Client Id: 77

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FTS.TO - Q4 2016 Fortis Inc Earnings Call

EVENT DATE/TIME: FEBRUARY 16, 2017 / 1:30PM GMT

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PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by. Welcome to the Fortis Q4 2016 conference call and webcast.

(Operator Instructions)

At this time, I would like to turn the conference over to Janet Craig, Vice President, Investor Relations, Fortis Inc. Please go ahead Ms. Craig.

Janet Craig *- Fortis Inc. - VP of IR*

Thanks, Melissa, and good morning, everyone. And welcome to Fortis' 2016 fourth-quarter and annual results conference call. I am joined by Barry Perry, President and CEO; Karl Smith, Executive VP and CFO; other members of the Senior Management Team; as well as our CEOs from certain subsidiaries.

Before we begin today's call, I want to remind you that the discussion will include forward-looking information which is subject to the forward-looking statement contained in the supporting slide show. All non-GAAP financial measures referenced in our prepared remarks are reconciled to the related US GAAP financial measures in our 2016 annual MD&A. Also, unless otherwise specified, all information referenced is in Canadian dollars. With that, I will turn the call over to Barry.

Barry Perry *- Fortis Inc. - President & CEO*

Thank you, Janet, and good morning, everyone. 2016 was a big year for Fortis. Just over a year ago, we announced the biggest transaction in our history, the CAD16-billion acquisition of ITC. This transformational transaction closed on October 14, just about eight months after announcement.

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As part of the transaction, we issued 114 million shares valued at CAD4.7 billion into the market, which were readily absorbed by existing and new shareholders. We also listed on the New York Stock Exchange, facilitating trading of our stock in US dollars, raising our profile in the United States and providing Fortis easier access to the largest pool of capital in the world. At the same time, we delivered strong earnings and cash flow, driven by our low-risk and highly diversified portfolio of utilities.

Excluding the earnings benefit from ITC in the fourth quarter, adjusted earnings per common share were up 18% for the quarter and 8% for the year. Including ITC, adjusted earnings per common share were up 25% for the quarter and 10% for the year.

We continue to invest capital in our business to provide our customers with safe, reliable, and affordable energy. In 2016, we invested CAD1.9 billion in capital, excluding ITC. Including ITC, from the date of the acquisition, we invested an additional CAD200 million, which brought the total for the year to CAD2.1 billion.

2016 was also an important year of progress on the regulatory front. We received constructive regulatory decisions in a number of jurisdictions, positioning us well for a period of regulatory stability in the near term. Of special mention is the conclusion of TEP's rate case in Arizona last week with terms consistent with the settlement agreement announced in August.

In the fourth quarter, we began to see the power of the earnings contribution of ITC to our business. With almost a full quarter of earnings, ITC was immediately in nicely accretive to EPS. While we frequently refer to the integration of ITC into the Fortis family, the fact is that our model means that there is very little integration activity, and it is largely complete.

There been no staff reductions related to the merger, no relocational functions, and no change of focus at ITC. A new Board of Directors has been created, which combines existing and new Directors, including myself; a representative from GIC; and Joseph Welch, the former President and CEO of ITC, as the Chairman of the Board. ITC, led by Linda Blair, who was named President and CEO upon close of the transaction, has an impressive Senior Management Team who are charged with delivering ITC's results and growth.

We are also very fortunate to be able to welcome Joe Welch as a nominee to the Fortis Board. I know he will be a dynamic and engaged Member of the Board who brings unparalleled insight into the transmission business in the United States, and obviously, ITC.

As we highlighted last quarter, planned capital expenditures for 2017 to 2021 are forecasted to be approximately CAD13 billion, consisting of highly executable, low-risk, and diversified projects. Given the size and scale of Fortis, we are bringing the segmentation of our business up from the individual utility level and expect to segment business going forward as shown on slide 6.

You may recall, Fortis like most utilities, has a declining capital budget curve in the outer years of its five-year capital plan. This reflects the inherent challenges with projecting capital projects over a five-year horizon, and as a result, we are focused on the three-year CapEx and rate base growth rates. For 2016, including ITC, consolidated mid-year rate base was CAD24 billion. Consolidated mid-year is projected to approach CAD26 billion in 2017 and CAD30 billion by 2021.

Over the three-year period, mid-year rate base is forecasted to increase from CAD24.3 billion in 2016 to CAD28.3 billion in 2019, delivering a three-year CAGR of 5.2%. This growth rate, coupled with our highly diversified business and unique operating model will continue to deliver superior risk-adjusted returns for our shareholders.

Capital expenditures for 2017 are expected to be approximately CAD 3 billion. While the bulk of the projects in the forecast are small in nature and generally represent less than CAD50 million each in total, we do have a handful of major capital projects in the plan. At ITC, the multi-value projects, or MVPs, are underway, which consist of four regional electric transmission projects that have been identified by the Midcontinent Independent System Operator to address system capacity needs and reliability in various states. In 2017, we plan to spend CAD354 million on these projects, with three of the MVPs scheduled to be completed by the end of 2018 and the fourth MVP scheduled for completion by 2023.

