****

9B18M020

FORTIS INC. AND THE $11.8 Billion ITC DECISION

Selena Shannon Pritchard wrote this case under the supervison of Professors Roderick E. White and W. Glenn Rowe solely to provide material for class discussion. The authors do not intend to illustrate either effective or ineffective handling of a managerial situation. The authors may have disguised certain names and other identifying information to protect confidentiality.

*This publication may not be transmitted, photocopied, digitized, or otherwise reproduced in any form or by any means without the permission of the copyright holder. Reproduction of this material is not covered under authorization by any reproduction rights organization. To order copies or request permission to reproduce materials, contact Ivey Publishing, Ivey Business School, Western University, London, Ontario, Canada, N6G 0N1; (t) 519.661.3208; (e)* [*cases@ivey.ca*](mailto:cases@ivey.ca)*;* [*www.iveycases.com*](http://www.iveycases.com)*.*

Copyright © 2018, Ivey Business School Foundation Version: 2018-02-01

In the late fall of 2015, Karl Smith, executive vice-president and chief financial officer (CFO) of Fortis Inc. (Fortis), a homegrown energy delivery company based in St John’s, Newfoundland and Labrador, was preparing to meet with Fortis’s leadership committee. On the agenda, was whether Fortis should make an offer to acquire ITC Holdings Corporation (ITC), the largest independent transmission utility in the United States, for US$11.8 billion.[[1]](#footnote-1) If Fortis went ahead with the offer and it was accepted, this deal would be Fortis’s most significant acquisition in its history and would mark the company’s entry into the electricity transmission industry.[[2]](#footnote-2) Smith reflected on his past 30 years with Fortis and how far the small energy company from Newfoundland and Labrador had come. The company had grown from CA$390 million in assets in 1987 to an anticipated CA$48 billion, if the ITC transaction were to proceed. The ITC deal would make Fortis one of the 14 largest public utilities by enterprise value in North America. Furthermore, the deal would increase Fortis’s U.S. presence to nine states from two, in addition to the five Canadian provinces and three Caribbean countries in which the company already operated. While the potential ITC acquisition marked a big move for Fortis, Smith wondered whether this acquisition was the best decision for the company.

Fortis’s Background

Fortis had been founded in 1987 as a holding company for the Newfoundland Light & Power Company, which had a long history dating back to 1885 and was one of Canada’s few investor-owned electricity distribution companies. After Fortis was formed, the company continued to focus on growing in electricity distribution and made its first investment, outside of the province of Newfoundland and Labrador, in Maritime Electric in Prince Edward Island, Canada. During this period, energy distribution, particularly in Canada, remained mostly publicly owned and heavily regulated. Consequently, Fortis invested in new regions when opportunities were available, in part to diversify its regulatory risk.

Starting in 1987, Fortis’s chief executive officer (CEO), Angus Bruneau, spearheaded the transformation of Fortis. Bruneau was a former academic who had been the founding dean of the Faculty of Engineering and Applied Science and later the vice-president for Professional Schools and Community Services at Memorial University of Newfoundland in St. John’s. “He [Bruneau] changed what was a very traditional utility into an exciting employee-, customer-, and community-focused company which provided many of us [with] a fulfilling career,” said Earl Ludlow,[[3]](#footnote-3) executive vice-president, Eastern Canadian and Caribbean Operations at Fortis. When Bruneau retired in 1996, Stan Marshall was named CEO of Fortis. Karl Smith noted, “Stan was the primary architect—Angus was the visionary and Stan was the architect. Stan carried that torch for so many years.”

Marshall’s primary goal for Fortis was to ensure no more than 25 per cent of the company was exposed to one regulator. Regulation of the energy industry added significant pressures to companies operating within this space. Said Smith: “This is the way regulation works. You have a regulator in the province of Alberta (for example) whose obligation is to make sure that electricity customers in Alberta pay the least amount they should for electricity. That’s all they care about.” Accordingly, the company focused on acquisitions to diversify its regulatory risk (see Exhibit 1). In 1999, Fortis made its first international investment, in Belize, where Fortis owned a 33 per cent interest in Belize Electricity as of late 2015; and in 2000, Fortis invested in the Cayman Islands, where it owned a 60 per cent interest in Caribbean Utilities on Grand Cayman, and in the Turks and Caicos, where Fortis TCI was owned 100 per cent.

During this time, Fortis also expanded into a variety of non-electricity-related subsidiaries, including the ownership of a hotel business, a real estate business, a finance business, and a partnership with AT&T Inc. The company anticipated expanding its customer service strengths from the public utility sector into these different industries. These subsidiaries were designed to reduce the company’s risk from regulatory pressures, while providing tax benefits. However, the decision was eventually made to exit these businesses and focus on energy delivery through distribution. By 2015, these non-core businesses had been sold.

