CITY OF VAUGHAN

EXTRACT FROM SPECIAL COUNCIL MEETING MINUTES OF OCTOBER 7, 2015

Item 1, Report No. 33, of the Committee of the Whole (Working Session), which was adopted, as amended, by the Council of the City of Vaughan on October 7, 2015, as follows:

By approving the confidential recommendation contained in Confidential Communication C2, from the City Solicitor, the Director of Financial Planning, Analytics, Development Finance and Investments & Deputy City Treasurer, dated October 2, 2015; and

By receiving the following Communications:

C1 Director of Financial Planning, Analytics, Development Finance and Investments & Deputy City Treasurer, dated October 1, 2015; and

C3 Confidential Communication from the City Solicitor, the Chief Financial Officer & City Treasurer and the Director of Financial Planning and Development Finance & Deputy City treasurer, dated October 6, 2015.

1 POWERSTREAM MERGER AND ACQUISITION

The Committee of the Whole (Working Session) recommends:

1) That the recommendation contained in the following report of the Commissioner of Finance and City Treasurer and Interim Commissioner of Legal and Administrative Services and City Solicitor, dated September 22, 2015, be approved;

2) That the following be approved in accordance with Communication C1 from the Commissioner of Finance and City Treasurer and the Interim Commissioner of Legal and Administrative Services/City Solicitor, dated September 18, 2015:

1. **That the City of Vaughan approve the Vaughan Holdings Inc. Board's recommendation that PowerStream Holdings Inc. ("PowerStream") enter into a three way merger with Enersource Corporation ("Enersources") and Horizon Holdings Inc. ("Horizon") and then proceed to acquire Hydro One Brampton Networks Inc. ("Hydro One Brampton"), subject to the identical conditions set out by Vaughan Holdings Inc. as further described in this communication;**

2. **That the City of Vaughan agree to subscribe for equity common shares in Vaughan Holdings Inc. in the maximum amount of $45,600,000 to partially fund Vaughan Holdings Inc.'s portion of the acquisition of Hydro One Brampton;**

3. **That the City of Vaughan's investment in such common shares be made consistent with the timing and amounts deemed necessary by Vaughan Holdings Inc. in order to complete the merger and acquisition transaction;**

4. **That the City of Vaughan authorize Vaughan Holdings Inc. to pursue a sale from treasury of up to 10% of its shares related to its PowerStream interests to substantially recover the City's portion of the required equity investment and that a report on the process and recommendations be provided prior to completing the merger;**

5. **That the Mayor, together with the City Clerk, are hereby authorized to execute all documents and agreements on behalf of the City with respect to the proposed merger and acquisition, in a form satisfactory to the City Solicitor, and that City staff be authorized to take such steps as may be**

necessary (and substantially in accordance with the terms set out in this communication and its related report) to give effect to the proposed merger and acquisition;

6. **That staff report to Council if it appears that transaction negotiations could result in agreements which deviate substantially from the principles set out in this communication and its related report; and**

7. **That, within 60 days of executing the agreements and documents required to finalize the merger and acquisition, staff provide Council with an update; and**

3) That the following deputations and Communications be received:

1. **Mr. Brian Bentz, President and Chief Executive Officer, Powerstream, Cityview Boulevard, Vaughan, and Communication C2, dated September 22, 2015;**
2. **Mr. Todd Williams, Managing Director, Navigant Consulting Inc., Bay Street, Toronto, and Communication C3, entitled *"PowerStream Merger and Acquisition: Decision Support",* dated September 22, 2015; and**
3. **Mr. Paul H. Harricks, Legal Counsel, Gowlings LLP, King Street West, Toronto.**

Recommendation

The Commissioner of Finance and City Treasurer, and Interim Commissioner of Legal and Administrative Services and City Solicitor, in consultation with the Director of Development Finance and Investments recommend:

1. That the presentation by PowerStream Inc. on the merger and acquisition proposal be received;

2. That the presentation by Navigant Consulting Ltd. on the proposal's financials be received;

3. That the presentation by Gowlings LLP on the proposal's governance topics be received;

4. That such resolutions or recommendations as may be submitted by Vaughan Holdings Inc. be considered; and

5. That the City Clerk be requested to schedule a Special Meeting of Council between September 23, 2015 and October 9, 2015 to consider the recommendations of Committee of the Whole (Working Session) in this matter.

Contribution to Sustainability

Additional revenue opportunities provide support and financial sustainability to the City of Vaughan. Therefore investment opportunities must be considered and evaluated to determine if they present investment value and are aligned with the City's investment principles.

Economic Impact

Vaughan Holdings Inc. (VHI), which is wholly owned by the City of Vaughan, has been presented with a new investment opportunity for a three way merger between PowerStream Holdings Inc., Enersource Corporation and Horizon Holdings Inc. and subsequent acquisition of Hydro One Brampton. The proposed transaction would require an equity cash injection of approximately

$56M from VHI, subject to closing costs. There is a potential for increased dividend income for the City and synergy savings are expected to result in reduced upward pressure on future hydro rates to the average rate payer. As discussed in detail further in this report several funding options were considered for the estimated $56M cash injection, including a combination of using funds accumulated within VHI and available funds within the City's investment portfolio, or a conversion of the City's promissory note with PowerStream, or 10% sale of equity in PowerStream. A combination of using funds accumulated within VHI and the 10% equity sale is deemed the preferred funding option as it allows the City to benefit from the proposed transaction with minimal cash injection. However, available funds within the City's investment portfolio will be leveraged until a sale is finalized.

Several key economic impacts are discussed in further detail throughout the body of this report.

Communications Plan

On April 16, 2015, the Premier of Ontario made several announcements with respect to recommendations received from her Advisory Council of Government Assets including the initiation of negotiations with PowerStream, Enersource, and Horizon on a transaction that would see the three local distribution companies merge and also acquire 100 per cent of Hydro One Brampton Networks Inc. to create the second largest local distribution company in Ontario.

Negotiations have been ongoing over the last several months. Given the imminent shareholder decisions expected on the proposal, communications has been an important consideration, which is why the Communications teams from Vaughan, Markham, Barrie and PowerStream have had meetings and ongoing discussions to develop a collaborative approach to informing stakeholders about the proposal.

