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ON BEHALF OF AVISTA CORPORATION

Boise, Idaho

DAVID J. MEYER
VICE PRESIDENT AND CHIEF COUNSEL FOR
REGULATORY & GOVERNMENTAL AFFAIRS
P.O. BOX 3727
1411 EAST MISSION AVENUE
SPOKANE, WASHINGTON 99220-3727
TELEPHONE: (509) 495-4316
FACSIMILE: (509) 495-8851
DAVID.MEYER@AVISTACORP.COM

ON BEHALF OF HYDRO ONE LIMITED

ELIZABETH THOMAS, PARTNER
KARI VANDER STOEP, PARTNER
K&L GATES LLP
925 FOURTH AVENUE, SUITE 2900
SEATTLE, WA 981014-1158
TELEPHONE: (206) 623-7580
FACSIMILE: (206) 370-6190
LIZ.THOMAS@KLGATES.COM
KARI.VANDERSTOEP@KLGATES.COM

BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

IN THE MATTER OF THE JOINT)
APPLICATION OF HYDRO ONE LIMITED) CASE NO. AVU-E-17-09
(ACTING THROUGH ITS INDIRECT) CASE NO. AVU-G-17-05
SUBSIDIARY, OLYMPUS EQUITY LLC))
AND)
AVISTA CORPORATION) SUPPLEMENTAL TESTIMONY
FOR AN ORDER AUTHORIZING PROPOSED) OF
TRANSACTION) JOHN R. REED

FOR CONCENTRIC ENERGY ADVISORS
ON BEHALF OF HYDRO ONE LTD.
AND AVISTA CORPORATION

1 I. INTRODUCTION

2 Q. Please state your name and business address.

3 A. My name is John J. Reed. I am President and Chief
4 Executive Officer of Concentric Energy Advisors, Inc.
5 ("Concentric") and CE Capital Advisors, Inc. ("CE Capital"),
6 which has its headquarters at 293 Boston Post Road West, Suite
7 500, Marlborough, Massachusetts 01752.

8 Q. On whose behalf are you submitting this testimony?

9 A. I am testifying on behalf of Hydro One Limited
10 ("Hydro One") and Avista Corporation ("Avista"). Hydro One
11 filed an Application seeking an order authorizing Hydro One,
12 acting through its indirect subsidiary Olympus Equity LLC, to
13 acquire all of the outstanding common stock of Avista and
14 Avista would become a direct, wholly-owned subsidiary of
15 Olympus Equity LLC and an indirect, wholly-owned subsidiary of
16 Hydro One (the "Proposed Transaction" and "Application for
17 Approval of Transaction"). Hydro One and Avista subsequently
18 executed a stipulation and settlement ("Settlement
19 Stipulation") with the Staff of the Idaho Public Utilities
20 Commission ("Staff"), Clearwater Paper Corporation
21 ("Clearwater"), Idaho Forest Group, LLC, Idaho Conservation
22 League ("ICL"), the Community Action Partnership Association
23 of Idaho ("CAPAI"), and the Washington and Northern Idaho

1 District Council of Laborers ("WNIDCL") (individually a
2 "Party" and collectively the "Parties"). The Settlement
3 Stipulation was filed with the Idaho Public Utilities
4 Commission ("Commission") on April 13, 2018.

5 **Q. Please describe your educational background and**
6 **professional experience in the energy and utility industries.**

7 A. I have more than 40 years of experience in the
8 energy industry and have worked as an executive in, and
9 consultant and economist to, the energy industry. Over the
10 past 29 years, I have directed the energy consulting services
11 of Concentric, Navigant Consulting, and Reed Consulting Group.
12 I have served as Vice Chairman and co-CEO of the nation's
13 largest publicly-traded consulting firm and as Chief Economist
14 for the nation's largest gas utility. I have provided
15 regulatory policy and regulatory economics support to more
16 than 100 energy and utility clients and have provided expert
17 testimony on regulatory, economic, and financial matters on
18 more than 150 occasions before the Federal Energy Regulatory
19 Commission ("FERC"), Canadian regulatory agencies, state
20 utility regulatory agencies, various state and federal courts,
21 and before arbitration panels in the United States and Canada.
22 As an industry expert, I have been involved in numerous
23 utility transactions over the past 20 years, including

1 mergers, divestitures, asset acquisitions, and
2 reorganizations. In addition to this transaction, I have
3 advised clients involved in utility transactions in Arizona,
4 Connecticut, Delaware, the District of Columbia, Hawaii,
5 Kansas, Illinois, Indiana, Iowa, Louisiana, Maryland,
6 Massachusetts, Michigan, Minnesota, New Hampshire, New Jersey,
7 New York, Pennsylvania, Rhode Island, Texas, Utah, and
8 Wisconsin. I have appeared as an expert witness in several
9 jurisdictions on the topics of merger policy standards,
10 acquisition financing plans, merger benefits analyses,
11 affiliate codes of conduct, impacts on competition and energy
12 markets, and merger-related commitments or conditions. I am a
13 graduate of the Wharton School of Business at the University
14 of Pennsylvania, and previously attended the University of
15 Kansas. My background is presented in more detail in Exh. No.
16 13, Schedule 1.

