

COUNCIL AGENDA



Location: **City Hall Council Chambers**, 1 Carden Street

DATE **Wednesday, October 14, 2015 – 6:00 p.m.**

Please turn off or place on non-audible all cell phones, PDAs, Blackberrys and pagers during the meeting.

Disclosure of Pecuniary Interest and General Nature Thereof

OPEN MEETING

Guelph Municipal Holdings Inc. – Update on the Asset
(report attached)

AUTHORITY TO MOVE INTO CLOSED MEETING

THAT the Council of the City of Guelph now hold a meeting that is closed to the public, pursuant to The Municipal Act, to consider:

Guelph Municipal Holdings Inc. – Update on the Asset

Municipal Act Section 239 (2) (a) the security of the property of the municipality or local board.

CLOSED MEETING

ADJOURNMENT

INFORMATION REPORT



TO City Council

SERVICE AREA Office of the CAO
Legal, Realty and Risk Services
Business Development and Enterprise

DATE October 14, 2015

**SUBJECT Consolidation of Local Distribution Companies (LDC)
Guelph Hydro Electrical Systems Inc. (GHESI)**

EXECUTIVE SUMMARY

SUMMARY OF REPORT

To provide background information regarding the potential consolidation of Local Distribution Companies. Specifically:

- Previous efforts to merge with another utility.
- Process for collaborative consideration of the impact of consolidation between Shareholder and Guelph Municipal Holdings Inc. (GMHI) and its LDC subsidiary, Guelph Hydro Electrical Systems Inc..
- Current Provincial policy context for consolidation.
- Market activity related to consolidation.

KEY FINDINGS

- Governance structures will provide for full, open and complete consideration of potential consolidation.
- Strategic alignment supported by these structures will provide full risk assessment of both community impacts and impacts to the business of GHESI.
- The Shareholder agreement between the City (as Shareholder), GMHI and its subsidiary GHESI provides the tools that ensure this strategic alignment.
- The Province of Ontario is clearly signalling its desire to see fewer Local Distribution Companies in Ontario through consolidation.

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BACKGROUND

On **September 29, 2008** City Council considered a recommendation from Guelph Hydro Inc. (since merged with Guelph Municipal Holdings Inc.):

"THAT Guelph City Council accept the recommendations of the Board of Directors of Guelph Hydro Inc. [GHI] for the merger of the assets of Guelph Hydro Electric Systems Inc. with those of Horizon Utilities Corporation."

The motion was defeated.

Subsequently, on **November 24, 2008** Council approved the following recommendation:

"That a steering committee representing the Mayor and four members of City Council (as shareholder) and the Guelph Hydro Inc. Board be established to explore the future direction and opportunities of the Guelph Hydro business enterprise."

To that end, a Guelph Hydro Steering Committee was struck and in **February, 2009** and Council approved its Mandate and Charter detailing core responsibilities and duties. As part of the Committee's work, GHI members of the committee considered staff-recommended modifications to the current approach to asset management and related changes to the existing GHI Shareholder Declaration.

Proposed benefits included streamlined shareholder approvals, improved asset management, strengthened strategy alignment and more regular communications.

On **October 26, 2009**, the model framework agreed upon by the Committee members along with the revised GHI Shareholder Agreement was presented to Council. At that time, and with respect to the legislatively required Business Case Study and MOU with GHI, Council directed staff as follows:

"THAT Council approve the development of a business case study to support the formation of a Holding Company for current and future owned city assets and that staff proceed with identified next steps as prescribed under the Municipal Act."

On **June 28, 2010**, Council approved:

"THAT Council approve the proposed design of a Holding Company for current and future owned city assets, including Guelph Hydro Incorporated (GHI) and Guelph Junction Railway (GJR), as outlined in the attached Business Case Study;

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THAT Council direct staff to prepare an Implementation Strategy for the proposed Holding Company to be approved by Council that includes financial and resource requirements planned for through the 2011 budget process."

All activities were complete by **August 11, 2011** and, with Council's approval on that date, Guelph Municipal Holdings Inc. was up and running.

REPORT

1. Chronology of Consideration for Potential Mergers and Acquisitions

- In **May of 2013**, GMHI reported to Council the high-level findings of **Ontario Distribution Sector Review Panel**. The Panel recommended that the current 73 Local Distribution Companies (LDCs) be consolidated into 8 to 12 larger regional distributors with a minimum of 400,000 customers each. The panel advocates that this should be 'compelled' by legislation.
- On **November 14, 2013** the GMHI Board created a Mergers and Acquisitions Task Force. This was reported to Council on two occasions:
 - In its report to Council, **March 13, 2014**, GMHI reported that the Mergers and Acquisitions Task Force was up and running.
 - The **2013 Annual Report to the Shareholder** (delivered in June of 2014) indicated that the Board of GMHI initiated the **Task Force on Mergers and Acquisitions**. The Task Force was made up of board members from GMHI and Guelph Hydro Inc. as well as officers and staff from both organizations. The Task Force's primary objective was to consider various merger or acquisition scenarios related to industry consolidation that may be presented to GMHI from Guelph Hydro Inc. and to assess the impact on issues such as local oversight, reliability of services, asset value to the City and the ability to continue to develop the Community Energy Initiative.
- The work of the Task Force was paused after its last meeting of **July 28, 2014** to focus attention on the amalgamation of GMHI and Guelph Hydro Inc. (GHI). This amalgamation was completed with Council approval on **December 15, 2014** resulting in the current governance structure with Council as Shareholder to GMHI and GHESI as a direct subsidiary.
- In **September, 2015** the GMHI board approved the creation of the "Transactional Committee" comprised of members representing the GMHI board, GHESI and the City (as Shareholder). The Committee will continue the work originally begun by the **Task Force on Mergers and Acquisitions**.