The first phase of the communication approach was the issuance of a news release by the City of Vaughan on August 24, 2015. It cited the status of the ongoing negotiations of the merger and acquisition, background on the proposal, benefits to the community, a quote from the Mayor and expected decision timelines. This release was posted on the City of Vaughan's website. PowerStream has also created a webpage with information on the proposal at www.PowerStream.ca/Merger.

The next phase in the approach was promoting this at the September 22, 2015 Committee of the Whole Working Session and informing members of the public that they are welcome to attend and make a deputation. This was done with advertisements in four local newspapers – Vaughan Citizen, Thornhill Liberal, Lo Specchio, and Corriere Canadese, posts on the City's corporate social media sites, and through promotions on Vaughan TV, the City's blog and an eBlast to subscribers of the City's eNewsletter. The City contacted local reporters directly to ensure they were aware of this meeting.

MergeCo is considering issuing a joint news release prior to the first Committee or Council meeting Working Group of any shareholder among the shareholder cities. If this release is issued, the City will promote it via Vaughan's website, social media accounts and eNewsletter.

If all the PowerStream shareholders approve the merger proposal, MergeCo will issue a joint news release after final shareholder approval has been completed. Subsequently, MergeCo may also place advertisements in several dailies. The City will support these activities and promote them via Vaughan's website, social media accounts and eNewsletter.

…/4

Purpose

The purpose of this report is to inform Council and the public on the proposed three way merger and subsequent acquisition of Hydro One Brampton.

PowerStream, Enersource and Horizon utilities are working to finalize details of their proposed merger and joint proposal to purchase Hydro One Brampton from the Government of Ontario. This proposal is the result of many months of effort and negotiation between the parties, and is currently at the critical phase of PowerStream's Board approval. Once endorsed by PowerStream's Board recommendations will flow to the shareholder's holding companies and subsequently to their respective municipal Councils for consideration.

Subject to PowerStream's Board meeting on September 11, 2015 and Vaughan Holdings Inc. (VHI) Board meeting on September 16, 2015, a written communication will follow this report outlining VHI Board's recommendation.

The attached Business Case and Navigant Consultant report provides full details of the proposed Merger and Acquisition.

The contents of this report are based substantially on the investment proposal negotiated to date and business case provided and highlights key areas for consideration. Given the size of the documents, for the reader's reference, the MergeCo Business Plan from PowerStream (Attachment 1), the MergeCo Business Case from PowerStream (Attachment 2) and the written consultant report from Navigant Consulting (Attachment 3) are available for viewing in hard copy at the Office of the City Clerk located on the 1st floor of Vaughan City Hall at 2141 Major Mackenzie Drive, Vaughan, ON L6A 1T1.

Given the complexity of the report, the contents are reported in the following format:

Executive Summary
A. Background on PowerStream
B. Local Distribution Company's (LDCs) mergers in the Provincial context
C. History of current merger and acquisition proposal
D. Shareholder due diligence
E. Context for evaluation of proposal
F. Benefits and Risks of proposal
G. Governance issues associated with proposal
H. Funding options for acquisition
I. Financial impacts to the City
J. Benefits to the rate payer from merger and acquisition

Background - Analysis and Options

Executive Summary

On April 16, 2015, four of Ontario's largest electricity distribution companies (LDCs) announced they would work together to form a new utility that would serve almost a million customers in York Region, Simcoe County, Peel Region, Hamilton and St. Catharines.

The proposed merger transaction comprises the following:

- A merger of the regulated and non-regulated business activities of: PowerStream, Enersource, and Horizon (individually, a 'Party' and collectively, the 'Parties').
- An acquisition by the Parties of the regulated electricity distribution business of Hydro One Brampton Networks Inc. (HOBNI) for gross proceeds of $607M, net of any purchase price adjustments

The combined entities described above are referred to as "MergeCo" and the corresponding transactions are referred to as the "Transaction". The creation of MergeCo must be approved by all shareholders and is subject to regulatory approvals.

The Transaction will create the second largest electricity distribution company in Ontario with almost 1 million customers, 2.7 billion in assets, and 2.5 billion rate base. In total, MergeCo is expected to deliver approximately **$427M of net cash savings (pre-tax) through synergies** in the first 10 years following the merger thereafter sustained at approximately $51M per year ($310M in operating synergies + $111M of capital synergies, net of transition costs).

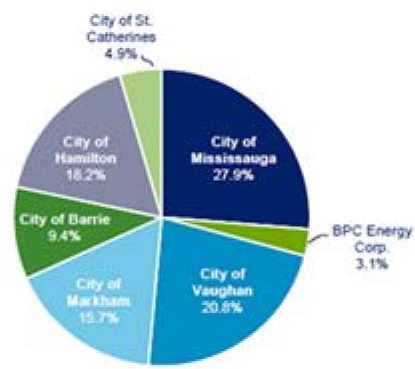
The City of Vaughan holds 45.31% of PowerStream via its holding company VHI. Under the merger, the City's ownership of MergeCo will be approximately 20.80% (second largest shareholder in the proposed MergeCo). Figure 1 below illustrates the pre and post ownership shares involved in the Transaction.

The City of Vaughan receives regular dividend and interest revenues from PowerStream, estimated to be approximately $16M in 2015. The equity investment required from the three PowerStream shareholders is expected to be $125M, while Vaughan's portion of this is approximately $56M.

Figure 1: Individual Shareholder Ownerships

Pre-Merger Shareholding	
Enersource	
City of Mississauga	90.0%
BPC Energy Corp. (Borealis)	10.0%
	100.0%
PowerStream	
City of Vaughan	45.3%
City of Markham	34.2%
City of Barrie	20.5%
	100.0%
Horizon Utilities	
City of Hamilton	78.9%
City of St. Catharines	21.1%
	100.0%

Potential Merge Co Shareholding Contribution



Key Aspects of the Merger

Following months of negotiation with merger partners, PowerStream, on behalf of its shareholders, has reached substantial agreement on a number of key aspects.