17 **Q. Please describe Concentric's activities in energy**
18 **and utility engagements.**

19 A. Concentric provides financial and economic advisory
20 services to many energy and utility clients across North
21 America. Our regulatory, economic, and market analysis
22 services include utility ratemaking and regulatory advisory
23 services, energy market assessments, market entry and exit

1 analysis, corporate and business unit strategy development,
2 demand forecasting, resource planning, and energy contract
3 negotiations. Our financial advisory activities include both
4 buy- and sell-side merger, acquisition and divestiture
5 assignments, due diligence and valuation assignments, project
6 and corporate finance services, and transaction support
7 services. In addition, we provide litigation support services
8 on a wide range of financial and economic issues on behalf of
9 clients throughout North America. CE Capital is a fully
10 registered broker-dealer securities firm specializing in merger
11 and acquisition activities. As CEO of CE Capital, I hold
12 several securities licenses that cover all forms of securities
13 and investment banking activities

14 **Q. What is the purpose of your testimony?**

15 A. The purpose of my testimony is to provide my
16 assessment of the reasonableness and sufficiency of the
17 governance, financial integrity and ring-fencing provisions of
18 the Commitments attached as Exhibit A to the Settlement
19 Stipulation¹ in light of the recent political developments in
20 the Province of Ontario (the "Province") and changes in Hydro
21 One's executive management and board of directors.

¹ AVU-E-17-09, AVU-G-17-05, Stipulation and Settlement (April 13, 2018) (including Appendix A, "Master List of Commitments in Idaho") ("Settlement Stipulation").

1 **Q. What is your understanding of the recent political**
2 **developments in the Province and the governance changes at**
3 **Hydro One?**

4 A. Hydro One agreed on July 11, 2018, that its existing
5 Board of Directors would resign by August 15, 2018, and Hydro
6 One's President and Chief Executive Officer (the "CEO") would
7 retire, effective immediately. On August 14, 2018, Hydro One
8 announced its new 10-member Board of Directors (the "Board").
9 Hydro One's new Board is in the process of selecting a new
10 CEO. It is my understanding that the replacement of Hydro
11 One's Board was generally consistent with the Governance
12 Agreement (the "Governance Agreement") between Hydro One and
13 Her Majesty the Queen in Right of Ontario, provided as Exh.
14 No. 10, Schedule 3, as described in the Supplemental Testimony
15 of James Scarlett ("Scarlett Testimony"), and with the July
16 11, 2018 Letter Agreement between Hydro One and the Province
17 ("July 2018 Letter Agreement"), provided as Exh. No. 10,
18 Schedule 1 and as an attachment to the Letter from Joint
19 Applicants Regarding Update on Recent Changes in Hydro One
20 Management (July 18, 2018) ("Avista and Hydro One Comments").

21 On July 16, 2018, the new Provincial government
22 introduced the *Urgent Priorities Act, 2018*, which, included as
23 Schedule 1, the *Hydro One Accountability Act, 2018*, provided

1 as Exh. No. 10, Schedule 2. The *Urgent Priorities Act*
2 received Royal Assent on July 25, 2018, which is the day it
3 came into force as law in the Province. Schedule 1, the *Hydro*
4 *One Accountability Act* (the "Act") came into force on the day
5 named by proclamation of the Lieutenant Governor, which
6 occurred on August 15, 2018. The Act requires, among other
7 things, the Board of Hydro One to establish a new compensation
8 framework for the Board, CEO, and other executives in
9 consultation with the Province and the other five largest
10 shareholders. The Act will not apply to Avista if Avista
11 becomes a subsidiary of Hydro One.

12 Please refer to the Scarlett Testimony and the Avista and
13 Hydro One Comments for a more in-depth discussion of these
14 recent developments at Hydro One.

15 **Q. How is the remainder of your testimony organized?**

16 A. Section II summarizes my key conclusions. In
17 Section III, I evaluate the governance-related commitments
18 made by Hydro One and Avista in the Settlement Stipulation.
19 Section IV provides my evaluation of the ring-fencing
20 commitments made by Hydro One and Avista. In Section V, I
21 evaluate the financial integrity commitments made in the
22 Settlement Stipulation. Finally, Section VI presents my
23 conclusions regarding the Proposed Transaction.

1 Q. Are you sponsoring any exhibits as part of your
2 testimony?

3 A. Yes. Attached to my testimony are:

- 4 • Exh. No. 13, Schedule 1 - Resume and testimony
5 listing
- 6 • Exh. No. 13, Schedule 2 - Recent Merger
7 Governance-Related Conditions
- 8 • Exh. No. 13, Schedule 3 - Recent Merger Ring-
9 Fencing Conditions
- 10 • Exh. No. 13, Schedule 4 - Recent Merger Financial
11 Integrity-Related Conditions

12 A table of contents for my testimony is as follows:

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1 II. SUMMARY OF KEY CONCLUSIONS

2 Q. Please begin by providing your general observations
3 about the recent political developments in the Province and
4 the governance changes at Hydro One.

