million in net periodic pension benefit costs. Our annual funding contributions for 2009 will be approximately $105 million.

As a result of current economic uncertainty and financial market volatility, consistent with other pension plans, our pension plan experienced negative returns. Should the plan continue to incur negative returns in 2009, or if the discount rate falls sufficiently by the end of 2009, the deficit position at that time could lead to a large increase in our contribution requirements beyond 2009. The recovery of pension costs is subject to approval by the OEB. Failure to attain OEB approval could have an adverse effect on our results of operations.

The Pension Fund has broad exposure from its investments in domestic and international equity markets, as well as in fixed income markets. As a result, the Fund was negatively impacted in 2008 and into the first quarter of 2009, consistent with negative returns experienced in financial markets. The overall exposure of the Fund reflects its holdings across a number of sectors, and a well-diversified portfolio to support long-term objectives.

STATUS OF OUR TRANSITION TO INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS)

On February 13, 2008, the Canadian Accounting Standards Board confirmed that publicly accountable enterprises will be required to adopt IFRS in place of Canadian generally accepted accounting principles (GAAP) for interim and annual reporting purposes for fiscal years beginning on or after January 1, 2011. At this time, we are assessing the impact on our future financial position and results of operations.

We commenced our IFRS conversion project in 2007 and we have established a formal project governance structure. This structure includes a steering committee consisting of senior levels of management from finance, information technology, treasury and our operations organizations, among others. Regular reporting is provided to our senior executive management and to the Audit and Finance Committee of our Board of Directors. We have also engaged an external expert advisor.

Our project consists of four phases: diagnostic, design and planning, solution development, and implementation. We have completed the diagnostic phase, which involved a high level review of the major differences between current Canadian GAAP and IFRS. Currently, we have determined that the areas of accounting difference with the highest potential to significantly impact our company are rate regulated accounting, accounting for fixed assets, payments in lieu of corporate income taxes, employee future benefits, as well as initial adoption of IFRS under the provisions of IFRS 1, *First-Time Adoption of IFRS* .

We are currently simultaneously engaged in the design and planning, solution development and implementation phases of our project. We are working in issue-specific teams to focus on generating options and making recommendations in the identified areas and implementing financial reports and systems solutions in our high impact areas. We have established a regular staff communication plan, started to roll out staff training programs, and have begun to evaluate the impacts of the IFRS transition on other business activities including our subsidiaries.

In addition, we have been involved in documenting the high impact areas identified, including an analysis of financial system impacts, the establishment of key milestones and ongoing discussions with our external auditors. Our implementation phase for our high impact accounting and systems issues has commenced. The impact on disclosure controls and internal controls over financial reporting are also being examined. Analysis of other business impacts, such as impacts on debt covenants and performance measures, continues to proceed.

The OEB began a process in May 2008 to determine the nature of any changes that should be made in regulatory reporting requirements in response to IFRS. We have participated in each of the OEB consultation meetings with stakeholders, including distribution utility, industry and ratepayer representatives to indentify and manage IFRS conversion issues. In early May 2009, we attended and took an active role in a formal OEB stakeholder conference that is anticipated to lead to a final regulatory accounting and reporting framework for entities operating under OEB jurisdiction. We also continue to monitor and contribute as appropriate to International Accounting Standards Board initiatives with the potential to impact rate regulated accounting under IFRS.

At the Canadian Public Sector Accounting Board’s (PSAB’s) meeting on November 17 and 18, 2008, it agreed to a stakeholder request to re-evaluate an earlier conclusion that government organizations following commercial practices, such as our company, should continue to prepare their financial statements in accordance with GAAP for profit-oriented enterprises. For such enterprises that are also publicly accountable, this would become IFRS after January 1, 2011. As a result, the PSAB directed its staff to develop an Invitation to Comment (ITC) that was scheduled at a special meeting that took place in January 2009 that sought input from all of PSAB’s stakeholders on this issue. The ITC was issued on February 24, 2009, and we responded to the request by submitting our comments on April 17, 2009. The ITC supported the opinion that affected government business enterprises such as Hydro One follow IFRS. Until a decision is rendered, it remains uncertain how this initiative could affect the nature or timing of our conversion to IFRS.

