

Building a better and brighter future

hydroOne



2020 Annual Report

Corporate Profile

Hydro One Limited (TSX: H) through its wholly-owned subsidiaries, is Ontario's largest electricity transmission and distribution provider with approximately 1.4 million valued customers, approximately \$30.3 billion in assets as of December 31, 2020, and annual revenues in 2020 of approximately \$7.3 billion.

Our team of approximately 8,700 skilled and dedicated employees proudly build and maintain a safe and reliable electricity system which is essential to energizing life in communities across the province. In 2020, Hydro One invested approximately \$1.9 billion in its transmission and distribution networks and supported the economy through buying approximately \$1.7 billion of goods and services. We are committed to the communities where we live and work through community investment, sustainability and diversity initiatives. We are designated as a Sustainable Electricity Company by the Canadian Electricity Association. Hydro One Limited's common shares are listed on the TSX and certain of Hydro One Inc.'s medium term notes are listed on the NYSE. Additional information can be accessed at www.hydroone.com; www.sedar.com or www.sec.gov.

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1

Higher Customer Satisfaction

Our focus on customers and customer advocacy helped achieve high customer satisfaction scores, with residential and small business customer satisfaction increasing to 87% from 86%, and Hydro One Telecom customer satisfaction increasing to 91% from 90%.

6

Reducing Costs

A 9.4% or approximately \$111 million reduction in annual operating costs since 2019.



2020 Highlights

Guided by our purpose of energizing life in Ontario, we are living up to our deep responsibility to put people first as we navigate COVID-19. Throughout the pandemic, our decisions and actions were continuously guided by two priorities – protecting our employees and maintaining the safe and reliable supply of electricity to our valued customers.

2

Stronger Safety Culture

We launched our Safety Improvement Team, which made concrete recommendations to improve the safety culture of our organization to eliminate serious injuries at Hydro One. We will put these recommendations to work in the coming years.

3

Standing Up for Communities

Our community partnerships supported Ontarians through the pandemic, helping local and Indigenous communities respond to emerging and urgent needs for critical food, medical, safety and other supplies.

4

Reliable Electricity Supply

We improved the System Average Interruption Duration Index (SAIDI) of our transmission network by approximately 41.8%¹ over 2019, successfully delivering reliable power to our electricity utility customers.

5

More Productivity Savings

A 41.4% increase in year-over-year productivity savings with \$286.0 million saved in 2020 as compared to \$202.3 million in 2019. Total productivity savings since 2015 amount to \$738 million.

7

Critical Capital Investments

We invested approximately \$1.9 billion in capital to expand the electricity grid and renew and modernize existing infrastructure.

8

Sustainability Leadership

Our sustainability progress was again recognized by our peers, with Corporate Knights ranking us 11th in its annual list of Best 50 Canadian Corporate Citizens and the Canadian Electricity Association re-designating Hydro One as a Sustainable Electricity Company.

9

Progressive Aboriginal Relations

We increased total procurement spending with Indigenous businesses to \$42.0 million, our highest spend to date. In addition, the Canadian Council for Aboriginal Business advanced Hydro One to Silver level certification in Progressive Aboriginal Relations from our Bronze level in 2017.

10

Best Employer, 6th Year

For the sixth consecutive year, Hydro One has been recognized by Forbes in its list of Canada's Best Employers for 2021, reflecting our commitment to creating a diverse, inclusive and engaged workforce, both during these unprecedented times and into the future.

¹ Transmission SAIDI for multi-circuit supplied delivery points

A message from our

Chair



I am incredibly proud of the resilience employees have shown this past year, doing everything possible to maintain the critical supply of electricity to customers across the province – keeping loved ones safe, hospitals running, protecting the most vulnerable in communities, and providing financial relief across Ontario.



18.5%

total shareholder return in 2020

50%

women on our Independent Non-Executive Board Members

This effort required strong leadership and a focused strategy as the COVID-19 pandemic fundamentally changed how we live and work. I know Mark and his team will retain the insights gained from the pandemic to help Ontario emerge stronger, as we work together to create a better and brighter future for all.

Our primary focus at the Board level has been to support Hydro One's executive team, ensuring they have the tools and capacity to achieve our two pandemic priorities – to protect our employees and to maintain the safe and reliable supply of electricity to Hydro One customers.

They have successfully delivered on these priorities, while simultaneously executing our corporate strategy and capital investment commitments. As a result, Hydro One added 18.5% in total returns to our shareholders and acquired the Orillia Power Distribution Corporation and the business and assets of Peterborough Distribution Inc. this past year.

Equally important in this time of great need, Hydro One has stood with our communities and charitable organizations across Ontario to respond to the urgent challenges presented by COVID-19, lending a helping hand to those making a lasting difference in the communities we serve.

As we move forward into the future, we will continue to fulfill our mission of energizing life for people and communities through a network built for the possibilities of tomorrow.

Our corporate strategy supports that mission, driving us to deliver an improved safety culture, a more reliable grid for our customers, high customer satisfaction, sustainable business practices and a lower environmental footprint.

In 2020, the Board revamped the structure and mandates of its committees to support Hydro One's new corporate strategy and further embed our vision across the organization. We established the Indigenous Peoples, Safety & Operations Committee¹ in order to elevate the importance of improving our safety culture and strengthening our partnerships with First Nations. We also elevated the review of Hydro One's annual sustainability report to the full Board, underscoring the improved transparency and accountability of our environmental, social and governance (ESG) disclosures. Finally, we recognized the importance of regulatory and public policy matters within the electricity sector by expanding our Governance & Regulatory Committee.²

¹ Previously the Health, Safety, Environment and Indigenous Peoples Committee

² Previously the Governance Committee

The Board met virtually and frequently throughout 2020 to ensure Mark and his team had the support they needed to execute Hydro One's corporate strategy and achieve our pandemic priorities. Technology allowed more people from more places to participate virtually in our annual general meeting. While we anticipate hosting a virtual AGM in 2021, we look forward to hosting our next in person gathering.

Throughout the pandemic, the Board has deepened our level of engagement with Hydro One stakeholders. We have been extremely supportive of Hydro One's Pandemic Relief Program, established in mid-March to assist customers affected by COVID. We applaud management for pledging its support for the anti-racism BlackNorth Initiative, as well as to Indigenous Peoples and People of Colour. We will continue to collectively work toward ending systemic racism and ensuring our organization reflects the communities we serve.

We welcomed Stacey Mowbray to the Board of Directors in July, who brings extensive CEO and public company board experience. Her strong track record in leading successful and high profile publicly traded consumer brands reinforces our Board and reaffirms our support of management's focus on delivering

exceptional customer service in the digital age. The Board thanks Anne Giardini for her service and for spearheading our First Nations partnership strategy and our renewed commitment to safety. Our Independent Non-Executive Board Members remain composed of 50% women and 50% men, again reflecting best practices in board diversity and surpassing our Catalyst Accord commitment.

On behalf of my Board colleagues and all Hydro One stakeholders, I would like to thank Mark and his executive team for their steady leadership in these uncertain times. We also want to recognize the resilience and dedication of Hydro One's 8,700 employees, particularly those on the frontlines who continued to support our customers and communities across the province. Together, we are confident that Hydro One will continue to energize life for families, businesses and communities across Ontario.



Timothy Hodgson
Chair



“As we move forward into the future, we will continue to fulfill our mission of energizing life for people and communities through a network built for the possibilities of tomorrow.”



A message from our

President & CEO



Power is a lifeline connecting families, businesses and communities, especially during times of crisis. During this historic moment governments, companies, and individuals are being evaluated for their commitment to helping people and communities, standing up for equity and inclusion, and contributing to a more sustainable world.



We have stood by our customers, providing financial relief and flexibility during a period of great uncertainty. Hydro One was the first utility in Ontario to launch a Pandemic Relief Program, supporting customers experiencing hardship with financial assistance and increased payment flexibility. We also extended our Winter Relief Program to ensure our customers remained connected, suspended late fees for all customers, and returned approximately \$5 million in security deposits to more than 4,000 businesses across the province. We will continue to put the needs of customers and communities first, advocating on their behalf to provide relief, flexibility and choice, now and in the future.

Our employees are our greatest asset and through their passion, determination and ingenuity, we came together, dug deep and emerged from 2020 even stronger. We have kept our colleagues and workplaces safe, and maintained the critical supply of electricity to the benefit of all Ontarians.

Hydro One achieved strong performance despite facing unprecedented challenges – we strengthened our customer advocacy, deepened our community partnerships, and increased our productivity savings by 41.4%, while never losing our focus on safety.



Hydro One teams worked around the clock to ensure an uninterrupted supply of power for every Ontarian – proactively patrolling power lines that feed hospitals, health care facilities and other critical infrastructure, prioritizing projects that enable our food supply, and connecting new homes to ensure people have shelter.

Living Our Strategy

More than simply aspirational words on paper, our new corporate strategy, along with our vision and mission, have been our guidepost in navigating our way through the pandemic. It has anchored us to our purpose, while providing us with the flexibility to quickly respond to evolving stakeholder needs. Despite a pause in our operations early in the pandemic to introduce new practices to ensure the safety of our crews on the front lines, we successfully executed Hydro One’s 2020 workplan. This is not only vital to ensuring system safety and reliability for today, but also for longer-term work that will help restart and sustain the economy in the future.

Build a Grid for the Future: In 2020, we continued to invest in the reliability and performance of our transmission and distribution systems, renew aging infrastructure, connect new load customers and generation sources, and improve our service to customers. We made capital investments of approximately \$1.9 billion, placed approximately \$1.6 billion in projects into service and supported the economy through buying approximately \$1.7 billion of goods and services.

While our restoration times were impacted by challenging weather, and the pandemic, we were still able to improve our transmission reliability and maintain the frequency of customer interruptions on our distribution network.

We continue to invest in infrastructure and technology to build a sustainable grid for the future – investments that harden and protect our assets against the changing climate. As part of our ESG commitments, we are working to align our climate-related disclosures with the Taskforce on Climate-related Financial Disclosures, reduce our carbon footprint, and manage the impacts

of climate change on our business. For example, we remain on track to convert 50% of our fleet of sedans and SUVs to electric vehicles or hybrids by 2025 in order to reduce carbon emissions.

Safety & Efficiency: Protecting the health and safety of our employees has been our top priority throughout the pandemic. While we were successful in minimizing the impact of the pandemic on our employees, our success is muted because we sadly lost an employee during the year to a motor vehicle crash. Our entire executive team will continue to focus on transforming our safety culture and implement the concrete recommendations made by our Safety Improvement Team to improve our safety culture and eliminate serious injuries at Hydro One.

In 2020, we continued to engage with employees on transforming work processes to drive productivity, reliability and efficiency. Through this work and other initiatives, we achieved \$286.0 million in annual total productivity savings and reduced our operating costs by approximately \$111 million.

Trusted Partner: We continued to strengthen our community and Indigenous partnerships in 2020. We contributed \$42 million to the Indigenous economy by sourcing goods and services from Indigenous businesses – this represents the highest spend to date. We also launched a new fund to support those who provide services to Ontarians, helping to strengthen community resiliency and safety.

Our ability to problem-solve and be nimble would not have been possible without the devotion and hard work of our employees and the partnership of our unions. We were pleased that despite COVID-19, we were able to renew two collective agreements with the Power Workers’ Union, covering a large sector of our employees, which will be critical to our journey toward zero serious injuries.



\$1.7b

supported economy by buying goods and services

\$286m

in annual total productivity savings in 2020

41.4%

increase in annual total productivity savings (capital and OM&A) in 2020 over 2019

\$111m

in reduced operating costs in 2020



“To us, energizing life doesn't just mean supplying safe and reliable power, it also means we are a company that puts people first, especially when they need it most.”

On the regulatory front, we continued to work constructively with the Ontario Energy Board (OEB) and secured approval for our 2020–2022 transmission rate application.

We also collaborated with others in the electricity sector, including the Ontario Energy Association and the Electricity Distributors Association, to bring a united voice to government and to regulatory policy decisions.

Customer Advocacy: In addition to the Pandemic Relief Program, we undertook a number of initiatives that put people first and supported customers through COVID-19. Our customer advocacy efforts, for example, successfully led to residential customers – for the first time ever – having choice in their pricing plans.

We voluntarily deferred rate increases for our transmission customers and extended financial relief and flexibility to small businesses that have been experiencing hardship. We applauded the Ontario government's decision to help our commercial and industrial customers save between 14%–16%, enabling Ontario businesses to be competitive with other North American jurisdictions. We also supported the government's decision to introduce a temporary electricity relief rate for residential, small business and farm customers.

Customers responded to our efforts to keep them connected to safe and reliable power while helping them access financial relief programs and more flexible service options. We received a record high residential and small business customer satisfaction rate of 87%.

Innovate and Grow the Business:

We are pursuing investments designed to energize life for Ontarians well into the future. As part of our strategy to be the provider of choice for Ontario communities,

we successfully completed the acquisition of Orillia Power Distribution Corporation and the business assets of Peterborough Distribution Inc. Joining the Hydro One family are approximately 51,000 new customers and over 75 employees. This consolidation of our business benefits all Hydro One customers because it makes the provincial grid more efficient, while reducing costs across the system.

We officially launched our innovative joint venture Ivy Charging Network™ (Ivy) in 2020 to support a greener transportation sector. Ivy opened 23 fast charging sites across Ontario, and is on track to have over 160 fast chargers across approximately 60 locations in Ontario by the end of 2021.

Our IT team leveraged our secure technology environment to seamlessly transition a large portion of employees to work-from-home. Additionally, the substantial increase in Ontarians working from home increased demand for Hydro One Telecom's service, resulting in the expansion of its fibre connectivity options and more cloud services, data backup tools and secure data storage for business customers to choose from.

Strong Foundation, Sustainable Future

Looking forward, we are energized by the possibilities ahead. While COVID-19 has brought new challenges to Hydro One, our ability to quickly learn and adapt gives me great confidence that we will emerge from this pandemic as a stronger organization. To us, energizing life doesn't just mean supplying safe and reliable power, it also means we are a company that puts people first, especially when they need it most.

We stand ready to help power Ontario's economic recovery from this global pandemic. To that end, we are preparing for the upcoming joint rate application for both our transmission and distribution businesses. As a company that puts customers first we engaged in an extensive customer outreach to inform the development of our investment plan. This plan will inform our views and plans on affordability, service levels, and sustainability over the next five years, starting in 2023. We expect to file our application later this year, and we look forward to a regulatory decision that will provide clarity and stability in our transmission and distribution capital plans, allowing us to focus on executing our strategy.

On behalf of everyone at Hydro One, I thank Darlene Bradley and Saylor Militz-Lee for their service to our organization and I welcome Lyla Garzouzi, our new Chief Safety Officer and Megan Telford, our new Chief Human Resources Officer, to our leadership team. Finally, I want to thank Hydro One employees for the incredible passion, pride, ingenuity and resilience you have shown during these uncertain times. Your commitment has enabled us to deliver great results to our shareholders and proudly energize life for our customers and communities across Ontario.

Mark Poweska
President and Chief Executive Officer

Standing with Ontarians

Hydro One's Pandemic Response



Hydro One has played a critical role in energizing life in Ontario throughout the pandemic – supporting families, the economy and those on the frontlines fighting this virus. Our priorities have been to ensure the safety of our employees and customers, and to support the electricity grid to keep all essential services operating and the economy open and ready to grow again.

Easing Customer Hardship

Hydro One has a deep responsibility to support our customers as they navigate these challenging times. We are focused on keeping customers connected and advocating for the programs that help them avoid the stress of falling behind. Through our Pandemic Relief Program, we are providing financial assistance and increased payment flexibility to residential and small business customers experiencing hardship. We also extended our Winter Relief Program to ensure our residential customers stayed connected during this challenging time and suspended late payment fees for all our customers.

We introduced other measures to provide our customers with rate relief including the return of approximately \$5 million in security deposits to more than 4,000 commercial businesses; and connecting customers with the government's enhanced COVID-19 Energy Assistance Program (CEAP) for residential and small business customers (as well as registered charities), which offers one-time credits on their bill.³

We will continue to stand with Ontarians, providing them with relief, flexibility and choice now and in the future.

Standing With Our Communities

Hydro One aspires to help build safe communities across Ontario. As a result of COVID-19, our community investment work has become more critical than ever. We focused on protecting society's most vulnerable during this period of uncertainty.

- We partnered with GlobalMedic, a registered Canadian charity specializing in disaster relief, to deliver 13,500 critical aid kits of food and safety supplies – including food staples, reusable face masks and soap – to Indigenous communities across the province during the COVID-19 pandemic.
- We supported the [Métis Nation of Ontario's \(MNO's\)](#) pandemic relief fund and its 31 community councils, helping them provide food, medical and pharmaceutical supplies to their vulnerable citizens.
- We supported Feed Ontario's [COVID-19 Emergency Food Box Program](#), donating \$300,000 worth of meals through customer, employee and social media campaigns. With the help of our community, we were able to donate an additional 51,000 meals to those in need.
- We fast-tracked \$32.9 million in payments to small, medium and Indigenous suppliers in Ontario to help with much needed cash flow.

³ In late December 2020, Hydro One offered enhanced CEAP and CEAP-Small Business (CEAP-SB) benefits for 2021 in recognition of the impact the second wave of COVID-19 was having on our customers.



13,500

food and safety kits
provided to First Nations
communities

\$300,000

worth of meals through
customer, employee and
social media campaigns

A better & brighter future for all

Energizing Life



Hydro One has a critical role to play in helping Ontario emerge stronger from the COVID-19 global pandemic. We will achieve this by building a more sustainable business, supporting our communities, and contributing to a more inclusive and equitable society.

In 2020, we continued to execute the sustainability priorities of our corporate strategy – climate change and extreme weather, Indigenous and community partnerships and diversifying talent – in order to deliver on our vision of a better and brighter future for all.

Supporting the Environment: Hydro One’s climate policy and climate change management plan guide our climate-related business activities.

In 2020, we made investments to increase the resiliency of our assets to better withstand the impact of climate change and extreme weather while simultaneously limiting the environmental impacts of our activities.

Responding to demand for greener transportation options, our joint venture Ivy opened 23 electric vehicle fast-charger locations, making charging on-the-go easy and convenient for Ontarians.

Making a Social Impact: COVID-19 brought serious challenges to many communities that worked tirelessly to meet critical and emerging local needs.

In response, we launched a new fund to support those who provide services to Ontarians – helping to strengthen community resiliency and safety. Charitable organizations, municipalities and Indigenous communities were able to apply for up to \$25,000 toward pandemic

response efforts and initiatives that improve physical and emotional safety. From supporting well-being through an outdoor skating trail or delivering meals to vulnerable populations, the fund helps local organizations build a better and brighter future for their communities.

An Inclusive Equitable Society: Hydro One is on a journey to better understand the experiences of Black, Indigenous Peoples, People of Colour and other marginalized employees at the company in order to address systemic racism and biases, while creating an inclusive environment. As part of this, our CEO Mark Poweska joined other Canadian CEOs in signing the BlackNorth Initiative Pledge – which aims to move Canada toward ending anti-Black systemic racism and creating opportunities for underrepresented groups. We are committed to listening, understanding, and examining our own assumptions in order to eliminate unconscious bias in the workplace and to promote racial equity. We are also committed to identifying systemic barriers and putting plans in place to remove and prevent them in the future, all in an effort to advance racial equity.

We established a new Diversity and Inclusion Council, which has a mandate to advocate for and drive change on diversity, inclusion and equity programming, initiatives, and policies.

Transparent Governance: Hydro One is committed to transparent disclosures in our ESG reporting. That is why we enhanced our sustainability reporting to align with the Global Reporting Initiative’s (GRI) core standards and the Sustainability Accounting Standards Board (SASB) framework. We also committed to aligning our climate-related disclosures with the Taskforce on Climate-related Financial Disclosures (TCFD) over time.



\$42m

total procurement spending with Indigenous businesses in 2020

50%

fleet conversion of sedans and SUVs to electric vehicles or hybrids by 2025

Corporate Governance

Strong corporate governance practices are the heart of how we manage our day-to-day operations in the interest of all stakeholders.

Hydro One and its independent Board of Directors recognize the importance of corporate governance in the effective management of the company. A governance agreement between Hydro One and the Province of Ontario, which was executed in advance of the November 2015 Initial Public Offering of the company, supports strong corporate governance centered on independence, integrity and accountability which is in the best interests of shareholders, and promotes and strengthens relationships with our customers, employees, the communities where we operate and other stakeholders.

Hydro One's Board of Directors is composed of a diverse and accomplished group of independent, proven business leaders with deep corporate governance experience. The Board's primary role is overseeing corporate performance and the quality, depth and continuity of management required to meet the company's strategic objectives. Hydro One is committed to establishing and maintaining

best corporate governance practices. The company's practices are fully aligned with the rules and regulations issued by Canadian Securities Administrators and the Toronto Stock Exchange.

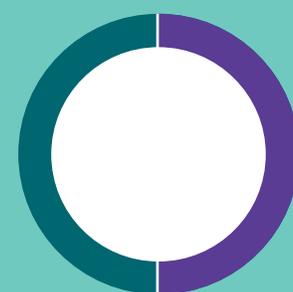
Board Structure: The Chair is responsible for leading the Board of Directors in carrying out its duties and responsibilities effectively, efficiently and independent of management. The Chair is nominated and confirmed annually by special resolution of the Board. Consistent with best practices, Hydro One's Board Chair is separate from the role of President and Chief Executive Officer and is independent of Hydro One and the Province of Ontario.

In 2020, the Board revised the structure and mandates of its committees to support Hydro One's new corporate strategy. The Board established the Indigenous Peoples, Safety & Operations Committee⁴ (IPSO) in order to elevate the importance of an improved safety culture and strong First Nations partnerships. The IPSO Committee also oversees the company's sustainability and climate change strategies and major capital projects. The Board also recognized the importance of regulatory and public policy matters within the electricity sector by establishing the Governance & Regulatory committee⁵.

Hydro One's Gender Balanced Independent Board of Directors

Much work remains in advancing diversity and inclusion at all levels of Hydro One to better reflect where we work and the communities we represent across the province. However, we are pleased to note, that with the appointment of Stacey Mowbray, the current composition of our Independent Non Executive Board Members are five women (50%) and five men (50%). We believe this balance makes us one of the most gender progressive boards in North America, reflecting best practices in board diversity and surpassing our Catalyst Accord commitment to maintaining at least 30% female board members.

Board Gender Diversity¹



¹ Hydro One's Independent Non Executive Board Members

To learn more about the Directors, committee mandates and composition, go to www.HydroOne.com/Investors

Board of Directors and Committees (as of March 23, 2021)

★ Chair • Committee Member

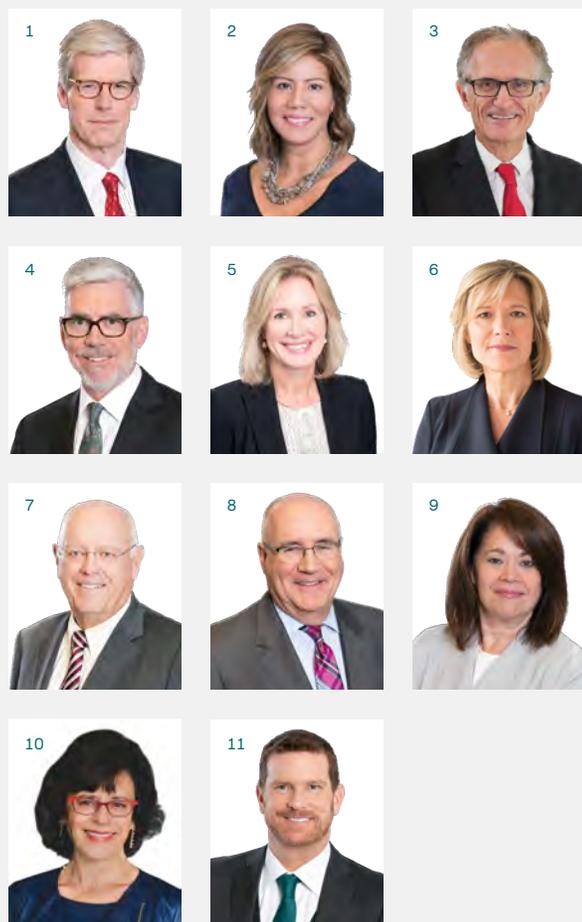
| Committees | Audit | Governance & Regulatory | Human Resources | Indigenous Peoples, Safety & Operations ⁴ |
|--------------------------------|-------|-------------------------|-----------------|--|
| Timothy Hodgson (Chair) | | | | |
| Mark Poweska (President & CEO) | | | | |
| Cherie Brant | • | | | • |
| Blair Cowper-Smith | | ★ | • | |
| David Hay | • | | | ★ |
| Jessica McDonald | | | • | • |
| Stacey Mowbray ⁶ | | • | | • |
| Russel Robertson | ★ | | • | |
| William Sheffield | • | • | | |
| Melissa Sonberg | • | | ★ | |
| Susan Wolburgh Jenah | | • | | • |

⁴ Previously the Health, Safety, Environment and Indigenous Peoples Committee

⁵ Previously the Governance Committee

⁶ Became a director on July 23, 2020

Board of Directors



1. **Timothy Hodgson**, MBA, FCPA, ICD.D
Corporate Director, Chair of Hydro One Ltd, Chair of Sagcor Financial Company Limited, Director Public Sector Pension Investment Board (PSP Investments), Former Director Alignvest Acquisition II Corporation, retired Managing Partner Alignvest Management Corporation, Former Special Advisor to Bank of Canada Governor Mark Carney, Former CEO Goldman Sachs Canada
2. **Cherie Brant**, J.D.
Partner, Borden Ladner Gervais LLP, Director Anishnawbe Health Foundation, Director Canadian Council for Aboriginal Business, Aboriginal Education Council for Centennial College, Aboriginal Energy Working Group-IESO
3. **Blair Cowper-Smith**, LLB, LLM, ICD.D
Principal and founder Erin Park Business Solutions, Former Chief Corporate Affairs Officer OMERS
4. **David Hay**, LLB, ICD.D
Managing Director Delgate Incorporated, Former President and CEO New Brunswick Power Corporation, Former Vice-Chair and Managing Director of CIBC World Markets Inc., Director EPCOR Utilities Inc., Council Member of the Council for Clean and Reliable Energy
5. **Jessica McDonald**, ICD.D
Corporate Director, Former Chair, Canada Post Corporation, Former President & CEO BC Hydro & Power Authority, Director Coeur Mining Inc., Member Council of Sustainable Development Technology Canada and Greater Vancouver Board of Trade
6. **Stacey Mowbray**, MBA, BBA
Corporate Director, Former President North America WW International (formerly Weight Watchers), Director Currency Exchange International, Director Sleep Country Canada
7. **Russel Robertson**, FCPA, FCA, ICD.D
Corporate Director, Former EVP and Head, Anti-Money Laundering, BMO Financial Group, Former Vice-Chair, Deloitte & Touche LLP (Canada), Director Bausch Health Companies Inc., Director Turquoise Hill Resources Ltd.
8. **William Sheffield**, BSC, MBA, ICD.D
Corporate Director, Former CEO Sappi Fine Papers, Director Houston Wire & Cable Company, Director Velan Inc., Former Board Member OPG
9. **Melissa Sonberg**, BSC, MHA, ICD.D
Professor in Practice, McGill University, Desautels Faculty of Management, Director Exchange Income Corporation, Director Athenian, Director Group Touchette, Director Canadian Professional Sales Association, Director Women in Capital Markets, Former Senior Vice President, Human Resources & Corporate Affairs and Senior Vice President, Global Brands, Communications and External Affairs at AIMIA
10. **Susan Wolburgh Jenah**, J.D., ICD.D
Corporate Director, Director Laurentian Bank of Canada, Director Aecon Group Inc, and Vice-Chair Humber River Hospital. Member of the Independent Review Committee of Vanguard Investments Canada, and Former Public Governor of the U.S. Financial Industry Regulatory Authority (FINRA)
11. **Mark Poweska**, President and CEO of Hydro One Limited, Former Executive Vice President, Operations at BC Hydro, Chair of Ontario Energy Association, Director Western Energy Institute

Executive Leadership Team



11. **Mark Poweska**
President and Chief Executive Officer
12. **Brad Bowness**
Chief Information Officer
13. **Jason Fitzsimmons**
Chief Corporate Affairs & Customer Care Officer
14. **Lyla Garzouzi**
Chief Safety Officer
15. **Paul Harricks**
Chief Legal Officer
16. **David Lebeter**
Chief Operating Officer
17. **Chris Lopez**
Chief Financial Officer
18. **Megan Telford**
Chief Human Resources Officer

For detailed biographical information of Hydro One Limited Board members, visit www.HydroOne.com/Investors.
The biographical information of Hydro One Limited Board members is based on information available as of March 23, 2021.

Hydro One's

Business Network

Our Regulated Business

Transmission: Our transmission system transmits high-voltage electricity from nuclear, hydroelectric, natural gas, wind and solar sources to distribution companies and industrial customers across Ontario. Our system accounts for approximately 98%⁷ of Ontario's transmission capacity with approximately 30,000 circuit kilometres of high-voltage transmission lines. We also own and operate 25 cross-border interconnections with neighbouring provinces and the United States, which allow electricity to flow into and out of Ontario.

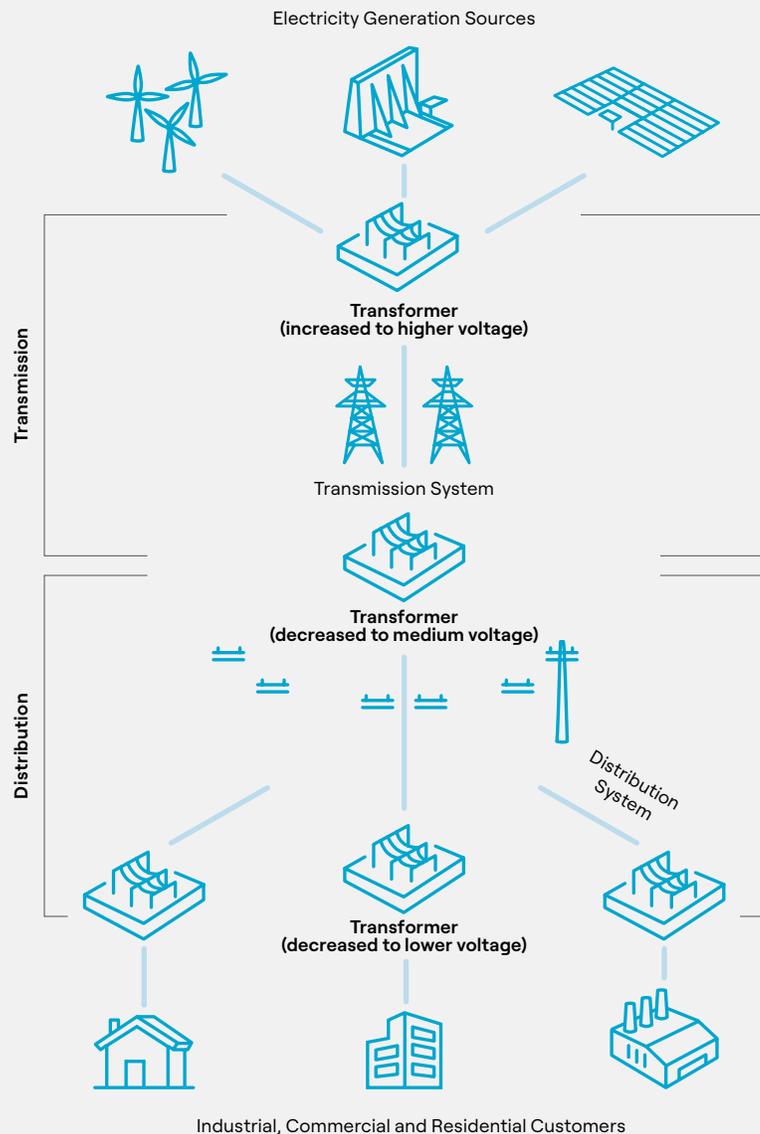
Distribution: Our distribution system is the largest⁸ in Ontario. It consists of approximately 124,000 circuit kilometres of primary low-voltage power lines serving approximately 1.4 million customers, mostly in rural areas. As well, Hydro One Remote Communities Inc. serves customers in one grid-connected and 21 off-grid communities in Ontario's far north.

Our Unregulated Business

Our other segment consists principally of our telecommunications business, Hydro One Telecom Inc. (HOT), which provides telecommunications support for Hydro One's transmission and distribution businesses, as well as for its other business customers. HOT offers comprehensive communications and information technology services and solutions (cloud services, managed services and security-based services) to businesses that extend beyond the core fibre and connectivity services it has traditionally offered.

Hydro One's Role in the Ontario Electric Power System

Our transmission and distribution systems safely and reliably serve communities throughout Ontario. Our customers are suburban, rural and remote homes and businesses across the province. Our communities are proudly and safely serviced by a team of skilled and dedicated employees.



⁷ Based on revenue approved by the OEB
⁸ Based on customers (per OEB yearbook)

1



Everyone Uses Electricity

One of the largest electricity utilities in North America, with significant scale and leadership position across Canada's most populated province.

2



Strong Balance Sheet

One of the strongest investment grade balance sheets in the North American utility sector.

3



Pure-play Transmission and Distribution

Unique combination of electric power transmission and local distribution, with no power generation assets or material exposure to commodity prices.

Why invest?

Hydro One is a unique low-risk opportunity to participate in the transformation of a premium large-scale electric utility.

4



Stable Operations

Stable and growing cash flows with 99% of business fully rate regulated in a constructive, transparent and collaborative regulatory environment.

5



Financial Performance

Predictable self funding organic growth profile with expanding rate base and strong cash flows, together with broad support for refurbishment of aging infrastructure and with ~5% expected rate base CAGR.⁹ No external equity required to fund planned growth.

6



Transparent ESG Reporting

Transparency in our environmental, social and governance (ESG) reporting.

7



Attractive Dividend

Annualized dividend of \$1.0144 per share with attractive 70% 80% target payout ratio.

8



Rate Base Expansion

Opportunity for continued dividend growth with rate base expansion, continued consolidation and efficiency realization.

⁹ Compound Annual Growth Rate (CAGR)

Financial Highlights

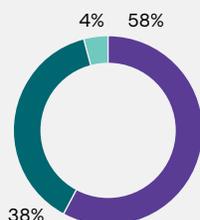
| Year ended December 31 (millions of dollars, except as otherwise noted) | 2020 | 2019 |
|--|--------------|------------|
| Revenues | 7,290 | 6,480 |
| Purchased power | 3,854 | 3,111 |
| Revenues, net of purchased power ¹ | 3,436 | 3,369 |
| Operation, maintenance and administration (OM&A) costs | 1,070 | 1,181 |
| Depreciation, amortization and asset removal costs | 884 | 878 |
| Financing charges | 471 | 514 |
| Income tax expense recovery | (785) | (6) |
| Net income (loss) to common shareholders of Hydro One | 1,770 | 778 |
| Adjusted net income to common shareholders of Hydro One¹ | 903 | 918 |
| Basic earnings per common share (EPS) | \$2.96 | \$1.30 |
| Diluted EPS | \$2.95 | \$1.30 |
| Basic adjusted non-GAAP EPS (Adjusted EPS) ¹ | \$1.51 | \$1.54 |
| Diluted Adjusted EPS ¹ | \$1.51 | \$1.53 |
| Net cash from operating activities | 2,030 | 1,614 |
| Funds from operations (FFO) ¹ | 1,830 | 1,532 |
| Capital investments | 1,878 | 1,667 |
| Assets placed in-service | 1,639 | 1,703 |
| Transmission: Average monthly Ontario 60-minute peak demand (MW) | 20,091 | 19,896 |
| Distribution: Electricity distributed to Hydro One customers (GWh) | 28,379 | 27,536 |
| Debt to capitalization ratio ² | 56.3% | 56.3% |

- See section "Non-GAAP Measures" for description and reconciliation of adjusted net income, basic and diluted Adjusted EPS, FFO and revenues, net of purchased power.
- Debt to capitalization ratio is a non-GAAP measure and has been calculated as total debt (including total long-term debt and short-term borrowings, net of cash and cash equivalents) divided by total debt plus total shareholders' equity, including preferred shares but excluding any amounts related to noncontrolling interest. Management believes that the debt to capitalization ratio is helpful as a measure of the proportion of debt in the Company's capital structure.

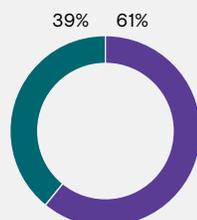
This report contains forward-looking information within the meaning of applicable Canadian securities laws that are based on current expectations, estimates, forecasts and projections about our business and the industry in which we operate, and includes beliefs and assumptions made by the management of Hydro One. Such information includes, but is not limited to, statements relating to: Hydro One's investments in infrastructure and technology to build a sustainable grid, Hydro One's stable and growing cash flows, organic growth profile, expanding rate base and cash flows, expected rate base CAGR, and the elements of Hydro One's strategy, including expectations regarding the company's transmission and distribution rate applications and resulting decisions, rates and impacts. Words such as "expect" and "will" 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. Some of the factors that could cause actual results or outcomes to differ materially from the results expressed, implied or forecasted by such forward-looking information, including some of the assumptions used in making such statements, are discussed more fully in Hydro One Limited's and Hydro One Inc.'s filings with the securities regulatory authorities in Canada, which are available on SEDAR at www.sedar.com. We do not intend, and we disclaim any obligation, to update any forward-looking statements, except as required by law.

All figures in this document are approximate figures that are rounded to the nearest decimal place.

Total Assets
\$30.3b

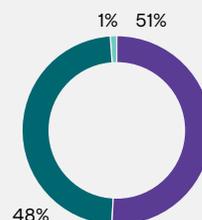


Rate Base
\$21.7b



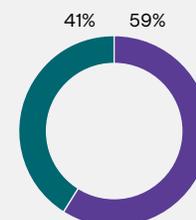
Revenues
(Net of purchased power costs)

\$3.44b



Regulated Earnings
(Before financing charges and income taxes)

\$1.5b



● Transmission ● Distribution ● Other

Total Shareholder Return (TSR)

January 1, 2020 to December 31, 2020



Financial Report



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Management's Discussion and Analysis

For the years ended December 31, 2020 and 2019

The following Management's Discussion and Analysis (MD&A) of the financial condition and results of operations should be read together with the consolidated financial statements and accompanying notes thereto (Consolidated Financial Statements) of Hydro One Limited (Hydro One or the Company) for the year ended December 31, 2020. The Consolidated Financial Statements have been prepared in accordance with United States (US) Generally Accepted Accounting Principles (GAAP). All financial information in this MD&A is presented in Canadian dollars, unless otherwise indicated.

The Company has prepared this MD&A in accordance with National Instrument 51-102 – Continuous Disclosure Obligations of the Canadian Securities Administrators. Under the US/Canada Multijurisdictional Disclosure System, the Company is permitted to prepare this MD&A in accordance with the disclosure requirements of Canadian securities laws and regulations, which can vary from those of the US. This MD&A provides information as at and for the year ended December 31, 2020, based on information available to management as of February 23, 2021.

Consolidated Financial Highlights and Statistics

| Year ended December 31 (millions of dollars, except as otherwise noted) | 2020 | 2019 | Change |
|--|----------------|------------|---------------|
| Revenues | 7,290 | 6,480 | 12.5% |
| Purchased power | 3,854 | 3,111 | 23.9% |
| Revenues, net of purchased power ¹ | 3,436 | 3,369 | 2.0% |
| Operation, maintenance and administration (OM&A) costs | 1,070 | 1,181 | (9.4%) |
| Depreciation, amortization and asset removal costs | 884 | 878 | 0.7% |
| Financing charges | 471 | 514 | (8.4%) |
| Income tax recovery | (785) | (6) | 12,983% |
| Net income to common shareholders of Hydro One | 1,770 | 778 | 127.5% |
| Adjusted net income to common shareholders of Hydro One¹ | 903 | 918 | (1.6%) |
| Basic earnings per common share (EPS) | \$ 2.96 | \$ 1.30 | 127.7% |
| Diluted EPS | \$ 2.95 | \$ 1.30 | 126.9% |
| Basic adjusted non-GAAP EPS (Adjusted EPS) ¹ | \$ 1.51 | \$ 1.54 | (1.9%) |
| Diluted Adjusted EPS ¹ | \$ 1.51 | \$ 1.53 | (1.3%) |
| Net cash from operating activities | 2,030 | 1,614 | 25.8% |
| Funds from operations (FFO) ¹ | 1,830 | 1,532 | 19.5% |
| Capital investments | 1,878 | 1,667 | 12.7% |
| Assets placed in-service | 1,639 | 1,703 | (3.8%) |
| Transmission: Average monthly Ontario 60-minute peak demand (MW) | 20,091 | 19,896 | 1.0% |
| Distribution: Electricity distributed to Hydro One customers (GWh) | 28,379 | 27,536 | 3.1% |
| As at December 31 | 2020 | 2019 | |
| Debt to capitalization ratio ² | 56.3% | 56.3% | |

¹ See section "Non-GAAP Measures" for description and reconciliation of adjusted net income, basic and diluted Adjusted EPS, FFO and revenues, net of purchased power.

² Debt to capitalization ratio is a non-GAAP measure and has been calculated as total debt (including total long-term debt and short-term borrowings, net of cash and cash equivalents) divided by total debt plus total shareholders' equity, including preferred shares but excluding any amounts related to noncontrolling interest. Management believes that the debt to capitalization ratio is helpful as a measure of the proportion of debt in the Company's capital structure.

Overview

Through its wholly-owned subsidiary Hydro One Inc., Hydro One is Ontario's largest electricity transmission and distribution utility. Hydro One owns and operates substantially all of Ontario's electricity transmission network and is the largest electricity distributor in Ontario by number of customers. The Company's regulated transmission and distribution operations are owned by Hydro One Inc. Hydro One delivers

electricity safely and reliably to approximately 1.4 million customers across the province of Ontario, and to large industrial customers and municipal utilities. Hydro One Inc. owns and operates approximately 30,000 circuit kilometres of high-voltage transmission lines and approximately 124,000 circuit kilometres of primary low-voltage distribution lines. Hydro One has three segments: (i) transmission; (ii) distribution; and (iii) other.

For the years ended December 31, 2020 and 2019, Hydro One's segments accounted for the Company's total revenues, net of purchased power, as follows:

| Year ended December 31 | 2020 | 2019 |
|------------------------|------|------|
| Transmission | 51% | 49% |
| Distribution | 48% | 50% |
| Other | 1% | 1% |

As at December 31, 2020 and 2019, Hydro One's segments accounted for the Company's total assets as follows:

| Year ended December 31 | 2020 | 2019 |
|------------------------|------|------|
| Transmission | 58% | 56% |
| Distribution | 38% | 37% |
| Other | 4% | 7% |

Transmission Segment

Hydro One's transmission business owns, operates and maintains Hydro One's transmission system, which accounts for approximately 98% of Ontario's transmission capacity based on revenue approved by the Ontario Energy Board (OEB). As at December 31, 2020, the Company's transmission business consists of the transmission system operated by Hydro One Inc.'s subsidiaries, Hydro One Networks Inc. (Hydro One Networks) and Hydro One Sault Ste. Marie LP (HOSSM), as well as an approximately 66% interest in B2M Limited Partnership

(B2M LP), a limited partnership between Hydro One and the Saugeen Ojibway Nation (SON), and an approximately 55% interest in Niagara Reinforcement Limited Partnership (NRLP), a limited partnership between Hydro One and Six Nations of the Grand River Development Corporation and the Mississaugas of the Credit First Nation (collectively, the First Nations Partners). The Company's transmission business is rate-regulated and earns revenues mainly by charging transmission rates that are approved by the OEB.

| As at and for the year ended December 31 | 2020 | 2019 |
|---|-------------|-------------|
| Electricity transmitted ¹ (MWh) | 132,225,424 | 135,101,455 |
| Transmission lines spanning the province (circuit-kilometres) | 30,093 | 30,122 |
| Rate base (millions of dollars) | 13,185 | 12,609 |
| Capital investments (millions of dollars) | 1,157 | 1,035 |
| Assets placed in-service (millions of dollars) | 948 | 1,082 |

¹ Electricity transmitted represents total electricity transmitted in Ontario by all transmitters.