5 A. While changes in Directors and executives are part
6 of the normal course of business, simultaneously changing both
7 the Board of Directors and the CEO is unusual. It is
8 important to consider the potential implications of these
9 changes for the Proposed Transaction, Avista, its ratepayers
10 and the public interest. I have reviewed the Settlement
11 Stipulation, which includes an integrated and comprehensive
12 set of governance, ring-fencing, financial integrity and other
13 regulatory commitments (individually "Stipulated Commitment
14 No.", collectively, the "Stipulated Commitments"). The
15 Parties to the Settlement Stipulation agree that the
16 Settlement Stipulation "represents a fair, just and reasonable
17 compromise of all the issues raised in the proceeding and its
18 acceptance by the Commission represents a reasonable
19 resolution of the multiple issues identified in this case.
20 The Parties, therefore, recommend that the Commission, in
21 accordance with RP 174, approve the Settlement Stipulation and
22 all of its terms and conditions without material change or

1 condition."² Nothing in the recent political changes in the
2 Province and governance changes at Hydro One should change
3 that conclusion. The Stipulated Commitments made in the
4 Settlement Stipulation, in particular the Avista governance,
5 ring-fencing and financial integrity commitments, provide
6 significant protections for customers and support the public
7 interest. There is nothing to suggest that once the Proposed
8 Transaction closes, Avista customers or the public interest in
9 Idaho will suffer any ill effects from the recent events
10 discussed above or from potential future actions of the
11 Provincial government.

12 **Q. Please summarize your key conclusions regarding the**
13 **Avista Board of Directors, ring-fencing, financial integrity**
14 **and other Stipulated Commitments in the Settlement**
15 **Stipulation.**

16 A. The Settlement Stipulation provides a robust, state-
17 of-the-art set of governance, ring-fencing, and other
18 Stipulated Commitments both to provide the appropriate
19 separation of Avista from Hydro One and its other affiliates
20 and subsidiaries, and to protect Avista customers from
21 potential future risks. The Stipulated Commitments are very
22 robust and well in excess of industry norms established by

² Settlement Stipulation at p. 2.

1 commitments made in other recent utility mergers and
2 acquisitions.

3 The Stipulated Commitments were specifically designed to
4 address Hydro One's ownership of Avista and the Province's
5 role as the largest investor in Hydro One. The Stipulated
6 Commitments also address the regulation of Hydro One by the
7 Ontario Energy Board (the "OEB"), an agent of the Province
8 which regulates natural gas and electricity utilities in
9 Ontario. Among other things, the OEB sets rates and licenses
10 all participants in the Province's electricity and natural gas
11 sectors. While the OEB is an independent agency, it is still
12 subject to provincial legislation. In summary, these
13 Stipulated Commitments provide for:

14 • The independence of Avista's Board of
15 Directors, CEO, and executives whereby seven of
16 Avista's nine Directors will either be
17 independent as defined by the New York Stock
18 Exchange ("NYSE") rules ("Independent
19 Directors") or appointed by Avista, making it
20 impossible for Hydro One, the Province, or any
21 shareholder to direct the governance or
22 management of Avista;

- 1 • The Avista Board of Directors to make all
2 decisions regarding the governance, business
3 operations and local presence/community
4 involvement Stipulated Commitments;
- 5 • Continued capital investment in strategic and
6 economic development items;
- 7 • Hydro One's provision of equity to support
8 Avista's capital structure; and
- 9 • Ensuring Avista's financial integrity by
10 maintaining separate credit ratings and debt
11 instruments, prohibiting inter-company debt and
12 lending, restriction on pledging utility
13 assets, and restrictions on Avista's upwards
14 dividends and distributions, as well as
15 restrictions and protections in the unlikely
16 event of a bankruptcy.

17 The efficacy of the Stipulated Commitments made as part
18 of the Settlement Stipulation is unchanged by recent events.
19 If anything, recent events highlight the validity of these
20 Stipulated Commitments and the unusual level of separation
21 they provide between Hydro One and Avista and restrictions on
22 Hydro One and the Province as it pertains to Avista.

1 Taken as a whole, and in combination with the
2 Commission's on-going regulatory oversight and authority over
3 Avista, these Stipulated Commitments are appropriate and fully
4 address potential risks by ensuring that customers are
5 protected from potential risks of the Proposed Transaction and
6 will continue to enjoy safe and reliable electric service.

7

8 **III. THE SETTLEMENT STIPULATION'S GOVERNANCE COMMITMENTS**

9 **Q. Please briefly highlight the Stipulation**
10 **Settlement's governance-related commitments.**

11 A. The Settlement Stipulation's governance-related
12 commitments start with specific requirements regarding
13 Avista's Board of Directors. As discussed by Hydro One's
14 Executive Vice President and Chief Legal Officer James
15 Scarlett,³ if the Proposed Transaction is approved and closes
16 Avista will continue to be governed by its own, independent
17 Board of Directors, separate from the Hydro One Board.
18 Stipulated Commitment No. 3 requires that Avista's Board of
19 Directors consist of nine members: (1) three Independent
20 Directors, as defined by the NYSE rules, and who are also
21 residents of the Pacific Northwest, (2) three Directors who
22 are members of Avista's current Board, (3) Avista's CEO, and

³ Scarlett Testimony, § VIII.

1 (4) two executives of Hydro One or any of its subsidiaries.
2 The implementation of Stipulated Commitment No. 3 will result
3 in seven of the nine members of Avista's post-closing Board of
4 Directors being either NYSE-independent or designated by
5 Avista, ensuring continued Avista focus for its Board of
6 Directors.

7 **Q. How do the NYSE rules define "Independent" and what**
8 **is its import for Avista's post-closing governance?**

9 A. The NYSE rules define "independent" as "no material
10 relationship" with the company "either directly or as a
11 partner, shareholder or officer of an organization that has a
12 relationship with the company".⁴ In establishing this
13 definition, the NYSE noted that "[e]ffective boards of
14 directors exercise independent judgment in carrying out their
15 responsibilities. Requiring a majority of independent
16 directors will increase the quality of board oversight and
17 lessen the possibility of damaging conflicts of interest."⁵

⁴ NYSE, Inc., Listed Company Manual Section 303A.02 (2018), <http://wallstreet.cch.com/LCMTTools/PlatformViewer.asp?selectednode=chp%5F1%5F4%5F3&manual=%2F1cm%2Fsections%2F1cm%2Dsections%2F> (last visited Sept. 5, 2018, 4:17 PM).