In 2004, the company had made substantial investments in Western Canada, acquiring electricity distribution companies in Alberta and British Columbia from the energy company Aquila. These acquisitions were formalized into subsidiaries under the names FortisAlberta Inc. and FortisBC. In 2007, Fortis made its first investment in gas distribution with the purchase of Terasen, which was later renamed FortisBC Energy. These acquisitions were considerable for the company, and at one point FortisBC and FortisBC Energy represented 35 per cent of the company’s asset base. Given Fortis’s goal to ensure more diverse regulatory exposure, the executive team continued to consider new acquisition targets. During this time, Fortis attempted to acquire Central Vermont Public Service Corporation, an integrated electricity company in Vermont. The sale would have marked the company’s first foray into the United States, a market with substantially more investor-owned utilities. However, the deal fell through during the review period, when the sale was reopened to additional bids. Gaz Metro, another Canadian utility company, placed a higher bid and eventually acquired Central Vermont Public Service Corporation for an additional premium.[[4]](#footnote-4)

Fortis continued to target investments in the United States, recognizing the lack of viable targets in Canada. In 2012, Fortis announced its first American acquisition, the CH Energy Group Inc., the parent company of an electricity and gas distributor in the state of New York, for $1.5 billion. The 2013 acquisition of Arizona-based UNS Energy Corp., the parent company of a vertically integrated electric utility and a gas distribution utility, for $4.3 billion followed. The following year, 2014, marked the retirement of Stan Marshall. Under his leadership, Fortis’s assets had grown from CA$1 billion in 1996 to CA$26 billion. Upon Marshall’s retirement, Barry Perry, the company’s vice-president of Finance and its CFO, was named CEO.

While the majority of Fortis’s subsidiaries were regulated, the company also operated several non-regulated entities, including Fortis Generation, which comprised power generation facilities in British Columbia and Belize. In 2015, these non-regulated entities contributed a little less than 10 per cent of the company’s earnings (see Exhibit 2).

fortis’s Financial Situation

Through its history of acquisitions, Fortis had continued to post consistent financial results. Smith expected the ITC acquisition to be completed by October of 2016. If the deal were to close on that timeline, Fortis anticipated having CA$6.838 billion in fiscal 2016 revenue (given that Fortis would have owned ITC for only two and one-half months by Fortis’s fiscal year-end) up from CA$6.757 billion the year before. Fortis had historically delivered its shareholders sustained dividends, attaining a 9 per cent compound annual growth rate on dividends over the past 10 years. Over the past 43 years, Fortis had delivered an increased dividend payment to shareholders every year, among the longest records for continuous dividend payments by any public company in Canada. If the ITC acquisition was completed, Fortis anticipated its financials to include a 22 per cent increase to its adjusted earnings and a 5 per cent increase to its adjusted earnings per share (EPS) year-over-year after 2016 (see Exhibits 3 and 4).

Fortis had delivered above-normal performance for its industry. Total shareholder returns over the 10-year period from 2006 to 2016 were 8.3 per cent annually. In the same period, the S&P 500 utility sector had returned 7.4 per cent, and the TSX Utilities Index had returned 4.8 per cent.

ITC Background

ITC, Fortis’s acquisition target, had been founded in 1999, as a subsidiary of Detroit Edison and operated primarily in the U.S. Midwest. ITC had changed ownership and structures several times and by 2003 had become the first independent electricity transmission company in the United States. ITC operated across Iowa, Michigan, Minnesota, Illinois, Missouri, Kansas, and Oklahoma.[[5]](#footnote-5) ITC and its subsidiaries—Michigan Electric Transmission Company, ITC Midwest, and ITC Great Plains—faced regulations and rate setting from the Federal Energy Regulation Commission (FERC). ITC was headquartered in Novi, Michigan; became publicly listed in 2005; and had assets of nearly $7.4 billion.

Prior to the deal announcement by Fortis, ITC shares had been trading at around $40 per share, and the company had a market capitalization around $10.5 billion. In 2015, ITC delivered $1,045 million in revenue, up from $1,023 million in 2014 and $941 million in 2013. ITC had also delivered year-over-year increased earnings per share, growing from $1.49 per share in 2013 to $1.57 per share in 2015. Over the past five years, ITC had also delivered above-normal results in the capital markets, delivering returns 15 per cent above the S&P 500 Index and 22 per cent above the Dow Jones U.S. Utilities Index.[[6]](#footnote-6)

When asked why Fortis should acquire ITC, given it would be Fortis’s first foray into the transmission industry, Smith said:

ITC has a great franchise and is very well managed. It is a company we have been following for years but was valued too high to make an acquisition work. When their premium valuation disappeared, it made the transaction doable. We love the regulation of transmission assets in the United States—higher returns and no regulatory lag. Transmission is not that different than distribution from an operations perspective.

When asked to explain regulatory lag, Smith described it as follows:

Regulatory lag refers to the time it takes to get through the regulatory process and have new rates approved. Some jurisdictions look at historical costs and some look ahead. As our industry is very capital-intensive, in jurisdictions that look backwards (e.g., Arizona), we may have invested significant capital without commensurate revenue to compensate for it.

ITC is regulated by the FERC, which trues up costs and investments every year and provides new revenue to compensate for the same. We refer to it as “real time” rates. The less regulatory lag, the quicker we recoup our investment.

If the ITC acquisition were to go through, it would mark the first time in its history that more than half of Fortis’s assets and roughly 62 per cent of the company’s earnings would come from the United States.[[7]](#footnote-7) The deal also would enlarge the company from about 7,700 employees to 8,800 employees.

