

**BEFORE THE WASHINGTON  
UTILITIES AND TRANSPORTATION COMMISSION**

**In the Matter of the Joint Application of  
HYDRO ONE LIMITED (acting through its  
indirect subsidiary, Olympus Equity LLC)**

**and**

**AVISTA CORPORATION**

**For an Order Authorizing Proposed  
Transaction**

Docket No. U-170970\_\_\_\_\_

**PETITION OF HYDRO ONE AND  
AVISTA FOR RECONSIDERATION  
AND FOR REHEARING**

**TABLE OF CONTENTS**

**I. INTRODUCTION..... 1**

**II. PETITION FOR RECONSIDERATION..... 3**

    A. The Commission misapprehended political risks because it failed to consider and identify any specific Provincial actions that could actually impact Avista, and therefore, erroneously failed to take into account the commitments agreed to by all parties to this Docket that protect Avista from any influence by the Province. ....4

        1. The governance, financial integrity, and ring-fencing commitments fully protect Avista from any Provincial influence. ....7

        2. The Revised Stipulated Commitments protect Avista customers. ....14

        3. In addition to the Revised Stipulated Commitments, the Governance Agreement provides additional protections to Avista from Provincial influence. ....16

    B. Order 07 failed to properly evaluate and thus undervalued the proposed benefits to Avista customers, and made flawed assumptions about the availability of retained earnings at the Avista level to fund the rate credits and other financial commitments. ....20

    C. The Commission undervalued the benefits to Avista’s customers because it failed to recognize benefits provided by the commitments. ....25

        1. The financial benefits of the Proposed Transaction are not designed to address the potential risks posed by the Province and, by considering the financial benefits in that context, the Commission undervalued them. ....26

        2. The full settlement of all issues, joined in by all parties, was carefully crafted to mitigate risks and provide real, tangible net benefits. ....26

    D. Order 07 is beyond the Commission’s jurisdiction, and unsupported by evidence because it is based upon perceived harms to the shareholders of an Ontario corporation and whether the Hydro One Board and executive leadership acted in the best interests of Hydro One’s stakeholders. ....28

**III. PETITION FOR REHEARING ..... 31**

**IV. CONCLUSION..... 33**

## I. INTRODUCTION

1. Pursuant to RCW 34.05.470 and WAC 480-07-850, Hydro One Limited (“Hydro One”) and Avista Corporation (“Avista”) respectfully request that the Washington Utilities and Transportation Commission (“Commission”) reconsider Order 07 entered on December 5, 2018, in this proceeding (“Order 07”). Order 07 should be reconsidered for the following reasons:

- Order 07 misapprehended the political risks that the Province of Ontario’s (“Province”) ownership stake in Hydro One poses to Avista and its customers because the Commission failed to identify with any specificity how Provincial actions could actually impact Avista. The Commission failed to meaningfully take into account the commitments agreed to by all parties to this proceeding that protect Avista from any influence by the Province.
- Order 07 understated the value of the transaction’s benefits to ratepayers because the Commission made incorrect assumptions unsupported by substantial evidence to conclude that customers could receive the rate credits and other financial commitments regardless of the merger.
- Order 07 based its conclusions about possible Provincial interference with Avista upon perceived harms to Hydro One shareholders.
- Correction of the above-noted errors leads to the conclusion that the transaction is in the public interest, provides net benefits to customers, and should be approved and supported by the Commission.

2. This Petition is intended to ensure that, to the extent required by RCW 34.05.534 and RCW 34.05.554, Hydro One and Avista have fully exhausted all administrative remedies and brought new issues arising from Order 07 to this Commission. Hydro One and Avista also request that the Commission rehear Order 07 under WAC 480-07-870 to accept additional evidence proffered with this Petition as follows:

- (i) the Declaration of Kari L. Vander Stoep, which includes, as Exhibit A, a copy of a letter from the Office of the Deputy Minister of Energy of the Province of Ontario, dated

November 29, 2018, in which the Province “reiterate[s] the Ministry’s commitment to supporting Hydro One in its efforts to complete the Avista acquisition,”;

(ii) testimony to be provided by Hydro One’s new President and Chief Executive Officer (“CEO”) following the CEO’s appointment; and

(iii) additional conditions related to future actions by the Province (if the Commission determines the additional conditions constitute additional evidence<sup>1</sup>).

3. Good and sufficient cause exists to grant this Petition because Order 07 raises additional concerns regarding (1) potential Provincial influence on Hydro One and Avista,<sup>2</sup> (2) the inability of the Commission to hear from Hydro One’s new CEO in October,<sup>3</sup> and (3) Provincial support for the Proposed Transaction.<sup>4</sup> *See* WAC 480-07-870(1) (establishing criteria for petitions for rehearing). Further, the additional evidence is available due to changed conditions since the Commission entered Order 07, *see id.*, and directly addresses the Commission’s concerns.

4. In the event that the Commission determines that rehearing on Order 07 is necessary to consider the proposed additional conditions and the letter from the Province, or to take additional testimony from Hydro One’s new CEO, Hydro One and Avista request expedited proceedings to address these limited issues. Due to the March 29, 2019 closing deadline in the merger agreement and the expiration of Hydro One’s funding for the transaction shortly thereafter, Hydro One and Avista request that any additional process conclude by the end of January 2019. Hydro One and

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<sup>1</sup> Hydro One and Avista believe the new conditions do not constitute additional evidence, are supported by the current record, and the Commission, without rehearing Order 07, can approve the Joint Application by conditioning its approval on these additional conditions. Hydro One and Avista also recognize, however, that if the Commission so chooses, it can rehear Order 07 to consider the new conditions as additional evidence.

<sup>2</sup> *See, e.g.*, Order 07 at ¶ 90.

<sup>3</sup> Order 07 at ¶¶ 43-44, 65.

<sup>4</sup> Order at ¶ 46, n.51; *id.* at ¶ 79.

Avista will do everything possible to assist with an expedited schedule if the Commission is inclined to rehear Order 07 for the limited purposes described.

5. In summary, the Commission denied the Joint Application on two alternative grounds: (1) the political risks posed by the Province's ownership of 47% of Hydro One's stock makes the acquisition of Avista inconsistent with the public interest; and (2) the benefits to customers included in the Joint Application and the Revised Settlement Stipulation do not amount to net benefits.<sup>5</sup> Hydro One and Avista respectfully submit that the Commission erred on both grounds, and therefore, should grant the petition for reconsideration and rehearing and grant the Joint Application.

## II. PETITION FOR RECONSIDERATION

6. Order 07 lists multiple concerns regarding the Province's ability to harm Avista and Washington customers and ultimately concludes that these are "unavoidable risks" that cannot be mitigated. Hydro One and Avista ask the Commission to reconsider the extensiveness and effectiveness of the 82 Revised Stipulated Commitments, and how the relevant commitments in will protect against the risks the Commission identified. Hydro One and Avista respectfully submit that the Commission committed legal error because its assessment of the potential risk posited generalized fears of potential Provincial political interference without meaningfully examining all of the state-of-the-art ring fencing commitments. In our judgment, had the Commission examined those commitments on their explicit terms, it would have concluded that there is no significant, non-mitigated risk and that the transaction provides sufficient net benefits. Hydro One and Avista

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<sup>5</sup> Order 07 at p. II, IV; *id.* at ¶ 15.

therefore request that the Commission consider these commitments and the details outlined below, and grant the request for reconsideration.

**A. The Commission misapprehended political risks because it failed to consider and identify any specific Provincial actions that could actually impact Avista, and therefore, erroneously failed to take into account the commitments agreed to by all parties to this Docket that protect Avista from any influence by the Province.**

7. In Order 07, the Commission states repeatedly that the Province’s interference with the governance and management of Hydro One after the June 7, 2018 Ontario election (the “June 2018 Ontario Election”) indicates that the Province can cause harm to Avista and its customers if Avista becomes a subsidiary of Hydro One.<sup>6</sup> The Commission, however, never identifies a specific way in which the Province could actually reach through the corporate structure and the state-of-the-art ring fencing commitments to impact Avista and its customers. Nor does it enter sufficient findings of fact in that regard; instead, it offers only conclusory statements unsupported by the evidence.<sup>7</sup> In fact, the Commission stated that it did not even need to consider the details of the all-party, all-issue Revised Settlement Stipulation—renegotiated and updated after the June 2018 Ontario election—to conclude that the Province’s actions with respect to Hydro One’s Board and CEO

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<sup>6</sup> Order 07 at ¶¶ 13-14, 78.