⁵ NYSE, Inc., Listed Company Manual Section 303A.01 Commentary (2018), <http://wallstreet.cch.com/LCMTTools/PlatformViewer.asp?selectednode=chp%5F1%5F4%5F3&manual=%2F1cm%2Fsections%2F1cm%2Dsections%2F> (last visited Sept. 5, 2018, 4:18 PM).

1 Q. Were commitments made to ensure that the composition
2 of Avista's Board of Directors provided in Stipulated
3 Commitment No. 3 will be maintained in the future as
4 individual Directors may turn over?

5 A. Yes. Stipulated Commitment No. 3 specifically
6 provides that if any Avista designee resigns, retires or
7 otherwise ceases to serve as a director of Avista for any
8 reason, the remaining Avista designees shall nominate a
9 replacement director to fill such vacancy. Nominations are
10 approved by the Avista Board of Directors.

11 The Delegation of Authority (see Appendix 5 of the Joint
12 Application)⁶ provides that Hydro One may replace the Hydro One
13 designated Directors, provided that three are Independent.
14 The Delegation of Authority also provides Hydro One with some
15 limited latitude in satisfying this commitment: if it were
16 unable to appoint an Independent Director residing in the
17 Pacific Northwest in a timely manner, Hydro One could appoint
18 an interim Director for no more than a six-month term who is
19 an employee of Hydro One or one of its subsidiaries while it
20 found a suitable Independent Director.

⁶ AVU-E-17-09, AVU-G-17-05, Joint Application for Order Authorizing Proposed Transaction, Appendix 5 Delegation of Authority to Avista Board of Directors (Sep. 14, 2017).

1 **Q. Are you aware of Hydro One and Avista's proposal to**
2 **limit Hydro One's latitude with respect to Hydro One's**
3 **designated Independent Directors on the Avista post-merger**
4 **board?**

5 A. Yes. Hydro One and Avista propose to amend the
6 Delegation of Authority to eliminate this limited latitude
7 under certain circumstances. As discussed in the Scarlett
8 Testimony, Hydro One and Avista propose that this exception
9 shall not apply if, at any time a circumstance arises, and
10 during the pendency of any such circumstance, whereby the
11 Province exercises its rights as a shareholder of Hydro One,
12 or uses legislative authority, or acts in any other manner
13 whatsoever, that results, or would result, in Ontario
14 appointing nominees to the Board of Directors of Hydro One
15 that constitute, or would constitute a majority of the
16 directors of such board.

17 **Q. What is the importance of this amendment to the**
18 **Delegation of Authority?**

19 A. This proposed amendment to the Delegation of
20 Authority provides extra protection for the independence of
21 the Avista Board in the event that the Province takes some
22 action in the future to control a majority of the Hydro One
23 Board. If that event occurs, this amendment is triggered and

1 blocks Hydro One's limited right to replace any of its three
2 Independent Director designees on the Avista board with a
3 Hydro One executive or employee. This limitation makes clear
4 that there are no circumstances under which the Province or
5 Hydro One can control the Avista Board.

6 **Q. Does the Settlement Stipulation include any other**
7 **specific governance commitments?**

8 A. Yes. Stipulated Commitment No. 2 provides that
9 Avista will seek to retain its current executives post-closing
10 of the Proposed Transaction subject to voluntary retirements
11 and Avista's ability to select and retain personnel best able
12 to meet its needs over time. The Avista Board of Directors
13 retains the ability to dismiss executive management of Avista
14 and other Avista personnel for standard corporate reasons.
15 This commitment reinforces Avista's control over its
16 executives.

17 **Q. Has Hydro One made any additional governance-related**
18 **commitments incremental to those made in the Settlement**
19 **Stipulation?**

20 A. Yes. In response to recent events, Hydro One and
21 Avista have proposed an additional commitment to provide
22 additional clarity regarding the responsibility of the Avista

1 Board of Directors. In the Avista and Hydro One Comments,
2 Hydro One made the following additional commitment:

3 Avista Employee Compensation: Any decisions
4 regarding Avista employee compensation shall be
5 made by the Avista Board consistent with the
6 terms of the Merger Agreement between Hydro One
7 and Avista, and current market standards and
8 prevailing practices of relevant U.S. electric
9 and gas utility benchmarks. The determination of
10 the level of any compensation (including equity
11 awards) approved by the Avista Board with respect
12 to any employee in accordance with the foregoing
13 shall not be subject to change by Hydro One or
14 the Hydro One Board.⁷

15 This new commitment makes clear that the Avista Board,
16 and not the Hydro One Board, the Province, or any other party,
17 will make decisions regarding Avista employee compensation.

18 **Q. Did you evaluate how the Settlement Stipulation's**
19 **governance commitments compare to other recent utility mergers**
20 **and acquisitions in the U.S.?**

21 A. Yes. I considered 40 transactions involving the
22 merger or acquisition of a U.S. investor owned utility ("IOU")
23 that have been completed since 2010. My review was based upon
24 publicly-available information about these transactions
25 including state commission orders and information published by
26 SNL Financial, an industry-specific financial market data
27 source for public and private companies worldwide.

