

DATE September 29, 2008

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

O Canada
Silent Prayer
Disclosure of Pecuniary Interest

SPECIAL MEETING WITH RESPECT TO THE PROPOSED MERGER WITH HORIZON UTILITIES

PRESENTATIONS

Guelph Hydro Incorporated / Guelph Hydro Electric Systems Incorporated:

- Jasmine Urisk
- Art Stokman

- Hans Loewig, Chief Administrative Officer

DELEGATIONS (Councillor Findlay)

"THAT persons desiring to address Council be permitted to do so at this time."
(limited to a maximum of five minutes)

- a) Patrick Vlanich on behalf of the International Brotherhood of Electrical Workers, Local Union 636 (Tracy O'Meara also available to answer questions)
- b) Lloyd Longfield on behalf of the Guelph Chamber of Commerce

CORRESPONDENCE

- Colleen Pearse
- Stephen Rodd
- Magee McGuire

1. Hydro Merger – Report of the Chief Administrative Officer

THAT a decision be made by Council as the sole shareholder, on the recommendation from the Board of Directors of Guelph Hydro Inc.

2. Recommendation of the Board of Directors of Guelph Hydro Inc.

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

3. Approval Resolutions if Merger Approved

In the event that City Council makes the decision to accept the recommendation of the Board of Directors of Guelph Hydro Inc. for the merger, City Council would need to pass the resolutions attached to the report of the Chief Administrative Officer as Appendix B.

BY-LAWS

Resolution – Adoption of By-laws (Councillor Findlay)

"THAT By-law Number (2008)-18644 is hereby passed."

By-law Number (2008)-18644 A by-law to confirm the proceedings of a meeting of Guelph City Council held September 29, 2008.	To confirm the proceedings of City Council meeting held September 29, 2008.
--	---

ADJOURNMENT

Dear Mayor and Council Members,

I am writing as a 17 year Employee of Guelph Hydro Electric Systems. I spent the first 25 years of my life in Guelph and still reside within Wellington County. I have many, many misgivings about the proposed merger of your local utility with Horizon Utilities.

Currently, we are a mid-sized local distribution company. We have been in the business of serving Guelph for over one hundred years. We are 91 highly skilled individuals who work with pride and integrity. We are honoured that our community thinks highly of our company as was demonstrated in the results of our most recent customer survey. Our distribution system is top notch and our customer service is excellent. The technology we utilize is more advanced than what many larger utilities in the province use.

First, I am at a loss to understand why the City of Guelph would even consider giving up control of this local treasure. There have been wild promises of doubled dividends that will be realized by the shareholder, simply through economies of scale. Take a second to think about how great those economies of scale would have to be in order to double your 1.5 million dollar dividend to 3 million dollars. While considering this, keep in mind that Horizons distribution system needs considerable updating and upgrading just to reach the standard that we are at in Guelph now, let alone keep up with routine maintenance. Also, every utility in the province has to change every meter to meet upcoming new regulations in metering (time of use or smart metering). This will be done at considerable cost to every utility in the province. Dividends can only be paid based on "cash on hand", it is not a matter of assets but how much you have to give. To even propose that dividends can be doubled is a ridiculous statement to make.

Next, the reduction of customer rates is being announced as 20%. That possible 20% reduction is only on the distribution portion of the bill which currently accounts for about 20% of a customer's bill. Furthermore, that reduction is based on today's rates, although any savings wouldn't even begin until 2012 and would be accrued over a ten year period thereafter. 20% rate reduction on 20% of the bill sometime by 2022. And if the rates happen to go up? What happens to that 20% proposed reduction - then it's called rate mitigation. This means the rates will still go up, just maybe not as much. Maybe.

Also, special emphasis was placed on the fact that the Conservation and Demand Management department will be located in the Guelph facility. This entire department is currently five fulltime employees that are located in Horizon's Hamilton office. During the May 26th presentation to City Council it was stated that "Enhanced environmental stewardship and CEP support will be ensured through the establishment of a corporate-wide conservation and demand management function located in Guelph". Yes, this department may be located in Guelph but it will work for Horizon

Utilities. This department will be working to the corporate vision not Guelph's. Along this line consider the amount of employee displacement. About 25% of the employees of Guelph Hydro will be moved to either the Hamilton or Saint Catharine's locations. Also, about 17 Horizon employees will be relocated to Guelph. This puts almost 40 extra vehicles on the road. Let's assume that the people who are moved to Saint Catharine's move their families to that area. That will still leave about 32 more vehicles moving between Guelph and Hamilton on a daily basis. How does this fit in to Guelph's current environmental vision?

