

ON BEHALF OF AVISTA CORPORATION

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ON BEHALF OF HYDRO ONE LIMITED

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BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

IN THE MATTER OF THE JOINT)	
APPLICATION OF HYDRO ONE LIMITED)	CASE NO. AVU-E-17- <u>09</u>
(ACTING THROUGH ITS INDIRECT)	CASE NO. AVU-G-17- <u>05</u>
SUBSIDIARY, OLYMPUS EQUITY LLC))	
AND)	
AVISTA CORPORATION)	DIRECT TESTIMONY
FOR AN ORDER AUTHORIZING PROPOSED)	OF
<u>TRANSACTION</u>)	CHRISTOPHER F. LOPEZ

FOR HYDRO ONE LIMITED

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1 I. INTRODUCTION

2 Q. Please state your name and business address.

3 A. My name is Christopher F. Lopez, and my business
4 address is 483 Bay Street, South Tower, 8th Floor, Toronto,
5 Ontario M5G 2P5.

6 Q. By whom are you employed and in what capacity?

7 A. I am Senior Vice President of Finance for Hydro One
8 Limited ("Hydro One"). Hydro One is a major North American
9 electric transmission and distribution utility, serving more
10 than 1.3 million residential and business customers in
11 Ontario, Canada.

12 Q. Please summarize your education and business
13 experience.

14 A. I received a Bachelor of Commerce in accounting and
15 finance from Edith Cowan University in 1996. I qualified from
16 the Institute of Chartered Accountants in Australia in 1999.
17 I received a graduate diploma in corporate governance and
18 directorships from the Australian Institute of Company
19 Directors in 2007.

20 Prior to joining Hydro One, I was the Vice President of
21 Planning and Mergers & Acquisitions at TransAlta from 2011 to
22 2015. Prior to that, I was Director of Operations Finance at
23 TransAlta in Calgary from 2007 to 2011, and was Country

1 Financial Controller for TransAlta in Australia, from 2002 to
2 2007.

3 **Q. Have you provided a copy of your résumé?**

4 A. Yes, a copy of my résumé that covers my experience
5 prior to joining Hydro One is included as Exhibit No. 4,
6 Schedule 1.

7 Summary of Testimony

8 **Q. What is the purpose of your direct testimony in this**
9 **proceeding?**

10 A. The purpose of my testimony is as follows:

- 11 • describe the Proposed Transaction;
- 12 • discuss Hydro One's corporate structure and where
13 Avista Corporation ("Avista") will reside within
14 that structure;
- 15 • discuss Hydro One's capital structure and
16 financial strength;
- 17 • describe Hydro One's financing for, and the
18 mechanics of, the Proposed Transaction;
- 19 • describe Avista's post-transaction access to
20 capital;
- 21 • enumerate certain financial, structural, and
22 ring-fencing commitments that Hydro One and
23 Avista are proposing as part of their request for
24 approval of the Proposed Transaction; and
- 25 • describe the Rate Credits included as part of the
26 Proposed Transaction.

27 A table of contents of my testimony is as follows:

28

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10 **Q. Are you sponsoring exhibits with your testimony?**

11 A. Yes. Attached to my testimony are:

- 12 • Exhibit No. 4, Schedule 1: Christopher Lopez
- 13 Résumé
- 14 • Exhibit No. 4, Schedule 2: Pre- and Post-
- 15 Transaction Corporate Structure of Hydro One
- 16 Limited
- 17 • Exhibit No. 4, Schedule 3: Hydro One's 2016
- 18 Annual Report and 2016 Annual Information Form

20 **I. SUMMARY OF THE PROPOSED TRANSACTION**

21 **Q. Please describe Hydro One's proposed acquisition of**
22 **Avista.**

23 A. The boards of directors for Hydro One and Avista
24 unanimously approved an all-cash transaction pursuant to
25 which Avista shareholders will receive \$53 per common share,
26 representing a 24% premium to Avista's closing share price of
27 \$42.74 on July 18, 2017. Avista shareholders will receive
28 cash consideration totaling approximately \$3.4 billion.

1 Upon completion of the transaction, based on pro forma
2 financial information at March 31, 2017, following the merger,
3 Hydro One's total assets will increase from approximately
4 C\$25.4 billion to approximately C\$34.9 billion. Together,
5 Hydro One and Avista will serve more than two million end-use
6 customers¹ and will operate across multiple North American
7 jurisdictions, including Ontario, Washington, Idaho, Oregon,
8 Montana and Alaska.

9 Once acquired by Hydro One, Avista will be operated much
10 as it is today, with the same management team, and it will
11 continue to be headquartered in Spokane, Washington.