⁷ See Avista and Hydro One Comments at pp.5-6.

1 **Q. How do the governance Stipulated Commitments compare**
2 **to governance commitments made in these other IOU**
3 **transactions?**

4 A. The governance Stipulated Commitments compare very
5 favorably with the governance commitments made in these other
6 IOU transactions. Exh. No. 13, Schedule 2 provides a summary
7 of the governance conditions in these transactions. As shown
8 in that exhibit, none of the transactions I reviewed included
9 all of the governance commitments made by the Parties in the
10 Stipulated Commitments. In particular, the new commitment
11 regarding executive compensation was only made or required in
12 one other transaction I reviewed or have been involved in.
13 Further, commitments similar to Stipulated Commitment No. 3,
14 Board of Directors, and Stipulated Commitment No. 2, Executive
15 Management, are rarely used or required.

16 **Q. Why is comparing the Stipulated Commitments made by**
17 **Hydro One and Avista to the commitments made by counterparties**
18 **to IOU transactions informative?**

19 A. While the commitments made in a given transaction
20 should be specific to that transaction's specific
21 circumstances, there are clear industry norms regarding the
22 nature of merger commitments. Some amount of governance-
23 related commitments, ring-fencing-related commitments, and

1 financial integrity commitments are seen in many transactions.
2 The Parties' Stipulated Commitments, however, are well beyond
3 industry norms. I discuss this further in my review of ring-
4 fencing commitments. The import of this observation is simply
5 that more restrictive commitments are being made by Hydro One
6 and Avista through the Settlement Stipulation to ensure that
7 Avista and its Idaho customers are protected from risk.

8 **Q. Did your comparison include foreign acquisitions of**
9 **U.S. IOUs?**

10 A. Yes. Eleven of the transactions I reviewed involved
11 the acquisition of a U.S. IOU by a foreign entity. Of these
12 eleven transactions, ten involved a Canadian acquirer. See
13 Exh. No. 13, Schedule 2. None of these transactions included
14 all of the Parties' governance Stipulated Commitments. Only
15 two, Alta Gas' acquisition of WGL and Fortis' acquisition of
16 CH Energy, contained both a majority Independent Board
17 requirement and a commitment to offer employment to executives
18 of the acquired utility.

19 **Q. Are there examples of mergers involving the**
20 **acquisition of a U.S. IOU by a foreign government?**

21 A. Yes. While less common, there are examples of
22 foreign government ownership of U.S. IOUs. EPCOR Utilities
23 Inc., an Edmonton, Alberta-based water and wastewater utility

1 company owned by the City of Edmonton, has acquired four U.S.
2 water utilities collectively serving approximately 175,000
3 customers for a combined transaction value of approximately
4 \$510 million.⁸ Each of these transactions was approved by the
5 Arizona Public Service Commission ("APSC"). No governance
6 commitments were made, nor were any governance conditions
7 required by the APSC in these transactions.

8 **Q. Does the Settlement Stipulation include other**
9 **Stipulated Commitments supportive of its governance**
10 **commitments?**

11 A. Yes. Several other Stipulated Commitments
12 pertaining to Avista's business operations and local
13 presence/community involvement post-merger make clear and
14 binding Hydro One's commitment to Avista's management and
15 provision of safe and reliable utility service regardless of
16 changes at Hydro One or the Province. Stipulated Commitment
17 No. 4 specifies that Avista will maintain its brand and Avista
18 will establish the plan for its operation. Avista will also
19 maintain both its staffing and presence in the communities in
20 which Avista operates at levels sufficient to maintain the
21 provision of safe and reliable service and cost-effective
22 operations, consistent with pre-merger levels (Stipulated

⁸ 2011 acquisition of Chaparral, 2012 acquisition of Arizona-American Water, 2013 acquisition of North Mohave, and 2016 acquisition of Willow Valley Water Company. Source: SNL.

1 Commitment No. 10) and its headquarters in Spokane, Washington
2 and office locations in each of its other service territories
3 (Stipulated Commitment No. 9). Stipulated Commitment No. 5
4 specifies Avista will maintain existing levels of capital
5 allocations for capital investment in strategic and economic
6 development items. Avista has specific safety and reliability
7 standards and policies and service quality measures in place
8 in Washington and is working with the Staff to develop similar
9 performance standards, customer guarantees and a reporting
10 mechanism for its customers in Idaho, which will include
11 penalty provisions (Stipulated Commitment 15). Finally,
12 Stipulated Commitment No. 1 reserves all decision-making
13 authority over the governance, business operations and local
14 presence/community involvement Stipulated Commitments to
15 Avista's Board of Directors. Any changes to policies provided
16 for in these Stipulated Commitments requires a two-thirds vote
17 of the Avista Board and approval from the Commission and all
18 regulatory bodies with jurisdiction over the Stipulated
19 Commitments (Stipulated Commitment No. 1). Collectively,
20 these Stipulated Commitments support the Settlement
21 Stipulation's governance Stipulated Commitments and make clear
22 that Avista's governance will be independent of Hydro One and

1 Avista's focus will be on the provision of safe and reliable
2 service to its customers.

3 **Q. Do the recent political developments in Ontario and**
4 **changes in governance at Hydro One have any impact on the**
5 **Settlement Stipulation's governance commitments?**

