



EB-2005-0257

IN THE MATTER OF the *Ontario Energy Board Act, 1998*,
S. O. 1998, c.15, Schedule B;

AND IN THE MATTER OF an application by Veridian
Connections Inc. and Gravenhurst Hydro Electric Inc. under
section 86 of the *Ontario Energy Board Act, 1998* seeking leave
for Veridian Connections Inc. to acquire all outstanding shares in
and subsequently to amalgamate with Gravenhurst Hydro Electric
Inc., and for related orders.

BEFORE

Gordon Kaiser
Vice Chair and Presiding Member

DECISION AND ORDER

The Application

On March 24, 2005, Veridian Connections Inc. (“VCI”) and Gravenhurst Hydro Electric Inc. (“GHEI”) (collectively, the “Applicants”) filed an application with the Ontario Energy Board (the “Board”) under section 86 of the *Ontario Energy Board Act, 1998* (the “Act”) seeking leave for VCI to acquire all outstanding shares in and subsequently to amalgamate with GHEI (the “Application”). The Application also seeks, as of a date to be notified by the Applicants, the cancellation of VCI’s and GHEI’s electricity distribution licences under section 77(5) of the Act, and the issuance of a new electricity distribution licence under section 60 of the Act to the corporation created through the amalgamation of VCI and GHEI.

Both VCI and GHEI are licensed electricity distributors.

VCI owns, operates and manages assets associated with the distribution of electricity within the geographic territory and municipal boundaries as outlined in Schedule 1 of its electricity distribution licence ED-2002-0503. VCI's licensed service area covers all or a portion of the City of Pickering, the Municipality of Clarington, the City of Belleville, the Township of Ajax, the former Villages of Beaverton and Cannington and the former Police Village of Sunderland (now part of the Township of Brock in the Region of Durham), the former Town of Port Hope (now part of the Town of Port Hope and Hope in Northumberland County), the former Town of Uxbridge (now part of the Township of Uxbridge in the Region of Durham) and the Town of Port Perry. VCI is wholly owned by Veridian Corporation, which in turn is owned by the City of Pickering, the Municipality of Clarington, the City of Belleville and the Township of Ajax.

GHEI owns, operates and manages assets associated with the distribution of electricity within the geographic territory and municipal boundaries as outlined in Schedule 1 of its electricity distribution licence ED-2002-0576. GHEI's licensed service area covers the Town of Gravenhurst and certain surrounding areas. GHEI is owned by Gravenhurst Power Inc., which in turn is wholly owned by the Town of Gravenhurst.

According to documentation filed with the Application, all internal approvals necessary to enable the parties to enter into the agreement that underlies the transactions contemplated in the Application have been obtained.

VCI does not intend to undergo any immediate rate harmonization, but rather will maintain a separate rate schedule for Gravenhurst urban and suburban customer classes. VCI has indicated that it will consider rate harmonization, in accordance with the Board's Electricity Distribution Rate Handbook and any other Board requirements, following the completion of a cost allocation study. If rate harmonization occurs, it will not take place until 2007.

A Notice of Application and Written Hearing was published as directed by the Board. Mr. Ross Ashforth, Mr. William Black, Ms. Diane Cross and Mr. Keith Cross, Mr. Peter Sutherland and a committee of ratepayers in the Town of Gravenhurst (the “Committee”) (collectively, the “Intervenors”) have been granted intervenor status in respect of the Application.

The full record of this proceeding is available for review at the Board’s offices. While the Board has considered the full record, the Board has summarized and referred only to those portions of the record that it considers helpful to provide context to its findings.