In December, 2008, the International Accounting Standards Board (IASB) added a project on rate regulated activities to its agenda. The issue is whether entities with such activities could or should recognize assets and/or liabilities as a result of rate regulation imposed by regulatory bodies or governments. At the IASB’s meeting on April 23, 2009, a proposal was made to publish an exposure draft by July, 2009 with a 120-day comment period. The IASB also plans to issue a standard within a

June, 2010 timeframe and effective on January, 2011. The Company is in the process of evaluating the impact of this project on its ongoing conversion activities and adoption of IFRS.

DISCLOSURE CONTROLS AND INTERNAL CONTROLS OVER FINANCIAL REPORTING

We are continuing to transition our major financial systems to a SAP enterprise-wide platform as part of the entity-wide information system replacement and improvement project. A formal project governance structure is in place to ensure an effective transition of the information technology systems and business processes. The governance structure includes a steering committee consisting of senior levels of management which reports to senior executive management and the Business Transformation Committee of the Board of Directors.

The first phase of the transition including the supply chain, asset, and work management modules within SAP was implemented in 2008. A portion of the Financial Accounting and Control modules were also implemented to facilitate financial reporting. This implementation included both new controls over Internal Controls over Financial Reporting (ICFR) and replaced controls in the previous information technology system.

The second phase of the transition, which is planned for implementation in August, 2009, involves the replacement of remaining finance, human resources and pay modules.

In compliance with the requirements of National Instrument 52-109, *Certification of Disclosure in Issuers' Annual and Interim Filings*, our Certifying Officers have reviewed and certified the Consolidated Financial Statements for the quarter ended March 31, 2009, together with other financial information included in our quarterly securities filings. Our Certifying Officers have also certified that disclosure controls and procedures have been designed to provide reasonable assurance that material information relating to our company is made known within our company. We also certify that ICFR has been designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements.

RECENT DEVELOPMENTS

Green Energy and Green Economy Act

On February 23, 2009, the Government of Ontario introduced Bill 150, the proposed *Green Energy and Green Economy Act, 2009*. Among other provisions, the Act proposes that the renewable energy generators have a right to connect to the transmission and distribution system, subject to the applicable technical, economic and other requirements that may be prescribed in regulation. Under the proposed Act, transmitters' and distributors' licences would require the provision of priority connection access for renewable energy generation facilities that meet the requirements set by regulation. The proposed Act would also direct the OEB to require transmitters and distributors to file plans that would lead to expansion of their systems to facilitate renewable energy.

Ensuring reasonably broad-based implementation of a right for renewable resource producers to connect to Ontario's grid will likely require additional investment by us beyond the currently planned level. The extent of these additional investments will depend, to some extent, on which investments are determined by the government and the OEB to be appropriate system investments to be borne by the rate base, and which are assigned to connecting generators.

Status of Rate Applications

On March 6, 2009, the oral portion of the hearing regarding our rate application for 2009 and 2010 transmission rates concluded. An OEB decision is expected by June 2009.

On March 13, 2009, the OEB released its decision regarding the 2009 rate application made by our subsidiary, Hydro One Brampton Networks Inc. The OEB approved our submission on the basis of the OEB's cost of capital and second generation incentive regulation mechanism (IRM) policies. The revised rates, including an amount of $1.00 per month per metered customer for smart meters, were approved with an implementation date of May 1, 2009.

The oral hearing for Hydro One Networks distribution rate application, filed under the OEB's third generation IRM policies, concluded on March 27, 2009. A decision is anticipated by June, 2009 with the proposed increase scheduled to take effect on May 1, 2009.

On April 30, 2009, the OEB issued a decision regarding the 2009 cost of service distribution rate application for our subsidiary, Hydro One Remote Communities Inc., approving all work program expenditures and the proposed rate increase of 4.4% effective May 1, 2009.

Status of Applications to Construct Facilities

On April 8, 2009, we filed an application with the OEB to build a second transmission circuit as an addition to the existing single circuit transmission line in the Lower Mattagami area. The addition is required to improve the reliability and quality of electricity service in this region and increases the capacity of the existing circuit to add new generation to the system.

On May 1, 2009, we filed an application with the OEB to build a transmission line and transformer facilities in the County of Oxford. These facilities are required to increase transmission capacity to ensure the availability and quality of electricity supply to consumers in the Woodstock area.