Other major projects include FortisBC Energy's ongoing Tilbury LNG facility expansion, which is estimated at a total project cost of CAD470 million, including approximately CAD70 million in allowance for funds used during construction and develop costs. The facility will include a second LNG

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tank and new liquifier, and is forecasted to be in service by mid 2017. Work continues on FortisAlberta's pole-management program to extend the service life of existing poles and make needed replacements.

The total capital cost of the programs through 2021 is expected to be CAD341 million. Approximately CAD45 million was spent on this program in 2016, for a total of CAD245 million spent to date.

A key part of our business strategy is to achieve rate base growth that exceeds our base plan. The CEOs of each of our subsidiaries have been charged with identifying and capitalizing on areas of additional investment in their franchise regions. As you are aware, we have identified several of these projects.

We don't expect to hit a home run on each project, but landing a couple of these key projects, particularly LNG in British Columbia or transmission at ITC, will result in meaningful upside to mid-year rate base growth. For instance, if we held our capital investments at CAD2.9 billion in the outer years, the three-year and five-year compound annual growth rates will increase by 30 basis points and 90 basis points, respectively.

At FortisBC Energy, the proposed pipeline project Woodfibre LNG continues to progress. While the project is currently not included in our five-year capital or rate base forecast, the initial capital expectations were approximately CAD600 million, but are obviously dependent on final scoping and detailed estimates. The project could commence in 2017, pending conclusion of Woodfibre LNG's current front-end engineering design process, permitting, and other approvals.

This year, we plan to continue our preparations to move the project forward, including discussions with aboriginal groups and local stakeholders. The in-service date is expected at the earliest in late 2020. The Woodfibre project could potentially add 40 basis points to our compound average mid-year rate base growth over the next five years.

At ITC, we are continuing to pursue the Lake Erie Connector project. Recent milestones were met in January of this year when ITC received a Presidential Permit from the US Department of Energy and a Certificate of Public Convenience and Necessity from the Canadian National Energy Board. These regulatory approvals, and particularly the project rationale described in the National Energy Board's decision, make for good reading and does give us increased confidence in the potential of this project.

The project will be the first direct interconnection between the Ontario energy grid and the PJM energy market, which coordinates the movement of wholesale energy in 13 states, representing 61 million people. Currently, substantially all of Ontario's energy exports go to New York and Michigan, so the benefits of having direct access to the PJM market are obvious. There are still key milestones to be met, not the least of which is completing long-term contracted transmission service agreements, but we are encouraged by the progress.

Lastly, the Wataynikaneyap Power project continues to advance in Ontario. In December, FortisOntario released an agreement with Renewable Energy Systems Canada to acquire its ownership interest in the partnership. The transaction is subject to approval by the OEB and is expected to close in the first quarter of 2017. As a result, our ownership interest in the partnership will increase to 49%, with the remaining 51% held by 22 First Nation communities.

Our participation in this project highlights our commitment to our collective mandate with First Nations to connect remote communities to the provincial electric transmission grid. This will reduce their reliance on high-cost diesel for power and also serve as a platform for further infrastructure and social economic development in northern Canada. I will now turn the call over to Karl for an update on our 2016 fourth-quarter and annual performance.

Karl Smith - *Fortis Inc. - EVP & CFO*

Thanks, Barry. Good morning, everyone. Our 2016 fourth-quarter and annual financial results were quite strong and exceeded our expectations. This puts us into a good position heading into 2017, a year that will benefit from the addition of ITC, the rate case outcome at Tucson Electric, and for the most part, regulatory stability in the remainder of our business.

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Adjusted earnings for the quarter of CAD246 million were higher by CAD104 million compared to the same quarter in 2015. Adjusted earnings per share of CAD0.64 for the quarter was higher by CAD0.13, or 25%. Our fourth-quarter results exceeded expectations, and there were a number of factors that contributed to the result that are not expected to be repeated. These factors total CAD0.06 per share and relate to lower tax expense for the early adoption of an accounting standard on stock -based compensation at ITC and timing differences at FortisBC Electric, Central Hudson, and UNS.

For the full year, adjusted earnings of CAD721 million were higher by CAD132 million compared to 2015. And adjusted earnings per share was higher by CAD0.22, reaching CAD2.33, an increase of 10%. Cash flow from operations was CAD1.9 billion in 2016, an increase of approximately 13% compared to 2015 and results from higher cash earnings at our regulated utilities, particularly from ITC.

As you can see from the waterfall chart, adjusted earnings per share increase CAD0.13 compared to the third quarter of 2015. CAD0.04 was due to accretion from ITC after considering finance charges and an increase in the weighted average of number of common shares outstanding associated with financing the transaction.

Strong performance in most of our regulated utilities also resulted in higher earnings per share for the quarter. And highlights include Central Hudson due to an increase in delivery revenue consistent with its three-year rate settlement, higher allowance for funds used during construction at FortisBC Energy, the timing of the recovery of power purchase cost in 2015 at FortisBC Electric, as well as a positive contribution from Aitken Creek. Partially offsetting these increases was the higher weighted average number of common shares outstanding, reflecting normal course investment in Fortis through our dividend reinvestment and share plans.