This leads me to my next concern. We have been given the impression that quite a battle was fought over representation on the Horizon Board within this newly merged company and that our Board would settle for nothing less than 3 of the 13 proposed Board members being from the Guelph area and representing Guelph interests. This is all based on basic math. If the merge does go through the City of Guelph will own about 24% percent of the company which coincidentally will be the same percentage of representation on the Board. What happens when Horizon continues to merge and acquire more territory in this province, as they have been quite vocal about? Well, then the City of Guelph's percentage of ownership will drop and correspondingly representation on the Board will drop. In the future it is quite probable that there won't be any specific person or persons on the Board to represent our community's interests. It is a Board made up to look after the corporate interests not the communities where the business satellites are run from.

Lastly, why Horizon Utilities? We have been told during our employee "Town Hall" meetings that this proposed merger is thought to be the best fit. In reality this is the only utility that the Guelph Hydro Board of Directors has even talked to. Why jump at this? Would it not be prudent to at least look into other opportunities before jumping at the first offer that knocks at our door? Is this the best way to conduct business?

It is my hope that City of Guelph Council will take a long hard look at this proposal. Test the numbers using real scenarios. Do not give up this local treasure without exhaustive research to ensure that you are absolutely without a doubt making the best decision on behalf of the city. Don't let hindsight be 20/20. Once your utility is gone, it's gone.

Yours very truly,

Colleen Pearse
Guelph Hydro Electric Systems Inc.

The Proposed Merger of Guelph Hydro Inc. with Horizon

by R. Stephen Rodd
revised 3 June 08

I find it very troubling to study the proposal for Guelph Hydro Inc. (GHI) to merge with the enlarged Horizon system based in Hamilton.

There are two quite distinct aspects to this idea. The first facet is one which I admit is beyond my expertise. I am not an accountant or a financial management economist and of course I do not have access to the information which has been examined by Hydro experts to search for savings and efficiencies.

I do have two observations to make on this side, however. In my opinion, the public consensus appears to be that amalgamation rarely provides the savings which were hypothesized at first. The actual experience, whether it is the idea of combining two university departments, two municipalities, two Ministries, or two companies is that when the two groups have to live together, often with job losses, is that the unit does not get along as well together as they had before. The lost positions turn out to have had unrealized advantages that had been overlooked. One unit will feel that it has been mistreated or undervalued and seek to be compensated for the losses.

My other comment on the financial accountant's side of the proposal is when two partners are unequal in size, they have to negotiate with each other, in an unequal relationship and the minority side does not fair well. The accounting analysis looks at each matter as if all dollars are equal, but pride, prestige and loyalties are involved. One side will end up with hurt feelings and their staff members will feel they have been treated as mediocre or treated unfairly. A large factor in labour productivity is the matter of morale and loyalty; all of that will be disturbed and this subtle factor will show up in balance sheets.

In Community planning we must teach students about the need to be familiar with many tools to meet the variety of situations when helping to make a healthier community. One saying is that if the only tool you have is a hammer, very quickly everything begins to look like a nail. I often feel that accountants may have the same problem, because their main tool, speaking as a non-accountant, is to add, subtract and multiply dollars. Everything is evaluated in terms of dollars. Nothing else is visible on a spreadsheet. However, Guelph has embarked on a Community Energy Plan that is based on diverse goals that are beyond the accountant's spreadsheet.

In Ontario public utilities for more than the last one hundred years we have had local public ownership of and accountability of the management of the utilities. The merger with Horizon may weaken this product of the reform movement for urban government.

A century ago the urban reform movement in municipal government found that enormous gains in efficiency and improved service were realized when the Province put pressure and incentives to get rid of private companies which had abused the community with their monopoly power. Sir Adam Beck made a great contribution by his pioneering use of utility commissions.

In my mind, the greatest possible reason to back off this proposal is that the City of Guelph has launched the Community Energy Plan, as a pioneer in Ontario and Canada. The Plan is extraordinary as a community plan. It is based not only on dollar savings for our local community by becoming more efficient in energy use but also the beneficial impact on the environmental and ecological systems of the world. No other local utility in Canada has taken on this challenge and our successful implementation will make Guelph a model in energy use and ethical behaviour to be followed elsewhere. It is essential that the merger be structured in a way to ensure that the Guelph community will not be handicapped or held back by other partners who do not have the same environmental commitments which are ethical commitments essentially.

With GHI in a minority situation, the enlarged merged company would almost certainly sacrifice this ethical commitment by Guelph. This loss is something our world cannot afford. In the proposal, thus far, I see no commitment, promise or will to guarantee that the Community Energy Plan will be protected for Guelph or enlarged to include Hamilton. There is no evidence that those cities have undertaken the costs and adjustments in their cities to adopt this Plan.

Hamilton and St. Catharines (Horizon) must leave us alone to do our pilot study with the Community Energy Plan, OR they must walk in our shoes by formulating their own Energy Plans.

Magee McGuire
Guelph

May 26, 2008

Re: Proposed Hydro Merger

Dear Mayor Farbridge,

I am writing this to you because I have just read about the meeting regarding the proposed Hydro merger tomorrow evening. Unfortunately, I have a board meeting and can not attend. I hope this note will give you some indication of my concerns briefly. I was pleased to read that you plan on having community open houses.