12 The terms of the transaction are set forth in the
13 Agreement and Plan of Merger (the "Merger Agreement") dated
14 as of July 19, 2017 among Hydro One Limited, Olympus Holding
15 Corp., Olympus Corp. and Avista which has been provided as
16 Exhibit No. 3, Schedule 3 to Avista Thies' testimony and in
17 Appendix 2 to the Joint Application. Under the terms of the
18 Merger Agreement, Hydro One would acquire Avista through the
19 merger of Olympus Corp. with and into Avista, with Avista as
20 the surviving corporation and a wholly-owned, indirect
21 subsidiary of Hydro One. No material changes are expected to

¹ Including 1.3 million Hydro One electric customers, 378,000 Avista electric customers, and 342,000 Avista natural gas customers.

1 the operations, management, or corporate structure of Avista
2 and its subsidiaries.

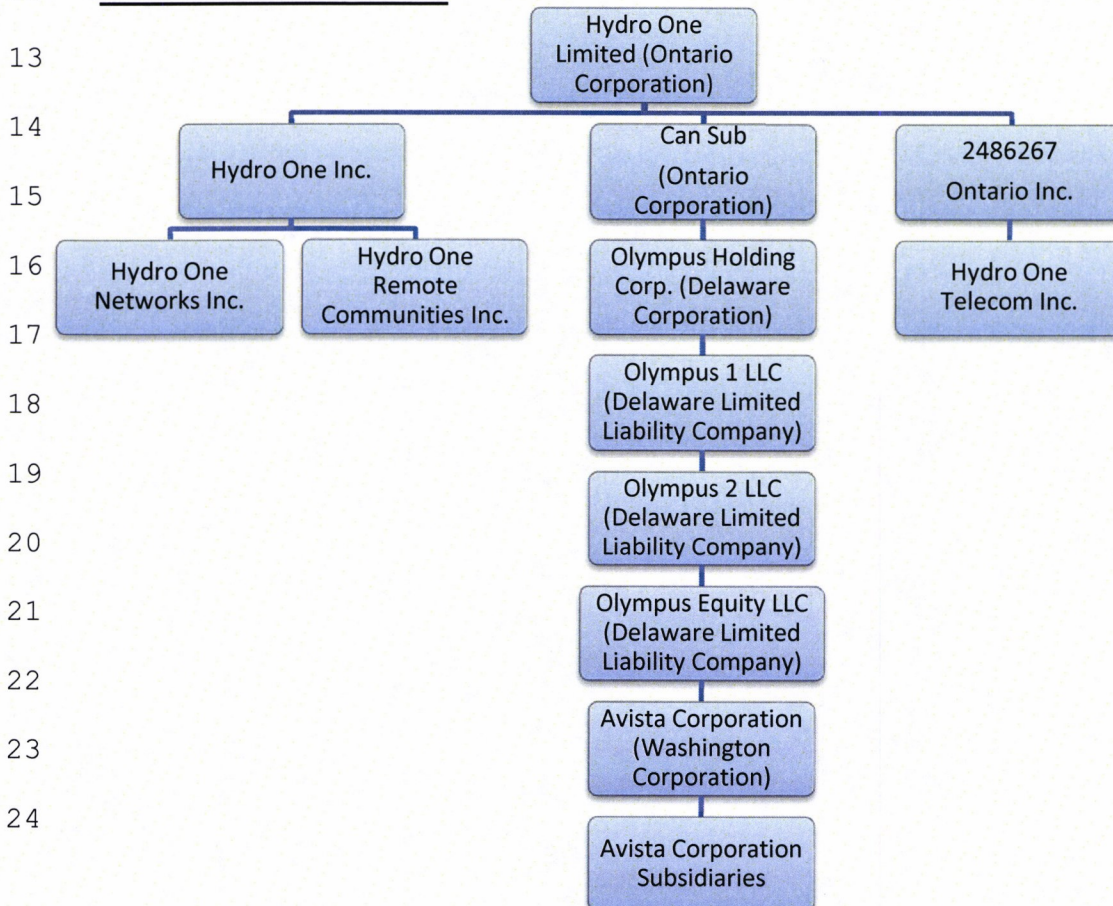
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4 **II. POST-TRANSACTION CORPORATE STRUCTURE**

5 **Q. Please explain Hydro One's post-transaction**
6 **corporate structure.**

7 A. Upon completion of the transaction, Avista will be
8 an indirect, wholly-owned subsidiary of Hydro One as
9 illustrated in the following organizational chart, which is
10 included in Appendix 1 to the Joint Application and is Exhibit
11 No. 4, Schedule 2 to my testimony:

12 **Illustration No. 1:**



1 **Q. Why is Hydro One employing this type of structure?**

2 A. The structure has been set up to provide segregation
3 between the rate-regulated business in the United States and
4 the Ontario rate-regulated business, which is held by Hydro
5 One Inc. Subsequent to the transaction, Avista will be a
6 wholly-owned subsidiary of Olympus Equity LLC, which is a
7 bankruptcy-remote entity with no debt. Together with the
8 ring-fencing provisions described later in my testimony, this
9 structure insulates Avista and its customers from any
10 potential financial weakness at Olympus Equity LLC or other
11 entities up the chain from Olympus Equity LLC.

