

**BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION**

In the Matter of the Joint Application of)
HYDRO ONE LIMITED (acting through its) DOCKET U-170970
indirect subsidiary, Olympus Equity LLC))
And)
AVISTA CORPORATION)
For an Order Authorizing Proposed)
Transaction.)
_____)

**DIRECT TESTIMONY OF DR. MARC M. HELLMAN
ON BEHALF OF THE
ALLIANCE OF WESTERN ENERGY CONSUMERS**

April 10, 2018

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1 **I. INTRODUCTION AND SUMMARY**

2 **Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

3 A. Dr. Marc Hellman. My business address is 2760 Eagle Eye Ave. NW, Salem, Oregon,
4 97304.

5 **Q. PLEASE STATE YOUR OCCUPATION AND ON WHOSE BEHALF YOU ARE**
6 **TESTIFYING.**

7 A. I am an economist by training with significant experience in energy utility regulation. I
8 am testifying on behalf of the Alliance of Western Energy Consumers (“AWEC”). The
9 Northwest Industrial Gas Users (“NWIGU”) merged into the Industrial Consumers of
10 Northwest Utilities (“ICNU”) on March 31, 2018, and ICNU changed its name to AWEC
11 on April 1, 2018. Both ICNU and NWIGU were original parties to this docket.

12 **Q. PLEASE SUMMARIZE YOUR EDUCATION AND WORK EXPERIENCE.**

13 A. I have a Masters and PhD in Economics awarded by Claremont Graduate School and a
14 Bachelor’s degree in both Economics and Mathematics awarded by California State
15 Polytechnic University, Pomona.

16 With regards to my work experience, I was employed for 38 years in various
17 capacities by the Public Utility Commission of Oregon, with the last twenty years or so in
18 a management capacity leading economists, accountants and financial analysts in the
19 review of utility general rate filings and rate proposals, financing and affiliated interest
20 applications, property sales, and merger and acquisitions. I have also provided consulting
21 services with my most recent projects for the Commonwealth Utilities Corporation with
22 headquarters in Saipan, the Smart Energy Alliance in a Nevada Power general rate filing

1 before the Public Utilities Commission of Nevada, and the South Dakota Intrastate
2 Pipeline Company.

3 **Q. WHAT IS THE PURPOSE OF YOUR DIRECT TESTIMONY?**

4 A. The purpose of this testimony is to provide support for the all-party proposed stipulation,
5 dated March 27, 2018 (“Settlement or Stipulation”), and to describe and explain the
6 Settlement provisions specific and critical to the customers represented by AWEC.

7 **Q. PLEASE SUMMARIZE YOUR TESTIMONY.**

8 A. AWEC recommends the Washington Utilities and Transportation Commission
9 (“Commission” or “WUTC”) adopt the all-party Settlement, concluding that its terms and
10 conditions provide net benefits to the customers of Avista Corporation (“Avista” or the
11 “Company”) and are in the public interest.

12 **Q. IS THERE ANY OTHER OBSERVATION YOU WOULD LIKE TO OFFER?**

13 A. Yes. The Stipulation is an all-party settlement representing a consensus position of
14 numerous parties with diverse and often contrary positions. That it includes such a broad
15 coalition of parties representing ratepayer, environmental, low-income, and labor
16 interests should be considered evidence that it is in the public interest.

17 **II. DISCUSSION OF OVERALL RECOMMENDATION**

18 **Q. PLEASE DISCUSS YOUR OVERALL POSITION REGARDING THE**
19 **PROPOSED SETTLEMENT.**

20 A. As discussed in the Joint Testimony, the Settlement includes commitments designed to
21 prevent harm to customers as well as commitments that, in aggregate, produce net
22 benefits to customers.

1 **Q. PLEASE DESCRIBE YOUR EXPERIENCE REVIEWING AND ANALYZING**
2 **UTILITY MERGERS AND ACQUISITIONS.**

3 A. I have either participated in the review or led the Oregon Public Utility Commission's
4 Staff team responsible for reviewing merger and acquisition filings submitted for
5 approval in Oregon over the course of more than ten years. These include the separate
6 Scottish Power and Mid-American acquisitions of PacifiCorp; the MDU acquisition of
7 Cascade; and the separate applications to purchase Portland General Electric that were
8 filed by TPG (not approved), Northwest Natural (later withdrawn by NW Natural), and
9 Sierra Pacific (approved but not consummated), as well as the PGE stock distribution as
10 an outcome of Enron's bankruptcy filing. I also led the review of the recent Northwest
11 Natural holding-company formation as well as the Avista proposal filed several years ago
12 to form a holding company—which Avista later withdrew. Some of the mergers and
13 acquisitions, such as those for PacifiCorp and Cascade, for example, also required
14 approvals in more than one state, such as Oregon and Washington – a

15 Each of the proposed mergers and acquisitions listed above had their own unique
16 set of risks and potential benefits. To address the risks posed by the transaction, a host of
17 conditions were designed to mitigate those risks as well as other commitments that
18 resulted either in a net benefit or no harm to customers.