First of all, I don't know if a small hydro company like ours could experience a hostile takeover, but I do believe that a bigger company would be very attractive. I should consider this in my discernment. It's considered fashionable to merge. To me, it might reflect a lack of innovation and leadership ability.

Next, I am not clear about the role of Hydro in issuing our water bill. Is there some convoluted way that the next chess player could spin the direction of a merged company? Would it separate hydro from water as two utilities? Guess what...another bill for everyone..(just like the union gas split with rental and maintainance services doubling in cost to the consumer in less than ten years). It is old school that one never gives up ownership of rail, jail, water or Hydro utilities to be sustainable. The corollary is that one can gain wealth and stability by acquiring all of these commodities.

These are just some instant questions that I would appreciate a balanced perspective on.

Next, I have had experience with the Hamilton community. Their councils have a history of making poor decisions and repeating their mistakes with public-private partnerships because they did not pre-establish indicators and outcome measures to reflect on. In this case it was a waterworks management decision. It's now costing the taxpayers dearly due to lack of foresight.. Communication with adhoc community groups has not been fruitful for the community(eg: Red River Valley decision). I perceive a partnership as requiring a very good communication and building capacity through mutual collaboration. There is no evidence for nurturing these skills in their leadership. Another example of their values is the great Gage Park. It provides a canope of green in a cement city and is always in some state of neglect. Planning "green" is not an obvious priority.

St. Catherines is making changes without community consultation in its health care decisions. I have been down there assisting when the community has attempted to bring important issues to public awareness. The people for the most part are very comfortable financially (think Niagra-on-the Lake) and prefer not to get involved. This is hard on any group trying to bring an issue to council with substantial support. It's an uphill battle. It has been with the help of outsiders that decisions have been postphoned. Guelph has fared far better in its community management of health services than St. Catherines in that context.

This proposed merger is like a marriage...we need to have a lot in common. Show me the evidence of our mutualities and especially how Guelph benefits better from an agreement like this. What barriers will it create for Guelph's vision, values and interests?

It's off topic, but I'd prefer to build up a city of alternative electricity technologies and create an excess to load to our grid to sell to others. Guelph's community is more co-operative and could meet such a challenge. I don't believe the other communities can organize this way. Their characters are different. Maybe we could share our knowledge with them..to inspire proactive collaboration. To reduce energy consumption takes a whole community to believe it is needed. There is no community forum that engages its citizens for that in those cities.

I look forward to the open houses. Please share this with your council as you see fit.

Warm regards,

Magee McGuire



395 Southgate Drive
Guelph, Ontario, N1G 4Y1
Fax (519) 836-1055
www.guelphhydro.com

September 22, 2008

Recommendation Statement:

The Board of Directors of Guelph Hydro Inc. recommends to its shareholder, the City of Guelph, the acceptance of the business case and accompanying legal agreements to merge the assets of Guelph Hydro Electric Systems Inc. (GHESI) with those of Horizon Utilities Corporation. This merger would be completed upon acceptance and ratification of City Council for the Municipality of the City of Guelph, the Ontario Energy Board (OEB) and any other Government bodies as required by legislation of the Province of Ontario.

Highlights of Business Case Benefits

The following benefits to be achieved as a result of this merger are derived from key business and community principles that were identified by key stakeholder groups and reviewed with Council prior to merger discussions:

1. **OPPORTUNITY AND FAIRNESS TO EMPLOYEES:**
The merger will provide opportunities and fair treatment to employees. The merged organization is committed to being an employer of choice.
2. **FINANCIAL ADVANTAGES:**
Economies of scale gained through operational efficiencies will result in lower overall distribution rates for Guelph's electricity customers when new rates are filed with the OEB while ensuring that a reliable and safe electricity infrastructure is sustained in the service area.
3. **SIGNIFICANT LEVEL OF OWNERSHIP:**
The City of Guelph will own a significant interest (24.25%) in a regional utility serving over 280,000 customers with assets of \$0.5 billion. This will provide the Guelph community with an effective voice in the management of the utility and provide substantial long term financial returns to the City.
4. **RESOURCES TO SUPPORT the Community Energy Plan (CEP):**
The merged entity will have the resources to support the City of Guelph's Community Energy Plan with the addition of specialized resources focused specifically on conservation and demand management programs. This corporate function will be located in Guelph to service the entire company.

5. **INNOVATIVE USE OF SOUTHGATE:**

The current Southgate location will continue to serve as a major facility in the newly merged company. In addition to regional operations and engineering, it will house many critical functions, including Information Technology, Conservation and Demand Management, GIS mapping, and Procurement for the entire organization.

6. **ADVANCES IN TECHNOLOGY:**

The depth of capital and human resources in the merged company will enable rapid deployment of advanced technology including smart meters and control systems. This will enable new ways to reduce electricity demand and more efficient forms of distributed generation and cogeneration.