12 **Q. Why is Hydro One creating three intermediate**
13 **subsidiaries between Avista / Olympus Equity LLC and the**
14 **Canadian Sub?**

15 A. The entities are created for Canadian tax planning
16 purposes and to manage intercorporate funds flows.

17 **Q. Will this corporate structure result in any**
18 **additional costs that will be recovered through Avista**
19 **ratepayers?**

20 A. No. This corporate structure will not result in
21 any additional costs to be recovered from Avista ratepayers.

22 **Q. Have Hydro One and Avista offered ring-fencing**
23 **commitments to ensure that Avista ratepayers will be protected**

1 **from any transactions that will occur in relation to these**
2 **subsidiaries?**

3 A. Yes. These ring-fencing commitments will be
4 explained in more detail later in my testimony. Olympus 2
5 LLC will not operate or own any business and will limit its
6 activities to investing in and attending to its shareholdings
7 in Olympus Equity LLC, which, in turn, will not operate or
8 own any business and will limit its activities to investing
9 in and attending to its shareholdings in Avista. Furthermore,
10 there will be no cross-subsidization of unregulated
11 activities by Avista customers, and Avista will provide access
12 to books and records required to verify or examine
13 transactions with Avista or that result in costs that may be
14 allocable to Avista.

15
16 **III. HYDRO ONE'S CURRENT CAPITAL STRUCTURE AND FINANCIAL**
17 **STRENGTH**

18 **Q. Does Hydro One have financial statements that are**
19 **similar to a 10K or 10Q in the United States?**

20 A. Yes. Exhibit No. 4, Schedule 3 to my testimony
21 contains Hydro One's 2016 Annual Report and 2016 Annual
22 Information Form filed with Canadian Securities regulators.
23 These are also contained in Appendix 6 to the Joint
24 Application.

1 **Q. Please describe Hydro One's current capital**
2 **structure.**

3 A. Table 1 below shows that, on a consolidated basis,
4 Hydro One's balance sheet as at December 31, 2016, reflects
5 a capital structure that is approximately 53% debt and 47%
6 equity.

Table 1			
As at December 31, 2016:		\$ CAD	% of total Capital
Long-term debt payable within one year		602	
Short-term notes payable		469	
Long-term debt		10,078	
Less: cash and cash equivalents		(50)	
Total Debt		11,099	53%
Total Shareholders' Equity		10,017	47%
Total Capital		21,116	

14 **Q. To what extent has Hydro One employed long-term debt**
15 **in its capital structure?**

16 A. As at December 31, 2016, of the 53% debt in Hydro
17 One's capital structure, approximately 51% is long-term debt,
18 which is defined as debt instruments with maturity of 12
19 months or greater.

20 **Q. Given its balance sheet, how would you characterize**
21 **the financial strength of Hydro One?**

22 A. As shown in the financial statements contained in
23 my Exhibit No. 4, Schedule 3, Hydro One maintains a strong
24 balance sheet providing it with access to capital. This is

1 recognized by the rating agencies, as reflected in the strong
2 ratings of Hydro One.

3 **Q. What are the credit ratings that are currently**
4 **assigned to Hydro One by the major credit rating agencies,**
5 **and how did the ratings agencies respond to announcement of**
6 **the transaction?**

7 A. On July 19, 2017, following the announcement of
8 the transaction, Standard and Poors ("S&P") affirmed an 'A'
9 long-term corporate credit rating for Hydro One and revised
10 the outlook to Negative from Stable. It mentioned the
11 negative outlook on Hydro One reflects its view that the
12 Avista acquisition signals a shift in Hydro One's business
13 strategy, which will align the company with its global peers.
14 On July 19, 2017, following the announcement of the
15 transaction, Moody's affirmed the ratings of Hydro One Inc.'s:
16 (i) senior unsecured regular bonds (A3); (ii) senior unsecured
17 medium-note program ((P)A3); and (iii) senior unsecured
18 commercial paper (P-2). At the same time, Moody's changed
19 the outlook on Hydro One Inc. to Negative from Stable. It
20 mentioned that the negative outlook on Hydro One Inc. reflects
21 its view that the probability of extraordinary support from
22 the Province of Ontario ("Province") will be reduced following
23 the transaction.

1 The rating agency DBRS (originally known as Dominion Bond
2 Rating) rates Hydro One Inc.'s long-term debt at A (High) and
3 its short-term debt at R1 (low). It expressed its view that,
4 should the merger be financed as contemplated in the
5 announcement, it will have no impact on Hydro One Inc.'s
6 credit profile.