Debt Issue

On March 3, 2009, we issued $300 million of 30-year notes at a coupon rate of 6.03% and with a maturity date of March 3, 2039. In the first quarter, we successfully issued $600 million of cost effective debt financing.

SELECTED FINANCIAL HIGHLIGHTS AND RATIOS

Three months ended March 31 (Canadian dollars in millions) (except as otherwise noted)	**2009**	**2008**
Net income	177	157
Net cash from operating activities	185	229
Capital expenditures	336	211
Earnings per common share *(Canadian dollars)*	1,724	1,524
Earnings coverage ratio[1]	2.53	2.68
Net asset coverage on long-term debt[2]	1.82	1.84
Total debt to capitalization[3]	55%	54%

[1]The earnings coverage ratio has been presented for the twelve months ended March 31, 2009 and March 31, 2008, respectively and has been calculated as the sum of net income, provision for payments in lieu of corporate income taxes and financing charges divided by the sum of financing charges, capitalized interest and cumulative preferred dividends.

[2]The net asset coverage on long-term debt ratio has been presented as at March 31, 2009 and December 31, 2008 and has been calculated as total assets minus total liabilities excluding long-term debt (including current portion) divided by long-term debt (including current portion).

[3]Total debt to capitalization ratio has been presented as at March 31, 2009 and December 31, 2008 and has been calculated as total debt divided by total debt plus total shareholder's equity.

FORWARD-LOOKING STATEMENTS AND INFORMATION

Our oral and written public communications, including this document, often contain forward-looking statements that are based on current expectations, estimates, forecasts and projections about our business and the industry in which we operate and include beliefs and assumptions made by the management of our company. Such statements include, but are not limited to: expectations regarding developments in the statutory and operating framework for electricity distribution and transmission in Ontario including the timing of decisions from the OEB and other governing bodies; statements regarding our future liquidity and capital resources; expectations regarding our financing activities; expectations regarding the results of our projects and completion dates; statements regarding future capital expenditures and our investment plans; expectations regarding the impact of the proposed *Green Energy and Green Economy Act, 2009* on our company; statements regarding contractual obligations and other commercial commitments; statements regarding future pension contributions; and statements about IFRS and our conversion to IFRS. Words such as “expect”, “anticipate”, “intend”, “attempt”, “may”, “plan”, “will”, “believe”, “seek”, “estimate”, “target”, and “continue”, and variations of such words and similar expressions, are intended to identify such forward-looking statements. These statements are not guarantees of future performance and involve assumptions and risks and uncertainties that are difficult to predict. Therefore, actual outcomes and results may differ materially from what is expressed, implied or forecasted in such forward-looking statements. We do not intend, and we disclaim any obligation to update any forward-looking statements, except as required by law. These forward-looking statements are based on a variety of factors and assumptions including, but not limited to the following: no unforeseen changes in the legislative and operating framework for Ontario's electricity market; no unfavourable decisions from the OEB and other regulatory bodies concerning outstanding rate and other applications; no unforeseen changes in rate orders or rate structures for our distribution and transmission businesses; a stable regulatory environment; and no significant event occurring outside the ordinary course of business. These assumptions are based on information currently available to us, including information obtained from third party industry analysts. Actual results may differ materially from those predicted by such forward-looking statements. While we do not know what impact any of these differences may have, our business, results of operations, financial condition and our credit stability may be materially adversely affected. Factors that could cause actual results or outcomes to differ materially from the results expressed or implied by forward-looking statements include, among other things:

- any opposition to and delays or denials of the requisite approvals and accommodations for our planned projects;
- the timing and result of regulatory decisions regarding our revenue requirements, cost recovery and rates;
- the risk that we are not able to arrange sufficient financing to repay maturing debt and to fund capital expenditures and other obligations;
- the impact of the proposed *Green Energy and Green Economy Act, 2009* on our company and the expenditures arising therefrom; and
- future interest rates, future investment returns, inflation, changes in benefits and changes in actuarial assumptions.

We caution the reader that the above list of factors is not exhaustive. Some of these and other factors are discussed in more detail under “Risk Management and Risk Factors” in the 2008 annual Management’s Discussion and Analysis (MD&A). You should review the section entitled “Risk Management and Risk Factors” in detail.