<sup>7</sup> Order 07 at pp. III-IV (“The events following the provincial election in June 2018 demonstrate the material and significant risk of the proposed transaction to Avista’s customers that results from the Province of Ontario’s dominant ownership interest in Hydro One and the willingness of the provincial government to exert its dominance in ways that are contrary to the best interest of Hydro One and, by extension, Avista, were it to be owned by Hydro One.”); *id.* at ¶ 14 (“The unavoidable risks of the proposed transaction associated with the province’s evident intent and ability to participate directly in the direction and management of Hydro One in ways that are harmful to the enterprise, which would include Avista, are significant.”); *id.* at ¶ 46 (“Considering events that already have transpired, we cannot trust that the province will not take additional actions without regard to the harmful consequences they may have for Hydro One and Avista. This would be a continuing risk that no provision in a settlement agreement between Hydro One and Avista can adequately protect against.”); *id.* at ¶ 79 (“We simply have no assurances that the province will not, using legislative or other powers, exert its control over Hydro One in ways that undercut one or more of the Settlement Stipulation commitments or otherwise cause harm to Avista.”).

inevitably mean that Avista will face too much risk as a Hydro One subsidiary.<sup>8</sup> The Commission erred in its failure to identify and articulate actual risks to Avista and its customers, and by failing to consider, once the actual risks were identified, whether the commitments contained in the Revised Settlement Stipulation protect against such risks.

8. An example of this failure in the Commission’s analysis is found in footnote 15 of the decision:<sup>9</sup>

Looking into the future, it is easy enough to imagine that actions by the province that strain Hydro One’s revenue could result in pressure being brought to bear on Avista, whose directors would have a fiduciary duty to their shareholder (*i.e.*, Hydro One) to limit expenditures so as to maximize the retained earnings available to dividend up to Hydro One.

9. As explained in more detail below, this ill-defined risk to Avista’s financial health is speculative, and is otherwise addressed by several of the Revised Stipulated Commitments<sup>10</sup> in the all-party, all-issue Revised Settlement Stipulation: (1) Revised Stipulated Commitment No. 26, requiring Hydro One to maintain Avista’s actual common equity ratio at 44 percent, (2) Revised Stipulated Commitment No. 34, requiring Hydro One to provide equity support to Avista’s capital structure, (3) Revised Stipulated Commitment No. 37, requiring Hydro One and Avista to notify the Commission of any downgrade of Avista’s credit rating to non-investment grade status, (4) Revised Stipulated Commitment No. 38, restricting Avista’s ability to provide dividends to Hydro One, (5) Revised Stipulated Commitment No. 46, prohibiting the loan or

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<sup>8</sup> Order 07 at ¶ 45 (“We agree with the parties that the Settlement commitments collectively present state of the art ring fencing and other provisions that, to the extent they are allowed to function as written, would provide significant protections to Avista with respect to the specific subject matters they cover. ... Point-by-point mitigation of individual risks, however, is neither the first, nor the only, relevant level of analysis given the facts of this case.”); *id.* at ¶ 46 (“We find no particular need to discuss the individual Settlement commitments because the evidence in this proceeding undermines our ability to trust that the provincial government in Ontario will not interfere in the business of Hydro One in ways that undercut these commitments.”); *see also id.* at ¶ 80.

<sup>9</sup> Order 07 at ¶ 13 n.15.

<sup>10</sup> *See* U-170970, Revised Appendix A to Settlement Stipulation, Exh. JNT-3 (Oct. 19, 2018) (each, a “Revised Stipulated Commitment,” collectively, the “Revised Stipulated Commitments”).

pledge of Avista's utility assets to Hydro One, (6) Revised Stipulated Commitment Nos. 50 and 51, requiring Commission approval for inter-company debt transactions or lending between Avista and Hydro One, (7) Revised Stipulated Commitment No. 33, establishing that the commitments are fully binding upon Hydro One and its subsidiaries, (8) Revised Stipulated Commitment No. 30, establishing the Commission's ongoing jurisdiction to enforce the commitments, and (9) Revised Stipulated Commitment No. 31, submitting Hydro One and its subsidiaries to the jurisdiction of Washington's court for enforcement of the commitments.

10. Hydro One's operation of Avista will be constrained by the Revised Stipulated Commitments and the laws of the United States and the five states in which Avista operates (Washington, Oregon, Idaho, Montana, and Alaska). Each of these commitments are enforceable by the various commissions and by the courts of the various states – and Hydro One has willingly submitted to the jurisdiction of the commissions and courts for that purpose.<sup>11</sup> The Revised Stipulated Commitments dealing with governance, financial integrity, and ring-fencing fully protect Avista from any Provincial influence and these, together with the rest of the Revised Stipulated Commitments, are legally binding on Hydro One and Avista. As a result, Avista customers are protected from any consequences of Provincial influence. The Revised Stipulated Commitments mitigate Order 07's perceived political risks associated with the merger (the “merger” or “Proposed Transaction”). Indeed, there are more protections for Avista's Washington customers against outside political interference from the Province than there are, at present, for the ramifications of political actions taken by states where Avista operates.

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<sup>11</sup> Revised Stipulated Commitment Nos. 20, 30, 31, 33.



**1. The governance, financial integrity, and ring-fencing commitments fully protect Avista from any Provincial influence.**

11. In Order 07, the Commission declined to discuss the 82 Revised Stipulated Commitments in any level of detail and instead considered the Proposed Transaction only at a high level.<sup>12</sup>

We find no particular need to discuss the individual Settlement commitments because the evidence in this proceeding undermines our ability to trust that the provincial government in Ontario will not interfere in the business of Hydro One in ways that undercut these commitments.<sup>13</sup>

12. By foregoing a meaningful discussion of the Revised Stipulated Commitments—which do, in fact, adequately address and mitigate the risks raised by the Commission—the Commission showed an unwillingness to examine how each of the safeguards built into the Settlement Stipulation and Revised Stipulated Commitments (agreed to by all parties) would protect Avista’s customers from any potential interference by the Province. Without addressing the Revised Stipulated Commitments, the Commission concluded that “[t]he protective provisions in the Settlement Stipulation unfortunately do not, and cannot, protect Avista from harm that might follow from actions that the [P]rovince may take with respect to Hydro One.”<sup>14</sup> The Commission did not provide any evidence to support this conclusory statement. In a similar vein, the Commission made the sweeping (and inaccurate) statement that “[t]here is nothing to prevent legislation in Ontario that might undercut by indirect means Avista’s ability to provide its customers or the broader community one or more of the benefits promised by the Settlement

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<sup>12</sup> Order 07 at ¶¶ 45-46.

<sup>13</sup> Order 07 at ¶ 46.

<sup>14</sup> Order 07 at ¶ 80.

Stipulation.”<sup>15</sup> We respectfully submit that there is nothing in Order 07 that explains how this could actually occur. As outlined in more detail below, the Revised Stipulated Commitments agreed to by all of the parties in this proceeding protect Avista’s independence and fully protect Avista from any Provincial influence.

a) *The governance commitments insulate Avista’s board of directors from any Provincial influence.*

13. As a matter of corporate law, structure and governance, Avista operates under the supervision of its board of directors (the “Avista Board”). Any Provincial “influence” on Avista must flow through the post-merger Avista Board. But under Revised Stipulated Commitment Nos. 2 and 3, and the revised Delegation of Authority, the Province lacks the ability to exert direct or indirect pressure on the Avista Board.

