CFRA Interview with Hydro One Vice-President, Ferio Pugliese

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Speaker(s):	Ferio Pugliese, Hydro One Executive Vice-President, Customer Care & Corporate Affairs

CFRA: Ferio Pugliese is Executive Vice-president of Consumer Care and Corporate Affairs at Hydro One. Good morning.

FERIO PUGLIESE, HYDRO ONE EXECUTIVE VICE-PRESIDENT OF CONSUMER CARE AND CORPORATE AFFAIRS: Good morning.

CFRA: Hydro One is buying an American company, Avista Corporation. Why?

PUGLIESE: Well, we believe that this is both a smart and a strategic, a good strategic move for Hydro One right now. It helps us expand our portfolio of assets into another jurisdiction, but a jurisdiction that is complementary to the work that we do here in Ontario and allows us to diversify our asset mix and which will further return back to the business.

CFRA: Okay. How much? How much is this going to cost?

PUGLIESE: Well the transaction itself is, in terms of overall, the enterprise value purchase of Avista is $6.7-billion.

CFRA: Okay.

PUGLIESE: A billion dollar transaction--

CFRA: U.S. or Canadian sir?

PUGLIESE: That's Canadian.

PUGLIESE: Thank you, okay. Yeah.

PUGLIESE: And so the way that's being financed is through debt based on our strong investment grade balance sheet as well as through the issue of equity at 1.4-billion in equities been issued and raised to complement the purchase of the and the transaction.

CFRA: So in other words, to deconstruct that a little bit; because I've heard this a lot already since this deal was announced. Where the heck did Hydro One get $6.7-billion in cold hard cash to buy an American company? You sold shares. You issued shares, investors bought them, you raised money and you sold bonds to bond investors and you raised money and that's where you got the 'cash'?

PUGLIESE: Yup.

CFRA: Right?

PUGLIESE: That's right.

CFRA: OK.

PUGLIESE: That's right.

CFRA: A lot of people, Ferio Pugliese, Executive Vice-president, Hydro One, you know this; a lot of people are already expressing concern, even outrage, about this deal. First of all, they point out that your company right now is applying to race to the regulator to have an increase in hydro rates. If you have the corporate capacity to buy an American company for $6-billion, people are wondering why do you need an increase in hydro rates?

PUGLIESE: Yeah, and these are great questions and I think what's important as people look at this is to understand how-- and to be equipped with the facts on how these transactions work. First of all, the cost to buy another utility like this of this magnitude at $6.7-billion, there is absolutely no impact, zero impact, to the rate to the customer, to the rate base in Ontario with respect to this. This transaction clearly comes from earnings to the company and the impact and the cost of that is borne by shareholders. They regulated environment to which we operate in here in Ontario and even now with Avista in the jurisdictions that they operate in don't allow you to make purchases like this and allow them to be borne by the customer base. They're two separate transactions. When you look at the current distribution rate filing that we have in front of the Ontario Energy Board, what is different about that is that we need to inject capital into our existing system in Ontario which is declining. We have more polls than people in this province and we have to--

CFRA: More hydro polls than people.

PUGLIESE: We have, we have, we service, we service in our territory we have more hydro polls than we do customers. We have roughly 1.6 million polls and we have 1.35 million customers. So what's important to us is that we continue to put capital into that system so that the lights stay on, we have reliability in the power and at the same time we're able to try to return-- make the operation efficient and return savings back to customers as best we can. And so what you're seeing in that rate filing is the increases that are suggested there are coming from the capital that we have to invest in the system to keep the system upgraded and running. If we don't do that, over time what will happen is that will decline and we'll have major service interruptions to which we know our customers are not going to appreciate either.

CFRA: Well in fact the auditor general has said that you have gone before the regulator and you have asked for increases before and your record when it comes to things like reliability, the number of outages, how long those outages last is not a great record sir.

PUGLIESE: Well and on the distribution side it's an area that is not a good record and we're trying to improve it. And one of the ways that we improve that is by having to inject capital, as I mentioned, back into the system into these things again with managing it, right--?

CFRA: I'm trying not to be difficult sir. But I.

PUGLIESE: No, I understand.