19 My recommendation that the Commission approve the Hydro One application
20 contingent upon adoption of the Stipulation and the commitments contained therein is
21 based on this extensive background and experience in analyzing mergers and
22 acquisitions.

1 **Q. THE PARTIES HAVE REACHED A SETTLEMENT PRIOR TO THE**
2 **SUBMITTAL OF RESPONSIVE TESTIMONY BY THE NON-APPLICANT**
3 **PARTIES. DO YOU BELIEVE THE REVIEW UNDERTAKEN BY THE NON-**
4 **APPLICANT PARTIES TO BE BOTH COMPREHENSIVE AND RIGOROUS?**

5 A. Absolutely. The fact that the all-party Settlement has been submitted prior to the filing of
6 responsive testimony by the Non-Applicant parties in no way implicates the quality and
7 independence of the review performed by the settling parties. The discovery in this case
8 demonstrates that many hard questions were asked of the Joint Applicants, including
9 numerous questions seeking clarification of the responses or additional information. As
10 ICNU, AWEC alone issued nearly 90 data requests to Avista and over 100 to Hydro One.
11 AWEC demanded and received detailed information regarding Hydro One's past history
12 of operating practices; its management expertise, corporate culture and use of training;
13 the scope of Hydro One's business operations, including its experience with conservation
14 and demand side management programs; the nature of Ontario Board Oversight and
15 ownership; the premium paid by Hydro One; the incentives to Avista management to
16 obtain approval; the consequences of non-approval, such as termination fees; the
17 restrictions on Avista operations during pendency of merger reviews by governmental
18 and regulatory agencies; the set-up of Avista's board and member configuration; and the
19 due diligence deployed by Hydro One prior to and after its initial merger filing with the
20 Securities and Exchange Commission. Staff, Public Counsel, The Energy Project, NW
21 Energy Coalition, the Sierra Club, and the Washington and Northern Idaho District
22 Council of Laborers all issued additional discovery to the Joint Applicants and performed
23 further due diligence.

1 **Q. PLEASE DESCRIBE HOW YOU APPROACHED YOUR REVIEW OF THE**
2 **SETTLEMENT.**

3 A. I examined the Settlement's provisions with two objectives in mind. First, my review
4 focused on whether the agreed upon terms would protect the Washington customers of
5 the Company. Next, I ascertained whether the Settlement as a whole would confer a net
6 benefit to Avista's Washington customers.

7 Initially through NWIGU's participation, AWEC is also participating in the
8 Public Utility Commission of Oregon's review of the proposed merger. Although
9 Washington and Oregon have a similar net benefits standard, Avista's operations in
10 Oregon are much different than in Washington and do not include electric services.
11 Consequently, my review of the Settlement is limited to the impact of the merger and the
12 Settlement on Avista's Washington customers and in the context of this Commission's
13 application of Washington's standard for approval. The Settlement also provides that the
14 non-company parties' support of the merger is limited to this proceeding before the
15 Commission.

16 **III. COMMITMENTS THAT PROTECT CUSTOMERS**

17 **Q. PLEASE DESCRIBE A FEW OF THE PROVISIONS YOU BELIEVE ARE**
18 **DESIGNED TO PREVENT HARM TO CUSTOMERS.**

19 A. There are many provisions designed to ensure the continuity of Avista operations and
20 activities. For example, Commitments 5, 9 through 14, and 18 relate to maintaining:

- 21 • Avista capital investment levels associated with economic development
22 (Commitment 5);
23 • Avista's headquarters in Spokane (Commitment 9);

- 1 • Local staffing levels in local communities consistent with providing safe and reliable
2 service (Commitment 10);
- 3 • Increasing charitable contributions to the local community (Commitment 11);
- 4 • Community involvement including low-income service agencies and support
5 initiatives (Commitment 12);
- 6 • Economic development consistent with past practices (Commitment 13); and
- 7 • Dues and memberships paid to various trade groups and organizations (Commitment
8 14).