14. Under Revised Stipulated Commitment No. 3, the Avista Board will consist of five Hydro One designees, three of whom must be independent directors who reside in the Pacific Northwest. This means only two of the nine members of the post-merger Avista Board can be executives of Hydro One or any of its subsidiaries. The other three Hydro One designees must be independent of Hydro One, Avista, and Hydro One’s other affiliates, and be residents of the Pacific Northwest. The Province has no role in selecting Hydro One’s designees on Avista’s Board.<sup>16</sup>

15. Further, per Revised Stipulated Commitment No. 3, of the four Avista designees, three initially will be from Avista’s pre-merger board, including the Chairman of Avista’s pre-merger

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<sup>15</sup> Order 07 at ¶ 81. This is inaccurate for a host of reasons. For example, the restrictions on Avista’s capital structure (Revised Stipulated Commitment No. 26), credit ratings (Revised Stipulated Commitment No. 36) and upward dividends (Revised Stipulated Commitment No. 38) ensure that Avista will retain earnings as need be to meet customer needs and otherwise support compliance with the commitments. Thus they help prevent Ontario legislation from undercutting the benefits of the merger. As another example, the \$7 million charitable contribution is due at or promptly following closing (Revised Stipulated Commitment No. 64), which ensures this benefit will be provided.

<sup>16</sup> See Revised Stipulated Commitment No. 3 and § 2.1.3 of the Governance Agreement (Exh. MMS-5). The Province may appoint 40% of Hydro One’s Board, but as an investor and not a manager, it has no authority to appoint board members of any of Hydro One’s subsidiaries.

board, and the fourth will be Avista's CEO. Two of Avista's designees will be independent. If any Avista designee resigns, retires, or otherwise ceases to serve as a director of Avista, then the remaining Avista designees will have the sole right to replace the departing Avista designee, *not* Hydro One. *See* Revised Stipulated Commitment No. 3.

16. Presuming that one of the two Hydro One executives on the post-merger Avista Board might be directed by the Hydro One Board or pressured by the Province to bring to the post-merger Avista Board an initiative that would benefit Hydro One and/or Ontario but diminish Avista's financial resources and service, Revised Stipulated Commitment No. 3 ensures that the seven remaining members of the post-merger Avista Board, all of whom will not be executives of Hydro One, would have sufficient votes to reject that initiative. Overall, Revised Stipulated Commitment No. 3 ensures the post-merger Avista Board will be independent and free from any improper influence from the Hydro One Board or the Province. Hydro One and Avista recently announced who will serve as the independent directors on the post-merger Avista Board. These individuals are well-known residents of the Pacific Northwest whose independence and integrity cannot be doubted.<sup>17</sup>

17. In addition, the revised Delegation of Authority, agreed to by all parties, provides an important and final barrier for the Avista Board against any Provincial influence.<sup>18</sup> The revised Delegation of Authority is designed to protect the independence of the Avista Board in the event that the Province takes some action in the future to attempt to control a majority of the Hydro One Board. If that event occurs, the amendment to the Delegation of Authority is triggered and blocks

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<sup>17</sup> The Commission rejected Hydro One and Avista's motion to reopen the record to admit as a bench exhibit a copy of a News Release dated November 7, 2018, identifying five out of the nine post-merger Avista Board members *see* Docket U-170970, Order 06 (Dec. 5, 2018), but on rehearing, the record would benefit by submittal of evidence surrounding the newly-named directors of the new Avista board, including their biographies and connections with the Pacific Northwest.

<sup>18</sup> *See* U-170970, Revised Appendix 5 to Joint Application (Delegation of Authority) (Oct. 19, 2018).

Hydro One's limited, interim right to replace any of its three Independent Director designees on the Avista Board with a Hydro One executive or employee. Avista's board, of course, has a duty to comply with its legal obligations under the commitments.

18. Under Revised Stipulated Commitment No. 2, the Avista Board retains full and unfettered authority to select and set the compensation for Avista's CEO and senior officers. *See* Revised Stipulated Commitment No. 2. Any concern that the Province could somehow direct the Hydro One CEO to bypass the Avista Board and apply influence directly on Avista's CEO is unfounded.

19. In Order 07, the Commission concluded that the "[P]rovince can interfere with Hydro One's affairs in ways that could undercut commitments set out in the merger agreement and Settlement Stipulation that will harm Avista."<sup>19</sup> As explained above, Hydro One and Avista respectfully submit that this finding was made in error. Nonetheless, to address this concern, Hydro One and Avista offer an additional commitment and request that the Commission reverse Order 07 on reconsideration and include the following new condition in its approval of the Proposed Transaction:<sup>20</sup>

\_\_\_ **No Substantial Provincial Influence**

- a. Hydro One and Avista will advise each member of the Avista Board of Directors prior to being seated post Proposed Transaction and annually thereafter that the Province may not attempt to, directly or indirectly, acquire the power to exercise any substantial influence over the policies and actions of Avista. Hydro One and Avista will require each of their respective director designees to execute a new affidavit filed annually on June 1 of each year with the Commission that attests that the individual director will notify the Commission immediately if they have any reason to believe that the Province is directly or indirectly seeking to exercise or is

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<sup>19</sup> Order 07 at ¶ 90.

<sup>20</sup> As noted in the introduction and in the petition for rehearing below, Hydro One and Avista believe the conditions do not constitute additional evidence, are supported by the current record, and the Commission, without rehearing Order 07, can approve the Joint Application by conditioning its approval on these additional conditions. Hydro One and Avista also recognize, however, that if the Commission so chooses, it can rehear Order 07 to consider the conditions as additional evidence.

exercising any substantial influence over the policies and actions of Avista through the Avista Board or otherwise.

- b. If a member of the Avista Board of Directors provides notice to the Commission pursuant to subparagraph a of this Commitment, the Commission may initiate a proceeding to determine whether the Commission should amend its final order in this docket, including reopening and strengthening of any of the Stipulated Commitments (inclusive of the financial ring-fencing commitments and/or the governance commitments), or requiring the addition of a new commitment to address the Province's attempt to, directly or indirectly, exercise substantial influence over the policies and actions of Avista, and neither Hydro One, nor any of its subsidiaries, including Avista, will oppose the Commission's authority to proceed as outlined in this Commitment.
- c. Hydro One's authority to replace an Independent Director on the Avista Board with an employee or executive on an interim six-month basis is suspended for the pendency of any proceeding initiated pursuant to subparagraph b of this Commitment.

20. With this additional condition included in an order approving the Proposed Transaction, the Commission can rest assured that the post-merger Avista Board will guard against Provincial influence over Avista and will immediately report to the Commission any attempts by the Province to exercise such influence. This additional condition as part of an order approving the Proposed Transaction will give the Commission the information it needs to protect Avista customers and will serve as a deterrent to any activities by the Province that might undercut the Revised Settlement Commitments or otherwise harm Avista customers.

*b) The financial integrity commitments ensure the Province cannot deny Avista its capital and assets.*

21. The Revised Stipulated Commitments protect Avista's assets and capital from any Provincial influence. For example, Revised Stipulated Commitment No. 34 requires Hydro One to provide "equity to support Avista's capital structure that is designed to allow Avista access to debt financing under reasonable terms and on a sustainable basis." This commitment requires

Hydro One to provide Avista with enough equity so that Avista can access debt on reasonable terms. Therefore, the Province cannot deprive Avista of its capital and assets for the benefit of the Province.

22. Revised Stipulated Commitment No. 38 prohibits Avista from issuing dividends under certain circumstances to protect Avista's financial health and its customers. Basically, this operates to keep retained earnings at the Avista level where they will improve Avista's financial strength. This too prevents the Province from depriving Avista of its capital and assets for the benefit of the Province.

23. As recognized in the supplemental testimony of Commission Staff, these and other financial integrity commitments appropriately and sufficiently protect Avista:

The Financial Integrity Commitments ensure that earnings cannot flow upward to the parent company (i.e., the shareholder) unless Avista remains financially healthy, as demonstrated by a number of objective measures. The Ring-Fencing commitments ensure that Avista is shielded from financial risks of the parent company, including bankruptcy, and prohibit Avista from making loans to the parent or pledging assets to the parent.<sup>21</sup>

24. Moreover, Staff witness McGuire was asked during the October hearings whether he still believed that adequate protections safeguard against Provincial interference:.

CHAIRMAN DANNER: So, Mr. McGuire, my question to you, then, is Commitment 82 just belts [sic] and suspenders, are you satisfied with 1 through 81 as being sufficient?

MR. MCGUIRE: Yes, I was satisfied with those commitments as being sufficient ...<sup>22</sup>

25. The Revised Stipulated Commitments also protect Avista's assets from any possible misuse by the Province. Revised Stipulated Commitment No. 46 prohibits Avista from loaning or

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<sup>21</sup> Exh. CRM-1T at 10.