1. Relative Value: PowerStream Shareholders will own 46% of the new company, (Vaughan's portion will be 20.8%)

2. Solar "Carve Out": PowerStream's Solar business is expected to be kept as a separate operating subsidiary under MergeCo; the dividend stream from existing PowerStream solar investments will be maintained through special shares

3. Local Presence & Facilities: all of PowerStream's existing facilities will be maintained following the merger

4. Governance: Six of 13 board members are to be appointed by PowerStream Shareholders, (Vaughan will have 3 representatives)

5. Executive: significant Executive presence of current PowerStream staff

6. Liquidity Rights: improved rights to raise capital for growth, or to monetize existing investments

Managing the Risks of the Transaction

The key risks to the Transaction may be seen as follow:

- Synergies (cost savings) may not be achieved
- Integration challenges
- Unidentified expenses / liabilities
- Regulatory uncertainty affects business plan going forward
- Shared ownership and a greater investor focus

Many of the risks identified above are seen to be mitigated through PowerStream's history of achieving synergy and integration post-merger/acquisition. PowerStream has entered four transactions of a similar nature in the last ten years. Additionally, the consolidation of these smaller LDCs will produce a larger and presumably more prominent corporation that will have the ability to exert more influence on the industry and related policy. The new MergeCo will also see greater independence on the Board of Directors with more powers delegated to that Board to steer the corporation in its pursuit to create value for the shareholders and bring savings to the electricity consumer. PowerStream was more closely held by its shareholders whereas MergeCo will see many more shareholders providing a greater deal of autonomy to its Board to steer the organization to a larger corporation mentality. This risk is mitigated by the fact that current PowerStream shareholders are still represented by 6 of the 13 Board members, of which Vaughan has 3 representatives. Effectively, Vaughan will need to focus its attention towards being an investor rather than the operations of the corporation.

Key benefits of the Transaction

Improved Financial Returns to Shareholders
- Steady and growing dividend stream at a higher level than the current arrangement; Vaughan can expect dividends to increase in the first 10 year post transaction by $62M
- Payback of equity investment for Hydro One Brampton of approximately ten years; Vaughan's $56M equity investment expected to increase to a value of approximately $90M – $135M over 10 years

Reduced upward pressure on future hydro rates for customers compared to the current arrangement
- Overall, approximately 8% decrease in future distribution rates (e.g. mitigates future increases). Customers will benefit through the savings of $450M over 25 years or an average of $40 annually. This will help reduce upward pressure on future rates.

Stronger Platform for Growth in the Future
- Much larger utility with a bigger geographic footprint, more diversification, and greater capital resources and opportunities to finance expansion

Greater Influence on Government Policy
- Merged utility will be in a key position of leadership to influence government and regulatory energy policy for the benefit of customers and shareholders

…/7

Part A - Background on PowerStream

PowerStream is the second largest municipally owned LDC in Ontario, serving over 370,000 residential and commercial customers. PowerStream is regulated by the Ontario Energy Board (OEB).

The principal activity of PowerStream is the distribution of electricity within Alliston, Aurora, Barrie, Beeton, Bradford West Gwillimbury, Markham, Penetanguishene, Richmond Hill, Thornton, Tottenham and Vaughan, as well as Collingwood, Stayner, Creemore and Thornbury through its strategic partnership with Collus PowerStream.

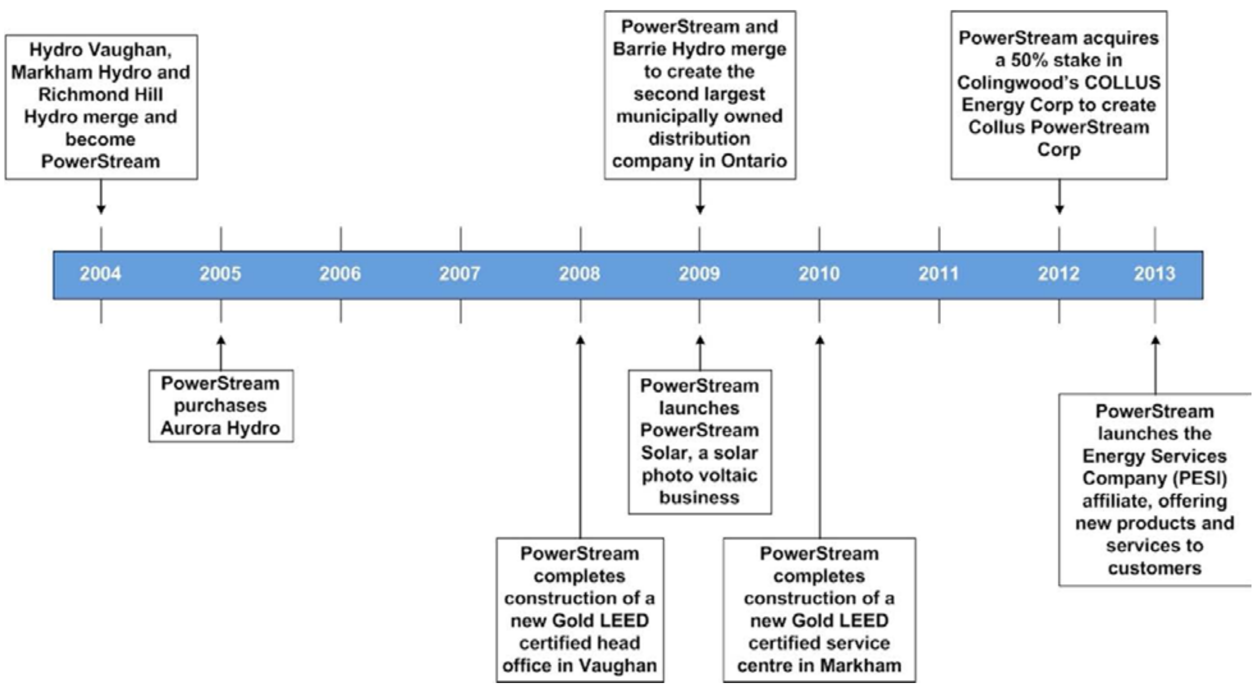
PowerStream encompasses an 854 sq. km service territory and delivers over 8,384 GWh of electricity to customers annually.

Growth is a key performance driver for PowerStream

PowerStream's strategy is to build on its core distribution business to become Ontario's premier integrated energy service provider. PowerStream's aim is to be a leading utility with respect to size, scale and scope, enabling the Corporation to realize the potential synergies and efficiencies that come with growth.