Distribution Segment

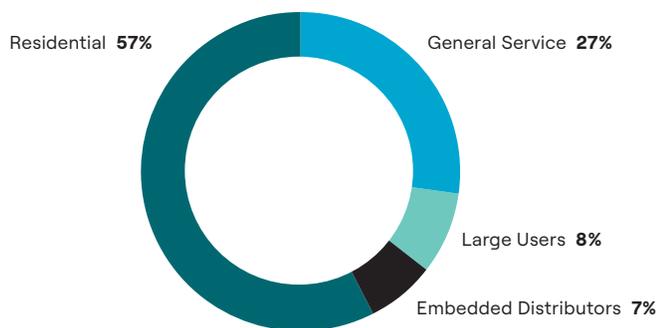
Hydro One's distribution business is the largest in Ontario and consists of the distribution system operated by Hydro One Inc.'s subsidiaries, Hydro One Networks, Hydro One Remote Communities Inc. (Hydro One Remote Communities), and Orillia Power Distribution Corporation (Orillia Power), as well as the distribution business and assets acquired

from Peterborough Distribution Inc. (Peterborough Distribution). Please see section "Other Developments" for additional information regarding the acquisition of Orillia Power and the acquisition of the business and distribution assets of Peterborough Distribution. The Company's distribution business is rate-regulated and earns revenues mainly by charging distribution rates that are approved by the OEB.

| As at and for the year ended December 31 | 2020 | 2019 |
|--|-----------|-----------|
| Electricity distributed to Hydro One customers (GWh) | 28,379 | 27,536 |
| Electricity distributed through Hydro One lines (GWh) ¹ | 39,131 | 38,446 |
| Distribution lines spanning the province (circuit-kilometres) | 124,571 | 123,422 |
| Distribution customers (number of customers) | 1,449,629 | 1,381,011 |
| Rate base (millions of dollars) | 8,505 | 8,101 |
| Capital investments (millions of dollars) | 712 | 624 |
| Assets placed in-service (millions of dollars) | 684 | 602 |

¹ Units distributed through Hydro One lines represent total distribution system requirements and include electricity distributed to consumers who purchased power directly from the Independent Electricity System Operator (IESO).

2020 Distribution Revenues



Other Segment

Hydro One's other segment consists principally of its telecommunications business, which provides telecommunications support for the Company's transmission and distribution businesses, as well as certain corporate activities.

The telecommunication business is carried out by Hydro One's wholly-owned subsidiary Hydro One Telecom Inc. (Hydro One Telecom). In addition to supporting Hydro One's regulated business segments, Hydro One Telecom offers comprehensive communications and information technology (IT) services and solutions (for example, cloud services, managed services and security-based services) that extend beyond its fibre optic network, in a competitive commercial market. Hydro One Telecom is not regulated by the OEB, however Hydro One Telecom is registered with the Canadian Radio-television and Telecommunications Commission as a non-dominant, facilities-based carrier, providing broadband telecommunications services in Ontario with connections to Montreal, Quebec; Buffalo, New York; and Detroit, Michigan.

Hydro One's other segment also includes the deferred tax asset which arose from the revaluation of the tax bases of Hydro One's assets to fair market value when the Company transitioned from the provincial payments in lieu of tax regime to the federal tax regime at the time of the Company's initial public offering in 2015.

Primary Factors Affecting Results of Operations

Transmission Revenues

Transmission revenues primarily consist of regulated transmission rates approved by the OEB which are charged based on the monthly peak electricity demand across Hydro One's high-voltage network. Transmission rates are designed to generate revenues necessary to construct, upgrade, extend and support a transmission system with sufficient capacity to accommodate maximum forecasted demand and a regulated return on the Company's investment. Peak electricity demand is primarily influenced by weather and economic conditions. Transmission revenues also include export revenues associated with transmitting electricity to markets outside of Ontario. Ancillary revenues include revenues associated with providing maintenance services to power generators and from third-party land use.

Distribution Revenues

Distribution revenues primarily consist of regulated distribution rates approved by the OEB, as well as the recovery of purchased power costs. Distribution rates are designed to generate revenues necessary to construct and support the local distribution system with sufficient capacity to accommodate existing and new customer demand and a regulated return on the Company's investment. Accordingly, distribution revenues are influenced by distribution rates, the cost of purchased power, and the amount of electricity the Company distributes. Distribution revenues also include ancillary distribution service revenues, such as fees related to the joint use of Hydro One's distribution poles by the telecommunications and cable television industries, as well as miscellaneous revenues such as charges for late payments.

Purchased Power Costs

Purchased power costs are incurred by the distribution business and represent the cost of the electricity purchased by the Company for delivery to customers within Hydro One's distribution service territory. These costs are comprised of: (i) the wholesale commodity cost of energy; (ii) the Global Adjustment, which is the difference between the guaranteed price and the money the generators earn in the wholesale marketplace; and (iii) the wholesale market service and transmission charges levied by the IESO. Hydro One passes on the cost of electricity that it delivers to its customers, and is therefore not exposed to wholesale electricity commodity price risk.

Operation, Maintenance and Administration Costs

OM&A costs are incurred to support the operation and maintenance of the transmission and distribution systems, and include other costs such as property taxes related to transmission and distribution stations and buildings, and the operation of IT systems. Transmission OM&A costs are required to sustain the Company's high-voltage transmission stations, lines, and rights-of-way, and include preventive and corrective maintenance costs related to power equipment, overhead transmission lines, transmission station sites, and forestry control to maintain safe distances between line spans and trees. Distribution OM&A costs are required to maintain the Company's low-voltage distribution system to provide safe and reliable electricity to the Company's residential, small business, commercial, and industrial customers across the province. These include costs related to distribution line clearing and forestry control to reduce power outages caused by trees, line maintenance and repair, land assessment and remediation, as well as issuing timely and accurate bills and responding to customer inquiries.

Hydro One manages its costs through ongoing efficiency and productivity initiatives, while continuing to complete planned work programs associated with the development and maintenance of its transmission and distribution networks.

Depreciation, Amortization and Asset Removal Costs

Depreciation and amortization costs relate primarily to depreciation of the Company's property, plant and equipment, and amortization of certain intangible assets and regulatory assets. Asset removal costs consist of costs incurred to remove property, plant and equipment where no asset retirement obligations have been recorded on the balance sheet.

Financing Charges

Financing charges relate to the Company's financing activities, and include interest expense on the Company's long-term debt and short-term borrowings, as well as gains and losses on interest rate swap agreements, foreign exchange or other similar contracts, net of interest earned on short-term investments. A portion of financing charges incurred by the Company is capitalized to the cost of property, plant and equipment associated with the periods during which such assets are under construction before being placed in-service.

Results of Operations

Net Income

Net income attributable to common shareholders for the year ended December 31, 2020 of \$1,770 million is an increase of \$992 million, or 127.5%, from the prior year. Significant influences on net income included:

- higher revenues, net of purchased power, primarily resulting from:
 - an increase in transmission revenues primarily due to the OEB's decision on 2020 rates; partially offset by
 - a decrease in distribution revenues, net of purchased power, mainly due to 2018 foregone revenue recognized in March 2019 following the receipt of the OEB decision on rates; partially offset by the OEB's decision on 2020 rates and revenues related to the Peterborough Distribution and Orillia Power acquisitions which closed during the third quarter of 2020.
- lower OM&A costs primarily resulting from:
 - the payment of the termination fee in 2019 related to the terminated acquisition of Avista Corporation (Merger);
 - lower vegetation management and work program expenditures, and the 2019 write-off of the Lake Superior Link project; partially offset by
 - costs related to COVID-19, as discussed below;
 - additional other post-employment benefit (OPEB) costs that are recognized in OM&A following the 2020-2022 OEB transmission decision and recovered in rates, therefore net income neutral; and

- lower insurance proceeds received in 2020.
- lower financing charges primarily resulting from financing costs related to the Merger incurred in the first quarter of 2019; partially offset by an increase in interest expense on long-term debt due to increased debt levels in 2020.
- higher income tax recovery primarily attributable to:
 - income tax recovery recorded following the July 2020 decision of the Ontario Divisional Court (ODC Decision); partially offset by
 - 2019 income tax recovery following the payment of the termination fee and financing charges related to the Merger; and
 - lower incremental tax deductions and deductible temporary differences.

Included in the Company's results for the year ended December 31, 2020 are costs incurred as a result of the COVID-19 pandemic. Total COVID-19 related costs of \$50 million consist primarily of labour costs associated with the temporary stand-down of the Company's workforce in the first half of the year, the recognition of the bad debt provision following the issuance of the OEB staff proposal in December 2020, and other direct expenses, including purchases of additional facility-related cleaning supplies.

For additional disclosure related to the impact of COVID-19 on the Company's operations for the year ended December 31, 2020, please see section "Other Developments – COVID-19".

EPS and Adjusted EPS

EPS was \$2.96 for the year ended December 31, 2020, compared to EPS of \$1.30 in 2019. The increase in EPS was driven by higher earnings for the year ended December 31, 2020, as discussed above. Adjusted EPS, which excludes the impacts of the income tax recovery related to the ODC Decision received in 2020, and for income and costs related to the Merger in 2019, was \$1.51 for the year ended December 31, 2020, compared to \$1.54 in 2019. The decrease in Adjusted EPS was driven by changes in net income for the year ended December 31, 2020, as discussed above, but excluding the impacts of the Merger and the ODC Decision. See section "Non-GAAP Measures" for description and reconciliation of Adjusted EPS.

Revenues

| Year ended December 31 (millions of dollars, except as otherwise noted) | 2020 | 2019 | Change |
|---|--------------|--------------|--------------|
| Transmission | 1,740 | 1,652 | 5.3% |
| Distribution | 5,507 | 4,788 | 15.0% |
| Other | 43 | 40 | 7.5% |
| Total revenues | 7,290 | 6,480 | 12.5% |
| Transmission | 1,740 | 1,652 | 5.3% |
| Distribution, net of purchased power ¹ | 1,653 | 1,677 | (1.4%) |
| Other | 43 | 40 | 7.5% |
| Total revenues, net of purchased power¹ | 3,436 | 3,369 | 2.0% |
| Transmission: Average monthly Ontario 60-minute peak demand (MW) | 20,091 | 19,896 | 1.0% |
| Distribution: Electricity distributed to Hydro One customers (GWh) | 28,379 | 27,536 | 3.1% |

¹ See section "Non-GAAP Measures" for description and reconciliation of distribution revenues, net of purchased power, and revenues, net of purchased power.

Management's Discussion and Analysis

Transmission Revenues

Transmission revenues increased by 5.3% during the year ended December 31, 2020, primarily due to the following:

- the OEB's decision on 2020 rates, including:
 - the recovery of certain OPEB costs through OM&A that were previously capitalized and recovered in rates, therefore net income neutral, and
 - the recognition of Conservation and Demand Management (CDM) revenues in the second quarter of 2020; partially offset by deferred regulatory adjustment related to transmission asset removal costs in 2020,
- full year contribution of the NRLP assets placed in-service in the third quarter of 2019.

OM&A Costs

Year ended December 31 (millions of dollars)

| | 2020 | 2019 | Change |
|--------------|-------|-------|---------|
| Transmission | 391 | 355 | 10.1% |
| Distribution | 619 | 610 | 1.5% |
| Other | 60 | 216 | (72.2%) |
| | 1,070 | 1,181 | (9.4%) |

Transmission OM&A Costs

The 10.1% increase in transmission OM&A costs for the year ended December 31, 2020 was primarily due to the following:

- additional OPEB costs that are recognized in OM&A following the 2020-2022 OEB transmission decision and recovered in rates, therefore net income neutral;
- costs related to COVID-19, primarily consisting of labour costs associated with the temporary stand-down of the Company's workforce in the first half of the year, and other direct expenses; and
- lower insurance proceeds received in 2020; partially offset by
- lower work program expenditures related to stations and lines maintenance.

Distribution OM&A Costs

The 1.5% increase in distribution OM&A costs for the year ended December 31, 2020 was primarily due to the following:

- costs related to COVID-19, primarily consisting of labour costs associated with the temporary stand-down of the Company's workforce in the first half of the year, the recognition of the bad debt provision following the issuance of the OEB staff proposal in December 2020, and other direct expenses, including purchases of additional facility-related cleaning supplies; and
- costs related Peterborough Distribution and Orillia Power acquisitions which closed during the third quarter of 2020; partially offset by
- lower vegetation management expenditures; and
- lower spend on IT projects.

Other OM&A Costs

The decrease in other OM&A costs for the year ended December 31, 2020 was primarily due to the payment of the Merger termination fee and the write-off of the Lake Superior Link project in the prior year.

Distribution Revenues, Net of Purchased Power

Distribution revenues, net of purchased power, decreased by 1.4% during the year ended December 31, 2020 primarily due to the following:

- the 2018 foregone revenue recognized in prior year following the 2019 OEB decision on rates; and
- the suspension of late payment charges following the onset of COVID-19; partially offset by
- the OEB's decision on 2020 rates;
- distribution revenues related to the Peterborough Distribution and Orillia Power acquisitions which closed during the third quarter of 2020; and
- a lower deferred regulatory adjustment related to the Earnings Sharing Mechanism in 2020.

Depreciation, Amortization and Asset Removal Costs

The increase of \$6 million or 0.7% in depreciation, amortization and asset removal costs in 2020 was mainly due to the growth in capital assets as the Company continues to place new assets in-service, consistent with its ongoing capital investment program.

Financing Charges

The \$43 million, or 8.4%, decrease in financing charges for the year ended December 31, 2020 was primarily due to the following:

- financing costs related to the Merger incurred in the first quarter of 2019; and
- lower interest expense on short-term notes due to lower interest rate in the current year; partially offset by
- higher interest expense on long-term debt as a result of increased debt levels driven by the debt issuances completed in 2020.

Income Tax Expense

Income taxes are accounted for using the asset and liability method. Current taxes are recorded based on the taxes expected to be paid in respect of the current and prior years' taxable income. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to temporary differences between the financial statement carrying amounts and the respective tax basis of assets and liabilities including carryforward unused tax losses and credits.

As prescribed by the regulators, the Company recovers income taxes in revenues from ratepayers based on estimate of current tax expense in respect of regulated operations. The amounts of deferred income taxes related to regulated operations, which are considered to be more likely-than-not of recovery from, or refund to, ratepayers in future periods are recognized as deferred income tax regulatory assets or liabilities, with an offset to deferred tax expense. Therefore the consolidated tax expense or recovery for the current period is based on the total current

Management's Discussion and Analysis

and deferred tax expense or recovery, net of the regulatory accounting offset to deferred tax expense arising from temporary differences recoverable from or refundable to customers in the future.

Income tax recovery was \$785 million for the year ended December 31, 2020 compared to \$6 million in 2019. The \$779 million increase in income tax recovery for the year ended December 31, 2020 was principally attributable to the recognition of \$867 million income tax recovery arising from the ODC Decision and the recognition of \$51 million income tax recovery in 2019 related to the Merger termination fee and related financing charges. When adjusted for these non-recurring recoveries, the adjusted tax expense for the year ended December 31, 2020 was of \$82 million compared to \$45 million in the

same period last year. The \$37 million increase in the tax expense is primarily attributable to the following:

- lower incremental tax deductions from deferred tax asset sharing due to the 2018 foregone revenue recognized in 2019 following the receipt of the OEB decision on rates; and
- lower deductible temporary differences.

The Company realized an effective tax rate (ETR) of approximately (77.6%) in 2020, compared to approximately (0.8%) in 2019. Excluding the impact of the income tax recovery related to the ODC Decision received in 2020, and the impacts of costs related to the Merger in 2019, the adjusted ETR of 8.1% for the year ended December 31, 2020, compares to 4.6% in 2019.

See section "Non-GAAP Measures" for description and reconciliation of adjusted tax expense and adjusted ETR.

Common Share Dividends

In 2020, the Company declared and paid cash dividends to common shareholders as follows:

| Date Declared | Record Date | Payment Date | Amount per Share | Total Amount (millions of dollars) |
|-------------------|-------------------|--------------------|------------------|------------------------------------|
| February 11, 2020 | March 11, 2020 | March 31, 2020 | \$ 0.2415 | 144 |
| May 7, 2020 | June 10, 2020 | June 30, 2020 | \$ 0.2536 | 152 |
| August 10, 2020 | September 9, 2020 | September 30, 2020 | \$ 0.2536 | 151 |
| November 5, 2020 | December 9, 2020 | December 31, 2020 | \$ 0.2536 | 152 |
| | | | | 599 |

Following the conclusion of the fourth quarter of 2020, the Company declared a cash dividend to common shareholders as follows:

| Date Declared | Record Date | Payment Date | Amount per Share | Total Amount (millions of dollars) |
|-------------------|----------------|----------------|------------------|------------------------------------|
| February 23, 2021 | March 17, 2021 | March 31, 2021 | \$ 0.2536 | 152 |

Selected Annual Financial Statistics

| Year ended December 31 (millions of dollars, except per share amounts) | 2020 | 2019 | 2018 |
|--|----------------|---------|-----------|
| Revenues | 7,290 | 6,480 | 6,150 |
| Net income (loss) to common shareholders of Hydro One | 1,770 | 778 | (89) |
| Basic EPS | \$ 2.96 | \$ 1.30 | \$ (0.15) |
| Diluted EPS | \$ 2.95 | \$ 1.30 | \$ (0.15) |
| Basic Adjusted EPS ¹ | \$ 1.51 | \$ 1.54 | \$ 1.35 |
| Diluted Adjusted EPS ¹ | \$ 1.51 | \$ 1.53 | \$ 1.35 |
| Dividends per common share declared | \$ 1.00 | \$ 0.96 | \$ 0.91 |
| Dividends per preferred share declared ² | \$ 1.20 | \$ 1.06 | \$ 1.06 |
| As at December 31 (millions of dollars) | 2020 | 2019 | 2018 |
| Total assets | 30,294 | 27,061 | 25,657 |
| Total non-current financial liabilities ³ | 12,813 | 10,897 | 10,479 |

¹ See section "Non-GAAP Measures" for description and reconciliation of basic and diluted Adjusted EPS.

² Preferred dividends per share are calculated using the weighted average number of preferred shares outstanding during each year. The preferred share dividends paid in each year presented were \$18 million. All the preferred shares were redeemed on November 20, 2020. See section "Share Capital" for details.

³ Total non-current financial liabilities includes long-term debt, long-term lease obligations, derivative liabilities, long-term accounts payable, and convertible debentures.

Management's Discussion and Analysis

Net Income (Loss) – 2019 compared to 2018

Net income attributable to common shareholders for the year ended December 31, 2019 of \$778 million is an increase of \$867 million or 974.2% from the year prior. Significant influences on earnings included:

- higher revenues, net of purchased power, primarily resulting from:
 - an increase in distribution revenues, net of purchased power, due to the OEB's decision on the 2018 and 2019 distribution rates; partially offset by
 - lower average monthly Ontario 60-minute peak demand and energy consumption driven by less favourable weather in 2019; and
 - lower revenues as a result of deferred tax asset sharing mandated by the OEB and deferred tax regulatory adjustment related to accelerated tax depreciation (Accelerated CCA), both of which will flow through to customers and are offset with lower taxes, with no impact on regulated return on equity (ROE);
- higher OM&A costs primarily resulting from the payment of the termination fee related to the Merger and higher vegetation management coverage; partially offset by lower corporate support costs, insurance proceeds received in 2019, and lower spend on station and lines maintenance programs;

- higher financing charges primarily resulting from an increase in interest expense on long-term debt; and increased Merger-related financing charges; and
- lower income tax expense as a result of the prior year charge to deferred tax expense related to the impairment of Hydro One's deferred income tax regulatory asset, as well as the deferred tax asset sharing and Accelerated CCA, both of which will flow through to customers and are offset with lower revenues, with no impact on regulated ROE.

EPS and Adjusted EPS – 2019 compared to 2018

EPS was \$1.30 in 2019, compared to a loss per share of \$0.15 in 2018.

The increase in EPS was driven by higher earnings in 2019, as discussed above. Adjusted EPS in 2019, which excludes the impacts of the Merger, was \$1.54, compared to adjusted EPS of \$1.35 in 2018, which excludes the impacts of the OEB's March 2019 reconsideration decision (DTA Decision) relating to Hydro One's treatment of benefits of the deferred tax assets resulting from Hydro One's transition from the provincial payments in lieu of tax regime to the federal tax regime in 2015.

The increase in adjusted EPS was driven by the net income impacts discussed above, but excluding the impacts of the Merger and the DTA Decision.

Quarterly Results of Operations

| Quarter ended (millions of dollars, except EPS and ratio) | Dec 31, 2020 | Sep 30, 2020 | Jun 30, 2020 | Mar 31, 2020 | Dec 31, 2019 | Sep 30, 2019 | Jun 30, 2019 | Mar 31, 2019 |
|--|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|
| Revenues | 1,867 | 1,903 | 1,670 | 1,850 | 1,715 | 1,593 | 1,413 | 1,759 |
| Purchased power | 1,046 | 993 | 808 | 1,007 | 914 | 737 | 653 | 807 |
| Revenues, net of purchased power ¹ | 821 | 910 | 862 | 843 | 801 | 856 | 760 | 952 |
| Net income to common shareholders | 161 | 281 | 1,103 | 225 | 211 | 241 | 155 | 171 |
| Adjusted net income to common shareholders ¹ | 161 | 281 | 236 | 225 | 211 | 241 | 155 | 311 |
| Basic EPS | \$ 0.27 | \$ 0.47 | \$ 1.84 | \$ 0.38 | \$ 0.35 | \$ 0.40 | \$ 0.26 | \$ 0.29 |
| Diluted EPS | \$ 0.27 | \$ 0.47 | \$ 1.84 | \$ 0.38 | \$ 0.35 | \$ 0.40 | \$ 0.26 | \$ 0.29 |
| Basic Adjusted EPS ¹ | \$ 0.27 | \$ 0.47 | \$ 0.39 | \$ 0.38 | \$ 0.35 | \$ 0.40 | \$ 0.26 | \$ 0.52 |
| Diluted Adjusted EPS ¹ | \$ 0.27 | \$ 0.47 | \$ 0.39 | \$ 0.38 | \$ 0.35 | \$ 0.40 | \$ 0.26 | \$ 0.52 |
| Earnings coverage ratio ² | 2.8 | 2.9 | n/a | n/a | n/a | n/a | n/a | n/a |

¹ See section "Non-GAAP Measures" for description of revenues, net of purchased power, adjusted net income and Adjusted EPS.

² Earnings coverage ratio is a non-GAAP measure that has been presented for the twelve months ended December 31, 2020 and September 30, 2020, and has been calculated as net income before financing charges and income taxes attributable to shareholders of Hydro One, divided by the sum of financing charges and capitalized interest.

Variations in revenues and net income over the quarters are primarily due to the impact of seasonal weather conditions on customer demand and market pricing, as well as timing of regulatory decisions.

Capital Investments

The Company makes capital investments to maintain the safety, reliability and integrity of its transmission and distribution system assets and to provide for the ongoing growth and modernization required to meet the expanding and evolving needs of its customers and the electricity market. This is achieved through a combination of sustaining capital investments, which are required to support the continued operation of Hydro One's existing assets, and development capital investments, which involve both additions to existing assets and large-scale projects such as new transmission lines and transmission stations.

Assets Placed In-Service

The following table presents Hydro One's assets placed in-service during the years ended December 31, 2020 and 2019:

| Year ended December 31 (millions of dollars) | 2020 | 2019 | Change |
|--|--------------|--------------|---------------|
| Transmission | 948 | 1,082 | (12.4%) |
| Distribution | 684 | 602 | 13.6% |
| Other | 7 | 19 | (63.2%) |
| Total assets placed in-service | 1,639 | 1,703 | (3.8%) |

Transmission Assets Placed In-Service

Transmission assets placed in-service decreased by \$134 million or 12.4% during the year ended December 31, 2020 compared to the year ended December 31, 2019 primarily due to the following:

- the in-servicing of several projects in 2019, including the Niagara Reinforcement Project, the Brant transmission station, the new Leamington transmission, and Enfield transmission station;
- lower volume of overhead lines and component replacements in 2020;
- lower volume of assets placed in-service for IT projects in 2020; and
- lower volume of demand work due to equipment failures in 2020; partially offset by
- timing of assets placed in-service for station sustainment investments (including Lennox transmission station, Sheppard transmission station, Elgin transmission station, Runnymede transmission station, Cherrywood transmission station placed in-service in 2020, and Bronte transmission station, Alexander switching station, Hanmer transmission station, Palmerston

transmission station, National Research Council transmission station placed in-service in 2019); and

- assets placed in-service in 2020 (High-Voltage Underground Cable replacement in Toronto, and Kapuskasing area Reinforcement project line upgrade).

Distribution Assets Placed In-Service

Distribution assets placed in-service increased by \$82 million or 13.6% during the year ended December 31, 2020 compared to the year ended December 31, 2019 primarily due to the following:

- completion of Customer Contact Centre Technology Modernization project;
- substantial completion of the Leamington transmission station feeder development project in 2020;
- higher volume of storm related asset replacements; and
- completion of Woodstock Operation Centre; partially offset by
- lower volume of distribution station refurbishment work and equipment replacements.

Capital Investments

The following table presents Hydro One's capital investments during the years ended December 31, 2020 and 2019:

| Year ended December 31 (millions of dollars) | 2020 | 2019 | Change |
|--|--------------|--------------|--------------|
| Transmission | | | |
| Sustaining | 819 | 811 | 1.0% |
| Development | 226 | 143 | 58.0% |
| Other | 112 | 81 | 38.3% |
| | 1,157 | 1,035 | 11.8% |
| Distribution | | | |
| Sustaining | 317 | 272 | 16.5% |
| Development | 289 | 265 | 9.1% |
| Other | 106 | 87 | 21.8% |
| | 712 | 624 | 14.1% |
| Other | 9 | 8 | 12.5% |
| Total capital investments | 1,878 | 1,667 | 12.7% |

Total 2020 capital investments of \$1,878 million were largely in-line with the previously disclosed expected amount of \$1,841 million.

Management's Discussion and Analysis

Transmission Capital Investments

Transmission capital investments increased by \$122 million or 11.8% during the year ended December 31, 2020 compared to the year ended December 31, 2019. Principal impacts on the levels of capital investments included:

- higher investments in multi-year development projects, including the new shunt reactors at the Lennox transmission station, the East-West Tie Connection, the new Lakeshore switching station, and the Kapuskasing area reinforcement project;
- higher volume of station refurbishments and replacements;
- investment in the new Ontario grid control centre in the City of Orillia; and
- higher volume of work required to adhere to the North American Electric Reliability Corporation (NERC) Critical Infrastructure Protection standards; partially offset by
- lower volume of overhead line refurbishments and replacements, customer connections, and transportation and work equipment investments.

Distribution Capital Investments

Distribution capital investments increased by \$88 million or 14.1% during the year ended December 31, 2020 compared to the year ended December 31, 2019. Principal impacts on the levels of capital investments included:

- investment in the new Ontario grid control centre in the City of Orillia;
- higher volume of storm related asset replacements and emergency power restoration work;
- investment in the new Woodstock Operation Centre;
- higher investments in IT projects including the Customer Contact Centre Technology Modernization project; and
- higher volume of line refurbishments work; partially offset by
- lower volume of transportation and work equipment investments.

Major Transmission Capital Investment Projects

The following table summarizes the status of significant transmission projects as at December 31, 2020:

| Project Name | Location | Type | Anticipated In-Service Date | Estimated Cost | Capital Cost To Date |
|---|--|---|-----------------------------|-----------------------|----------------------|
| | | | (year) | (millions of dollars) | |
| Development Projects: | | | | | |
| Wataynikaneyap Power LP Line Connection | Pickle Lake Northwestern Ontario | New stations and transmission connection | 2021 | 28 | 6 |
| East-West Tie Station Expansion | Northern Ontario | New transmission connection and station expansion | 2022 ¹ | 160 | 129 |
| Waasigan Transmission Line | Thunder Bay-Atikokan-Dryden Northwestern Ontario | New transmission line | 2024 ² | 68 ² | 6 |
| Leamington Area Transmission Reinforcement ³ | Leamington Southwestern Ontario | New transmission line and stations | 2026 ³ | 525 ³ | 54 |
| Sustainment Projects: | | | | | |
| Richview Transmission Station Circuit Breaker Replacement | Toronto Southwestern Ontario | Station sustainment | 2021 | 118 | 115 |
| Bruce A Transmission Station | Tiverton Southwestern Ontario | Station sustainment | 2021 | 146 | 144 |
| Beck #2 Transmission Station Circuit Breaker Replacement | Niagara area Southwestern Ontario | Station sustainment | 2023 | 136 | 89 |
| Bruce B Switching Station Circuit Breaker Replacement | Tiverton Southwestern Ontario | Station sustainment | 2024 | 146 | 50 |
| Lennox Transmission Station Circuit Breaker Replacement | Napanee Southeastern Ontario | Station sustainment | 2026 | 152 | 91 |
| Middleport Transmission Station Circuit Breaker Replacement | Middleport Southwestern Ontario | Station sustainment | 2025 | 123 | 71 |

¹ The East-West Tie Station Expansion project is impacted by the construction schedule of the new East-West Tie transmission line being built by Upper Canada Transmission Inc., operating as NextBridge Infrastructure, LP (NextBridge). In September 2020, NextBridge advised the OEB of a delay in the in-service date of the East-West Tie transmission line to March 31, 2022. As a result of this delay, the majority of the East-West Tie Station Expansion project, enabling the connection and energization of the new East-West Tie transmission line, is now expected to be placed in-service in 2022.

² The estimated cost of the Waasigan Transmission Line relates to the development phase of the project and the anticipated in-service date reflects the anticipated completion date of the development phase.

³ The Leamington Area Transmission Reinforcement project consists of the construction of a new double-circuit line between Chatham and Leamington and associated transmission stations and connections. The project is currently in the development stage and as such the estimated cost is subject to change. The anticipated in-service dates for the line and stations are between 2022 and 2026.

Future Capital Investments

The Company estimates future capital investments based on management's expectations of the amount of capital expenditures that will be required to provide transmission and distribution services that are efficient, reliable, and provide value for customers, consistent with the OEB's Renewed Regulatory Framework.

The 2021 through 2022 transmission capital investment estimates differ from the prior year disclosures, reflecting the OEB's decision on Hydro One Networks' 2021-2022 rate application. See section "Regulation"

for further details on the OEB's decision. The 2021 through 2024 distribution capital investments estimates have also been updated to include capital investments for the Peterborough Distribution and Orillia Power acquisitions in the third quarter of 2020. See section "Other Developments" for information related to the acquisitions. The 2021 through 2022 distribution capital investments estimates reflect reprioritization of work and revised pacing of investments. The projections and the timing of the transmission and distribution expenditures in 2023 and 2024 are subject to approval by the OEB.

The following table summarizes Hydro One's annual projected capital investments for 2021 to 2024, by business segment:

| (millions of dollars) | 2021 | 2022 | 2023 | 2024 |
|--|--------------|--------------|--------------|--------------|
| Transmission | 1,172 | 1,204 | 1,386 | 1,380 |
| Distribution | 713 | 648 | 742 | 759 |
| Other | 23 | 18 | 14 | 11 |
| Total capital investments¹ | 1,908 | 1,870 | 2,142 | 2,150 |

1 Total capital investments for 2021 include \$85 million related to a new Ontario grid control centre with an anticipated in-service date of 2021.

The following table summarizes Hydro One's annual projected capital investments for 2021 to 2024, by category:

| (millions of dollars) | 2021 | 2022 | 2023 | 2024 |
|--|--------------|--------------|--------------|--------------|
| Sustainment | 1,125 | 1,296 | 1,555 | 1,558 |
| Development | 544 | 405 | 439 | 459 |
| Other ¹ | 239 | 169 | 148 | 133 |
| Total capital investments² | 1,908 | 1,870 | 2,142 | 2,150 |

1 "Other" capital expenditures include investment in fleet, real estate, IT, and operations technology and related functions.

2 Total capital investments for 2021 include \$85 million related to a new Ontario grid control centre with an anticipated in-service date of 2021.

Summary of Sources and Uses of Cash

Hydro One's primary sources of cash flows are funds generated from operations, capital market debt issuances and bank credit facilities that are used to satisfy Hydro One's capital resource requirements, including the Company's capital expenditures, servicing and repayment of debt, and dividend payments.

| Year ended December 31 (millions of dollars) | 2020 | 2019 |
|---|----------------|---------|
| Cash provided by operating activities | 2,030 | 1,614 |
| Cash provided by (used in) financing activities | 674 | (439) |
| Cash used in investing activities | (1,977) | (1,628) |
| Increase (decrease) in cash and cash equivalents | 727 | (453) |

Management's Discussion and Analysis

Cash provided by operating activities

Cash from operating activities increased by \$416 million for the year ended December 31, 2020 compared to 2019. The increase was impacted by various factors, including the following:

- higher earnings in 2020;
- changes in certain regulatory accounts; and
- increases in net working capital attributable to higher payments received from the IESO during 2020 associated with Fair Hydro Plan credits, as well as lower non-energy receivables.

Cash provided by (used in) financing activities

Cash provided by financing activities increased by \$1,113 million for the year ended December 31, 2020 compared to 2019. The increase was impacted by various factors, including the following:

Sources of cash

- The Company issued \$2,725 million of long-term debt in 2020, compared to \$1,500 million long-term debt issued in 2019.
- The Company received proceeds of \$4,070 million from the issuance of short-term notes in 2020, compared to \$4,217 million received in 2019.

Uses of cash

- The Company repaid \$4,413 million of short-term notes in 2020, compared to \$4,326 million repaid in 2019.
- The Company repaid \$653 million of long-term debt in 2020, compared to \$730 million of long-term debt in 2019.
- In 2019, the Company redeemed \$513 million of convertible debentures.
- Dividends paid in 2020 were \$617 million, consisting of \$599 million of common share dividends and \$18 million of preferred share dividends, compared to dividends of \$588 million paid in 2019, consisting of \$570 million of common share dividends and \$18 million of preferred share dividends.
- The Company redeemed preferred shares of \$418 million in 2020, compared to no preferred shares redeemed in 2019. See section "Share Capital" for details of the preferred shares redemption.

Cash used in investing activities

Cash used in investing activities increased by \$349 million for the year ended December 31, 2020 compared to 2019. The increase is primarily attributable to a \$216 million increase in capital expenditures in 2020, as well as the acquisitions of Orillia Power and the assets of Peterborough Distribution in the current year (\$126 million). Please see section "Capital Investments" for comparability of capital investments made by the Company during the year ended December 31, 2020 compared to prior year.

Liquidity and Financing Strategy

Short-term liquidity is provided through FFO, Hydro One Inc.'s commercial paper program, and the Company's consolidated bank credit facilities. Under the commercial paper program, Hydro One Inc. is authorized to issue up to \$2,300 million in short-term notes with a term to maturity of up to 365 days.

At December 31, 2020, Hydro One Inc. had \$800 million in commercial paper borrowings outstanding, compared to \$1,143 million outstanding at December 31, 2019. In addition, the Company has revolving bank credit facilities (Operating Credit Facilities) with a total availability balance of \$2,550 million as at December 31, 2020. No amounts were drawn on the Operating Credit Facilities as at December 31, 2020 or 2019. The Company may use the Operating Credit Facilities for working capital and general corporate purposes. The short-term liquidity under the commercial paper program, the Operating Credit Facilities, available cash on hand and anticipated levels of FFO are expected to be sufficient to fund the Company's operating requirements. The Company's currently available liquidity is also expected to be sufficient to address any reasonably foreseeable impacts that the COVID-19 pandemic may have on the Company's cash requirements. See section "Other Developments – COVID-19" for additional information of the impact of COVID-19 on the Company's operations.

At December 31, 2020, the Company had long-term debt outstanding in the principal amount of \$13,558 million, which included \$425 million of long-term debt issued by Hydro One, \$12,995 million of long-term debt issued by Hydro One Inc., and long-term debt in the principal amount of \$138 million issued by HOSSM. The long-term debt issued by Hydro One was issued under its base shelf prospectus (Universal Base Shelf Prospectus), as further described below. The majority of long-term debt issued by Hydro One Inc. has been issued under its Medium Term Note (MTN) Program, as further described below. The long-term debt consists of notes and debentures that mature between 2021 and 2064, and as at December 31, 2020, had a weighted-average term to maturity of approximately 14.5 years (2019 – 15.7 years) and a weighted-average coupon rate of 3.8% (2019 – 4.2%).

On August 20, 2020, Hydro One filed a short form Universal Base Shelf Prospectus with securities regulatory authorities in Canada to replace a previous prospectus that expired in July 2020. The Universal Base Shelf Prospectus allows Hydro One to offer, from time to time in one or more public offerings, up to \$2,000 million of debt, equity or other securities, or any combination thereof, during the 25-month period ending in September 2022. On October 15, 2020, Hydro One issued \$425 million of long-term debt resulting in \$1,575 million remaining available for issuance under the Universal Base Shelf Prospectus at December 31, 2020. The Company used the net proceeds of this offering to fund the redemption on November 20, 2020 of all of its Series 1 preferred shares (Preferred Shares) and for general corporate purposes. See section "Share Capital" for further details of the Preferred Shares redemption.

On September 21, 2020, in order to secure required funding for the redemption of the Preferred Shares, Hydro One secured binding commitments for three bilateral two-year senior unsecured term credit facilities (Bilateral Credit Facilities) totalling \$201 million. On October 15, 2020, these bilateral commitments were terminated upon receipt of the proceeds of Hydro One's \$425 million long-term debt offering.

In April 2020, Hydro One Inc. filed a short form base shelf prospectus for its MTN Program, which has a maximum authorized principal amount of notes issuable of \$4,000 million, expiring in May 2022. At December 31, 2020, \$2,800 million remained available for issuance under the MTN Program prospectus.

On December 17, 2020, Hydro One Holdings Limited (HOHL), an indirect wholly-owned subsidiary of Hydro One, filed a short form base shelf prospectus (US Debt Shelf Prospectus) with securities regulatory authorities in Canada and the US, to replace a previous prospectus that expired in December 2020. The US Debt Shelf Prospectus allows HOHL to offer, from time to time in one or more public offerings, up to US\$3,000 million of debt securities, unconditionally guaranteed by Hydro One, during the 25-month period ending in January 2023. At December 31, 2020, no securities have been issued under the US Debt Shelf Prospectus.

Compliance

At December 31, 2020, the Company was in compliance with all financial covenants and limitations associated with the outstanding borrowings and credit facilities.

Credit Ratings

Various ratings organizations review the Company's and Hydro One Inc.'s debt ratings from time to time. These ratings organizations may take various actions, positive or negative. The Company cannot predict what actions rating agencies may take in the future. The failure to maintain the Company's current credit ratings could adversely affect the Company's financial condition and results of operations, and a downgrade in the Company's credit ratings could restrict the Company's ability to access debt capital markets and increase the Company's cost of debt.

On September 21, 2020, DBRS Limited (DBRS) assigned an issuer rating of "A" to the Company. DBRS also assigned a provisional rating of "A" to the Company's then proposed \$425 million long-term debt issuance. Both trends are Stable. On September 22, 2020, S&P Global Ratings (S&P) assigned an issue-level rating of "BBB+" to the Company's \$425 million long-term debt issuance.

At December 31, 2020, Hydro One's long-term credit ratings were as follows:

| Rating Agency | Long-term Debt Rating |
|---------------|-----------------------|
| DBRS | A |
| S&P | BBB+ |

At December 31, 2020, Hydro One Inc.'s long-term and short-term debt ratings were as follows:

| Rating Agency | Short-term Debt Rating | Long-term Debt Rating |
|---------------|------------------------|-----------------------|
| DBRS | R-1 (low) | A (high) |
| Moody's | Prime-2 | A3 |
| S&P | A-1 (low) | A- |

Effect of Interest Rates

The Company is exposed to fluctuations of interest rates as its regulated ROE is derived using a formulaic approach that takes into account changes in benchmark interest rates for Government of Canada debt and the A-rated utility corporate bond yield spread. The Company issues debt from time to time to refinance maturing debt and for general corporate purposes. The Company is therefore exposed to fluctuations in interest rates in relation to such issuances of debt. See section "Risk Management and Risk Factors – Risks Relating to Hydro One's Business – Market, Financial Instrument and Credit Risk" for more details.

Pension Plan

In 2020, Hydro One made cash contributions of \$57 million to its pension plan, compared to cash contributions of \$61 million in 2019, and incurred \$146 million in net periodic pension benefit costs, compared to \$41 million incurred in 2019.

In September 2019, Hydro One filed a triennial actuarial valuation of its pension plan as at December 31, 2018. The next actuarial valuation will be performed no later than effective December 31, 2021. Hydro One estimates that total Company pension contributions for 2021, 2022, 2023, 2024, 2025, 2026 and 2027 are approximately \$59 million, \$93 million, \$107 million, \$111 million, \$113 million, and \$118 million, respectively. The estimated pension contributions for years beyond 2021 increased from amounts previously disclosed primarily due to a remeasurement of the Company's contributions at the end of 2020, reflecting a decrease in discount rate and an increase in the number of employees.

The Company's pension benefits obligation is impacted by various assumptions and estimates, such as discount rate, rate of return on plan assets, rate of cost of living increase and mortality assumptions. A full discussion of the significant assumptions and estimates can be found in the section "Critical Accounting Estimates – Employee Future Benefits".

Other Obligations

Off-Balance Sheet Arrangements

There are no off-balance sheet arrangements that have, or are reasonably likely to have, a material current or future effect on the Company's financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources.

Management's Discussion and Analysis

Summary of Contractual Obligations and Other Commercial Commitments

The following table presents a summary of Hydro One's debt and other major contractual obligations and commercial commitments:

| As at December 31, 2020 (millions of dollars) | Total | Less than 1 year | 1-3 years | 3-5 years | More than 5 years |
|---|---------------|---------------------|--------------|--------------|----------------------|
| Contractual obligations (due by year) | | | | | |
| Long-term debt – principal repayments | 13,558 | 803 | 1,335 | 1,450 | 9,970 |
| Long-term debt – interest payments | 8,411 | 498 | 950 | 886 | 6,077 |
| Short-term notes payable | 800 | 800 | – | – | – |
| Pension contributions ¹ | 712 | 59 | 200 | 222 | 231 |
| Environmental and asset retirement obligations | 160 | 34 | 46 | 24 | 56 |
| Outsourcing and other agreements ² | 162 | 106 | 26 | 15 | 15 |
| Lease obligations | 90 | 16 | 25 | 22 | 27 |
| Long-term software/meter agreement | 13 | 8 | 3 | 2 | – |
| Total contractual obligations | 23,906 | 2,324 | 2,585 | 2,621 | 16,376 |
| Other commercial commitments (by year of expiry) | | | | | |
| Operating Credit Facilities | 2,550 | – | – | 2,550 | – |
| Letters of credit ³ | 196 | 194 | 2 | – | – |
| Guarantees ⁴ | 491 | 491 | – | – | – |
| Total other commercial commitments | 3,237 | 685 | 2 | 2,550 | – |

1 Contributions to the Hydro One Pension Fund are generally made one month in arrears. Company and employee contributions to the pension plan are based on actuarial reports, including valuations performed at least every three years, and actual or projected levels of pensionable earnings, as applicable. The most recent actuarial valuation was performed effective December 31, 2018.