<sup>22</sup> *In the Matter of Hydro One and Avista Corporation*, Docket U-170970, October 23, 2018 Hearing Transcript at 501, line 22, through 502, line 2 ("October Hearing Transcript").

pledging utility assets to Hydro One, Olympus Holding Corp., or any of their subsidiaries or affiliates without Commission approval. Revised Stipulated Commitment No. 46 also states “Avista’s assets will not be pledged by Avista or any of its affiliates, including Hydro One and Olympus Holding Corp. and any of their subsidiaries or affiliates, for the benefit of any entity other than Avista.” This commitment ensures that Avista’s utility assets are used only for the benefit of Avista’s ratepayers and Avista’s financial health. Therefore, the Province cannot strip Avista of its capital and assets for the benefit of the Province.

26. The Revised Stipulated Commitments ensure that the Province cannot obtain Avista’s capital and assets through a bankruptcy proceeding unless that would be in the best interests of Avista’s customers. Avista will issue a single share of preferred stock referred to as the Golden Share to an independent third party. The vote of this share will be required to place Avista into voluntary bankruptcy. *See* Revised Stipulated Commitment No. 42. Further, Avista’s entry into voluntary bankruptcy would require the consent of a two-thirds majority of all of its directors, including the affirmative vote of an independent director at Avista. *See* Revised Stipulated Commitment No. 43. Hydro One and Avista must also provide a non-consolidation opinion to confirm the effectiveness of the ring-fencing measures to prevent the substantive consolidation of the assets and liabilities of Avista with those of the entities above it in the corporate chain of ownership. *See* Revised Stipulated Commitment No. 44. The corporate structure also includes Olympus Equity LLC, a bankruptcy-remote special purpose entity that will have no debt. *See* Revised Stipulated Commitment No. 45. The Revised Stipulated Commitments protect Avista from being drawn into bankruptcy proceedings that are not in the best interest of Avista or its customers.

**2. The Revised Stipulated Commitments protect Avista customers.**

27. The Revised Stipulated Commitments protect Avista customers from any harm as a result of the Proposed Transaction or any business or financial risks associated with Hydro One. The Commission alleges that the benefits from the Proposed Transaction are “inadequate to compensate for the risks of harm Avista’s customers would face were we to approve this transaction.”<sup>23</sup> But here again, the Commission fails to appreciate Revised Stipulated Commitment No. 47(a), which provides, “Avista customers will be held harmless from any business and financial risk-exposures associated with Olympus Holding Corp., Hydro One, and Hydro One’s other affiliates.”

28. Moreover, Avista customers are protected from any higher cost of debt or equity capital as a result of the Proposed Transaction or Hydro One’s future actions. Revised Stipulated Commitment No. 25 provides, “Avista will not advocate for a higher cost of debt or equity capital as compared to what Avista’s cost of debt or equity capital would have been absent Hydro One’s ownership.” If there are increases to Avista’s cost of debt or equity capital, Avista bears the burden to prove that the increase is unrelated to the financial risks or other characteristics of the Proposed Transaction. This commitment is indefinite and serves to mitigate the concern that Washington ratepayers could experience a rate increase resulting from increases to the cost of debt or equity capital as a result of the Proposed Transaction and future actions by Hydro One or the Province. The Revised Stipulated Commitments are binding on Hydro One and Avista.

29. Hydro One is legally obligated to honor and abide by its obligations under the Revised Stipulated Commitments, and there is nothing the Province can do to nullify the legally binding nature of Revised Stipulated Commitments -- they are enforceable by this Commission and the

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<sup>23</sup> Order 07 at page IV.



courts of this state. While the Commission asserts that “[t]here is nothing to prevent the [P]rovince from passing legislation that will prevent Hydro One from living up to one or more of the protective commitments in the Settlement Stipulation,”<sup>24</sup> But Revised Settlement Commitment Nos. 30, 31, and 33 legally require Hydro One and Avista to satisfy their obligations under the Revised Stipulated Commitments and give the Commission and Washington courts the jurisdiction to enforce these commitments against Hydro One, regardless of any Provincial action. Hydro One and Avista are unaware of any Provincial authority that can be used to abrogate or modify the relevant commitments. And, even if the Province tried to do so, recourse does not require this Commission to take action against the Province for any failure of Hydro One to abide by the Revised Stipulated Commitments – only against Hydro One. And the Commission may do so in the courts of this State (to whose jurisdiction Hydro One has willingly submitted).

30. Revised Stipulated Commitment No. 33 demonstrates that Hydro One and Avista accept and understand that it is their legal responsibility to implement the Revised Stipulated Commitments: “Hydro One, its subsidiaries in the post-close corporate structure between Hydro One and Avista (as those companies in between may change over time) and Avista, acknowledge that the commitments being made by them are fully binding upon them and their successors in interest and upon their affiliates where specifically noted.”

31. Revised Stipulated Commitment No. 30 grants the Commission the authority “to enforce these commitments in accordance with their terms.” Hydro One and Avista agree to the Commission’s administrative authority to enforce the Revised Stipulated Commitments.

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<sup>24</sup> Order 07 at ¶ 81; *see also id.* (“Were such legislation to affect adversely Hydro One’s ability to provide financial protection and support to Avista, the Company’s ability to continue providing safe and reliable service to Washington customers at reasonable rates could be impaired.”).

32. Revised Stipulated Commitment No. 31 ensures that Hydro One and Avista will submit to the jurisdiction of Washington courts for enforcement of the Commission’s orders. Hydro One realizes that it would not otherwise be subject to the jurisdiction of the Commission but for its new relationship with Avista after the merger. Therefore, Hydro One will submit an affidavit affirming that it and its subsidiaries will submit to the jurisdiction of the Commission and Washington courts for the enforcement of the Revised Stipulated Commitments and subsequent orders affecting Avista. No Provincial influence or legislation can change this.

33. All of these commitments together ensure that Hydro One and Avista will “live up to” the protections enumerated in the Revised Stipulated Commitments. Hydro One and Avista are legally bound to the Revised Stipulated Commitments and subject to the jurisdiction of the Commission and Washington courts for enforcement proceedings. As a result, the Commission was in error to conclude that:

There is nothing to prevent legislation in Ontario that might undercut by indirect means Avista’s ability to provide its customers or the broader community one or more of the benefits promised by the Settlement Stipulation. There is nothing to prevent the province from passing legislation that will prevent Hydro One from living up to one or more of the protective commitments in the Settlement Stipulation.<sup>25</sup>

The Commission ignored Revised Stipulated Commitment Nos. 30, 31, and 33 when it reached these conclusions.

**3. In addition to the Revised Stipulated Commitments, the Governance Agreement provides additional protections to Avista from Provincial influence.**

34. The Commission recognizes that the Province “cannot act directly against Avista in Washington”<sup>26</sup> due to the fact that the Province does not have legislative jurisdiction to reach

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<sup>25</sup> Order 07 at ¶ 81; *see also, id.* at ¶ 84.

<sup>26</sup> Order 07 at ¶ 90.

Avista, even as the subsidiary of an Ontario corporation.<sup>27</sup> The only way in which the Province could conceivably influence Avista would be through Hydro One's Board. The Province, however, cannot give direction to Hydro One Board members. Section 4.2 of the Governance Agreement requires that Hydro One's directors, including those nominated by the Province, must be entirely independent of the Province and Hydro One.<sup>28</sup>

35. The Governance Agreement also protects Hydro One from Provincial influence by providing in Section 2.1.2 that the Hydro One "Board shall be responsible for the management of or supervising the management of the business and affairs of Hydro One" and in Section 2.1.3 that the "Province shall, with respect to its ownership interest in Hydro One, engage in the business and affairs of Hydro One . . . as an investor and not as a manager" (emphasis added). In addition, Section 2.3 of the Governance Agreement specifically enumerates the matters for which the Hydro One Board is responsible and in respect of which it has full authority.