PowerStream has led the industry with successful mergers, improving service reliability, reducing upward pressure on rates, and has been an active member that supports its local communities. A few of PowerStream's recent business activities are illustrated below.

Figure 2: PowerStream 10 Year History



Part B - LDC mergers in the Provincial Context

LDCs in Ontario operate in a complex regulated environment highly responsive to shifts in Ontario government policy. The current distribution sector makeup is a product of a number of pieces of legislation and is summarized below.

Up until 1996 most municipalities in Ontario had their own Municipal Electricity Utility or MEU. These MEU's were governed similar to any other municipal department such as water or sewage and were not revenue generating. This changed in 1996 when the Macdonald Commission suggested significant changes to the structure of MEUs. Legislation enacted by the Ontario government in 1998 confirmed that municipal governments should continue to own electric utilities, but required that they be transformed into business corporations under the Ontario Business Corporations Act (OBCA).

The City's existing PowerStream assets (Principal Investment) were inherited

The incentive to structure sustainable corporations, or LDCs, in a deregulated market contributed to the initial wave of consolidation in the sector. This brought the number of MEUs in the province from 307 to around 89 by 2001. Since then, government policy surrounding a transfer tax holiday have led to a handful of LDC consolidations, (with PowerStream in a notable leadership position) and acquisitions by Hydro One which have brought the number of utilities currently operating in the province down to 66. There has also been some private equity participation in LDCs, although these have been by and large limited to 10% due to prohibitive tax treatment.

The Province of Ontario has endorsed LDC consolidation

The policy rationale for LDC consolidation (for the benefit of ratepayers and shareholders) has been well established and consistently advanced from multiple sources over the past few years. In 2012, the Ontario government created the multi-partisan Distribution Sector Review Panel to provide expert advice to the government on how to improve efficiencies in the electricity sector with the aim of reducing costs for customers and increasing efficiencies. The Panel strongly endorsed industry consolidation and noted the following:

Regarding Consolidation:

"...LDCs in Ontario should be consolidated into eight to twelve larger regional distributors...six to ten regional distributors would be located in southern Ontario and typically have a minimum of 400,000 customers..."

"...regional distributors must be contiguous and stand shoulder to shoulder."

Regarding New Investment:

"New investment in the distributor sector, notably from pension funds, should be encouraged. The report recommends that the Ontario Government enter into negotiations with the Federal Government on a tax agreement which would facilitate the removal of the transfer tax on the sale of LDC assets."

Regarding Governance:

"The membership of the boards of directors of regional distributors should have at least two thirds independent directors..."

Part C - History of Current Merger and Acquisition Proposal

LDC consolidations reduce upward pressure on hydro rates

In the spring of 2014, the Ontario government, seized with the issue of seeking efficiencies out of publicly-owned assets, began the review of government-owned assets. The review was specifically geared towards the optimization of government-owned assets including Hydro One and Ontario Power Generation (OPG). PowerStream was actively engaged in the review headed by former TD Bank Chair, Ed Clark. Although not originally tasked with the issue of LDC consolidation, the Clark panel quickly determined that the potential savings to ratepayers were too significant to not address. The panel released their final report in the spring of 2015.

The report stated the following with respect to Hydro One Brampton and utility consolidation:

1. The Province should proceed immediately with a sale or merger of its interest in Hydro One Brampton Networks Inc. to or with Enersource Corporation, PowerStream Holdings Inc. and Horizon Holdings Inc., intended to catalyze consolidation in the Greater Toronto and Hamilton Area and to strengthen competition in the electricity distribution sector by increasing the number of LDCs with the capacity to drive further consolidation.

2. The Province should amend the transfer tax rules and departure tax rules that apply when municipal electricity utilities leave the payment-in-lieu of taxes regime both on a time-limited basis and implement these changes as quickly as possible.

3. The mandate and powers of the Ontario Energy Board should be strengthened to ensure that changes in industry structure do not put upward pressure on rates.

Through the passing of the 2015 budget and ongoing efforts with the OEB, the government has effectively endorsed all of the Clark panel's recommendations with respect to electricity distribution. Refer to Attachment 4, Province of Ontario press release on April 16, 2015, for a description of the relationship of these recommendations to this Transaction.

At the May 1, 2015 PowerStream Board Strategic Planning Session options were discussed and it was resolved that the preferred option to be executed was a 3-Way Merger acquiring Hydro One Brampton.

The proposed merger transaction comprises the following:

- A merger of the regulated and non-regulated business activities of: PowerStream Inc., Enersource Corporation, and Horizon Holdings Inc. (individually, a 'Party' and collectively, the 'Parties').
- An acquisition by the Parties of the regulated electricity distribution business of Hydro One Brampton Networks Inc. (HOBNI) for gross proceeds of $607M net of any purchase price adjustments

Merger Synergy Savings benefits customers in the form of reduced upwards pressure on rates

As a result of the merger, MergeCo expects to generate the following material savings (values are pre-tax):

- Aggregate gross operations, maintenance and administration expenditure (OM&A) savings of $355M over the first 10 years, or 14% of total OM&A expenditures, thereafter continuing at a savings rate of approximately 15% annually, (i.e., not cumulative).
- Aggregate gross capital expenditure savings of $168M over the first 10 years, thereafter continuing at a sustained level of $8M annually.

MergeCo will incur transition costs of approximately $95M in the first three years with respect to systems and process integration and human resource costs.

…/10

In total, MergeCo will deliver approximately $427M of net cash savings (pre-tax) in the first 10 years following the merger thereafter sustained at approximately $51M per year.

Part D - Shareholders Due Diligence

To determine if the Transaction is in VHI's and in turn the City's best interest, due diligence has been undertaken on the valuation, level of investment and financing options. To ensure independent advice and recommendations are provided; the shareholders of PowerStream have jointly retained industry experts Navigant Consulting, Ltd. and BDR North America Inc. In addition, Gowlings LLP has been jointly retained for legal advice. PowerStream Inc. agreed to pay for the Consulting fees incurred. Furthermore, each utility company in the Transaction have secured their own independent advisor to perform due diligence work.