Moving on to the next slide. A somewhat similar story plays out for the full year of 2016. On an adjusted basis, earnings-per-share growth in 2016 was driven by accretion associated with the acquisition of ITC, which amounted to CAD0.06. The difference in the accretion of ITC for the quarter and the year is the result of the issuance of 114 million shares in the third quarter as part of the financing of the transaction and its relative impact to the weighted average number of shares for the quarter and the year.

Additionally, earnings per common share for 2016 were favorably impacted by strong performance at most of our regulated utilities, including UNS Energy, largely due to the settlement of the Springerville Unit 1 matters; favorable foreign exchange associated with US dollar and denominated earnings; a higher allowance for funds used during construction at FortisBC Energy; an increase in delivery revenue at Central Hudson, consistent with its three-year rate settlement; stronger performance from the Caribbean operations; a positive contribution from Aitken Creek; and a full-year of earnings from the Waneta Expansion, which commenced production in early April, 2015.

Growth in earnings-per-share was tempered, however, by the sale of commercial real estate and hotel assets in 2015, higher corporate and other expenses, and lower earnings at FortisAlberta mainly due to lower average energy consumption. Increasing earnings and cash flows contribute to our financial flexibility and support our investment-grade credit ratings.

Our consolidated credit facilities, including ITC, totaled approximately CAD6 million, of which, CAD3.7 billion was unused at the end of 2016. The consolidated credit facilities include a CAD500-million senior unsecured equity bridge used to finance a portion of the ITC transaction, which matures in October, 2017. Our financial strength and borrowing capacity position us well to fund our organic growth and identify opportunities.

As Barry mentioned earlier, 2016 was a year in which we made significant progress on a number of key regulatory fronts, providing regulatory stability in the near term. Just last week, the Arizona Corporation Commission issued a rate order in Tucson Electric's general rate application that was filed in November, 2015. The rate order approved rates effective on or before March 1, 2017. The provisions of the rate order include an increase in non-fuel base revenue of $81.5 million and allowed ROE of 9.75% and a common equity component of the capital structure of approximately 50%.

In September 2016, ITC received an order from FERC regarding the first MISO regional base ROE complaint, which set the base ROE at 10.32%, with a maximum ROE of 11.35%, and established that those rates are to be used prospectively until a new approved rate is established for the second complaint. A decision from FERC on the second complaint is expected in 2017.

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During the third quarter, FortisBC Energy received a decision from its regulator, the British Columbia Utilities Commission, regarding its application to review the 2016 allowed ROE and common equity thickness. The decision maintained and allowed ROE of 8.75% and common equity thickness of 38.5%. Further, in October, FortisAlberta received a decision from the Alberta Utilities Commission regarding the 2016-2017 Generic Cost of Capital Proceeding, which maintained an ROE of 8.3% for 2016 and increased the allowed ROE to 8.5% for 2017. The decision also included a decrease in the common equity thickness from 40% to 37% for both 2016 and 2017.

More recently, in December, the second performance-based rate term for the period of 2018 through 2022 was confirmed. Alberta utilities have been directed to file a rebasing application in March 2017 to establish the going-in revenue requirement for the second PBR term, which will be used to determine the going-in distribution rates for 2018. A decision on this application is expected in the second half of 2017.

We are confident with the capital plan and associated rate base growth which supports our 6% average annual dividend growth guidance through 2021 and will continue on our record for the longest consecutive dividend increases for a public company in Canada. In September, our Board of Directors declared a fourth-quarter 2016 dividend of CAD0.40 per common share, an increase of approximately 7% from CAD0.375 paid in the third quarter of 2016. This translation to an annualized dividend of CAD1.60.

There has been a lot of focus of speculation about the elements and effects of US tax reform on utilities in general and for Fortis specifically. We don't have anything new to add to the conversation from an industry perspective, and there have certainly been many companies that have reported ahead of us that have done a good job of describing what each element of the potential tax reform is, so we don't want to duplicate that.

When looking at Fortis, it is important to remember that about 40% of our earnings come from operating subsidiaries outside of the US, where the US tax reform proposals do not apply. Fortis does not expect to pay cash taxes through 2021, largely due to bonus depreciation, and we are seeing economic growth and opportunities to drive investments in the states in which we operate.

The cost of service regulatory constructs at each of our US facilities means that tax reform should reduce pressure on customer rates. In our opinion, any reduction on customer rates will allow regulators to support prudent investment of additional capital to strengthen energy delivery infrastructure. At Fortis, we have stress tested various US tax reform proposals at the consolidated and US subsidiary levels, focusing on corporate tax rate changes, 100% deductibility of capital investments, and nondeductibility of interest expense, assuming it has applied prospectively.

In each case, we looked at these scenarios for impacts on earnings. The impact are not material at a consolidated level and do not change our operating approach or strategy. In addition, the impact is minimal at the US operating subsidiaries and presents opportunities to advance investments in energy infrastructure.

On balance, there is a slight negative impact to earnings, assuming we do not factor in additional capital investment, improved economic conditions, or any other mitigating factors. In fact, the impact is well within the range of outcomes that we would generally see in our planning process. This concludes my remarks. I will now turn the call back to Barry.