7. **INFLUENCE IN THE FUTURE:**

Considerable control has been retained for Guelph Hydro Inc and the City of Guelph through a comprehensive Shareholder Agreement. This includes proportional Board representation and unanimous shareholder and Municipal approval of significant transactions such as future mergers, acquisitions, or the sale of the business.

Background

With the support of its Board and Municipal shareholder, GHESI entered into a Memorandum of Understanding (MOU) with Horizon Utilities Corporation on June 28, 2007 to jointly explore a business case for merging the two companies.

As noted , the MOU sets out key principles which address important business and community interests of our community, customers, employees, and Municipal shareholder. These principles have been addressed and satisfied and served as the primary framework for the development of the business case and legal documents.

A Strategic Task Group was formed to lead the process with the following individuals:

Jasmine Urisk	Chair, GHI Strategic Task Group & Vice-Chair, GHESI and GHI
Jane Armstrong	Director, GHESI
Brian Cowan	Director, GHESI and GHI
Ian Miles	VP Business Development and CFO, GHI
Art Stokman	President, GHESI
Nicole Mailloux	VP Human Resources, GHESI

The process of developing the Business Case and Legal Agreements included retaining independent advisors to ensure consistency of assumptions and methodology.

The following table highlights the advisors and the roles they played:

Advisor	Retention	Roles
Borden, Ladner, Gervais LLP	Joint GHESI/Horizon	<ul style="list-style-type: none"> • Facilitate legal negotiation • Draft legal agreements • Legal due diligence • Validate regulatory assumptions • Review customer rate impact analysis
Deloitte LLP	Joint GHESI/Horizon	<ul style="list-style-type: none"> • Develop business valuation model • Prepare valuation reports using management assumptions • Conduct sensitivity analysis on key assumptions • Prepare valuation estimates using prior transactions and comparable public companies
Kinectrics	Joint GHESI/Horizon	<ul style="list-style-type: none"> • Technical due diligence • Validate management's capital expenditure plans • Identify environmental issues
Gowlings LLP	GHESI/GHI	<ul style="list-style-type: none"> • Provide independent legal advice

In addition to these advisors, the City of Guelph retained the law firm of Aird and Berlis for independent legal advice and BDR for independent financial advice.

Public Consultation

Since presenting its recommendation to Council on May 26th, GHESI has participated in numerous comprehensive sessions to discuss the details and merits of the proposed merger transaction. These sessions have included:

- A public open house sessions June 19, 2008
- Presentation and discussion with the Chamber of Commerce
- Presentation and discussion with the Rotary Club
- Presentation and discussion with the Kiwanis Club
- Discussion with the Friends of Guelph
- Discussion with the Guelph Developers Association
- Town Hall meeting in Ward 2
- Hosting a web site to publish merger related documents
- Hosting a web based Q&A to address specific questions from the public
- Meetings with Employees and the IBEW

TO **Guelph City Council**

SERVICE AREA Corporate Administration
DATE Monday, September 29, 2008

SUBJECT **Hydro Merger**
REPORT NUMBER

RECOMMENDATION

WHEREAS the Board of Guelph Hydro Inc. (hereinafter referred to as "GHI") has presented a business case for the proposed merger between Guelph Hydro Electric Systems Inc. (hereinafter referred to as "GHESI") and Horizon Utilities Corporation (hereinafter referred to as "HUC");

AND WHEREAS there is a recommendation to City Council from the Board of GHI to proceed with the merger;

AND WHEREAS the Council as the sole shareholder of GHI, has engaged the services of independent financial and legal consultants to review the business case for the proposed merger;

AND WHEREAS the Council has asked City staff to work with the Board of GHI and the City's independent consultants to review the business case;

AND WHEREAS there has been considerable public consultation as part of the due diligence process;

AND WHEREAS from a staff perspective, an appropriate due diligence process has taken place and there is a sound business case in support of the proposed merger;

IT IS THEREFORE RECOMMENDED THAT a decision be made by Council as the sole shareholder, on the recommendation from the Board of Directors of Guelph Hydro Inc.

And further, in the event that City Council makes the decision to accept the recommendation of the Board of Directors of Guelph Hydro Inc. for the merger that City Council pass the resolutions attached to this report as Appendix (B).

BACKGROUND

The City of Guelph is the sole shareholder of Guelph Hydro Electric Systems Inc. (GHESI) which is managed and operated by Guelph Hydro Inc. (GHI). The Board of GHI is appointed by City Council acting as the sole shareholder of the company.

In October 2006 the Province of Ontario introduced a public sector only "transfer tax holiday" for a 2 year period to expire on October 17, 2008.