2 In February 2021, Hydro One entered into an agreement for information technology services with Capgemini Canada Inc., which expires on February 29, 2024, and includes an option to extend for two additional one-year terms at Hydro One's discretion, resulting in an additional commitment of \$143 million, which has not been reflected in the table above.

3 Letters of credit consist of \$167 million in letters of credit related to retirement compensation arrangements, a \$22 million letter of credit provided to the IESO for prudential support, \$4 million in letters of credit to satisfy debt service reserve requirements, and \$3 million in letters of credit for various operating purposes.

4 Guarantees consist of \$484 million prudential support provided to the IESO by Hydro One Inc. on behalf of its subsidiaries, and guarantees totalling \$7 million provided by Hydro One to the Minister of Natural Resources (Canada) relating to Ontario Charging Network LP (OCN LP) (OCN Guarantee). Ontario Power Generation Inc. (OPG) has provided a \$2.5 million guarantee to Hydro One related to the OCN Guarantee.

Share Capital

The common shares of Hydro One are publicly traded on the Toronto Stock Exchange (TSX) under the trading symbol "H". Hydro One is authorized to issue an unlimited number of common shares. The amount and timing of any dividends payable by Hydro One is at the discretion of the Hydro One Board of Directors (Board) 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 may consider relevant. At February 23, 2021, Hydro One had 597,611,787 issued and outstanding common shares.

The Company is authorized to issue an unlimited number of preferred shares, issuable in series. The Company has two series of preferred shares authorized for issuance: the Series 1 preferred shares and Series 2 preferred shares. At February 23, 2021, the Company had no Series 1 preferred shares and no Series 2 preferred shares issued and outstanding.

On November 20, 2020, Hydro One exercised its option to redeem all of its 16,720,000 outstanding Preferred Shares in accordance with their terms. The Preferred Shares were redeemed at a price of \$25.00 per share, plus all accrued and unpaid dividends up to, but excluding

November 20, 2020, for an aggregate redemption price of \$423 million, including \$418 million for the Preferred Shares balance and \$5 million for accrued dividends. The Preferred Shares were not exchangeable or convertible into the common shares of the Company and the redemption had no impact on the Province of Ontario's (Province) voting rights or ownership percentage of the outstanding common shares of Hydro One.

The number of additional common shares of Hydro One that would be issued if all outstanding awards under the share grant plans and the Long-term Incentive Plan (LTIP) were vested and exercised as at February 23, 2021 was 3,502,185.

Regulation

The OEB approves both the revenue requirements and the rates charged by Hydro One's regulated transmission and distribution businesses. The rates are designed to permit the Company's transmission and distribution businesses to recover the allowed costs and to earn a formula-based annual rate of return on its deemed 40% equity level invested in the regulated businesses. This is done by applying a specified equity risk premium to forecasted interest rates on long-term bonds. In addition, the OEB approves rate riders to allow for the recovery or disposition of specific regulatory deferral and variance accounts over specified time frames.

The following table summarizes the status of Hydro One's major regulatory proceedings with the OEB:

| Application | Years | Type | Status |
|---|-----------|----------------------------|------------------------------------|
| Electricity Rates | | | |
| Hydro One Networks | 2020-2022 | Transmission – Custom | OEB decision received |
| Hydro One Networks | 2018-2022 | Distribution – Custom | OEB decision received |
| B2M LP | 2020-2024 | Transmission – Revenue Cap | OEB decision received |
| HOSSM | 2017-2026 | Transmission – Revenue Cap | OEB decision received |
| NRLP | 2020-2024 | Transmission – Revenue Cap | OEB decision received |
| Peterborough Distribution | 2020-2029 | Distribution – Revenue Cap | OEB decision received ¹ |
| Orillia Power | 2020-2029 | Distribution – Revenue Cap | OEB decision received ² |
| Mergers Acquisitions Amalgamations and Divestitures (MAAD) | | | |
| Peterborough Distribution | n/a | Acquisition | OEB decision received |
| Orillia Power | n/a | Acquisition | OEB decision received |
| Leave to Construct | | | |
| Power Downtown Toronto | n/a | Section 92 | OEB decision pending ³ |

¹ Peterborough Distribution is under a 10-year deferred rebasing period for years 2020-2029, as approved in the OEB MAAD decision dated April 30, 2020.

² Orillia Power is under a 10-year deferred rebasing period for years 2020-2029, as approved in the OEB MAAD decision dated April 30, 2020.

³ On October 27, 2020, Hydro One Networks filed a Leave to Construct application with the OEB seeking approval to upgrade five circuit kilometres of transmission cable facilities in the downtown Toronto area. These facilities are required to ensure that the area continues to receive a safe and reliable supply of electricity.

The following table summarizes the key elements and status of Hydro One's electricity rate applications:

| Application | Year | Return on Equity (ROE) Allowed (A) | Rate Base Allowed (A) | Rate Application Status |
|---------------------|-----------|------------------------------------|-----------------------|--------------------------|
| Transmission | | | | |
| Hydro One Networks | 2020 | 8.52% (A) | \$12,360 million (A) | Approved in April 2020 |
| | 2021 | 8.52% (A) | \$12,927 million (A) | Approved in April 2020 |
| | 2022 | 8.52% (A) | \$13,641 million (A) | Approved in April 2020 |
| B2M LP | 2020-2024 | 8.52% (A) | \$488 million (A) | Approved in January 2020 |
| HOSSM ¹ | 2017-2026 | 9.19% (A) | \$218 million (A) | Approved in October 2016 |
| NRLP | 2020-2024 | 8.52% (A) | \$118 million (A) | Approved in April 2020 |
| Distribution | | | | |
| Hydro One Networks | 2020 | 9.00% (A) | \$8,175 million (A) | Approved in March 2019 |
| | 2021 | 9.00% (A) | \$8,514 million (A) | Approved in March 2019 |
| | 2022 | 9.00% (A) | \$8,804 million (A) | Approved in March 2019 |

¹ HOSSM is under a 10-year deferred rebasing period for years 2017-2026, as approved in the OEB MAAD decision dated October 13, 2016.

Electricity Rates Applications

Hydro One Networks – Transmission

Deferred Tax Asset

On September 28, 2017, the OEB issued its decision and order on Hydro One Networks' 2017 and 2018 transmission revenue requirements (Original Decision).

In its Original Decision, the OEB concluded that the net deferred tax asset resulting from transition from the payments in lieu of tax regime under the *Electricity Act, 1998* (Ontario) to tax payments under the federal and provincial tax regime should not accrue entirely to Hydro One shareholders and that a portion should be shared with ratepayers. On November 9, 2017, the OEB issued a decision and order that calculated the portion of the tax savings that should be shared with ratepayers. The OEB's calculation would have resulted in an impairment of a portion of both Hydro One Networks' transmission and distribution deferred income tax regulatory asset. In October 2017, the Company filed a motion to review and vary (Motion) the Original Decision and filed

an appeal with the Ontario Divisional Court (Appeal). In both cases, the Company's position was that the OEB made errors of fact and law in its determination of allocation of the tax savings between the shareholders and ratepayers. On December 19, 2017, the OEB granted a hearing of the merits of the Motion which was held on February 12, 2018. On August 31, 2018, the OEB granted the Motion and returned the portion of the Original Decision relating to the deferred tax asset to an OEB panel for reconsideration.

On March 7, 2019, the OEB issued its reconsideration decision (DTA Decision) and concluded that their Original Decision was reasonable and should be upheld. Also, on March 7, 2019, the OEB issued its decision for Hydro One Networks' 2018-2022 distribution rates, in which it directed the Company to apply the Original Decision to Hydro One Networks' distribution rates. As a result, as at December 31, 2018, the Company recorded impairment charges relating to Hydro One Networks' distribution and transmission deferred income tax regulatory asset. Notwithstanding the recognition of the effects of the DTA Decision in

Management's Discussion and Analysis

the 2018 financial statements, on April 5, 2019, the Company filed an appeal with the Ontario Divisional Court with respect to the OEB's DTA Decision. The appeal was heard on November 21, 2019.

On July 16, 2020, the Ontario Divisional Court rendered the ODC Decision on the Company's appeal of the OEB's DTA Decision. In its decision, the Ontario Divisional Court set aside the OEB's DTA Decision. The Ontario Divisional Court found that the OEB's DTA Decision was incorrect in law because the OEB had failed to apply the correct legal test. In its decision, the Ontario Divisional Court agreed with the submissions of Hydro One that the deferred tax asset should be allocated to shareholders in its entirety. However, the Ontario Divisional Court concluded that it does not have jurisdiction to substitute its own decision for that of the OEB and, with clear directions as to what the OEB's decision must be, ordered that the matter be returned to the OEB. The OEB did not file a notice for leave to appeal the ODC Decision to the Ontario Court of Appeal by the required deadline of July 31, 2020.

In connection with the ODC Decision, the Company recorded a reversal of the previously recognized impairment charge of Hydro One Networks' distribution and transmission deferred income tax regulatory asset in its financial statements for the year ended December 31, 2020. The reversal of the previously recognized impaired charge included the regulatory asset relating to the cumulative deferred tax asset amounts shared with ratepayers (deferred tax asset sharing) up to and including June 30, 2020 by Hydro One Networks' distribution and transmission segments of \$58 million and \$118 million, respectively. Hydro One recognized deferred income tax regulatory assets of \$504 million and \$673 million for Hydro One Networks distribution and transmission segments, respectively, and associated deferred income tax liability of \$310 million. The Company also recorded an increase in net income of \$867 million as deferred income tax recovery during the year ended December 31, 2020.

On September 21, 2020, the Ontario Divisional Court issued its final order (ODC Order) with respect to the ODC Decision. Following the ODC Order, on October 2, 2020, the OEB issued a procedural order to implement the direction of the Ontario Divisional Court and required Hydro One to submit its proposal for the recovery of the deferred tax asset amounts allocated to ratepayers for the 2017 to 2022 period. The proceeding on this matter is currently ongoing, and a decision is anticipated in the first half of 2021.

2020-2022 Transmission Rates

On April 23, 2020, the OEB rendered its decision on Hydro One Networks' 2020-2022 transmission rate application (2020-2022 Transmission Decision). On July 16, 2020, the OEB issued its final rate order for the 2020-2022 transmission rates approving a revenue requirement of \$1,630 million, \$1,701 million and \$1,772 million for 2020, 2021 and 2022, respectively. On July 30, 2020, the OEB issued its decision for Uniform Transmission Rates (UTRs). The 2020 UTRs that were put in place on an interim basis on January 1, 2020 continued for the remainder of 2020 in light of the COVID-19 pandemic. On December 17, 2020, the OEB issued its decision and order setting the final 2021 UTRs effective January 1, 2021, which included the approval of a two-year disposition period for Hydro One Network's 2020 foregone revenue including interest, beginning on January 1, 2021.

Hydro One Networks – Distribution

On March 31, 2017, Hydro One Networks filed a custom application with the OEB for 2018-2022 distribution rates under the OEB's incentive-based regulatory framework (2018-2022 Distribution Application), which was subsequently updated on June 7 and December 21, 2017.

On March 7, 2019, the OEB rendered its decision on Hydro One Networks' 2018-2022 distribution rate application (2018-2022 Distribution Decision). In accordance with the 2018-2022 Distribution Decision, as well as the DTA Decision, the Company filed its draft rate order reflecting updated revenue requirements of \$1,459 million for 2018, \$1,498 million for 2019, \$1,532 million for 2020, \$1,578 million for 2021, and \$1,624 million for 2022. On June 11, 2019, the OEB approved the rate order confirming these updated revenue requirements, which include impacts of both the 2018-2022 Distribution Decision and the DTA Decision.

On March 26, 2019, the Company filed a motion to review and vary the OEB's decision as it relates to rates revenue requirement recovery of employer pension costs. Concurrently, the Company filed an appeal with the Ontario Divisional Court. The appeal was held in abeyance pending the outcome of the motion made before the OEB. In 2019, the Company reflected a portion of pension costs incurred in the Hydro One Networks' distribution Pension Cost Differential regulatory account, pending the outcome of the motion before the OEB. On December 19, 2019, the OEB affirmed its earlier decision with respect to recovery of the revenue requirement associated with pension costs. As a result, Hydro One derecognized the portion relating to pension costs charged to operations as a reversal of revenues of \$13 million, and also transferred \$37 million to property, plant and equipment and intangible assets, which represents the portion attributable to capital expenditures.

Hydro One Remote Communities

On April 16, 2020, the OEB approved a 2% increase to Hydro One Remote Communities' 2019 base rates for new rates effective May 1, 2020, with a deferred implementation date of November 1, 2020 due to COVID-19. On October 8, 2020, the OEB authorized Hydro One Remote Communities to implement a rate rider for the recovery of foregone revenues resulting from postponing rate implementation. The rider is effective until April 30, 2021. On November 3, 2020, Hydro One Remote Communities filed an application with the OEB seeking approval for a 2% increase to 2020 base rates, effective May 1, 2021, which was subsequently updated to 2.2% in accordance with the OEB's 2021 inflation parameters for electricity distributors issued on November 9, 2020.

Hydro One Remote Communities is fully financed by debt and is operated as a break-even entity with no ROE.

NRLP

On October 25, 2019, NRLP filed its revenue cap incentive rate application for 2020-2024. On December 19, 2019, the OEB approved NRLP's proposed 2020 revenue requirement of \$9 million on an interim basis effective January 1, 2020. On February 12, 2020, all parties reached a full settlement agreement on all issues, accepting the 2020 base costs and the 2019 incurred costs as presented. The settlement included a 50% reduction to the inflation component and a 0.6% capital adjustment factor to account for a lowering rate

base value. On March 6, 2020, the settlement agreement was filed for the OEB's approval, and on April 9, 2020, the OEB approved the settlement agreement.

B2M LP

On July 31, 2019, B2M LP filed a transmission rate application for 2020-2024. A settlement agreement was reached on December 9, 2019. The settlement accepted all of B2M LP's cost submissions, including additional reliability reporting and a capital adjustment (reduction) factor of 0.6% to account for the decreasing rate base value. On January 16, 2020, the OEB approved the settlement agreement, including a 2020 base revenue requirement of \$33 million (updated for lower ROE and interest rates), and a revenue cap escalator index for 2021 to 2024.

MAAD Applications

Peterborough Distribution MAAD Application

On April 30, 2020, the OEB issued its decision approving Hydro One's application to acquire the business and distribution assets of Peterborough Distribution, from the City of Peterborough. See section "Other Developments" for additional information.

Orillia Power MAAD Application

On April 30, 2020, the OEB issued its decision approving Hydro One's application to acquire Orillia Power from the City of Orillia. See section "Other Developments" for additional information.

Hydro One Transmission Licence Amendment

On December 17, 2020, the Province issued a directive to the OEB to amend Hydro One Networks' electricity transmission licence to include a requirement that Hydro One proceed to develop and seek all approvals necessary related to the Leamington Area Transmission Reinforcement project in order to keep the project on schedule to meet the IESO's recommended in-service date. The OEB amended Hydro One's licence on December 23, 2020. See section "Major Transmission Capital Investment Projects" for further details on Leamington Area Transmission Reinforcement project.

Other Developments

COVID-19

Throughout the COVID-19 pandemic, the Company's decisions and actions have continuously been guided by two priorities: to protect Hydro One's employees and to maintain the safe and reliable supply of electricity to Hydro One's customers. Since the onset of the COVID-19 pandemic in March 2020, Hydro One employees have worked extremely hard to overcome the challenges that COVID-19 has presented. Over the course of the last 11 months Hydro One has been extremely successful in achieving its priorities as it was able to return to full capacity within its field operations after a short stand-down of its workforce and has also experienced very few suspected cases of workplace transmission of the COVID-19 virus to date.

The Company continues to monitor and adhere to guidance provided by the Province and public health experts in an effort to ensure employee, customer and public safety. After focusing on high priority and essential work at the onset of pandemic, the Company returned substantially all of its field crews to work, where it was safe to do so, in the second quarter. In the third quarter of 2020, the Company implemented enhanced safety procedures within its office locations

across the province to reopen its offices to a small portion of its office and administrative staff. However, the Company has since reinstated its business continuity procedures, including work from home protocols for all office staff, in light of the Provincial Stay at Home Order announced in December 2020. The Company's focus remains on ensuring that its teams are equipped to operate safely as the Company continues to advance work on capital and operating work programs.

As part of the Company's continued commitment to customers, Hydro One implemented a number of customer relief measures at the outset of the pandemic to assist customers impacted by COVID-19. These measures included (i) the Pandemic Relief Fund, (ii) financial assistance and increased payment flexibility, (iii) extending the Winter Relief program, and (iv) the temporary suspension of late fees until December 31, 2020. In January 2021, the Company announced a Small Business Pandemic Relief Program to provide financial assistance and payment flexibility to its small business customers.

In addition to the impact on the Company's operations noted above, the COVID-19 pandemic had the following impact on Hydro One's financial results for the twelve months ended December 31, 2020:

- While electricity consumption and demand can be impacted by numerous variables, it is difficult to determine the exact impact that the COVID-19 pandemic has had on peak demand and customer consumption over this period with any level of precision.
- The temporary deferral of operating and capital work at the onset of the pandemic resulted in the recognition of costs associated with the stand-down and stranded labour costs of the Company's casual workforce in the second and third quarters of 2020.
- The pandemic resulted in the prolonged temporary closures of businesses across Ontario, which also impacted employment rates locally. As a result of the financial and economic impact of the COVID-19 pandemic on residents and business alike, the Company has recorded a \$14 million allowance for doubtful accounts as of December 31, 2020. While there have been no significant permanent losses incurred to date, management continues to believe that there remains increased risk associated with the ultimate collection of billed energy consumption.
- Lost revenues associated with the ongoing customer relief efforts noted above have approximated \$10 million.
- The COVID-19 pandemic resulted in no significant impacts on the Company's critical accounting estimates and judgments, and internal controls over financial reporting.

In March 2020, the OEB issued initial guidance for the tracking of incremental costs and lost revenues related to the COVID-19 pandemic. In accordance with OEB updates issued in August 2020, the Company has established five deferral accounts to track costs associated with (i) Billing and System Changes as a result of the Emergency Order Regarding Time-Of-Use Pricing, (ii) Lost Revenues Arising from the COVID-19 Emergency, (iii) Foregone Revenues from Postponing Rate Implementation, (iv) incremental Bad Debt, and (v) Other Incremental Costs.

In May 2020, the OEB commenced a consultation on the COVID-19 emergency deferral accounts to assist in its development of new accounting guidance related to the accounts as well as filing requirements for the review and disposition of these accounts. In

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September 2020, the OEB engaged external consultants to commission certain reports to assist the OEB in its preparation of an OEB staff proposal (Staff Proposal) which was issued on December 16, 2020. In its proposal, OEB staff suggested that utilities must demonstrate a financial need and meet certain criteria to be eligible to seek recovery of COVID-19 related costs and lost revenues. Stakeholders were provided an opportunity to submit feedback on the Staff Proposal in January 2021, and it is currently expected that the OEB will issue final guidance sometime in the first half of 2021. Although the consultation is ongoing and the Staff Proposal is subject to change, based on the Company's current interpretation of the Staff Proposal, it appears that Hydro One is unlikely to qualify for any significant recovery of COVID-19 related incremental costs or lost revenues. As a result, during the three months ended December 31, 2020, the Company has reversed the recognition of the regulatory asset associated with the aforementioned incremental bad debt provision recognized in the first quarter of 2020, and has recognized this expense in OM&A in the period.

As at December 31, 2020, the Company is tracking approximately \$60 million in the deferral accounts noted above in accordance with the guidelines published by the OEB in the Staff Proposal. The Company has assessed that these amounts are not probable for future recovery in rates and no amounts related to the COVID-19 pandemic have been recognized as regulatory assets.

Looking ahead, it is very difficult to determine or estimate the exact impacts of COVID-19 on Hydro One's operations as it will be largely dependent on the duration of the pandemic and severity of the measures implemented to combat this virus. Hydro One continues to take the necessary steps to mitigate the impact of COVID-19 on the Company's operations.

The COVID-19 pandemic subjects the Company to additional risks and uncertainties. Please see section "Risk Management and Risk Factors – Infectious Disease Risk" for a discussion of the potential impacts of a pandemic such as COVID-19 on Hydro One.

Federal and Ontario Budgets

2019 Federal and Ontario Budgets

Certain 2019 federal and Ontario budget measures enacted in 2019 provide certain time-limited investment incentives permitting Hydro One to deduct Accelerated CCA of up to three times the first-year rate for eligible capital investments acquired after November 20, 2018 and placed in-service before January 1, 2028. The 2019 enactment of the Accelerated CCA has resulted in a temporary reduction in the Company's ETR for the years ended December 31, 2019 and 2020 with the recognition of a tax regulatory liability relating to the Accelerated CCA impact (Tax Rule Change Variance) that has not been reflected in the OEB approved rates. The timing of the disposition of the Tax Rule Change Variance is subject to OEB approval, and may have a material impact on Hydro One's future cash flows in the near term.

Hydro One currently expects the Company's ETR to remain in the range of 6% to 13% over the next five years, subject to changes arising from the timing and manner in which the OEB seeks to implement the ODC Decision.

Ontario Budget

In November 2020, the Province released its 2020 Ontario Budget: Ontario's Action Plan: Protect, Support, Recover (Ontario Budget) which included a rate mitigation plan to help certain business and industrial customers. Starting on January 1, 2021, a portion of non-hydro renewable energy contracts (i.e., wind, solar, bioenergy) will be funded by the Province and not ratepayers. According to the Ontario Budget, this represents approximately 25% of the current cost of the Global Adjustment. This reduction in the Global Adjustment will not benefit regulated price plan customers (households, farms, small businesses), who will instead continue to be protected by means of the Ontario Electricity Rebate program. These changes impact purchased power costs which are recovered in rates, and as such have no impact on the Company's net income.

Exemptive Relief

Disclosure of Ownership by the Province

On June 6, 2017, the Canadian securities regulatory authorities granted (i) the Minister of Energy, (ii) OPG (on behalf of itself and the segregated funds established as required by the *Nuclear Fuel Waste Act* (Canada)) and (iii) agencies of the Crown, provincial Crown corporations and other provincial entities (collectively, the Non-Aggregated Holders) exemptive relief, subject to certain conditions, to enable each Non-Aggregated Holder to treat securities of Hydro One that it owns or controls separately from securities of Hydro One owned or controlled by the other Non-Aggregated Holders for purposes of certain take-over bid, early warning reporting, insider reporting and control person distribution rules and certain distribution restrictions under Canadian securities laws. Hydro One was also granted relief permitting it to rely solely on insider reports and early warning reports filed by Non-Aggregated Holders when reporting beneficial ownership or control or direction over securities in an information circular or annual information form in respect of securities beneficially owned or controlled by any Non-Aggregated Holder subject to certain conditions.

US GAAP

On March 27, 2018, Hydro One was granted exemptive relief by securities regulators in each province and territory of Canada which allows Hydro One to continue to report its financial results in accordance with US GAAP (Exemptive Relief). The Exemptive Relief will remain in effect until the earlier of: (i) January 1, 2024; (ii) the first day of Hydro One's financial year that commences after Hydro One ceases to have activities subject to rate regulation; and (iii) the effective date prescribed by the International Accounting Standards Board for the mandatory application of a standard within International Financial Reporting Standards specific to entities with activities subject to rate regulation. In late January 2021, the IASB published an Exposure Draft – *Regulatory Assets and Liabilities* (ED). The effective date for mandatory application of the eventual final standard is not yet determinable and the Company continues to monitor the developments of the ED and determine the potential impacts to the Company's financial statements.

Hydro One Limited is also permitted to report its financial results in accordance with US GAAP by virtue of being, and for so long as it remains, a SEC issuer (within the meaning of National Instrument 52-107 – Acceptable Accounting Principles and Auditing Standards). There can be no assurance that Hydro One Limited will remain a SEC issuer indefinitely.

NRLP

In 2018, Hydro One entered into an agreement with the First Nations Partners, wherein a noncontrolling equity interest in Hydro One's limited partnership, NRLP, would be made available for purchase at fair value by the First Nations Partners. On September 12, 2019, the OEB granted NRLP a transmission licence and granted Hydro One Networks leave to sell the applicable Niagara Line assets to NRLP.

On September 18, 2019, the applicable Niagara Line assets were transferred from Hydro One Networks to NRLP for \$119 million and operation of the line was contracted to Hydro One Networks. This transfer was financed with 60% debt (\$71 million) and 40% equity (\$48 million). The cash payment of \$71 million was financed by debt sourced by NRLP from a Hydro One subsidiary, and the \$48 million equity comprised partnership units issued by NRLP to Hydro One Networks. Subsequently, on the same date, Hydro One Networks sold to the Six Nations of the Grand River Development Corporation and, through a trust, to the Mississaugas of the Credit First Nation a 25.0% and 0.1%, respectively, equity interest in NRLP partnership units for total consideration of \$12 million, representing the fair value of the equity interest acquired.

On January 31, 2020, the Mississaugas of the Credit First Nation purchased an additional 19.9% equity interest in NRLP partnership units from Hydro One Networks for total cash consideration of \$9 million. Following this transaction, Hydro One's interest in the equity portion of NRLP partnership units was reduced to 55%, with the Six Nations of the Grand River Development Corporation and the Mississaugas of the Credit First Nation owning 25% and 20%, respectively, of the equity interest in NRLP partnership units.

Building Transit Faster Act

On February 18, 2020, the Ministry of Transportation introduced Bill 171, to enact the *Building Transit Faster Act, 2020* (Transit Act), relating to four priority transit projects in the Toronto area. The Transit Act was passed on July 8, 2020. The Transit Act poses commitments on utilities, including Hydro One, to relocate infrastructure to allow the timely construction of the transit projects. Metrolinx, the builder of the transit projects, and Hydro One must work together on a notice that agrees to the timing of when the relocation work must be completed. If Hydro One is non-compliant, Metrolinx can file an application with the Ontario Superior Court of Justice, where a judge can either order Hydro One to comply or authorize Metrolinx to carry out the work, or impose a monetary penalty on Hydro One. On July 8, 2020, the *Ontario Energy Board Act, 1998* (OEB Act) was accordingly amended to prohibit a utility from recovering the monetary penalty in rates. On October 22, 2020, Bill 222, *An Act to Amend Various Acts in Respect of Transportation-Related Matters* passed first reading. Bill 222 includes amendments to the Transit Act so that the Transit Act would also apply to "any other prescribed provincial transit project" in addition to the four priority transit projects in the Toronto area. The Bill 222 received Royal Assent on December 8, 2020.

Peterborough Distribution Acquisition

On August 1, 2020, Hydro One completed the acquisition of the business and distribution assets of Peterborough Distribution, an electricity distribution company located in east central Ontario, from the City of Peterborough, for a purchase price of \$104 million, including the assumption of agreed upon liabilities and closing adjustments.

Orillia Power Acquisition

On September 1, 2020, Hydro One completed the acquisition of Orillia Power, an electricity distribution company located in Simcoe County, Ontario, from the City of Orillia for a purchase price of \$28 million, including closing adjustments.

Sustainability Report

The Hydro One 2019 Sustainability Report entitled "For the Possibilities of Tomorrow" is available on the Company's website at www.hydroone.com/sustainability.

By using its corporate strategy as the roadmap, Hydro One is more focused than ever on being customer-driven, sustainable, safe and efficient. The 2019 Sustainability Report highlights the Company's progress on operating safely, managing emissions, building relationships with communities and achieving a more diverse workforce. As the Company carries out its mission to energize life for people and communities, it does so with an understanding of the responsibility it has to build a more sustainable world.

The social elements of sustainability are key to ensuring affordability for Hydro One's customers, removing racism and building an inclusive culture, all while adapting the Company's business model to support a greener economy. Going forward, Hydro One is focused on reducing its environmental footprint; strengthening its Indigenous and community partnerships; and diversifying talent across its workforce. No matter how challenging the time, the success of the Company's long-term performance depends on incorporating sustainability into all aspects of its business.

Hydro One is committed to operating safely in an environmentally and socially responsible manner and to partnering with its customers and community stakeholders to build a brighter future for all.

Termination of the Avista Corporation Purchase Agreement

In July 2017, Hydro One reached an agreement to acquire Avista Corporation. In January 2019, Hydro One and Avista Corporation announced that the companies mutually agreed to terminate the Merger agreement. The following amounts related to the termination of the Merger agreement were recorded by the Company during the first quarter of the year ended December 31, 2019.

- \$138 million (US\$103 million) for payment of the Merger termination fee recorded in operation, maintenance and administration costs;
- \$22 million financing charges, due to reversal of previously recorded unrealized gains upon termination of the deal-contingent foreign-exchange forward contract (Foreign-Exchange Contract);
- redemption of \$513 million convertible debentures and payment of related interest of \$7 million; and
- \$24 million financing charges, due to derecognition of the deferred financing costs related to convertible debentures.

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Hydro One Board of Directors and Executive Officers

Board of Directors

Effective May 7, 2020, Anne Giardini resigned from the Company's Board. On July 23, 2020, Stacey Mowbray was appointed to the Board.

Executive Officers

Effective January 2, 2020, David Lebeter was appointed as the Chief Operating Officer of Hydro One and Hydro One Inc.

On September 1, 2020, Saylor Millitz-Lee, Executive Vice President and Chief Human Resources Officer, retired, and effective September 28, 2020, Megan Telford was appointed as the new Chief Human Resources Officer.

On November 1, 2020, Darlene Bradley, Chief Safety Officer, retired, and Lyla Garzouzi was subsequently appointed as the new Chief Safety Officer, effective the same date.

The following table sets out the number of Hydro One employees as at December 31, 2020:

| | Regular Employees | Non-Regular Employees | Total |
|---|-------------------|-----------------------|-------|
| Power Workers' Union (PWU) ^{1,2} | 3,607 | 494 | 4,101 |
| Society of United Professionals (Society) ² | 1,555 | 39 | 1,594 |
| Canadian Union of Skilled Workers (CUSW) and construction building trade unions | — | 1,563 | 1,563 |
| Total employees represented by unions | 5,162 | 2,096 | 7,258 |
| Management and non-represented employees | 788 | 39 | 827 |
| Total employees ³ | 5,950 | 2,135 | 8,085 |

1 Includes 398 non-regular "hiring hall" employees covered by the PWU agreement.

2 In February 2021, Hydro One has finalized agreements with the PWU, the Society, Inergi LP, and Caggemini Canada Inc. to transfer approximately 250 represented Inergi LP employees to Hydro One by January 2022.

3 The average number of Hydro One employees in 2020 was approximately 8,700, consisting of approximately 5,900 regular employees and approximately 2,800 non-regular employees.

Collective Agreements

The collective agreement with the PWU (for classifications other than Customer Service Operations (CSO)) expired on March 31, 2020. The collective agreement with the PWU for CSO was set to expire on September 30, 2019; however, it was extended to allow for bargaining at the same time as the non-CSO agreement. On July 17, 2020, Hydro One and the PWU reached tentative deals for both collective agreements. The PWU ratified the CSO and non-CSO collective agreements on September 4, 2020 and October 6, 2020, respectively. The new CSO agreement expires on September 30, 2022, and the new non-CSO collective agreement expires on March 31, 2023.

The construction building trade unions have collective agreements with the Electrical Power Systems Construction Association (EPSCA). EPSCA is an employers' association of which Hydro One is a member. The EPSCA construction collective agreements, which bind Hydro One, expired on April 30, 2020. Ratified five-year renewal collective agreements, covering May 1, 2020 to April 30, 2025, have been reached with all nineteen building trades.

The current collective agreement with the Society expires on March 31, 2021. In February 2021, Hydro One and the Society commenced collective bargaining with the official exchange of bargaining agendas. Both sides acknowledged their commitment to working towards the timely completion of collective bargaining.

Stock-based Compensation

The Company granted awards under its LTIP, consisting of Performance Share Units (PSUs), Restricted Share Units (RSUs), and Stock Options. At December 31, 2020 and 2019, the following LTIP awards were outstanding:

| December 31 (number of units) | 2020 | 2019 |
|-------------------------------|---------|---------|
| PSUs | 111,920 | 171,344 |
| RSUs | 139,730 | 206,993 |
| Stock Options | 108,710 | 403,550 |

Non-GAAP Measures

FFO, basic and diluted Adjusted EPS, adjusted net income, revenues, net of purchased power, and distribution revenues, net of purchased power are not recognized measures under US GAAP and do not have a standardized meaning prescribed by US GAAP. They are therefore unlikely to be directly comparable to similar measures presented by other companies. They should not be considered in isolation nor as a substitute for analysis of the Company's financial information reported under US GAAP.

FFO

FFO is defined as net cash from operating activities, adjusted for (i) changes in non-cash balances related to operations, (ii) dividends paid on preferred shares, and (iii) distributions to noncontrolling interest. Management believes that FFO is helpful as a supplemental measure of the Company's operating cash flows as it excludes timing-related fluctuations in non-cash operating working capital and cash flows not attributable to common shareholders. As such, management believes that FFO provides a consistent measure of the cash generating performance of the Company's assets.

| Year ended December 31 (millions of dollars) | 2020 | 2019 |
|--|--------------|-------|
| Net cash from operating activities | 2,030 | 1,614 |
| Changes in non-cash balances related to operations | (180) | (55) |
| Preferred share dividends | (18) | (18) |
| Distributions to noncontrolling interest | (2) | (9) |
| FFO | 1,830 | 1,532 |

Adjusted Net Income and Adjusted EPS

The following adjusted net income, and basic and diluted Adjusted EPS have been calculated by management on a supplementary basis which adjusts net income under US GAAP for income and costs related to the Merger and impacts related to the ODC Decision and the OEB's DTA Decision on Hydro One Networks' distribution and transmission businesses. Adjusted net income and Adjusted EPS are used internally

by management to assess the Company's performance and are considered useful because they exclude the impacts of the Merger as well as the ODC Decision and the OEB's DTA Decision as noted above. Adjusted net income and Adjusted EPS provide users with a comparative basis to evaluate the current ongoing operations of the Company compared to prior year.

| Year ended December 31 (millions of dollars, except number of shares and EPS) | 2020 | 2019 | 2018 |
|---|--------------------|-------------|-------------|
| Net income (loss) attributable to common shareholders | 1,770 | 778 | (89) |
| Impacts related to the Merger: | | | |
| OM&A – Merger-related costs (before tax) | – | 138 | 11 |
| Financing charges – Merger-related costs (before tax) | – | 31 | 58 |
| Financing charges – loss (gain) on Foreign-Exchange Contract (before tax) | – | 22 | (25) |
| Tax impact | – | (51) | (15) |
| Merger-related impacts (after tax) | – | 140 | 29 |
| Impacts related to the ODC Decision | (867) | – | 867 |
| Adjusted net income attributable to common shareholders | 903 | 918 | 807 |
| Weighted average number of shares | | | |
| Basic | 597,421,127 | 596,437,577 | 595,756,470 |
| Effect of dilutive stock-based compensation plans | 2,497,161 | 2,410,860 | 2,147,473 |
| Diluted | 599,918,288 | 598,848,437 | 597,903,943 |
| Adjusted EPS | | | |
| Basic | \$ 1.51 | \$ 1.54 | \$ 1.35 |
| Diluted | \$ 1.51 | \$ 1.53 | \$ 1.35 |

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| Quarter ended (millions of dollars, except number of shares and EPS) | Dec 31, 2020 | Sep 30, 2020 | Jun 30, 2020 | Mar 31, 2020 |
|--|--------------|--------------|--------------|--------------|
| Net income attributable to common shareholders | 161 | 281 | 1,103 | 225 |
| Impacts related to the ODC Decision | — | — | (867) | — |
| Adjusted net income attributable to common shareholders | 161 | 281 | 236 | 225 |
| Weighted-average number of shares | | | | |
| Basic | 597,588,309 | 597,557,787 | 597,551,514 | 596,983,560 |
| Effect of dilutive stock-based compensation plans | 2,586,310 | 2,362,569 | 2,423,441 | 2,663,999 |
| Diluted | 600,174,619 | 599,920,356 | 599,974,955 | 599,647,559 |
| Adjusted EPS | | | | |
| Basic | \$ 0.27 | \$ 0.47 | \$ 0.39 | \$ 0.38 |
| Diluted | \$ 0.27 | \$ 0.47 | \$ 0.39 | \$ 0.38 |

| Quarter ended (millions of dollars, except number of shares and EPS) | Dec 31, 2019 | Sep 30, 2019 | Jun 30, 2019 | Mar 31, 2019 |
|--|--------------|--------------|--------------|--------------|
| Net income attributable to common shareholders | 211 | 241 | 155 | 171 |
| OM&A – Merger-related costs (before tax) | — | — | — | 138 |
| Financing charges – Merger-related costs (before tax) | — | — | — | 31 |
| Financing charges – loss on Foreign-Exchange Contract (before tax) | — | — | — | 22 |
| Tax impact | — | — | — | (51) |
| Impacts related to the Merger (after tax) | — | — | — | 140 |
| Adjusted net income attributable to common shareholders | 211 | 241 | 155 | 311 |
| Weighted-average number of shares | | | | |
| Basic | 596,670,374 | 596,605,054 | 596,503,988 | 595,961,260 |
| Effect of dilutive stock-based compensation plans | 2,564,789 | 2,420,792 | 2,442,181 | 2,354,970 |
| Diluted | 599,235,163 | 599,025,846 | 598,946,169 | 598,316,230 |
| Adjusted EPS | | | | |
| Basic | \$ 0.35 | \$ 0.40 | \$ 0.26 | \$ 0.52 |
| Diluted | \$ 0.35 | \$ 0.40 | \$ 0.26 | \$ 0.52 |

Revenues, Net of Purchased Power

Revenues, net of purchased power is defined as revenues less the cost of purchased power. Management believes that revenue, net of purchased power is helpful as a measure of net revenues for the distribution segment, as purchased power is fully recovered through revenues.

| Year ended December 31 (millions of dollars) | 2020 | 2019 |
|--|--------------|--------------|
| Revenues | 7,290 | 6,480 |
| Less: Purchased power | 3,854 | 3,111 |
| Revenues, net of purchased power | 3,436 | 3,369 |

| Year ended December 31 (millions of dollars) | 2020 | 2019 |
|--|--------------|--------------|
| Distribution revenues | 5,507 | 4,788 |
| Less: Purchased power | 3,854 | 3,111 |
| Distribution revenues, net of purchased power | 1,653 | 1,677 |

| Quarter ended (millions of dollars) | Dec 31, 2020 | Sep 30, 2020 | Jun 30, 2020 | Mar 31, 2020 | Dec 31, 2019 | Sep 30, 2019 | Jun 30, 2019 | Mar 31, 2019 |
|---|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|
| Revenues | 1,867 | 1,903 | 1,670 | 1,850 | 1,715 | 1,593 | 1,413 | 1,759 |
| Less: Purchased power | 1,046 | 993 | 808 | 1,007 | 914 | 737 | 653 | 807 |
| Revenues, net of purchased power | 821 | 910 | 862 | 843 | 801 | 856 | 760 | 952 |

| Quarter ended (millions of dollars) | Dec 31, 2020 | Sep 30, 2020 | Jun 30, 2020 | Mar 31, 2020 | Dec 31, 2019 | Sep 30, 2019 | Jun 30, 2019 | Mar 31, 2019 |
|--|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|
| Distribution revenues | 1,457 | 1,410 | 1,201 | 1,439 | 1,298 | 1,140 | 1,029 | 1,321 |
| Less: Purchased power | 1,046 | 993 | 808 | 1,007 | 914 | 737 | 653 | 807 |
| Distribution revenues, net of purchased power | 411 | 417 | 393 | 432 | 384 | 403 | 376 | 514 |

Adjusted Income Tax Expense and Adjusted ETR

The following adjusted income tax expense and adjusted ETR has been calculated by management on a supplementary basis which adjusts ETR for income and costs related to the Merger and impacts related to the ODC Decision. Adjusted ETR is used internally by management to assess the Company's income tax impacts and is considered useful because it excludes the impacts of the Merger and the ODC Decision. Adjusted ETR provides users with a comparative basis to evaluate the income tax impacts on the Company compared to prior year.

| Year ended December 31 (millions of dollars) | 2020 | 2019 |
|--|--------------|------|
| Income before income tax expense | 1,011 | 796 |
| OM&A – Merger-related costs (before tax) | – | 138 |
| Financing charges – Merger-related costs (before tax) | – | 31 |
| Financing charges – loss on Foreign-Exchange Contract (before tax) | – | 22 |
| Impacts related to the Merger | – | 191 |
| Adjusted income before income tax expense | 1,011 | 987 |
| Income tax (recovery) | (785) | (6) |
| Impacts related to the ODC Decision | (867) | – |
| Impacts related to the Merger | – | (51) |
| | (867) | (51) |
| Adjusted income tax expense | 82 | 45 |
| Adjusted ETR | 8.1% | 4.6% |

Related Party Transactions

The Province is a shareholder of Hydro One with approximately 47.3% ownership at December 31, 2020. The IESO, OPG, Ontario Electricity Financial Corporation (OEFC), and the OEB are related parties to Hydro One because they are controlled or significantly influenced by the Ministry of Energy. OCN LP is a joint-venture limited partnership between a subsidiary of Hydro One and OPG. The following is a summary of the Company's related party transactions during the years ended December 31, 2020 and 2019:

| Year ended December 31 (millions of dollars) | | 2020 | 2019 |
|--|---|--------------|-------|
| Related Party | Transaction | | |
| Province | Dividends paid ¹ | 301 | 288 |
| IESO | Power purchased | 2,506 | 1,808 |
| | Revenues for transmission services | 1,717 | 1,636 |
| | Amounts related to electricity rebates | 1,588 | 692 |
| | Distribution revenues related to rural rate protection | 242 | 240 |
| | Distribution revenues related to the supply of electricity to remote northern communities | 35 | 35 |
| | Funding received related to CDM programs | 26 | 42 |
| OPG² | Power purchased | 6 | 8 |
| | Revenues related to provision of services and supply of electricity | 8 | 9 |
| | Capital contribution received from OPG | 3 | – |
| | Costs related to the purchase of services | 3 | 1 |
| OEFC | Power purchased from power contracts administered by the OEFC | 1 | 2 |
| OEB | OEB fees | 9 | 9 |
| OCN LP³ | Investment in OCN LP | 2 | 2 |

1 On November 20, 2020, Hydro One redeemed the Preferred Shares held by the Province. See section Share Capital.

2 OPG has provided a \$2.5 million guarantee to Hydro One related to the OCN Guarantee. See Other Obligations – Summary of Contractual Obligations and Other Commercial Commitments for details related to the OCN Guarantee.