Barry Perry - *Fortis Inc. - President & CEO*

Thank you, Karl. Taking a look at the bigger picture, economic growth in US, as well as a focus on infrastructure spending by the administration, are positive for us and the industry. As Karl highlighted, tax reform in the US is on the horizon, and it has created some investor uncertainty. Fortis, as well as other utilities and EEI, are working with policymakers in Washington, DC to drive constructive outcomes on tax reform.

Changing times underline the strength Fortis business model. Our business is highly diversified. We have balance between Canadian and US assets. We operate in constructive regulatory jurisdictions, and we have conservative base capital plan that delivers superior risk-adjusted returns. This differentiated model is one we strongly believe will deliver long-term value creation for our shareholders, while at the same time, providing safe, reliable, and cost-effective energy for our customers.

To wrap up, we are very pleased with our ability to deliver strong results in 2016 while successfully closing the ITC transaction. Some would say that is excellent execution. In 2017, the outlook is strong. With a constructive outcome of the TEP rate case and the addition of ITC to our business,

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we are creating a new baseline upon which Fortis can grow. We remain confident in our future and the ability of our Team to execute against our strategy. I will now turn the call back over to Janet.

Janet Craig - *Fortis Inc. - VP of IR*

Thanks, Barry. This concludes the presentation, and at this time, we would like to open the call to address questions from the investment community, so I will hand the call back over to Melissa.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Robert Kwan, RBC Capital Markets.

Robert Kwan - *RBC Capital Markets - Analyst*

Good morning. Just with the fourth-quarter results, you put a pretty big number based on your adjusted EPS, and you noted you exceeded your expectations. I'm just wondering, with that roughly CAD0.06 of timing factors, if you could took that out of Q4, did the quarter still exceed your expectations?

And then as you get more granular, can you just talk a little bit more about some of the timing items with the utilities and whether you expect that to reverse in 2017 or just not recur?

Barry Perry - *Fortis Inc. - President & CEO*

Robert, thank you, and thank you for being up so early. I will maybe make a general comment and let Karl add some detail. We had a great finish to the year, and especially given the fact that we are just closing the ITC transaction.

We had great performance out of our Arizona business. They've overcome some difficult conditions last year and performed very well. ITC itself, good contributions from them as well. And, yes, we expect it was better than we were thinking, and that should translate into some upside for 2017 as well.

Karl Smith - *Fortis Inc. - EVP & CFO*

Hi, Robert. It's Karl. For the most, that referenced to the timing differences will not reverse in 2017. They are, for the most part, one time. And for instance, the ITC one was just an adoption of an accounting standard. That's a one-time impact.

At FortisBC, the reference is more with respect to the timing from the previous year and just the matching of the purchases power comps with the revenue there, so that expires at the end of 2016 as well. And then at FortisBC Energy, a little bit different. There's some AFUDC impact there until the Tilbury 1A project is complete. That will carry through some period of 2017.

As Barry mentioned, we're hopeful that we'll put that in service by the middle part of the year, and so that will have some impact in 2017 with respect to that. But for the most part, you can assume that CAD0.06 that we refer to is one time and will not repeat itself or will not have an impact in 2017.

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Robert Kwan - *RBC Capital Markets - Analyst*

Understood. If I could just finish this, take a step back at something higher level. You've got a lot of small- to medium-sized projects, so high visibility driving your base growth. But as you noted earlier, you've got that push that you had in recent years trying to get your local utility businesses to focus on corporate development. We've seen that with the Ontario Transmission, a couple of projects out my, and Erie Connector.

Barry, as you think about it, though, are there any things that are currently getting less fanfare, whether that's the New York Transmission or solar at UNS, that you see as being larger, more meaningful investments that could come to the forefront in 2017? And are there any one or two trends in the sector you are really pushing all of your teams to proactively get in front of to try to create opportunities?

Barry Perry - *Fortis Inc. - President & CEO*

Yes, Robert. Good question. We are excited about the ones that we've mentioned, obviously, and I would add that the potential on LNG infrastructure in BC remains front and center for us.

We're obviously building that Tilbury tank right now, but that site at Tilbury is highly expandable, and we had an arrangement with Hawaiian Electric that fell away, but we have received other interest in expansion of that site, and we continue to work on that opportunity. That could be substantial, in a CAD2-billion range if we're successful there.

One other area I think is grid security, cyber, physical security. The real -- a focus on these areas now in North America, and we haven't really built in, I think, capital expenditures, significant capital expenditure related to enhancing that going forward, and I think that's going to add to the capital budgets of our utilities over the next number of years and as we improve our facilities, frankly.

So those are probably a couple of areas. We're clearly working on expanding renewable power in Arizona, those kind of things. But I would think the big ones are L&G and the cyber-physical security areas, especially at ITC as well.

Robert Kwan - *RBC Capital Markets - Analyst*

Okay. That's great. Thank you very much.

Barry Perry - *Fortis Inc. - President & CEO*

Thanks, Robert.

Operator

Linda Ezergailis, TD Securities.