We understand that GHI had approached neighbouring utilities in respect to partnership opportunities which resulted in little interest. However, in the spring of 2007 discussions with Horizon Utilities Corporation (HUC) resulted in a memorandum of understanding to explore merger opportunities between HUC and GHESI. This was reported to City Council (as shareholder) and the community in July, 2007, with the understanding that a business case would be prepared by staff of both utilities with the assistance of legal and financial advisors representing the groups involved in preparing and reviewing the business case.

Once the business case was completed it was reviewed by GHI with advice from other independent financial and legal advisors.

As a result of the reviews by the respective utilities a recommendation was brought forward to the respective shareholders to merge the two utilities. When this recommendation was brought forward by GHI to City Council in May 2008, it was also proposed that the shareholder undertake their own independent review of the business case and the proposed agreements along with a review of the options available to the City.

Aird & Berlis as legal advisors and BDR as financial advisors undertook a thorough peer review of all the documentation, agreements, financial assumptions and modeling of the business case. In fact, as part of the process BDR also provided an options analysis workshop in July 2008. In both cases, with some modifications to the terms of the agreements, both independent advisors confirmed that the business case was fair and reasonable and the merger with HUC has sound business and financial benefit to Guelph and its residents.

Both GHI and City Council conducted separate public consultation sessions to allow the public, business community and interest groups the opportunity to comment and provide input.

We understand that both the City of Hamilton and City of St. Catharines as shareholders of HUC have unanimously voted their approval of the merger recommendation.

LEGAL REPORT

Attached as Appendix A is a summary report from Aird & Berlis on their review and findings of the merger agreements and documents.

HUMAN RESOURCE STRATEGY

The Director of Human Resources conducted a review of the HR Strategy and also met with representatives of GHI. His confidential report advises that there is a good communication strategy and that the change management plan is in keeping with

best practices. In his discussions with GHI, the assumptions and strategies proposed were reasonable and acceptable.

FINANCIAL IMPLICATIONS

Value of Guelph's proportionate share of ownership in Mergco

The calculations of the GHI Board's financial advisors analyzing the merger indicated that Guelph's value in the merged company should be in the range of 21% to 26%. Through negotiation, the shareholders arrived at the following proportionate ownership:

Guelph Hydro Inc.	24.25%
St Catharines Hydro Inc.	15.98%
Hamilton Utilities Corp	59.77%

BDR analyzed the relative value of GHESI as a percentage of the total value of the merged GHESI/Horizon entity and confirmed the relative value was between 21.1% and 25.1%. With its expertise in evaluating the business case and financial information in the context of Ontario's regulated electricity market, BDR modelled approximately 150 scenarios using assumptions and methodologies applied consistently to both Horizon and GHESI.

BDR has provided its professional opinion that the conclusions reached with respect to the proportionate values of proposed ownership for Guelph and Horizon are fair and reasonable, from a financial point of view.

Guelph's 24.25% ownership of the combined fixed assets in the merged company is worth \$5.7 million more than the book value of its assets going into the merger. The premium over book value is attributed to GHESI in consideration for GHESI's higher forecasted growth rate, relative to Horizon's.

The valuation is based on the merger being eligible for the exemption from transfer tax. After October 17, 2008, the transfer tax would be equivalent to \$33 million.

Cash Flows to Guelph as a Shareholder

Several factors influence the amount of dividends payable to the shareholder:

- OEB permitted rate of return, based on efficiency of the utility,
- Capital structure (debt/equity ratio) required by the OEB
- Current year earnings
- Dividend policy contained in the shareholder agreement

The OEB approves the rates that can be charged to customers, including the return on shareholder's investment, and therefore the OEB directly influences the revenue stream and net income of the utility. The approved rate is influenced by the efficiency of the utility's cost structure, in comparison to other Ontario Local Distribution Companies (LDC's).

The Board anticipates annual savings of \$3.9 million annually, through a detailed review of expenditures which helped identify opportunities for productivity

improvements and reductions in expenses such as administrative overhead, legal costs associated with regulatory filings, and technology investments. Further, the increased size of the merged organization, and Horizon's credit rating would allow the merged entity to more efficiently access public debt markets, resulting in lower interest expenses.

The Board advises that these economies of scale will result in a stable and growing source of dividends. The Board further advises of its concern, that without a merger, it will not be able to realize efficiencies to meet the OEB's expected cost structure and could thus be subjected to a penalty in the form of a rate cap, which would result in reduced revenues and therefore reduced dividends to the shareholder.

Productivity benefits initially accrue to the shareholder until distribution rates are re-filed with the OEB, which the Board expects will happen in 2012. The benefits thereafter, accrue to customers.

The Dividend Policy for Mergeco as provided in the shareholder's agreement, subject to conditions related to maintaining financial stability, is that regular dividends would be paid at a target rate of 60% of annual net earnings.