The Interventions

The concerns expressed by the Intervenors were varied, but can generally be described as falling within four categories of issues. The first is concerns relating to the process surrounding the negotiation of the transactions contemplated in the Application, including allegations that the proper process was not followed; that there was inadequate public consultation on, and public disclosure about, the proposed transactions; and that the seller was motivated by purposes unrelated to the interests of electricity consumers. The second is concerns relating to the purchase price and, more specifically, that the price payable for the shares of GHEI is too low. The third is concerns relating to the loss to the municipality of revenue from the operations of GHEI, and the impact of that loss on taxpayers in the community, as well as to the loss of local control over the operations of GHEI. The fourth is that inadequate consideration may have been given to other more advantageous potential bids or alternatives to the sale of GHEI. The fifth is that public opinion in the Town of Gravenhurst is strongly against the transactions.

The Committee also noted that it could not reach any conclusions about whether the transactions contemplated in the Application are in the best interests of ratepayers

without further information about the transactions and an open and transparent examination of all of the relevant facts.

Mr. Ashforth raised the further issue of whether the capital expenditure plan proposed by VCI in relation to the operations of GHEI was adequate as it only covered a five-year period. He also questioned whether VCI's proposed capital expenditures were directly comparable to those already proposed by GHEI, as it was not clear whether those proposed by VCI are net of developer contributions and government grants.

Two of the Intervenors requested that the Application proceed by way of oral hearing.

In addition to the submissions of the Intervenors, the Board received several letters of comment objecting to the transactions contemplated in the Application. Many of the objections contained in those letters of comment reflect the concerns expressed by the Intervenors. In addition, some of the letters of comment raise concerns regarding potential increases in rates in the GHEI service area, in part as a result of attempts by VCI to recover the monies spent on the acquisition of GHEI. One of the letters of comment expresses a concern about reduced reliability in the event that the transactions contemplated in the Application are approved.

Procedural Order No. 1

On June 21, 2005, the Board issued its Procedural Order No. 1 in this proceeding. The Procedural Order made provision for a hearing by the Board on two matters; namely, (a) the issues that are relevant to the matter to be decided in the Application; and (b) the need for further evidence to be filed by VCI and GHEI, and the appropriate discovery process. The Procedural Order also established a deadline for filing written submissions on these two matters, and allowed an opportunity for any Intervenor that had not already done so to indicate by letter whether it intends to make a request for an award of costs. On June 23, 2005 a letter was filed with the Board by GHEI and the Town of Gravenhurst relating to the matters addressed in Procedural Order No. 1. On

June 28, 2005, a letter was filed with the Board by the Committee in response to the letter filed by GHEI and the Town of Gravenhurst. On June 30, 2005, the parties were notified that the July 5, 2005 deadline for filing written submissions was being deferred. The process contemplated in Procedural Order No. 1 was superseded by the Procedural Order that gave rise to the combined proceeding described below.

The Combined Proceeding

On July 5, 2005, the Board issued a Procedural Order combining the Application with two others for the purpose of addressing common issues relating to the scope of the issues that the Board will consider in determining applications under section 86 of the Act. The Procedural Order combined the Application with an application by Greater Sudbury Hydro Inc. for leave to acquire shares in West Nipissing Energy Services Ltd. (EB-2005-0234) and an application by PowerStream Inc. and Aurora Hydro Connections Limited for leave for PowerStream Inc. to acquire shares in and subsequently amalgamate with Aurora Hydro Connections Limited (EB-2005-0254). The Board assigned file number RP-2005-0018/EB-2005-0234/EB-2005-0254/EB-2005-0257 to the combined proceeding.

The Procedural Order asked the parties to identify matters that they considered to be relevant to the Board's determination of applications under section 86 of the Act as well as matters they considered to be outside the scope of the Board's review. The Board also requested, without limiting the matters that the parties may wish to raise, submissions on the relevance of two specific issues:

- (i) the adequacy of the purchase price payable in relation to the proposed transaction; and
- (ii) the adequacy or integrity of, or the motivation underlying, the tendering, public consultation, public disclosure or decision-making processes associated with the proposed transaction.