7 **Q. How much equity does the Province own in Hydro One?**

8 A. As of June 30, 2017, the Province owns approximately
9 49.9% of Hydro One's common shares.

10 **Q. Please explain the laws that govern the level of**
11 **equity that the Province must maintain in Hydro One.**

12 A. The Province has a preemptive right to subscribe to
13 up to 45% of any new equity. If the Province's ownership in
14 Hydro One drops below 40%, then the Province has an obligation
15 to increase ownership to meet or exceed 40%. No other
16 shareholder may own more than 10% of Hydro One, so Hydro One
17 is essentially take-over proof.

18 **Q. How do the provincial laws requiring the Government**
19 **of Ontario to maintain a 40% equity interest in Hydro One**
20 **impact Hydro One's ability to issue additional equity?**

21 A. Under the Electricity Act, 1998, if as a result of
22 the issuance of additional voting securities by Hydro One
23 Limited, the Province of Ontario owns less than 40% of the
24 outstanding number of voting securities of Hydro One Limited,

1 the Province is required to take steps to increase its
2 ownership to not less than 40% of the outstanding voting
3 securities. In order to assist the Province in meeting its
4 ownership obligations under the Electricity Act, 1998, under
5 the governance agreement with the Province, Hydro One has
6 granted the Province a preemptive right to subscribe for and
7 purchase up to 45% of any proposed issuance by Hydro One
8 Limited of voting securities or securities that are
9 convertible or exchangeable into voting securities (other
10 than certain specified excluded issuances). Any offered
11 securities not subscribed for and purchased by the Province
12 pursuant to its preemptive right may be issued to any other
13 person pursuant to the proposed offering.

14 Hydro One is permitted to issue voting securities or
15 securities that are convertible into or exchangeable for
16 voting securities at any time, provided that it must first
17 give the Province the opportunity to subscribe for the number
18 of securities to which it is entitled to pursuant to its
19 preemptive right before offering them to others.

20 **Q. Does the fact that Hydro One is only traded on the**
21 **Toronto Stock Exchange impact its access to capital?**

22 A. Hydro One Limited's listing on the Toronto Stock
23 Exchange (TSX) requires it to comply with applicable TSX rules
24 regarding additional listings in the event that the company

1 proposes to issue additional common shares in the future. Any
2 such listing will require prior approval of the TSX and,
3 depending on the size of the issuance or other factors, the
4 TSX could require shareholder approval of the issuance as a
5 condition of its approval. However, listing on the TSX in
6 and of itself does not limit the company's access to equity.
7 Hydro One Limited may in the future determine that listing
8 its common shares on a second exchange would increase its
9 access to equity. Under the governance agreement with the
10 Province, Hydro One Limited is required to maintain a listing
11 of its common shares on the Toronto Stock Exchange, but it is
12 not prevented from listing on any other stock exchange in the
13 future (so long as it maintains its TSX listing as well).

14 **Q. Is the Ontario Electric Board ("OEB") required to**
15 **approve Hydro One's proposals to issue more equity?**

16 A. No, the OEB has no jurisdiction to review and
17 approve issuance of new equity by Hydro One.

18 **Q. Does the OEB have jurisdiction to review and approve**
19 **Hydro One's acquisition of Avista?**

20 A. No, the OEB has no jurisdiction to review and
21 approve Hydro One's acquisition of Avista.

22 **Q. What style of rate regulation does OEB use to**
23 **regulate Hydro One?**

1 A. The OEB's scheme for regulating Hydro One Networks
2 Inc. is a hybrid of cost-based rates with an allowed equity
3 return and performance-based regulation.

4
5 **IV. PROPOSED TRANSACTION FINANCING**

6 **Q. Please describe the steps that will be taken to**
7 **effectuate the transaction.**

8 A. Olympus Holding Corp., a Delaware Corporation, and
9 an indirect wholly-owned subsidiary of Hydro One, proposes to
10 acquire all of the shares of Avista through a merger of a
11 wholly-owned indirect subsidiary, Olympus Corp., and Avista.
12 After the merger, Avista will be the surviving corporation
13 and Olympus Corp. will cease to exist.

14 **Q. Please describe how the acquisition of Avista by**
15 **Hydro One will be financed.**

16 A. Hydro One is committed to maintaining an
17 investment-grade balance sheet through and after completion
18 of the acquisition. Hydro One plans to finance this all-cash
19 transaction using a mix of long-, medium- and short-term debt
20 together with a convertible debenture installment receipts
21 offering. Hydro One is planning to issue the debt financing
22 in U.S. dollars totaling US\$2.6 billion (and issued
23 convertible debenture installment receipts in Canada of
24 C\$1.54 billion or approximately US\$1.2 billion). We expect

1 the convertible debenture to be fully converted to equity
2 around the time of the closing of the transaction. The
3 planned US\$ debt financing contemplates a combination of 5-
4 year, 10-year and 30-year US\$ denominated notes.