Navigant (NYSE: NCI)

Navigant is a specialized, global professional services firm dedicated to assisting clients in creating and protecting value in the face of critical business risks and opportunities. Navigant Consulting services include a wide range of financial management services, investigation services, litigation support services, and business management consulting services, as well as software programs for use in database management, analysis and benchmarking.

Through senior level engagement with clients, Navigant professionals deliver expert and advisory work through implementation and business process management services. The firm combines deep technical expertise in Disputes and Investigations, Economics, Financial Advisory and Management Consulting, with business pragmatism to address clients' needs in highly regulated industries, including Construction, Energy, Financial Services and Healthcare.

BDR North America Inc.

BDR is a Toronto-based consulting firm of seasoned professionals specializing in the energy sector in terms of mergers and acquisitions, business and strategic planning and regulatory.

BDR has for many years managed and advised regarding the process of merger, acquisition and divestment of both generation and "wires" facilities in the electricity industry and related affiliates. Key to these assignments is the development of appropriate valuations for the businesses in the context of the relative risks.

Gowlings LLP

Gowlings is a leading Canadian and international law firm, with over 700 legal professionals serving clients in 10 offices across Canada and around the world.

Process Approach and Roles for Merger and Acquisition Proceedings

The Transaction is the result of many months of effort and negotiation between the Parties.

Working Groups - *w*orking groups were established and comprised of representatives from each LDC's departments to determine synergies and transition costs

Deloitte - Deloitte was engaged to provide a third party valuation of PowerStream, Enersource, and Horizon*.* Deloitte produced a business case model to assess the merger and purchase transaction, considering net synergies, capital structure, financing, and regulatory impacts

The Valuation model and Business Case model were reviewed, stress tested, and negotiated over six months by each of the following parties:

Navigant Consulting, Ltd. - representing PowerStream Shareholders

Morrison Park Advisors Inc. – providing advisory services to PowerStream

PricewaterhouseCoopers LLP – representing Enersource Shareholders

Ernst & Young Global Limited – representing Horizon Shareholders

CFO & Supporting Management Teams – of each LDC

The Business Plan (Attachment 1) which described comprehensive details of the proposed transaction and the Business Case (Attachment 2) are both available for viewing at the Office of the City Clerk.

Part E - Evaluation of the proposed transaction

The City's Investment Policy is a good context for evaluating the opportunity

The City's Investment Policy lists three investment objectives in priority order:

1. Preservation of principal investment
2. Maintenance of adequate level of liquidity
3. Earning a competitive rate of return

Based on the order priority from the above list it can be seen that certain risk "trade-offs" may occur between the items. While preservation of principal is the number one priority, investment in a utility corporation does not come with the same guarantees that might accompany a bond transaction for instance. Furthermore, due to prohibitive tax consequence as discussed further below in this report, the ability to withdraw the investment based on cash needs is minimal at best pointing to a very low level of liquidity. In turn, these two items must be weighed against the opportunity for a rate of return that is not available under virtually any other investment opportunity that a municipality is able to enter within the City's existing portfolio and legislation. The City does, however, have legal authority to enter this proposed transaction as set out in the Ontario's Electricity Act, 1998 and Ontario's Municipal Act. Some of these elements are discussed further throughout this report.

Since the City's investment in PowerStream is different than a traditional municipal investment (i.e.T-bill, bonds, etc.), there are other factors that also need to be taken into consideration. These other factors may include governance/control, impact on customer hydro rates, and utility market trend and risks.

The written report by Navigant, the shareholders financial consultant, provides professional and independent analysis on the proposed transaction.

Staff and consultants have been in frequent discussions with PowerStream to assess the proposed transaction. The written Navigant report is based on these discussions and the business case provided to the shareholders by PowerStream. Information discussed in the report is based on a variety of topics, but most importantly the following key areas of consideration:

- Is the PowerStream's relative valuation in MergeCo reasonable?
- How much equity investment is required by the City of Vaughan?

- What are areas to maximize value in the transaction?
- What is the treatment for Solar shares?
- What are the benefits and risks to City of Vaughan?
- How does the City fund its share of the acquisition of Hydro One Brampton?
- What are the governance issues to consider?

Further details on these key areas are discussed below and in subsequent parts of the report, but a more fulsome discussion from the consultants may be found in their written analysis.

Is the PowerStream's relative valuation in MergeCo reasonable?

The proposed relative valuation of PowerStream Inc. under the merger is approximately 46% (excluding the Solar Class A shares) based on enterprise values using discounted cash flows of the three utilities. Reasons to exclude Solar Class A shares are discussed in more detail below.

The City owns 45.315% of PowerStream and based on the relative valuation, the City's ownership of MergeCo will be approximately 20.80%. The 20.80% represents the proportional market value of PowerStream in the combined market value of MergeCo.

Navigant Consulting Ltd., the shareholder's financial consultant, had review the valuation model and did an independent standalone valuation of the PowerStream relative valuation. Navigant's assessment is that the relative valuation of PowerStream is reasonable and fair.

How much equity investment is required by Vaughan?

The proposed acquisition of Hydro One Brampton is priced at $607M. The rate base valuation is approximately $404M. The equity injection required from the three PowerStream shareholders is expected to be $125M, while Vaughan's portion of this is approximately $56M, subject to closing costs. The closing costs are uncertain at this time, however it is expected that a contingency of up to 10% of the equity injection ($5.6M) will be requested in order to cover these expenses. Additionally, the transaction costs may also have an effect on the 2015/2016 dividend payouts by PowerStream. The acquisition price of Hydro One Brampton has been set at 1.5 times the rate base valuation of approximately $404M. The market valuation (premium) for utilities companies has increased due to the current low interest rate environment.

What are areas to maximize value in the transaction?

There are two areas that were substantially agreed to in the negotiation that maximize value in the transaction for Vaughan, which include: 1) Separation of PowerStream's Solar business Class A shares under MergeCo, and 2) Favourable Transfer tax treatment for the Brampton purchase.