6 A. No. The governance Stipulated Commitments clearly
7 separate and insulate Avista from the governance of Hydro One
8 and its largest shareholder, the Province. The efficacy of
9 this separation and insulation was demonstrated through the
10 recent developments in the Province, in particular in the
11 acknowledgement and commitment that the *Hydro One*
12 *Accountability Act, 2018* will not apply to Avista if Avista
13 becomes a subsidiary of Hydro One, as discussed in the
14 Scarlett Testimony (Exh. No. 10, Schedule 2). The governance-
15 related Stipulated Commitments provide Avista and its Idaho
16 customers with appropriate independence and protections;
17 recent events have not created any need for modifications to
18 these commitments. Further, these governance Stipulated
19 Commitments are binding (Stipulated Commitment No. 33), the
20 Commission has the authority to enforce them (Stipulated
21 Commitment No. 30) and Avista and Hydro One and/or its
22 subsidiaries submit to state court jurisdiction for
23 enforcement of the Commission's orders (Stipulated Commitment

1 No. 31). Taken as a whole, and in combination with the
2 Commission's on-going regulatory oversight and authority, as
3 well as the ring-fencing and financial integrity Stipulated
4 Commitments that I discuss later in my testimony, the
5 Settlement Stipulation's governance Stipulated Commitments
6 provide customers with appropriate protections and assurances
7 that they will continue to enjoy safe and reliable electric
8 service at rates that reflect their Commission-approved cost
9 of service.

10

11 **IV. THE SETTLEMENT STIPULATION'S RING-FENCING COMMITMENTS**

12 **Q. In addition to its governance Stipulated**
13 **Commitments, have you also reviewed the ring-fencing**
14 **Stipulated Commitments?**

15 **A. Yes, I have. While the governance-related**
16 **Stipulated Commitments address the independence of the going-**
17 **forward governance of Avista under Hydro One ownership, the**
18 **ring-fencing Stipulated Commitments provide clear objectives,**
19 **practices and policies, and restrictions to protect Avista and**
20 **its Idaho customers from the unlikely event of a bankruptcy**
21 **and other potential risks, including potential risks perceived**
22 **with the recent governance changes at Hydro One and political**
23 **changes in the Province.**

1 Q. Please briefly highlight the Settlement
2 Stipulation's bankruptcy-related ring-fencing Stipulated
3 Commitments.

4 A. Stipulated Commitment Nos. 42 through 45 are
5 intended to protect Avista in the unlikely event of a
6 bankruptcy. Stipulated Commitment No. 42 provides for a
7 "Golden Share" in the event Avista were to declare voluntary
8 bankruptcy. The "Golden Share" is the sole share of Preferred
9 Stock authorized by the Commission and held by an independent
10 third-party with no financial stake, affiliation,
11 relationship, interest, or tie to Avista or any of its
12 affiliates. The holder of the Golden Share must be authorized
13 by the Commission. Any declaration of voluntary bankruptcy
14 would require the vote of the holder of the Golden Share and
15 in any matters of bankruptcy the Golden Share will override
16 all other outstanding shares of all types or classes of stock.
17 In addition to the holder of the Golden Share, a two-thirds
18 majority vote of Avista's Board of Directors, including the
19 affirmative vote of the Independent Director at Avista, is
20 required for Avista to enter into voluntary bankruptcy
21 (Stipulated Commitment No. 43).

22 Stipulated Commitment No. 44 requires Hydro One and
23 Avista to file with the Commission within 90-days of the

1 closing of the Proposed Transaction a non-consolidation
2 opinion, which is a legal opinion addressing the likelihood of
3 the utility becoming an involuntary party to the bankruptcy of
4 an affiliate, concluding that the ring-fencing Stipulated
5 Commitments are sufficient that a bankruptcy court would not
6 order the substantive consolidation of the assets and
7 liabilities of Avista with Hydro One or any of its other
8 affiliates or subsidiaries in the unlikely event of
9 bankruptcy. If the Settlement Stipulation's ring-fencing
10 commitments are not sufficient to secure such a non-
11 consolidation opinion, then Hydro One must propose and
12 implement upon the Commission's approval additional ring-
13 fencing protections sufficient to obtain a non-consolidation
14 opinion. Further, Hydro One and Olympus Holding Corp. must
15 file an affidavit with the Commission stating that neither
16 Hydro One, Olympus Holding Corp., nor any of their
17 subsidiaries, will seek to include Avista in a bankruptcy
18 without the consent of a two-thirds majority of Avista's board
19 of directors including the affirmative vote of at least one of
20 Avista's independent directors.

21 Finally, Stipulated Commitment No. 45 provides that all
22 of the common stock of Avista will be owned by Olympus Equity
23 LLC, a bankruptcy-remote special purpose entity, with no debt.