5 **Q. Will Avista pledge any assets or guarantee any of**
6 **these transactions for the purpose of the acquisition of**
7 **Avista by Hydro One?**

8 A. No. Avista has not and will not pledge any assets
9 or guarantee any of the transactions necessary for this
10 acquisition.

11 **Q. What is Hydro One's current estimate of the excess**
12 **of the purchase price over the value of Avista as of the**
13 **expected closing date?**

14 A. The boards of directors for Hydro One and Avista
15 approved an all-cash transaction through which Avista
16 shareholders will receive \$53 per common share, representing
17 a 24% premium to the market value of Avista's shares of \$42.74
18 on July 18, 2017. The estimated excess of the purchase
19 price over the book value of Avista's net assets is
20 approximately \$1.7 billion as of June 30, 2017.

21 **Q. In and of itself, as a result of the closing of this**
22 **transaction, will Avista's financial statements change?**

23 A. No. Avista's U.S. financial statements, prepared
24 using generally accepted accounting principles ("GAAP"), will

1 not be impacted by the closing of this transaction. Avista
2 will maintain its own accounting system, separate from Hydro
3 One's accounting system. The acquisition will be accounted
4 for in accordance with GAAP. The premium paid by Hydro One
5 for Avista will be recorded in the accounts of the acquisition
6 company and not in the utility accounts of Avista.

7 As indicated in the merger commitments described below,
8 Hydro One and Avista will not propose to recover the
9 acquisition premium in Avista's regulated retail rates.

10 **Q. Will the proposed transaction have any impact on**
11 **the availability of Avista's books and records?**

12 A. No. All Avista financial books and records will
13 continue to be available to the Commission. As indicated by
14 the commitments described below, Olympus Holding Corp. and
15 Avista will provide the Commission access to all books of
16 account, as well as all documents, data, and records of their
17 affiliated interests, which pertain to transactions between
18 Avista and its affiliated interests.

19

20 **V. AVISTA'S POST-CLOSING ACCESS TO CAPITAL**

21 **Q. How will the acquisition by Hydro One affect**
22 **Avista's access to capital?**

23 A. We believe Avista's access to capital will be
24 enhanced in light of Hydro One's strong balance sheet. On July

1 19, 2017, S&P affirmed its BBB' issuer rating on Avista and
2 revised the outlook to positive from stable. S&P noted that
3 the positive outlook reflects the potential for higher ratings
4 on Avista if the acquisition is completed as proposed. Higher
5 ratings would provide Avista with enhanced access to debt
6 capital.

7 **Q. Will Avista maintain its own capital structure and,**
8 **if so, how will that affect its cost of capital for**
9 **ratemaking?**

10 A. Yes, Avista will maintain its own balance sheet.
11 We have committed that Avista's cost of capital for ratemaking
12 purposes will be no greater than it would have been absent
13 this transaction.

14 **Q. Will Avista maintain separate credit ratings?**

15 A. Yes, Hydro One and Avista will seek a separate
16 rating for Avista from at least one nationally recognized
17 statistical rating agency ("Rating Agency").

18 **Q. Please describe opportunities for Hydro One and**
19 **Avista to share certain costs.**

20 A. Initially, Hydro One and Avista do not expect there
21 to be significant opportunities for cost sharing. Over time,
22 however, Hydro One and Avista will look for opportunities to
23 share certain costs such as IT investments. Further, Hydro
24 One and Avista will benefit from increased purchasing power.

1 **Q. Does Hydro One make any commitment with respect to**
2 **how corporate costs will be allocated?**

3 A. Yes. **Commitment 23** provides that Avista will file
4 cost allocation methodologies used to allocate to Avista any
5 cost related to Olympus Holding Corp. or its other
6 subsidiaries and that Avista will bear the burden of proof in
7 any general rate case that any corporate and affiliate cost
8 allocation methodology it proposes is reasonable for
9 ratemaking purposes. Also, Avista witness Ehrbar sponsors as
10 Exhibit No. 7, Schedule 3, the "Protocol for Direct Assignment
11 of Costs Between Avista and Hydro One".

12 Avista will notify the Commission of any change in
13 corporate structure that affects Avista's corporate and
14 affiliate cost allocation methodologies and will propose
15 revisions to such cost allocation methodologies to
16 accommodate such changes.

17 **Q. Do the Joint Applicants make any commitment with**
18 **respect to Commission auditing of such allocations?**

19 A. Yes, Olympus Holding Corp. and Avista commit to
20 provide audit rights with respect to the documents supporting
21 any costs that may be allocable to Avista. Please refer to
22 "Access to and Maintenance of Books and Records" (**Commitment**
23 **No. 22**) in Appendix 8 (Master List of Commitments) to the
24 Joint Application.