GHESI staff advise that, *under an equivalent dividend policy (60% payout of net earnings), Guelph's dividends are projected to be \$400,000 higher in 2009, and \$600,000 higher in 2010 in the merged entity, than if GHESI does not merge.* This is due to the shared efficiency savings, as well as the premium percentage of ownership (1.5%) it has negotiated in the merged entity. GHI's projected share of dividends in a mergeco scenario for 2009 are \$3.5 million.

The City currently has a dividend policy in its shareholder declaration with GHI that provides for an annual dividend to the City of \$1.5 million. The balance of earnings from GHESI have, in the past, been reinvested in GHESI or retained in GHI and invested in a number of Community Energy Plan initiatives, rather than paid out to the City. The City currently uses the \$1.5 million dividend as part of its operating budget.

As far as capital structure, the OEB is requiring a move towards a capital structure of 60% debt/ 40% equity. Horizon Mergeco is currently targeting a structure of 50% to 55% debt. Special dividends may be paid by Horizon Mergeco to Guelph to maintain this capital structure. As well, a one-time pre-merger dividend would be payable from GHESI to GHI of approximately \$2 million, in order to achieve the initial targeted capital structure.

Note Payable

GHESI currently has a Note Payable to the City of Guelph in the amount of \$30 million, which bears interest at an OEB approved rate of 6.25% (\$1,875,000), and is payable on demand within 18 months. The City currently invests the interest in its capital reserves, towards the construction of major capital projects.

The promissory note does not provide for any pre-payment rights by GHESI. The Merger Participation Agreement provides that the Promissory Note will continue as an obligation of the newly created post-merger entity to the City of Guelph.

Provincial regulations which limit the term of certain investments to 10 years were thought to be applicable to the promissory note, requiring it to be monetized by February 2011. Staff requested legal interpretation of the legislation and are advised that the original promissory note can continue to be held for longer than 10 years, but not any refinancing, renewal or replacement thereof.

The City's future use of dividends (\$3.5 million annually) and interest (\$1.875 million annually), the one-time recapitalization dividend (\$2 million) as well as monetization of the promissory note (\$30 million) from its hydro investments should be incorporated into the city's upcoming long range financial planning exercise.

Customer Impact

The Board advises that customer distribution rates are anticipated to decrease by an average of 20% when the merger integration is complete and rates reset in 2012. Savings accruing to Guelph customers are expected to total over \$40 million over a 10 year period. The following chart, provided by GHESI staff shows the expected impact on customers of various classes:

Distribution Rate Comparison – Monthly Rates Effective Upon Harmonization (2012)

	GHESI	Horizon Pre Merger	Horizon Post Merger	Monthly Savings vs GHESI
Average residential rate per month	\$ 27.50	\$ 22.67	\$ 22.67	\$ 4.83
Average small commercial <50kW	\$ 66.25	\$ 56.83	\$ 56.67	\$ 9.58
Average mid-large >50kW	\$ 958.33	\$ 666.67	\$ 704.17	\$ 254.17
City of Guelph total of all accounts	\$ 27,255	N/A	\$ 23,303	\$ 3,952

The Board has provided the following statistics on service reliability from the Canadian Electrical association and a survey by the MEARI Group (which is an association of large distributors):

Reliability Statistics

	<u>5-Year Average (2002 - 2006)</u>		
	GHESI	Horizon	Ontario Average (2)
Index of Reliability - average number of minutes of outage per year (1)	38	56	96

This is an overall measure of the reliability of the distribution system. It is influenced by customer density, the age and condition of the distribution system, susceptibility to lightning and other weather related problems, tree trimming practices, speed of response crews, after hours availability and the scope of monitoring systems.

GHESI staff also provided additional information with respect to Customer Service:

Customer Service Statistics	<u>% of Electricity bill payers who are "very + fairly" satisfied</u>			
	2005	2006	2007	2008
GHESI	89%	89%	93%	91%
Horizon	82%	84%	86%	89%
National Average			88%	
Ontario Average			84%	

Source: Independent survey conducted by UtilityPULSE

ATTACHMENTS

Appendix A - Aird & Berlis report dated September 23, 2008

Appendix B - Resolutions in the event City Council approves the merger



Prepared By:
Hans Loewig
Chief Administrative Officer
519-837-5602
hans.loewig@guelph.ca

AIRD & BERLIS LLP

Barristers and Solicitors

MEMORANDUM

Date: September 23, 2008

To: City Council of The Corporation of the City of Guelph

From: Aird & Berlis LLP

Subject: Legal Report on Horizon Utilities Corporation/Guelph Hydro Electric Systems Inc. Merger Transaction Documents.

1. INTRODUCTION

Aird & Berlis LLP ("A&B") has been retained as independent legal advisors by the City of Guelph (the "Guelph") to assist Guelph in its review of legal documentation concerning the proposed merger of Guelph Hydro Electric Systems Inc. ("GHESI") and Horizon Utilities Corporation ("Horizon"). This memorandum summarizes the principal transaction documents in connection with the proposed merger of the electricity distribution corporations serving customers in the Cities of Hamilton, St. Catharines and Guelph.