36. The Governance Agreement also prohibits the Province from initiating fundamental changes to Hydro One described in Part XIV of the *Business Corporations Act* (Ontario) ("OBCA") (e.g., amendment to articles, continuance, arrangements, and amalgamations).<sup>29</sup> The Province may vote its shares as it sees fit in the event a fundamental change is initiated by another shareholder.<sup>30</sup> The Province also cannot solicit (either on its own or acting with others) any person to exercise rights as a shareholder in a manner that the Province would be prohibited from doing directly.<sup>31</sup>

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<sup>27</sup> October Hearing Transcript at 461, line 22, through page 462, line 2..

<sup>28</sup> Exh. MMS-5, §§ 4.2.2, 4.2.3.

<sup>29</sup> *Id.* at § 2.5.

<sup>30</sup> *Id.*

<sup>31</sup> *Id.* at § 2.6.

In Order 07, the Commission concluded that the Governance Agreement was of little value in protecting Hydro One's shareholders after the June 2018 Ontario Election and is, therefore, of little value to the Commission's assessment of whether Avista would be protected from Provincial influence.<sup>32</sup> Hydro One and Avista respectfully submit that this conclusion was in error for the reasons set forth above,<sup>33</sup> but to address this concern, Hydro One and Avista request that the Commission reverse Order 07 on reconsideration and include the following condition in its order approving the Proposed Transaction:<sup>34</sup>

\_\_\_\_. **Hydro One Governance Agreement**

- a. For purposes of this Commitment, "Governance Agreement" means the agreement between Hydro One and the Province of Ontario dated as of November 5, 2015 and submitted as Exhibit MMS-5 in this docket as amended by the letter agreement dated as of July 11, 2018 and submitted as Exhibit JDS-2 in this docket.
- b. Prior to close of the Proposed Transaction, the board of directors of Hydro One (the "Board") shall adopt a resolution providing that in the event the Board, or any director thereon, is informed or becomes aware that there is a proposal or steps being considered or taken to amend, effectively modify, or eliminate the Governance Agreement, whether by legislation, mutual agreement of the parties thereto or otherwise, Hydro One will immediately notify the Commission and, to the extent feasible, will provide the Commission with information available to the Board regarding the proposal. The Board will confirm annually its obligations under this

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<sup>32</sup> Order 07 at ¶ 12.

<sup>33</sup> In Section 16 of the July 2018 Letter Agreement, "the Province ratifies and reaffirms its obligations under the Governance Agreement and agrees that, except as specifically set out in this Agreement with respect to the subject matter hereof [board removal, CEO retirement, and compensation issues], (i) the execution, delivery and effectiveness of this Agreement or any other documents delivered in connection herewith shall not amend, modify or operate as a waiver or forbearance of any right, power, obligation, remedy or provision under the Governance Agreement, and (ii) such agreement shall continue in full force and effect." See Exh. JDS-2.

<sup>34</sup> As noted in the introduction and in the petition for rehearing below, Hydro One and Avista believe the conditions do not constitute additional evidence, are supported by the current record, and the Commission, without rehearing Order 07, can approve the Joint Application by conditioning its approval on these conditions. Hydro One and Avista also recognize, however, that if the Commission so chooses, it can rehear Order 07 to consider the conditions as additional evidence.

commitment, which confirmation will be signed by the Hydro One Chair and provided to the Commission.

- c. If Hydro One provides notice to the Commission pursuant to subparagraph b. of this Commitment, the Commission may initiate a proceeding to determine whether the actions described in subsection (b.) to amend, effectively modify, or eliminate the Governance Agreement would result in the Province seeking to exercise or exercising substantial influence over the policies and actions of Avista, and if so, whether the Commission should amend its final order in this docket, including reopening and strengthening any of the Stipulated Commitments (inclusive of the financial ring-fencing commitments and/or the governance commitments), or requiring the addition of new commitments to address the Province's attempt to, directly or indirectly, exercise or exercising substantial influence over the policies and actions of Avista, and neither Hydro One nor any of its subsidiaries, including Avista, will oppose the Commission's authority to proceed as outlined in this subparagraph (c.)

With this additional condition included in an order approving the Proposed Transaction, the Commission can rest assured that the Hydro One Board will report any attempts by the Province to revise the Governance Agreement. This additional condition as part of an order approving the Proposed Transaction will give the Commission the information and authority it needs to protect Avista customers and will serve as a deterrent to any activities by the Province that might undercut the protections of the Governance Agreement to the detriment of Avista customers.

38. In addition to incorporating the condition above into the Commission's approval of the Joint Application, the Commission could bolster this protection by rehearing Order 07 to receive testimony from Hydro One's new CEO, after he or she is appointed.<sup>35</sup> Hydro One will promptly notify the Commission of the appointment of its new CEO. Upon granting this Petition for Rehearing of Order 07, Hydro One will make the newly-appointed CEO and other Hydro One

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<sup>35</sup> The Commission pointed out in several locations in Order 07 that it was being forced to make a decision before a new CEO for Hydro One has been selected. Order 07 at ¶¶ 43-44, 65.

executives with duties relating to Avista available to appear and respond under oath to any questions and concerns identified by the Commission or other parties.<sup>36</sup>

**B. Order 07 failed to properly evaluate and thus undervalued the proposed benefits to Avista customers, and made flawed assumptions about the availability of retained earnings at the Avista level to fund the rate credits and other financial commitments.**

39. The Commission's evaluation of rate credits and other monetary benefits to customers, such as the \$11 million dollars for low-income programs in Revised Stipulated Commitment Nos. 67, 69, and 70, mischaracterized the nature of retained earnings and how they would be used to fund the financial commitments. The Proposed Transaction would give a total of \$42.4 million in financial benefits to customers. Further, if the merger occurs, Hydro One will cause Avista to make a one-time contribution of \$7,000,000 to Avista's charitable foundation at or promptly following closing of the Proposed Transaction<sup>37</sup>, and for five years after the close of the Proposed Transaction, Avista will maintain a \$4,000,000 annual budget for charitable contributions (funded by both Avista and the Avista Foundation) and additionally a \$2,000,000 annual contribution will be made to Avista's charitable foundation.<sup>38</sup> (Revised Stipulated Commitment Nos. 11, 64.) In sum, rejection of the Proposed Transaction will eliminate approximately \$42.4 million in customer benefits and significant charitable contributions over a ten-year period.

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<sup>36</sup> Hydro One and Avista will also waive the statutory deadline under RCW 80.12.030(2) to the extent that deadline would bar the rehearing of Order 07 for purposes of taking such testimony.

<sup>37</sup> Revised Stipulated Commitment No. 64: Hydro One will cause Avista to make a one-time \$7,000,000 contribution to Avista's charitable foundation at or promptly following closing. (footnote omitted)

<sup>38</sup> Revised Stipulated Commitment No. 11: For five years after the close of the Proposed Transaction, Avista will maintain a \$4,000,000 annual budget for charitable contributions (funded by both Avista and the Avista Foundation) and additionally a \$2,000,000 annual contribution will be made to Avista's charitable foundation. No approval from any regulatory bodies with jurisdiction over the Commitments is required for any changes to this commitment from and after the sixth year following closing; however any such changes will continue to require a two-thirds (2/3) vote of the Avista Board. (footnote omitted)

40. The Commission also failed to recognize the non-monetary benefits provided to customers by the Proposed Transaction, such as the financial integrity commitments discussed above in Section II(A)(1)(b)—benefits and protections that do not exist today. As a result, the Commission undervalued the Proposed Transaction’s net benefits—both tangible and intangible.

41. Order 07 improperly concludes that: “Effectively, Avista ratepayers, not ‘shareholders’ or Hydro One are paying for the rate credits and other monetary benefits of the Settlement commitments.”<sup>39</sup> Hydro One and Avista respectfully submit that this statement is in error because retained earnings *are shareholder funds—not ratepayer funds*. Mr. Thies discussed the fundamentals of the “regulatory compact” with the Commission, when he was asked whether Avista ratepayers are actually funding these various commitments in the settlement stipulation at the October 23, 2018 hearing:

MR. THIES: I don’t believe so, Commissioner. I believe the — the ratepayers, the customers are — are paying Avista for a service. We’re providing electric service or natural gas service, so their funds are coming in for a service they’re receiving, and then Avista’s retaining earnings is really the shareholders’ benefits.