1) Separation of PowerStream's Solar Business Class A Shares

   Based on Navigant's analysis, keeping the Class A shares of Solar business separate in the merger transaction is preferred. Solar would be kept as an operating subsidiary of MergeCo and existing PowerStream shareholders would retain ownership of economic interests of those assets. There are three advantages to this:

   - Undervalued - the Solar business is undervalued in the relative valuation. Separating it out through Special Class shares maximize value.
   - Certainty of cash flow the Solar business is based on fixed contracts and provides a predictable income stream. Table 1 below provides the Solar cash flow forecast provided by PowerStream under the MergeCo Transaction.
   - Liquidity – The Solar program provides a repayment of the initial investment providing greater financial flexibility and access to cash.

…/13

Table 1 – Solar Dividends 10 year forecast

Solar Dividends (10 Years Forecast) - All values in $'Mil	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	Total
Status Quo											
Dividend - Total	10.10	10.60	10.20	9.20	8.10	7.00	6.00	5.70	4.40	3.40	74.70
Dividend - Vaughan 45.31%	4.58	4.80	4.62	4.17	3.67	3.17	2.72	2.58	1.99	1.54	33.85
MergeCo											
Dividend - Total	10.10	10.30	9.90	8.70	7.20	6.40	5.40	5.20	4.10	3.20	70.50
Dividend - Vaughan 45.31%	4.58	4.67	4.49	3.94	3.26	2.90	2.45	2.36	1.86	1.45	31.94
Variance: Status Quo vs. MergeCo*	-	(0.14)	(0.14)	(0.23)	(0.41)	(0.27)	(0.27)	(0.23)	(0.14)	(0.09)	(1.90)

Source: PowerStream's forecast

* Variance of the Solar Dividend under MergeCo due to service management fees, financing costs, and dividend policy

While the dividends are tracking slightly less under the merger scenario it should be noted that this is mainly attributable to interest rate adjustments resulting from a planned debenture renewal and the management services cost recovery to MergeCo for the management of these assets. These are costs that were previously covered through PowerStream overhead and are therefore now affecting the dividends in a more direct manner. Combined with the increased dividends for MergeCo as a whole, this dividend schedule forecast is still deemed reasonable in the context of the overall transaction.

The terms and conditions of keeping the Solar business separate from MergeCo will be based on the draft Solar term sheet. The draft Solar term sheet outlines the nature of the agreement including management services, cost recovery, ownership principles, dividend policy and intercompany financing.

Although the final form will not be ready until transaction closing, addressing the terms above provide a good basis for assurance to the current PowerStream shareholders that the segregation of the Solar business continues returning an expected high level of value while being fully incorporated in to the merger and acquisition transaction. Additionally, it is important to note that PowerStream shareholders are still able to participate and benefit from any **new** solar asset projects under MergeCo.

2) Reducing future Tax obligation for the Brampton Purchase

The Transfer Tax on Hydro One Brampton is 33% of the sale price, which translates to approximately $200M. PowerStream negotiated with the Province for the removal of this tax. Through discussion with the Province has not removed this tax, they have agreed to provide a PILs tax credit of approximately $60M, which can be used to partially offset the future transfer taxes.

This will help with liquidity concerns, but the full departure and transfer tax would be applied to PowerStream or MergeCo sale transactions above 10%. To assist with future growth, limited partnerships are being proposed, which effectively permits growth capital investment without triggering tax liabilities. This will be determined through future tax rulings before closing the Brampton purchase.

…/14

To further illustrate the severity of the tax consequence, if PowerStream shareholders were to receive an equity value of $900M for their current holdings in PowerStream then approximately $350M in tax would be owing, which equates to approximately 40% of the value.

Part F - Risks and Benefits

What Are the Benefits and Risks to the City of Vaughan?

Figure 3 below illustrates the benefits and risks to the City of Vaughan of a potential merger.

Figure 3: Benefits and Risks of Merger

Benefits

- Potential net synergies of $427M
- Potential average rate of return of 6.3%
- Consistent with Provincial mandate for consolidation
- Future utility rate reductions of $40 per customer per year
- Potential for increased cash flow and equity growth over forecast
- Provide economies of scale for growth and innovation
- Platform to expand in to new lines of business
- Greater opportunity for alternative equity funding
- Retain the value of Solar business

Risks

- Payback period is long term if funded by cash
- Forecasted synergy, returns, and equity growth lower than expected
- Purchase price of Hydro One Brampton on the high end
- Burdensome tax treatment on ownership changes
- Disruptive technologies could impact value
- Regulatory changes could affect future value
- Less direct control in terms of governance
- Growth strategy will require undetermined additional future equity investment

Part G – Governance issues associated with proposal

Gowlings LLP will provide a memo to speak to many of the governance issues cited and this memo will be attached to a communication to Committee of the Whole (Working Session) subsequent to the VHI Board meeting, however below is a list of the issues for consideration.

- Board Composition
- Independent vs. Non-Independent Members
- Proposed Management Structure
- Special Approvals
- Dividend Policy
- Agreement Structure

Part H - Funding options

How does the City fund its share of the acquisition of Hydro One Brampton?

…/15

The proposed transaction would require an equity investment of approximately $56M, subject to closing costs, from Vaughan.

The three funding options identified in order of preference are:

- Sell 10% of existing PowerStream shares
- Use City cash reserves
- Convert promissory note in PowerStream

Selling 10% of PowerStream to fund transaction is the recommended funding option

The sale of 10% of PowerStream Inc. is expected to bring in approximately $40M to Vaughan specifically. This cash can be used to fund most of the equity investment required at approximately $56M, with the remainder coming from funds retained in VHI for investment opportunity.

Based on Navigant's analysis, the sale of 10% is preferred for the following reasons:

- Provide higher dividend cash flow with minimal equity investment
- Lock in the current market value
- Minimize risk on liquidity and preservation of capital with no tax consequence
- Hold City's cash reserve for future investment opportunities
- May attract a strategic private partner that could influence tax rule change and increase internal competition on future divesture
- Selling 10% effectively transfers a portion of the risk
- 10% sale aligns with Provincial mandate
- Allows the merger to move forward which will ultimately benefit utility users

On August 12, 2015, VHI Board approved the potential sale of 10% of existing PowerStream shares as a source of funding for the approximately $56M equity investment required from Vaughan. The acquisition will be initially funded by funds retained within VHI of $16M and the remaining $40M funded through the City's investment portfolio. It is anticipated that the City's portion will be recovered by the sale of the 10% shares of PowerStream.