2. THE TRANSACTION**(a) Pre-Merger Corporate Structure**

GHESI is the electricity distribution corporation that serves the residents and businesses of the City. GHESI is 100% owned by Guelph Hydro Inc. ("GHI"). GHI is 100% owned by the City.

Horizon is the electricity distribution corporation that serves the residents and businesses of the City of Hamilton ("Hamilton") and the City of St. Catharines ("St. Catharines"). Horizon is 100% owned by Horizon Holdings Inc. ("Horizon Holdco"). Horizon Holdco is owned 78.9% by Hamilton Utilities Corporation ("HUC") and 21.10% by St. Catharines Hydro Inc. ("SCHI"). SCHI is 100% owned by St. Catharines and HUC is 100% owned by Hamilton. Horizon Energy Services Inc. ("HESI") is a wholly-owned subsidiary of Horizon Holdco which was formed to acquire certain businesses, such as the meter servicing business being conducted by Horizon, and which are appropriately held in a company that is not regulated by the Ontario Energy Board ("OEB").

(b) The Proposed Transaction

The proposed transaction involves the statutory amalgamation under the *Ontario Business Corporations Act* ("OBCA") of Horizon and GHESI (the "Merger"), the electricity distribution corporations, to form a new merged corporation and continue as Horizon Utilities Corporation

(“Mergeco”), a wholly-owned subsidiary of Horizon Holdco. Following the Merger the shares of Horizon Holdco would be owned by HUC, SCHI, and GHI in the following percentages :

HUC	59.77%
SCHI	15.98%
GHI	24.25%

The proportionate shareholding of HUC, SCHI, and GHI in Horizon Holdco has been determined by the parties through negotiation and based on a comparative valuation prepared by Deloitte.

These valuations have been reviewed independently by BDR, independent financial advisors to Guelph.

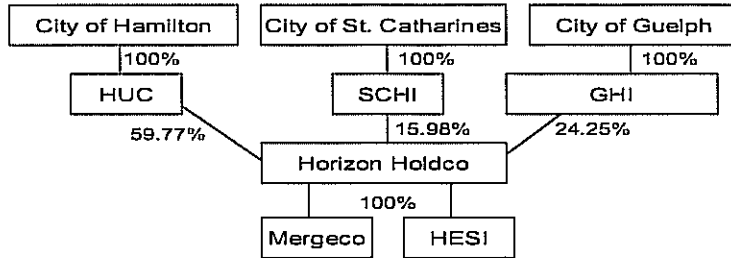
3. OVERVIEW OF KEY AGREEMENTS

The principal documents that are required to implement the Merger (the “Transaction Agreements”) and which have been prepared in draft form for review by the boards of HUC, SCHI and GHI and their jointly retained legal counsel and financial advisors are as follows:

- (a) Merger Participation Agreement among HUC, SCHI, GHI, Horizon Holdco, GHESI and Horizon (the “Merger Agreement”);
- (b) Amalgamation Agreement among GHI, Horizon Holdco, GHESI and Horizon for purposes of effecting the Merger pursuant to the OBCA;
- (c) Shareholders Agreement among HUC, SCHI, GHI and Horizon Holdco as shareholders of Horizon Holdco (the “Shareholders Agreement”);
- (d) Merger Co-operation Agreement among the City of Hamilton, the City of St. Catharines and the City of Guelph (the “City Agreement”); and
- (e) new Shareholder Declarations for each of Hamilton, St. Catharines and Guelph which relate only to Horizon Holdings and Mergeco (the “New Shareholder Declarations”).

4. CORPORATE STRUCTURE

The following is the proposed corporate structure following the merger:



5. MERGER AGREEMENT

The Merger Agreement contains comprehensive representations and warranties concerning Horizon and GHESI and covenants concerning the manner in which the amalgamation of Horizon and GHESI will proceed. The parties to the Merger Agreement are HUC, SCHI, GHI, Horizon Holdco, GHESI and Horizon.

6. SHAREHOLDER AGREEMENT

The Shareholder Agreement deals with governance of Horizon Holdco, Mergeco and HESI, and transfers of shares in Horizon Holdco.

7. MERGER COOPERATION AGREEMENT AMONG THE MUNICIPALITIES

This agreement sets out certain understandings and obligations of the municipalities with respect to the Merger, including approval of the Merger of Horizon and GHESI on the terms and conditions set out in the Merger Agreement (including the allocation of shares among HUC, SCHI and GHI as well as approval of the Merger Agreement and the Shareholders Agreement, and the New Shareholders Declaration relating to Mergeco).

8. NEW SHAREHOLDER DECLARATIONS

New Shareholder Declarations incorporate certain approval provisions contained in the draft Shareholders Agreement between HUC, SCHI, Horizon Holdco and GHI in respect of the new amalgamated corporation Mergeco. Such Shareholder Declarations must be identical with respect to Mergeco.