1 **Q. Please briefly highlight the Settlement**
2 **Stipulation's other ring-fencing Stipulated Commitments.**

3 A. Stipulated Commitment Nos. 46 through 51 work
4 together to provide for the separation and independence of
5 Avista from Hydro One and Hydro One's other affiliates.
6 Stipulated Commitment No. 48 provides that Olympus Equity LLC
7 will not operate or own any business and will limit its
8 activities to investing in and attending to its shareholdings
9 in Avista. Stipulated Commitment No. 49 commits Hydro One and
10 Avista to making no material amendments to the ring-fencing
11 provisions without the approval of the Commission. Stipulated
12 Commitment No. 47 requires that Avista customers be held
13 harmless from any business and financial risk exposure
14 associated with Hydro One and its other affiliates and any
15 liabilities of any unregulated activity of Avista or Hydro One
16 and its affiliates. Notice will be provided to all current
17 and prospective lenders describing the ring-fencing Stipulated
18 Commitments and stating that there is no recourse to Avista
19 assets as collateral or security for debt issued by Hydro One
20 or any of its subsidiaries. Olympus Holding Corp. and Avista
21 will notify the Commission of any acquisition by Olympus
22 Holding Corp. of a regulated or unregulated business that is
23 equivalent to 5% or more of the capitalization of Avista or

1 any change in control or ownership of Avista. In addition,
2 Commission approval will be sought of any sale or transfer of
3 any material part (i.e. 10% or more) of Avista, or of any
4 transaction or series of transactions, regardless of size,
5 that would result in a person or entity, other than a wholly
6 owned subsidiary of Hydro One, directly or indirectly,
7 acquiring a controlling interest in Avista or Olympus Holding
8 Corp. Finally, Commission approval will be sought of any
9 divestiture, spin-off, or sale of any integral Avista asset as
10 required by Idaho Code 61-328 and neither Avista nor Hydro One
11 will assert in any future proceedings that, by virtue of the
12 Proposed Transaction, the Commission is without jurisdiction
13 over any transaction that results in a change in control of
14 Avista.

15 Stipulated Commitment Nos. 46 and 51 prohibit the
16 pledging of Avista utility assets and inter-company lending
17 without prior Commission approval. Stipulated Commitment No.
18 50 prohibits inter-company debt without prior notification to
19 the Commission.

20 **Q. How do the Settlement Stipulation's ring-fencing**
21 **Stipulated Commitments compare to other recent utility mergers**
22 **and acquisitions?**

1 A. The Settlement Stipulation's ring-fencing Stipulated
 2 Commitments compare very favorably with the ring-fencing
 3 commitments made in other IOU transactions effectuated since
 4 2010. Exh. No. 13, Schedule 3 provides a summary of the ring-
 5 fencing conditions in these 40 recent transactions. As shown
 6 in that exhibit, the ring-fencing Stipulated Commitments made
 7 by the Parties are rarely offered or required. As shown in
 8 that exhibit, only one of the transactions I reviewed included
 9 all of the ring-fencing commitments in the Settlement
 10 Stipulation. In fact, most transactions included none or very
 11 few of the ring-fencing Stipulated Commitments. These ring-
 12 fencing Stipulated Commitments, in combination with the
 13 governance Stipulated Commitments made by the Parties, provide
 14 a very strong degree of separation of Avista from Hydro One
 15 post-merger. The efficacy of this separation and insulation
 16 is unaffected by the recent developments in the Province.

17
 18 **V. THE SETTLEMENT STIPULATION'S FINANCIAL INTEGRITY**
 19 **COMMITMENTS**

20 **Q. Please briefly highlight the Settlement**
 21 **Stipulation's financial integrity Stipulated Commitments.**

22 A. Financial integrity Stipulated Commitment Nos. 34
 23 through 41 work together to ensure that Avista's financial
 24 integrity, including its access to capital and ability to make

1 the investments necessary to continue to provide its customers
2 with safe and reliable service, will be maintained post-
3 merger. Stipulated Commitment No. 34 addresses Avista's post-
4 closing access to capital, committing Hydro One to providing
5 Avista with equity to support Avista's capital structure and
6 allow it to access debt financing on reasonable terms and on a
7 sustainable basis. Avista will also maintain separate debt
8 and preferred stock (Stipulated Commitment No. 35). Hydro One
9 and Avista will use reasonable best efforts to ensure that
10 Avista's debt will continue to be separately rated by at least
11 one nationally recognized ratings agency (Stipulated
12 Commitment No. 36) and will notify the Commission of any
13 downgrade of Avista's credit rating to non-investment grade
14 status (Stipulated Commitment No. 37).

15 Stipulated Commitment No. 38 ensures that dividends paid
16 by Avista to Hydro One cannot be financially detrimental to
17 Avista. If Avista does not have an investment-grade credit
18 rating and the ratio of earnings before interest, taxes,
19 depreciation and amortization ("EBITDA") to Avista's interest
20 expense is less than 3.0, then no dividend distribution to
21 Olympus Equity LLC will occur.

22 Finally, Hydro One will not seek to change Avista's
23 pension funding policy and Avista will maintain this policy in

1 accordance with sound actuarial practice (Stipulated
2 Commitment 39), and Avista will continue to file reports with
3 the Securities Exchange Commission (Stipulated Commitment No.
4 40) and comply with the Sarbanes-Oxley Act (Stipulated
5 Commitment No. 41).

6 **Q. Are there any other Stipulated Commitments which**
7 **support the financial integrity commitments that you would**
8 **like to highlight?**

9 A. Yes. In addition to the ring-fencing Stipulated
10 Commitments which insulate Avista and its customers from Hydro
11 One, a number of other regulatory Stipulated Commitments were
12 made in the Settlement Stipulation that provide additional
13 protections from potential financial risks. Avista will not
14 advocate for a higher cost of debt or equity capital as
15 compared to what Avista's cost of debt or equity capital would
16 have been absent Hydro One's ownership (Stipulated Commitment
17 No. 25). In addition, Avista's actual common equity ratio
18 will be maintained at a level no less than 44% (Stipulated
19 Commitment No. 26). Finally, as I noted earlier in my
20 testimony, Avista will hold Avista customers harmless from any
21 business and financial risk exposures associated with Olympus
22 Holding Corp., Hydro One, and Hydro One's other affiliates
23 (Stipulated Commitment No. 47).