Other funding options are available, but less financially advantageous

The use of available City cash in the City's investment portfolio without a subsequent sale of 10% of PowerStream for recovery is the second preferred funding option. There is approximately $16M funds retained in VHI. The additional cash required would need to come from the City's investment portfolio with no immediate recovery. Although, the City can financially manage the funding, these are earmarked for other purposes, albeit in the distant future. The use of cash investment is subject to risks, particularly liquidity constraint of the transaction. The City's cash on hand is the most liquid financial asset whether it's collecting interest in the bank or investment in low risk and high liquidity short term investments. This investment would not allow easy access to fund the City's future long-term capital program when required, hence the sale of 10% is preferred to reduce these risks. This merger transaction should be viewed as a long term income generator, with a long payback period and restricted liquidity.

Converting the promissory note to fund the transaction is the least preferred option. The City currently has an $86M promissory note with PowerStream. The promissory note has a rate of return of 5.58% on $78M and 4.03% on $8M and can be called at any time. Therefore the promissory note is a liquid asset that earns a very competitive rate in today's environment. The promissory note is not subject to other risks, namely liquidity and preservation of principal, which would exist if converted.

…/16

Part I - Financial impacts to the City

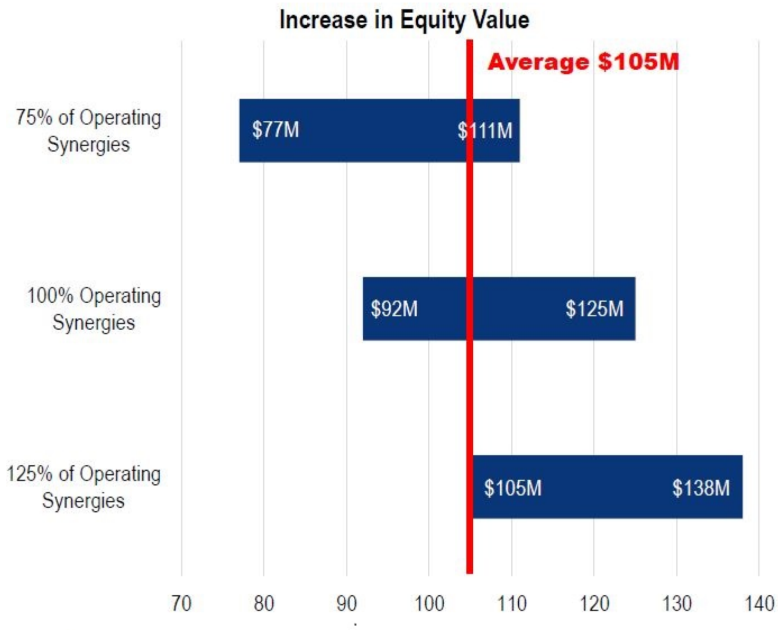
The proposed transaction is expected to increase equity value and provide a steady and growing dividend stream to shareholders

Subject to assumptions and risks described in this report and attachments, MergeCo is expected to deliver meaningful shareholder benefits both in terms of equity growth and dividend cash flow. The following assumes financing through a cash contribution and are summarized as follows:

To the benefit of City of Vaughan

- Vaughan's contribution to the acquisition of Hydro One Brampton is estimated at $56M. Vaughan's share of the $230M – $300M increase in shareholder value is approximately $90M-$135M.

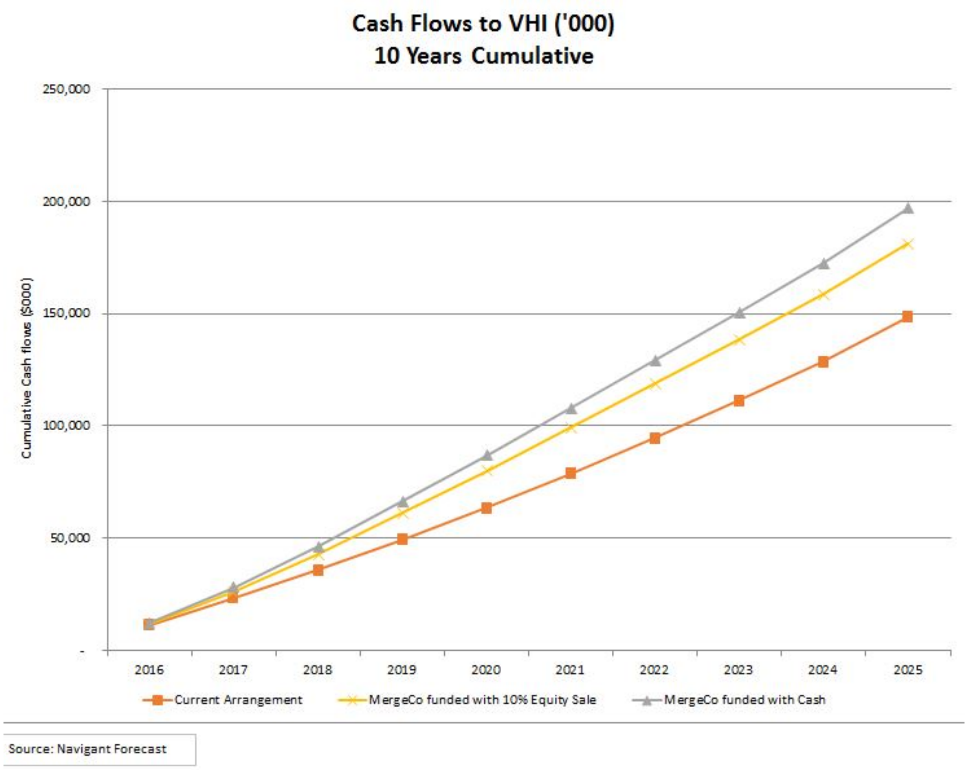
Figure 4 – Growth of equity value



Source: Navigant Project Aura Valuation and Business Case Model (August 28, 2015)
Notes:
1) Range of for each synergy scenario based on alternative terminal value calculations, e.g., perpetuity growth rate, final year cash flow, and exit multiple
2) Assumes 5% discount rate

- Vaughan can expect their dividend to increase in the first ten years post transaction by $62M.