3 OCN LP owns and operates electric vehicle fast charging stations across Ontario, under the Ivy Charging Network brand.

Management's Discussion and Analysis

Risk Management and Risk Factors

Hydro One is subject to numerous risks and uncertainties. Critical to Hydro One's success is the identification, management, and to the extent possible, mitigation of these risks. Hydro One's Chief Risk Officer has accountability for the Company's Enterprise Risk Management (ERM) program, which assists decision-makers throughout the organization with the management of key business risks, including new and emerging risks and opportunities.

The material risks relating to Hydro One and its business that the Company believes would be the most likely to influence an investor's decision to purchase Hydro One's securities are set out in the risk factors below. These risks, if they materialize, could have a materially adverse effect on the Company or its business, financial condition, or results of operations. This list is not a comprehensive list of all the risks to the Company, and the actual effect of any of the risks cited below could be materially different from what is described below. Additionally, other risks may arise or risks currently not considered material may become material in the future.

Risks Relating to Hydro One's Business

Regulatory Risks and Risks Relating to Hydro One's Revenues

Risks Relating to Obtaining Rate Orders

The Company is subject to the risk that the OEB will not approve the Company's transmission and distribution revenue requirements requested in outstanding or future applications for rates. Rate applications for revenue requirements are subject to the OEB's review process, usually involving participation from intervenors and a public hearing process. There can be no assurance that resulting decisions or rate orders issued by the OEB will permit Hydro One to recover all costs actually incurred, costs of debt and income taxes, or to earn a particular ROE. A failure to obtain acceptable rate orders, or approvals of appropriate returns on equity and the ability to recover in rates costs actually incurred, may materially adversely affect: Hydro One's transmission and distribution businesses, the undertaking or timing of capital expenditures, ratings assigned by credit rating agencies, the cost and issuance of long-term debt, and other matters, any of which may in turn have a material adverse effect on the Company. In addition, there is no assurance that the Company will receive regulatory decisions in a timely manner and, therefore, the Company may incur costs before having an approved revenue requirement and cash flows could be impacted. The Company is also subject to the risk that the OEB could change the regulatory treatment of certain costs which may affect the Company's accounting treatment of and ability to recover such costs.

Risks Relating to Actual Performance Against Forecasts

The Company's ability to recover the actual costs of providing service and earn the allowed ROE depends on the Company achieving its forecasts established and approved in the rate-setting process. Actual costs could exceed the approved forecasts if, for example, the Company incurs operations, maintenance, administration, capital and financing costs above those included in the Company's approved revenue requirement. The inability to recover any significant difference between forecast and actual expenses and to obtain associated regulatory approvals to recover the difference could materially adversely affect the Company's financial condition and results of operations.

Further, the OEB approves the Company's transmission and distribution rates based on projected electricity load and consumption levels, among other factors. If actual load or consumption materially falls below projected levels, the Company's revenue and net income for either, or both, of these businesses could be materially adversely affected. Also, the Company's current revenue requirements for these businesses are based on cost and other assumptions that may not materialize. There is no assurance that the OEB would allow rate increases sufficient to offset unfavourable financial impacts from unanticipated changes in electricity demand or in the Company's costs.

The Company is subject to risk of revenue loss from other factors, such as economic trends and conditions, changes in service territory, and weather conditions that influence the demand for electricity. The Company's overall operating results may fluctuate substantially on a seasonal and year-to-year basis based on these trends and weather conditions. For instance, a cooler than normal summer or warmer than normal winter can be expected to reduce demand for electricity below that forecast by the Company, causing a decrease in the Company's revenues from the same period of the previous year.

The Company's load could also be negatively affected by successful CDM programs whose results exceed forecasted expectations.

Risks Relating to Other Applications to the OEB

Hydro One may face increased competition with other transmitters for opportunities to build new, large-scale transmission facilities in Ontario. The Company is subject to the risk that it will not be selected to build new transmission in Ontario, which could impair growth, disrupt operations and/or development, or have other adverse impacts. The Company is also subject to the risk that it will not obtain, or will not obtain in a timely manner, required regulatory approvals for other matters, such as leave to construct applications, applications for mergers, acquisitions, amalgamations and divestitures, and environmental approvals. Decisions to acquire or divest other regulated businesses licensed by the OEB are subject to OEB approval. Accordingly, there is the risk that such matters may not be approved, that the Company may not be selected to build new transmission as part of the competitive process, or that unfavourable conditions will be imposed by the OEB.

Risks Relating to Rate-Setting Models for Transmission and Distribution

The OEB approves and periodically changes the rate-setting models and methodology for the transmission and distribution businesses. Changes to the application type, filing requirements, rate-setting model or methodology, or revenue requirement determination may have a material negative impact on Hydro One's revenue and net income. For example, the OEB may in the future decide to reduce the allowed ROE for either of these businesses, modify the formula or methodology it uses to determine the ROE, or reduce the weighting of the equity component of the deemed capital structure. Any such reduction could reduce the net income of the Company. Similarly, the OEB is currently considering other utility remuneration models, and any such change could affect Hydro One's revenue and net income.

The OEB's Custom Incentive Rate-setting model requires that the term of a custom rate application be for multi-year periods. There are risks associated with forecasting key inputs such as revenues,

operating expenses and capital over such a long period. For instance, if unanticipated capital expenditures arise that were not contemplated in the Company's most recent rate decision, the Company may be required to incur costs that may not be recoverable until a future period or not recoverable at all in future rates. This could have a material adverse effect on the Company.

When rates are set for a multi-year period, including under a Custom Incentive Rate application, the OEB expects there to be no further rate applications for annual updates within the multi-year period, unless there are exceptional circumstances, with the exception of the clearance of established deferral and variance accounts. For example, the OEB does not expect to address annual rate applications for updates for cost of capital (including ROE), working capital allowance or sales volumes. If there were an increase in interest rates over the period of a rate decision and no corresponding changes were permitted to the Company's allowed cost of capital (including ROE), then the result could be a decrease in the Company's financial performance.

To the extent that the OEB approves an in-service variance account for the transmission and/or distribution businesses, and should the Company fail to meet the threshold levels of in-service capital, the OEB may reclaim a corresponding portion of the Company's revenues.

Risks Relating to Capital Expenditures

In order to be recoverable in rates, capital expenditures require the approval of the OEB. There can be no assurance that all capital expenditures, including any imposed by or resulting from government or regulatory bodies, incurred by Hydro One will be approved by the OEB. For example, capital cost overruns, unexpected capital expenditures in maintaining or improving the Company's assets, unexpected costs as a result of proposed legislation, including that relating to the expansion of broadband service in Canada, may not be recoverable in transmission or distribution rates. To the extent possible, Hydro One aims to mitigate this risk by ensuring expenditures are reasonable and prudent, and also by seeking from the regulator clear policy direction on cost responsibility, and by obtaining pre-approval of the need for capital expenditures.

Any regulatory decision by the OEB to disallow or limit the recovery of any capital expenditures would lead to a lower-than-expected approved revenue requirement or rate base, potential asset impairment or charges to the Company's results of operations, any of which could have a material adverse effect on the Company.

Risk of Recoverability of Total Compensation Costs

Hydro One manages all of its total compensation costs, including pension and other post-employment and post-retirement benefits (OPEBs), subject to restrictions and requirements imposed by the collective bargaining process and legislative requirements. Any element of total compensation costs which is disallowed in whole or part by the OEB and therefore not recoverable from customers in rates could result in costs which could be material and could decrease net income, which could have a material adverse effect on the Company. The OEB Act prohibits Hydro One from recovering specified executive compensation costs in its rates.

The Company provides OPEBs, including workers compensation benefits and long-term disability benefits to qualifying employees. Hydro One currently maintains the accrual accounting method with

respect to OPEBs. If the OEB directed Hydro One to transition to a different accounting method for OPEBs or otherwise adjusted the basis of recovery for OPEB costs, this could result in income volatility, due to an inability of the Company to book the difference between the accrual and cash as a regulatory asset, and the Company might not be able to recover some costs. A determination that some of the Company's post-employment and post-retirement benefit costs are not recoverable could have a material adverse effect on the Company.

Risks Relating to Regulatory Treatment of Deferred Tax Asset

As a result of leaving the payments in lieu of corporate income taxes (PILs) regime and entering the federal tax regime in connection with the 2015 initial public offering (IPO) of the Company, Hydro One recorded additional deferred tax assets due to the revaluation of the tax basis of Hydro One's fixed assets at their fair market value and recognition of eligible capital expenditures. At the time of the IPO, the Company determined the tax savings derived from the additional deferred tax assets should accrue to the shareholders of Hydro One Limited. The OEB's September 28, 2017 Original Decision (see details above in "Regulation – Electricity Rates Applications – Hydro One Networks – Transmission") altered Hydro One's allocation of the tax savings derived from the additional deferred tax assets and determined that a portion of the tax savings should accrue to ratepayers. In October 2017, the Company filed a motion to review and vary (Motion) the Original Decision and filed an appeal with the Ontario Divisional Court (Appeal) which was stayed pending the outcome of the Motion. In both cases, the Company's position was that the OEB made errors of fact and law in its determination of the allocation of the tax savings between shareholders and ratepayers.

On March 7, 2019, the OEB issued a decision upholding its Original Decision on the handling of the deferred tax asset. Also, on March 7, 2019, the OEB issued its decision for Hydro One Networks' 2018-2022 distribution rates in which it directed the Company to apply the Original Decision to Hydro One Networks' distribution rates. Based on these decisions, the Company recognized a total one-time \$867 million decrease to net income. On April 5, 2019, the Company filed a motion to commence a new appeal with respect to the OEB's deferred tax asset decision. The appeal was heard on November 21, 2019, and on July 16, 2020, the Ontario Divisional Court rendered its decision, setting aside the decision of the OEB and ordered the matter be returned to the OEB to correct the errors identified and made the appropriate tax savings allocation. If the OEB again fails to make the appropriate tax savings allocation, it could have a material adverse effect on the Company.

Risks Relating to Government Action

The Province is, and is likely to remain, the largest shareholder in Hydro One Limited. The Province may be in a position of conflict from time to time as a result of being an investor in Hydro One Limited and also being a government actor setting broad policy objectives in the electricity industry. Government actions may not be in the interests of the Company or investors.

Governments may pass legislation or issue regulations at any time, including legislation or regulation impacting Hydro One, which could have potential material adverse effects on Hydro One and its business. Such government actions may include, but are not limited to, legislation, regulation, directives or shareholder action intended to reduce electricity

Management's Discussion and Analysis

rates, place constraints on compensation, or affect the governance of Hydro One. Such government actions could adversely affect the Company's financial condition and results of operations, as well as public opinion and the Company's reputation. Government action may also hinder Hydro One's ability to pursue its strategy and/or objectives.

Additionally, involvement by the Province in placing constraints on executive compensation (through the compensation framework implemented as a result of the *Hydro One Accountability Act, 2018*) may inhibit the Company's ability to attract and retain qualified executive talent, which may also impact the Company's performance, strategy and/or objectives. The failure to attract and retain qualified executives could have a material adverse effect on the Company.

Government action may also impact the Company's credit ratings as the Company's credit ratings reflect, in part, the rating agencies' assessment of government involvement in the business of Hydro One. The Company cannot predict what actions rating agencies may take in the future, positive or negative, including in response to government action or inaction relating to or impacting Hydro One. The failure to maintain the Company's current credit ratings could adversely affect the Company's financial condition and results of operations, and a downgrade in the Company's credit ratings could restrict the Company's ability to access debt capital markets and increase the Company's cost of debt.

Indigenous Claims Risk

Some of the Company's current and proposed transmission and distribution assets are or may be located on reserve (as defined in the *Indian Act* (Canada)) (Reserve) lands, or lands over which Indigenous people have Aboriginal, treaty, or other legal claims. Some Indigenous leaders, communities, and their members have made assertions related to sovereignty and jurisdiction over Reserve lands and traditional territories (land traditionally occupied or used by a First Nation, Métis or Inuit group) and are increasingly willing to assert their claims through the courts, tribunals, or direct action. These claims, and/or the settlement or resolution of these claims could have a material adverse effect on the Company or otherwise materially adversely impact the Company's operations, including the development of current and future projects.

The Company's operations and activities may give rise to the Crown's duty to consult and potentially accommodate Indigenous communities. Procedural aspects of the duty to consult may be delegated to the Company by the Province or the federal government. A perceived failure by the Crown to sufficiently consult an Indigenous community, including communities with a traditional governance model not recognized under the *Indian Act*, or a perceived failure by the Company in relation to delegated consultation obligations, could result in legal challenges against the Crown or the Company, including judicial review or injunction proceedings, or could potentially result in direct action against the Company by a community or its citizens. If this occurs, it could disrupt or delay the Company's operations and activities, including current and future projects, and have a material adverse effect on the Company.

Risk from Transfer of Assets Located on Reserves

The transfer orders by which the Company acquired certain of Ontario Hydro's businesses as of April 1, 1999 did not transfer title to assets located on Reserves. The transfer of title to these assets did not occur

because authorizations originally granted by the federal government for the construction and operation of these assets on Reserves could not be transferred without required consent. In several cases, the authorizations had either expired or had never been issued.

Currently, OEFC holds legal title to these assets and it is expected that the Company will manage them until it has obtained permits to complete the title transfer. To occupy Reserves, the Company must have valid permits. For each permit, the Company must negotiate an agreement with the First Nation, OEFC and any members of the First Nation who have occupancy rights. The agreement includes provisions whereby the First Nation consents to the issuance of a permit. For transmission assets, the Company must negotiate terms of payment. It is difficult to predict the aggregate amount that the Company may have to pay to obtain the required agreements from First Nations. If the Company cannot reach satisfactory agreements with the relevant First Nation to obtain federal permits, it may have to relocate these assets to other locations and restore the lands at a cost that could be substantial. In a limited number of cases, it may be necessary to abandon a line and replace it with diesel generation facilities. In either case, the costs relating to these assets could have a material adverse effect on the Company if the costs are not recoverable in future rate orders.

Executive Recruitment and Retention Risk

Involvement by the Province relating to executive compensation, and Hydro One executive compensation constraints flowing from the *Hydro One Accountability Act, 2018*, may inhibit the Company's ability to attract and retain qualified executive talent. The Company's strategy is tied to its ability to continue to attract and retain qualified executives. The failure to attract and retain qualified executives could have a material adverse effect on the Company.

Compliance with Laws and Regulations

Hydro One must comply with numerous laws and regulations affecting its business, including requirements relating to transmission and distribution companies, environmental laws, employment laws and health and safety laws. The failure of the Company to comply with these laws could have a material adverse effect on the Company's business. See also "– Environment Risk" and "– Health and Safety Risk".

For example, Hydro One's licensed transmission and distribution businesses are required to comply with the terms of their licences, with codes and rules issued by the OEB, and with other regulatory requirements. In Ontario, the Market Rules issued by the IESO require the Company to, among other things, comply with applicable reliability standards established by the North American Electric Reliability Corporation (NERC) and Northeast Power Coordinating Council, Inc. (NPCC). The costs associated with compliance with these reliability standards are expected to be recovered through rates, but there can be no assurance that the OEB will approve the recovery of all of such costs. Failure to obtain such approvals could have a material adverse effect on the Company.

There is the risk that new legislation, regulations, requirements or policies will be introduced in the future. These may reduce Hydro One's revenue, or may require Hydro One to incur additional costs, which may or may not be recovered in future transmission and distribution rates.

Risk of Natural and Other Unexpected Occurrences

The Company's facilities are exposed to the effects of severe weather conditions, natural disasters, man-made events including, but not limited to, cyber and physical terrorist type attacks, events which originate from third-party connected systems, and any other potentially catastrophic events. The Company's facilities may not withstand occurrences of these types in all circumstances.

The Company could also be subject to claims for damages from events which may be proximately connected with the Company's assets (for example, forest fires), claims for damages caused by its failure to transmit or distribute electricity, costs related to ensuring its continued ability to transmit or distribute electricity or costs related to information or cyber security.

The Company does not have insurance for damage to its transmission and distribution wires, poles and towers located outside its transmission and distribution stations resulting from these or other events. Where insurance is available for the Company's other assets and for damage claims and cyber security claims, such insurance coverage may have deductibles, limits and/or exclusions that may still expose the Company to material losses. Losses from lost revenues and repair costs could be substantial, especially for many of the Company's facilities that are located in remote areas.

In the event that the Company is unable to recover such costs, this could have a material adverse effect on the Company.

Infectious Disease Risk

An outbreak of infectious disease, in the form of an epidemic, a pandemic (such as COVID-19), or a similar public health threat, could materially adversely impact the Company. The extent of any such adverse impact on the Company is uncertain, and may depend on the length and severity of any such infectious disease outbreak, any resultant government regulations, guidelines and actions, and any related adverse changes in general economic and market conditions. Such an outbreak, the resultant government regulations, guidelines and actions, and related adverse changes in general economic and market conditions could impact, in particular: the Company's operations and workforce, including its ability to complete planned operating and capital work programs within scope and budget; certain financial obligations of the Company, including pension contributions and other post-retirement benefits, as a result of changes in prevailing market conditions; the Company's expected revenues; reductions in overall electricity consumption and load, both short term and long term; overdue accounts and bad debt increases as a result of changes in the ability of the Company's customers to pay; liquidity and the Company's ability to raise capital; the Company's ability to pay or increase dividends; the timing of increased rates; the Company's ability to recover incremental costs and lost revenues linked to the outbreak; the Company's ability to file regulatory filings on a timely basis; timing of regulatory decisions and the impacts those decisions may have on the Company or its ability to implement them; and customer and stakeholder needs and expectations.

The Company also faces risks and costs associated with implementation of business continuity plans and modified work conditions, including the risks and costs associated with maintaining or reducing its workforce, making the required resources available to its workforce to enable them to continue essential work, including remotely where possible, and to keep its workforce healthy, as well as risks and costs associated with

recovery of normal operations. Furthermore, the Company is dependent on third-party providers for certain activities, and relies on a strong international supply chain, which may also be adversely impacted, and which, in turn, could materially adversely impact the Company. See also "Other Developments – COVID-19".

Environment Risk

The Company is subject to extensive Canadian federal, provincial and municipal environmental regulation. Failure to comply could subject the Company to fines or other penalties. In addition, the presence or release of hazardous or other harmful substances could lead to claims by third parties or governmental orders requiring the Company to take specific actions such as investigating, controlling and remediating the effects of these substances. Although Hydro One is not a large emitter of greenhouse gases, the Company monitors its emissions to track and report on all sources, including sulphur hexafluoride or "SF6". The Company could be subject to costs and other risks related to emissions. Contamination of the Company's properties could limit its ability to sell or lease these assets in the future.

In addition, actual future environmental expenditures may vary materially from the estimates used in the calculation of the environmental liabilities provided for in the Company's financial statements. The Company does not have insurance coverage for these environmental expenditures.

There is also risk associated with obtaining governmental approvals, permits, or renewals of existing approvals and permits related to constructing or operating facilities. This may require environmental assessment or result in the imposition of conditions, or both, which could result in delays and cost increases. Failure to obtain necessary approvals or permits could result in an inability to complete projects which may have a material adverse effect on the Company.

The Company's facilities are exposed to the effects of severe weather conditions and natural disasters. The Company recognizes the risks associated with potential climate change and has developed plans to respond as appropriate. Climate change may have the effect of shifting weather patterns and increasing the severity and frequency of extreme weather events and natural disasters, which could impact Hydro One's business. The Company's facilities may not withstand occurrences of these types in all circumstances. Notwithstanding Hydro One's efforts to adapt and increase grid resilience, the Company's facilities are exposed to risks which may have an adverse effect on grid resilience. The Company could also be subject to claims for damages from events which may be proximately connected with the Company's assets (for example, forest fires), claims for damages caused by its failure to transmit or distribute electricity or costs related to ensuring its continued ability to transmit or distribute electricity. The Company does not have insurance for damage to its transmission and distribution wires, poles and towers located outside its transmission and distribution stations resulting from these or other events. Where insurance is available for the Company's other assets and for damage claims, such insurance coverage may have deductibles, limits and/or exclusions that may still expose the Company to material losses. Losses from lost revenues and repair costs could be substantial, especially for many of the Company's facilities that are located in remote areas.

In the event that the Company is unable to recover such costs, this could have a material adverse effect on the Company.

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Risk Associated with Information Technology (IT), Operational Technology (OT) Infrastructure and Data Security

The Company's ability to operate effectively in the Ontario electricity market is, in part, dependent upon it developing, modernizing, maintaining and managing complex IT and OT systems which are employed to operate and monitor its transmission and distribution facilities, financial and billing systems and other business systems. The Company's increasing reliance on information systems and expanding data networks, as well as growing volume and complexity of data, increases its vulnerability, and exposure to information security threats. The Company's transmission business is required to comply with various rules and standards for transmission reliability, including mandatory standards established by the NERC and the NPCC. These include standards relating to cyber-security and OT, which only apply to certain of the Company's assets (generally being those whose failure could impact the functioning of the bulk electricity system). The Company may maintain different or lower levels of security for its assets that are not subject to these mandatory standards. The Company must also comply with various cyber-security and privacy-related regulatory requirements under the OEB's Ontario Cyber Security Framework and legislative and licence requirements relating to the collection, use and disclosure of personal information and information regarding consumers, wholesalers, generators and retailers.

Cyber-attacks or unauthorized access to corporate IT and OT systems could result in service disruptions and system failures, which could have a material adverse effect on the Company, including as a result of a failure to provide electricity to customers. Because it operates critical infrastructure, Hydro One may be at greater risk of cyber-attacks from third parties (including state run or controlled parties) that could impair or incapacitate its assets. In addition, in the course of its operations, the Company collects, uses, processes and stores information which could be exposed in the event of a cyber-security incident or other unauthorized access or disclosure, such as information about customers, suppliers, counterparties, employees and other third parties.

Security and system disaster recovery controls are in place; however, there can be no assurance that there will not be system failures or security breaches or that such threats would be detected or mitigated on a timely basis. Upon occurrence and detection, the focus would shift from prevention to isolation, remediation and recovery until the incident has been fully addressed. Any such system failures or security breaches could have a material adverse effect on the Company.

Labour Relations Risk

A substantial majority of the Company's employees are unionized and are primarily represented by either the PWU or the Society. Over the past several years, significant effort has been expended to increase Hydro One's flexibility to conduct operations in a more cost-efficient manner. Although the Company has achieved improved flexibility in its collective agreements, the Company may not be able to achieve further improvements. Agreements were also reached with the Society and the PWU to facilitate the insourcing of CSO services effective March 1, 2018. The Company reached an agreement with the Society for a collective agreement, covering the period from April 1, 2019 to March 31, 2021. The Company also reached a non-CSO collective agreement with the PWU, covering the period from April 1, 2020 to March 31 2023, and a CSO collective agreement with the PWU covering the period from October 1, 2019 to September 30, 2022. The Company also reached a collective

agreement with the CUSW, covering the period from May 1, 2017 to April 30, 2022. Additionally, EPSCA and a number of building trade unions have agreements, to which Hydro One is bound, covering the period from May 1, 2020 to April 30, 2025 (see "Hydro One Work Force – Collective Agreements" for details). Future negotiations with unions present the risk of a labour disruption or dispute, risk to the Company's ability to sustain the continued supply of electricity to customers, as well as potential risks to public safety. The Company also faces financial risks related to its ability to negotiate collective agreements consistent with its rate orders. Any of these could have a material adverse effect on the Company. The Society collective agreement requires renewal in 2021 (see "Hydro One Work Force – Collective Agreements" for details). Failure to renew this agreement on terms acceptable to Hydro One could have a material adverse effect on its business and results of operations and expose Hydro One to the risks noted above.

Work Force Demographic Risk

By the end of 2020, approximately 14% of the Company's employees who are members of the Company's defined benefit and defined contribution pension plans were eligible for retirement, and by the end of 2021, approximately 15% could be eligible. These percentages are not evenly spread across the Company's workforce, but tend to be most significant in the most senior levels of the Company's staff and among management staff. During 2020, approximately 3% of the Company's workforce (approximately the same percentage in 2019) elected to retire. Accordingly, the Company's continued success will be tied to its ability to continue to attract and retain sufficient qualified staff to replace the capability lost through retirements and meet the demands of the Company's work programs.

In addition, the Company expects the skilled labour market for its industry will remain highly competitive. Many of the Company's current and potential employees are sought after as they possess skills and experience that are also highly coveted by other organizations inside and outside the electricity sector. The failure to attract, retain and deploy qualified personnel for Hydro One's business could have a material adverse effect on the Company.

Risk Associated with Arranging Debt Financing

The Company expects to borrow to repay its existing indebtedness and to fund a portion of capital expenditures. Hydro One Inc. has substantial debt principal repayments coming due, including \$803 million in 2021, \$604 million in 2022 and \$731 million in 2023. In addition, from time to time, the Company may draw on its syndicated bank lines and/or issue short-term debt under Hydro One Inc.'s \$2,300 million commercial paper program which would mature within one year of issuance. The Company also plans to incur continued material capital expenditures for each of 2021 and 2022. Cash generated from operations, after the payment of expected dividends, will not be sufficient to fund the repayment of the Company's existing indebtedness and capital expenditures. The Company's ability to arrange sufficient and cost-effective debt financing could be materially adversely affected by numerous factors, including the regulatory environment in Ontario, the Company's results of operations and financial position, market conditions, the ratings assigned to its debt securities by credit rating agencies, an inability of the Company to comply with its debt covenants, and general economic conditions. A downgrade in the Company's credit ratings could restrict the Company's ability to access debt capital markets and increase the Company's cost of debt. Any failure or inability

on the Company's part to borrow the required amounts of debt on satisfactory terms could impair its ability to repay maturing debt, fund capital expenditures and meet other obligations and requirements and, as a result, could have a material adverse effect on the Company.

Market, Financial Instrument and Credit Risk

Market risk refers primarily to the risk of loss that results from changes in costs, foreign exchange rates and interest rates, including potentially negative interest rates. The Company is exposed to fluctuations in interest rates as its regulated ROE is derived using a formulaic approach that takes into account anticipated interest rates. The Company issues debt from time to time to refinance maturing debt and for general corporate purposes. The Company is therefore exposed to fluctuations in interest rates in relation to such issuances of debt. Fluctuations in interest rates may also impact the funded position of Hydro One's Defined Benefit Pension Plan, and associated pension liability (See also "– Pension Plan Risk"). The Company is not currently exposed to material commodity price risk or material foreign exchange risk.

The OEB-approved adjustment formula for calculating ROE in a deemed regulatory capital structure of 60% debt and 40% equity provides for increases and decreases depending on changes in benchmark interest rates for Government of Canada debt and the A-rated utility corporate bond yield spread. For the transmission and distribution businesses in 2021, after transmission rates are set as part of a Custom Incentive Rate application, the OEB does not expect to address annual rate applications for updates to allowed ROE, so fluctuations will have no impact to net income. The Company has interest rate exposure associated with the refinancing of short- and long-term debt maturing in 2021 and beyond. The Company periodically uses interest rate swap agreements to mitigate elements of interest rate risk.

Financial assets create a risk that a counterparty will fail to discharge an obligation, causing a financial loss. Derivative financial instruments result in exposure to credit risk, since there is a risk of counterparty default. Hydro One monitors and minimizes credit risk through various techniques, including dealing with highly rated counterparties, limiting total exposure levels with individual counterparties, entering into agreements which enable net settlement, and by monitoring the financial condition of counterparties. The Company does not trade in any energy derivatives. The Company is required to procure electricity on behalf of competitive electricity retailers and certain local distribution companies for resale to their customers. The resulting concentrations of credit risk are mitigated through the use of various security arrangements, including letters of credit, which are incorporated into the Company's service agreements with these retailers in accordance with the OEB's Retail Settlement Code.

The failure to properly manage these risks could have a material adverse effect on the Company.

Risks Relating to Asset Condition, Capital Projects and Innovation

The Company continually incurs sustainment and development capital expenditures and monitors the condition of its assets to manage the risk of equipment failures and to determine the need for and timing of major refurbishments and replacements of its transmission and distribution infrastructure.

While traditionally a mature and stable industry, the electricity industry is facing rapid and dramatic technological change and increasing

innovation, the consequences of which could have a material adverse effect on the Company, including a reduction in revenue.

Execution of the Company's capital expenditure programs is partially dependent on external factors, such as OEB approvals, environmental approvals, municipal permits, equipment outage schedules that accommodate the IESO, generators and transmission-connected customers, other interrelated projects being on schedule, and supply chain availability for equipment suppliers and consulting services. Many of these external factors are beyond the Company's control. There may also be a need for, among other things, *Environmental Assessment Act* (Ontario) approvals, approvals which require public meetings, appropriate engagement with Indigenous communities, OEB approvals of expropriation or early access to property, and other activities. Obtaining approvals and carrying out these processes may also be impacted by opposition to the proposed site of the capital investments. Delays in obtaining required approvals or failure to complete capital projects on a timely basis could materially adversely affect transmission reliability or customers' service quality or increase maintenance costs which could have a material adverse effect on the Company. Failure to receive approvals for projects when spending has already occurred would result in the inability of the Company to recover the investment in the project as well as forfeit the anticipated return on investment. The assets involved may be considered impaired and result in the write off of the value of the asset, negatively impacting net income. If the Company is unable to carry out capital expenditure plans in a timely manner, equipment performance may degrade, which may reduce network capacity, result in customer interruptions, compromise the reliability of the Company's networks or increase the costs of operating and maintaining these assets. Any of these consequences could have a material adverse effect on the Company.

Increased competition for the development of large transmission projects and legislative changes relating to the selection of transmitters could impact the Company's ability to expand its existing transmission system, which may have an adverse effect on the Company. To the extent that other parties are selected to construct, own and operate new transmission assets, the Company's share of Ontario's transmission network would be reduced. Any delays in these new transmitters' projects may impact the Company's own projects that it is undertaking to in-service these new transmission assets.

Health and Safety Risk

Hydro One's work environment can be inherently dangerous and there is a risk to health and safety of both the public and our employees, as well as possible resultant operational and/or financial impacts. The Company is subject to federal and provincial legislation and regulations relating to health and safety. Findings of a failure to comply with these requirements could result in penalties and reputational risk, which could negatively impact the Company. Failure to comply could subject the Company to fines or other penalties. Any regulatory decision to disallow or limit the recovery of such costs could have a material adverse effect on the Company.

Pension Plan Risk

Hydro One has the Hydro One Defined Benefit Pension Plan in place for the majority of its employees. Contributions to the pension plan are established by actuarial valuations which are required to be filed with the Financial Services Regulatory Authority of Ontario on a triennial

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basis. The most recently filed valuation was prepared as at December 31, 2018, and was filed in September 2019, covering a three-year period from 2019 to 2021. Hydro One's contributions to its pension plan satisfy, and are expected to continue to satisfy, minimum funding requirements. Contributions beyond 2021 will depend on the funded position of the plan, which is determined by investment returns, interest rates and changes in benefits and actuarial assumptions at that time. A determination by the OEB that some of the Company's pension expenditures are not recoverable through rates could have a material adverse effect on the Company, and this risk may be exacerbated if the amount of required pension contributions increases.

Hydro One currently reports and recovers its pension costs on a cash basis, and maintains the accrual method with respect to OPEBs. Transitioning from the cash basis to an accrual method for pension costs may have material negative rate impacts for customers or material negative impacts on the Company should recovery of costs be disallowed by the OEB.

See also "– Regulatory Risks and Risks Relating to Hydro One's Revenues – Risk of Recoverability of Total Compensation Costs" for risks relating to recovery of pension costs.

Risk Associated with Outsourcing Arrangements

Hydro One has entered into an outsourcing arrangement with a third-party for the provision of back office and IT services. If the services are disrupted, it could have a material adverse effect on the Company. Additionally, if the outsourcing arrangement or statements of work thereunder are terminated for any reason or expire before a new supplier is selected and fully transitioned, the Company could be required to transfer to another service provider or insource, which could have a material adverse effect on the Company's business, operating results, financial condition or prospects.

Risk from Provincial Ownership of Transmission Corridors

The Province owns some of the corridor lands underlying the Company's transmission system. Although the Company has the statutory right to use these transmission corridors, the Company may be limited in its options to expand or operate its systems. Also, other uses of the transmission corridors by third parties in conjunction with the operation of the Company's systems may increase safety or environmental risks, which could have a material adverse effect on the Company.

Litigation Risks

In the normal course of the Company's operations, it becomes involved in, is named as a party to and is the subject of, various legal proceedings, including regulatory proceedings, tax proceedings and legal actions, relating to actual or alleged violations of law, common law damages claims, personal injuries, property damage, property taxes, land rights, the environment, contract disputes, claims by former employees and claims and proceedings by Indigenous groups. The outcome of outstanding, pending or future proceedings cannot be predicted with certainty and may be determined adversely to the Company, which could have a material adverse effect on the Company. Even if the Company prevails in any such legal proceeding, the proceedings could be costly and time-consuming and would divert the attention of management and key personnel from the Company's business operations, which could adversely affect the Company.

Transmission Assets on Third-Party Lands Risk

Some of the lands on which the Company's transmission assets are located are owned by third parties, including the Province and federal Crown, and are or may become subject to land claims by First Nations. The Company requires valid occupation rights to occupy such lands (which may take the form of land use permits, easements or otherwise). If the Company does not have valid occupational rights on third-party owned or controlled lands or has occupancy rights that are subject to expiry, it may incur material costs to obtain or renew such occupancy rights, or if such occupancy rights cannot be renewed or obtained it may incur material costs to remove and relocate its assets and restore the subject land. If the Company does not have valid occupancy rights and must incur costs as a result, this could have a material adverse effect on the Company or otherwise materially adversely impact the Company's operations.

Reputational, Public Opinion and Political Risk

Reputation risk is the risk of negative publicity or the public's negative perceptions towards Hydro One that may result in a detrimental impact to Hydro One's business, operations or financial condition leading to a deterioration of Hydro One's reputation. Hydro One's reputation could be negatively impacted by changes in public opinion, attitudes towards the Company's privatization, failure to deliver on its customer promises, failure to comply with mandatory reliability regulations established by the NERC and NPCC, failure to adequately respond to social issues raised by employees, partners and/or stakeholders and other external forces. Adverse reputational events or political actions could have a material adverse effect on Hydro One's business and prospects including, but not limited to, delays or denials of requisite approvals, such as denial of requested rates, and accommodations for Hydro One's planned projects, escalated costs, legal or regulatory action, and damage to stakeholder and community relationships. Any of these could have a material adverse impact on Hydro One and its business, financial condition and results of operations.

Risks Associated with Acquisitions

Acquisitions include inherent risks that some or all of the expected benefits may fail to materialize, or may not occur within the time periods anticipated, and Hydro One may incur material unexpected costs or liabilities. Realization of the anticipated benefits would depend, in part, on the Company's ability to successfully integrate the acquired business, including the requirement to devote management attention and resources to integrating business practices and support functions. The failure to realize the anticipated benefits, the diversion of management's attention, or any delays or difficulties encountered in connection with the integration could have an adverse effect on the Company's business, results of operations, financial condition or cash flows.

Risks Relating to the Common Shares of Hydro One Limited

Hydro One's Common Shares trade on the TSX. The trading price of the Common Shares has in the past been, and may in the future be, subject to significant fluctuations. These fluctuations may be caused by events or factors related or unrelated to Hydro One's operating performance and/or beyond its control, including: the risk factors described herein; general economic conditions within Ontario and Canada, including changes in interest rates; changes in electricity prices; changes in electricity demand; weather conditions; actual or anticipated

fluctuations in Hydro One's quarterly and annual results and the results of public companies similar to Hydro One; Hydro One's businesses, operations, results and prospects; Hydro One's reputation and its relationship with the Province; the timing and amount of dividends, if any, declared on the Common Shares; future issuances of Common Shares or other securities by Hydro One or Hydro One Inc.; Hydro One's relationship with its regulator; changes in government regulation, taxes, legal proceedings or other developments; shortfalls in Hydro One's operating results from levels forecasted by securities analysts; investor sentiment toward energy companies in general; maintenance of acceptable credit ratings or credit quality; the impact of COVID-19 on Hydro One and the Province; and the general state of the securities markets. These and other factors may impair the development or sustainability of a liquid market for the Common Shares and the ability of investors to sell Common Shares at an attractive price.

Risks Relating to the Company's Relationship with the Province

Ownership and Continued Influence by the Province and Voting Power; Share Ownership Restrictions

The Province currently owns approximately 47.3% of the outstanding common shares of Hydro One. The *Electricity Act* restricts the Province from selling voting securities of Hydro One (including common shares) of any class or series if it would own less than 40% of the outstanding number of voting securities of that class or series after the sale and in certain circumstances also requires the Province to take steps to maintain that level of ownership. Accordingly, the Province is expected to continue to maintain a significant ownership interest in voting securities of Hydro One for an indefinite period.

As a result of its significant ownership of the common shares of Hydro One, the Province has, and is expected indefinitely to have, the ability to determine or significantly influence the outcome of shareholder votes, subject to the restrictions in the Governance Agreement. Despite the terms of the Governance Agreement in which the Province has agreed to engage in the business and affairs of the Company as an investor and not as a manager, there is a risk that the Province's engagement in the business and affairs of the Company as an investor will be informed by its policy objectives and may influence the conduct of the business and affairs of the Company in ways that may not be aligned with the interests of other investors. Notwithstanding the Governance Agreement, and in light of actions historically taken by the Province, there can be no assurance that the Province will not take other actions in the future that could be detrimental to the interests of investors in Hydro One. See "Risks Relating to Government Action" above.

The share ownership restrictions in the *Electricity Act* (Share Ownership Restrictions) and the Province's significant ownership of common shares of Hydro One together effectively prohibit one or more persons acting together from acquiring control of Hydro One. They also may limit or discourage transactions involving other fundamental changes to Hydro One and the ability of other shareholders to successfully contest the election of the directors proposed for election pursuant to the Governance Agreement. The Share Ownership Restrictions may also discourage trading in, and may limit the market for, the common shares and other voting securities.

Nomination of Directors and Confirmation of CEO and Chair

Although director nominees (other than the CEO) are required to be independent of both the Company and the Province pursuant to the Governance Agreement, there is a risk that the Province will nominate or confirm individuals who satisfy the independence requirements but who it considers are disposed to support and advance its policy objectives and give disproportionate weight to the Province's interests in exercising their business judgment and balancing the interests of the stakeholders of Hydro One. This, combined with the fact certain matters require a two-thirds vote of the Board, could allow the Province to unduly influence certain Board actions such as confirmation of the Chair and confirmation of the CEO.

Board Removal Rights

Under the Governance Agreement, the Province has the right to withhold from voting in favour of all director nominees and has the right to seek to remove and replace the entire Board, including in each case its own director nominees but excluding the CEO and, at the Province's discretion, the Chair. In exercising these rights in any particular circumstance, the Province is entitled to vote in its sole interest, which may not be aligned with the interests of other stakeholders of Hydro One.

More Extensive Regulation

Although under the Governance Agreement, the Province has agreed to engage in the business and affairs of Hydro One as an investor and not as a manager and has stated that its intention is to achieve its policy objectives through legislation and regulation as it would with respect to any other utility operating in Ontario, there is a risk that the Province will exercise its legislative and regulatory power to achieve policy objectives in a manner that has a material adverse effect on the Company. See "Risks Relating to Government Action" above.

Prohibitions on Selling the Company's Transmission or Distribution Business

The *Electricity Act* prohibits the Company from selling all or substantially all of the business, property or assets related to its transmission system or distribution system that is regulated by the OEB. There is a risk that these prohibitions may limit the ability of the Company to engage in sale transactions involving a substantial portion of either system, even where such a transaction may otherwise be considered to provide substantial benefits to the Company and the holders of the common shares.

Future Sales of Common Shares by the Province

Although the Province has indicated that it does not intend to sell further common shares of Hydro One, the registration rights agreement between Hydro One and the Province dated November 5, 2015 (available on SEDAR at www.sedar.com) grants the Province the right to request that Hydro One file one or more prospectuses and take other procedural steps to facilitate secondary offerings by the Province of the common shares of Hydro One. Future sales of common shares of Hydro One by the Province, or the perception that such sales could occur, may materially adversely affect market prices for these common shares and impede Hydro One's ability to raise capital through the issuance of additional common shares, including the number of common shares that Hydro One may be able to sell at a particular time or the total proceeds that may be realized.

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Limitations on Enforcing the Governance Agreement

The Governance Agreement includes commitments by the Province restricting the exercise of its rights as a holder of voting securities, including with respect to the maximum number of directors that the Province may nominate and on how the Province will vote with respect to other director nominees. Hydro One's ability to obtain an effective remedy against the Province, if the Province were not to comply with these commitments, is limited as a result of the *Proceedings Against the Crown Act* (Ontario). This legislation provides that the remedies of injunction and specific performance are not available against the Province, although a court may make an order declaratory of the rights of the parties, which may influence the Province's actions. A remedy of damages would be available to Hydro One, but damages may not be an effective remedy, depending on the nature of the Province's non-compliance with the Governance Agreement.

Critical Accounting Estimates and Judgments

The preparation of Hydro One Consolidated Financial Statements requires the Company to make key estimates and critical judgments that affect the reported amounts of assets, liabilities, revenues and costs, and related disclosures of contingencies. Hydro One bases its estimates and judgments on historical experience, current conditions and various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities, as well as identifying and assessing the Company's accounting treatment with respect to commitments and contingencies. Actual results may differ from these estimates and judgments. Hydro One has identified the following critical accounting estimates used in the preparation of its Consolidated Financial Statements:

Revenues

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. At the end of each month, electricity delivered to customers since the date of the last billed meter reading is estimated, and the corresponding unbilled revenue is recorded. The unbilled revenue estimate is affected by energy consumption, weather, and changes in the composition of customer classes.

Regulatory Assets and Liabilities

Hydro One's regulatory assets represent certain amounts receivable from future electricity customers and costs that have been deferred for accounting purposes because it is probable that they will be recovered in future rates. The regulatory assets mainly include amounts related to the deferred income taxes, pension benefit liability, post-retirement and post-employment benefits, post-retirement and post-employment non-service costs, share-based compensation costs, foregone revenue, and environmental liabilities. The Company's regulatory liabilities represent certain amounts that are refundable to future electricity customers. They pertain primarily to deferral and variance accounts. The regulatory assets and liabilities can be recognized for rate-setting and financial reporting purposes only if the amounts have been approved for inclusion in the electricity rates by the OEB, or if such approval is judged to be probable by management. If, at some future date, management judges that it is no longer probable that the OEB will allow the

inclusion of a regulatory asset or liability in future electricity rates, the appropriate carrying amount would be reflected in results of operations prospectively from the date the Company's assessment is made, unless the change meets the requirements for a subsequent event adjustment.

Environmental Liabilities

Hydro One records a liability for the estimated future expenditures associated with the removal and destruction of polychlorinated biphenyl (PCB)-contaminated insulating oils and related electrical equipment, and for the assessment and remediation of chemically contaminated lands. 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. 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. Environmental liabilities are reviewed annually or more frequently if significant changes in regulations or other relevant factors occur. Estimate changes are accounted for prospectively.