Electricity and Gas Distribution

Fortis considered itself an energy delivery company (i.e., a distribution company), operating primarily in the delivery of electricity and gas. The ITC acquisition would move Fortis heavily into the transmission segment of the electricity business (see Exhibit 5).

The energy delivery industry for both electricity and gas comprised three different stages—generation and production, longer-distance transmission, and local distribution (see Exhibit 6). Both private, investor-owned companies and public, government institutions operated in parts, or all, of the system. In some jurisdictions, energy delivery was fully integrated and run by government-owned entities. In others, each aspect from generation, transmission, distribution, and retailing was owned and operated by different investor-owned companies, with various government regulators establishing the base rates and the production and transmission volumes. As Smith explained, “The regulatory construct between a company and the regulator and its customers, basically, is that in return for running a utility well the regulator will let you earn a reasonable return.”

Local distributors received their energy through transmission companies and distributed it locally. In Canada, electricity was traditionally distributed by local publicly owned utility commissions. Increasingly this segment of the industry was consolidating and being privatized. The transmission segment of the electricity delivery industry had been owned and regulated along provincial and territorial jurisdictions. While some privatization had occurred beginning in the 1990s, most transmission utilities were still Crown-owned corporations. The most significant privatization had occurred in Ontario and Alberta. Both operated electricity markets that opened components of the energy generation and delivery process to private ownership and, when possible, competitive markets. Newfoundland and Labrador, the Northwest Territories, Yukon, British Columbia, Saskatchewan, Manitoba, Quebec, and New Brunswick had Crown-operated generators but relied on investor-owned distributors, such as Fortis. Nova Scotia was the only province that had completely divested all of its energy holdings and had granted a virtual monopoly to Nova Scotia Power, Inc.[[8]](#footnote-8)

In Canada, the generation and sale of natural gas (but not its transmission and distribution) were deregulated, starting in the mid-1980s.[[9]](#footnote-9) This change had created open marketplaces in many provinces; however, incumbent distributors were able to effectively fight off competition in open markets and the majority of provinces still had few competitive options for consumers.[[10]](#footnote-10)

In the United States, electricity generation and distribution had become increasingly complex, as 16 states were deregulated to some extent, while other states had a variety of regulatory policies that governed the electricity industry. No state, however, was fully deregulated.[[11]](#footnote-11) In addition, the U.S. federal government provided policy guidance through the Department of Energy, the Environmental Protection Agency, and the Federal Trade Commission. Deregulation had initially caused chaos in some early adopter states, including California, during the Enron scandal. As a result of such issues, many states had halted deregulation proceedings.

The deregulation of the sale of natural gas at the wellhead source had begun in full in 1989 with the passing of the *Natural Gas Wellhead Decontrol Act*. This legislation enabled natural gas producers to sell at any price, free of regulation to the “first sale,” whether to a pipeline company, a local distributor, or directly to the end-user.[[12]](#footnote-12)

Industry Trends

Over the past five years, large players within the electricity industry continued to consistently grow their asset bases through both investment and acquisitions (see Exhibit 7). While Ontario Power Generation remained a pure-play generation company, other major players in both Canada and the United States maintained operations in more than one segment of the energy creation and distribution business. As noted in Exhibit 7, other large electricity utility companies in Canada and the United States (outside of Ontario Power Generation) operated in transmission, while Fortis operated primarily in distribution with a few generation assets.

Demand for energy at a global level was consistently increasing. By 2050, it was expected that demand for electricity would account for 25 per cent of all energy demand, up from 18 per cent to date. According to research performed by McKinsey & Company, wind and solar energy generation would account for 77 per cent of the new generation capacity that would be required. However, 71 per cent of the new energy demand would come from China and India, while European and North American demand was expected to decline.[[13]](#footnote-13) This expected growth led to increased investment in the energy industry from private firms. From 2012 to 2017, it was expected that private equity firms would have invested more than $200 billion into the energy industry, investing in both traditional energy companies and innovative technologies.[[14]](#footnote-14)

Fortis’S Company Structure

Fortis allowed its subsidiaries a tremendous amount of autonomy in their respective operations. Additionally, the company strove to provide certainty to its subsidiaries upon acquisition by maintaining their existing leadership wherever possible. Fortis focused on extending influence over its subsidiaries by placing senior Fortis leaders on the respective boards of the acquired companies. Fortis would also seek to cross-pollinate its leadership, inviting senior leaders of its subsidiaries, to sit on the boards of other Fortis subsidiary companies. As Smith noted:

The way we run our business is an ongoing conversation. We don’t have regularly scheduled meetings. Around here, we manage by walking into each other’s offices and talking. Every week I will probably talk to each of our [subsidiary] CFOs. Barry [Barry Perry, Fortis’s CEO] will definitely talk to each of our [subsidiary] CEOs. That’s the culture of how we run our business.