9 Commitment 18 is designed to prevent harm by ensuring that the costs incurred related to
10 the transaction will be tracked and recorded as non-utility costs and will not be recovered
11 from customers directly or indirectly through some corporate allocation mechanism.

12 In addition, the Regulatory Commitments 20 through 33, the Financial Integrity
13 Commitments 34 through 41, the Ring-Fencing Commitments 42 through 51 and the
14 Source of Funds Commitment 75 are intended to protect ratepayers by:

- 15 • Ensuring that Avista and its affiliates will comply with applicable laws and
16 requirements (Commitments 20, 21, 27, 30 and 31);
- 17 • Maintaining separate books and records for Avista (Commitment 22);
- 18 • Providing access to books and records of affiliates so that charges can be verified and
19 examined for transactions between affiliates and Avista, or result in costs being
20 allocated to Avista (Commitment 23);

- 1 • Providing cost allocation methodologies that do not allow for cross subsidization
2 while maintaining Avista’s burden of proof that such charges resulting from such
3 allocations are fair and reasonable (Commitment 24);
- 4 • Ensuring Avista’s cost of capital will be no higher than what it otherwise would be
5 absent Hydro One’s ownership. (Commitment 25);
- 6 • Maintaining at least a 44 percent minimum equity level in the capital structure
7 (Commitment 26);
- 8 • Continuing to meet Avista’s reporting requirements and participation in national and
9 regional forums (Commitments 27 and 28); and
- 10 • Providing an annual report through 2029 regarding the status of compliance with the
11 merger commitments (Commitment 32).

12 The Financial Integrity Commitments 34 through 41 require Avista to maintain its own
13 credit ratings for debt and preferred stock (Commitments 35 and 36); promptly notify the
14 Commission if there is a downgrade in credit ratings (Commitment 37); adequately
15 maintain Avista’s pension fund (Commitment 39); comply with federal finance reporting
16 requirements (Commitments 40 and 41); and restrict the access of Hydro One and its
17 affiliates to Avista’s equity under circumstances specified so as to maintain adequate
18 liquidity and financial strength (Commitment 38).

19 The ring fencing commitments 42-51 ensure that: Avista will not involuntarily be
20 drawn into a bankruptcy (Commitments 42, 43, and 44); and Avista assets or credit will
21 not be pledged for any affiliates, and any inter-company lending (Commitments 46 and
22 51).

1 Finally, Commitment 75 ensures that Avista will not seek recovery for any
2 commitment funded or arranged by Hydro One.

3 **Q. WHY DO YOU BELIEVE SUCH PROVISIONS ARE IMPORTANT IN THE**
4 **CONTEXT OF THE COMMISSION’S DUTY UNDER RCW 80.12.020 TO**
5 **ENSURE THE TRANSACTION PROVIDES A NET BENEFIT TO**
6 **CUSTOMERS?**

7 A. While I am not a lawyer, in my opinion based on extensive experience analyzing energy
8 company mergers, commitments that mitigate harm to customers are inextricably
9 intertwined with ensuring a net benefit overall to customers from the transaction. It is
10 helpful to think of the analysis in terms of a scale, with “harms” on one side and
11 “benefits” on the other. In a transaction that provides “net benefits” to customers, the
12 “benefits” side of the scale would outweigh the “harms” side. Thus, the Commission can
13 ensure “net benefits” to customers not only by increasing the weight on the “benefits”
14 side of the scale (i.e., adding more benefits), but also by *decreasing* the weight on the
15 “harms” side (i.e., imposing commitments that protect customers from such harms).
16 Therefore, commitments in the Stipulation that protect customers from potential harm
17 from the transaction also help ensure that the transaction provides net benefits to
18 customers.

19 **Q. DO YOU HAVE OTHER EXAMPLES OF HOW THE SETTLEMENT**
20 **PROTECTS CUSTOMERS?**

21 A. Yes. Commitment 47 is a hold harmless provision that is intended to hold Avista
22 customers harmless from financial risks associated with Hydro One. This is a sensible
23 provision to include in the agreement. If, for example, Avista’s cost of debt increased

1 due to the actions of Hydro One or one of its other affiliates, the Commission can act to
2 protect Avista's ratepayers, relying upon the terms of this Commitment.