Employee Future Benefits

Hydro One's employee future benefits consist of pension and post-retirement and post-employment plans, and include pension, group life insurance, health care, and long-term disability benefits provided to the Company's current and retired employees. Employee future benefits costs are included in Hydro One's labour costs that are either charged to results of operations or capitalized as part of the cost of property, plant and equipment and intangible assets. Changes in assumptions affect the benefit obligation of the employee future benefits and the amounts that will be charged to results of operations or capitalized in future years. The following significant assumptions and estimates are used to determine employee future benefit costs and obligations:

Weighted Average Discount Rate

The weighted average discount rate used to calculate the employee future benefits obligation is determined at each year end by referring to the most recently available market interest rates based on "AA"-rated corporate bond yields reflecting the duration of the applicable employee future benefit plan. The discount rate at December 31, 2020 decreased to 2.60% (from 3.10% at December 31, 2019) for pension benefits and decreased to 2.60% (from 3.10% at December 31, 2019) for the post-retirement and post-employment plans. The decrease in the discount rate has resulted in a corresponding increase in employee future benefits liabilities for the pension, post-retirement and post-employment plans for accounting purposes. The liabilities are determined by independent actuaries using the projected benefit method prorated on service and based on assumptions that reflect management's best estimates.

Expected Rate of Return on Plan Assets

The expected rate of return on pension plan assets of 5.75% is based on expectations of long-term rates of return at the beginning of the year and reflects the current pension plan asset mix. A new investment policy was adopted by Hydro One effective May 14, 2018 and is being implemented over several years. Notably this includes the move to real estate and infrastructure and the removal of specific regional equity and fixed income mandates. Hydro One's current expectation is that the new policy asset mix will not be fully implemented until 2021-2022. The expected rate of return for the December 31, 2020 disclosures and the 2021 registered pension plan expense is based on the plan's ultimate target asset mix.

Rates of return on the respective portfolios are determined with reference to respective published market indices. The expected rate of return on pension plan assets reflects the Company's long-term expectations. The Company believes that this assumption is reasonable because, with the pension plan's balanced investment approach, the higher volatility of equity investment returns is intended to be offset by the greater stability of fixed-income and short-term investment returns. The net result, on a long-term basis, is a lower return than might be expected by investing in equities alone. In the short term, the pension plan can experience fluctuations in actual rates of return.

Rate of Cost of Living Increase

The rate of cost of living increase is determined by considering differences between long-term Government of Canada nominal bonds and real return bonds, which increased from 1.30% per annum as at December 31, 2019 to approximately 1.40% per annum as at December 31, 2020. Based on the Bank of Canada's commitment to keep long-term inflation between 1.00% and 3.00%, in addition to current and anticipated trends, management believes that a long-term assumption of 1.75% per annum is reasonable for employee future benefits liability valuation purposes as at December 31, 2020 (2.00% per annum was used for the purpose of December 31, 2019 disclosures and 2020 benefit cost).

Salary Increase Assumptions

Salary increases should reflect general wage increases plus an allowance for merit and promotional increases for current members of the plan and should be consistent with the assumptions for consumer price inflation and real wage growth in the economy. The merit and promotion scale was developed based on the salary increase assumption review performed in 2017. The review considers actual salary experience from 2002 to 2016 using valuation data for all active members as at December 31, 2016, based on age and service and Hydro One's expectation of future salary increases. Additionally, the salary scale reflects negotiated salary increases over the contract period as well as slightly lower expected increases in the short-term.

Mortality Assumptions

The Company's employee future benefits liability is also impacted by changes in life expectancies used in mortality assumptions. Increases in life expectancies of plan members result in increases in the employee future benefits liability. The mortality assumption used at December 31, 2020 is 95% of 2014 Canadian Pensioners Mortality Private Sector table projected generationally using improvement Scale B.

Rate of Increase in Health Care Cost Trends

The costs of post-retirement and post-employment benefits are determined at the beginning of the year and are based on assumptions for expected claims experience and future health care cost inflation. For the post-retirement benefit plans, a trend study of historical Hydro One experience was conducted in 2017. The health and dental trends reflect this study as well as slightly lower expected increases in long-term inflation.

Disclosure Controls and Procedures and Internal Control Over Financial Reporting

Disclosure controls and procedures are the processes designed to ensure that information is recorded, processed, summarized and reported on a timely basis to the Company's management, including its CEO and CFO, as appropriate, to make timely decisions regarding required disclosure in the MD&A and financial statements. At the direction of the Company's CEO and CFO, management evaluated disclosure controls and procedures as of the end of the period covered by this report. Based on that evaluation, management concluded that the Company's disclosure controls and procedures were effective as at December 31, 2020.

Internal control over financial reporting is designed by, or under the direction of the CEO and CFO to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with US GAAP. The Company's internal control over financial reporting framework includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and disposition of the assets of the Company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with US GAAP, and that receipts and expenditures of the Company are being made only in accordance with authorization of management and directors of the Company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Company's assets that could have a material effect on the Company's consolidated financial statements.

The Company's management, at the direction of the CEO and CFO, evaluated the effectiveness of the design and operation of internal control over financial reporting based on the criteria established in the Internal Control – Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based

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on that evaluation, management concluded that the Company's internal control over financial reporting was effective as at December 31, 2020.

Internal control, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives and due to its inherent limitations, may not prevent or detect all misrepresentations. Furthermore, the effectiveness of internal control is affected by change and subject to the risk that internal control effectiveness may change over time.

There were no changes in the design of the Company's internal control over financial reporting during the three months ended December 31, 2020 that have materially affected, or are reasonably likely to materially affect, the operation of the Company's internal control over financial reporting.

Management will continue to monitor its systems of internal control over reporting and disclosure and may make modifications from time to time as considered necessary.

New Accounting Pronouncements

The following tables present Accounting Standards Updates (ASUs) issued by the Financial Accounting Standards Board (FASB) that are applicable to Hydro One:

Recently Adopted Accounting Guidance

| Guidance | Date issued | Description | Effective date | Impact on Hydro One |
|-------------|--------------|--|-----------------|-------------------------|
| ASU 2017-04 | January 2017 | The amendment removes the second step of the previous two-step goodwill impairment test to simplify the process of testing goodwill. | January 1, 2020 | No impact upon adoption |
| ASU 2018-13 | August 2018 | Disclosure requirements on fair value measurements in Accounting Standard Codification (ASC) 820 are modified to improve the effectiveness of disclosures in financial statement notes. | January 1, 2020 | No impact upon adoption |
| ASU 2019-01 | March 2019 | This amendment carries forward the exemption previously provided under ASC 840 relating to the determination of the fair value of underlying assets by lessors that are not manufacturers or dealers. It also provides for clarification on cash-flow presentation of sales-type and financing leases and clarifies that transition disclosures under Topic 250 are applicable in the adoption of ASC 842. | January 1, 2020 | No impact upon adoption |

Recently Issued Accounting Guidance Not Yet Adopted

| Guidance | Date issued | Description | Effective date | Anticipated Impact on Hydro One |
|-------------|---------------|--|-----------------|---------------------------------|
| ASU 2018-14 | August 2018 | Disclosure requirements related to single-employer defined benefit pension or other post-retirement benefit plans are added, removed or clarified to improve the effectiveness of disclosures in financial statement notes. | January 1, 2021 | No impact upon adoption |
| ASU 2019-12 | December 2019 | The amendments simplify the accounting for income taxes by removing certain exceptions to the general principles and improving consistent application of Topic 740 by clarifying and amending existing guidance. | January 1, 2021 | No impact upon adoption |
| ASU 2020-01 | January 2020 | The amendments clarify the interaction of the accounting for equity securities under Topic 321, investments under the equity method of accounting in Topic 323 and the accounting for certain forward contracts and purchased options accounted for under Topic 815. | January 1, 2021 | No impact upon adoption |
| ASU 2020-06 | August 2020 | The update addresses the complexity associated with applying GAAP for certain financial instruments with characteristics of liabilities and equity. The amendments reduce the number of accounting models for convertible debt instruments and convertible preferred stock. | January 1, 2022 | Under assessment |
| ASU 2020-10 | October 2020 | The amendments are intended to improve the Codification by ensuring the guidance required for an entity to disclose information in the notes of financial statements are codified in the disclosure sections to reduce the likelihood of disclosure requirements being missed. | January 1, 2021 | No impact upon adoption |

Summary of Fourth Quarter Results of Operations

| Three months ended December 31 (millions of dollars, except EPS) | 2020 | 2019 | Change |
|--|--------------|--------------|----------------|
| Revenues | | | |
| Distribution | 1,457 | 1,298 | 12.2% |
| Transmission | 398 | 407 | (2.2%) |
| Other | 12 | 10 | 20.0% |
| | 1,867 | 1,715 | 8.9% |
| Costs | | | |
| Purchased power | 1,046 | 914 | 14.4% |
| OM&A | | | |
| Distribution | 185 | 162 | 14.2% |
| Transmission | 73 | 59 | 23.7% |
| Other | 15 | 18 | (16.7%) |
| | 273 | 239 | 14.2% |
| Depreciation, amortization and asset removal costs | 239 | 226 | 5.8% |
| | 1,558 | 1,379 | 13.0% |
| Income before financing charges and income tax expense | 309 | 336 | (8.0%) |
| Financing charges | 119 | 116 | 2.6% |
| Income before income tax expense | 190 | 220 | (13.6%) |
| Income tax expense | 27 | 2 | 1,250.0% |
| Net income | 163 | 218 | (25.2%) |
| Net income to common shareholders of Hydro One | 161 | 211 | (23.7%) |
| Adjusted net income to common shareholders of Hydro One¹ | 161 | 211 | (23.7%) |
| Basic EPS | \$ 0.27 | \$ 0.35 | (22.9%) |
| Diluted EPS | \$ 0.27 | \$ 0.35 | (22.9%) |
| Basic Adjusted EPS ¹ | \$ 0.27 | \$ 0.35 | (22.9%) |
| Diluted Adjusted EPS ¹ | \$ 0.27 | \$ 0.35 | (22.9%) |
| Assets Placed In-Service | | | |
| Distribution | 308 | 271 | 13.7% |
| Transmission | 565 | 573 | (1.4%) |
| Other | 5 | 5 | 0.0% |
| | 878 | 849 | 3.4% |
| Capital Investments | | | |
| Distribution | 210 | 249 | (15.7%) |
| Transmission | 361 | 311 | 16.1% |
| Other | 6 | 2 | 200.0% |
| | 577 | 562 | 2.7% |

¹ See section "Non-GAAP Measures" for description and reconciliation of adjusted net income, and basic and diluted Adjusted EPS.

Net Income

Net income attributable to common shareholders for the quarter ended December 31, 2020 of \$161 million is a decrease of \$50 million or 23.7% from the prior year. Significant influences on net income included:

- higher revenues, net of purchased power, primarily resulting from:
 - an increase in distribution revenues, net of purchased power, mainly due to the OEB's decision on 2020 rates, as well as revenues related to the Peterborough Distribution and Orillia Power acquisitions which closed during the third quarter of 2020; partially offset by
 - a decrease in transmission revenues primarily due to lower peak demand, partially offset by the OEB's decision on 2020 rates.
- higher OM&A costs primarily resulting from:
 - COVID-19 related expenses, as discussed below,
 - lower insurance proceeds received in 2020; and
 - additional OPEB costs that are recognized in OM&A following the 2020-2022 OEB transmission decision and recovered in rates, therefore net income neutral;
- higher depreciation, amortization and asset removal costs in 2020 mainly due to the growth in capital assets and timing of asset removal costs.
- higher income tax expense primarily attributable to the following:
 - lower net tax deductions primarily related to tax depreciation in excess of depreciation, as well as additional tax on recovery

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of certain OPEB costs through OM&A that were previously capitalized; and

- lower incremental tax deductions from deferred tax asset sharing mainly due to the 2018 foregone distribution revenue recognized in March 2019 following the receipt of the OEB decision on rates; partially offset by
- lower income before taxes.

Included in the Company's results for the quarter ended December 31, 2020 are costs incurred as a result of the COVID-19 pandemic. Total COVID-19 related costs in the quarter of \$18 million consist primarily of the recognition of the bad debt provision following the issuance of the OEB staff proposal in December 2020, and direct expenses.

For additional disclosure related to the impact of COVID-19 on the Company's operations please see section "Other Developments – COVID-19".

EPS and Adjusted EPS

EPS and adjusted EPS was \$0.27 in the fourth quarter of 2020, compared to EPS and adjusted EPS of \$0.35 in the fourth quarter of 2019. The decrease in EPS and adjusted EPS was driven by lower earnings for the fourth quarter of 2020, as discussed above. See section "Non-GAAP Measures" for description and reconciliation of Adjusted EPS.

Revenues

The year-over-year decrease of \$9 million or 2.2% in quarterly transmission revenues was primarily due to the following:

- lower peak demand driven by unfavourable weather in the fourth quarter of 2020, partially offset by
- the OEB's decision on 2020 rates, including the recovery of certain OPEB costs through OM&A that were previously capitalized and recovered in rates, therefore net income neutral, and a deferred regulatory adjustment related to asset removal costs in 2020.

The year-over-year increase of \$27 million or 7.0% in quarterly distribution revenues, net of purchased power, was primarily due to the following:

- the OEB's decision on 2020 rates,
- higher revenues related to the Peterborough Distribution and Orillia Power acquisitions which closed during the third quarter of 2020, and
- a lower deferred regulatory adjustment related to the Earnings Sharing Mechanism in 2020.

See section "Non-GAAP Measures" for description and reconciliation of revenues, net of purchased power.

OM&A Costs

The year-over-year increase of \$14 million or 23.7% in quarterly transmission OM&A costs was primarily due to the following:

- lower insurance proceeds received in 2020,
- additional OPEB costs that are recognized in OM&A following the 2020-2022 OEB transmission decision and recovered in rates, therefore net income neutral, and
- costs related to COVID-19.

The year-over-year increase of \$23 million or 14.2% in quarterly distribution OM&A costs was primarily due to the following:

- costs related to COVID-19, consisting primarily of the recognition of the bad debt provision following the issuance of the OEB staff proposal in December 2020, and direct expenses, as well as
- higher corporate support costs.

Depreciation, Amortization and Asset Removal Costs

The increase of \$13 million or 5.8% in depreciation, amortization and asset removal costs in the fourth quarter of 2020 was mainly due to the growth in capital assets and timing of asset removal costs.

Financing Charges

The \$3 million or 2.6% year-over-year increase in financing charges for the quarter ended December 31, 2020 was primarily attributable to:

- higher interest expense on long-term debt as a result of increased debt levels largely driven by the debt issuances completed in the last quarter of 2020; partially offset by
- lower interest expense on short-term notes due to lower interest rate in the current year.

Income Taxes

Income tax expense for the fourth quarter of 2020 increased by \$25 million compared to the same period in 2019. This resulted in a realized ETR of approximately 14.2% in the fourth quarter of 2020, compared to approximately 0.9% in the fourth quarter of the prior year.

The increase in income tax expense for the three months ended December 31, 2020 was primarily attributable to:

- lower net tax deductions primarily related to tax depreciation in excess of depreciation, as well as additional tax on recovery of certain OPEB costs through OM&A that were previously capitalized; and
- lower incremental tax deductions from deferred tax asset sharing mainly due to the 2018 foregone distribution revenue recognized in March 2019 following the receipt of the OEB decision on rates; partially offset by
- lower income before taxes.

Assets Placed In-Service

The decrease in transmission assets placed in-service during the fourth quarter was primarily due to the following:

- substantial investment placed in-service for the new Leamington transmission station in 2019;
- lower volume of demand work due to equipment failures; and
- lower volume of assets placed in-service for IT projects; partially offset by
- timing of assets placed in-service for station sustainment investments; and
- higher volume of overhead lines and component replacements in 2020.

The increase in distribution assets placed in-service during the fourth quarter was primarily due to the following:

- completion of Customer Contact Centre Technology Modernization project;

- completion of Woodstock Operation Centre; and
- higher volume of storm related asset replacements; partially offset by
- lower volume of distribution station refurbishments and equipment replacements; and
- timing of assets placed in-service for system capability reinforcement projects.

Capital Investments

The increase in transmission capital investments during the fourth quarter was primarily due to the following:

- higher investments in multi-year development projects, including investments in the new Lakeshore switching station;
- higher volume of station refurbishments and replacements;
- investment in the new Ontario grid control centre in the City of Orillia; and
- higher volume of work required to adhere to the NERC Critical Infrastructure Protection standards; partially offset by
- lower volume of transportation and work equipment investments.

The decrease in distribution capital investments during the fourth quarter was primarily due to the following:

- lower investments in system capability reinforcement projects;
- lower spend on work for customer connections;
- lower volume of transportation and work equipment investments; partially offset by
- investment in the new Ontario grid control centre in the City of Orillia; and
- investment in the new Woodstock Operation Centre.

Hydro One Holdings Limited – Consolidating Summary Financial Information

Hydro One Limited fully and unconditionally guarantees the payment obligations of its wholly-owned subsidiary Hydro One Holdings Limited (HOHL) issuable under the short form base shelf prospectus dated December 17, 2020. Accordingly, the following consolidating summary financial information is provided in compliance with the requirements of section 13.4 of National Instrument 51-102 – *Continuous Disclosure Obligations* providing for an exemption for certain credit support issuers. The tables below contain consolidating summary financial information as at and for the years ended December 31, 2020 and December 31, 2019 for: (i) Hydro One Limited; (ii) HOHL; (iii) the subsidiaries of Hydro One Limited, other than HOHL, on a combined basis, (iv) consolidating adjustments, and (v) Hydro One Limited and all of its subsidiaries on a consolidated basis, in each case for the periods indicated. Such summary financial information is intended to provide investors with meaningful and comparable financial information about Hydro One Limited and its subsidiaries. This summary financial information should be read in conjunction with Hydro One Limited's most recently issued annual financial statements. This summary financial information has been prepared in accordance with US GAAP, as issued by the FASB.

| Year ended December 31 (millions of dollars) | Hydro One Limited | | HOHL | | Subsidiaries of Hydro One Limited, other than HOHL | | Consolidating Adjustments | | Total Consolidated Amounts of Hydro One Limited | |
|---|-------------------|-------|------|------|--|-------|---------------------------|-------|---|-------|
| | 2020 | 2019 | 2020 | 2019 | 2020 | 2019 | 2020 | 2019 | 2020 | 2019 |
| Revenue | 9 | 17 | – | – | 7,694 | 6,775 | (413) | (312) | 7,290 | 6,480 |
| Net Income (Loss) Attributable to Common Shareholders | (7) | (133) | – | (19) | 2,127 | 1,188 | (350) | (258) | 1,770 | 778 |

| Year ended December 31 (millions of dollars) | Hydro One Limited | | HOHL | | Subsidiaries of Hydro One Limited, other than HOHL | | Consolidating Adjustments | | Total Consolidated Amounts of Hydro One Limited | |
|---|-------------------|-------|------|------|--|--------|---------------------------|----------|---|--------|
| | 2020 | 2019 | 2020 | 2019 | 2020 | 2019 | 2020 | 2019 | 2020 | 2019 |
| Current Assets | 97 | 84 | – | – | 3,446 | 2,440 | (1,554) | (1,256) | 1,989 | 1,268 |
| Non-Current Assets | 3,426 | 3,979 | – | – | 44,408 | 41,188 | (19,529) | (19,374) | 28,305 | 25,793 |
| Current Liabilities | 454 | 408 | – | – | 4,066 | 3,925 | (1,541) | (1,246) | 2,979 | 3,087 |
| Non-Current Liabilities | 423 | – | – | – | 28,810 | 25,201 | (12,546) | (11,096) | 16,687 | 14,105 |

Forward-looking Statements and Information

The Company's oral and written public communications, including this document, often contain forward-looking statements that are based on current expectations, estimates, forecasts and projections about the Company's business, the industry, regulatory and economic environments in which it operates, and includes beliefs and assumptions made by the management of the Company. Such statements include, but are not limited to, statements regarding: the Company's transmission and distribution rate applications, including resulting decisions, rates, recovery and expected impacts and timing; expectations about the Company's liquidity and capital resources and operational requirements, including as a result of COVID-19; the Operating Credit Facilities; expectations regarding the Company's financing activities; the Company's maturing debt; the Company's derivative instruments; the Company's ongoing and planned projects, initiatives and expected capital investments, including expected results, costs and in-service and completion dates; the potential impact of delays on the Company's transmission in-service additions; the potential impact of COVID-19 on the Company's business and operations, including its impact on peak demand and electricity consumption, capital programs, supply chains, costs, allowance for doubtful accounts, foregone revenues, deferral accounts and the likelihood of recovery of certain costs in future rates; the Company's priorities in its response to COVID-19; contractual obligations and other commercial commitments; expected impacts relating to the deferred tax asset and the OEB's treatment thereof, including expected timing for the OEB's final decision in respect thereof and the Company's recognition of deferred tax regulatory assets, deferred tax liabilities and net income results; expectations relating to the recoverability of incremental costs and lost revenues from ratepayers in connection with the COVID-19 pandemic; expectations regarding the Company's ETR over the next five years; the impact of the Ontario Budget and the Ontario Electricity Rebate on customers; Bill 222 and its expected impacts; the number of Hydro One common shares issuable in connection with outstanding awards under the share grant plans and the LTIP; collective agreements and expectations regarding the ability to negotiate renewal collective agreements consistent with rate orders; the pension plan, future pension contributions, valuations and expected impacts; dividends; non-GAAP measures; risks relating to infectious disease outbreak, such as COVID-19; internal controls over financial reporting and disclosure; the MTN Program; the Universal Base Shelf Prospectus; the US Debt Shelf Prospectus; and the Company's acquisitions and mergers. Words such as "expect", "anticipate", "intend", "attempt", "may", "plan", "will", "would", "believe", "seek", "estimate", "goal", "aim", "target", 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. Hydro One does not intend, and it disclaims 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: the scope of the COVID-19 pandemic and duration thereof as well as the effect and severity of corporate and other mitigation measures on the Company's operations, supply chain or employees; no unforeseen changes in the

legislative and operating framework for Ontario's electricity market or for Hydro One specifically; favourable decisions from the OEB and other regulatory bodies concerning outstanding and future rate and other applications; no unexpected delays in obtaining the required approvals; no unforeseen changes in rate orders or rate setting methodologies for the Company's distribution and transmission businesses; continued use of US GAAP; a stable regulatory environment; no unfavourable changes in environmental regulation; no significant changes to the Company's current credit ratings; no unforeseen impacts of new accounting pronouncements; no changes to expectations regarding electricity consumption; no unforeseen changes to economic and market conditions; recoverability of costs and expenses related to the COVID-19 pandemic, including the costs of customer defaults resulting from the pandemic; completion of operating and capital projects that have been deferred; and no significant event occurring outside the ordinary course of business. These assumptions are based on information currently available to the Company, including information obtained from third-party sources. Actual results may differ materially from those predicted by such forward-looking statements. While Hydro One does not know what impact any of these differences may have, the Company's business, results of operations, financial condition and 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:

- a significant expansion in length or severity of the COVID-19 pandemic restricting or prohibiting the Company's operations or significantly impacting the Company's supply chain or workforce;
- severity of mitigation measures related to the COVID-19 pandemic;
- delays in completion of and increases in costs of operating and capital projects;
- regulatory risks and risks relating to Hydro One's revenues, including risks relating to rate orders and the rate-setting models for transmission and distribution, actual performance against forecasts and capital expenditures, competition with other transmitters and other applications to the OEB, the regulatory treatment of the deferred tax asset, the recoverability of total compensation costs or denials of applications;
- risks associated with the Province's share ownership of Hydro One and other relationships with the Province, including potential conflicts of interest that may arise between Hydro One, the Province and related parties, risks associated with the Province's exercise of further legislative and regulatory powers in the implementation of the *Hydro One Accountability Act*, risks relating to the ability of the Company to attract and retain qualified executive talent or the risk of a credit rating downgrade for the Company and its impact on the Company's funding and liquidity;
- risks relating to the location of the Company's assets on Reserve lands and the risk that Hydro One may incur significant costs associated with transferring assets located on Reserves;
- the risk that the Company may be unable to comply with regulatory and legislative requirements or that the Company may incur additional costs for compliance that are not recoverable through rates;
- the risk of exposure of the Company's facilities to the effects of severe weather conditions, natural disasters, man-made events or

other unexpected occurrences for which the Company is uninsured or for which the Company could be subject to claims for damage;

- the risk of non-compliance with environmental regulations and inability to recover environmental expenditures in rate applications and the risk that assumptions that form the basis of the Company's recorded environmental liabilities and related regulatory assets may change;
- risks associated with information system security and maintaining complex information technology (IT) and operational technology (OT) system infrastructure, including system failures or risks of cyber-attacks or unauthorized access to corporate IT and OT systems;
- the risk of labour disputes and inability to negotiate or renew appropriate collective agreements on acceptable terms consistent with the Company's rate decisions;
- risks related to the Company's workforce demographic and its potential inability to attract and retain qualified personnel;
- the risk that the Company is not able to arrange sufficient cost-effective financing to repay maturing debt and to fund capital expenditures;
- risks associated with fluctuations in interest rates and failure to manage exposure to credit and financial instrument risk;
- risks associated with economic uncertainty and financial market volatility;
- the risk that the Company may not be able to execute plans for capital projects necessary to maintain the performance of the Company's assets or to carry out projects in a timely manner or the risk of increased competition for the development of large transmission projects or legislative changes affecting the selection of transmitters;
- risks associated with asset condition, capital projects and innovation, including public opposition to or delays or denials of the requisite approvals and accommodations for the Company's planned projects;
- the risk of failure to mitigate significant health and safety risks;
- the risk of not being able to recover the Company's pension expenditures in future rates and uncertainty regarding the future

regulatory treatment of pension, other post-employment benefits and post-retirement benefits costs;

- the potential that Hydro One may incur significant expenses to replace functions currently outsourced if agreements are terminated or expire before a new service provider is selected;
- the impact of the ownership by the Province of lands underlying the Company's transmission system;
- the risk associated with legal proceedings that could be costly, time-consuming or divert the attention of management and key personnel from the Company's business operations;
- the impact if the Company does not have valid occupational rights on third-party owned or controlled lands and the risks associated with occupational rights of the Company that may be subject to expiry;
- risks relating to adverse reputational events or political actions;
- risks relating to acquisitions, including the failure to realize anticipated benefits of such transaction at all, or within the time periods anticipated, and unexpected costs incurred in relation thereto;
- the inability to prepare financial statements using US GAAP; and
- the risk related to the impact of any new accounting pronouncements.

Hydro One cautions the reader that the above list of factors is not exhaustive. Some of these and other factors are discussed in more detail in the section entitled "Risk Management and Risk Factors" in this MD&A.

In addition, Hydro One cautions the reader that information provided in this MD&A regarding the Company's outlook on certain matters, including potential future investments, is provided in order to give context to the nature of some of the Company's future plans and may not be appropriate for other purposes.

Additional information about Hydro One, including the Company's Annual Information Form, is available on SEDAR at www.sedar.com, the US Securities and Exchange Commission's EDGAR website at www.sec.gov/edgar.shtml, and the Company's website at www.HydroOne.com/Investors.

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 Limited (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.

Management is responsible for establishing and maintaining adequate disclosure controls and procedures and internal control over financial reporting as described in the annual MD&A. Management evaluated the effectiveness of the design and operation of disclosure controls and procedures and internal control over financial reporting based on the framework and criteria established in the Internal Control – Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on that evaluation, management concluded that the Company's internal control over financial reporting was effective at a reasonable level of assurance as of December 31, 2020. As required, the results of that evaluation were reported to the Audit Committee of the Hydro One Board of Directors and the external auditors.

The Consolidated Financial Statements have been audited by KPMG LLP, independent external auditors appointed by the shareholders of the Company. The external auditors' responsibility is to express their opinion on whether the Consolidated Financial Statements are fairly presented in all material respects 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 fulfils its responsibilities for financial reporting and internal control over reporting and disclosure. 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.

On behalf of Hydro One's management:



Mark Poweska
President and Chief Executive Officer



Christopher Lopez
Chief Financial Officer

Report of Independent Registered Public Accounting Firm

To the Shareholders and Board of Directors of Hydro One Limited

Opinion on the Consolidated Financial Statements

We have audited the accompanying consolidated balance sheets of Hydro One Limited (the Company) as of December 31, 2020 and 2019, the related consolidated statements of operations and comprehensive income, changes in equity, and cash flows for each of the years in the two-year period ended December 31, 2020, and the related notes (collectively, the consolidated financial statements). In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2020 and 2019, and the results of its operations and its cash flows for each of the years in the two-year period ended December 31, 2020, in conformity with U.S. generally accepted accounting principles.

Basis for Opinion

These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (PCAOB) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement, whether due to error or fraud. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. As part of our audits, we are required to obtain an understanding of internal control over financial reporting but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion.

Our audits included performing procedures to assess the risks of material misstatement of the consolidated financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the consolidated financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. We believe that our audits provide a reasonable basis for our opinion.

Critical Audit Matter

The critical audit matter communicated below is a matter arising from the current period audit of the consolidated financial statements that was communicated or required to be communicated to the audit committee and that: (1) relates to accounts or disclosures that are material to the consolidated financial statements and (2) involved our especially challenging, subjective, or complex judgments. The communication of a critical audit matter does not alter in any way our opinion on the consolidated financial statements, taken as a whole, and we are not, by communicating the critical audit matter below, providing a separate opinion on the critical audit matter or on the accounts or disclosures to which it relates.

Evaluation of regulatory assets and liabilities and the impact of rate regulation on the consolidated financial statements

As discussed in Note 2 to the consolidated financial statements, the Company accounts for its regulated operations in accordance with Financial Accounting Standards Board Accounting Standard

Codification Topic 980, Regulated Operations (ASC 980). Under ASC 980, the actions of the Company's regulator may result in the recognition of revenue and costs in time periods that are different than non-rate-regulated enterprises. When this occurs, the Company records incurred and accrued costs that it has assessed are probable of recovery in future electricity rates as regulatory assets. Obligations imposed or probable to be imposed by the regulator to refund previously collected revenue or to spend revenue collected from customers on future costs are recorded as regulatory liabilities. Under ASC 980, the carrying amounts of property, plant and equipment are impacted by the regulator's actions to the extent that incurred costs are allowed or disallowed to be recovered for rate-making purposes. As disclosed in Note 13 to the consolidated financial statements, as of December 31, 2020, the Company's regulatory assets were \$4,676 million and regulatory liabilities were \$297 million.

We identified the evaluation of regulatory assets and liabilities and the impact of rate regulation as a critical audit matter. Accounting for regulated operations under ASC 980 affects multiple financial statement accounts and disclosures in the Company's consolidated financial statements. Assessing the accounting for regulated operations requires industry knowledge and significant auditor judgment due to interpretations of regulatory decisions and judgments involved in evaluating the Company's assessment of the probability associated with recovery of regulatory assets and property, plant and equipment, and imposition of regulatory liabilities.

The following are the primary procedures we performed to address this critical audit matter. We evaluated the design and tested the operating effectiveness of certain internal controls over the Company's regulatory accounting process. This included controls over the evaluation of the probability of (1) the recovery in future rates of costs deferred as regulatory assets, and (2) a refund or a future reduction in rates that should be reported as regulatory liabilities, and controls over the monitoring and evaluation of regulatory developments that may affect the probability of recovering costs in future rates or imposing of regulatory liabilities. We evaluated the Company's assessment of the probability of recovery of the carrying amount of regulatory assets and property, plant and equipment and the disposition of regulatory liabilities, through consideration of selected on-going regulatory proceedings and decisions. For a selection of regulatory proceedings and decisions, we read the Company's assessment and interpretations and any written advice of management's external specialists with respect to the selected assessments and interpretations. For a selection of regulatory assets and liabilities, we recalculated the amounts recorded based on methodologies approved by the regulator and agreed the data used in the calculations to the Company's underlying books and records. We compared the amounts calculated by the Company to the amounts recorded in the consolidated financial statements.



Chartered Professional Accountants, Licensed Public Accountants

We have served as the Company's auditor since 2008.

Toronto, Canada
February 23, 2021

Consolidated Statements of Operations and Comprehensive Income

| Year ended December 31 (millions of Canadian dollars, except per share amounts) | 2020 | 2019 |
|--|---------------|---------------|
| Revenues | | |
| Distribution (includes \$283 related party revenues; 2019 – \$282) (Note 29) | 5,507 | 4,788 |
| Transmission (includes \$1,718 related party revenues; 2019 – \$1,637) (Note 29) | 1,740 | 1,652 |
| Other | 43 | 40 |
| | 7,290 | 6,480 |
| Costs | | |
| Purchased power (includes \$2,513 related party costs; 2019 – \$1,818) (Note 29) | 3,854 | 3,111 |
| Operation, maintenance and administration (Notes 4, 29) | 1,070 | 1,181 |
| Depreciation, amortization and asset removal costs (Note 5) | 884 | 878 |
| | 5,808 | 5,170 |
| Income before financing charges and income tax expense | 1,482 | 1,310 |
| Financing charges (Notes 4, 6) | 471 | 514 |
| Income before income tax expense | 1,011 | 796 |
| Income tax recovery (Note 7) | (785) | (6) |
| Net income | 1,796 | 802 |
| Other comprehensive loss (Note 8) | (24) | (2) |
| Comprehensive income | 1,772 | 800 |
| Net income attributable to: | | |
| Noncontrolling interest (Note 28) | 8 | 6 |
| Preferred shareholders (Note 24) | 18 | 18 |
| Common shareholders | 1,770 | 778 |
| | 1,796 | 802 |
| Comprehensive income attributable to: | | |
| Noncontrolling interest (Note 28) | 8 | 6 |
| Preferred shareholders (Note 24) | 18 | 18 |
| Common shareholders | 1,746 | 776 |
| | 1,772 | 800 |
| Earnings per common share (Note 26) | | |
| Basic | \$2.96 | \$1.30 |
| Diluted | \$2.95 | \$1.30 |
| Dividends per common share declared (Note 25) | \$1.00 | \$0.96 |

See accompanying notes to Consolidated Financial Statements.

Consolidated Balance Sheets

| As at December 31 (millions of Canadian dollars) | 2020 | 2019 |
|---|---------------|--------|
| Assets | | |
| Current assets: | | |
| Cash and cash equivalents | 757 | 30 |
| Accounts receivable (Note 9) | 722 | 701 |
| Due from related parties (Note 29) | 326 | 415 |
| Other current assets (Note 10) | 184 | 122 |
| | 1,989 | 1,268 |
| Property, plant and equipment (Note 11) | 22,631 | 21,501 |
| Other long-term assets: | | |
| Regulatory assets (Note 13) | 4,571 | 2,676 |
| Deferred income tax assets (Note 7) | 124 | 748 |
| Intangible assets (Note 12) | 514 | 456 |
| Goodwill (Note 4) | 373 | 325 |
| Other assets (Note 14) | 92 | 87 |
| | 5,674 | 4,292 |
| Total assets | 30,294 | 27,061 |
| Liabilities | | |
| Current liabilities: | | |
| Short-term notes payable (Note 17) | 800 | 1,143 |
| Long-term debt payable within one year (includes \$303 measured at fair value; 2019 – \$nil) (Notes 17, 18) | 806 | 653 |
| Accounts payable and other current liabilities (Note 15) | 1,044 | 989 |
| Due to related parties (Note 29) | 329 | 302 |
| | 2,979 | 3,087 |
| Long-term liabilities: | | |
| Long-term debt (includes \$nil measured at fair value; 2019 – \$351) (Notes 17, 18) | 12,726 | 10,822 |
| Regulatory liabilities (Note 13) | 231 | 167 |
| Deferred income tax liabilities (Note 7) | 56 | 61 |
| Other long-term liabilities (Note 16) | 3,674 | 3,055 |
| | 16,687 | 14,105 |
| Total liabilities | 19,666 | 17,192 |
| <i>Contingencies and Commitments</i> (Notes 31, 32) | | |
| <i>Subsequent Events</i> (Note 34) | | |
| Noncontrolling interest subject to redemption (Note 28) | 22 | 20 |
| Equity | | |
| Common shares (Note 24) | 5,678 | 5,661 |
| Preferred shares (Note 24) | – | 418 |
| Additional paid-in capital (Note 27) | 47 | 49 |
| Retained earnings | 4,838 | 3,667 |
| Accumulated other comprehensive loss | (29) | (5) |
| Hydro One shareholders' equity | 10,534 | 9,790 |
| Noncontrolling interest (Note 28) | 72 | 59 |
| Total equity | 10,606 | 9,849 |
| | 30,294 | 27,061 |

See accompanying notes to Consolidated Financial Statements.

On behalf of the Board of Directors:



Timothy Hodgson
Chair



Russel Robertson
Chair, Audit Committee

Consolidated Statements of Changes in Equity

| Year ended December 31, 2020 (millions of Canadian dollars) | Common Shares | Preferred Shares | Additional Paid-in Capital | Retained Earnings | Accumulated Other Comprehensive Loss | Hydro One Shareholders' Equity | Non- controlling Interest (Note 28) | Total Equity |
|--|------------------|---------------------|----------------------------------|----------------------|---|--------------------------------------|--|-----------------|
| January 1, 2020 | 5,661 | 418 | 49 | 3,667 | (5) | 9,790 | 59 | 9,849 |
| Net income | — | — | — | 1,788 | — | 1,788 | 6 | 1,794 |
| Other comprehensive loss (Note 8) | — | — | — | — | (24) | (24) | — | (24) |
| Distributions to noncontrolling interest | — | — | — | — | — | — | (2) | (2) |
| Contributions from sale of noncontrolling interest (Note 4) | — | — | — | — | — | — | 9 | 9 |
| Dividends on preferred shares | — | — | — | (18) | — | (18) | — | (18) |
| Dividends on common shares | — | — | — | (599) | — | (599) | — | (599) |
| Common shares issued | 17 | — | (10) | — | — | 7 | — | 7 |
| Stock-based compensation (Note 27) | — | — | 8 | — | — | 8 | — | 8 |
| Preferred shares redeemed (Note 24) | — | (418) | — | — | — | (418) | — | (418) |
| December 31, 2020 | 5,678 | — | 47 | 4,838 | (29) | 10,534 | 72 | 10,606 |

| Year ended December 31, 2019 (millions of Canadian dollars) | Common Shares | Preferred Shares | Additional Paid-in Capital | Retained Earnings | Accumulated Other Comprehensive Loss | Hydro One Shareholders' Equity | Non- controlling Interest (Note 28) | Total Equity |
|--|------------------|---------------------|----------------------------------|----------------------|---|--------------------------------------|--|-----------------|
| January 1, 2019 | 5,643 | 418 | 56 | 3,459 | (3) | 9,573 | 49 | 9,622 |
| Net income | — | — | — | 796 | — | 796 | 4 | 800 |
| Other comprehensive loss (Note 8) | — | — | — | — | (2) | (2) | — | (2) |
| Distributions to noncontrolling interest | — | — | — | — | — | — | (6) | (6) |
| Contributions from sale of noncontrolling interest (Note 4) | — | — | — | — | — | — | 12 | 12 |
| Dividends on preferred shares | — | — | — | (18) | — | (18) | — | (18) |
| Dividends on common shares | — | — | — | (570) | — | (570) | — | (570) |
| Common shares issued | 18 | — | (12) | — | — | 6 | — | 6 |
| Stock-based compensation (Note 27) | — | — | 5 | — | — | 5 | — | 5 |
| December 31, 2019 | 5,661 | 418 | 49 | 3,667 | (5) | 9,790 | 59 | 9,849 |

See accompanying notes to Consolidated Financial Statements.

Consolidated Statements of Cash Flows

| Year ended December 31 (millions of Canadian dollars) | 2020 | 2019 |
|--|----------------|----------------|
| Operating activities | | |
| Net income | 1,796 | 802 |
| Environmental expenditures | (23) | (25) |
| Adjustments for non-cash items: | | |
| Depreciation and amortization (Note 5) | 783 | 777 |
| Regulatory assets and liabilities | 68 | (48) |
| Deferred income tax recovery | (823) | (30) |
| Unrealized loss on Foreign-Exchange Contract (Note 4) | — | 22 |
| Derecognition of deferred financing costs (Note 4) | — | 24 |
| Other | 49 | 37 |
| Changes in non-cash balances related to operations (Note 30) | 180 | 55 |
| Net cash from operating activities | 2,030 | 1,614 |
| Financing activities | | |
| Long-term debt issued | 2,725 | 1,500 |
| Long-term debt repaid | (653) | (730) |
| Short-term notes issued | 4,070 | 4,217 |
| Short-term notes repaid | (4,413) | (4,326) |
| Short-term debt repaid (Note 4) | (20) | — |
| Convertible debentures redeemed (Note 4) | — | (513) |
| Dividends paid | (617) | (588) |
| Distributions paid to noncontrolling interest | (2) | (9) |
| Contributions received from sale of noncontrolling interest (Note 4) | 9 | 12 |
| Common shares issued (Note 24) | 7 | 6 |
| Costs to obtain financing | (14) | (8) |
| Preferred shares redeemed (Note 24) | (418) | — |
| Net cash from (used in) financing activities | 674 | (439) |
| Investing activities | | |
| Capital expenditures (Note 30) | | |
| Property, plant and equipment | (1,718) | (1,513) |
| Intangible assets | (126) | (115) |
| Capital contributions received (Note 30) | — | 3 |
| Acquisitions (Note 4) | (126) | — |
| Other | (7) | (3) |
| Net cash used in investing activities | (1,977) | (1,628) |
| Net change in cash and cash equivalents | 727 | (453) |
| Cash and cash equivalents, beginning of year | 30 | 483 |
| Cash and cash equivalents, end of year | 757 | 30 |

See accompanying notes to Consolidated Financial Statements.

Notes to Consolidated Financial Statements

For the years ended December 31, 2020 and 2019

1. DESCRIPTION OF THE BUSINESS

Hydro One Limited (Hydro One or the Company) was incorporated on August 31, 2015, under the *Business Corporations Act* (Ontario). On October 31, 2015, the Company acquired Hydro One Inc., a company previously wholly-owned by the Province of Ontario (Province). At December 31, 2020, the Province held approximately 47.3% (2019 – 47.3%) of the common shares of Hydro One. The principal businesses of Hydro One are the transmission and distribution of electricity to customers within Ontario.

Rate Setting

The Company's transmission business consists of the transmission system operated by Hydro One Inc.'s subsidiaries, Hydro One Networks Inc. (Hydro One Networks) and Hydro One Sault Ste. Marie LP (HOSSM), as well as an approximately 66% interest in B2M Limited Partnership (B2M LP), a limited partnership between Hydro One and the Saugeen Ojibway Nation (SON), and an approximately 55% interest in Niagara Reinforcement Limited Partnership (NRLP), a limited partnership between Hydro One and Six Nations of the Grand River Development Corporation and the Mississaugas of the Credit First Nation (collectively, the First Nations Partners). See Note 4 – Business Combinations for additional information.

Hydro One's distribution business consists of the distribution system operated by Hydro One Inc.'s subsidiaries, Hydro One Networks, Hydro One Remote Communities Inc. (Hydro One Remote Communities), and Orillia Power Distribution Corporation (Orillia Power), as well as the distribution business and assets acquired from Peterborough Distribution Inc. (Peterborough Distribution). See Note 4 – Business Combinations for additional information.

Transmission

On March 7, 2019, the Ontario Energy Board (OEB) issued its reconsideration decision (DTA Decision) with respect to Hydro One's rate-setting treatment of the benefits of the deferred tax asset resulting from the transition from the payments in lieu of tax regime to tax payments under the federal and provincial tax regimes. On July 16, 2020, the Ontario Divisional Court rendered its decision on the Company's appeal of the OEB's DTA Decision. See Note 13 – Regulatory Assets and Liabilities.