Linda Ezergailis - *TD Securities - Analyst*

Thank you. Maybe I can just build on Robert Kwan's questions about (inaudible) the Q4. Can you give us a senses maybe either at some of your business units or even on a consolidated Fortis level going forward in a normal year how we might think of seasonality, a typical seasonality of your earnings?

And then as a subset of that, Aitken Creek, maybe some run rate or range? Looks like it had a blockbuster quarter, so how might we think of your gas storage business going forward within that mix of questions?

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Karl Smith - *Fortis Inc. - EVP & CFO*

Linda, it's Karl. The seasonality of our earnings will be somewhat muted with the addition of ITC. ITC earnings, you can anticipate that they will be relatively consistent and growing consistently on a quarter-by-quarter basis as they continue to invest in their system. As you know, the gas business in British Columbia is highly seasonal, first quarter, fourth order. That will continue, obviously, but it will be muted somewhat compared to what it has been in the past.

With respect to Aitken Creek, we had excellent performance in the fourth quarter. We were able to take advantage of some market dynamic I referred to in terms of the gas price. On a go-forward -- and again, there will be some seasonality in that business that will become apparent once we get through a full cycle. But for the most part, the run rate that you saw in 2016 will be something that you should anticipate seeing on a go-forward basis.

Barry Perry - *Fortis Inc. - President & CEO*

And Linda, just to add a couple of things there. One of the things we are learning about ITC is the lack of volatility in their earnings and cash flow. This marvelous formula rate structure at FERC provides a lot of stability for that company. And as Karl said, really, each quarter's earnings should, as they invest their capital, should provide higher earnings for the Corporation.

And just one added comment as well. Our Arizona business, obviously, does very well during the summer months, and that goes a long way to offset the lower earnings from our BC gas business as well. So we have actually reduced at that seasonality very much overall in the business now.

Linda Ezergailis - *TD Securities - Analyst*

Okay. Thank you. And just a followup to how you are looking at some of these potential tax reforms in the US. Is it reasonable to think that one of the takeaways in all your sensitivity analysis would be that from a cash-flow-from-operations perspective, that it would be slightly negative, similar to earnings, assuming no mitigating factors as well?

Karl Smith - *Fortis Inc. - EVP & CFO*

That is absolutely correct, Linda.

Linda Ezergailis - *TD Securities - Analyst*

Okay. Thanks. I will jump back in the queue.

Operator

Robert Catellier, CIBC World Markets.

Robert Catellier - *CIBC World Markets - Analyst*

Hi. Good morning. Congratulations on the results, and thank you for your comments on the tax reform. But I would like to see if you can put a little more detail around the slightly negative impact. It doesn't sound like it's material, but if you were to quantify it, would that be less than 5%? Less than 5% of earnings or funds from operations?

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Karl Smith - *Fortis Inc. - EVP & CFO*

Robert, it's -- we won't be giving very specific guidance around that, but I would say that I would agree mostly with your comment in the question, and I think that's where we will leave it for the time being.

Robert Catellier - *CIBC World Markets - Analyst*

Yes. I appreciate there is still considerable uncertainty there. But just moving on, has there been a change to the capital spend outlook for the Tilbury project, and if so, who is at risk for the CapEx increase?

Barry Perry - *Fortis Inc. - President & CEO*

The project has slipped in timeline. So we were originally looking at the project coming online around the end of 2016. It is now mid 2017. So Robert, there is normal, obviously, AFUDC carrying cost with that slippage. The underlying cost of the project we believe we still can bring in on budget at this point in time.

Robert Catellier - *CIBC World Markets - Analyst*

Okay. Maybe I will follow that one up with you. The numbers I calculated showed the CapEx going from CAD128 million to CAD144 million, which seems to imply a little bit more than the cost of carry.

Barry Perry - *Fortis Inc. - President & CEO*

The underlying value of the project before carrying cost, around CAD400 million, and we are still on that number.

Robert Catellier - *CIBC World Markets - Analyst*

Okay. And then just as you look at your large inventory of major projects that aren't effectively in your capital plan, as you go forward and look at your dividend policy, if you were to be successful in securing these growth projects, are you more likely or more inclined to increase the dividend growth rate or extend the dividend growth horizon?

Barry Perry - *Fortis Inc. - President & CEO*

To be honest, I think we are focused on a nice annual growth rate in our dividend. We look at the business very long term, and there are always going to be pluses and minuses. I am pretty comfortable with a 6% dividend growth rate, and I would expect us to just continue to extend it rather than increasing it going forward.

So that's -- we are right on top of our average payout ratio for our peer group. We use the 25 companies in our peer group, 23 American utilities, two Canadians, and that 65% percent to 70% payout ratio is where we think we should be around. So we're going to get -- we're going to land some of these bigger projects, but I think for us, it will just make us to be able to continue to make sure that we can grow that dividend nicely each year going forward rather than going -- upsizing the dividend dramatically.

Robert Catellier - *CIBC World Markets - Analyst*

Okay. Great. Thank you.

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Operator

Ben Pham, BMO.