1 **Ring-Fencing Merger Commitments**

2 **Q. Please describe the "ring-fencing" protections the**
3 **Joint Applicants will employ to isolate Avista from Hydro One**
4 **and Hydro One's other subsidiaries.**

5 A. Hydro One commits to the following ring-fencing
6 protections to isolate Avista from Hydro One and Hydro One's
7 other subsidiaries. The following descriptions are merely
8 summaries of these commitments. The complete text of these
9 ring-fencing commitments is set forth in Appendix 8 to the
10 Joint Application and in Exhibit No. 3, Schedule 4 sponsored
11 by Avista witness Thies.

- 12 • *Olympus Equity LLC*: **Commitment 42** provides that Hydro
13 One will include an entity, designated as "Olympus Equity
14 LLC," between Avista and Olympus 2 LLC. Following closing
15 of the Proposed Transaction, all of the common stock of
16 Avista will be owned by Olympus Equity LLC, which is a
17 Delaware limited liability company. Olympus Equity LLC
18 is a wholly-owned subsidiary of Olympus 2 LLC. Olympus
19 Equity LLC is a bankruptcy-remote special purpose
20 entity, and will not have debt.

- 21 • *Independent Directors and Managers*: **Commitment 40**
22 provides that at least one of the nine members of the
23 board of directors of Avista will be an Independent
24 Director who is not a member, stockholder, director

1 (except as an independent director of Avista or Olympus
2 Equity LLC), officer, or employee of Hydro One or its
3 affiliates. At least one of the members of the board of
4 directors of Olympus Equity LLC will be an independent
5 director who is not a member, stockholder, director
6 (except as an independent director of Olympus Equity LLC
7 or Avista), officer, or employee of Hydro One or its
8 affiliates. The same individual may serve as an
9 independent director of both Avista and Olympus Equity
10 LLC.

11 • Bankruptcy Protections: **Commitment 40** provides that the
12 organizational documents for Avista will not permit
13 Avista, without the consent of a two-thirds majority of
14 all its directors, including the affirmative vote of the
15 independent director (or if at that time Avista has more
16 than one independent director, the affirmative vote of
17 at least one of Avista's independent directors), to
18 consent to the institution of bankruptcy proceedings or
19 the inclusion of Avista in bankruptcy proceedings.

20 • Non-Consolidation Opinion: **Commitment 41** provides that
21 within ninety (90) days of the Proposed Transaction
22 closing, Avista and Olympus Holding Corp. will file a
23 non-consolidation opinion with the Commission which
24 concludes, subject to customary assumptions and

1 exceptions, that the ring-fencing provisions are
2 sufficient that a bankruptcy court would not order the
3 substantive consolidation of the assets and liabilities
4 of Avista with those of Olympus Holding Corp. or its
5 affiliates or subsidiaries (other than Avista and its
6 subsidiaries).

7 • Separate Books and Records: **Commitment 21** provides that
8 Avista will maintain separate books and records.

9 • Restriction on Pledge of Utility Assets: **Commitment 43**
10 provides that Avista will agree to prohibitions against
11 loans or pledges of utility assets to Hydro One, Olympus
12 Holding Corp., or any of their subsidiaries or
13 affiliates, without Commission approval.

14 • Hold Harmless; Notice to Lenders; Restriction on
15 Acquisitions and Dispositions: **Commitment 44** includes
16 a number of provisions designed to ensure Avista's
17 customers are held harmless from certain events and that
18 such events are subject to regulatory supervision:

19 • Avista customers must be held harmless from
20 any business and financial risk exposures
21 associated with Olympus Holding Corp., Hydro
22 One, and Hydro One's other affiliates.

23 • Prospective lenders must receive a notice
24 explaining the ring-fencing provisions.

- 1 • Avista commits that Avista's regulated utility
2 customers will be held harmless from the
3 liabilities of any unregulated activity of
4 Avista or Hydro One and its affiliates. In any
5 proceeding before the Commission involving
6 rates of Avista, the fair rate of return for
7 Avista will be determined without regard to
8 any adverse consequences that are demonstrated
9 to be attributable to unregulated activities.
10 Measures providing for separate financial and
11 accounting treatment will be established for
12 each unregulated activity.
- 13 • Olympus Holding Corp. and Avista will notify
14 the Commission subsequent to Olympus Holding
15 Corp.'s board approval and as soon as
16 practicable following any public announcement
17 of: (1) any acquisition by Olympus Holding
18 Corp. of a regulated or unregulated business
19 that is equivalent to five (5) percent or more
20 of the capitalization of Avista; or (2) the
21 change in effective control or acquisition of
22 any material part of Avista by any other firm,
23 whether by merger, combination, transfer of
24 stock or assets.