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2. Provincial Context

The Province has previously embarked on two key studies to review and recommend on the general issue of LDC consolidation.

A. The Ontario Distribution Sector Review Panel Report

Often referred to as the “Blue Ribbon Panel”, this report, delivered to the Province in **April, 2012** made a focused high-level recommendations supported by a longer list of enabling recommendations. The main recommendation was to “Consolidate most of the present 80 LDCs through mergers (the recommendations apply to 73 utilities, with 7 excluded for various reasons), to a final number of 8 to 12 regional distributors including two distributors in Northern Ontario, one each in northeast and northwest Ontario. The rest of Ontario to be served by 6-10 distributors, each with a minimum of 400,000 customers.

When this report was published Ontario had almost twice as many LDCs as all of the remaining provinces combined and 29 LDCs in Ontario that had fewer than 12,500 customers each. These ‘small’ LDCs account for over a third of all the utilities in Ontario, but less than 4% of the province’s electricity customers

B. Premier’s Advisory Council on Government Assets

Sometime referred to as the “Clark Report”. This advisory council was tasked with on how Ontario can maximize the value of its key provincial assets, including Hydro One. Delivered in **November, 2014**, this report made two recommendations related to Local Distribution Companies:

- Support the recommendations of the Ontario Distribution Sector Review Panel Report (see above).
- Sell Hydro One assets to act as a catalyst to broader consolidation across the Province.

C. Market Activity – What’s Happening in Other Municipal Jurisdictions

Recent consolidation activity in Ontario’s LDC sector:

- PowerStream took a 50% interest in Collus Utility Corp. from the Town of Collingwood (2012)
- Hydro One purchased Norfolk Power (2014), Woodstock Hydro (2014) and Haldimand County Hydro (2015)
- Cambridge and North Dumfries Hydro Inc. acquired Brant County Power (2014)
- Sale of 50 percent sale of Innisfil Hydro to Epcor (City of Edmonton)

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- Hydro One negotiating purchase of Orillia Power Distribution corporation (September 2015)
- Ongoing merger negotiations– Horizon Utilities, Powerstream, Enersource, Hydro One Brampton
- Hydro One IPO - A preliminary prospectus was filed in mid-September with the Ontario Securities Commission and its counterparts across Canada, providing a detailed overview of Hydro One, which lists \$22.6 billion in total assets.

D. Role Clarity: GMHI, Shareholder and the Shareholder Agreement

The division of responsibility for decisions on major issues affecting GMHI and its Subsidiaries is governed by the City-GMHI Shareholder Declaration and the GMHI-GHESI Shareholder Declaration.

The principles set out in the City-GMHI Shareholder Declaration which describe the relationship between the City and GMHI are:

- a) A Shareholder Declaration for municipal entities should foster and reinforce a collaborative relationship and shared values among all parties and recognize that the interface between the worlds governed by the Municipal Act (public sector) and the OBCA (private sector) requires mutual respect, understanding and flexibility and regular communication between GMHI and the City regarding the activities of GMHI and its Subsidiaries. Such communication should take place whether or not such activities would require the approval of the City.
- b) The activities of the City and GMHI which may be applicable to the Community Energy Initiative shall be a fundamental aspect of the relationship between GMHI and Envida.
- c) Decision making authority shall be clearly assigned to the City and GMHI, recognizing that the GMHI Board is the primary decision-making body of the corporation.
- d) The authority of the GMHI Board will be accompanied by clearly articulated reporting to ensure transparency, accountability and recognition of its status as a public sector entity and of the role of the City as the ultimate authority over GMHI, subject to the fiduciary responsibilities of directors of the GMHI Board.
- e) In making decisions concerning GMHI Subsidiaries, the GMHI Board and management of GMHI shall act in a commercially reasonable manner consistent with the City's requirements from time to time and having regard to the City's Strategic Plan.