3 **IV. COMMITMENTS THAT BENEFIT CUSTOMERS**

4 **Q. DO ANY OF THE ABOVE COMMITMENTS THAT PROTECT CUSTOMERS**
5 **FROM HARM ALSO CONFER A BENEFIT TO AVISTA'S CUSTOMERS?**

6 A. I believe that future enforcement of the Commitments will confer benefits to customers.
7 For example, Commitment 38 does not allow the issuance of dividends if Avista's debt to
8 equity ratio is equal to or greater than 44 percent. Currently, there is no restriction on
9 Avista's rights to issue dividends to shareholders. In my opinion, the enforcement of this
10 Commitment should confer a net benefit to customers by establishing a threshold where
11 none currently exists today. Further, this commitment also offsets a potential harm
12 created as a result of this transaction by ensuring that Avista does not become too highly
13 leveraged.

14 Similarly, Commitment 15 on Safety and Reliability adds service quality
15 provisions for SAIFI and SAIDI to help address the risk that the transaction will
16 negatively impact Avista's reliability. This commitment also, however, imposes
17 reliability targets and subjects Avista to financial penalties if it fails to meet these targets,
18 thus potentially resulting in improved safety and reliability as a consequence of the
19 transaction. This commitment does not guarantee that service quality will not suffer;
20 however, the Commitment does provide a quantitative benchmark for SAIDI and SAIFI
21 and a remedy if service should degrade.

1 **Q. ARE THERE COMMITMENTS THAT ARE DESIGNED SPECIFICALLY TO**
 2 **CONFER BENEFITS TO CUSTOMERS?**

3 A. Yes, Commitment 19 requires Avista and Hydro One to provide Washington customers a
 4 \$30.7 million rate credit over a five-year period.^{1/} This provision confers a direct and
 5 quantifiable benefit to Avista’s customers, and significantly increases the annual rate
 6 credits from those initially offered by the Applicants.

7 The Applicants had originally proposed a rate credit that in aggregate, over a ten-
 8 year period, equated to 3.1 percent of today’s revenue requirement. The rate credit
 9 contained in the Settlement provides the rate credit monies over five years instead of ten,
 10 so customers receive the rate credit in half the time of what the Applicants originally
 11 proposed. Second, the rate credit in aggregate equates to not 3.1 percent of Avista’s
 12 annual utility revenues but 5.0 percent of Avista’s annual utility revenues. Third, even
 13 though the rate credit percentage was increased substantially, the amount that is off-
 14 settable each year remains at \$1.02 million, meaning that the percentage of the rate credit
 15 that is offsettable is significantly lower than what the Applicants initially proposed.

16 **Table 1**

					Year						Net Present Value at
	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	3 %/Year
Washington Electric as Originally Proposed	\$1.51	\$1.51	\$1.51	\$1.51	\$1.51	\$1.51	\$1.51	\$1.51	\$1.51	\$1.51	\$12.88
Washington Natural Gas as Originally Proposed	\$0.45	\$0.45	\$0.45	\$0.45	\$0.45	\$0.45	\$0.45	\$0.45	\$0.45	\$0.45	\$3.84
Total											\$16.72
Washington Electric per Stipulation	\$4.92	\$4.92	\$4.92	\$4.92	\$4.92						\$22.54
Washington Natural Gas per Stipulation	\$1.22	\$1.22	\$1.22	\$1.22	\$1.22						\$5.59
											\$28.13

^{1/} The Settlement would allow the rate credit to be offset by up to \$1.02 million annually, so long as Avista demonstrates that such savings were captured in Avista’s base rates.

1 Table 1 illustrates the net present value of the rate credit over the period of time
2 that the rate credit is provided to customers. The annual discount rate is assumed to be
3 three percent. Assuming the values in Table 1, the net present value of the rate credit
4 increases from a total net present value of \$16.72 million to \$28.13 million. This is an
5 increase of 68.2 percent.

6 **Q. WHY IS IT REASONABLE TO SHORTEN THE TIME FRAME OVER WHICH**
7 **THE RATE CREDIT IS PROVIDED TO CUSTOMERS?**

8 A. I believe it is very reasonable in the context that Avista's shareholders, which includes
9 Avista executive management, received an immediate benefit when Avista's share price
10 increased dramatically when Hydro One announced the merger agreement with Avista.
11 Also, Avista management stands to receive additional monetary benefits immediately or
12 soon after the transaction closes. Therefore, accelerating the disbursement of rate credits
13 to customers better aligns with the timing of benefits received by shareholders and Avista
14 executive management.