The Board held an oral hearing on this matter on July 19, 2005. The Committee, Mr. Sutherland and Mr. Ashforth filed written submissions and participated in the oral hearing. Other Intervenors made written submissions with respect to the issues identified in either Procedural Order No. 1 or the Procedural Order that gave rise to the combined proceeding.

The Board issued its Decision in the combined proceeding on August 31, 2005 (the “Combined Decision”). In the Combined Decision, the Board made two significant determinations in relation to the manner in which the Board will review applications for leave to acquire shares or amalgamate under section 86 of the Act. First, the factors to be considered in deciding such applications are those identified in the Board’s objectives as set out in section 1 of the Act. Second, in deciding whether to approve a share acquisition or amalgamation transaction, the Board will use a “no harm” test. In other words, the Board will approve a transaction if it is satisfied that the transaction will not have an adverse effect in terms of the factors identified in the Board’s objectives. Based on these two findings, the Board concluded that the price payable by a purchaser is only relevant if the price is too high and creates a financial burden on the acquiring company. In such a case, there could be an adverse effect on economic viability. A price that is too low would not have an adverse effect in terms of the factors identified in the Board’s objectives. Similarly, the Board concluded that the conduct or motivation of a seller leading up to the transaction (including, for example, the amount of public consultation on, or public disclosure about, the transaction) are not in and of themselves grounds for denying the approval of a transaction. The “no harm” test looks at the effect of a transaction, not the reason for or the process preceding the transaction.

Based on the Combined Decision, with one exception all of the issues raised up to that point by the Intervenors with respect to the Application are no longer “in scope” for this proceeding, because they have been determined not to be factors relevant to the Board’s review of applications for leave to acquire shares or amalgamate under section 86 of the Act. The exception is the issue raised by Mr. Ashforth with respect to VCI’s

proposed capital expenditure plans for GHEI, which is addressed later in this Decision and Order.

On September 12, 2005, a conference call was held to allow the Board to hear the views of the parties on the following questions:

1. Does any Intervenor contest the Application on the basis of issues that remain in scope in this proceeding, based on the Board's August 31, 2005 Decision?
2. If so:
 - (a) what are those issues?
 - (b) what materials or evidence filed by the Applicants with respect to those issues does the Intervenor wish to test, and by what means? Is an oral hearing required for this purpose?
 - (c) does the Intervenor wish to have the Applicants produce further materials or evidence?
 - (d) does the Intervenor intend to produce evidence in support of its position in relation to the Application?

Representatives of the Applicants, Mr. Ashforth and Mr. Sutherland participated in the conference call. Mr. William Black and Mr. Ray Lingk, one or both of which represented the Committee, also participated in the conference call.

Each of the Intervenors participating in the conference call made submissions reiterating their earlier concerns. The Applicants responded that all of those concerns were, based on the Combined Decision, no longer in scope in this proceeding, and that

no new “in scope” issues had been raised. The Board agrees, and has therefore proceeded with its determination of the Application on that basis.

Board Findings

Section 86 of the Act provides, among other things, that leave of the Board is required before an electricity distributor can amalgamate with any other corporation. In addition, under that section no person may acquire voting shares in an electricity distributor without leave of the Board if, as a result of the acquisition, the person would hold more than 20 percent of the voting securities of the distributor.

The Combined Decision has made it clear that, in deciding whether or not to grant leave in relation to the Application, the Board must determine whether the transactions contemplated in the Application will have an adverse effect on:

- (i) the interests of consumers with respect to prices and the adequacy, reliability and quality of electricity service; or
- (ii) economic efficiency and cost effectiveness in the generation, transmission, distribution, sale and demand management of electricity or the maintenance of a financially viable electricity industry.