This MD&A is dated as at May 13, 2009. Additional information about our company, including our Annual Information Form, is available on SEDAR at www.sedar.com.

HYDRO ONE INC.

CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME (unaudited)

Three months ended March 31 (Canadian dollars in millions)	**2009**	**2008**
Revenues		
Transmission	302	304
Distribution	986	908
Other	15	10
	1,303	1,222
Costs		
Purchased power	666	596
Operation, maintenance and administration *(Note 5)*	243	221
Depreciation and amortization	124	130
	1,033	947
Income before financing charges and provision for payments in lieu of corporate income taxes	270	275
Financing charges *(Note 5)*	72	69
Income before provision for payments in lieu of corporate income taxes	198	206
Provision for payments in lieu of corporate income taxes	21	49
Net income	177	157
Other comprehensive loss	-	(1)
Comprehensive income	177	156
Basic and fully diluted earnings per common share *(Canadian dollars)*	1,724	1,524

CONSOLIDATED STATEMENTS OF RETAINED EARNINGS (unaudited)

Three months ended March 31 (Canadian dollars in millions)	**2009**	**2008**
Retained earnings, beginning of period	1,497	1,258
Change in accounting policy for the recognition of future income tax assets and liabilities *(Note 2)*	12	-
Net income	177	157
Dividends *(Note 3)*	(108)	(41)
Retained earnings, end of period	1,578	1,374

CONSOLIDATED STATEMENTS OF ACCUMULATED OTHER COMPREHENSIVE INCOME (unaudited)

Three months ended March 31 (Canadian dollars in millions)	**2009**	**2008**
Accumulated other comprehensive income, beginning of period	(10)	(9)
Other comprehensive loss	-	(1)
Accumulated other comprehensive income, end of period	(10)	(10)

See accompanying notes to Consolidated Financial Statements.

HYDRO ONE INC.
CONSOLIDATED BALANCE SHEETS (unaudited)

(Canadian dollars in millions)	**March 31, 2009**	**December 31, 2008**
Assets		
Current assets:		
Cash and cash equivalents	-	16
Short-term investments	142	-
Accounts receivable (net of allowance for doubtful accounts)	840	754
Regulatory assets	68	64
Materials and supplies	22	19
Other *(Note 2)*	31	15
	1,103	868
Fixed assets:		
Fixed assets in service	17,455	17,334
Less: accumulated depreciation	(6,515)	(6,418)
	10,940	10,916
Construction in progress	1,091	912
Future use land, components and spares	127	132
	12,158	11,960
Long-term assets:		
Deferred pension asset	438	441
Regulatory assets *(Note 2)*	875	291
Goodwill	133	133
Intangibles (net of accumulated amortization) *(Note 2)*	179	162
Future tax asset *(Note 2)*	14	-
Other assets	18	21
	1,657	1,048
Total assets	14,918	13,876

See accompanying notes to Consolidated Financial Statements.

HYDRO ONE INC.
CONSOLIDATED BALANCE SHEETS (unaudited)

(Canadian dollars in millions)	**March 31, 2009**	**December 31, 2008**
Liabilities		
Current liabilities:		
Bank indebtedness	22	-
Accounts payable and accrued charges *(Note 2)*	720	791
Regulatory liabilities *(Note 2)*	76	43
Accrued interest	109	64
Short-term notes payable	150	-
Long-term debt payable within one year *(Note 4)*	-	400
	1,077	1,298
Long-term debt *(Note 4)*	6,337	5,733
Other long-term liabilities:		
Employee future benefits other than pension	920	908
Regulatory liabilities *(Note 2)*	563	564
Future tax liabilities *(Note 2)*	565	-
Environmental liabilities	238	237
Long-term accounts payable and accrued charges	13	12
	2,299	1,721
Total liabilities	9,713	8,752
Shareholder's equity		
Preferred shares (authorized: unlimited; issued: 12,920,000)	323	323
Common shares (authorized: unlimited; issued: 100,000)	3,314	3,314
Retained earnings *(Note 2)*	1,578	1,497
Accumulated other comprehensive income	(10)	(10)
Total shareholder's equity	5,205	5,124
Total liabilities and shareholder's equity	14,918	13,876

See accompanying notes to Consolidated Financial Statements.