Ben Pham - *BMO Capital Markets - Analyst*

Okay. Thanks. Good morning. I wanted to go back to the -- some of the questions on the tax reform slide and your commentary there. Is the slight negative impact to earnings, is that a combined impact from all the three factors you looked at, or is that all separate?

Karl Smith - *Fortis Inc. - EVP & CFO*

That on a consolidated basis, Ben.

Ben Pham - *BMO Capital Markets - Analyst*

Okay. And then the order that you've laid it out here, is that from highest magnitude to earnings impact, or is it just an arbitrary ordering for the three?

Karl Smith - *Fortis Inc. - EVP & CFO*

The ordering is not meant -- is not particular in terms of impact. It's just a laundry list so to speak.

Ben Pham - *BMO Capital Markets - Analyst*

Okay. And then my other question is on, how do you guys think about your balance sheet today relative to where you wanted to be, and with the high CapEx program leads to how do you finance over time? You've mentioned no need for equity before on that, but you -- did notice a bit of a draw on the remaining balance of your equity bridge. So can you talk about your credit metrics and capacity on perhaps some debt at the moment?

Barry Perry - *Fortis Inc. - President & CEO*

Ben, it's Barry. Clearly, we are focused on maintaining a good balance sheet. And we do have this equity bridge that we will refinance with equity at some point during the course of this year. It's a pretty small amount relatively speaking, 3% of our market cap kind of thing. But the cap -- that relates to the purchase of ITC, so that's just the final piece we have to do there. The actual capital plan itself, at this point, at the CAD13-billion level over the next five years, doesn't require any, I would say, market equity. We do get -- 30% to 40% of our dividends are reinvested in stock on an annual basis, so that's going to provide upwards to CAD1 billion over the five-year period.

Clearly, with that, we don't need to do incremental equity for that base capital plan. If we're successful with Erie Connector, with LNG expansion, with Wataynikaneyap, these kind of projects, we are going to be going into the market, and I'll be happy to do that, but the base plan is financed within the business.

Karl Smith - *Fortis Inc. - EVP & CFO*

And Ben, our credit metric is primarily FFO to debt. The other metric that is important is holdco debt to total debt. They continue to improve throughout the forecast or the plan period. So we see those improving over time.

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You probably heard Barry say in the past that we think our credit rating from Moody's has probably been a little harsher than it should be, so we are hopeful that over the next three to five years, we will see some improvement there as well. But we are not anticipating that now. We're not counting on it. The balance sheet continues to improve during the course of the plan, and we don't anticipate any issues in raising capital to fund the plan going forward.

Ben Pham - *BMO Capital Markets - Analyst*

And to clarify, your definition of equity includes preferred shares, or do you not include that?

Karl Smith - *Fortis Inc. - EVP & CFO*

We're not thinking about preferred shares. That (inaudible) all comes and goes. Currently, we don't view it as an attractive source of capital. So it's possible that if that market changes going forward, we would resort to that again as we have in the past, but as we sit here today, we are not anticipating preferred share issuance.

Ben Pham - *BMO Capital Markets - Analyst*

Okay. Great. Thanks, everybody.

Barry Perry - *Fortis Inc. - President & CEO*

Thank you, Ben.

Operator

Rob Hope, Scotiabank.

Rob Hope - *Scotiabank - Analyst*

Good morning, everyone, and congratulations on a good quarter. Just wanted maybe to take a look at ITC. You have a full quarter under your belt, and there's been some pushes and takes since the announcement was initially announced. Just want to get a sense of whether or not this is tracking above or below the expectations you that laid out at the transaction announcement.

Barry Perry - *Fortis Inc. - President & CEO*

That's a tricky question, Rob. (Laughter) You know what we said on announcement, it was a 5% accretion, and we have now gone to a term nicely accretive. So I would tell you that I'm very pleased with how the company has done, how the ITC Team has performed in these early days of our owning the company. I couldn't have asked for anything more, so we are very pleased.

We want to get through 2017, and I'm always -- the formulaic rates, the advantages of that, and it's hard for us to get our minds around that. The ITC Team keeps telling me don't worry. It's good, and there's not a lot of volatility in their earnings. But obviously, from an oversight perspective in the business, I want to post up good 2017 results, and then we will see where we go from there, but we are in very good shape at this point in time.

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Rob Hope - *Scotiabank - Analyst*

And that's good to hear. And then just looking on the FERC front. You are one of the few companies who's hoping for a long and protracted confirmation progress there. Do you have any expectation of when the second complaint will be ruled upon now?

Barry Perry - *Fortis Inc. - President & CEO*

No, we don't. Clearly, FERC has to get some new commissioners, and there has to be the confirmation process for those things, and we can't really predict how quickly that would happened. We continue to earn the higher 11.35% while we await this decision, obviously, and the decision will -- it's not retroactive, so there are benefits if it goes longer if you are expecting the returns to go lower, and that's not a foregone conclusion for sure at this point in time.

Rob Hope - *Scotiabank - Analyst*

All right. Thank you. Those are my questions.

Barry Perry - *Fortis Inc. - President & CEO*

Thanks, Rob.

Operator

David Quezada, Raymond James.