Executives of the subsidiaries were said to have tremendous autonomy. Reporting requirements to Fortis were minimal. However, Smith noted that the subsidiaries’ ownership by Fortis led to “more tools at their disposal in the bigger enterprise and, therefore, we’d like to think they are better at managing their businesses as a consequence of our ownership.” Fortis also would act as a cushion between the board of the subsidiary and the subsidiary’s management, by positioning members of Fortis’s senior management team on the subsidiary boards and, when necessary, by advocating on behalf of the subsidiary’s management.

Smith noted that influence at the subsidiary board level from experienced Fortis leaders was especially important in the electricity industry:

Most other businesses share some common aspects, but the electric utility business because of the significant amount of regulatory oversight and the fact that people think it is a public good—it is so different than anything else. So it’s hard to be intuitive about the electric utility business—I’ve seen this so many times over the years where a new board member comes on—and we see them in Newfoundland Power, we see them in other companies, and they are sitting there saying, “How does that work?”

Talent Development

Fortis generally did not move talent across subsidiaries in an attempt to support each subsidiary acting as a separate entity with its own respective succession and talent development plans. However, Fortis’s head office was able to exert significant influence on the selection of executives for its subsidiaries, through its membership on their respective boards (see Exhibit 8). In Fortis’s history, there had been a few occasions where a high-potential employee was suited for a role in a different subsidiary, and that employee was able to apply for that role when it became open, as long as the role fell within the employee’s individual leadership development plan. In general, Fortis encouraged talent development and liked to see some talent move across its subsidiaries, but doing so was difficult and happened rarely.

Fortis also encouraged information sharing between its subsidiaries by having the senior leaders meet regularly to focus on topics that impacted all of its subsidiaries, such as safety and corporate communications. When it came to assigning promotions, Fortis’s senior leadership preferred to lead through influence at the board level of its subsidiaries. However, as Smith noted: “We do have a role and a say but the approach we take is one of convincing them rather than ordering them.”

Compensation

Compensation at the executive level within the subsidiaries was tied to several metrics, including Fortis’s financial performance and the overall safety, reliability, and customer service performance of their respective organization. The payout of their compensation was both in a base salary and in an annual cash-based, short-term incentive; a long-term stock incentive of either stock options or performance shares; full-career performance tied to an employee share purchase plan; and a matching program for a registered retirement savings plan. At the corporate level, senior executives’ compensation was more significantly tied to total shareholder return (TSR). For example, over a three-year period, the TSR would contribute approximately 25 per cent of the compensation for the CEO of FortisBC; over the same period, the TSR would contribute closer to 70 per cent of the compensation for a Fortis executive. This compensation structure was designed to ensure that the compensation of senior executives at the respective subsidiaries would be connected to the overall performance of Fortis, but more closely tied to the results they individually controlled.

Investment Decisions

As Smith reflected on the industry today, he noted the consistent consolidation that was occurring, primarily in the United States: “When we started traipsing around the United States about 10 years ago, there were over 100 investor-owned utilities in the United States compared to three in Canada. Today, we are down to about 40 in the United States.” The active consolidation had created an opportunity for Fortis to make a variety of acquisitions.

In addition, because energy distribution was a capital-intensive industry, in 2016, Fortis expected to spend CA$2.1 billion on capital improvements and expansion and expected to spend CA$13 billion over the next five years. The company also had two large development projects in the pipeline through its FortisBC and FortisOntario subsidiaries. Both projects were still in the early stages and were not expected to be operational until early 2020. Furthermore, the FortisOntario project was not expected to be approved by regulatory boards until early 2017.

Despite Fortis’s success to date, Smith recognized the risk. Every investment needed to balance the demands of the shareholders, customers, acquisition targets, and regulators. Internally, Fortis was clear its growth and market capitalization should be greater than the average of other North American energy utilities of a similar size and that its risk tolerance should be no greater than any other North American utility of a similar size. In short, the company wanted to structure itself like a singularly well-run utility that enjoyed the diversification of risk brought on by operating in a variety of regulatory landscapes.

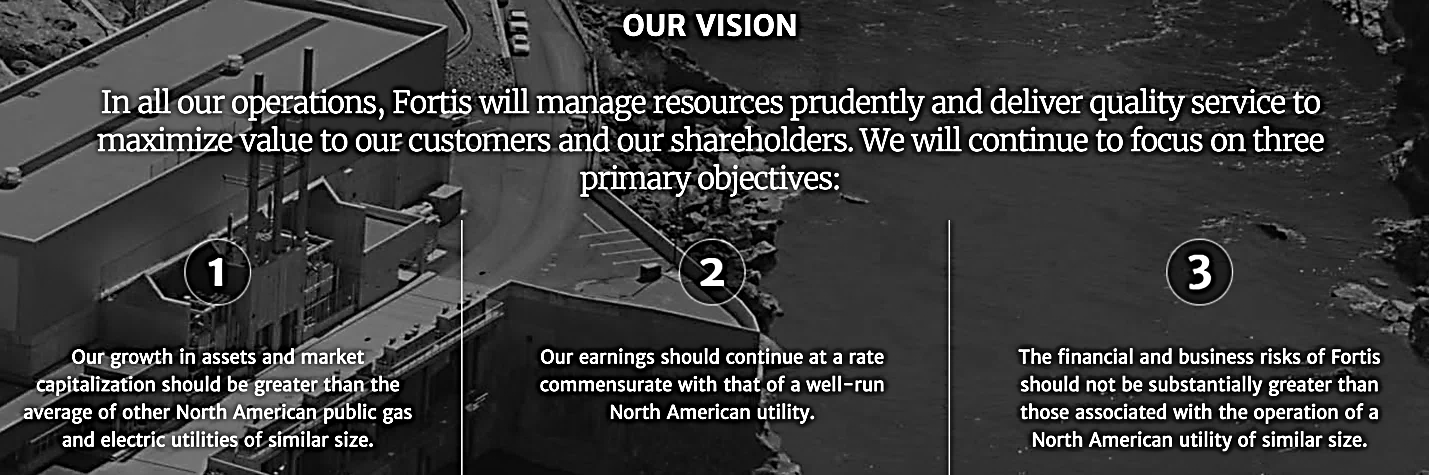
Fortis was intentional in marketing the sale of its shares toward sophisticated investors, who were well versed in the industry. To those investors, focused diversification was a strong selling feature, and, according to Smith, “Of all the utilities in our sector, we believe that we are probably the most diversified.”