HYDRO ONE INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS (unaudited)

Three months ended March 31 (Canadian dollars in millions)	**2009**	**2008**
Operating activities		
Net income	177	157
Environmental expenditures	(1)	(2)
Adjustments for non-cash items:		
Depreciation and amortization (excluding removal costs)	115	123
Revenue difference deferral account	-	(20)
Regulatory liability refund account	(5)	22
Other regulatory asset and liability accounts	(10)	4
Future taxes	3	-
Amortization of debt issuance costs	-	1
	279	285
Changes in non-cash balances related to operations	(94)	(56)
Net cash from operating activities	185	229
Financing activities		
Long-term debt issued	600	550
Long-term debt retired	(400)	-
Short-term notes payable	150	-
Dividends paid	(108)	(41)
Other	6	5
Net cash from financing activities	248	514
Investing activities		
Capital expenditures	(311)	(193)
Intangibles	(25)	(18)
Other assets	7	6
Net cash used in investing activities	(329)	(205)
Net change in cash and cash equivalents	104	538
Cash and cash equivalents, beginning of period	16	(12)
Cash and cash equivalents, end of period	120	526

See accompanying notes to Consolidated Financial Statements.

1. BASIS OF PRESENTATION

These interim Consolidated Financial Statements do not conform in all respects to the disclosure requirements of Canadian generally accepted accounting principles for annual financial statements and should, therefore, be read in conjunction with the annual Consolidated Financial Statements of Hydro One Inc. (Hydro One or the Company) for the year ending December 31, 2008 which include information necessary or useful to understanding the Company's business and financial statement presentation. In particular, the Company's significant accounting policies and practices are presented as Note 2 to the annual Consolidated Financial Statements, and have been consistently applied in the preparation of these interim Consolidated Financial Statements, except as described below in Note 2.

The demand for electricity generally follows normal weather-related variations, and therefore the Company's energy-related revenues, all other things being equal, will tend to be higher in the first and third quarters than in the second and fourth quarters.

2. ACCOUNTING CHANGES

Change in Accounting Policy –Goodwill and Intangibles

Effective January 1, 2009, the Company adopted Canadian Institute of Chartered Accountants' (CICA) Handbook Section 3064, *Goodwill and Intangible Assets*, which replaced CICA Handbook Sections 3062, *Goodwill and Other Intangible Assets*, and CICA Handbook Section 3450, *Research and Development Costs*. The new Section establishes standards for the recognition, measurement, presentation and disclosure of goodwill and other intangible assets.

As a result of adopting this new accounting standard, the Company reclassified computer applications software previously classified as fixed assets to intangible assets. These assets had a net book value of $177 million as at March 31, 2009 ($159 million as at December 31, 2008). In addition, the Company also reclassified other assets with a net book value of $2 million as at March 31, 2009 ($3 million as at December 31, 2008) previously classified as long-term other assets.

Change in Accounting Policy –Accounting for Income Taxes

Effective January 1, 2009, the Company adopted amendments to the CICA Handbook Section 3465 - *Income Taxes* and CICA Handbook Section 1100 – *Generally Accepted Accounting Standards*. These amended Sections establish new standards for the recognition, measurement, presentation and disclosure of future income tax assets and liabilities of rate regulated enterprises.

For transactions and events that cause temporary differences between the tax basis of assets and liabilities and their carrying amounts for accounting purposes, the adoption of these amended sections requires the recognition of future income tax assets and liabilities, and correspondingly the recognition of regulatory liabilities and assets. The temporary differences primarily relate to capital cost allowance in excess of deprecation and employee future benefits other than pension.

As a result of adopting these amended standards, on January 1, 2009, the Company recognized current future income tax assets of $20 million, long-term future income tax assets of $12 million and long-term future income tax liabilities of $503 million. The current future income tax asset is included with other assets on the Balance Sheet. The Company also recognized corresponding current regulatory liabilities of $29 million, long-term regulatory liabilities of $14 million and long-term regulatory assets of $526 million. An adjustment to retained earnings of $12 million was recorded as at January 1, 2009 for the cumulative earnings impact of future income tax assets and liabilities as at December 31, 2008 that are excluded from the rate setting process.

3. DIVIDENDS

During the three months ended March 31, 2009, preferred dividends in the amount of $4 million (2008 - $4 million) and common dividends in the amount of $104 million (2008 - $37 million) were declared.