APPENDIX B

Form of Resolution of Council of The Corporation of the City of Guelph

RE: GUELPH HYDRO ELECTRIC SYSTEMS INC.

RECITALS:

1. The Corporation of the City of Guelph (the “**City**”) is the sole shareholder of Guelph Hydro Inc. (“**GHI**”) and GHI is the sole shareholder of Guelph Hydro Electric Systems Inc. (“**GHESI**”), a licensed electricity distribution carrying on its business within the municipal boundary of Guelph and the Town of Rockwood;
2. Pursuant to the shareholder declaration dated November 1, 2000 (the “**Original Declaration**”) the approval of the City is required, *inter alia*, in respect of an amalgamation by GHESI with a non-related corporation;
3. The board of directors of GHI has requested that the City accept its recommendation, as contained in its Recommendation Statement dated September 22, 2008 (the “**GHI Recommendation**”) and submitted to Council, to approve the amalgamation (the “**Merger**”) of GHESI and Horizon Utilities Corporation (“**Horizon**”) which will result in the creation of a new merged corporation to continue under the name Horizon Utilities Corporation (“**Mergeco**”) pursuant to the terms and subject to the conditions of the merger documents described in City Staff Report (as defined below) and comprised of the following proposed documents:
 - (a) a merger participation agreement (the “**MPA**”) between GHI, Hamilton Utilities Corporation (“**HUC**”), St. Catharines Hydro Inc. (“**SCHI**”), Horizon Holdings Inc. (“**Horizon Holdco**”), GHESI and Horizon;
 - (b) an amended and restated shareholders agreement (the “**Shareholders Agreement**”) between GHI, HUC, SCHI and Horizon Holdco;
 - (c) an amalgamation agreement (the “**Amalgamation Agreement**”) between Horizon Holdco, GHI, Horizon and GHESI;
 - (d) an agreement among the City, City of Hamilton (“**Hamilton**”) and the City of St. Catharines (“**St. Catharines**”) (collectively, the “**Cities**”) relating to the co-operation of the municipalities with respect to the Merger (a “**Municipal Co-operation Agreement**); and
 - (e) an amended and restated shareholder declaration to be issued by the City relating to GHI, Horizon Holdco and Mergeco (the “**Shareholder Declaration**”);
4. Council has received a City staff report (the “**City Staff Report**”) dated September 29, 2008 with respect to the Merger and recommending a decision be made with respect to the GHI Recommendation;

NOW THEREFORE BE IT RESOLVED THAT,

1. the Merger based substantially on the terms and conditions set out in the MPA, the Shareholders Agreement and the Amalgamation Agreement is hereby approved and authorized to take effect following approval of the Merger by the Ontario Energy Board;
2. each of the MPA, the Shareholders Agreement and the Amalgamation Agreement is approved and authorized;
3. the execution by GHI and GHESI of the MPA, Shareholders Agreement and Amalgamation Agreement, as applicable, are approved and authorized;
4. the entering into the Municipal Co-operation Agreement by the City is approved and authorized;
5. the Shareholder Declaration is approved and authorized;
6. the Mayor and City Clerk are authorized to finalize, execute and deliver the Municipal Co-operation Agreement with such alterations, amendments, deletions or additions thereto as the Mayor and City Clerk shall determine to be necessary or appropriate, such determination to be conclusively evidenced by the execution thereof by the Mayor and City Clerk, and such execution shall be conclusive evidence that the Municipal Co-operation Agreement is approved by Council;
7. the Mayor and City Clerk are authorized to execute and deliver the Shareholder Declaration, or otherwise declare or certify its enforceability, with such alterations, amendments, deletions or additions thereto as the Mayor and City Clerk shall determine to be necessary or appropriate, such determination to be conclusively evidenced by the execution thereof by the Mayor and City Clerk, and such execution, declaration or certification shall be conclusive evidence that the Shareholder Declaration is approved by Council;
8. the Mayor and City Clerk are authorized to approve the final form of the MPA, the Shareholders Agreement and the Amalgamation Agreement and to do all things necessary or desirable in connection with the Merger and all matters ancillary thereto including the execution and delivery of all such instruments, certificates, agreements and other documents and to do and perform all such other acts and things as the Mayor and City Clerk shall determine to be necessary or advisable in connection with the Merger and all matters ancillary thereto and to otherwise give effect to these resolutions, and any such instruments, certificates, agreements and other documents as aforesaid shall be in such form as the Mayor and City Clerk shall determine to be necessary or appropriate, and any such determination to be conclusively evidenced by the execution and delivery thereof by the Mayor and City Clerk; and

9. the Mayor and City Clerk are authorized to execute and deliver, for and on behalf of the City, a resolution in writing of the City in its capacity as sole shareholder of GHI, substantially in the form of these resolutions for the purposes of section 6.2 of the Original Declaration.