The ITC deal was structured such that Fortis would incur $6.4 billion in incremental debt, $4.4 billion of which was ITC debt assumed on acquisition and $2 billion of debt issued by Fortis in exchange for cash to complete the deal. Fortis would also need to issue an additional 115 million shares to buy out the current shareholders of ITC, representing a 41 per cent increase of shares to Fortis. Fortis, however, was expected to maintain a consistent investment grade rating of A– from S&P. The deal was also expected to be accretive by approximately 5 per cent to Fortis’s 2017 EPS.[[15]](#footnote-15) The deal was supported by ITC’s board; however, the deal still needed regulatory approval from the FERC and the individual state regulators from Iowa, Michigan, Minnesota, Illinois, Missouri, Kansas, and Oklahoma.

The ITC Decision

The ITC acquisition marked a significant investment for the homegrown Fortis—the largest in its history. Not only would this acquisition move a significant portion of the company’s operations into the United States but it would also considerably alter the makeup of the organization. Smith was confident in Fortis’s ability to manage acquisitions, given the company’s long history, and he knew that Fortis’s investors looked favourably upon the company becoming more diversified from a regulatory risk perspective. However, the ITC deal still held considerable risk, considering the cost of the transaction, the new regulatory environment, and the fact that ITC operated in transmission, in which Fortis had no previous experience, not to mention that the deal required approval by the U.S. federal regulatory bodies. The question remained: should Fortis move forward with this deal, or was taking on ITC too big a risk?

Exhibit 1: Fortis’S Values

****

Source: Company documents.

Exhibit 2: Fortis’s Subsidiary Summary

Part One: Fortis’s Regulated Subsidiaries Customers, Earnings, and Assets,(as expected with the ITC acquisition)

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|  | **2015 Customers (#)** | **2015**  **Earnings (CA$ millions)** | **2015**  **Assets (CA$ billions)** | **2016 Customers (#)** | **2016**  **Earnings (CA$ millions)** | **2016**  **Assets (CA$ billions)** |
| **ITC** | N/A | N/A | N/A | N/A | 59 | 18 |
| **UNS Energy** | 663,000 | 195 | 8.9 | 669,000 | 199 | 8.9 |
| **Central Hudson** | 379,000 | 58 | 3.2 | 379,000 | 70 | 3.2 |
| **FortisBC**(1) | 1,150,000 | 190 | 8.1 | 1,164,000 | 205 | 8.4 |
| **Fortis Alberta** | 539,000 | 138 | 3.8 | 549,000 | 121 | 4.1 |
| **Eastern Canadian**(2) | 405,000 | 62 | 2.3 | 408,000 | 64 | 2.4 |
| **Caribbean Electric**(3) | 42,000 | 34 | 1.3 | 44,000 | 46 | 1.3 |
| **Total** | 3,178,000 | 677(4) | 27.6 | 3,213,000 | 764 | 46.3 |

Note: N/A = not applicable; (1) FortisBC includes FortisBC Energy and FortisBC Electric; (2) Eastern Canadian includes Newfoundland Power, Maritime Electric, and FortisOntario; (3) Caribbean Electric includes Caribbean Utilities (specifically 100 per cent of Caribbean Utilities’ operational data and the earnings attributed to Fortis through Fortis’s 60 per cent ownership of the company), Fortis Turks and Caicos, and 33 per cent equity investment in Belize Electricity; (4) 2015 earnings total includes gains on the sale of Fortis’s power generation facilities in Ontario in 2015.

Source: Company documents.

Exhibit 2 (continued)

Part Two: Fortis’s Non-regulated Subsidiaries, Customers, Earnings, Assets,(as expected with the ITC acquisition)

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | **2015 Earnings**  **(CA$ millions)** | **2015 Assets**  **(CA$ billions)** | **2016 Earnings**  **(CA$ millions)** | **2016 Assets**  **(CA$ billions)** |
| **Non-Regulated Energy Infrastructure** | 77 | 1.0 | 60 | 1.5 |

Source: Company documents.