4. LONG-TERM DEBT

During the three months ended March 31, 2009, Hydro One issued additional notes under the Company's Medium-Term Note Program.

The first issue on January 13, 2009 was an additional offering of medium term notes with a principal amount of $100 million having a term of 1.8 years with a coupon rate of 3.89%. The notes are due on November 19, 2010. The original issue, on November 19, 2008 had a principal amount of $100 million, bringing the total amount outstanding for this issue to $200 million.

The second issue on January 14, 2009 was an additional offering of medium term notes with a principal amount of $200 million having a term of 4.8 years with a coupon rate of 5.0%. The notes are due on November 12, 2013. The original issue, on November 10, 2008 had a principal amount of $400 million, bringing the total amount outstanding for this issue to $600 million.

The third issue on March 3, 2009 was a medium term note with a principal amount of $300 million having a term of 30 years with a coupon rate of 6.03%. The notes are due on March 3, 2039.

In the first quarter, the Company entered into three forward rate agreements in order to lock-in three interest rate resets on the floating rate it pays on a $250 million interest rate swap with settlement dates of March 3, 2009, June 3, 2009 and September 3, 2009 respectively. The three forward rate agreements are classified as held-for-trading and measured at fair value. As at March 31, 2009, the fair value of these forward rate agreements is insignificant.

5. EMPLOYEE FUTURE BENEFITS

Pension Asset Transfer

Effective March 1, 2002, Hydro One began receiving a range of services from Inergi LP, including information technology, customer care, supply chain and certain human resources and financial services. In connection with this agreement, the Company transferred approximately 770 regular employees to Inergi LP. On March 10, 2008, the Company was granted consent from the Financial Services Commission of Ontario to transfer pension assets and related pension liabilities for affected employees from the Hydro One Pension Plan to the Inergi LP Pension Plan. Under the agreement, the Company recognized a settlement of $21 million in its results of operations for the first quarter of 2008, inclusive of a related interest credit of $6 million. The pension asset transfer took place in the second quarter of 2008.

Total benefit costs are as follows:

Three months ended March 31 (Canadian dollars in millions)	**2009**	**2008**
Pension		
Net periodic benefit cost	32	10
Pension fund contribution	29	25
Less: Portion attributable to labour and capitalized as part of the cost of fixed assets	12	10
Charged to results of operations	17	15
Employee Future Benefits Other than Pension		
Net periodic benefit cost	20	23
Less: Portion attributable to labour and capitalized as part of the cost of fixed assets	8	9
Charged to results of operations	12	14

6. SEGMENTED REPORTING

Hydro One has three reportable segments:

- The Transmission Business, which comprises the core business of providing 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
- An "other" segment primarily consisting of a telecommunications business.

The designation of segments has been based on a combination of regulatory status and the nature of the products and services provided. Segment information on the above basis is as follows:

Three months ended March 31 (Canadian dollars in millions)	**Transmission**	**Distribution**	**Other**	**Consolidated**
2009				
Segment profit				
Revenues	302	986	15	1,303
Purchased power	-	666	-	666
Operation, maintenance and administration	103	127	13	243
Depreciation and amortization	58	64	2	124
Income before financing charges and provision for payments in lieu of corporate income taxes	141	129	-	270
Financing charges				72
Income before provision for payments in lieu of corporate income taxes				198
Capital expenditures	187	148	1	336
2008				
Segment profit				
Revenues	304	908	10	1,222
Purchased power	-	596	-	596
Operation, maintenance and administration	97	115	9	221
Depreciation and amortization	59	70	1	130
Income before financing charges and provision for payments in lieu of corporate income taxes	148	127	-	275
Financing charges				69
Income before provision for payments in lieu of corporate income taxes				206
Capital expenditures	107	102	2	211

(Canadian dollars in millions)	**March 31, 2009**	**December 31, 2008**
Total assets		
Transmission	8,488	7,877
Distribution	6,177	5,873
Other	253	126
	14,918	13,876

All revenues, costs and assets, as the case may be, are earned, incurred or held in Canada.

7. COMPARATIVE FIGURES

The comparative unaudited interim Consolidated Financial Statements have been reclassified from statements previously presented to conform to the presentation of the March 31, 2009 unaudited interim Consolidated Financial Statements.