CFRA: I want to ask you-- this is a big deal here, and I want to ask you some serious questions because--

PUGLIESE: Sure.

CFRA: A lot of people want to want some answers okay. Could you not also raise capital the same way you're raising capital right now to buy this American company, through the capital markets; by issuing common shares to the stock market or by auctioning off debt through the bond market? You could raise capital that way couldn't you?

PUGLIESE: Yes you could, but this is the point I guess I'm trying to make is to ensure that we're comparing-- we're making the right distinction between these two issues we're talking about. One is what we're doing in our rate filing to improve the system in Ontario. Irrespective of where we raise that money we still have to inject it into the system and it still needs to be recovered because of the way the model works. In Ontario it's a cost recovery model. And so that money would still need to be injected and we have that capital available to us from our current financing and that's what we're suggesting to the OEB be we put in so that we can continue to service the people of Ontario. The advantage that a deal like buying Avista makes for me, and when I say-- or for us, when I say it's strategic is this: the fact that now we purchased another entity that is in a very similar business to ours, even though it's not contiguous to Ontario, is it gives us now supply chain efficiencies. We now are going to be buying more polls together, more copper wire together, more transformers, more insulators, more steel towers. That advantage and purchasing power now can come back in a savings into both of our businesses and can be returned right back to the customer because our intention is to make this operation more and more efficient. And with this rate filing that's in front of the OEB today, it's what's called-- there's what's called an incentive rate mechanism there which means that whatever savings that we carve out of our business and efficiencies, we return back to our customers in the form of savings. And I'll give you one example of that. In 2017, our distribution rates were flat because we carved out several millions of dollars in 2017 in cost savings that we returned right back to the customer. So our focus here at Hydro One; we understand the challenges in Ontario. We are all over the affordability issue. We were very instrumental in making suggestions on the Fair Hydro Plan and we've been out in communities, we've been talking to customers. We are trying to be a very fair, efficient operation and we're trying to return back as many savings as we can back to our customers along with good service and reliable service. And this deal helps us to do that, hence the reason I mentioned it was strategic up front.

CFRA: One more question sir--

PUGLIESE: Yeah.

CFRA: And you've been very generous with your time today. Ferio Pugliese, Executive Vice-president Consumer Care, Corporate Affairs, Hydro One. Tell me about the coal operations of Avista.

PUGLIESE: Yeah, Avista has a-- I'll give you just a sense. They are in generation. As you know, Hydro One is not in generation. Roughly 5-per-cent of their whole asset mix is generation; it's a combination of things. They have a minority interest, a 10-per-cent minority interest in coal generation in the state of Montana--

CFRA: Colstrip, right?

PUGLIESE: It's called Colstrip. It employs roughly 3,000 people and, as I mentioned, it's a minority interest that they have in that operation.

CFRA: Okay, that operation has been described by the EPA in the United States as the largest producer of greenhouse gases in the entire northwestern United States and the 15th worst greenhouse gas polluter in the entire United States of America. So Hydro One is going to control this company now, do you plan to maintain that asset?

PUGLIESE: No decisions as of yet with respect to that. We're in the early stages of this transaction. The transaction actually isn't consummated completely yet and that won't be the case until late 2018. So we have a lot of time to explore and, you know, have discussions and review of all of the assets that we're going to be taking on.

CFRA: But you know sir, you know the political environment very well and that it has been a source of pride for some people that we don't make electricity from coal in Ontario. But now the most important utility in electricity in Ontario, Hydro One, is buying a major coal generating station in the United States. How do you think that looks?

PUGLIESE: Yeah, I would again, I'm going to stress that the interest that Avista has in that operation is very-- it's a passive and a minority share in it.

CFRA: Okay.

PUGLIESE: At this stage of the game we're very new to making this acquisition. We-- the acquisition is not consummated until such time as the regulators approve. And when that takes place we-- again, we will have a more fulsome review of the assets that we will be taking into our control and we'll have a review at that point in time.

CFRA: Thank you Mr. Pugliese. Good to hear from you sir.

PUGLIESE: Thank you. Thanks for having us.

CFRA: Bye-bye. That is Ferio Pugliese, Executive Vice-president at Hydro One.