Exhibit 3: Summary of Fortis Inc.’s Financial Results, 2012–2016

(For Years Ended December 31)

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | **2012** | **2013** | **2014** | **2015** | **2016 (with ITC acquisition completing in October)** |
| **Total Assets (CA$ billions)** | 15.0 | 17.9 | 26.2 | 28.8 | 47.9 |
| **Total Revenue (CA$ millions)** | 3,654 | 4,047 | 5,401 | 6,727 | 6,838 |
| **Net Earnings (CA$ millions)** | 371 | 420 | 390 | 840 | 713 |
| **Basic Earnings per Common Share (CA$)** | 1.66 | 1.74 | 1.41 | 2.61 | 1.89 |
| **Dividend per Common Share (CA$)** | 1.20 | 1.24 | 1.28 | 1.40 | 1.53 |
| **Dividend Payout Ratio (%)** | 72.3 | 71.3 | 90.8 | 53.6 | 81.0 |
| **Long-Term Debt Offerings (CA$ millions)** | 125 | 657 | 1,200 | 1,000 | 4,100 |

Source: Company documents.

Exhibit 4: Fortis’s Consolidated Income Statement and Balance Sheet

**Consolidated Results of Operations (Year Ending December 31, CA$ Millions)**

|  |  |  |
| --- | --- | --- |
|  | **2015** | **2016 (With ITC completing in October)** |
| **Revenue** | **6,757** | **6,838** |
| Energy Supply Costs | 2,591 | 2,341 |
| Operating Expenses | 1,874 | 2,031 |
| Depreciation and Amortization | 873 | 983 |
| Other Income (Expenses), Net | 197 | 53 |
| Finance Charges | 553 | 678 |
| Income Tax Expense | 223 | 145 |
| **Net Earnings** | **840** | **713** |
| **Net Earnings Attributable to** |  |  |
| Non-Controlling Interests | 35 | 53 |
| Preferred Equity Shareholders | 77 | 75 |
| Common Equity Shareholders | 728 | 585 |
| **Net Earnings** | **$840** | **$713** |

Exhibit 4 (continued)

**Consolidated Balance Sheet (Year Ending December 31, CA$ Millions)**

|  |  |  |
| --- | --- | --- |
| **ASSETS** | **2015** | **2016 (With ITC)** |
| **Current assets** |  |  |
| Cash and cash equivalents | 242 | 269 |
| Accounts receivable and other current assets | 964 | 1,127 |
| Prepaid expenses | 68 | 85 |
| Inventories | 337 | 372 |
| Regulatory assets1 | 246 | 313 |
| **Total Current Assets** | **1,857** | **2,166** |
| **Other assets** | 352 | 406 |
| **Regulatory assets**1 | 2,286 | 2,620 |
| **Utility capital assets** | 19,595 | 29,337 |
| **Intangible assets** | 541 | 1,011 |
| **Goodwill** | 4,173 | 12,364 |
| **Total Assets** | **28,804** | **47,904** |
|  |  |  |
| **LIABILITIES AND SHAREHOLDERS’ EQUITY** |  |  |
| **Current liabilities** |  |  |
| Short-term borrowings | 511 | 1,155 |
| Accounts payable and other current liabilities | 1,419 | 1,970 |
| Regulatory liabilities | 298 | 492 |
| Current installments of long-term debt | 384 | 251 |
| Current installments of capital lease and finance obligations | 26 | 76 |
| **Total current liabilities** | **2,638** | **3,944** |
| **Other liabilities** | 1,152 | 1,279 |
| **Regulatory liabilities** | 1,340 | 1,691 |
| **Deferred income taxes** | 2,050 | 3,263 |
| **Long-term debt** | 10,784 | 20,8172 |
| **Capital lease and finance obligations** | 487 | 460 |
| **Total liabilities** | **18,451** | **31,454** |
| **Shareholders’ equity** |  |  |
| Common shares | 5,867 | 10,762 |
| Preferred shares | 1,820 | 1,623 |
| Additional paid-in capital | 14 | 12 |
| Accumulated other comprehensive income | 791 | 745 |
| Retained earnings | 1,388 | 1,455 |
| **Total Fortis Inc. shareholders’ equity** | 9,880 | 14,597 |
| **Non-controlling interests** | 473 | 1,853 |
| **Total liabilities and shareholders’ equity** | **28,804** | **47,904** |

Note: (1)Regulatory assets and liabilities arise as a result of the rate-setting process at the regulated utilities and have been recognized based on previous, existing or expected regulatory orders or decisions. (2) The increase was mainly due to the issuance of long-term debt at the corporation to finance a portion of the acquisition of ITC, the acquisition of Aitken Creek, and the redemption of First Preference Shares, Series E. Issuances of long-term debt at the regulated utilities, largely in support of energy infrastructure investment, were partially offset by regularly scheduled debt repayments and the impact of foreign exchange on the translation of U.S. dollar-denominated debt.