On April 23, 2020, the OEB rendered its decision on Hydro One Networks' 2020-2022 transmission rate application (2020-2022 Transmission Decision). On July 16, 2020, the OEB issued its final rate order for the 2020-2022 transmission rates approving a revenue requirement of \$1,630 million, \$1,701 million and \$1,772 million for 2020, 2021 and 2022, respectively. On July 30, 2020, the OEB issued its decision for Uniform Transmission Rates (UTRs). The 2020 UTRs that were put in place on an interim basis on January 1, 2020 continued for the remainder of 2020 in light of the COVID-19 pandemic. On December 17, 2020, the OEB issued its decision and order setting the final 2021 UTRs effective January 1, 2021, which included the approval of a two-year disposition period for Hydro One Network's 2020 foregone revenue including interest, beginning on January 1, 2021.

On July 31, 2019, B2M LP filed a transmission rate application for 2020-2024. On January 16, 2020, the OEB approved the 2020 base revenue requirement of \$33 million, and a revenue cap escalator index for 2021 to 2024.

On October 25, 2019, NRLP filed its revenue cap incentive rate application for 2020-2024. On December 19, 2019, the OEB approved NRLP's proposed 2020 revenue requirement of \$9 million on an interim basis effective January 1, 2020. On April 9, 2020, final OEB approval was received.

HOSSM is under a 10-year deferred rebasing period for years 2017-2026, as approved in the OEB Mergers Acquisitions Amalgamations and Divestitures (MAAD) decision dated October 13, 2016.

Distribution

In March 2017, Hydro One Networks filed an application with the OEB for 2018-2022 distribution rates. On March 7, 2019, the OEB rendered its decision on the distribution rates application. In accordance with the OEB decision, the Company filed its draft rate order reflecting updated revenue requirements of \$1,459 million for 2018, \$1,498 million for 2019, \$1,532 million for 2020, \$1,578 million for 2021, and \$1,624 million for 2022. On June 11, 2019, the OEB approved the rate order confirming these updated revenue requirements.

On April 16, 2020, the OEB approved a 2% increase to Hydro One Remote Communities' 2019 base rates for new rates effective May 1, 2020, with a deferred implementation date of November 1, 2020 due to COVID-19. On October 8, 2020, the OEB authorized Hydro One Remote Communities to implement a rate rider for the recovery of foregone revenues resulting from postponing rate implementation, effective until April 30, 2021.

2. SIGNIFICANT ACCOUNTING POLICIES

Basis of Consolidation and Presentation

These Consolidated Financial Statements (Consolidated Financial Statements) include the accounts of the Company and its subsidiaries. Inter-company 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.

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, contingencies, and unbilled revenues. Actual results may differ significantly from these estimates.

Since late March 2020, the impact of the COVID-19 pandemic (COVID-19 or the pandemic) has been reflected in the Consolidated Financial Statements. While the pandemic has resulted in incremental operating costs and lost revenues, the Company has analyzed the impact of the pandemic on its estimates and assumptions that affect its financial results as at and for the year ended December 31, 2020 and has determined that there was no material impact. Additional details

Notes to Consolidated Financial Statements

regarding the impact of the pandemic on the Consolidated Financial Statements are available in Note 9 – Accounts Receivable and Note 13 – Regulatory Assets and Liabilities.

As the duration of the pandemic remains uncertain, the Company continues to assess its impact to the Company's financial results and operations.

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 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 include its regulatory assets and liabilities in setting 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 would be reflected in results of operations prospectively from the date the Company's assessment is made, unless the change meets the requirements for a subsequent event adjustment.

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

Nature of Revenues

Transmission revenues predominantly consist of transmission tariffs, which are collected through OEB-approved UTRs which are applied against the monthly peak demand for electricity across Hydro One's high-voltage network. OEB-approved UTRs are based on an approved revenue requirement that includes a rate of return. The transmission tariffs are designed to recover revenues necessary to support the Company's transmission system with sufficient capacity to accommodate the maximum expected demand which is influenced by weather and economic conditions. Transmission revenues are 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. At the end of each month, electricity delivered to customers since the date of the last billed meter reading is estimated, and the corresponding unbilled revenue is recorded. The unbilled revenue estimate is affected by energy consumption, weather, and changes in the composition of customer classes.

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, net of allowance for doubtful accounts. Overdue amounts related to regulated billings bear interest at OEB-approved rates. The allowance for doubtful accounts reflects the Company's current lifetime expected credit losses (CECL) for all accounts receivable balances. The Company estimates the CECL by applying internally developed loss rates to all 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, which may be further supplemented from time to time to reflect management's best estimate of the loss. Accounts receivable are written-off against the allowance when they are deemed uncollectible. The allowance for doubtful accounts is 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 and other comprehensive income (OCI) or other comprehensive loss (OCL) 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

Income taxes are accounted for using the asset and liability method. Current tax assets and liabilities are recognized based on the taxes payable or refundable on the current and prior year's taxable income. 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 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 using new information about recognition or measurement as it becomes available.

Deferred Income Taxes

Deferred income tax assets and liabilities are recognized on all temporary differences between the tax bases and carrying amounts of assets and liabilities, including the carryforward unused tax credits and tax losses to the extent that it is more likely than not that these deductions, credits, and losses can be utilized. Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply in the period when

Notes to Consolidated Financial Statements

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 associated with its regulated operations which are considered to be more likely than not to be recoverable or refunded in the future regulated rates charged to customers are recognized as deferred income tax regulatory assets and liabilities with an offset to deferred income tax expense.

Investment tax credits are recorded as a reduction of the related expenses or income tax expense in the current or future period to the extent it is more likely than not that the credits can be utilized.

Management reassesses the deferred income tax assets at each balance sheet date and reduces the amount to the extent that it is more likely than not that the deferred income tax asset will not 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.

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, and information technology (IT). 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 most recent reviews resulted in changes to rates effective January 1, 2015 and January 1, 2020 for Hydro One Networks' distribution and transmission businesses, respectively. A summary of average service lives and depreciation and amortization rates for the various classes of assets is included below:

Notes to Consolidated Financial Statements

| | Average Service Life | Rate | |
|--------------------------------|----------------------|----------|---------|
| | | Range | Average |
| Property, plant and equipment: | | | |
| Transmission | 55 years | 1% – 3% | 2% |
| Distribution | 46 years | 1% – 7% | 2% |
| Communication | 14 years | 1% – 15% | 5% |
| Administration and service | 21 years | 1% – 20% | 4% |
| Intangible assets | 10 years | 10% | 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.

Acquisitions and Goodwill

The Company accounts for business acquisitions using the acquisition method of accounting and, accordingly, the assets and liabilities of the acquired entities are primarily measured at their estimated fair value at the date of acquisition. Costs associated with pending acquisitions are expensed as incurred. Goodwill represents the cost of acquired 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 quantitative goodwill impairment assessment is performed. The quantitative assessment compares the fair value of the applicable reporting unit to its carrying amount, including goodwill. If the 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.

Based on the assessment performed as at September 30, 2020 and with no significant events since, the Company has concluded that goodwill was not impaired at December 31, 2020.

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 monitors the assets of its unregulated Hydro One Telecom Inc. subsidiary for indications of impairment. Management assesses the fair value of such long-lived assets using commonly accepted techniques. 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, 2020 and 2019, 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 and for convertible debentures, the Company defers the external transaction costs related to obtaining financing and presents such amounts net of related debt or convertible debentures on the consolidated balance sheets. Deferred issuance costs are amortized over the contractual life of the related debt or convertible debentures 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/Loss

Comprehensive income/loss is comprised of net income/loss and OCI/OCL. Hydro One presents net income/loss and OCI/OCL in a single continuous consolidated statement of operations and comprehensive income/loss.

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

Notes to Consolidated Financial Statements

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 its net realizable 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. The Company estimates the CECL for all accounts receivable balances, which are recognized as adjustments to the allowance for doubtful accounts. Accounts receivable are written-off against the allowance when they are deemed uncollectible. All financial instrument transactions are recorded at trade date.

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 18 – 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, any unrealized gain or loss, net of tax, is recorded as a component of accumulated OCI (AOCI). Amounts in AOCI are reclassified to results of operations in the same period or periods during which the hedged transaction affects results of operations and presented in the same line item as the earnings effect of the hedged item. Any gains or losses on the derivative instrument that represent hedge components excluded from the assessment of effectiveness are recognized in the same line item of the consolidated statements of operations as the hedged item. 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. The changes in fair value of the undesignated derivative instruments are reflected in results of operations.

Embedded derivative instruments are separated from their host contracts and are 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 that required bifurcation at December 31, 2020 or 2019.

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 plan (Pension Plan) and its 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 (PBO) exceeds the fair value of the plan assets. Liabilities are recognized on the consolidated balance sheets for any net underfunded PBO. The net underfunded PBO 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 PBO of the plan, an asset is recognized equal to the net overfunded PBO. The post-retirement and post-employment benefit plans are unfunded because there are no related plan assets.

Hydro One recognizes its contributions to the defined contribution pension plan (DC Plan) as pension expense, with a portion being capitalized as part of labour costs included in capital expenditures. The expensed amount is included in operation, maintenance and administration (OM&A) costs in the consolidated statements of operations and comprehensive income.

Defined Benefit Pension

Defined benefit 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

Notes to Consolidated Financial Statements

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, corporate and government debt securities as well as unlisted real estate and unlisted infrastructure investments, are recorded at fair value at the end of each year. Hydro One records a regulatory asset equal to the net underfunded PBO for its pension plan. Defined benefit pension costs are attributed to labour costs on a cash basis and a portion directly related to acquisition and development of capital assets is capitalized as part of the cost of property, plant and equipment and intangible assets. The remaining defined benefit pension costs are charged to results of operations (OM&A costs).

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.

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. 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 benefit costs are attributed to labour costs and are either charged to results of operations (OM&A costs) or capitalized as part of the cost of property, plant and equipment and intangible assets for service cost component and to regulatory assets for all other components of the benefit costs, consistent with their inclusion in OEB-approved rates.

Stock-Based Compensation

Share Grant Plans

Hydro One measures share grant plans based on fair value of share grants as estimated based on the grant date common 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. Costs are transferred from the regulatory asset to labour costs at the time the share grants vest and are issued, and are recovered in rates. Forfeitures are recognized as they occur.

Deferred Share Unit (DSU) Plans

The Company records the liabilities associated with its Directors' and Management DSU Plans 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 the Company's common share closing price at the end of each reporting period.

Long-term Incentive Plan (LTIP)

The Company measures the awards issued under its LTIP, at fair value based on the grant date common share price. The related compensation expense is recognized over the vesting period on a straight-line basis. Forfeitures are recognized as they occur.

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.

Notes to Consolidated Financial Statements

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 (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 that produces an amount at which the environmental liabilities could be settled in an arm's length transaction with a third-party. 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. This uncertainty is incorporated in the fair value measurement of the obligation.

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. The present value is determined with a discount rate that equates to the Company's credit-adjusted risk-free rate. 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 have been recorded 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.

Leases

At the commencement date of a lease, the minimum lease payments are discounted and recognized as a lease obligation. Discount rates used correspond to the Company's incremental borrowing rates. Renewal options are assessed for their likelihood of being exercised and are included in the measurement of the lease obligation when it is reasonably certain they will be exercised. The Company does not recognize leases with a term of less than 12 months. A corresponding Right-of-Use (ROU) asset is recognized at the commencement date of a lease. The ROU asset is measured as the lease obligation adjusted for any lease payments made and/or any lease incentives and initial direct costs incurred. ROU assets are included in other long-term assets, and corresponding lease obligations are included in other current liabilities and other long-term liabilities on the consolidated balance sheets.

Subsequent to the commencement date, the lease expense recognized at each reporting period is the total remaining lease payments over the remaining lease term. Lease obligations are measured as the present value of the remaining unpaid lease payments using the discount rate established at commencement date. The amortization of the ROU assets is calculated as the difference between the lease expense and the accretion of interest, which is calculated using the effective interest method. Lease modifications and impairments are assessed at each reporting period to assess the need for a remeasurement of the lease obligations or ROU assets.

Notes to Consolidated Financial Statements

3. NEW ACCOUNTING PRONOUNCEMENTS

The following tables present Accounting Standard Updates (ASUs) issued by the Financial Accounting Standards Board that are applicable to Hydro One:

Recently Adopted Accounting Guidance

| Guidance | Date issued | Description | Effective date | Impact on Hydro One |
|-------------|--------------|--|-----------------|-------------------------|
| ASU 2017-04 | January 2017 | The amendment removes the second step of the previous two-step goodwill impairment test to simplify the process of testing goodwill. | January 1, 2020 | No impact upon adoption |
| ASU 2018-13 | August 2018 | Disclosure requirements on fair value measurements in Accounting Standard Codification (ASC) 820 are modified to improve the effectiveness of disclosures in financial statement notes. | January 1, 2020 | No impact upon adoption |
| ASU 2019-01 | March 2019 | This amendment carries forward the exemption previously provided under ASC 840 relating to the determination of the fair value of underlying assets by lessors that are not manufacturers or dealers. It also provides for clarification on cash-flow presentation of sales-type and financing leases and clarifies that transition disclosures under Topic 250 are applicable in the adoption of ASC 842. | January 1, 2020 | No impact upon adoption |

Recently Issued Accounting Guidance Not Yet Adopted

| Guidance | Date issued | Description | Effective date | Anticipated Impact on Hydro One |
|-------------|---------------|--|-----------------|---------------------------------|
| ASU 2018-14 | August 2018 | Disclosure requirements related to single-employer defined benefit pension or other post-retirement benefit plans are added, removed or clarified to improve the effectiveness of disclosures in financial statement notes. | January 1, 2021 | No impact upon adoption |
| ASU 2019-12 | December 2019 | The amendments simplify the accounting for income taxes by removing certain exceptions to the general principles and improving consistent application of Topic 740 by clarifying and amending existing guidance. | January 1, 2021 | No impact upon adoption |
| ASU 2020-01 | January 2020 | The amendments clarify the interaction of the accounting for equity securities under Topic 321, investments under the equity method of accounting in Topic 323 and the accounting for certain forward contracts and purchased options accounted for under Topic 815. | January 1, 2021 | No impact upon adoption |
| ASU 2020-06 | August 2020 | The update addresses the complexity associated with applying GAAP for certain financial instruments with characteristics of liabilities and equity. The amendments reduce the number of accounting models for convertible debt instruments and convertible preferred stock. | January 1, 2022 | Under assessment |
| ASU 2020-10 | October 2020 | The amendments are intended to improve the Codification by ensuring the guidance required for an entity to disclose information in the notes of financial statements are codified in the disclosure sections to reduce the likelihood of disclosure requirements being missed. | January 1, 2021 | No impact upon adoption |

4. BUSINESS COMBINATIONS

Acquisition of Peterborough Distribution Assets

On August 1, 2020, Hydro One completed the acquisition of the business and distribution assets of Peterborough Distribution, an electricity distribution company located in east central Ontario, from the City of Peterborough, for a purchase price of \$104 million, including the assumption of agreed upon liabilities and closing adjustments. The purchase price is comprised of a cash payment of \$105 million, including a deposit of \$4 million paid in 2018 and \$101 million paid on closing of the transaction, partially offset by a purchase price adjustment of \$1 million. As the acquired business and distribution assets of Peterborough Distribution meet the definition of a business, the acquisition has been accounted for as a business acquisition.

The following table summarizes the determination of the fair value of the assets acquired and liabilities assumed:

| (millions of dollars) | |
|-------------------------------|------------|
| Working capital | 7 |
| Property, plant and equipment | 64 |
| Regulatory assets | 1 |
| Goodwill | 33 |
| Other long-term liabilities | (1) |
| | <u>104</u> |

The determination of the fair value of assets acquired and liabilities assumed is based upon management's estimates and assumptions and reflects the fair value of consideration paid.

The goodwill estimate of \$33 million arising from the Peterborough Distribution acquisition consists largely of the synergies and economies of scale expected from combining the operations of Hydro One and Peterborough Distribution. All of the goodwill was assigned to Hydro One's Distribution Business segment. Peterborough Distribution contributed revenues of \$51 million and net income of \$nil to the Company's consolidated financial results for the year ended December 31, 2020. All costs related to the acquisition have been expensed through the statement of operations and comprehensive income. The disclosure of Peterborough Distribution's pro forma information is immaterial to the Company's consolidated financial results for the year ended December 31, 2020.

Acquisition of Orillia Power

On September 1, 2020, Hydro One completed the acquisition of Orillia Power, an electricity distribution company located in Simcoe County, Ontario, from the City of Orillia for a purchase price of \$28 million, including closing adjustments. The purchase price is comprised of a cash payment of \$26 million, including a deposit of \$1 million paid in 2016, \$25 million paid on closing of the transaction, as well as a purchase price adjustment of \$2 million.

The following table summarizes the determination of the fair value of the assets acquired and liabilities assumed:

| (millions of dollars) | |
|-------------------------------|-----------|
| Working capital | 2 |
| Property, plant and equipment | 32 |
| Deferred income tax assets | 1 |
| Goodwill | 15 |
| Short-term debt | (20) |
| Regulatory liabilities | (1) |
| Other long-term liabilities | (1) |
| | <u>28</u> |

The determination of the fair value of assets acquired and liabilities assumed is based upon management's estimates and assumptions and reflects the fair value of consideration paid. In September 2020, Hydro One repaid the \$20 million of short-term debt assumed as part of the Orillia Power acquisition.

The goodwill estimate of \$15 million arising from the Orillia Power acquisition consists largely of the synergies and economies of scale expected from combining the operations of Hydro One and Orillia Power. All of the goodwill was assigned to Hydro One's Distribution Business segment. Orillia Power contributed revenues of \$15 million and net income of \$nil to the Company's consolidated financial results for the year ended December 31, 2020. All costs related to the acquisition have been expensed through the statement of operations and comprehensive income. The disclosure of Orillia Power's pro forma information is immaterial to the Company's consolidated financial results for the year ended December 31, 2020.

NRLP

In 2018, Hydro One entered into an agreement with the First Nations Partners, wherein a noncontrolling equity interest in Hydro One's limited partnership, NRLP, would be made available for purchase at fair value by the First Nations Partners. On September 19, 2018, NRLP was formed to own a new 230 kV transmission line (Niagara Line) in the Niagara region. The Niagara Line enables generators in the Niagara area to connect to the load centres of the Greater Toronto and Hamilton areas. Hydro One Networks maintains and operates the Niagara Line in accordance with an operation and management services agreement. On September 12, 2019, the OEB granted NRLP a transmission licence and granted Hydro One Networks leave to sell the applicable Niagara Line assets to NRLP.

On September 18, 2019, the applicable Niagara Line assets were transferred from Hydro One Networks to NRLP for \$119 million and operation of the line was contracted to Hydro One Networks. This transfer was financed with 60% debt (\$71 million) and 40% equity (\$48 million). The cash payment of \$71 million was financed by debt sourced by NRLP from a Hydro One subsidiary, and the \$48 million equity comprised partnership units issued by NRLP to Hydro One Networks. Subsequently, on the same date, Hydro One Networks sold to the Six Nations of the Grand River Development Corporation and,

Notes to Consolidated Financial Statements

through a trust, to the Mississaugas of the Credit First Nation a 25.0% and 0.1%, respectively, equity interest in NRLP partnership units for total consideration of \$12 million, representing the fair value of the equity interest acquired.

On January 31, 2020, the Mississaugas of the Credit First Nation purchased an additional 19.9% equity interest in NRLP partnership units from Hydro One Networks for total cash consideration of \$9 million. Following this transaction, Hydro One's interest in the equity portion of NRLP partnership units was reduced to 55%, with the Six Nations of the Grand River Development Corporation and the Mississaugas of the Credit First Nation owning 25% and 20%, respectively, of the equity interest in NRLP partnership units.

NRLP is fully consolidated in these Consolidated Financial Statements as it is controlled by Hydro One. The First Nations Partners' noncontrolling interest in NRLP is classified within equity. See Note 28 – Noncontrolling Interest for additional information.

Termination of the Avista Corporation Purchase Agreement

In July 2017, Hydro One reached an agreement to acquire Avista Corporation (Merger). In January 2019, Hydro One and Avista Corporation announced that the companies mutually agreed to terminate the Merger agreement. The following amounts related to the termination of the Merger agreement were recorded by the Company during the first quarter of the year ended December 31, 2019.

- \$138 million (US\$103 million) for payment of the Merger termination fee recorded in OM&A costs;
- \$22 million financing charges, due to reversal of previously recorded unrealized gains upon termination of the deal-contingent foreign-exchange forward contract (Foreign-Exchange Contract);
- redemption of \$513 million convertible debentures and payment of related interest of \$7 million; and
- \$24 million financing charges, due to derecognition of the deferred financing costs related to convertible debentures.

5. DEPRECIATION, AMORTIZATION AND ASSET REMOVAL COSTS

| Year ended December 31 (millions of dollars) | 2020 | 2019 |
|---|------------|------------|
| Depreciation of property, plant and equipment | 691 | 671 |
| Amortization of intangible assets | 69 | 81 |
| Amortization of regulatory assets | 23 | 25 |
| Depreciation and amortization | 783 | 777 |
| Asset removal costs | 101 | 101 |
| | 884 | 878 |

6. FINANCING CHARGES

| Year ended December 31 (millions of dollars) | 2020 | 2019 |
|--|------------|------------|
| Interest on long-term debt | 497 | 479 |
| Interest on short-term notes | 8 | 19 |
| Realized loss on cash flow hedges (interest-rate swap agreements) (Note 8, 18) | 7 | – |
| Derecognition of deferred financing costs (Note 4) | – | 24 |
| Unrealized loss on Foreign-Exchange Contract (Notes 4, 18) | – | 22 |
| Interest on convertible debentures (Note 4) | – | 7 |
| Other | 13 | 18 |
| Less: Interest capitalized on construction and development in progress | (49) | (48) |
| Interest earned on cash and cash equivalents | (5) | (7) |
| | 471 | 514 |

Notes to Consolidated Financial Statements

7. INCOME TAXES

As a rate regulated utility company, the Company recovers income taxes from its ratepayers based on estimated current income tax expense in respect of its regulated business. The amounts of deferred income taxes related to regulated operations which are considered to be more likely than not to be recoverable or refunded to, ratepayers in future periods are recognized as deferred income tax regulatory assets or liabilities, with an offset to deferred income tax expense (recovery). The Company's consolidated tax expense or recovery for the period includes all current and deferred income tax expenses for the period net of the regulated accounting offset to deferred income tax expense arising from temporary differences to be recoverable or refunded in future rates charged to customers. Thus, the Company's income tax expense or recovery 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 dollars) | 2020 | 2019 |
|--|----------------|--------|
| Income before income tax expense | 1,011 | 796 |
| Income tax expense at statutory rate of 26.5% (2019 – 26.5%) | 268 | 211 |
| Increase (decrease) resulting from: | | |
| Net temporary differences recoverable in future rates charged to customers: | | |
| Capital cost allowance in excess of depreciation and amortization ¹ | (102) | (105) |
| Impact of tax deductions from deferred tax asset sharing ² | (41) | (60) |
| Overheads capitalized for accounting but deducted for tax purposes | (21) | (21) |
| Interest capitalized for accounting but deducted for tax purposes | (13) | (13) |
| Environmental expenditures | (6) | (7) |
| Pension and post-retirement benefit contributions in excess of pension expense | (4) | (11) |
| Other | – | (3) |
| Net temporary differences attributable to regulated business | (187) | (220) |
| Net permanent differences | 1 | 3 |
| Recognition of deferred income tax regulatory asset (Note 13) | (867) | – |
| Total income tax recovery | (785) | (6) |
| Effective income tax rate | (77.6%) | (0.8%) |

1 Includes accelerated tax depreciation of up to three times the first-year rate for certain eligible capital investments acquired after November 20, 2018 and placed in-service before January 1, 2028, as introduced in the 2019 federal and Ontario budgets and enacted in the second quarter of 2019.

2 Prior to the ODC Decision, the impact represents tax deductions from deferred asset tax sharing given to ratepayers as previously mandated by the OEB. Subsequent to the ODC Decision, the impact represents the recovery of deferred tax asset sharing currently allocated to rate-payers. See Note 13 – Regulatory Assets and Liabilities.

The major components of income tax expense are as follows:

| Year ended December 31 (millions of dollars) | 2020 | 2019 |
|--|--------------|------|
| Current income tax expense | 29 | 24 |
| Deferred income tax recovery | (814) | (30) |
| Total income tax recovery | (785) | (6) |

Notes to Consolidated Financial Statements

Deferred Income Tax Assets and Liabilities

Deferred income tax assets and liabilities reflect the future tax consequences attributable to temporary differences between the tax bases and the financial statement carrying amounts of the assets and liabilities including the carryforward amounts of tax losses and tax credits. Deferred income tax assets and liabilities attributable to the Company's regulated business are recognized with a corresponding offset in deferred income tax regulatory assets and liabilities to reflect the anticipated recovery or repayment of these balances in the future electricity rates. At December 31, 2020 and 2019, deferred income tax assets and liabilities consisted of the following:

| As at December 31 (millions of dollars) | 2020 | 2019 |
|---|--------------|-------|
| Deferred income tax assets | | |
| Post-retirement and post-employment benefits expense in excess of cash payments | 685 | 638 |
| Pension obligations | 607 | 405 |
| Non-capital losses | 323 | 331 |
| Non-depreciable capital property | 271 | 271 |
| Tax credit carryforwards | 119 | 92 |
| Investment in subsidiaries | 100 | 95 |
| Depreciation and amortization in excess of capital cost allowance | 57 | 59 |
| Environmental expenditures | 48 | 51 |
| Other | 14 | 20 |
| | 2,224 | 1,962 |
| Less: valuation allowance | (380) | (375) |
| Total deferred income tax assets | 1,844 | 1,587 |
| Deferred income tax liabilities | | |
| Capital cost allowance in excess of depreciation and amortization | 1,022 | 377 |
| Regulatory assets and liabilities | 728 | 495 |
| Goodwill | 11 | 10 |
| Other | 15 | 18 |
| Total deferred income tax liabilities | 1,776 | 900 |
| Net deferred income tax assets | 68 | 687 |

The net deferred income tax assets are presented on the consolidated balance sheets as follows:

| As at December 31 (millions of dollars) | 2020 | 2019 |
|---|-----------|------|
| Long-term: | | |
| Deferred income tax assets | 124 | 748 |
| Deferred income tax liabilities | (56) | (61) |
| Net deferred income tax assets | 68 | 687 |

The valuation allowance for deferred tax assets as at December 31, 2020 was \$380 million (2019 – \$375 million). The valuation allowance primarily relates to temporary differences for non-depreciable assets and investments in subsidiaries. As of December 31, 2020 and 2019, the Company had non-capital losses carried forward available to reduce future years' taxable income, which expire as follows:

| Year of expiry (millions of dollars) | 2020 | 2019 |
|--------------------------------------|--------------|-------|
| 2034 | – | 2 |
| 2035 | 171 | 221 |
| 2036 | 552 | 551 |
| 2037 | 172 | 172 |
| 2038 | 95 | 95 |
| 2039 | 200 | 202 |
| 2040 | 27 | – |
| Total losses | 1,217 | 1,243 |

Notes to Consolidated Financial Statements

8. OTHER COMPREHENSIVE LOSS

| Year ended December 31 (millions of dollars) | 2020 | 2019 |
|--|-------------|------------|
| Gain (loss) on cash flow hedges (interest-rate swap agreements) (Notes 6, 18) ¹ | (20) | 2 |
| Loss on pension and other post-employment benefits (OPEB) transfer (Note 20) | (6) | — |
| Other | 2 | (4) |
| | (24) | (2) |

¹ Includes \$7 million realized loss on cash flow hedges reclassified to financing charges (2019 – \$nil).

9. ACCOUNTS RECEIVABLE

| As at December 31 (millions of dollars) | 2020 | 2019 |
|---|------------|------------|
| Accounts receivable – billed | 347 | 330 |
| Accounts receivable – unbilled | 421 | 393 |
| Accounts receivable, gross | 768 | 723 |
| Allowance for doubtful accounts | (46) | (22) |
| Accounts receivable, net | 722 | 701 |

The following table shows the movements in the allowance for doubtful accounts for the years ended December 31, 2020 and 2019:

| Year ended December 31 (millions of dollars) | 2020 | 2019 |
|---|-------------|-------------|
| Allowance for doubtful accounts – beginning | (22) | (21) |
| Write-offs | 11 | 18 |
| Additions to allowance for doubtful accounts ¹ | (35) | (19) |
| Allowance for doubtful accounts – ending | (46) | (22) |

¹ Additions to allowance for doubtful accounts for the year ended December 31, 2020 include incremental \$14 million related to the COVID-19 pandemic which were recognized in OM&A in 2020 (2019 – \$nil).

10. OTHER CURRENT ASSETS

| As at December 31 (millions of dollars) | 2020 | 2019 |
|---|------------|------------|
| Regulatory assets (Note 13) | 105 | 52 |
| Prepaid expenses and other assets | 53 | 49 |
| Materials and supplies | 23 | 21 |
| Derivative assets (Note 18) | 3 | — |
| | 184 | 122 |

Notes to Consolidated Financial Statements

11. PROPERTY, PLANT AND EQUIPMENT

| As at December 31, 2020 (millions of dollars) | Property, Plant and Equipment | Accumulated Depreciation | Construction in Progress | Total |
|---|-------------------------------|--------------------------|--------------------------|---------------|
| Transmission | 18,213 | 5,989 | 876 | 13,100 |
| Distribution | 11,544 | 3,949 | 101 | 7,696 |
| Communication | 1,395 | 1,079 | 45 | 361 |
| Administration and service | 1,729 | 959 | 113 | 883 |
| Easements | 671 | 80 | — | 591 |
| | 33,552 | 12,056 | 1,135 | 22,631 |

| As at December 31, 2019 (millions of dollars) | Property, Plant and Equipment | Accumulated Depreciation | Construction in Progress | Total |
|---|-------------------------------|--------------------------|--------------------------|---------------|
| Transmission | 17,454 | 5,714 | 711 | 12,451 |
| Distribution | 10,991 | 3,747 | 85 | 7,329 |
| Communication | 1,355 | 1,002 | 43 | 396 |
| Administration and service | 1,617 | 931 | 53 | 739 |
| Easements | 663 | 77 | — | 586 |
| | 32,080 | 11,471 | 892 | 21,501 |

Financing charges capitalized on property, plant and equipment under construction were \$46 million in 2020 (2019 – \$45 million).

12. INTANGIBLE ASSETS

| As at December 31, 2020 (millions of dollars) | Intangible Assets | Accumulated Amortization | Development in Progress | Total |
|---|-------------------|--------------------------|-------------------------|------------|
| Computer applications software | 1,034 | 581 | 59 | 512 |
| Other | 7 | 5 | — | 2 |
| | 1,041 | 586 | 59 | 514 |

| As at December 31, 2019 (millions of dollars) | Intangible Assets | Accumulated Amortization | Development in Progress | Total |
|---|-------------------|--------------------------|-------------------------|------------|
| Computer applications software | 912 | 512 | 56 | 456 |
| Other | 5 | 5 | — | — |
| | 917 | 517 | 56 | 456 |

Financing charges capitalized to intangible assets under development were \$3 million in 2020 (2019 – \$3 million). The estimated annual amortization expense for intangible assets is as follows: 2021 – \$73 million; 2022 – \$70 million; 2023 – \$60 million; 2024 – \$49 million; and 2025 – \$48 million.

13. 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:

| As at December 31 (millions of dollars) | 2020 | 2019 |
|---|-------|-------|
| Regulatory assets: | | |
| Deferred income tax regulatory asset | 2,343 | 1,109 |
| Pension benefit regulatory asset | 1,660 | 1,125 |
| Deferred tax asset sharing | 204 | — |
| Environmental | 133 | 141 |
| Post-retirement and post-employment benefits – non-service cost | 113 | 96 |
| Foregone revenue deferral | 63 | 67 |
| Post-retirement and post-employment benefits | 59 | 105 |
| Stock-based compensation | 41 | 42 |
| Conservation and Demand Management (CDM) variance | 16 | — |
| Debt premium | 12 | 17 |
| Other | 32 | 26 |
| Total regulatory assets | 4,676 | 2,728 |
| Less: current portion | (105) | (52) |
| | 4,571 | 2,676 |
| Regulatory liabilities: | | |
| Retail settlement variance account | 92 | 23 |
| Tax rule changes variance | 70 | 44 |
| Earnings sharing mechanism deferral | 37 | 21 |
| Pension cost differential | 31 | 31 |
| Green energy expenditure variance | 22 | 31 |
| Asset removal costs cumulative variance | 19 | — |
| External revenue variance | 7 | 6 |
| Deferred income tax regulatory liability | 4 | 5 |
| Distribution rate riders | 1 | 42 |
| Other | 14 | 9 |
| Total regulatory liabilities | 297 | 212 |
| Less: current portion | (66) | (45) |
| | 231 | 167 |

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 2020 income tax expense would have been higher by approximately \$187 million (2019 – higher by \$221 million), of which \$146 million is included in Deferred Income Tax Regulatory Asset and Liability with the remaining \$41 million included in Deferred Tax Asset Sharing.

On September 28, 2017, the OEB issued its decision and order on Hydro One Networks' 2017 and 2018 transmission rates revenue requirements (Original Decision). In its Original Decision, the OEB concluded that the net deferred tax asset resulting from transition from the payments in lieu of tax regime under the *Electricity Act, 1998* (Ontario) to tax

payments under the federal and provincial tax regime should not accrue entirely to Hydro One shareholders and that a portion should be shared with ratepayers. On November 9, 2017, the OEB issued a decision and order that calculated the portion of the tax savings that should be shared with ratepayers. The OEB's calculation would have resulted in an impairment of a portion of both Hydro One Networks' transmission and distribution deferred income tax regulatory asset. In October 2017, the Company filed a Motion to Review and Vary (Motion) the Original Decision and filed an appeal with the Ontario Divisional Court (Appeal). In both cases, the Company's position was that the OEB made errors of fact and law in its determination of allocation of the tax savings between the shareholders and ratepayers. On December 19, 2017, the OEB granted a hearing of the merits of the Motion which was held on February 12, 2018. On August 31, 2018, the OEB granted the Motion and returned the portion of the Original Decision relating to the deferred tax asset to an OEB panel for reconsideration.

On March 7, 2019, the OEB issued its DTA Decision and concluded that their Original Decision was reasonable and should be upheld. Also, on March 7, 2019 the OEB issued its decision for Hydro One Networks'

Notes to Consolidated Financial Statements

2018–2022 distribution rates, in which it directed the Company to apply the Original Decision to Hydro One Networks' distribution rates. As a result, as at December 31, 2018, the Company recorded impairment charges relating to Hydro One Networks' distribution and transmission deferred income tax regulatory asset. Notwithstanding the recognition of the effects of the DTA Decision in the 2018 financial statements, on April 5, 2019, the Company filed an appeal with the Ontario Divisional Court with respect to the OEB's DTA Decision. The appeal was heard on November 21, 2019.

On July 16, 2020, the Ontario Divisional Court rendered its decision (ODC Decision) on the Company's appeal of the OEB's DTA Decision.

In connection with the ODC Decision, the Company recorded a reversal of the previously recognized impairment charge of Hydro One Networks' distribution and transmission deferred income tax regulatory asset in its financial statements for the year ended December 31, 2020. The reversal of the previously recognized impaired charge included the regulatory asset relating to the cumulative deferred tax asset amounts shared with ratepayers (deferred tax asset sharing) up to and including June 30, 2020 by Hydro One Networks' distribution and transmission segments of \$58 million and \$118 million, respectively. Hydro One recognized deferred income tax regulatory assets of \$504 million and \$673 million for Hydro One Networks distribution and transmission segments, respectively, and associated deferred income tax liability of \$310 million. The Company also recorded an increase in net income of \$867 million as deferred income tax recovery during the year ended December 31, 2020.

Pension Benefit Regulatory Asset

In accordance with OEB rate orders, pension costs are recovered 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 the present value of the actuarially determined benefit obligation 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, OCL would have been higher by \$470 million (2019 – \$597 million) and OM&A expenses would have been higher by \$89 million (2019 – lower by \$20 million).

Deferred Tax Asset Sharing

On October 2, 2020, the OEB issued a procedural order to implement the direction of the Ontario Divisional Court and required Hydro One to submit its proposal for the recovery of the deferred tax asset amounts allocated to ratepayers for the 2017 to 2022 period. As at December 31, 2020, Hydro One recorded a regulatory asset of \$204 million for the cumulative deferred tax asset amounts shared with ratepayers since 2017 to date, consisting of \$70 million and \$134 million for Hydro One Networks' distributions and transmission segments, respectively. As a result of the OEB's procedural order, the \$204 million regulatory asset relating to the cumulative deferred tax asset amounts allocated to ratepayers since 2017 has been separately presented from the deferred income tax regulatory asset. Until the OEB issues the order to

implement the recovery of the deferred tax asset amounts allocated to ratepayers for the 2017 to 2022 period, this \$204 million regulatory asset will continue to increase to recognize the additional amounts shared with ratepayers during the reporting period.

Environmental

Hydro One records a liability for the estimated future expenditures required to remediate environmental contamination. A regulatory asset is recognized because management considers it to be probable environmental expenditures will be recovered in the future through the rate-setting process. The Company has recorded an equivalent amount as a regulatory asset. In 2020, the environmental regulatory asset increased by \$12 million (2019 – decreased by \$3 million) to reflect related changes in the Company's LAR environmental liabilities. 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 prudence and the timing of recovery of all of Hydro One's actual environmental expenditures. In the absence of rate-regulated accounting, 2020 OM&A expenses would have been higher by \$12 million (2019 – lower by \$3 million). In addition, 2020 amortization expense would have been lower by \$23 million (2019 – \$25 million), and 2020 financing charges would have been higher by \$3 million (2019 – \$4 million).

Post-Retirement and Post-Employment Benefits – Non-Service Cost

Hydro One has recorded a regulatory asset relating to the future recovery of its post-retirement and post-employment benefits other than service costs. The regulatory asset includes the applicable tax impact to reflect taxes payable. Prior to adoption of ASU 2017-07 in 2018, these amounts were capitalized to property, plant and equipment and intangible assets. As part of Hydro One Networks' 2020–2022 Transmission Decision, the OEB concluded that the non-service cost component of Hydro One's OPEB costs shall be recognized as OM&A for both its transmission and distribution businesses. Hydro One Networks distribution continues to record the non-service cost component of OPEBs in this account until its next rebasing application. The OEB approved the disposition of Hydro One Networks transmission's account balance as at December 31, 2018, including accrued interest, which is being collected from ratepayers over a three-year period ending December 31, 2022.

Foregone Revenue Deferral

As at December 31, 2020, the foregone revenue deferral account is primarily made up of the difference between revenue earned by Hydro One Networks transmission, NRLP, B2M LP, and HOSSM under the approved UTRs based on OEB-approved 2020 rates revenue requirement and load forecast and the revenues earned under interim 2020 UTRs. Hydro One Networks transmission's foregone revenue, including accrued interest, is being collected from ratepayers over a two-year period ending December 31, 2022. NRLP, B2M LP, and HOSSM's foregone revenue, including accrued interest, is being collected from ratepayers over a one-year period ended December 31, 2021. As at December 31, 2019, the foregone revenue deferral account was primarily made up of the difference between revenue earned based on distribution rates approved by the OEB in Hydro One Networks' 2018–2022 distribution rates application, effective May 1, 2018, and

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revenue earned under the interim rates until the approved 2018 and 2019 rates were implemented on July 1, 2019. This amount was recovered from ratepayers over an eighteen-month period ending December 31, 2020.

Post-Retirement and Post-Employment Benefits

In accordance with OEB rate orders, post-retirement and post-employment benefits costs are recovered on an accrual basis. 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 the present value of the actuarially determined benefit obligation at each year end based on an annual actuarial report, with an offset to the associated regulatory asset or liability as the case may be, to the extent of the remeasurement adjustment. In the absence of rate-regulated accounting, 2020 OCL would have been lower by \$46 million (2019 – higher by \$235 million).

Stock-based Compensation

The Company recognizes costs associated with share grant plans in a regulatory asset as management considers it probable that share grant plans' costs will be recovered in the future through the rate-setting process. In the absence of rate-regulated accounting, OM&A expenses would be lower by \$1 million (2019 – \$nil). Share grant costs are transferred to labour costs at the time the share grants vest and are issued, and are recovered in rates in accordance with recovery of said labour costs.

CDM Variance

The CDM variance account tracks the impact of actual CDM and demand response programs on the actual load forecast compared to the estimated load forecast included in revenue requirement. As per the OEB's decision on Hydro One Networks' 2017 and 2018 transmission rates, and 2019 transmission rates, this account was maintained to record any variances for 2017, 2018, and 2019. A CDM variance amount for 2017 was calculated and proposed for disposition in Hydro One Networks' 2020-2022 transmission rate application. In April 2020, the amount as at December 31, 2018, including accrued interest, was approved for disposition by the OEB and was recognized as a regulatory asset. The amount was approved to be recovered from ratepayers over a three-year period ending December 31, 2022.

Debt Premium

The value of debt assumed in the acquisition of HOSSM has been recorded at fair value in accordance with US GAAP – Business Combinations. The OEB allows for recovery of interest at the coupon rate of the Senior Secured Bonds and a regulatory asset has been recorded for the difference between the fair value and face value of this debt. The debt premium is recovered over the remaining term of the debt.

Retail Settlement Variance Account (RSVA)

Hydro One has deferred certain retail settlement variance amounts under the provisions of Article 490 of the OEB's Accounting Procedures Handbook. The RSVA account tracks the difference between the cost

of power purchased from the Independent Electricity System Operator (IESO) and the cost of power recovered from ratepayers. The balance as at December 31, 2014, including accrued interest, was approved for disposition by the OEB in March 2019, and was transferred to the 2019-2020 Rate Rider. The balance as at December 31, 2019, including accrued interest, was approved for disposition over a one-year period ending December 31, 2021 by the OEB as part of Hydro One Networks distribution 2021 annual update rate application.

Tax Rule Changes Variance

The 2019 federal and Ontario budgets (Budgets) provided certain time-limited investment incentives permitting Hydro One to deduct accelerated capital cost allowance of up to three times the first-year rate for capital investments acquired after November 20, 2018 and placed in-service before January 1, 2028 (Accelerated Depreciation). Following the enactment of the Budget measures in the second quarter of 2019, the OEB directed all Ontario regulated utilities including Hydro One to track the full revenue impact of the tax benefits related to the Accelerated Depreciation rules to ratepayers. The tax benefit to be returned to ratepayers in the future gave rise to a regulatory liability and resulted in a decrease in revenues as current rates do not include the benefit of the Accelerated Depreciation; therefore, the revenue subject to refund cannot be recognized.

Earnings Sharing Mechanism Deferral

In March 2019, the OEB approved the establishment of an earnings sharing mechanism deferral account for Hydro One Networks distribution to record over-earnings including tax impacts, if any, realized for any year from 2018 to 2022. Under this mechanism, Hydro One shares 50% of regulated earnings that exceed the OEB-approved regulatory return-on-equity by more than 100 basis points with distribution ratepayers. This account is asymmetrical to the benefit of ratepayers. The balance as at December 31, 2019, including accrued interest, was approved for disposition on an interim basis over a one year period ending December 31, 2021 by the OEB as part of Hydro One Networks distribution 2021 annual update rate application. A similar account was also approved for B2M LP in January 2020, and Hydro One Networks transmission and NRLP in April 2020. No amounts have been recorded for these subsidiaries.