15 **Q. DO YOU HAVE ANY OTHER COMMENTS ON THE RATE CREDIT?**

16 A. For Schedule 25, Commitment 19 directs that the rate credit be designed so that one-third
17 of the rate credit amount for Schedule 25 is apportioned to blocks one and two of the
18 three-energy block rate design. Two-thirds of the rate credit amount allocated to
19 Schedule 25 is apportioned to the third block. The credits would be \$0.00031 per kWh
20 for blocks 1 and 2, and \$0.00101 for block 3. The three-block rate design for Schedule
21 25 has been in place since Avista's 2007 general rate case.^{2/}

^{2/} WUTC v. Avista Corp., Docket Nos. UE-070804/UG-070805 & UE-070311, Order 05 ¶¶ 19, 31 (Dec. 19, 2007).

1 Assigning two-thirds of the Schedule 25 rate credit amounts to the third block
2 (greater than 6,000,000 kWh) is fair and reasonable for a number of reasons. First,
3 customers using this very large amount of kWh have significant investments in electrical
4 production processes, much greater than other relatively smaller Schedule 25 customers.
5 This means that any potential risks from the transaction are proportionally greater for
6 these customers than they are for customers with less investment in electrical
7 infrastructure.

8 Additionally, customers using greater than 6,000,000 kWh of electricity
9 necessarily have high load factors that use significant amounts of off-peak energy. Even
10 with a minimum 3000 KVA demand level, using 6,000,000 kWh means that a good
11 portion of the energy consumed has to be associated with off-peak use. As energy usage
12 grows beyond the 6,000,000 kWh level, at a given kW monthly demand, such usage can
13 be thought of as increasing energy use in off-peak times. The small \$0.00070 per kWh
14 differential in the credit (0.00101 – 0.00031) between the first two blocks and the last
15 block reflects both a peak/off-peak energy cost differential of energy supply and the
16 benefits other Avista customers receive by having available significant off-peak load in
17 Avista energy supply operations.

18 **Q. DOES THIS RATE CREDIT DESIGN FOR SCHEDULE 25 AFFECT ANY**
19 **OTHER RATE SCHEDULE?**

20 **A.** No. The total amount of dollars allocated to Schedule 25 of the annual merger rate credit
21 is the same regardless of the Schedule 25 rate design.

1 **Q. IS THERE ANY OPPOSITION TO THIS PROPOSAL?**

2 A. None has been identified.

3 **Q. ARE THER ANY OTHER COMMITMENTS THAT BENEFIT CUSTOMERS ON**
4 **WHICH YOU WISH TO COMMENT?**

5 A. Yes. Commitment 61 relates to a one-time self-direct customer option for a very large
6 conservation project (DSM Project). The DSM Project must cost at least \$15 million but
7 no more than \$30 million and be undertaken within five years of the close of Hydro
8 One's acquisition of Avista. After any available Schedule 91 funds are selected and used,
9 the remaining balance will be provided by Avista and paid back over time by the DSM
10 Project participant through the participant's Schedule 91 charges.

11 **Q. IS THIS PROPOSAL SIMILAR TO OTHER DSM PROGRAMS?**

12 A. Yes. Puget Sound Energy runs a self-direct DSM program for its largest customers under
13 its Schedule 258. Similarly, in Oregon large customers can obtain a credit against the
14 public purpose charge imposed under ORS 757.612 by self-directing their energy
15 efficiency. Allowing large customers to self-direct their energy efficiency makes sense
16 because these customers have the most knowledge of their often-complicated production
17 processes and, therefore, which DSM investments are workable within those processes.

18 **Q. WOULD OTHER CUSTOMERS BENEFIT FROM THIS DSM PROJECT?**

19 A. Yes. Just like all customers benefit from Avista purchasing cost-effective DSM
20 resources, all customers will benefit from Avista acquiring this cost-effective DSM
21 resource. In general, the largest conservation projects are also the most cost-effective.
22 This is a win-win outcome for all customers.

1 **Q. DOES THIS COMMITMENT POSE ANY RISK TO OTHER CUSTOMERS?**

2 A. No. In the unlikely event where the customer defaults or ceases operations prior to
3 Avista's full recovery of the DSM Project costs through the customer's levied Schedule
4 91 charges, the remaining Schedule 25 customers will be responsible for any remaining
5 unamortized balance through their Schedule 91 charges.

6 **Q. IS THE ALLOCATION OF THE RATE CREDIT IN SCHEDULE 25 AND**
7 **COMMITMENT 61 REGARDING THE LARGE CUSTOMER CONSERVATION**
8 **PROJECT INTEGRAL TO AWEC'S SUPPORT FOR THE SETTLEMENT?**

9 A. Yes.

10 **Q. DOES THAT CONCLUDE YOUR TESTIMONY?**

11 A. Yes.