In the Application and other materials filed by the Applicants, the Applicants have submitted that:

- VCI projects that it will be able to operate in the GHEI service area at a cost equal to or below the current cost of operating GHEI. The consolidation and rationalization of administrative functions are expected to save up to \$93.00 per customer in annual administrative costs;

- VCI's plan for capital investments will assist with reliability and maintenance of the GHEI distribution system, with the avoidance of supply restrictions, and with increasing distribution supply capacity for future growth and rate stability for customers;
- subject to technical review, VCI intends to proceed with GHEI's 2005 capital budget plan, and has a proposed five-year capital expenditure plan for system improvements to the GHEI service area that exceeds, on an annual basis, the average net annual capital expenditures made by GHEI since 2002. With respect to Mr. Ashforth's concerns regarding the comparability of VCI's proposed capital expenditure plans with those of GHEI, VCI indicated in its reply submissions filed in relation to the combined proceeding that its five-year forecast of annual capital spending is net of developer contributions and government grants;
- VCI's capital program will enable remote monitoring and control of GHEI's distribution system. VCI's existing control centre operation, which operates 24 hours a day, 7 days a week, will assume general oversight and operating management of the distribution system, to support and augment the existing operating staff complement. This, combined with system automation improvements, is expected to generally improve electrical reliability and reduce response time to power interruptions from their existing levels, and to improve employee and public safety;
- VCI's capital spending strategy for all of its service areas includes annual investments in system automation, capacity enhancements and system enhancements to meet customer and load growth requirements, and the sustainment of the general condition of assets to meet industry standards and ensure that reliability indices remain substantially below reference points established by the Board;

- VCI will retain GHEI's current operations centre for at least ten years, with GHEI's local service centre being supported by VCI's other existing fully equipped service centres located one or two hours away;
- rates for customers in GHEI's service area are not anticipated to be higher than rate levels that would otherwise apply in the absence of the transactions contemplated by the Application;
- the transactions contemplated by the Application provide opportunities to capitalize on economies of scale and scope, as well as allowing for greater efficiency and cost maintenance through consolidation; and
- the transactions contemplated by the Application will be financed from available cash reserves and unutilized credit, and will not appreciably affect VCI's cashflow to debt ratios.

The Board also notes VCI's proposal to establish a Gravenhurst Electricity Distribution Advisory Committee that would include two representatives of the Town of Gravenhurst and that would meet quarterly to discuss and report back on issues such as service reliability levels, distribution rate equity and conservation and demand management opportunities.

Finally, the Board notes the understanding of, and acknowledgement by, the Applicants of the Board's practice in relation to the recovery in rates of the costs of acquiring another distribution utility.

In light of the above, the Board is satisfied that the transactions contemplated in the Application will not have an adverse effect in relation to the factors identified in its objectives as set out in section 1 of the Act. In other words, the Board is satisfied that the Application meets the "no harm" test.

The Board therefore approves the proposed transactions and grants leave as requested in the Application.

Cost Awards

The Board will issue a separate decision on costs for this proceeding.

THE BOARD THEREFORE ORDERS THAT:

1. Veridian Connections Inc. is granted leave to acquire all outstanding shares in, and subsequently to amalgamate with, Gravenhurst Hydro Electric Inc.
2. Notice of completion of each of the share acquisition and the amalgamation shall be promptly given to the Board.
3. The Board's leave to acquire shares and amalgamate shall expire 18 months from the date of this Decision and Order. If either the share acquisition or the amalgamation has not been completed by that date, a new application for leave will be required in order for the non-completed transaction to proceed.

Pursuant to section 6(1) of the Act, the Management Committee of the Board has delegated to Mark Garner, an employee of the Board, the powers and duties of the Board with respect to the determination of applications under section 60 and section 77(5) of the Act. Accordingly, the Board refers to Mark Garner the application to issue an electricity distribution licence to the corporation created through the amalgamation of Gravenhurst Hydro Electric Inc. and Veridian Connections Inc. and the application to cancel Gravenhurst Hydro Electric Inc.'s and Veridian Connections Inc.'s electricity distribution licences.

ISSUED at Toronto, September 16, 2005

ONTARIO ENERGY BOARD

Original signed by

Gordon Kaiser
Vice Chair and Presiding Member