Pension Cost Differential

Variances between the pension cost recognized and the cost embedded in rates as part of the rate-setting process for Hydro One Networks' transmission and distribution businesses are recognized as a regulatory asset or regulatory liability, as the case may be. Variances into the account were not recognized for the distribution business in 2019 in accordance with the OEB's decision on the motion to review and vary the OEB's decision as it relates to rates revenue requirement recovery of employer pension costs. In March 2019, the OEB approved the disposition of the distribution business portion of the balance as at December 31, 2016, including accrued interest, and the balance was transferred to the 2019-2020 Rate Rider. In April 2020, the OEB approved the disposition of the transmission business portion of the balance as at December 31, 2018, including accrued interest, which is being returned to ratepayers over a three-year period ending December 31, 2022. In the absence of rate-regulated accounting, 2020 revenue would have been higher by \$1 million (2019 – \$5 million).

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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. The smart grid variance account balance as at December 31, 2016, including accrued interest, was approved for disposition by the OEB in March 2019, and was transferred to the 2019–2020 Rate Rider.

Asset Removal Costs Cumulative Variance

In April 2020, the OEB approved the establishment of an asset removal costs cumulative variance account for Hydro One Networks transmission to record the difference between the revenue requirement associated with forecast asset removal costs included in depreciation expense and actual asset removal costs incurred from 2020 to 2022. This account is asymmetrical to the benefit of ratepayers on a cumulative basis over the 2020–2022 rate period.

External Revenue Variance

The external revenue variance account balance reflects the difference between Hydro One Networks transmission's actual export service revenue and external revenues from secondary land use, and the OEB-approved amounts. The account also records the difference between actual net external station maintenance, engineering and construction services revenue, and other external revenue, and the OEB-approved amounts. In April 2020, the OEB approved the disposition of the external revenue variance account as at December 31, 2018, including accrued interest, which is being returned to ratepayers over a three-year period ending December 31, 2022.

Distribution Rate Riders

In March 2019, as part of its decision on Hydro One Networks' distribution rates application for 2018–2022, the OEB approved the disposition of certain deferral and variance accounts which were accumulated in a 2019–2020 Rate Rider. The Distribution Rate Riders

balance includes the 2019–2020 Rate Rider, where amounts were returned to ratepayers over an 18-months period ending December 31, 2020. There is a balance in the 2019–2020 Rate Rider that remains which represents amounts that shall be collected from ratepayers in a future rate application. This amount is largely offset by the 2015–2017 Rate Rider balance, which was approved for disposition over a one-year period ending December 31, 2021 by the OEB as part of Hydro One Networks distribution 2021 annual update rate application.

COVID-19 Emergency Deferral

The COVID-19 emergency deferral account comprises of five sub-accounts established to track incremental costs and lost revenues related to the COVID-19 pandemic: (i) Billing and System Changes as a Result of the Emergency Order Regarding Time-of-Use Pricing, (ii) Lost Revenues Arising from the COVID-19 Emergency, (iii) Other Incremental Costs, (iv) Foregone Revenues from Postponing Rate Implementation, and (v) Bad Debt.

During the year, the Company had initially assessed that it was probable that incremental bad debt expense associated with the COVID-19 pandemic would be recovered in future rates, and as a result, a \$14 million regulatory asset had been recognized. On December 16, 2020, the OEB Staff released their proposal on the COVID-19 deferral accounts which introduces certain criteria that may need to be satisfied for amounts to be eligible for recovery. Based on Hydro One's interpretation of the OEB Staff's proposal, the Company reversed the regulatory asset recorded for incremental bad debt and recognized a corresponding increase to bad debt expense in the consolidated statement of operations and comprehensive income. Hydro One continues to track certain incremental costs and lost revenues that have arisen due to the COVID-19 pandemic. As at December 31, 2020, Hydro One has assessed that these amounts are not probable for future recovery in rates and no amounts related to the COVID-19 pandemic have been recognized as regulatory assets.

14. OTHER LONG-TERM ASSETS

As at December 31 (millions of dollars)

| | 2020 | 2019 |
|-------------------------------|-----------|-----------|
| Right-of-Use assets (Note 23) | 77 | 75 |
| Investments (Note 18) | 7 | 2 |
| Derivative assets (Note 18) | — | 3 |
| Other long-term assets | 8 | 7 |
| | 92 | 87 |

15. ACCOUNTS PAYABLE AND OTHER CURRENT LIABILITIES

| As at December 31 (millions of dollars) | 2020 | 2019 |
|---|--------------|------------|
| Accrued liabilities | 566 | 612 |
| Accounts payable | 238 | 189 |
| Accrued interest | 118 | 104 |
| Regulatory liabilities (Note 13) | 66 | 45 |
| Environmental liabilities (Note 21) | 33 | 30 |
| Lease obligations (Note 23) | 12 | 9 |
| Derivative liabilities (Note 18) | 11 | — |
| | 1,044 | 989 |

16. OTHER LONG-TERM LIABILITIES

| As at December 31 (millions of dollars) | 2020 | 2019 |
|---|--------------|--------------|
| Post-retirement and post-employment benefit liability (Note 20) | 1,797 | 1,723 |
| Pension benefit liability (Note 20) | 1,660 | 1,125 |
| Environmental liabilities (Note 21) | 100 | 111 |
| Lease obligations (Note 23) | 70 | 69 |
| Derivative liabilities (Note 18) | 14 | — |
| Asset retirement obligations (Note 22) | 13 | 10 |
| Long-term accounts payable | 3 | 3 |
| Other long-term liabilities | 17 | 14 |
| | 3,674 | 3,055 |

17. 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 Hydro One Inc.'s Commercial Paper Program which has a maximum authorized amount of \$2,300 million. These short-term notes are denominated in Canadian dollars with varying maturities up to 365 days. The Commercial Paper

Program is supported by Hydro One Inc.'s revolving standby credit facilities totalling \$2,300 million.

At December 31, 2020, Hydro One's consolidated committed, unsecured and undrawn credit facilities (Operating Credit Facilities) consisted of the following:

| (millions of dollars) | Maturity | Total Amount | Amount Drawn |
|--|-----------|--------------|--------------|
| Hydro One Inc. | | | |
| Revolving standby credit facilities | June 2024 | 2,300 | — |
| Hydro One | | | |
| Five-year senior, revolving term credit facility | June 2024 | 250 | — |
| Total | | 2,550 | — |

The Company may use the Operating Credit Facilities for working capital and general corporate purposes. If used, interest on the Operating 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 that no event of default has occurred or would result from such credit extension.

Subsidiary Debt Guarantee

Hydro One Holdings Limited (HOHL) is an indirect wholly-owned subsidiary of Hydro One that may offer and sell debt securities. Any debt securities issued by HOHL are fully and unconditionally guaranteed by the Company. At December 31, 2020 and 2019, no debt securities have been issued by HOHL.

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Long-Term Debt

The following table presents long-term debt outstanding at December 31, 2020 and 2019:

| As at December 31 (millions of dollars) | 2020 | 2019 |
|---|--------|--------|
| 4.40% Series 20 notes due 2020 | — | 300 |
| 1.62% Series 33 notes due 2020 ¹ | — | 350 |
| 1.84% Series 34 notes due 2021 | 500 | 500 |
| 2.57% Series 39 notes due 2021 ¹ | 300 | 300 |
| 3.20% Series 25 notes due 2022 | 600 | 600 |
| 0.71% Series 48 notes due 2023 | 600 | — |
| 2.54% Series 42 notes due 2024 | 700 | 700 |
| 1.76% Series 45 notes due 2025 | 400 | — |
| 2.97% Series 40 notes due 2025 | 350 | 350 |
| 2.77% Series 35 notes due 2026 | 500 | 500 |
| 3.02% Series 43 notes due 2029 | 550 | 550 |
| 2.16% Series 46 notes due 2030 | 400 | — |
| 7.35% Debentures due 2030 | 400 | 400 |
| 1.69% Series 49 notes due 2031 | 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 |
| 3.91% Series 36 notes due 2046 | 350 | 350 |
| 3.72% Series 38 notes due 2047 | 450 | 450 |
| 3.63% Series 41 notes due 2049 | 750 | 750 |
| 2.71% Series 47 notes due 2050 | 500 | — |
| 3.64% Series 44 notes due 2050 | 250 | 250 |
| 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 |
| Hydro One Inc. long-term debt (a) | 12,995 | 11,345 |
| 1.41% Series 2020-1 notes due 2027 | 425 | — |
| Hydro One long-term debt (b) | 425 | — |
| 6.6% Senior Secured Bonds due 2023 (Principal amount – \$102 million) | 113 | 121 |
| 4.6% Note Payable due 2023 (Principal amount – \$36 million) | 38 | 39 |
| HOSSM long-term debt (c) | 151 | 160 |
| | 13,571 | 11,505 |
| Add: Net unamortized debt premiums | 10 | 12 |
| Add: Unrealized mark-to-market loss ¹ | 3 | 1 |
| Less: Unamortized deferred debt issuance costs | (52) | (43) |
| Total long-term debt | 13,532 | 11,475 |

¹ The unrealized mark-to-market net loss of \$3 million (2019 – \$1 million) relates to \$300 million Series 39 notes due 2021. The unrealized mark-to-market net loss is offset by a \$3 million unrealized mark-to-market net gain (2019 – \$1 million) on the related fixed-to-floating interest-rate swap agreements, which are accounted for as fair value hedges.

Notes to Consolidated Financial Statements

(a) Hydro One Inc. long-term debt

At December 31, 2020, long-term debt of \$12,995 million (2019 – \$11,345 million) was outstanding, the majority of which was issued under Hydro One Inc.'s Medium Term Note (MTN) Program. In April 2020, Hydro One Inc. filed a short form base shelf prospectus for its MTN Program, which has a maximum authorized principal amount of notes issuable of \$4,000 million, expiring in May 2022. At December 31, 2020, \$2,800 million remained available for issuance under this MTN Program prospectus.

In 2020, Hydro One Inc. issued long-term debt totalling \$2,300 million (2019 – \$1,500 million) and repaid long-term debt of \$650 million (2019 – \$728 million) under its MTN Program.

(b) Hydro One long-term debt

On August 20, 2020, Hydro One filed a short form base shelf prospectus (Universal Base Shelf Prospectus) with securities regulatory authorities in Canada. The Universal Base Shelf Prospectus allows Hydro One to offer, from time to time in one or more public offerings, up to \$2,000 million of debt, equity or other securities, or any combination thereof, during the 25-month period ending on September 20, 2022. At December 31, 2020, \$1,575 million remained available for issuance.

In 2020, Hydro One issued \$425 million of long-term debt with a maturity date of October 15, 2027 and a coupon rate of 1.41%, under the Universal Base Shelf Prospectus (2019 – \$nil).

(c) HOSSM long-term debt

At December 31, 2020, HOSSM long-term debt of \$151 million (2019 – \$160 million), with a principal amount of \$138 million (2019 – \$141 million) was outstanding. In 2020, no long-term debt was issued (2019 – \$nil), and \$3 million (2019 – \$2 million) of long-term debt was repaid.

The total long-term debt is presented on the consolidated balance sheets as follows:

| As at December 31 (millions of dollars) | 2020 | 2019 |
|---|---------------|---------------|
| Current liabilities: | | |
| Long-term debt payable within one year | 806 | 653 |
| Long-term liabilities: | | |
| Long-term debt | 12,726 | 10,822 |
| Total long-term debt | 13,532 | 11,475 |

Principal and Interest Payments

At December 31, 2020, future principal repayments, interest payments, and related weighted-average interest rates were as follows:

| | Long-Term Debt Principal Repayments (millions of dollars) | Interest Payments (millions of dollars) | Weighted-Average Interest Rate (%) |
|------------|---|---|--|
| Year 1 | 803 | 498 | 2.1 |
| Year 2 | 604 | 483 | 3.2 |
| Year 3 | 731 | 467 | 1.7 |
| Year 4 | 700 | 452 | 2.5 |
| Year 5 | 750 | 434 | 2.3 |
| | 3,588 | 2,334 | 2.3 |
| Years 6-10 | 2,275 | 2,004 | 3.3 |
| Thereafter | 7,695 | 4,073 | 4.6 |
| | 13,558 | 8,411 | 3.8 |

18. 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, 2020 and 2019, the Company's carrying amounts of cash and cash equivalents, accounts receivable, due from related parties, short-term notes payable, accounts payable, and due to related parties are representative of fair value due to 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, 2020 and 2019 are as follows:

| As at December 31 (millions of dollars) | 2020 Carrying Value | 2020 Fair Value | 2019 Carrying Value | 2019 Fair Value |
|---|------------------------|--------------------|------------------------|--------------------|
| Long-term debt measured at fair value: | | | | |
| \$50 million of MTN Series 33 notes | — | — | 50 | 50 |
| \$300 million MTN Series 39 notes | 303 | 303 | 301 | 301 |
| Other notes and debentures | 13,229 | 16,226 | 11,124 | 13,121 |
| Long-term debt, including current portion | 13,532 | 16,529 | 11,475 | 13,472 |

Fair Value Measurements of Derivative Instruments

Fair Value Hedges

At December 31, 2020, Hydro One Inc. had interest-rate swaps with a total notional amount of \$300 million (2019 – \$350 million) that were used to convert fixed-rate debt to floating-rate debt. These swaps are classified as fair value hedges. Hydro One Inc.'s fair value hedge exposure was approximately 2% (2019 – 3%) of its total long-term debt. At December 31, 2020, Hydro One Inc. had the following interest-rate swap designated as a fair value hedge:

- a \$300 million fixed-to-floating interest-rate swap agreement to convert the \$300 million MTN Series 39 notes maturing June 25, 2021 into three-month variable rate debt.

Cash Flow Hedges

At December 31, 2020, Hydro One Inc. had a total of \$800 million in 3-year pay-fixed, receive-floating interest-rate swap agreements designated as cash flow hedges. These cash flow hedges are intended to offset the variability of interest rates on the issuances of short-term commercial paper between January 9, 2020 and March 9, 2023.

In March 2020, Hydro One Inc. entered into \$400 million of bond forward agreements. Consistent with their intention to mitigate the Company's exposure to variability in interest rates on forecasted fixed-rate long-term debt issuance, the \$400 million bond forward

agreements were settled upon the issuance of the Series 48 notes in October 2020, for a payment of \$3 million on settlement, which is being amortized over the term of the related note.

At December 31, 2020 and 2019, the Company had no derivative instruments classified as undesignated contracts.

In October 2017, the Company entered into a Foreign-Exchange Contract to convert \$1,400 million Canadian to US dollars at an initial forward rate of 1.27486 Canadian per 1.00 US dollars, and a range up to 1.28735 Canadian per 1.00 US dollars based on the settlement date. The Foreign-Exchange Contract was contingent on the Company closing the proposed Merger (see Note 4 – Business Combinations) and was intended to mitigate the foreign currency risk related to the portion of the Merger purchase price financed with the issuance of Convertible Debentures. This contract was an economic hedge and did not qualify for hedge accounting. It has been accounted for as an undesignated contract with changes in fair value being recorded in earnings as they occurred. As a result of the termination of the Merger agreement (see Note 4 – Business Combinations) in January 2019, the Foreign-Exchange Contract was terminated and previously recorded unrealized gains of \$22 million were reversed in financing charges in 2019. No payment was due or payable by Hydro One related to the Foreign-Exchange Contract.

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Fair Value Hierarchy

The fair value hierarchy of financial assets and liabilities at December 31, 2020 and 2019 is as follows:

| As at December 31, 2020 (millions of dollars) | Carrying Value | Fair Value | Level 1 | Level 2 | Level 3 |
|---|----------------|---------------|----------|---------------|----------|
| Assets: | | | | | |
| Investments (Note 14) | 7 | 7 | — | — | 7 |
| Derivative instruments (Note 10) | | | | | |
| Fair value hedges | 3 | 3 | — | 3 | — |
| | 10 | 10 | — | 3 | 7 |
| Liabilities: | | | | | |
| Long-term debt, including current portion | 13,532 | 16,529 | — | 16,529 | — |
| Derivative instruments (Notes 15, 16) | | | | | |
| Cash flow hedges, including current portion | 25 | 25 | — | 25 | — |
| | 13,557 | 16,554 | — | 16,554 | — |

| As at December 31, 2019 (millions of dollars) | Carrying Value | Fair Value | Level 1 | Level 2 | Level 3 |
|---|----------------|------------|---------|---------|---------|
| Assets: | | | | | |
| Investments (Note 14) | 2 | 2 | — | — | 2 |
| Derivative instruments (Note 14) | | | | | |
| Fair value hedges | 1 | 1 | — | 1 | — |
| Cash flow hedges | 2 | 2 | — | 2 | — |
| | 5 | 5 | — | 3 | 2 |
| Liabilities: | | | | | |
| Long-term debt, including current portion | 11,475 | 13,472 | — | 13,472 | — |
| | 11,475 | 13,472 | — | 13,472 | — |

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 transfers between any of the fair value levels during the years ended December 31, 2020 or 2019.

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, 2020 and 2019:

| Year ended December 31 (millions of dollars) | 2020 | 2019 |
|---|------|------|
| Fair value of assets – beginning | 2 | 22 |
| Additions | 5 | 2 |
| Unrealized loss on Foreign-Exchange Contract included in financing charges (Note 4) | — | (22) |
| Fair value of assets – ending | 7 | 2 |

Notes to Consolidated Financial Statements

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 which results from changes in values, 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 anticipated interest rates into account. The Company is not currently exposed to material commodity price risk or material foreign exchange risk.

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 may utilize interest-rate swaps designated as fair value hedges as a means to manage its interest rate exposure to achieve a lower cost of debt. The Company may also utilize interest-rate derivative instruments, such as cash flow hedges, to manage its exposure to short-term interest rates or to lock in interest-rate levels on forecasted financing.

A hypothetical 100 basis points increase in 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, 2020 and 2019.

For derivative instruments that are designated and qualify as fair value hedges, the gain or loss on the derivative instrument 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, 2020 and 2019 were not material.

For derivative instruments that are designated and qualify as cash flow hedges, the unrealized gain or loss, net of tax, on the derivative instrument is recorded as OCI/OCL and is reclassified to results of operations in the same period during which the hedged transaction affects results of operations. The unrealized loss, net of tax, on the cash flow hedges for the year ended December 31, 2020 recorded in OCL was \$20 million (2019 – unrealized gain of \$2 million), resulting in an accumulated other comprehensive loss (AOCL) of \$18 million related to cash flow hedges at December 31, 2020 (2019 – AOCL of \$2 million). During the year ended December 31, 2020, a loss of \$7 million was reclassified to financing charges (2019 – \$nil). The Company estimates that the amount of AOCL, net of tax, related to cash flow hedges to be reclassified to results of operations in the next 12 months is \$8 million. Actual amounts reclassified to results of operations depend on the interest rate risk in effect until the derivative contracts mature. For all forecasted transactions, at December 31, 2020, the maximum term over which the Company is hedging exposures to the variability of cash flows is approximately two years.

The Pension Plan manages market risk by diversifying investments in accordance with the Pension Plan's Statement of Investment Policies and Procedures (SIPP). Interest rate risk arises from the possibility that changes in interest rates will affect the fair value of the Pension Plan's financial instruments. In addition, changes in interest rates can

also impact discount rates which impact the valuation of the pension and post-retirement and post-employment liabilities. Currency risk is the risk that the value of the Pension Plan's financial instruments will fluctuate due to changes in foreign currencies relative to the Canadian dollar. Other price risk is the risk that the value of the Pension Plan's investments in equity securities will fluctuate as a result of changes in market prices, other than those arising from interest rate risk or currency risk. All three factors may contribute to changes in values of the Pension Plan investments. See Note 20 – Pension and Post-Retirement and Post-Employment Benefits for further details.

Credit Risk

Financial assets create a risk that a counterparty will fail to discharge an obligation, causing a financial loss. At December 31, 2020 and 2019, 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 material amount of revenue from any single customer. At December 31, 2020 and 2019, there was no material accounts receivable balance due from any single customer.

At December 31, 2020, the Company's allowance for doubtful accounts was \$46 million (2019 – \$22 million). The allowance for doubtful accounts reflects the Company's CECL for all accounts receivable balances, which are based on historical overdue balances, customer payments and write-offs. At December 31, 2020, approximately 4% (2019 – 5%) of the Company's net accounts receivable were outstanding for more than 60 days. Please see Note 9 – Accounts Receivable for additions to allowance for doubtful accounts related to the impact of the COVID-19 pandemic.

Hydro One manages its counterparty credit risk through various techniques including (i) entering into transactions with highly rated counterparties, (ii) limiting total exposure levels with individual counterparties, (iii) entering into master agreements which enable net settlement and the contractual right of offset, and (iv) monitoring the financial condition of counterparties. The Company monitors current credit exposure to counterparties on both 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 maximum credit exposure of derivative contracts, before collateral, is represented by the fair value of contracts at the reporting date. At December 31, 2020 and 2019, the counterparty credit risk exposure on the fair value of these interest-rate swap contracts was not material. At December 31, 2020, Hydro One's credit exposure for all derivative instruments, and applicable payables and receivables, was with four financial institutions with investment grade credit ratings as counterparties.

The Pension Plan manages its counterparty credit risk with respect to bonds by investing in investment-grade corporate and government bonds and with respect to derivative instruments by transacting only with highly rated financial institutions and by ensuring that exposure is diversified across counterparties.

Notes to Consolidated Financial Statements

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 operating liquidity requirements using cash and cash equivalents on hand, funds from operations, the issuance of commercial paper, and the Operating Credit Facilities. The short-term liquidity under the commercial paper program, the Operating Credit Facilities, and anticipated levels of funds from operations are expected to be sufficient to fund the Company's operating requirements. The Company's currently available liquidity is also expected to be sufficient to address any reasonably foreseeable impacts that the COVID-19 pandemic may have on the Company's cash requirements.

On August 20, 2020, Hydro One filed a Universal Base Shelf Prospectus with securities regulatory authorities in Canada. The Universal Base Shelf Prospectus allows Hydro One to offer, from time to time in one or more public offerings, up to \$2,000 million of debt, equity or other securities, or any combination thereof, during the 25-month period ending on September 20, 2022.

On September 21, 2020, in order to secure required funding for the redemption of the Series 1 preferred shares (Preferred Shares), Hydro

One secured binding commitments for three bilateral two-year senior unsecured term credit facilities (Bilateral Credit Facilities) totalling \$201 million. On October 15, 2020, these bilateral commitments were terminated upon receipt of the proceeds of Hydro One's \$425 million long-term debt offering.

On December 17, 2020, HOHL filed a short form base shelf prospectus (US Debt Shelf Prospectus) with securities regulatory authorities in Canada and the US to replace a previous prospectus that expired in December 2020. The US Debt Shelf Prospectus allows HOHL to offer, from time to time in one or more public offerings, up to US\$3,000 million of debt securities, unconditionally guaranteed by Hydro One, during the 25-month period ending on January 17, 2023. At December 31, 2020, no securities have been issued under the US Debt Shelf Prospectus.

The Pension Plan's short-term liquidity is provided through cash and cash equivalents, contributions, investment income and proceeds from investment transactions. In the event that investments must be sold quickly to meet current obligations, the majority of the Pension Plan's assets are invested in securities that are traded in an active market and can be readily disposed of as liquidity needs arise.

19. 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. At December 31, 2020 and 2019, the Company's capital structure was as follows:

| As at December 31 (millions of dollars) | 2020 | 2019 |
|---|---------------|---------------|
| Long-term debt payable within one year | 806 | 653 |
| Short-term notes payable | 800 | 1,143 |
| Less: cash and cash equivalents | (757) | (30) |
| | 849 | 1,766 |
| Long-term debt | 12,726 | 10,822 |
| Preferred shares | — | 418 |
| Common shares | 5,678 | 5,661 |
| Retained earnings | 4,838 | 3,667 |
| Total capital | 24,091 | 22,334 |

Hydro One Inc. and HOSSM have customary covenants typically associated with long-term debt. Long-term debt and credit facility covenants limit 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, 2020, the Company was in compliance with all financial covenants and limitations associated with the outstanding borrowings and credit facilities.

20. PENSION AND POST-RETIREMENT AND POST-EMPLOYMENT BENEFITS

Hydro One has a Pension Plan, a DC Plan, a supplemental pension plan (Supplemental Plan), and post-retirement and post-employment benefit plans.

DC Plan

Hydro One established a DC Plan effective January 1, 2016. The DC Plan covers eligible management employees hired on or after January 1, 2016, as well as management employees hired before January 1, 2016 who were not eligible to join the Pension Plan as of September 30, 2015. Members of the DC Plan have an option to contribute 4%, 5% or 6% of their pensionable earnings, with matching contributions by Hydro One up to an annual contribution limit. There is also a Supplemental DC Plan that provides members of the DC Plan with employer contributions beyond the limitations imposed by the *Income Tax Act* (Canada) in the form of credits to a notional account. Hydro One contributions to the DC Plan for the year ended December 31, 2020 were \$2 million (2019 – \$1 million).

Pension Plan, Supplemental Plan, and Post-Retirement and Post-Employment Plans

The Pension Plan is a defined benefit contributory plan which covers eligible regular employees of Hydro One and its subsidiaries. The Pension Plan provides benefits based on highest three-year average pensionable earnings. For management employees who commenced employment on or after January 1, 2004, and for the Society of United Professionals (Society)-represented staff hired after November 17, 2005, benefits are based on highest five-year average pensionable earnings. After retirement, pensions are indexed to inflation. Membership in the Pension Plan was closed to management employees who were not eligible or had not irrevocably elected to join the Pension Plan as of September 30, 2015. These employees are eligible to join the DC Plan.

Company and employee contributions to the Pension Plan are based on actuarial reports, including valuations performed at least every three years, and actual or projected levels of pensionable earnings, as applicable. The most recent actuarial valuation was performed effective December 31, 2018 and filed on September 30, 2019. The next actuarial valuation will be performed no later than effective December 31, 2021. Total annual cash Pension Plan employer contributions for 2020 were \$57 million (2019 – \$61 million). Estimated annual Pension Plan employer contributions for the years 2021, 2022, 2023, 2024, 2025, 2026 and 2027 are approximately \$59 million, \$93 million, \$107 million, \$111 million, \$111 million, \$113 million and \$118 million, respectively.

The Supplemental Plan provides members of the Pension Plan with benefits that would have been earned and payable under the Pension Plan beyond the limitations imposed by the *Income Tax Act* (Canada). The Supplemental Plan obligation is included with other post-retirement and post-employment benefit obligations on the consolidated balance sheets.

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 and post-retirement benefit obligations is generally recognized over the expected average remaining service period of the employees and using the corridor approach for the post-retirement benefit plan. For post-employment benefit plan, the impact of changes in assumptions are recognized immediately in the net periodic benefit cost. The measurement date for the Plans is December 31.

Notes to Consolidated Financial Statements

The following tables provide the components of the unfunded status of the Company's Plans at December 31, 2020 and 2019:

| Year ended December 31 (millions of dollars) | Pension Benefits | | Post-Retirement and Post-Employment Benefits | |
|---|------------------|-------|--|-------|
| | 2020 | 2019 | 2020 | 2019 |
| Change in projected benefit obligation | | | | |
| Projected benefit obligation, beginning of year | 8,973 | 7,752 | 1,783 | 1,465 |
| Current service cost | 215 | 145 | 70 | 56 |
| Employee contributions | 56 | 55 | — | — |
| Interest cost | 284 | 303 | 58 | 60 |
| Benefits paid | (381) | (371) | (45) | (47) |
| Net actuarial loss (gain) | 465 | 1,089 | (42) | 243 |
| Transfers from other plans ^{1,2} | 151 | — | 33 | 6 |
| Projected benefit obligation, end of year | 9,763 | 8,973 | 1,857 | 1,783 |
| Change in plan assets | | | | |
| Fair value of plan assets, beginning of year | 7,848 | 7,205 | — | — |
| Actual return on plan assets | 425 | 922 | — | — |
| Benefits paid | (381) | (371) | (45) | (47) |
| Employer contributions | 57 | 61 | 45 | 47 |
| Employee contributions | 56 | 55 | — | — |
| Administrative expenses | (22) | (24) | — | — |
| Transfers from other plans ² | 120 | — | — | — |
| Fair value of plan assets, end of year | 8,103 | 7,848 | — | — |
| Unfunded status | 1,660 | 1,125 | 1,857 | 1,783 |

1 In 2019, liabilities associated with the HOSSM post-employment benefit plans were transferred to the Hydro One post-employment benefit plans.

2 See below for information related to the transfers from other plans in 2020.

Transfers from Other Plans

Effective March 1, 2018, certain employees who provided customer service operations for Hydro One through Inergi LP were transferred to Hydro One Networks (Transferred Employees), and began accruing pension and OPEB in the Pension Plan and post-retirement and post-employment benefit plans, respectively. Pursuant to the arrangement, Inergi LP, Vertex Customer Management (Canada) Ltd. (Vertex) and Hydro One Networks agreed to transfer the defined benefit assets and related pension obligations (for current and former members) of the Inergi LP Customer Service Operations Pension Plan and the Vertex Customer Management (Canada) Limited Pension Plan to the Pension Plan. In addition, Inergi LP, Vertex and Hydro One Networks agreed to transfer the OPEB liability related to the Transferred Employees to Hydro One's post-retirement and post-employment benefit plans. Regulatory approval for the pension transfer was received on November 27, 2019.

The transfer of the pension assets of \$120 million and related pension obligations of \$151 million was completed on March 2, 2020. The unfunded status of \$31 million was recorded as a pension benefit liability with an offsetting pension benefit regulatory asset. The transfer of the OPEB liability of \$33 million was completed on April 1, 2020. The liability was recorded as a post-retirement and post-employment benefit liability with an offset to OCL. In addition, as a part of the transfers, cash totalling \$24 million was transferred to Hydro One and recorded as an asset with an offset to OCI. Both, the OCI resulting from the transfer of the cash asset and the OCL resulting from the transfer of the other post-retirement benefit liability are being recognized in net income over the expected average remaining service lifetime (EARSL) of the Transferred Employees.

Notes to Consolidated Financial Statements

Hydro One presents its benefit obligations and plan assets net on its consolidated balance sheets as follows:

| As at December 31 (millions of dollars) | Pension Benefits | | Post-Retirement and Post-Employment Benefits | |
|---|------------------|--------------|--|--------------|
| | 2020 | 2019 | 2020 | 2019 |
| Other assets ¹ | 6 | 3 | — | — |
| Accrued liabilities | — | — | 60 | 60 |
| Pension benefit liability | 1,660 | 1,125 | — | — |
| Post-retirement and post-employment benefit liability | — | — | 1,797 | 1,723 |
| Net unfunded status | 1,654 | 1,122 | 1,857 | 1,783 |

¹ Represents the funded status of HOSSM defined benefit pension plan.

The funded or unfunded status of the Plans refers to the difference between the fair value of plan assets and the PBO 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 PBO, accumulated benefit obligation (ABO) and fair value of plan assets for the Pension Plan:

| As at December 31 (millions of dollars) | 2020 | 2019 |
|---|-------|-------|
| PBO | 9,763 | 8,973 |
| ABO | 8,817 | 8,183 |
| Fair value of plan assets | 8,103 | 7,848 |

On an ABO basis, the Pension Plan was funded at 92% at December 31, 2020 (2019 – 96%). On a PBO basis, the Pension Plan was funded at 83% at December 31, 2020 (2019 – 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, 2020 and 2019 for the Pension Plan:

| Year ended December 31 (millions of dollars) | 2020 | 2019 |
|---|------------|-----------|
| Current service cost | 215 | 145 |
| Interest cost | 284 | 303 |
| Expected return on plan assets, net of expenses | (450) | (462) |
| Prior service cost amortization | 2 | — |
| Amortization of actuarial losses | 95 | 55 |
| Net periodic benefit costs | 146 | 41 |
| Charged to results of operations¹ | 25 | 30 |

¹ The Company accounts for pension costs consistent with their inclusion in OEB-approved rates. During the year ended December 31, 2020, pension costs of \$69 million (2019 – \$73 million) were attributed to labour, of which \$25 million (2019 – \$30 million) was charged to operations, and \$44 million (2019 – \$43 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, 2020 and 2019 for the post-retirement and post-employment benefit plans:

| Year ended December 31 (millions of dollars) | 2020 | 2019 |
|---|------------|------------|
| Current service cost | 70 | 56 |
| Interest cost | 58 | 60 |
| Prior service cost amortization | 2 | — |
| Amortization of actuarial losses | 5 | 7 |
| Net periodic benefit costs | 135 | 123 |
| Charged to results of operations^{1,2} | 73 | 50 |

¹ The Company accounts for post-retirement and post-employment costs consistent with their inclusion in OEB-approved rates. During the year ended December 31, 2020, post-retirement and post-employment costs of \$135 million (2019 – \$123 million) were attributed to labour, of which \$73 million (2019 – \$50 million) was charged to operations, \$17 million (2019 – \$39 million) was recorded in the Hydro One Networks distribution post-retirement and post-employment benefits non-service cost regulatory asset, and \$45 million (2019 – \$34 million) was capitalized as part of the cost of property, plant and equipment and intangible assets.

² In the 2020-2022 Transmission Decision, the OEB approved the recovery of the non-service cost component of post-retirement and post-employment benefits as part of operation, maintenance and administration costs for the Company's transmission business. These costs were previously capitalized and recovered through rate base. As a result, during the year ended December 31, 2020, additional other post-retirement and post-employment costs of \$22 million attributed to labour were charged to operations.

Notes to Consolidated Financial Statements

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, 2020 and 2019:

| Year ended December 31 | Pension Benefits | | Post-Retirement and Post-Employment Benefits | |
|--|------------------|-------|--|-------|
| | 2020 | 2019 | 2020 | 2019 |
| Significant assumptions: | | | | |
| Weighted average discount rate | 2.60% | 3.10% | 2.60% | 3.10% |
| Rate of compensation scale escalation (long-term) | 2.25% | 2.50% | 2.25% | 2.50% |
| Rate of cost of living increase | 1.75% | 2.00% | 1.75% | 2.00% |
| Rate of increase in health care cost trends ¹ | — | — | 3.70% | 4.04% |

¹ 4.74% per annum in 2021, grading down to 3.70% per annum in and after 2031 (2019 – 5.09% per annum in 2020, grading down to 4.04% 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, 2020 and 2019. 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 | 2020 | 2019 |
|--|--------------|-------|
| Pension Benefits: | | |
| Weighted average expected rate of return on plan assets | 5.75% | 6.50% |
| Weighted average discount rate | 3.10% | 3.90% |
| Rate of compensation scale escalation (long-term) | 2.50% | 2.50% |
| Rate of cost of living increase | 2.00% | 2.00% |
| Average remaining service life of employees (years) | 15 | 15 |
| Post-Retirement and Post-Employment Benefits: | | |
| Weighted average discount rate | 3.10% | 4.00% |
| Rate of compensation scale escalation (long-term) | 2.50% | 2.50% |
| Rate of cost of living increase | 2.00% | 2.00% |
| Average remaining service life of employees (years) | 15.5 | 15.5 |
| Rate of increase in health care cost trends ¹ | 4.04% | 4.04% |

¹ 5.09% per annum in 2020, grading down to 4.04% per annum in and after 2031 (2019 – 5.19% per annum in 2019, grading down to 4.04% 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.

Notes to Consolidated Financial Statements

The effect of a 1% change in health care cost trends on the PBO for the post-retirement and post-employment benefits at December 31, 2020 and 2019 is as follows:

| As at December 31 (millions of dollars) | 2020 | 2019 |
|--|-------|-------|
| Projected benefit obligation: | | |
| Effect of a 1% increase in health care cost trends | 311 | 281 |
| Effect of a 1% decrease in health care cost trends | (234) | (213) |

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, 2020 and 2019 is as follows:

| Year ended December 31 (millions of dollars) | 2020 | 2019 |
|--|------|------|
| Service cost and interest cost: | | |
| Effect of a 1% increase in health care cost trends | 27 | 21 |
| Effect of a 1% decrease in health care cost trends | (19) | (16) |

The following approximate life expectancies were used in the mortality assumptions to determine the PBO for the pension and post-retirement and post-employment plans at December 31, 2020 and 2019:

| As at December 31 | 2020 | 2019 |
|--|---------|---------|
| Life expectancy at age 65 for a member currently at: | (years) | (years) |
| Age 65 – male | 22 | 22 |
| Age 65 – female | 25 | 25 |
| Age 45 – male | 23 | 23 |
| Age 45 – female | 26 | 26 |

Estimated Future Benefit Payments

At December 31, 2020, estimated future benefit payments to the participants of the Plans were:

| (millions of dollars) | Pension Benefits | Post-Retirement and Post-Employment Benefits |
|---|------------------|--|
| 2021 | 352 | 60 |
| 2022 | 360 | 61 |
| 2023 | 366 | 62 |
| 2024 | 371 | 62 |
| 2025 | 375 | 64 |
| 2026 through to 2030 | 1,927 | 326 |
| Total estimated future benefit payments through to 2030 | 3,751 | 635 |

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. These amounts are reflected in the following table:

| Year ended December 31 (millions of dollars) | 2020 | 2019 |
|--|------|------|
| Pension Benefits: | | |
| Actuarial loss for the year | 536 | 652 |
| Prior service cost for the year | 31 | – |
| Amortization of actuarial losses | (95) | (55) |
| Amortization of prior service cost | (2) | – |
| | 470 | 597 |
| Post-Retirement and Post-Employment Benefits: | | |
| Actuarial loss (gain) for the year | (44) | 242 |
| Amortization of actuarial losses | (2) | (7) |
| | (46) | 235 |

Notes to Consolidated Financial Statements

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, 2020 and 2019:

| Year ended December 31 (millions of dollars) | 2020 | 2019 |
|--|-------|-------|
| Pension Benefits: | | |
| Actuarial loss | 1,660 | 1,125 |
| Post-Retirement and Post-Employment Benefits: | | |
| Actuarial loss | 59 | 105 |

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:

| As at December 31 (millions of dollars) | Pension Benefits | | Post-Retirement and Post-Employment Benefits | |
|---|------------------|------|--|------|
| | 2020 | 2019 | 2020 | 2019 |
| Prior service cost | 2 | — | 4 | — |
| Actuarial loss | 124 | 95 | 2 | 2 |

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 it comes 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 fulfils its primary objective by adhering to specific investment policies outlined in its Statement of Investment Policies and Procedures (SIPP), which is

reviewed and approved annually by the Human Resource Committee of Hydro One's Board of Directors. The Company manages net assets by engaging external investment managers who are charged with the fiduciary 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 underlying investment 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, 2020, the Pension Plan target asset allocations and weighted average asset allocations were as follows:

| | Target Allocation (%) | Pension Plan Assets (%) |
|--------------------------------|-----------------------|-------------------------|
| Equity securities | 45 | 51 |
| Debt securities | 35 | 35 |
| Real Estate and Infrastructure | 20 | 14 |
| | 100 | 100 |

At December 31, 2020, the Pension Plan held \$23 million (2019 – \$21 million) Hydro One corporate bonds and \$565 million (2019 – \$504 million) of debt securities of the Province.

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, 2020 and 2019. 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, 2020 and 2019, there were no significant concentrations (defined as greater than 10% of plan assets) of risk in the Pension Plan's assets.

The Pension Plan's Statement of Investment Beliefs and Guidelines provides guidelines and restrictions for eligible investments taking

into account credit ratings, maximum investment exposure and other controls in order to limit the impact of this risk. 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 highly rated financial institutions, and also by 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.

Notes to Consolidated Financial Statements

Fair Value Measurements

The following tables present the Pension Plan assets and liabilities measured and recorded at fair value on a recurring basis and their level within the fair value hierarchy at December 31, 2020 and 2019:

| As at December 31, 2020 (millions of dollars) | Level 1 | Level 2 | Level 3 | Total |
|---|--------------|--------------|--------------|--------------|
| Pooled funds | — | 21 | 1,429 | 1,450 |
| Cash and cash equivalents | 163 | — | — | 163 |
| Short-term securities | — | 175 | — | 175 |
| Derivative instruments | — | 2 | — | 2 |
| Corporate shares – Canadian | 142 | — | — | 142 |
| Corporate shares – Foreign | 3,335 | 209 | — | 3,544 |
| Bonds and debentures – Canadian | — | 2,499 | — | 2,499 |
| Bonds and debentures – Foreign | — | 96 | — | 96 |
| Total fair value of plan assets¹ | 3,640 | 3,002 | 1,429 | 8,071 |
| Derivative instruments | — | 1 | — | 1 |
| Total fair value of plan liabilities¹ | — | 1 | — | 1 |

¹ At December 31, 2020, the total fair value of Pension Plan assets and liabilities excludes \$39 million of interest and dividends receivable, \$6 million of pension administration expenses payable, \$2 million of taxes payable, \$6 million payable to participants, \$17 million of sold investments receivable, and \$9 million of purchased investments payable.

| As at December 31, 2019 (millions of dollars) | Level 1 | Level 2 | Level 3 | Total |
|---|--------------|--------------|--------------|--------------|
| Pooled funds | — | 22 | 1,079 | 1,101 |
| Cash and cash equivalents | 159 | — | — | 159 |
| Short-term securities | — | 98 | — | 98 |
| Derivative instruments | — | 5 | — | 5 |
| Corporate shares – Canadian | 107 | — | — | 107 |
| Corporate shares – Foreign | 3,545 | 219 | — | 3,764 |
| Bonds and debentures – Canadian | — | 2,427 | — | 2,427 |
| Bonds and debentures – Foreign | — | 165 | — | 165 |
| Total fair value of plan assets¹ | 3,811 | 2,936 | 1,079 | 7,826 |
| Derivative instruments | — | 2 | — | 2 |
| Total fair value of plan liabilities¹ | — | 2 | — | 2 |

¹ At December 31, 2019, the total fair value of Pension Plan assets and liabilities excludes \$36 million of interest and dividends receivable, \$10 million of pension administration expenses payable, \$3 million of sold investments receivable, and \$5 million of purchased investments payable.

See Note 18 – Fair Value of Financial Instruments and Risk Management for a description of levels within the fair value hierarchy.

Notes to Consolidated Financial Statements

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, 2020 and 2019. 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 could, therefore, include changes in fair value based on both observable and unobservable inputs. The Level 3 financial instruments are comprised of pooled funds whose valuations are provided by the investment managers. Sensitivity analysis is not provided as the underlying assumptions used by the investment managers are not available.

| Year ended December 31 (millions of dollars) | 2020 | 2019 |
|--|-------|-------|
| Fair value, beginning of year | 1,079 | 651 |
| Realized and unrealized gains (losses) | 97 | (4) |
| Purchases | 288 | 463 |
| Sales and disbursements | (35) | (31) |
| Fair value, end of year | 1,429 | 1,079 |

There were no significant transfers between any of the fair value levels during the years ended December 31, 2020 and 2019.

Valuation Techniques Used to Determine Fair Value

Pooled funds mainly consist 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 are expected to 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, real estate and infrastructure investments have been categorized as Level 3 within pooled funds.

Cash equivalents consist of demand cash deposits held with banks and cash held by the investment managers. Cash equivalents are categorized as Level 1.

Short-term securities are valued at cost plus accrued interest, which approximates fair value due to their short-term nature. Short-term securities are categorized as Level 2.