- 1 • Neither Avista nor Olympus Holding Corp. will
2 assert in any future proceedings that, by
3 virtue of the Proposed Transaction and the
4 resulting corporate structure, the Commission
5 is without jurisdiction over any transaction
6 that results in a change of control of Avista.
- 7 • Within sixty (60) days following the notice
8 required by this subsection (c)(ii)(2), Avista
9 and Olympus Holding Corp. or its subsidiaries,
10 as appropriate, will seek Commission approval
11 of any sale or transfer of any material part
12 of Avista. The term "material part of Avista"
13 means any sale or transfer of stock
14 representing ten percent (10%) or more of the
15 equity ownership of Avista.
- 16 • If and when any subsidiary of Avista becomes
17 a subsidiary of Hydro One or one of its
18 subsidiaries other than Avista, Avista will so
19 advise the Commission within thirty (30) days
20 and will submit to the Commission a written
21 document setting forth Avista's proposed
22 corporate and affiliate cost allocation
23 methodologies.

1 • Corporate Structure - Cost Allocation: **Commitment 23**

2 establishes that Avista will provide cost allocation
3 methodologies used to allocate to Avista any costs
4 related to Olympus Holding Corp. or its other
5 subsidiaries, and commits that there will be no cross-
6 subsidization by Avista customers of unregulated
7 activities.

8 Avista will notify the Commission of any change in
9 corporate structure that affects Avista's corporate and
10 affiliate cost allocation methodologies. Avista will
11 propose revisions to such cost allocation methodologies
12 to accommodate such changes.

13 • Olympus 2 LLC and Olympus Equity LLC Sub-entities:

14 **Commitment 45** provides that Olympus 2 LLC will not
15 operate or own any business and will limit its activities
16 to investing in and attending to its shareholdings in
17 Olympus Equity LLC, which, in turn, will not operate or
18 own any business and will limit its activities to
19 investing in and attending to its shareholdings in
20 Avista.

21 • Access to and Maintenance of Books and Records:

22 **Commitment 22** provides that Olympus Holding Corp. and
23 its subsidiaries, including Avista, will provide
24 reasonable access to Avista's books and records; access

1 to financial information and filings; audit rights with
2 respect to the documents supporting any costs that may
3 be allocable to Avista; and access to Avista's board
4 minutes, audit reports, and information provided to
5 credit rating agencies pertaining to Avista.

6 • Utility-Level Debt, Preferred Stock and Ratings:

7 **Commitment 34** provides that Avista will maintain
8 separate debt and preferred stock, if any, to support
9 its utility operations.

10 • Ratemaking Cost of Debt and Equity: **Commitment 24**

11 provides that Avista will not advocate for a higher cost
12 of debt or equity capital as compared to what Avista's
13 cost of debt or equity capital would have been absent
14 Hydro One's ownership. For future ratemaking purposes:

15 (a) Determination of Avista's debt costs will be no
16 higher than such costs would have been assuming Avista's
17 credit ratings by at least one industry recognized rating
18 agency, including, but not limited to, S&P, Moody's,
19 Fitch or Morningstar, in effect on the day before the
20 Proposed Transaction closes and applying those credit
21 ratings to then-current debt, unless Avista proves that
22 a lower credit rating is caused by circumstances or
23 developments not the result of financial risks or other
24 characteristics of the Proposed Transaction; (b) Avista

bears the burden to prove prudent in a future general rate case any pre-payment premium or increased cost of debt associated with existing Avista debt retired, repaid, or replaced as a part of the Proposed Transaction; and (c) Determination of the allowed return on equity in future general rate cases will include selection and use of one or more proxy group(s) of companies engaged in businesses substantially similar to Avista, without any limitation related to Avista's ownership structure.

- Avista Capital Structure: **Commitment 25** provides that at all times following the closing of the Proposed Transaction, Avista will have a common equity ratio of not less than 44 percent (as calculated for ratemaking purposes) except to the extent the Commission establishes a lower equity ratio for Avista for ratemaking purposes.

- Restrictions on Upward Dividends and Distributions: **Commitment 36** imposes the following restrictions on Avista's upward dividends and distributions:

- o If either (i) Avista's corporate credit/issuer rating as determined by at least one industry recognized rating agency, including, but not limited to, S&P, Moody's, Fitch, or

1 Morningstar is investment grade or (ii) the
2 ratio of Avista's EBITDA to Avista's interest
3 expense is greater than or equal to 3.0, then
4 distributions from Avista to Olympus Equity
5 LLC shall not be limited so long as Avista's
6 equity ratio is equal to or greater than 44
7 percent on the date of such Avista
8 distribution after giving effect to such
9 Avista distribution, except to the extent the
10 Commission establishes a lower equity ratio
11 for ratemaking purposes. Both the EBITDA and
12 equity ratio shall be calculated on the same
13 basis that such calculations would be made for
14 ratemaking purposes for regulated utility
15 operations.