So in — in the regulatory compact, you know, the shareholders are allowed to earn a fair return. That return is funded by the customers, that is — that is correct, but it is a return for the shareholder. So that retained earnings and that — and that earning amount is really the shareholder dollars that either gets divided out or reinvested in the business.<sup>40</sup>

Mr. Thies also noted that shareholder dividends come out of retained earnings:

MR. THIES: Well, the — so all of our earnings go into retained earnings and then dividends come out of retained earnings. . . .

MR. THIES: So a hundred percent goes into the retained earnings and then the dividend comes out of retained earnings.<sup>41</sup>

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<sup>39</sup> Order 7 at ¶ 87.

<sup>40</sup> October Hearing Transcript, at 390, lines 4-18.

<sup>41</sup> October Hearing Transcript at 387, lines 11-17.

Any belief that ratepayers would be funding the commitments is simply incorrect and the Commission's conclusion in Order 07, in that regard, was erroneous.<sup>42</sup>

42. Importantly, Order 07 fails to acknowledge and appreciate that if the Proposed Transaction is approved, Hydro One—as Avista's sole shareholder—has effectively agreed to forgo substantial earnings, in order to fulfill the financial commitments of the Proposed Transaction. The Commission's decision also improperly assumes that, absent the Proposed Transaction, Avista shareholders would or should provide the same benefits offered by Hydro One and Avista here with Avista's retained earnings and thus also forgo earnings. In the Commission's words:

In principle, at least,<sup>[43]</sup> these revenues would be available to Avista for the purposes of the Settlement with or without the merger. That is, Avista, if it chose to do so,<sup>[44]</sup> could today propose to confer the same benefits to customers and the community using its retained earnings as would be made available under the terms of the Settlement Stipulation.<sup>45</sup>

The notion that Avista would give away its profits through rate credits and other commitments without good reason is at odds with sound financial management, where net income is either reinvested in the business for the purpose of earning future profits or is paid to shareholders as compensation for the use of their capital. Avista owes a fiduciary duty to its present shareholders to responsibly manage the financial affairs of its business. Here, however, Hydro One has agreed to bear the cost of the Revised Stipulated Commitments to ensure that Avista's customers receive net benefits as a result of the Proposed Transaction.

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<sup>42</sup> Order 07 also failed to recognize that less than all retained earnings would be available for purposes of satisfying monetary commitments. Only those retained earnings that would otherwise be available for distribution to Hydro One (after satisfaction of ring fencing commitments) could be applied to satisfying commitments. Commitment 75. This underscores the fact that it is Hydro One, not ratepayers, who will fund the commitments.

<sup>43</sup> That is, if Avista agreed to deprive its shareholders of their fair rate of return under the regulatory compact.

<sup>44</sup> Again, only if Avista wanted to disregard its shareholders' rights under the regulatory compact.

<sup>45</sup> Order 07 at ¶ 87.



43. Indeed, the Commission, itself, notes the unlikely scenario that Avista would provide these benefits absent the Proposed Transaction: “We acknowledge that this<sup>46]</sup> is not likely because it probably would force Avista to reduce dividends, which could adversely affect its share price.”<sup>47</sup> Such a consequence, of course, is untenable because the reduction in dividends would impact the share price and deprive shareholders of the value of their investment.<sup>48</sup> The Commission committed a clear error of law by disregarding and making assumptions in contravention of the regulatory compact. Under the compact, retained earnings are not customer funds. Rather, they are shareholder dollars in return for a service, and they belong to shareholders. Thus, funding the rate credits and other financial commitments with retained earnings means they will be funded by Avista’s shareholder — Hydro One.

44. The Commission must correct its clear errors in characterizing and analyzing the use of retained earnings to fund the financial benefits to customers. Only by properly categorizing and analyzing the financial benefits as shareholder funding can the Commission properly evaluate the financial benefits to Avista’s customers, which are substantial, state of the art,<sup>49</sup> and meet the net benefits standard.<sup>50</sup>

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<sup>46</sup> “This” being Avista providing the Proposed Transaction’s net benefits with retained earnings absent the Proposed Transaction.

<sup>47</sup> Order 07 at ¶ 87 n.113.

<sup>48</sup> As the Washington Supreme Court has recognized, when the shareholders of the utility absorb expenses, there is “a resulting reduction in the actual rate of return earned by them. This means that disallowance of an expense in a rate case has the very real effect, among others, of increasing the risks of investing in the utility.” *People’s Org. for Wash. Energy Res. v. Utils. & Transp. Comm’n*, 104 Wn.2d 798, 811, 711 P.2d 319 (Wash. 1985). (citation omitted). And as a utility becomes a riskier investment, its credit rating may drop and its cost of capital may increase. *Id.* That in turn will drive up its cost of providing service — not a good outcome for ratepayers.

<sup>49</sup> Order 07 at ¶ 45.

<sup>50</sup> Public Counsel’s expert witness agreed with this conclusion. *See, e.g.*, Exh. JRW-5T at 15 (“Public Counsel recommends that the Commission approve [the] Settlement and the agreed additions and modifications to the Commitments within the Settlement. Both the Settlement and the additions and modifications described above allow the proposed transaction to result in net benefits to Avista’s customers. In particular, the modifications, and new commitment, reduce the transaction risk associated with developments at Hydro One and in Ontario, while preserving the financial benefits associated with the merger.”).

45. The Commission improperly assumed that the “rate credits and other financial benefits promised under the terms of the Settlement Stipulation will be paid largely, if not completely, out of Avista’s revenue recovered in rates and otherwise recorded on Avista’s books as net income”<sup>51</sup> — that is, retained earnings. This assumption again occurred in the face of clear evidence to the contrary.

46. First, and most importantly, the Commission ignored Revised Stipulated Commitment No. 75, which states that Hydro One must fund all of the Revised Stipulated Commitments regardless of whether Avista has retained earnings that are eligible to be sent to Hydro One as a dividend or retained at Avista for the purpose of meeting the Revised Stipulated Commitments:

**75. Sources of Funds for Hydro One Commitments:** Throughout this list of merger commitments, any commitment that states Hydro One will arrange funding is not contingent on Hydro One’s ability to arrange funding, particularly from outside sources, but is a firm commitment to provide the dollar amount specified over the time period specified and for the purposes specified. To the extent Avista has retained earnings that are available for payment of dividends to Olympus Equity LLC consistent with the ring fencing provisions of this list of merger commitments, such retained earnings may be used. Funds available from other Hydro One affiliates may be used without limitation. Avista will not seek cost recovery for any of the commitments funded or arranged by Hydro One in this list of merger commitments. Hydro One will not seek cost recovery for such funds from ratepayers in Ontario. [Emphasis added.]

47. Second, at the October 23, 2018 hearing, Mr. Lopez testified as follows in response to the question of whether the rate credits can be paid by Avista without an independent determination by the Avista Board:

MR. LOPEZ: . . . So the way I understand it here is the rate credit is a requirement from Avista to pay to — to ratepayers. Ultimately, it will result in less funds being available to Hydro One as a shareholder. I think Mr. Thies testified this morning that it could come from an equity injection or it [could] come from retained earnings, which would have otherwise been available to the shareholders.

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<sup>51</sup> Order 07 at ¶ 86.

Ultimately, both of them reduce the funds available to Hydro One shareholders in the future, that's the intent.

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MR. LOPEZ: . . . So, again, I'll — I'll just reiterate. [The financial commitments] could be paid by an equity injection by Hydro One to Avista and Avista would then make the payment to the — the parties that are entitled to those payments. And that would be an injection of equity, more funds, more cash available at Avista or alternatively, it could be taken out of retained earnings that would otherwise be available to Avista share — to Hydro One shareholders who don't pay the dividend.<sup>52</sup>

48. The Commission committed a clear error by ignoring evidence that Avista retained earnings are not the only source, or even the majority source, for funding the Revised Stipulated Commitments. More importantly, as discussed above, even if the retained earnings were the only source for funding the Revised Stipulated Commitments, pursuant to the regulatory compact, those funds are indeed shareholder dollars and provide real value and benefits to Avista customers that would not occur absent the Proposed Transaction.

**C. The Commission undervalued the benefits to Avista's customers because it failed to recognize benefits provided by the commitments.**

49. Benefits to customers can be both monetary and non-monetary. The Proposed Transaction provides extensive non-monetary benefits to customers. The Commission has previously recognized that commitments like those made by Hydro One for a 44% equity floor and improved access to capital provide benefits to customers.<sup>53</sup>

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<sup>52</sup> October Hearing Transcript at 454, lines 6-21, and 455, lines 4-14.