David Quezada - *Raymond James - Analyst*

Thank you. Good morning, guys. My first question, on the Erie Connector, I understand it's part of the NEB's approval over a set of conditions that you had to meet there. I'm wondering if any of those were particularly material or significant?

Barry Perry - *Fortis Inc. - President & CEO*

Hey, they are all difficult, but we feel they are manageable. And for everyone on this call, I would encourage you to read that NEB decision because it does give a good analysis of the benefits of the project. It's right on the NEB website. I think we might have provided it to some of the analysts.

But no, I think we can work our way through those. We are waiting for a couple of other permits on the US side that we hope that we can get in the next couple of months here. The key work stream now that we are focusing on is securing a long-term offtaker or for the line, and we are making progress there, and we hopefully have more to say about that in the second half of this year.

David Quezada - *Raymond James - Analyst*

Great. Thank you. That's helpful. And then just my other question, more of a bigger picture. The US infrastructure spend (inaudible) it seems like that will probably be a positive for transmission investment. I think some of the initial priorities that they have mentioned included smart grid investment and energy storage. Do either of those elements factor in your plans longer term?

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Barry Perry - *Fortis Inc. - President & CEO*

Yes, I think those could play in some of our capital over the longer term. There were a number of large-scale transition projects in the top-50 infrastructure list as well. So I really see the overall focus on infrastructure as positive for our business, especially ITC.

Even in Arizona, we finally have seen growing sales at this point, first time I think in a decade that we've had positive sales growth in our TEP business. So we are really starting to see a pickup there. And the policies of the new president seem to be encouraging economic growth in the US, and our business is going to benefit from that if it actually occurs. So, yes, we're looking pretty positive on the next few years from possibly being able to add our capital program.

David Quezada - *Raymond James - Analyst*

Great. Thank you. That's all I had.

Barry Perry - *Fortis Inc. - President & CEO*

Thank you.

Operator

Jeremy Rosenfield, Industrial Alliance.

Jeremy Rosenfield - *Industrial Alliance Securities - Analyst*

Thanks. Just I wanted to follow on the Lake Erie Connector project. I'm wondering if you can comment in terms of where you are with the level of commercial support at this time? And do you need to have contracts, essentially, to cover the full capacity of that project, or can you move forward with a base level, let's say, and you have a percentage there or something like that.

Barry Perry - *Fortis Inc. - President & CEO*

Jeremy, we're obviously not going to comment on where exactly we are other than we are making very good progress with very strong counterparties. Probably not necessary for us to have 100% of the line contracted, although that would be what I would prefer, but we have to be realistic. If we can get a substantial amount, virtually all, substantially all contracted, then the project could proceed on that basis, but our goal is to try to get it all done.

Jeremy Rosenfield - *Industrial Alliance Securities - Analyst*

Okay. And then if I could just turn attention to the BC LNG and the outlook for Woodfibre LNG project there. What is the key milestone that you need to see to add that to the capital budget at this point?

Barry Perry - *Fortis Inc. - President & CEO*

Well, I think we need truly to lockdown the final capital cost for the line, to the site, and the final transmission rate that the proponent will pay for the use of that line, and we need the proponent to finish their FEED study really. I know they've announced that the project is -- they have released the funds for it to proceed, but there's still a process that they are going through, locking down the overall cost for the project. So I think there's a few more months here before we are able to really include that in our forecast, assuming we can get to reasonable conclusions of those matters.

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Jeremy Rosenfield - *Industrial Alliance Securities - Analyst*

And can you comment just in terms of have you spent any substantial amount of money related to the upfront development of that project, or is it still relatively immaterial at this point?

Barry Perry - *Fortis Inc. - President & CEO*

No, we've been working with the proponent, and they have been funding the work that we are doing. So we probably have spent about CAD60 million in total, and that has been funded by the proponent.

Jeremy Rosenfield - *Industrial Alliance Securities - Analyst*

Okay, perfect. Those are my questions. Thanks.

Operator

Mark Jarvi, Desjardins Capital Markets.

Mark Jarvi - *Desjardins Capital Markets - Analyst*

Good morning, everyone. I wanted to circle back on the Wat-k transition project, comments about you guys buying out your partner RES. Maybe you can just comment on what was the impetus to do that, whether or not that was driven by you guys or them maybe just wanting to step back from that project. And given some of the comments from the government ministries of -- but supporting transition in northwest Ontario, how -- a probability that something gets cemented in 2017 on that project?

Barry Perry - *Fortis Inc. - President & CEO*

Well, I think RES's decision, really, maybe you should ask them, but my sense is that they are removing themselves from this part of the business in North America. So this is change of strategy for them, and we obviously are very much focused on growing our wires transmission business in North America, so we're more than willing to look at acquiring their interest. That is still subject to the OEB approving that purchase at this point in time.

The big decision, the next big decision for that project is the approval of the deferral account, which is in front of the OEB at this point in time. That will essentially provide the funds, the confidence for us to go and do much more of the development planning and engineering work for the project, and we are expecting that we'll get that in the next two or three months here, and that's the next big hurdle for the project.

Clearly, this is a project that we are working with First Nations, the provincial government, the federal government, and the regulator on to move forward, but there's a lot of support right now to get this thing done, and we remain very optimistic that this is a viable project.

