

Tom Woods, Board Chair
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February 14, 2019

The Honourable Minister Greg Rickford
 Ministry of Energy, Northern Development and Mines
 Province of Ontario
 900 Bay St., 4th Floor
 Hearst Block
 Toronto, ON M7A 2E1

Dear Minister,

Thank you for your letter of February 13, 2019 regarding Hydro One's renewed compensation framework.

We want to assure you that throughout our discussions and the preparation of the framework, the Board has carefully considered its fiduciary duties to act in the long term interests of the Corporation taking into account the impact of our actions on our broad stakeholder base including customers, shareholders, employees and the communities in which Hydro One operates. In relation to compensation this has included careful attention to the quality of senior management and Board member expertise the Corporation needs to have, over the next many years, to deliver on its promise of safe, secure power for all Ontarians at the lowest possible cost.

We have also considered the requirements and obligations of the recently enacted Hydro One Accountability Act (Bill 2) for the Board to produce a compensation framework for the Corporation in consultation with its large shareholders.

We're respectful of the provisions of the legislation that state that the framework can only become effective when approved by the Management Board of Cabinet.

In your letter you have provided us with some additional input on the latest version of our draft compensation framework. Let me address some of the specific points you have raised.

1 – Regarding CEO "maximum compensation". It is important to note that the salary in the framework would be \$750,000 (significantly less than the \$1.5 million cap your letter refers to). Any balance would be performance related. The "expected compensation" would be \$2.475 million, if all performance objectives are met at target. "Maximum Compensation" would be payable only if performance objectives are far exceeded. Performance objectives will be more challenging than in the previous compensation framework, and will include metrics related to costs, **including the Province's objective to reduce electricity bills**. The vast majority of any performance pay will be in shares deliverable in three years, not cash. The maximum of \$2.775 million compares to the \$7.8 million maximum for the previous CEO, **down 65%**, and would only occur in a scenario where all stakeholders benefit.

2 – Reference is made in your letter to the Province's "desired maximum cap of \$1.5 million". This is well below the minimum range for expected (not maximum) compensation expressed by the other shareholders we were obliged to consult pursuant to Bill 2 (\$2.5 – \$3.0 million). Because Hydro One is a publicly traded

entity, with all of what that entails, we do not believe a capped compensation of \$1.5 million would be sufficient to recruit on an ongoing basis qualified individuals for the CEO role. We base this on our extensive CEO recruitment process in the fall, where we considered 140 candidates and interviewed 13. As you know, we have been in discussion with a very talented prospective CEO, who we believe would accept the role with compensation as contemplated under the proposed framework. Capped CEO compensation of \$1.5 million would make it very difficult to recruit certain other qualified senior executives, for example a CFO, at 75% of this capped amount. As we have previously advised, the entire top management team (five individuals) are under retention agreements and it appears likely that all five will depart soon after their agreements mature in the next 2 ½ months. While we appreciate your statement that the CEO hiring decision remains the exclusive prerogative of the Board, these retention challenges and the suggested \$1.5 million cap in effect preclude the Board from being able to effect a smooth transition to the next management team for Hydro One.

3 – Regarding “the interests and concerns of Ontario’s ratepayers”, we are steadfastly aligned with the Government’s objectives, and the compensation framework respects these objectives. The framework indicates that none of Hydro One’s top executive compensation will be charged to customer rates – it will all come out of bottom-line company profits, **borne by shareholders, not ratepayers**. Also, having the best possible management team, at reasonable compensation (which is what we are proposing), is in the interest of all Ontarians. Even if satisfactory executives could be recruited over time, the company would be immediately and chronically exposed to other publicly traded utilities hiring them away at market based compensation.

We have engaged in comprehensive consultations with other large shareholders and carried out extensive benchmarking, working with an independent advisory firm. We appreciate your and your team’s involvement in each step of our process, particularly during the past three months. We are proposing a responsible basis for setting Hydro One onto a path of stability. Our compensation framework will result in savings of approximately \$10 million per year, or \$40 million over the next four years covered by Bill 2.

As for the perceived appeal of trying to achieve even more savings than \$40 million by attempting to attract a CEO (and other executives) at compensation below the 65% rate cut we are proposing, there is risk in this approach – risk related to the stability of Hydro One, at a time when the company needs experienced leadership in place to tackle the broader cost efficiency and other objectives laid out by the Government in the past nine months – objectives we share. We would ask you to further consider these matters.

As the Board appointed in consultation with, and approved by, your government, we are proud of the work we have done in the past six months and are anxious to finalize our recruitment of Hydro One’s new CEO and senior management.

We look forward to continuing our dialogue as we embark on the final stage of the consultation process as contemplated by Bill 2. This will be an opportunity for you and us to consider the input that will come forward. This next stage begins with the posting of the framework by Hydro One by February 15, 2019.

With best regards,



Tom Woods,
Board Chair
Hydro One Limited