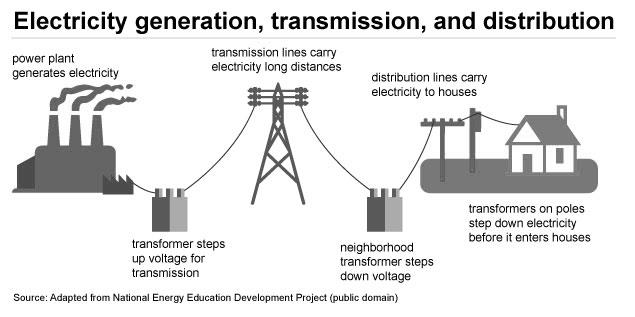
Source: Company documents.

Exhibit 5: Fortis Inc.’s Utility Capital Assets (Expected with ITC acquisition)

|  |  |
| --- | --- |
| **Capital Asset** | **Cost (in CA$ billions)** |
| Electrical Distribution | 9,245 |
| Gas Distribution | 3,829 |
| Electric Transmission | 3,093 |
| Gas Transmission | 1,735 |
| Generation | 6,465 |
| Assets Under Construction | 889 |
| Land | 186 |
| Other | 2,429 |

Source: Company documents.

Exhibit 6: Electricity Distribution



Source: “Electricity Explained: How Electricity is Delivered to Consumers,” EIA: U.S. Energy Information Administration, accessed June 18, 2017, https://www.eia.gov/Energyexplained/index.cfm?page=electricity\_delivery.

Exhibit 7: Select Electricity Companies in Canada and the United States: Assets and Industry Function 2011 versus 2015 (in $ billions)

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **Company** | **Country** | **Assets 2011** | **Assets Base 2015** | **Industries 2011** | **Industries 2015** |
| Hydro Quebec | Canada | CA$69.64 | CA$75.20 | Generation, Transmission, Distribution, Construction | Generation, Transmission, Distribution, Construction |
| Pacific Gas & Electric | United States | US$49.75 | US$63.34 | Generation, Transmission, Distribution | Generation, Transmission, Distribution |
| Edison International | United States | US$48.04 | US$49.87 | Generation, Transmission, Distribution | Generation, Transmission, Distribution |
| Consolidated Edison | United States | US$39.21 | US$45.64 | Generation, Transmission, Distribution | Generation, Transmission, Distribution |
| Ontario Power Generation | Canada | CA$32.14 | CA$44.30 | Generation | Generation |
| Georgia Power | United States | US$27.15 | US$32.87 | Generation, Transmission, Distribution | Generation, Transmission, Distribution |
| BC Hydro | Canada | CA$19.48 | CA$27.75 | Generation, Transmission, Distribution | Generation, Transmission, Distribution |
| Hydro One | Canada | CA$18.37 | CA$24.33 | Transmission, Distribution | Transmission, Distribution, Telecom |
| Enmax | Canada | CA$4.33 | CA$5.16 | Generation, Transmission, Distribution | Generation, Transmission, Distribution |

Source: All sources accessed August 12, 2017, Hydro Quebec, www.hydroquebec.com/publications/en/corporate-documents/annual-report.html; PG&E Corporation, http://investor.pgecorp.com/financials/annual-reports-and-proxy-statements/default.aspx; ConEdison, Inc., http://phx.corporate-ir.net/phoenix.zhtml?c=61493&p=irol-reportsannual; Edison International, www.edison.com/home/investors/sec-filings-financials/annual-reports.html; Ontario Power Generation, www.opg.com/about/finance/pages/financial-reports.aspx; Georgia Power, https://www.georgiapower.com/about-us/facts-and-financials/financial-annual-reports.cshtml; BC Hydro, https://www.bchydro.com/about/accountability\_reports/financial\_

reports/annual\_reports.html; Hydro One, www.hydroone.com/InvestorRelations/FinancialReporting/Pages/Default.aspx; Enmax, https://www.enmax.com/about-us/reports-and-publications.

Exhibit 8: Fortis Board of Directors Coverage

The following lists summarize the Fortis leadership sitting on subsidiary boards (as expected if ITC deal is approved and finalized).

**Fortis Inc.**

Barry V. Perry (CEO, Fortis Inc.)

Tracey Ball (FortisAlberta Board)

Ida J. Goodreau (FortisBC Board)

**ITC Board**

Linda Blair (President and CEO, ITC Holdings Corp.)

James Laurito (EVP, Business Development, Fortis Inc.)

Barry V. Perry (CEO, Fortis Inc.)

Joseph Welch (Chairman ITC Board, former President/CEO, ITC Holdings Corp.)

**FortisBC Board**

Phonse Delaney (President and CEO, FortisAlberta)

Ida J. Goodreau (Fortis Inc. Board)

David G. Hutchens (CEO of Tucson Electric Power, subsidiary of UNS Energy)

Michael Mulcahy (CEO, FortisBC and FortisBC Energy)

Barry V. Perry (CEO, Fortis Inc.)

Karl W. Smith (EVP, CFO Fortis Inc.)

**FortisAlberta**

Phonse Delaney (President and CEO, FortisAlberta)

David G. Hutchens (CEO of Tucson Electric Power, subsidiary of UNS Energy)

Nora Duke (Chief Human Resources Officer and EVP Corporate Services, Fortis Inc.)