<sup>53</sup> In the Matter of the Joint Application of Puget Holdings LLC and Puget Sound Energy, Inc., Docket U-072375, Order 08 (Dec. 30, 2008) at ¶ 24.

**1. The financial benefits of the Proposed Transaction are not designed to address the potential risks posed by the Province and, by considering the financial benefits in that context, the Commission undervalued them.**

50. The Commission improperly decided there was “no need to consider in detail” the financial benefits of the Proposed Transaction, stating “we consider briefly the extent to which the promised affirmative benefits compensate for the unavoidable risks presented.”<sup>54</sup> As discussed in Section II (A) above, the risks associated with the Province being Hydro One’s largest shareholder are addressed by the Revised Stipulated Commitments. The financial benefits to customers, on the other hand, are not designed to mitigate risks posed by the Province. Rather they are designed to provide net benefits to customers. For the additional reason that the Commission misunderstood the purpose of the Proposed Transaction’s financial benefits, it failed to properly analyze and value them in its net benefits analysis. Because the perceived risks have been sufficiently mitigated, it is not true that such “risks” outweigh the very real and tangible benefits to customers of this transaction (none of which were disputed by the Commission). Accordingly, the comparison of real and undisputed benefits against perceived (but mitigated) risks still results in a NET benefit.

**2. The full settlement of all issues, joined in by all parties, was carefully crafted to mitigate risks and provide real, tangible net benefits.**

51. Revised Stipulated Commitment No. 75 was the product of a thoroughly negotiated settlement amongst all parties to this proceeding.<sup>55</sup> The provision that retained earnings at Avista (which would otherwise go to Hydro One as dividends) could be used to fund the commitments was not offered by Hydro One and Avista in the Joint Application. Rather it was agreed upon during the course of settlement negotiations as a way of ensuring that cash residing at the Avista level, and otherwise available to Hydro One as a reasonable return on its investment and provision

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<sup>54</sup> Order 07 at ¶ 85.

<sup>55</sup> See Exh. JNT-1T at 30-31 n.3.

of service, could be directed to fulfilling the commitments, as necessary, before being directed up the corporate chain via dividends. The parties coupled this funding mechanism in Revised Stipulated Commitment No. 75 with the firm, non-negotiable obligation that “any commitment that states Hydro One will arrange funding is not contingent on Hydro One’s ability to arrange funding, particularly from outside sources, but is a firm commitment to provide the dollar amount specified over the time period specified and for the purposes specified.”

52. While the Commission certainly has the authority to override all-party settlements, it is noteworthy that the Revised Stipulated Commitments in this case were renegotiated *after* recent political developments in Ontario, with all parties reaffirming their belief that sufficient safeguards exist to address the risks associated with the Province being Hydro One’s largest shareholder. For example, in his supplemental testimony, Public Counsel’s expert witness Mr. J. Randall Woolridge testified about the parties’ efforts to address concerns raised after the events of July 2018:

The political developments in Ontario and the resulting changes to Hydro One’s board and management highlight the potential transaction risks for Avista’s ratepayers. In light of these events, the Settling Parties have negotiated additional terms and modifications to the original Settlement. These additional terms and modifications provide further benefits that are necessary in light of the specific risks to this transaction. Therefore, I believe that the revised Settlement meets the net benefit standard. . . .

Public Counsel recommends that the Commission approve Settlement and the agreed additions and modifications to the Commitments within the Settlement. Both the Settlement and the additions and modifications described above allow the proposed transaction to result in net benefits to Avista’s customers. In particular, the modifications, and new commitment, reduce the transaction risk associated with developments at Hydro One and in Ontario, while preserving the financial benefits associated with the merger.<sup>56</sup>

It is also noteworthy that the Commission distinguishes this case from the PSE/Macquarie transaction on the basis that in PSE/Macquarie the applicants refused to address Public Counsel’s

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<sup>56</sup> Exh. JRW-5T at 5 and 15.

stated concerns—that is, all the concerns raised by all the parties to that case—whereas here, Hydro One and Avista cooperated with all parties and diligently worked through their concerns to develop a robust settlement.<sup>57</sup> If anything, this factor should weigh in Hydro One’s and Avista’s favor.

**D. Order 07 is beyond the Commission’s jurisdiction, and unsupported by evidence, because it is based upon perceived harms to the shareholders of an Ontario corporation and whether the Hydro One Board and executive leadership acted in the best interests of Hydro One’s stakeholders.**

53. The Commission spends a significant amount of time in Order 07 discussing its views on the legal obligations of Canadian corporations and boards of directors and the harms it believes Hydro One’s shareholders suffered when the prior Hydro One CEO and Board resigned and from that analysis extrapolates that Avista’s customers will suffer harm if the merger is approved.<sup>58</sup>

54. The Commission’s approach to opining on what actions a publicly-traded company in Canada should take—in Canada, under Canadian law—reaches far beyond the Commission’s authority and expertise. The Commission reached unsupported conclusions that: (i) “[N]either the CEO nor the board were willing to defend the integrity of Hydro One as a publicly traded corporation with multiple investors”<sup>59</sup>; (ii) Hydro One’s leadership failed to exercise “due diligence ... in not even considering [shareholder impacts] before entering into the Letter Agreement with the province on July 11, 2018”<sup>60</sup>; (iii) “In this case, [Hydro One shareholder] rights were ignored; they were given no opportunity to air any concerns they may have had in connection with the removal of the CEO and the entire board of directors”<sup>61</sup>; (iv) “Nor do we find

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<sup>57</sup> The Commission inappropriately appears to punish Hydro One and Avista for willingly working through all party concerns, as opposed to Macquarie. Order 07 at ¶ 37. This is unfair to Hydro One, Avista, and all settling parties and can only serve to discourage the orderly resolution of Commission proceedings through settlement agreements.

<sup>58</sup> Order 07 at ¶¶ 13–15, 43, 62, 74, 77, 78, 80, 97.

<sup>59</sup> Order 07 at ¶ 63.

<sup>60</sup> Order 07 at ¶ 75; *see also id.* at ¶ 80.

<sup>61</sup> Order 07 at ¶ 78.

that ‘the Province and Hydro One complied with the spirit and intent of...the Governance Agreement’<sup>62</sup>; and (v) “[I]t became apparent that Hydro One management and direction were...subject to decisions by the Province of Ontario just as if Hydro One remained a Crown Corporation...<sup>63</sup> The Commission does not have the jurisdiction or the evidence to determine whether these actions by Hydro One’s Board and executive leadership following the election were in compliance with Canadian corporate law and securities law, whether the events surrounding the July 11, 2018 Letter Agreement were in the best interests of Hydro One or its shareholders or, whether Hydro One’s management and direction are subject to decisions by the Province of Ontario as if Hydro One were a Crown Corporation. Moreover, the Commission’s decision took out of context certain facts, evidence and testimony to reach its conclusions.<sup>64</sup>

55. The Commission erred in concluding that Hydro One shareholder rights were ignored in connection with the retirement of the CEO and resignation of the Board of Directors and that they had no say in the process.<sup>65</sup> Representatives of Hydro One’s most significant shareholders, other than the Province, were actively involved in identifying and nominating a majority of the new directors, and confirming all of the directors, who were appointed to the Hydro One Board on August 13, 2018.<sup>66</sup> Following the announcement of the Letter Agreement on July 11, 2018, Hydro

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<sup>62</sup> Order 07 at ¶ 77.

<sup>63</sup> Order 07 at ¶ 70.

<sup>64</sup> Order 07’s footnote 16 mischaracterizes Hydro One Board Chair Woods’ testimony regarding whether the sudden resignation of Hydro One’s Board and CEO was in the best interests of Hydro One as a “straightforward: ‘No.’” In fact, Mr. Woods continued by clarifying his statement:

[I]f I could just follow up. Technically, the sudden resignation was caused by events that were certainly not in the best interest of Hydro One. The process by which that took place, as Mr. Scarlett discussed, I think was the best process. But no, certainly the events leading up to that and the ultimate result were not in the best interest of the company.