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More specifically, as it relates to the Shareholder Agreement with GMHI Article 11, , sets out the decisions which are reserved to the City as follows:

Article 11 DECISIONS RESERVED TO THE SHAREHOLDER

11.01 Matters Requiring Shareholder Approval under the OBCA

GMHI shall not take any of the following actions without the approval of the City:

- a) Amend or repeal its articles of incorporation;
- b) Amalgamate with another corporation, apply to continue as a body corporate under the laws of another jurisdictions, merge, consolidate or reorganize or approve or effect any plan of arrangement, in each case whether statutory or otherwise;
- c) Take or institute proceedings for any winding up, arrangement, reorganization or dissolution;
- d) Create new classes of shares or reorganize, consolidate, subdivide or otherwise change its outstanding securities;
- e) Sell or otherwise dispose of, by conveyance, transfer, lease, sale and leaseback, or other transaction, all or substantially all of its assets or undertaking;
- f) Change the auditor;
- g) Make any changes to the number of directors comprising the Board; or,
- h) Enter into any other transaction or take any other action that requires shareholder approval pursuant to the OBCA.

11.02 Other Matters Requiring City Approval

Without the prior written approval of the City, GMHI shall not:

- a) Make representations or promises of any financial incentives or similar inducements that are binding on the City;
- b) Issue publicly traded debt, or any debt instruments with real or implied recourse to, or guarantees from, the City or any borrowing that, in the opinion of the City CFO, will have a negative impact on the City's credit rating;
- c) Sell any shares of a GMHI Subsidiary;
- d) Amend the dividend policy approved by the City in accordance with Article 5 or,

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- e) Approve an agreement for a transaction for the disposition or acquisition, whether by purchase, merger/amalgamation or otherwise, where the transaction involves GHESI or where the transaction has a value greater than 25% of the book value of GMHI on a consolidated basis.

In drafting this section, and particularly in the areas of sale of assets or shares, the intention was to allow GMHI to pursue opportunities without receiving approval from the City in advance, however requiring City approval to be obtained for the final transaction. This is subject however to the positive obligation and principles set out in the Declaration - that GMHI and the City communicate freely, whether or not the activities of GMHI would require City approval.

Similarly, the GMHI-GHESI Shareholder Declaration contains the same broad principles and the same requirement that GMHI approve any final decision on the matters set out in Article 9 in that document, as follows:

Article 9 DECISIONS RESERVED TO THE SHAREHOLDER

9.01 Matters Requiring Shareholder Approval under the OBCA

GHESI shall not take any of the following actions without the approval of GMHI:

- (a) Amend or repeal its articles of incorporation;
- (b) Amalgamate with another corporation, apply to continue as a body corporate under the laws of another jurisdictions, merge, consolidate or reorganize or approve or effect any plan of arrangement, in each case whether statutory or otherwise;
- (c) Take or institute proceedings for any winding up, arrangement, reorganization or dissolution;
- (d) Create new classes of shares or reorganize, consolidate, subdivide or otherwise change its outstanding securities;
- (e) Sell or otherwise dispose of, by conveyance, transfer, lease, sale and leaseback, or other transaction, all or substantially all of its assets or undertaking;
- (f) Change the auditor;
- (g) Make any changes to the number of directors comprising the Board; or,
- (h) Enter into any other transaction or take any other action that requires shareholder approval pursuant to the OBCA.

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9.02 Other Matters Requiring GMHI Approval

Without the prior written approval of GMHI, GHESI shall not:

- a) Make representations or promises of any financial incentives or similar inducements that are binding on GMHI;
- b) Issue publicly traded debt, or any debt instruments with real or implied recourse to, or guarantees from, GMHI or any borrowing that, in the opinion of the CFO, will have a negative impact on GMHI's credit rating;
- c) Issue any new shares of GHESI;
- d) Amend the dividend policy approved by GMHI in accordance with Article 5 or,
- e) Approve an agreement for a transaction for the disposition or acquisition, whether by purchase, merger/amalgamation or otherwise.

Process, Communication and Authorities

Either GHESI or GMHI could take the lead in consideration of any disposition or acquisition proposal relating to GHESI. If a transaction relating to GHESI was being contemplate by GHESI, the GHESI Board would communicate this up to the GMHI Board who would then communicate this to the City Shareholder Representative. If a transaction relating to GHESI was being contemplated by the GMHI Board, GMHI would communicate this to the City Shareholder Representative.

In either case, the Shareholder Representative may choose to obtain instructions from Council regarding their position on a potential sale of GHESI.

If Council was adamantly opposed, GHESI and/or GMHI would be required to take into account the City's position knowing that it was unlikely to receive final approval. If the GHESI Board was opposed to a GMHI proposal for sale or acquisition of GHESI, the transaction could still be approved by the GMHI Board and Council without the GHESI Board approval.

If Council was in favour of pursuing options, GMHI would take the lead in negotiating the transaction, with reports back to the City through its Shareholder Representative, on a regular basis. GMHI would also work with GHESI to ensure the Shareholder direction was implemented.

If an agreement was obtained, the GHESI Board would approve the transaction and recommend approval to the GMHI Board. If the GMHI Board approved the transaction, the Board would recommend that Council provide the final approval for the transaction

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Conclusions

Existing governance structures and the strategic alignment supported by the existing Shareholder Agreement between the City as Shareholder and GMHI will support full, open and collaborative consideration of scenarios related to LDC consolidation.



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