**UNS Energy**

Barry V. Perry (CEO, Fortis Inc.)

David G. Hutchens (CEO of Tucson Electric Power, subsidiary of UNS Energy)

Karl W. Smith (EVP, CFO, Fortis Inc.)

Michael Mulcahy (CEO, FortisBC and FortisBC Energy)

**Central Hudson**

Margarita Dilley (Board, Fortis Inc.)

James Laurito (EVP, Business Development, Fortis Inc.)

Barry V. Perry (CEO, Fortis Inc.)

Nora Duke (Chief Human Resources Officer and EVP Corporate Services, Fortis Inc.)

**Maritime Electric**

Earl A. Ludlow (EVP, Operations and Advisor to the President, Fortis Inc.)

John D. Gaudet (President and CEO, Maritime Electric)

Gary J. Smith (EVP, Eastern Canadian and Caribbean Operations, Fortis Inc.)

**Caribbean Utilities Company**

Gary J. Smith (EVP, Eastern Canadian & Caribbean Operations, Fortis Inc.)

Earl A. Ludlow (EVP, Operations and Advisor to the President, Fortis Inc.)

Eddington M. Powell (President and CEO, FortisTCI)

J.F. Richard Hew (President and CEO, Caribbean Utilities Company)

**Newfoundland Power**

John Gaudet (President and CEO, Maritime Electric)

Mike Mosher (President and CEO, Central Hudson Gas & Electric)

Gary Smith (EVP, Eastern Canadian & Caribbean Operations, Fortis Inc.)

Note: These board memberships do not include all board members, only those board members from Fortis and from other subsidiaries; CEO= chief executive officer; EVP = executive vice-president.

Source: Company documents.

1. All currency amounts are in US$ unless otherwise noted. [↑](#footnote-ref-1)
2. “Fortis Inc. to Acquire ITC Holdings Corp. for US$11.3 Billion,” Cision PR Newswire: News, February 9, 2016, accessed May 6, 2017, www.prnewswire.com/news-releases/fortis-inc-to-acquire-itc-holdings-corp-for-us113-billion-300217218.html. [↑](#footnote-ref-2)
3. Joan Sullivan, “In Memoriam: Engineer Angus Bruneau Led Multibillion-Dollar Utility,” *Globe and Mail*, March 26, 2017, accessed June 18, 2017, https://www.theglobeandmail.com/report-on-business/engineer-angus-bruneau-led-multibillion-dollar-utility/article34431116/. [↑](#footnote-ref-3)
4. Azam Ahmed, “Gaz Metro Bests Fortis to Buy Vermont Utility,” *New York Times*, July 12, 2011, accessed July 31, 2017, https://dealbook.nytimes.com/2011/07/12/gaz-metro-bests-fortis-to-buy-vermont-utility/. [↑](#footnote-ref-4)
5. CIBC Institutional Equity Research, February 9, 2016. [↑](#footnote-ref-5)
6. ITC Holdings Corp., *2015 Annual Report*, accessed August 20, 2017, www.annualreports.com/HostedData/AnnualReportArchive/i/NYSE\_ITC\_2015.pdf. [↑](#footnote-ref-6)
7. CIBC Institutional Equity Research, op. cit. [↑](#footnote-ref-7)
8. IEA: International Energy Agency, *Energy Policies of IEA Countries—Canada 2009 Review*, 2009, accessed July 9, 2017, https://www.iea.org/publications/freepublications/publication/canada2009.pdf [↑](#footnote-ref-8)
9. Natural Resources Canada, “Frequently Asked Questions about Natural Gas Prices,” accessed July 9, 2017, <https://www.nrcan.gc.ca/energy/natural-gas/5685#faq9>. [↑](#footnote-ref-9)
10. Direct Energy, “Energy Deregulation in the United States and Canada,” accessed May 6, 2017, https://business.directenergy.com/what-is-deregulation. [↑](#footnote-ref-10)
11. Electronic Choice, “Map of Deregulated Energy States and Markets,” accessed July 9, 2017, https://www.electricchoice.com/map-deregulated-energy-markets/. [↑](#footnote-ref-11)
12. Christopher G. Lipscombe, “Open Access to Natural Gas Transportation, Session 2,” presented at The Natural Gas Regulatory Workshop, Contonou, Benin, February 14–16, 2012, accessed May 6, 2017, http://pubs.naruc.org/pub/53724D07-2354-D714-51C9-BEF915B02FD7. [↑](#footnote-ref-12)
13. Scott Nyquist, *Energy 2050: Insights from the Ground Up*, McKinsey & Company, November 2016, accessed August 16, 2017, www.mckinsey.com/industries/oil-and-gas/our-insights/energy-2050-insights-from-the-ground-up. [↑](#footnote-ref-13)
14. Nikhil Patel, Thomas Seitz, and Kassia Yanosek, “Three Game Changes for Energy,” *McKinsey Quarterly*, April 2017, accessed August 16, 2017, www.mckinsey.com/industries/oil-and-gas/our-insights/three-game-changers-for-energy. [↑](#footnote-ref-14)
15. CIBC Institutional Equity Research, op. cit. [↑](#footnote-ref-15)