In other words, Mr. Woods found no fault at all with the resignation process. Rather, Mr. Woods stated that the events prompting the resignation and the result of the process -- i.e. the board turnover -- were not in the best interests of Hydro One.

<sup>65</sup> Order 07 at ¶ 78.

<sup>66</sup> Exh. JDS-1T at pp. 7-8.

One's shareholders had more than an additional 30 days to provide feedback to Hydro One concerning the Letter Agreement or the Board replacement process, if they desired, before the new board was seated on August 13, 2018.<sup>67</sup>

56. Further, the Commission mistakenly concluded, in the face of evidence to the contrary, that the July 11, 2018 Letter Agreement did not comply with the spirit and intent of the Governance Agreement.<sup>68</sup> The Letter Agreement was specifically negotiated, structured, and limited in scope, to do just that.<sup>69</sup> In fact, the only aspect of the board replacement process in the Letter Agreement that did not strictly conform to the Governance Agreement was the waiver of the requirement to provide a Removal Notice or call and hold a Removal Meeting under the Governance Agreement.<sup>70</sup> As stated in testimony,<sup>71</sup> this limited waiver was granted on the basis that the Board had determined that it would be in the best interests of Hydro One and its shareholders to forgo the delay of a shareholders meeting. This was in a context where the board removal procedures outlined in the

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<sup>67</sup> *Id.*

<sup>68</sup> Order 07 at ¶ 77.

<sup>69</sup> This was accomplished in several respects. First, the Letter Agreement required “the establishment of an Ad Hoc Nominating Committee consistent with the process set out in the Governance Agreement comprised of one representative of each of the five largest beneficial owners of Voting Securities of Hydro One, excluding the Province...”, or such lesser number of shareholders willing to act. Exh. JDS-2 at § 1.a.; Exh. MMS-5 § 4.7.2. Second, the Letter Agreement required that the Ad Hoc Nominating Committee and the Province then nominate and confirm a slate of ten (10) replacement Director nominees to be appointed to the Board, with 40% of the replacement directors being nominated by the Province and 60% of the replacement directors being nominated by the Ad Hoc Nominating Committee, consistent with the Governance Agreement. Exh. JDS-2 at § 1.b.; Exh. MMS-5 § 4.1.1. Third, the Letter Agreement required that all directors meet the requirements set out in section 4.2 of the Governance Agreement, including that each director be independent of Hydro One and the Province of Ontario. Exh. JDS-2 at § 1.b.; Exh. MMS-5 § 4.2. Fourth, also consistent with the Governance Agreement, the Letter Agreement required the appointment of the new Board in a sequential manner as contemplated by section 4.6.2(a) of the Governance Agreement and required the new Board to appoint “a new Chair of the Board in accordance with section 3.2 of the Governance Agreement” and to “identify, select and appoint a replacement President and Chief Executive Officer...in accordance with section 3.3 of the Governance Agreement.” Exh. JDS-2 at §§ 1.e., 1.c., 13; Exh. MMS-5 §4.6.2(a). All of these processes and procedures were implemented by the Hydro One Board, consistent with the Governance Agreement, with representatives of three of the five largest Hydro One shareholders (Exh. JDS-1T at pp. 7-8), excluding the Province, agreeing to serve on the Ad Hoc Nominating Committee and responsible for identifying, nominating and confirming the new Board nominees.

<sup>70</sup> Exh. JDS-2 at § 1.c.; Exh. MMS-5 § 4.7.

<sup>71</sup> Exh. JDS-1T at pp. 7-8.



Letter Agreement otherwise conformed to the Governance Agreement and the outcome of a shareholder vote on the election of directors nominated by representatives of the major non-Provincial shareholders on the Ad Hoc Nominating Committee and the Province would be a forgone conclusion.<sup>72</sup>

57. Importantly, under the Letter Agreement, the Province of Ontario also ratified and affirmed all of its obligations under the Governance Agreement, which remains “in full force and effect,” except solely to the extent modified in the Letter Agreement to facilitate the orderly replacement of the Board and to address compensation matters relating to the then-retired CEO and Hydro One’s Board and other executives in Canada. Otherwise, the Letter Agreement does not alter the protections outlined in the Governance Agreement, which agreement affords Hydro One’s investors greater protections than they would otherwise typically enjoy in any other public company that has a significant minority investor.<sup>73</sup>

58. For the foregoing additional reasons, the Commission’s decision was unsupported by the evidence, and exceeded the scope of the Commission’s jurisdiction.

### **III. PETITION FOR REHEARING**

59. The Commission should rehear Order 07 under WAC 480-07-870 to allow the admission of evidence that is available due to changed conditions since the Commission entered Order 07 and for other good and sufficient cause that the Commission did not consider or determine in Order 07.<sup>74</sup>

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<sup>72</sup> October Hearing Transcript at 402, lines 7-18.

<sup>73</sup> October Hearing Transcript at 403, line 23 through 404, line 7.

<sup>74</sup> See WAC 480-07-870(1).

60. Hydro One and Avista respectfully request that the Commission rehear Order 07 to consider the following items:

(i) the Declaration of Kari L. Vander Stoep, which includes, as Exhibit A, a copy of a letter from the Office of the Deputy Minister of Energy of the Province of Ontario, dated November 29, 2018, in which the Province “reiterate[s] the Ministry’s commitment to supporting Hydro One in its efforts to complete the Avista acquisition”;

(ii) testimony to be provided by Hydro One’s new President and CEO following the CEO’s appointment; and

(iii) additional conditions related to future actions by the Province (if the Commission determines the conditions constitute additional evidence<sup>75</sup>).

61. Hydro One and Avista have good and sufficient cause to request rehearing in this matter because Order 07 raised additional concerns and issues regarding the Province’s ability to influence Hydro One and Avista.

62. The additional evidence directly addresses the Commission’s concerns regarding the Province’s ability to influence Hydro One and Avista post-merger.<sup>76</sup> It also addresses the Commission’s concerns that the Province has not indicated its support for the Proposed Transaction.<sup>77</sup> Finally, the additional evidence was not available at the time of the May 22, 2018 hearing or October 23, 2018 hearing.

63. In the event that the Commission feels it is necessary to rehear Order 07 to consider the proposed conditions and the letter from the Province, or to take additional testimony from Hydro

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<sup>75</sup> Hydro One and Avista believe the conditions do not constitute additional evidence, are supported by the current record, and the Commission, without rehearing Order 07, can approve the Joint Application by conditioning its approval order on these conditions. Hydro One and Avista also recognize, however, that if the Commission so chooses, it can rehear Order 07 to consider the conditions as additional evidence.

<sup>76</sup> See, e.g., Order 07 at ¶ 90.

<sup>77</sup> Order 07 at ¶ 46, n.51.

One's new CEO, Hydro One and Avista request expedited proceedings to address these limited issues. Due to the March 29, 2019 closing deadline in the merger agreement and the expiration of Hydro One's funding for the transaction shortly thereafter, Hydro One and Avista request that any additional process conclude by the end of January 2019. Hydro One and Avista will do everything possible to assist with an expedited schedule if the Commission is inclined to rehear Order 07 for the limited purposes described.

#### **IV. CONCLUSION**

64. For the reasons stated above, the Commission should grant Hydro One's and Avista's Petition for Reconsideration and revise Order 07 to (1) properly analyze and account for the governance, financial integrity, and ring-fencing commitments that fully protect Avista from any potential Provincial influence, (2) enter sufficient findings in that regard that specifically address any perceived shortcomings in each of the structural safeguards, (3) properly evaluate and value the net benefits of the Proposed Transaction, and (4) approve the Joint Application. Unless revised in this manner, Order 07 will be in error of law and not based on substantial evidence backed by sufficient findings. The Commission should also rehear Order 07, as necessary and on an expedited basis, to receive into evidence (1) the Declaration of Kari L. Vander Stoep and Exhibit A included with this Petition, (2) testimony from Hydro One's new President and CEO once appointed, and (to the extent the Commission deems it necessary to rehear Order 07 to consider the additional conditions offered by Hydro One and Avista) (3) the additional conditions offered by Hydro One and Avista in this Petition.

DATED: December 17, 2018.

Respectfully Submitted,

K&L GATES, LLP

AVISTA CORPORATION



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