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BY COURIER

April 27, 2018

Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
Suite 2700, 2300 Yonge Street
P.O. Box 2319
Toronto, ON, M4P 1E4

Dear Ms. Walli,

EB-2014-0255 – Consultation on the Development of Corporate Governance Guidance for OEB Rate-Regulated Utilities – Hydro One Networks Inc. – Submission on Director Independence

Hydro One Networks Inc. (“Hydro One”) thanks the Ontario Energy Board (“OEB”) for the opportunity to provide comments on the OEB’s Draft Report, dated March 28, 2018, on Corporate Governance Guidance for OEB Rate-Regulated Utilities (“Draft Report”). In particular, we are writing to provide comments on the section of the Draft Report that deals with director independence.

The OEB expressed its position that utilities should have a board of directors at the utility level and a majority of those directors should be independent of the shareholder and any affiliate. The OEB expects utilities to have a board of directors that has oversight of all utility functions and is separate from the parent company. In its Draft Report, the OEB expresses its view that a director is considered independent if s/he is neither an employee nor a director of an affiliate (including the parent or holding company), nor an employee or director of the majority or controlling shareholder. The director independence portion of the Draft Report refers to the requirement in the OEB’s Affiliate Relationships Code for Electricity Distributors and Transmitters (“ARC”) that a utility must ensure that at least one third of its Board of Directors is independent from any affiliate. The OEB ultimately states that a majority (over 50 percent) of directors should be independent—a proportion of independent directors that is greater than the current requirement under the ARC.

We agree that director independence is a principle that is foundational to effective corporate governance. However, it is respectfully submitted that the OEB takes too restrictive an approach to director independence by expecting that the majority of a utility board of directors be neither an employee nor a director of an affiliate, nor an employee nor director of a majority or controlling shareholder. The application of a definition or criteria for director independence that is too restrictive, stringent and onerous will make it difficult for a utility to enlist a board that is composed of talented and competent individuals and will result in an administrative burden and potentially additional costs that may have to be borne by ratepayers.

The concept of board independence is designed to build high performance boards of directors that are able to exercise independent judgment in the best interests of the corporation, thereby contributing to a company's good corporate governance. As stated in Hydro One's September 28, 2016 comments on the Elenchus Report referred to in the Draft Report, the concept of director independence is best considered in the relevant context having regard to best corporate governance practices. In this respect, we agree with the position in the Draft Report that "the general and pervasive preference for independent directors to constitute a majority on the board is grounded in the view that this arrangement best enables the board of directors to act in the best interests of the company without undue influence."

For publicly traded companies, pursuant to National Policy 58-201 – Corporate Governance Guidelines of the Canadian Securities Administrators ("CSA"), a reporting issuer's board of directors should comprise a majority of independent directors and the chair of the board should be an independent director or, alternatively, an independent Lead Director be appointed. Independence is defined in the CSA's National Instrument 52-110 – Audit Committees ("NI 52-110"). Under NI 52-110, a board member will be considered to be "independent" if he or she has no direct or indirect material relationship with the issuer. A "material relationship" is defined as a relationship that could, in the view of the issuer's board of directors, reasonably interfere with the exercise of a board member's independent judgment. In addition, a director is automatically treated as not independent if s/he meets one of the listed criteria (for example, an individual who is, or within the prior 3 year period, has been an employee or executive officer of the issuer (which includes any parent or subsidiary entity).

One of the best practices for corporate governance enunciated by the Canadian Coalition for Good Governance ("CCGG"), a leading expert organization on corporate governance, is that a reporting issuer ought to ensure that at least two-thirds of directors are independent of management, do not have a material relationship with the corporation and, except for director fees and share ownership, do not financially benefit from his or her relationship with the corporation. According to the CCGG, a material relationship is any relationship that could



interfere with a director’s ability to exercise independent judgment or inhibit his or her ability to make difficult decisions about management and the business.

We respectfully submit that based on the above authorities, the independent status does not disappear if a director who is otherwise independent of a utility is also an independent member of the board of one of the entity’s affiliates, and this interpretation would satisfy the goals that the OEB is trying to achieve. While Hydro One Networks Inc.’s (“HONI”) board members are also members of the boards of its affiliates Hydro One Limited (“HOL”) and Hydro One Inc. (“HOI”), as mandated by the Governance Agreement dated November 5, 2015 between the Province of Ontario and HOL (the “Governance Agreement”), 14 of its current 15 directors are nonetheless independent of HONI, HOI (parent of HONI) and HOL (parent of HOI) within the meaning of Canadian securities laws. While these directors are shareholders of HOL pursuant to HOL’s share ownership guidelines, such ownership does not make them any less independent.

While the OEB's expectation that a majority (over 50 percent) of directors should be independent is an excellent governance practice, its definition of independence prohibiting the directors of a utility from being a director of an affiliate is too onerous and does not enhance good governance in a complex corporate structure. The OEB’s position in its Draft Report would in essence render HONI's directors to be “not independent”—a result that is contrary to the independence definition under securities laws and also contrary to the Governance Agreement. Hydro One is of the view that the OEB's guidance on director independence for rate-regulated utilities should more closely align with Canadian securities laws and corporate governance best practices by removing the restriction that a director of a utility who is otherwise independent would not be independent if s/he were on the board of a utility’s affiliate.

Sincerely,

ORIGINAL SIGNED BY FRANK D’ANDREA

Frank D’Andrea