Derivative instruments are used to hedge the Pension Plan's foreign currency exposure back to Canadian dollars. The notional principal amount of contracts outstanding as at December 31, 2020 was \$423 million (2019 – \$742 million), the most significant currencies being hedged against the Canadian dollar are the United States dollar, euro, British pound sterling, Swedish krona and Japanese yen. The net realized loss on contracts for the year ended December 31, 2020 was \$8 million (2019 – \$1 million net realized gain). The terms to maturity of the forward exchange contracts at December 31, 2020 are within three months. The fair value is determined using standard interpolation methodology primarily based on the World Markets exchange rates. Derivative instruments are categorized as Level 2.

Corporate shares are valued based on quoted prices in active markets and are categorized as Level 1. Corporate shares which are valued based on quoted prices in active markets, but held within a pension investment holding company, are categorized as Level 2. Investments denominated in foreign currencies are translated into Canadian currency at year-end rates of exchange.

Bonds and debentures are presented at published closing trade quotations, and are categorized as Level 2.

Notes to Consolidated Financial Statements

21. ENVIRONMENTAL LIABILITIES

The following tables show the movements in environmental liabilities for the years ended December 31, 2020 and 2019:

| Year ended December 31, 2020 (millions of dollars) | PCB | LAR | Total |
|--|-------------|------------|-------------|
| Environmental liabilities – beginning | 90 | 51 | 141 |
| Interest accretion | 3 | – | 3 |
| Expenditures | (17) | (6) | (23) |
| Revaluation adjustment | – | 12 | 12 |
| Environmental liabilities – ending | 76 | 57 | 133 |
| Less: current portion | (25) | (8) | (33) |
| | 51 | 49 | 100 |

| Year ended December 31, 2019 (millions of dollars) | PCB | LAR | Total |
|--|------|------|-------|
| Environmental liabilities – beginning | 108 | 57 | 165 |
| Interest accretion | 4 | – | 4 |
| Expenditures | (17) | (8) | (25) |
| Revaluation adjustment | (5) | 2 | (3) |
| Environmental liabilities – ending | 90 | 51 | 141 |
| Less: current portion | (19) | (11) | (30) |
| | 71 | 40 | 111 |

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:

| As at December 31, 2020 (millions of dollars) | PCB | LAR | Total |
|--|------------|-----------|------------|
| Undiscounted environmental liabilities | 80 | 57 | 137 |
| Less: discounting environmental liabilities to present value | (4) | – | (4) |
| Discounted environmental liabilities | 76 | 57 | 133 |

| As at December 31, 2019 (millions of dollars) | PCB | LAR | Total |
|--|-----|-----|-------|
| Undiscounted environmental liabilities | 97 | 51 | 148 |
| Less: discounting environmental liabilities to present value | (7) | – | (7) |
| Discounted environmental liabilities | 90 | 51 | 141 |

At December 31, 2020, the estimated future environmental expenditures were as follows:

| (millions of dollars) | |
|-----------------------|------------|
| 2021 | 33 |
| 2022 | 31 |
| 2023 | 15 |
| 2024 | 14 |
| 2025 | 10 |
| Thereafter | 34 |
| | 137 |

Notes to Consolidated Financial Statements

Hydro One records a liability for the estimated future expenditures for 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 2.0% 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.

At December 31, 2020, the Company's best estimate of the total estimated future expenditures to comply with current PCB regulations was \$80 million (2019 – \$97 million). These expenditures are expected to be incurred over the period from 2021 to 2025. As a result of its annual review of environmental liabilities, no revaluation adjustment to the PCB environmental liability was recorded in 2020 (2019 – revaluation adjustment was recorded to decrease the PCB environmental liability by \$5 million).

LAR

At December 31, 2020, the Company's best estimate of the total estimated future expenditures to complete its LAR program was \$57 million (2019 – \$51 million). These expenditures are expected to be incurred over the period from 2021 to 2057. As a result of its annual review of environmental liabilities, the Company recorded a revaluation adjustment in 2020 to increase the LAR environmental liability by \$12 million (2019 – \$2 million).

22. 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. 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 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 2.0% to 4.0%, 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. As a result of its annual review of asset retirement obligations, the Company recorded a revaluation adjustment in 2020 to increase the assets retirement liability by \$3 million (2019 – no revaluation adjustment to the asset retirement obligations was recorded).

At December 31, 2020, Hydro One had recorded asset retirement obligations of \$13 million (2019 – \$10 million), primarily 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.

Notes to Consolidated Financial Statements

23. LEASES

Hydro One has operating lease contracts for buildings used in administrative and service-related functions and storing telecommunications equipment. These leases have terms between three and seven years with renewal options of additional three- to five-year terms at prevailing market rates at the time of extension. 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. Renewal options are included in the lease term when their exercise is reasonably certain. Other information related to the Company's operating leases was as follows:

| Year ended December 31 (millions of dollars) | 2020 | 2019 |
|--|------|------|
| Lease expense | 14 | 10 |
| Lease payments made | 13 | 8 |
| As at December 31 | 2020 | 2019 |
| Weighted-average remaining lease term ¹ (years) | 7 | 8 |
| Weighted-average discount rate | 2.6% | 2.7% |

¹ Includes renewal options that are reasonably certain to be exercised.

At December 31, 2020, future minimum operating lease payments were as follows:

| (millions of dollars) | |
|---|-----|
| 2021 | 16 |
| 2022 | 13 |
| 2023 | 12 |
| 2024 | 12 |
| 2025 | 10 |
| Thereafter | 27 |
| Total undiscounted minimum lease payments | 90 |
| Less: discounting minimum lease payments to present value | (8) |
| Total discounted minimum lease payments | 82 |

At December 31, 2019, future minimum operating lease payments were as follows:

| (millions of dollars) | |
|---|-----|
| 2020 | 12 |
| 2021 | 12 |
| 2022 | 11 |
| 2023 | 10 |
| 2024 | 9 |
| Thereafter | 33 |
| Total undiscounted minimum lease payments ¹ | 87 |
| Less: discounting minimum lease payments to present value | (9) |
| Total discounted minimum lease payments | 78 |

¹ Excludes committed amounts of \$6 million for leases that have not yet commenced.

Hydro One presents its ROU assets and lease obligations on the consolidated balance sheets as follows:

| As at December 31 (millions of dollars) | 2020 | 2019 |
|--|------|------|
| Other long-term assets (Note 14) | 77 | 75 |
| Accounts payable and other current liabilities (Note 15) | 12 | 9 |
| Other long-term liabilities (Note 16) | 70 | 69 |

24. SHARE CAPITAL

Common Shares

The Company is authorized to issue an unlimited number of common shares. At December 31, 2020, the Company had 597,611,787 (2019 – 596,818,436) 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.

The following tables presents the changes to common shares during the years ended December 31, 2020 and 2019:

| Year ended December 31, 2020 (number of shares) | Ownership by | | |
|--|--------------|-------------|-------------|
| | Public | Province | Total |
| Common shares – beginning | 314,405,788 | 282,412,648 | 596,818,436 |
| Common shares issued – LTIP ¹ | 351,789 | – | 351,789 |
| Common shares issued – share grants ² | 441,562 | – | 441,562 |
| Common shares – ending | 315,199,139 | 282,412,648 | 597,611,787 |
| | 52.7% | 47.3% | 100% |

¹ In 2020, Hydro One issued from treasury 351,789 common shares in accordance with provisions of the LTIP. This included the exercise of 294,840 stock options for \$7 million.

² In 2020, Hydro One issued from treasury 441,562 common shares in accordance with provisions of the Power Workers' Union (PWU) and the Society Share Grant Plans.

| Year ended December 31, 2019 (number of shares) | Ownership by | | |
|--|--------------|-------------|-------------|
| | Public | Province | Total |
| Common shares – beginning | 313,526,327 | 282,412,648 | 595,938,975 |
| Common shares issued – LTIP ¹ | 416,519 | – | 416,519 |
| Common shares issued – share grants ² | 462,942 | – | 462,942 |
| Common shares – ending | 314,405,788 | 282,412,648 | 596,818,436 |
| | 52.7% | 47.3% | 100% |

¹ In 2019, Hydro One issued from treasury 416,519 common shares in accordance with provisions of the LTIP. This included the exercise of 302,520 stock options for cash proceeds of \$6 million.

² In 2019, Hydro One issued from treasury 462,942 common shares in accordance with provisions of the PWU and the Society Share Grant Plans.

Preferred Shares

The Company is authorized to issue an unlimited number of preferred shares, issuable in series. At December 31, 2020 and 2019, two series of preferred shares were authorized for issuance: the Series 1 preferred shares (Preferred Shares) and the Series 2 preferred shares. At December 31, 2020, the Company had no Preferred Shares (2019 – 16,720,000) and no Series 2 preferred shares (2019 – nil) issued and outstanding.

On November 20, 2020, Hydro One exercised its option to redeem all of its 16,720,000 outstanding Preferred Shares in accordance with their terms. The Preferred Shares were redeemed at a price of \$25.00 per share, plus all accrued and unpaid dividends up to, but excluding November 20, 2020, for an aggregate redemption price of \$423 million, including \$418 million Preferred Shares balance and \$5 million for accrued dividends. The Preferred Shares were not exchangeable or convertible into the common shares of the Company and the redemption had no impact on the Province's voting rights or ownership percentage of the outstanding common shares of Hydro One.

Hydro One may from time to time issue preferred shares in one or more series. Prior to issuing shares in a series, the Hydro One Board of Directors is required to fix the number of shares in the series and determine the designation, rights, privileges, restrictions and conditions attaching to that series of preferred shares. Holders of Hydro One's preferred shares are not entitled to receive notice of, to attend or to vote at any meeting of the shareholders of Hydro One except that votes

may be granted to a series of preferred shares when dividends have not been paid on any one or more series as determined by the applicable series provisions. Each series of preferred shares ranks on parity with every other series of preferred shares, and are entitled to a preference over the common shares and any other shares ranking junior to the preferred shares, with respect to dividends and the distribution of assets and return of capital in the event of the liquidation, dissolution or winding up of Hydro One.

For the period commencing from the date of issue of the Preferred Shares and ending on and including November 19, 2020, the holders of the Preferred Shares were entitled to receive fixed cumulative preferential dividends of \$1.0625 per share per year, if and when declared by the Board of Directors, payable quarterly.

Share Ownership Restrictions

The *Electricity Act* imposes share ownership restrictions on securities of Hydro One carrying a voting right (Voting Securities). These restrictions provide that no person or company (or combination of persons or companies acting jointly or in concert) may beneficially own or exercise control or direction over more than 10% of any class or series of Voting Securities, including common shares of the Company (Share Ownership Restrictions). The Share Ownership Restrictions do not apply to Voting Securities held by the Province, nor to an underwriter who holds Voting Securities solely for the purpose of distributing those securities to purchasers who comply with the Share Ownership Restrictions.

25. DIVIDENDS

In 2020, preferred share dividends in the amount of \$18 million (2019 – \$18 million) and common share dividends in the amount of \$599 million (2019 – \$570 million) were declared and paid.

See Note 34 – Subsequent Events for dividends declared subsequent to December 31, 2020.

26. EARNINGS PER COMMON SHARE

Basic earnings per common share (EPS) is calculated by dividing net income attributable to common shareholders of Hydro One by the weighted-average number of common shares outstanding.

Diluted EPS is calculated by dividing net income attributable to common shareholders of Hydro One by the weighted-average number of common shares outstanding adjusted for the effects of potentially dilutive stock-based compensation plans, including the share grant plans and the LTIP, which are calculated using the treasury stock method.

| Year ended December 31 | 2020 | 2019 |
|--|-------------|-------------|
| Net income attributable to common shareholders (millions of dollars) | 1,770 | 778 |
| Weighted-average number of shares | | |
| Basic | 597,421,127 | 596,437,577 |
| Effect of dilutive stock-based compensation plans | 2,497,161 | 2,410,860 |
| Diluted | 599,918,288 | 598,848,437 |
| EPS | | |
| Basic | \$ 2.96 | \$ 1.30 |
| Diluted | \$ 2.95 | \$ 1.30 |

The common shares contingently issuable as a result of the Convertible Debentures are not included in diluted EPS for the year ended December 31, 2019, as conditions for closing the Merger were not met. As a result of the termination of the Merger agreement (see Note 4 – Business Combinations), the Convertible Debentures were redeemed on February 8, 2019.

27. STOCK-BASED COMPENSATION

Share Grant Plans

Hydro One has two share grant plans (Share Grant Plans), one for the benefit of certain members of the PWU (PWU Share Grant Plan) and one for the benefit of certain members of the Society (Society Share Grant Plan).

The PWU Share Grant Plan provides for the issuance of common shares of Hydro One from treasury to certain eligible members of the PWU 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 began on July 3, 2015, which is the date the share grant plan was 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 in its Initial Public Offering (IPO). The aggregate number of common shares issuable under the PWU Share Grant Plan shall not exceed 3,981,763 common shares. In 2015, 3,979,062 common shares were granted under the PWU Share Grant Plan.

The Society Share Grant Plan provides for the issuance of common shares of Hydro One from treasury to certain eligible members of the Society 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 began 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 in its IPO. The aggregate number of common shares issuable under the Society Share Grant Plan shall not exceed 1,434,686 common shares. In 2015, 1,433,292 common shares were granted under the Society Share Grant Plan.

The fair value of the Hydro One 2015 share grants of \$111 million was estimated based on the grant date 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. In 2020, 441,562 common shares (2019 – 462,942) were issued under the Share Grant Plans. Total share-based compensation recognized during 2020 was \$7 million (2019 – \$9 million) and was recorded as a regulatory asset.

Notes to Consolidated Financial Statements

A summary of share grant activity under the Share Grant Plans during the years ended December 31, 2020 and 2019 is presented below:

| Year ended December 31, 2020 | Share Grants (number of common shares) | Weighted-Average Price |
|--------------------------------------|---|---------------------------|
| Share grants outstanding – beginning | 3,674,377 | \$ 20.50 |
| Vested and issued ¹ | (441,562) | – |
| Forfeited | (78,010) | \$ 20.50 |
| Share grants outstanding – ending | 3,154,805 | \$ 20.50 |

¹ In 2020, Hydro One issued from treasury 441,562 common shares to eligible employees in accordance with provisions of the Share Grant Plans.

| Year ended December 31, 2019 | Share Grants (number of common shares) | Weighted-Average Price |
|--------------------------------------|---|---------------------------|
| Share grants outstanding – beginning | 4,234,155 | \$ 20.50 |
| Vested and issued ¹ | (462,942) | – |
| Forfeited | (96,836) | \$ 20.50 |
| Share grants outstanding – ending | 3,674,377 | \$ 20.50 |

¹ In 2019, Hydro One issued from treasury 462,942 common shares to eligible employees in accordance with provisions of the Share Grant Plans.

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'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 the Company and is entitled to accrue common share dividend equivalents in the form of additional DSUs at the time dividends are paid, subsequent to declaration by Hydro One's Board of Directors.

A summary of DSU awards activity under the Directors' DSU Plan during the years ended December 31, 2020 and 2019 is presented below:

| Year ended December 31 (number of DSUs) | 2020 | 2019 |
|---|---------|----------|
| DSUs outstanding – beginning | 52,620 | 46,697 |
| Granted | 22,481 | 29,938 |
| Settled | (9,861) | (24,015) |
| DSUs outstanding – ending | 65,240 | 52,620 |

For the year ended December 31, 2020, an expense of \$1 million (2019 – \$1 million) was recognized in earnings with respect to the Directors' DSU Plan. At December 31, 2020, a liability of \$2 million (2019 – \$1 million) related to Directors' DSUs has been recorded at the closing price of the Company's common shares of \$28.65. This liability is included in other long-term liabilities on the consolidated balance sheets.

Management DSU Plan

Under the Management DSU Plan, eligible executive employees can elect to receive a specified proportion of their annual short-term incentive in a notional account of DSUs in lieu of cash. Each DSU represents a unit with an underlying value equivalent to the value of one common share of the Company and is entitled to accrue common share dividend equivalents in the form of additional DSUs at the time dividends are paid, subsequent to declaration by Hydro One's Board of Directors.

A summary of DSU awards activity under the Management DSU Plan during the years ended December 31, 2020 and 2019 is presented below:

| Year ended December 31 (number of DSUs) | 2020 | 2019 |
|---|----------|----------|
| DSUs outstanding – beginning | 52,186 | 108,296 |
| Granted | 22,132 | 24,996 |
| Paid | (12,438) | (81,106) |
| DSUs outstanding – ending | 61,880 | 52,186 |

For the year ended December 31, 2020, an expense of \$1 million (2019 – \$1 million) was recognized in earnings with respect to the Management DSU Plan. At December 31, 2020, a liability of \$2 million (2019 – \$1 million) related to Management DSUs has been recorded at the closing price of the Company's common shares of \$28.65. This liability is included in other long-term liabilities on the consolidated balance sheets.

Employee Share Ownership Plan

In 2015, Hydro One established Employee Share Ownership Plans (ESOP) for certain eligible management and non-represented employees (Management ESOP) and for certain eligible Society-represented staff (Society ESOP). Under the Management ESOP, the eligible management and non-represented employees may contribute between 1% and 6% of their base salary towards purchasing common shares of Hydro One.

Notes to Consolidated Financial Statements

The Company matches 50% of their contributions, up to a maximum Company contribution of \$25,000 per calendar year. Under the Society ESOP, the eligible Society-represented staff may contribute between 1% and 4% of their base salary towards purchasing common shares of Hydro One. The Company matches 25% of their contributions, with no maximum Company contribution per calendar year. In 2020, Company contributions made under the ESOP were \$2 million (2019 – \$2 million).

LTIP

Effective August 31, 2015, the Board of Directors of Hydro One adopted an LTIP. Under the LTIP, long-term incentives are granted to certain executive and management employees of Hydro One and its subsidiaries, and all equity-based awards will be settled in newly issued

shares of Hydro One from treasury, consistent with the provisions of the plan which also permit the participants to surrender a portion of their awards to satisfy related withholding taxes requirements. The aggregate number of shares issuable under the LTIP shall not exceed 11,900,000 shares of Hydro One.

The LTIP provides flexibility to award a range of vehicles, including Performance Share Units (PSUs), Restricted Share Units (RSUs), stock options, share appreciation rights, restricted shares, DSUs, 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.

PSUs and RSUs

A summary of PSU and RSU awards activity under the LTIP during the years ended December 31, 2020 and 2019 is presented below:

| Year ended December 31 (number of units) | PSUs | | RSUs | |
|--|-----------------|-----------|-----------------|----------|
| | 2020 | 2019 | 2020 | 2019 |
| Units outstanding – beginning | 171,344 | 605,180 | 206,993 | 442,470 |
| Vested and issued | (52,627) | (78,121) | (3,728) | (92,112) |
| Forfeited | (6,797) | (153,805) | (7,125) | (84,745) |
| Settled | – | (201,910) | (56,410) | (58,620) |
| Units outstanding – ending ¹ | 111,920 | 171,344 | 139,730 | 206,993 |

¹ Units outstanding at December 31, 2020 include 12,980 RSUs (2019 – 7,740 PSUs and 96,330 RSUs) that may be settled in cash if certain conditions are met. At December 31, 2020, a liability of \$1 million (2019 – \$3 million) has been recorded with respect to these awards and is included in accounts payable and other current liabilities on the consolidated balance sheets.

No awards were granted in 2020 or 2019. The compensation expense related to the PSU and RSU awards recognized by the Company during 2020 was \$3 million (2019 – \$9 million).

Stock Options

The Company is authorized to grant stock options under its LTIP to certain eligible employees. No stock options were granted in 2020 or 2019. The stock options previously granted are exercisable for a period not to exceed seven years from the date of grant. The original three-year vesting period for 706,070 stock options was modified in 2019 due to agreements reached with five option-holders, resulting in applicable stock options being fully vested in 2019. The incremental compensation

cost resulting from the modification was not significant. There was no modification of stock options in 2020.

The fair value-based method is used to measure compensation expense related to stock options and the expense was recognized over the vesting period on a straight-line basis. The fair value of the stock option awards granted was estimated on the date of grant using a Black-Scholes valuation model. Updates related to stock options subject to modification were not significant.

A summary of stock options activity during the years ended December 31, 2020 and 2019 is presented below:

| | Number of Stock Options | Weighted-average exercise price |
|--|-------------------------|---------------------------------|
| Stock options outstanding – January 1, 2019 | 949,910 | \$ 20.72 |
| Exercised ¹ | (302,520) | \$ 20.76 |
| Forfeited ⁴ | (243,840) | \$ 20.75 |
| Stock options outstanding – December 31, 2019 ^{2,3} | 403,550 | \$ 20.66 |
| Exercised ¹ | (294,840) | \$ 20.66 |
| Stock options outstanding – December 31, 2020 ^{2,3} | 108,710 | \$ 20.66 |

¹ Stock options exercised in 2020 had an aggregate intrinsic value of \$2 million (2019 – \$1 million).

² During 2020, no stock options vested (2019 – 706,070 stock options vested with a modified fair value of \$1.04 per option), and 294,840 (2019 – 302,520) stock options were exercised. At December 31, 2020 and 2019, all stock options outstanding were vested and exercisable.

³ Stock options outstanding at December 31, 2020 have an aggregate intrinsic value of \$1 million (2019 – \$2 million) and weighted-average remaining contractual term of 4.2 years (2019 – 5.2 years).

⁴ Stock options forfeited in 2019 had a fair value of \$1.65 per option.

No compensation expense related to stock options was recognized by the Company during 2020 (2019 – \$1 million).

Notes to Consolidated Financial Statements

28. NONCONTROLLING INTEREST

Total noncontrolling interest consists of noncontrolling interest attributable to B2M LP and NRLP. The following tables show the movements in total noncontrolling interest during the years ended December 31, 2020 and 2019:

| Year ended December 31, 2020 (millions of dollars) | Temporary Equity | Equity | Total |
|---|------------------|--------|-------|
| Noncontrolling interest – beginning | 20 | 59 | 79 |
| Contributions from sale of noncontrolling interest (Note 4) | – | 9 | 9 |
| Distributions to noncontrolling interest | – | (2) | (2) |
| Net income attributable to noncontrolling interest | 2 | 6 | 8 |
| Noncontrolling interest – ending | 22 | 72 | 94 |

| Year ended December 31, 2019 (millions of dollars) | Temporary Equity | Equity | Total |
|---|------------------|--------|-------|
| Noncontrolling interest – beginning | 21 | 49 | 70 |
| Contributions from sale of noncontrolling interest (Note 4) | – | 12 | 12 |
| Distributions to noncontrolling interest | (3) | (6) | (9) |
| Net income attributable to noncontrolling interest | 2 | 4 | 6 |
| Noncontrolling interest – ending | 20 | 59 | 79 |

B2M LP

On December 16, 2014, 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. 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 B2M LP noncontrolling interest during the years ended December 31, 2020 and 2019:

| Year ended December 31, 2020 (millions of dollars) | Temporary Equity | Equity | Total |
|--|------------------|--------|-------|
| Noncontrolling interest – beginning | 20 | 47 | 67 |
| Distributions to noncontrolling interest | – | (2) | (2) |
| Net income attributable to noncontrolling interest | 2 | 4 | 6 |
| Noncontrolling interest – ending | 22 | 49 | 71 |

| Year ended December 31, 2019 (millions of dollars) | Temporary Equity | Total | Equity |
|--|------------------|-------|--------|
| Noncontrolling interest – beginning | 21 | 49 | 70 |
| Distributions to noncontrolling interest | (3) | (6) | (9) |
| Net income attributable to noncontrolling interest | 2 | 4 | 6 |
| Noncontrolling interest – ending | 20 | 47 | 67 |

NRLP

On September 18, 2019, Hydro One Networks sold to the Six Nations of the Grand River Development Corporation and, through a trust, to the Mississaugas of the Credit First Nation a 25.0% and 0.1%, respectively, equity interest in NRLP partnership units for total consideration of \$12 million, representing the fair value of the equity interest acquired. On January 31, 2020, the Mississaugas of the Credit First Nation purchased an additional 19.9% equity interest in NRLP partnership units

from Hydro One Networks for total cash consideration of \$9 million. Following this transaction, Hydro One's interest in the equity portion of NRLP partnership units was reduced to 55%, with the Six Nations of the Grand River Development Corporation and the Mississaugas of the Credit First Nation owning 25% and 20%, respectively, of the equity interest in NRLP partnership units. The First Nations Partners' noncontrolling interest in NRLP is classified within equity.

The following table shows the movements in NRLP noncontrolling interest during the years ended December 31, 2020 and 2019:

| Year ended December 31 (millions of dollars) | 2020 | 2019 |
|---|------|------|
| Noncontrolling interest – beginning | 12 | – |
| Contributions from sale of noncontrolling interest (Note 4) | 9 | 12 |
| Net income attributable to noncontrolling interest | 2 | – |
| Noncontrolling interest – ending | 23 | 12 |

29. RELATED PARTY TRANSACTIONS

The Province is a shareholder of Hydro One with approximately 47.3% ownership at December 31, 2020. The IESO, Ontario Power Generation Inc. (OPG), Ontario Electricity Financial Corporation (OEFC), and the OEB are related parties to Hydro One because they are controlled or significantly influenced by the Ministry of Energy. Ontario Charging Network LP (OCN LP) is a joint-venture limited partnership between a subsidiary of Hydro One and OPG. The following is a summary of the Company's related party transactions during the years ended December 31, 2020 and 2019:

Year ended December 31 (millions of dollars)

| Related Party | Transaction | 2020 | 2019 |
|---------------------------|---|--------------|-------|
| Province | Dividends paid ¹ | 301 | 288 |
| IESO | Power purchased | 2,506 | 1,808 |
| | Revenues for transmission services | 1,717 | 1,636 |
| | Amounts related to electricity rebates | 1,588 | 692 |
| | Distribution revenues related to rural rate protection | 242 | 240 |
| | Distribution revenues related to supply of electricity to remote northern communities | 35 | 35 |
| | Funding received related to CDM programs | 26 | 42 |
| OPG² | Power purchased | 6 | 8 |
| | Revenues related to provision of services and supply of electricity | 8 | 9 |
| | Capital contribution received from OPG | 3 | — |
| | Costs related to the purchase of services | 3 | 1 |
| OEFC | Power purchased from power contracts administered by the OEFC | 1 | 2 |
| OEB | OEB fees | 9 | 9 |
| OCN LP³ | Investment in OCN LP | 2 | 2 |

1 On November 20, 2020 Hydro One redeemed the Preferred Shares held by the Province. See Note 24 – Share Capital.

2 OPG has provided a \$2.5 million guarantee to Hydro One related to the OCN Guarantee. See Note 32 – Commitments for details related to the OCN Guarantee.

3 OCN LP owns and operates electric vehicle fast charging stations across Ontario, under the Ivy Charging Network brand.

Sales to and purchases from related parties are based on the requirements of the OEB's Affiliate Relationships Code. Outstanding balances at period end are interest-free and settled in cash. Invoices are issued monthly, and amounts are due and paid on a monthly basis.

30. CONSOLIDATED STATEMENTS OF CASH FLOWS

The changes in non-cash balances related to operations consist of the following:

| Year ended December 31 (millions of dollars) | 2020 | 2019 |
|---|-------------|-------|
| Accounts receivable (Note 9) ¹ | 12 | (73) |
| Due from related parties | 89 | (160) |
| Materials and supplies (Note 10) ¹ | — | (1) |
| Prepaid expenses and other assets (Note 10) ¹ | (9) | (8) |
| Other long-term assets (Note 14) | (1) | (2) |
| Accounts payable (Note 15) ¹ | 37 | 7 |
| Accrued liabilities (Note 15) ¹ | (62) | 38 |
| Due to related parties | 27 | 213 |
| Accrued interest (Note 15) | 14 | 8 |
| Long-term accounts payable and other long-term liabilities (Note 16) ¹ | 1 | — |
| Post-retirement and post-employment benefit liability (Note 16) | 72 | 33 |
| | 180 | 55 |

1 Adjusted for amounts related to acquisitions. See Note 4 – Business Combinations for more details.

Notes to Consolidated Financial Statements

Capital Expenditures

The following tables reconcile investments in property, plant and equipment and intangible assets and the amounts presented in the consolidated statements of cash flows for the years ended December 31, 2020 and 2019. The reconciling items include net change in accruals and capitalized depreciation.

| Year ended December 31, 2020 (millions of dollars) | Property, Plant and Equipment | Intangible Assets | Total |
|--|-------------------------------|-------------------|---------|
| Capital investments | (1,751) | (127) | (1,878) |
| Reconciling items | 33 | 1 | 34 |
| Cash outflow for capital expenditures | (1,718) | (126) | (1,844) |

| Year ended December 31, 2019 (millions of dollars) | Property, Plant and Equipment | Intangible Assets | Total |
|--|-------------------------------|-------------------|---------|
| Capital investments | (1,551) | (116) | (1,667) |
| Reconciling items | 38 | 1 | 39 |
| Cash outflow for capital expenditures | (1,513) | (115) | (1,628) |

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 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 property, plant and equipment in service. In 2020, there were no capital contributions from these assessments (2019 – \$3 million). In 2019, this represented the difference between the revised load forecast of electricity transmitted compared to the load forecast in the original contract, subject to certain adjustments.

Supplementary Information

| Year ended December 31 (millions of dollars) | 2020 | 2019 |
|--|------|------|
| Net interest paid | 493 | 494 |
| Income taxes paid | 30 | 21 |

31. CONTINGENCIES

Legal Proceedings

Hydro One is involved in various lawsuits and claims 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 2020, the Company paid approximately \$2 million (2019 – \$2 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.

Notes to Consolidated Financial Statements

32. COMMITMENTS

The following table presents a summary of Hydro One's commitments under outsourcing and other agreements due in the next five years and thereafter:

| As at December 31, 2020 (millions of dollars) | Year 1 | Year 2 | Year 3 | Year 4 | Year 5 | Thereafter |
|---|--------|--------|--------|--------|--------|------------|
| Outsourcing and other agreements | 106 | 15 | 11 | 13 | 2 | 15 |
| Long-term software/meter agreement | 8 | 2 | 1 | 2 | — | — |

Outsourcing and Other Agreements

Hydro One has an agreement with Inergi LP for the provision of back-office and IT outsourcing services, including supply chain, pay operations, IT, and finance and accounting services. The agreement expires on February 28, 2021 for IT services and expires on October 31, 2021 for supply chain services. The agreement for pay operations, and for finance and accounting services was extended in October 2020 and now expires on December 31, 2021. In February 2021, Hydro One entered into an agreement for information technology services with Capgemini Canada Inc., which expires on February 29, 2024, and includes an option to extend for two additional one-year terms at Hydro One's discretion. Effective January 1, 2022, Ceridian Canada Ltd. will replace Inergi LP as the new provider of pay operations for a five-year term.

BGIS Global Integrated Solutions Canada LP (BGIS) provides services to Hydro One, including facilities management and execution of certain

capital projects as deemed required by the Company. The agreement with BGIS for these services expires in December 2024, with an option for the Company to renew the agreement for an additional term of three years.

Long-term Software/Meter Agreement

Trilliant Holdings Inc. and Trilliant Networks (Canada) Inc. (collectively Trilliant) provide services to Hydro One for the supply, maintenance and support services for smart meters and related hardware and software, including additional software licences, as well as certain professional services. The agreement with Trilliant for these services expires in December 2025, with an option for the Company to renew the agreement for an additional term of five years.

Other Commitments

The following table presents a summary of Hydro One's other commercial commitments by year of expiry in the next five years and thereafter:

| As at December 31, 2020 (millions of dollars) | Year 1 | Year 2 | Year 3 | Year 4 | Year 5 | Thereafter |
|---|--------|--------|--------|--------|--------|------------|
| Operating Credit Facilities | — | — | — | 2,550 | — | — |
| Letters of credit ¹ | 194 | 2 | — | — | — | — |
| Guarantees ² | 491 | — | — | — | — | — |

¹ Letters of credit consist of \$167 million letters of credit related to retirement compensation arrangements, a \$22 million letter of credit provided to the IESO for prudential support, \$4 million in letters of credit to satisfy debt service reserve requirements, and \$3 million in letters of credit for various operating purposes.

² Guarantees consist of \$484 million prudential support provided to the IESO by Hydro One Inc. on behalf of its subsidiaries, and guarantees totalling \$7 million provided by Hydro One to the Minister of Natural Resources (Canada) relating to OCN LP (OCN Guarantee). The OPG has provided a \$2.5 million guarantee to Hydro One related to the OCN Guarantee.

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. The IESO could draw on these guarantees and/or letters of credit if these purchasers 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 Hydro One Inc.'s liability under the terms of a trust fund established pursuant to the supplementary pension plan for eligible employees of Hydro One Inc. The supplementary pension plan trustee is required to draw upon these letters of credit if Hydro One Inc. 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 Hydro One Inc.'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. A bank letter of credit has also been issued to provide security for Hydro One's retirement compensation arrangement trust agreement.

Notes to Consolidated Financial Statements

33. SEGMENTED REPORTING

Hydro One has three reportable segments:

- The Transmission Segment, which comprises the transmission of high voltage electricity across the province, interconnecting local distribution companies and certain large directly connected industrial customers throughout the Ontario electricity grid;
- The Distribution Segment, which comprises the delivery of electricity to end customers and certain other municipal electricity distributors; and
- Other Segment, which includes certain corporate activities and the operations of the Company's telecommunications business. The Other Segment includes a portion of the deferred tax asset which arose from the revaluation of the tax bases of Hydro One's assets to

fair market value when the Company transitioned from the provincial payments in lieu of tax regime to the federal tax regime at the time of Hydro One's initial public offering in 2015. This deferred tax asset is not required to be shared with ratepayers, the Company considers it to not be part of the regulated transmission and distribution segment assets, and it is included in the other segment.

The designation of segments has been based on a combination of regulatory status and the nature of the 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 tax expense from continuing operations (excluding certain allocated corporate governance costs).

| Year ended December 31, 2020 (millions of dollars) | Transmission | Distribution | Other | Consolidated |
|--|--------------|--------------|-------------|--------------|
| Revenues | 1,740 | 5,507 | 43 | 7,290 |
| Purchased power | — | 3,854 | — | 3,854 |
| Operation, maintenance and administration | 391 | 619 | 60 | 1,070 |
| Depreciation, amortization and asset removal costs | 459 | 417 | 8 | 884 |
| Income (loss) before financing charges and income tax expense | 890 | 617 | (25) | 1,482 |
| Capital investments | 1,157 | 712 | 9 | 1,878 |

| Year ended December 31, 2019 (millions of dollars) | Transmission | Distribution | Other | Consolidated |
|--|--------------|--------------|--------------|--------------|
| Revenues | 1,652 | 4,788 | 40 | 6,480 |
| Purchased power | — | 3,111 | — | 3,111 |
| Operation, maintenance and administration | 355 | 610 | 216 | 1,181 |
| Depreciation, amortization and asset removal costs | 462 | 409 | 7 | 878 |
| Income (loss) before financing charges and income tax expense | 835 | 658 | (183) | 1,310 |
| Capital investments | 1,035 | 624 | 8 | 1,667 |

Total Assets by Segment:

| As at December 31 (millions of dollars) | 2020 | 2019 |
|---|---------------|---------------|
| Transmission | 17,761 | 15,029 |
| Distribution | 11,387 | 10,017 |
| Other | 1,146 | 2,015 |
| Total assets | 30,294 | 27,061 |

Total Goodwill by Segment:

| As at December 31 (millions of dollars) | 2020 | 2019 |
|---|------------|------------|
| Transmission | 157 | 157 |
| Distribution (Note 4) | 216 | 168 |
| Total goodwill | 373 | 325 |

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

34. SUBSEQUENT EVENTS

Dividends

On February 23, 2021, common share dividends of \$152 million (\$0.2536 per common share) were declared.

Corporate and Shareholder Information

Corporate Office

483 Bay Street, South Tower
Toronto, ON M5G 2P5
1.416.345.5000

www.HydroOne.com

Customer Inquiries

Customer Service: 1.888.664.9376

Report an Emergency (24 hours):
1.800.434.1235

Shareholder Services

If you are a registered shareholder and have inquiries regarding your account, wish to change your name or address, or have questions about dividends, duplicate mailings, lost stock certificates, share transfers or estate settlements, contact our transfer agent and registrar:

Computershare Trust Company of Canada

100 University Avenue, 8th Floor
Toronto, ON M5J 2Y1
1.514.982.7555 or 1.800.564.6253
service@computershare.com

Institutional Investors and Analysts

Institutional investors, securities analysts and others requiring additional financial information can visit www.HydroOne.com/Investors or contact us at: 1.416.345.6867
Investor.Relations@HydroOne.com or
OJaved@HydroOne.com

Media Inquiries

1.416.345.6868 or 1.877.506.7584
Media.Relations@HydroOne.com

Sustainability

Hydro One is committed to continuing to grow responsibly and we focus our social and environmental sustainability efforts where we can make the most meaningful impacts on both. To learn more, visit www.hydroone.com/sustainability or email Sustainability@HydroOne.com

Stock Exchange Listing

Toronto Stock Exchange (TSX): H
(CUSIP #448811208)



Independent Auditors

KPMG LLP

Equity Index Inclusions

Dow Jones Select Utilities (Canada) Index
FTSE All-World Index Series
MSCI World (Canada) Index
S&P/TSX Composite Index
S&P/TSX Utilities Index
S&P/TSX Composite Dividend Index
S&P/TSX Composite Low Volatility Index
S&P/TSX Composite High Dividend Index

Debt Securities

For details of the public debt securities of Hydro One and its subsidiaries, please refer to the "Debt Information" section under www.HydroOne.com/Investors.

Online Information

Hydro One is committed to open and full financial disclosure and best practices in corporate governance. We invite you to visit the Investor Relations section of www.HydroOne.com/Investors where you will find additional information about our business, including events and presentations, news releases, regulatory filings, governance practices, sustainability and our continuous disclosure materials, including quarterly financial releases, annual information forms and management information circulars. You may also subscribe to our news by email to automatically receive Hydro One news releases electronically.

Common Share Dividend Information

2021 Expected Dividend Dates

| Declaration Date | Record Date | Payment Date |
|-------------------|-------------------|--------------------|
| February 23, 2021 | March 17, 2021 | March 31, 2021 |
| May 6, 2021 | June 9, 2021 | June 30, 2021 |
| August 9, 2021 | September 8, 2021 | September 30, 2021 |
| November 8, 2021 | December 8, 2021 | December 31, 2021 |

Unless indicated otherwise, all common share dividends paid by Hydro One are designated as "eligible" dividends for the purposes of the Income Tax Act (Canada) and any similar provincial legislation.

Dividend Reinvestment Plan (DRIP)

Hydro One offers a convenient dividend reinvestment program for eligible shareholders to purchase additional Hydro One shares by reinvesting their cash dividends without incurring brokerage or administration fees. For plan information and enrolment materials or to learn more about the Hydro One DRIP, visit www.HydroOne.com/DRIP or Computershare Trust Company of Canada at www.InvestorCentre.com/HydroOne.

Regulatory Stakeholders

Hydro One is committed to maintaining and enhancing constructive long-term relationships with its regulatory stakeholders.



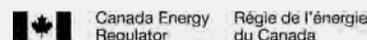
**Provincial Government,
Ministry of Energy**
Policy, legislation, regulations



Ontario Energy Board (OEB)
Independent electric utility price and service quality regulation



Independent Electricity System Operator
Wholesale power market rules, intermediary, North American reliability standards



Canadian Energy Regulator
Federal regulator, international power lines and substations



North American Electric Reliability Corporation
Continent-wide bulk power reliability standards, certification, monitoring



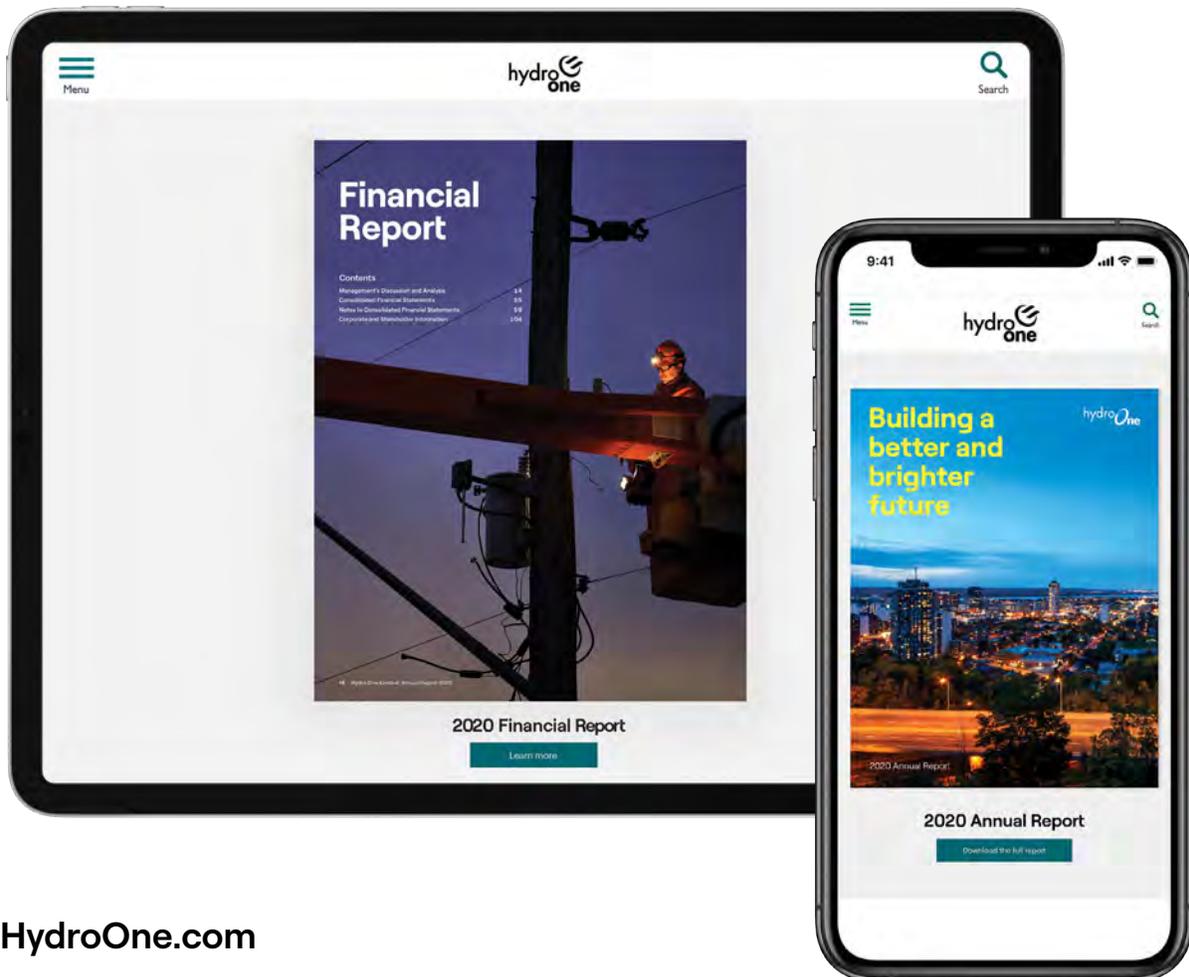
Northeast Power Coordinating Council
Northeastern North American grid reliability, standards, compliance

For more information, visit
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Why Invest in Hydro One?

- Utility business in a stable and rate-regulated environment
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- Solid investment grade balance sheet
- Fully independent Board
- Stable and growing dividend



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