16 o Under any other circumstances, distributions
17 from Avista to Olympus Equity LLC are allowed
18 only with prior Commission approval.

19 • Continued Credit Ratings: **Commitment 35** provides that
20 each of Hydro One and Avista will continue to be rated
21 by at least one nationally recognized statistical
22 "Rating Agency." Hydro One and Avista will use
23 reasonable best efforts to obtain and maintain a separate
24 credit rating for Avista from at least one Rating Agency

1 within the ninety (90) days following the closing of the
2 Proposed Transaction. If Hydro One and Avista are unable
3 to obtain or maintain the separate rating for Avista,
4 they will make a filing with the Commission explaining
5 the basis for their failure to obtain or maintain such
6 separate credit rating for Avista, and parties to this
7 proceeding will have an opportunity to participate and
8 propose additional commitments.

9 • No Amendment of Ring Fencing Provisions: **Commitment 46**

10 provides that Olympus Holding Corp. and Avista commit
11 that no material amendments, revisions or modifications
12 will be made to the ring-fencing provisions as specified
13 in these regulatory commitments without prior Commission
14 approval pursuant to a limited re-opener for the sole
15 purpose of addressing the ring-fencing provisions.
16

17 **VI. RATE CREDITS**

18 **Q. Will Avista provide Rate Credits to customers as**
19 **part of the Proposed Transaction?**

20 A. Yes. Customers will see immediate financial
21 benefits in the form of proposed retail Rate Credits ("Rate
22 Credits") beginning at the close of the Proposed Transaction.
23 Through **Commitment 18**, Avista and Hydro One are proposing to
24 flow through to Avista's retail customers in Idaho,

1 Washington, and Oregon a Rate Credit of \$31.5 million over a
2 10-year period, beginning at the time the merger closes. The
3 Rate Credit consists of two components, and reflects an
4 increased level of savings in years 6-10 as illustrated in
5 the table below.

6

Two-Step Rate Credit Proposal				
	Annual Credit Years 1-5	Annual Credit Years 6-10	Total Credit	
9 Total Credit	\$2.65 Million	\$3.65 Million	\$31.50 Million	
10 Offsetable Credit	\$1.70 Million	\$2.70 Million	\$22.00 Million	

11

12 **Commitment 18** further provides that the Total Rate Credit
13 to customers for the first five years following the closing
14 would be \$2.65 million per year, and the credit would increase
15 to \$3.65 million per year for the last five years of the 10-
16 year period. A portion of the annual total Rate Credit would
17 be offsetable, as indicated in the table above. During the
18 10-year period the financial benefits will be flowed through
19 to customers either through the separate Rate Credit described
20 above or through a reduction to the underlying cost of service
21 as these benefits are reflected in the test period numbers
22 used for ratemaking. At the time of the close, the \$2.65
23 million benefit will be provided to customers through a
24 separate Rate Credit, as long as the reduction in costs has

1 not already been reflected in base retail rates for Avista's
2 customers.

3 **Commitment 18** also provides that to the extent Avista
4 demonstrates in a future rate proceeding that cost savings,
5 or benefits, directly related to the Proposed Transaction are
6 already being flowed through to customers through base retail
7 rates, the separate Rate Credit to customers would be reduced
8 by an amount up to the offsetable Rate Credit amount. The
9 portion of the total Rate Credit that is not offsetable
10 effectively represents acceptance by Hydro One of a lower rate
11 of return during the 10-year period.

12 **Commitment 18** finally provides that the \$31.5 million
13 represents the "floor" of benefits that will be flowed through
14 to Avista's customers, either through the Rate Credit or
15 through benefits otherwise included in base retail rates. To
16 the extent the identifiable benefits exceed the annual
17 offsetable Rate Credit amounts, these additional benefits
18 will be flowed through to customers in base retail rates in
19 general rate cases as they occur. The increase in total Rate
20 Credits for years 6-10 will provide time for Avista and Hydro
21 One to identify and capture over time an increased level of
22 benefits, directly related to the Proposed Transaction, that
23 can be flowed through to customers. Avista and Hydro One
24 believe additional efficiencies (benefits) will be realized

1 over time from the sharing of best practices, technology and
2 innovation between the two companies. It will take time,
3 however, to identify and capture these benefits. The level
4 of annual net cost savings (and/or net benefits) will be
5 tracked and reported on an annual basis, and compared against
6 the offsetable level of savings. Mr. Thies provides additional
7 details related to the proposed Rate Credit.

8 **Q. Does this conclude your direct testimony?**

9 A. Yes, it does.