1 **Q. How do the Settlement Stipulation's financial**
2 **integrity Stipulated Commitments compare to other recent**
3 **utility mergers and acquisitions?**

4 A. The Settlement Stipulation's financial integrity
5 Stipulated Commitments compare favorably with financial
6 integrity commitments made in other IOU transactions
7 effectuated since 2010. Exh. No. 13, Schedule 4 provides a
8 summary of the financial integrity conditions in these 40
9 recent transactions. As shown in that exhibit, none of the
10 transactions I reviewed included all of the financial
11 integrity commitments in the Settlement Stipulation. In fact,
12 most transactions included only a few of the financial
13 integrity Stipulated Commitments. These financial integrity
14 Stipulated Commitments, in combination with the governance and
15 ring-fencing Stipulated Commitments made by the Parties,
16 provide for the continued prudent financial management of
17 Avista and ensure that Avista's financial management cannot be
18 harmed by Hydro One ownership.

19 **Q. Do the recent political developments in the Province**
20 **and changes in governance at Hydro One have any impact on the**
21 **Settlement Stipulation's financial integrity Stipulated**
22 **Commitments?**

1 A. No. The financial integrity Stipulated Commitments
2 agreed to by the Parties provide Avista and its Idaho
3 customers with appropriate assurances, independence and
4 protections. These Stipulated Commitments insulate Avista and
5 its Idaho customers from Hydro One and anything the Province
6 may do in its role as an investor in Hydro One. As I
7 discussed earlier, the dividend restrictions and commitment
8 that Hydro One will provide equity to Avista to support
9 Avista's capital structure agreed to by the Parties to the
10 Settlement Stipulation ensure that Avista cannot be stripped
11 of its capital (Stipulated Commitment 38).

12 Recent events have not created any need for modifications
13 to these Stipulated Commitments. Any recent or future changes
14 at Hydro One or in the Province have no impact on the facts
15 that the Stipulated Commitments are binding (Stipulated
16 Commitment No. 33) and the Commission has the authority to
17 enforce them (Stipulated Commitment No. 30).

18 **Q. Are the financial integrity Stipulated Commitments**
19 **included in the Settlement Stipulation appropriate for the**
20 **Proposed Transaction?**

21 A. Yes. Taken as a whole, and in combination with the
22 other Stipulated Commitments and the Commission's on-going
23 regulatory oversight and authority, the financial integrity

1 Stipulated Commitments provide customers with appropriate
2 assurances that they will continue to enjoy safe and reliable
3 electric service at rates that reflect their Commission-
4 approved cost of service.

5

6

VI. CONCLUSIONS

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Q. Do the recent developments at the Province and Hydro One have any impact on the public interest in Idaho?

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A. No, these developments do not affect the public interest. For all the reasons described above, the Stipulated Commitments are fully protective of the public interest in Idaho, as well as the interests of Avista's Idaho customers.

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Q. If the Province took action in the future to exercise influence over or control of the Board of Hydro One, would that negatively impact Avista and its customers or the public interest in Idaho?

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A. No. The governance, bankruptcy and financial ring-fencing and other Stipulated Commitments, coupled with the Commission's on-going regulatory oversight of Avista and the laws of the United States in the five states in which Avista operates (Idaho, Oregon, Washington, Montana, and Alaska) put parameters around how Avista will be owned and operated post-merger. As I discussed earlier, the Stipulated Commitments

1 are binding regardless of any actions the Province might take
2 in the future. The Province has no ability to directly
3 influence Avista. The Province cannot pass laws that apply to
4 Avista. Further, even in the speculative scenario where the
5 Province took control of Hydro One and directed the two Hydro
6 One executives on Avista's post-merger board to pursue
7 initiatives that would benefit Hydro One and/or Ontario to the
8 detriment of Avista's financial resources or service, the
9 remaining seven independent or Avista-designated directors on
10 Avista's post-merger board could override that direction.

11 **Q. Are the Stipulated Commitments included in the**
12 **Settlement Stipulation appropriate for the Proposed**
13 **Transaction?**

14 A. Yes. The Stipulated Commitments are robust and
15 ensure, as intended, that recent developments at Hydro One and
16 the Province, as well as potential future changes, can have no
17 adverse effect on Idaho customers or on the interest of the
18 public in Idaho. Nothing in the recent developments even
19 suggests that Avista's financial management, access to
20 capital, cost of capital, quality of service, rates, or Hydro
21 One's attention to Avista's needs will be adversely affected.
22 The Settlement Stipulation provides a comprehensive set of
23 Stipulated Commitments that collectively ensure the

1 appropriate level of separation between Avista and Hydro One
2 and Hydro One's other affiliates. The package of Stipulated
3 Commitments exceeds industry norms established by the 40
4 utility transactions completed since 2010 that I reviewed.
5 These Stipulated Commitments insulate Avista, protect its
6 customers from potential risks, and support the public
7 interest. In combination with the Commission's on-going
8 regulatory oversight and authority, the Stipulated Commitments
9 ensure that stakeholders will experience the benefits from the
10 Proposed Transaction, will be insulated from potential risks,
11 and will continue to ensure safe and reliable service at rates
12 that reflect their Commission-approved cost of service.

13 **Q. Does this conclude your testimony?**

14 A. Yes, it does.