Mark Jarvi - *Desjardins Capital Markets - Analyst*

Okay. That's helpful. And then looking at ITC and some of the trends in renewables in the US, just some of the recent data that came out showing a big build in utility scale solar eclipsing the growth of wind right now at least. So if that trend continued, would that maybe temper your optimism for some of the positive tailwinds in renewables and transition buildout, or is there aspects of the ITC business would do very well with continued for the growth in high-utility-scale solar?

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Barry Perry - *Fortis Inc. - President & CEO*

I don't think there's much to temper my optimism about ITC right now. This is a great business. It's a core of the great in many of these states that it operates in. They have been running it really well. And there's going to be a continuing need for investment in that 25,000 kilometers of line that they have.

This company has hooked over 5,000 megawatts of wind to its system. I think there's a couple of thousand megawatts still in the queue at this point in time. Wind is very economic in the Midwest, and I think that the states will continue to allow wind generation to be part of the portfolio that utilities have. And this may slow down a little bit, but the way we look at the business in five- and 10- and 15-year outlooks, we're very optimistic that ITC will continue to experience positive growth related to hooking up wind energy to the grid.

Mark Jarvi - *Desjardins Capital Markets - Analyst*

Okay. Thanks for those comments.

Operator

Andrew Kuske, Credit Suisse.

Andrew Kuske - *Credit Suisse - Analyst*

Thank you. Good morning. Perhaps just a bigger, broader question, and do you foresee just the US utilities industry going into a little bit of a holding pattern in the near term?

And I state that just in light of some of the uncertainty on tax reform, and in particular, not so much corporate tax rates, but just the deductibility of interest expenses and prospectively where that may go. And how is that balanced just on a policy basis versus -- apparently, the new administration that really wants to drive infrastructure investments and a lot of the broader initiatives that would really benefit the industry? How do you think about that at this point in time, of the tension on those two things?

Barry Perry - *Fortis Inc. - President & CEO*

Andrew, I would probably even not, like, focus on tax reform. Where I am -- and I may be wrong on this, obviously -- I think M&A is going to slow down in our sector. A lot of companies have done transactions. The big firms that bought utilities recently, the Canadian firms like ourselves and Emera, and how AltaGas, Algonquin have just recently bought utilities. So for me, the next couple of years, I think things do slow down. That's my opinion.

I know we are not done M&A right now. We are really focused on executing well with ITC and our growth capital and really creating that new level of earnings that will flow from, the ITC transaction and really making sure we lock down these organic growth projects that support our dividend guidance out to 2021, so that's where my team is focused. I can't speak for the other people, but my sense is we are probably going into a period of a pause, but again, I've been wrong on that before so.

Andrew Kuske - *Credit Suisse - Analyst*

Okay. I appreciate the color. And then just maybe a slightly different question as it relates to capital allocation from a Fortis Inc. standpoint. And obviously, it's still early days with ITC, but you've had a number of acquisitions under your belt for a period of time, and you have a diversity of regulators you deal with at this stage.

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So how do you think the regulators think about just the Fortis ability at the holdco level to think about capital allocation and really directing your cash, your excess cash to the higher-returning areas. Does that have any influence on a local regulator really thinking in one jurisdiction that maybe rates are too low and they should by us upwards, or conversely, that they are too high and they should by downwards? Has that had any influence to date, or do you perspectively see that have any influence?

Barry Perry - *Fortis Inc. - President & CEO*

Nothing to date, Andrew. We are very clear when we are meeting our regulators that we don't operate the business that way. We expect to be treated fairly within the jurisdiction, and we are going to provide the capital necessary to operate the utility well in that jurisdiction. And we have, as you know now, a very wide range of what I call regulatory compacts between equity thickness and ROEs in our Canadian businesses versus our US businesses.

There is also differences on future test years, historical test years, so it's a real mix of things out there, and we just focus on making sure within each jurisdiction that we run a good operation, serve our customers well, add positive regulatory relationships, and Fortis is going to provide the capital to these utilities that they need, and we're not going to be deciding between each one of them who gets the money. That's not how we run the business.

Andrew Kuske - *Credit Suisse - Analyst*

I think your quarter validated those statements and that operating philosophy. So with that, (multiple speakers) I will drop off.

Barry Perry - *Fortis Inc. - President & CEO*

Thank you for the headline (multiple speakers).

Andrew Kuske - *Credit Suisse - Analyst*

Thank you.

Operator

(Operator Instructions)

As there are no further questions, I would like to turn the call back to Mr. Perry for any closing remarks.

Barry Perry - *Fortis Inc. - President & CEO*

Thank you very much, operator. I just want to conclude by saying we had a very strong 2016. I'm very proud of my Team in terms of how we executed and got the ITC deal done well while we delivered strong results in the rest of the business.

We are positioned very well over the next number of years to continue to grow the business and supporting our dividend guidance through 2021 of CAGR of 6% a year over that period of time. So thanks, everyone, and I look forward to talking to you next quarter.

Operator

Thank you for participating. Ladies and gentlemen, this concludes today's conference. You may disconnect.

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