Figure 5 – Cash flows to Vaughan



MergeCo

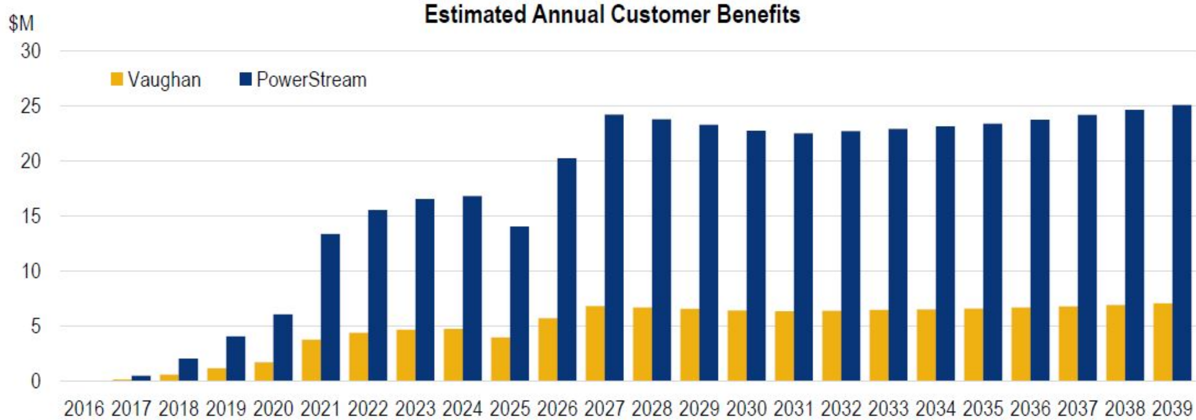
- Increase in the Net Present Value (NPV) of earnings of approximately $276M from $1,154M to $1,430M from 2016 to 2036 relative to the current arrangement, a 24% increase.
- Rates of return begin to normalize post 10 years, however projections beyond 10 years become less predictable given several uncertainties. Therefore, the focus is predominantly on the initial 10 year period.

Part J - Benefits to the rate payer

The proposed merger between PowerStream, Enersource and Horizon Utilities and the acquisition of Hydro One Brampton would bring significant value to customers. Analysis has found that customers will be able to save approximately $450 million over 25 years (an average of $40 per customer annually). Efficiencies realized as a result of the merger would reduce the upward pressure on distribution rates, allowing customers to benefit directly through lower bills than would be seen if the merger does not take place.

Figure 6 below illustrates the estimated annual customer benefits from the merger. It shows the overall savings to PowerStream customers and the Vaughan specific customer benefits. Included in these savings are also direct savings on City of Vaughan facilities, which equates to approximately $222K per annum. This results in an added benefit to City of Vaughan property tax payers in the form of reduced pressure on annual tax levy increases.

Figure 6 – Customer benefits



Source: Navigant Project Aura Valuation and Business Case Model (August 28, 2015)
Notes:
1) All values nominal
1) Customer benefits over the first 10 years are driven primarily by avoided capital expenditures
2) Customer benefits after the first 10 years are driven primarily by lower operating costs

In addition, there are numerous benefits of the merger that go beyond cost savings on customer bills. These include:

- Better ability to serve customers through enhanced and shared systems and range of products or services available.
- Increased resources to respond to reliability issues.
- Investment in new business opportunities improves economic development in the City.

Regional Implications

Residents of York and greater Toronto and Hamilton areas being served by MergeCo can expect reduced upward pressure on future hydro rates with the proposed transaction.

Conclusion

PowerStream, Enersource and Horizon utilities are working to finalize details of their proposed merger and joint proposal to purchase Hydro One Brampton from the Government of Ontario. This proposal is the result of many months of effort and negotiation between the parties, and is currently at the critical phase of PowerStream's Board approval. Once endorsed by PowerStream's Board, recommendations will flow to VHI and subsequently to City Council for consideration.

Subject to a PowerStream Board meeting on September 11, 2015 and a VHI Board meeting on September 16, 2015, a written communication will follow this report outlining VHI Board's recommendation.

The proposed transaction would require an equity cash injection of approximately $56M, subject to closing costs. There is a potential for increased dividend income for the City and synergy savings are also expected to reduce upward pressure on future hydro rates. The investment should be viewed as long term in nature. Additionally, the proposed transaction will result in more risk, slightly less liquidity, and a transformation in the governance structure compared to current arrangement, but is still seen as favourable given the potential economic benefits.

Attachments

1. MergeCo Business Plan from PowerStream Inc. (available at the Office of the City Clerk for viewing upon receipt)
2. MergeCo Business Case from PowerStream Inc. (available at the Office of the City Clerk for viewing upon receipt)
3. Navigant Consulting Ltd. written analysis of Business Case (available at the Office of the City Clerk for viewing upon receipt)
4. Province of Ontario April 16, 2015 Press release on proposed transaction

Report prepared by:

John Henry, Commissioner of Finance and City Treasurer
Heather Wilson, Interim Commissioner of Legal and Administrative Services/City Solicitor
Lloyd Noronha, Director of Development Finance and Investments
Alex Ly, Senior Analyst, Development Finance and Investments

(A copy of the attachments referred to in the foregoing have been forwarded to each Member of Council and a copy thereof is also on file in the office of the City Clerk.)

VAUGHAN

memorandum

C 1
Communication

CW (WORKING SESSION)
September 22, 2015

Item- 1

DATE: SEPTEMBER 18, 2015

TO: MAYOR AND MEMBERS OF COUNCIL

FROM: JOHN HENRY, COMMISSIONER OF FINANCE AND CITY TREASURER
HEATHER A. WILSON, INTERIM COMMISSIONER OF LEGAL AND ADMINISTRATIVE SERVICES/CITY SOLICITOR

RE: COMMUNICATION - COMMITTEE OF THE WHOLE (WORKING SESSION) - SEPTEMBER 22, 2015
ITEM 1 - POWERSTREAM MERGER AND ACQUISITION

Recommendations

1. That the City of Vaughan approve the Vaughan Holdings Inc. Board's recommendation that PowerStream Holdings Inc. ("PowerStream") enter into a three way merger with Enersource Corporation ("Enersources") and Horizon Holdings Inc. ("Horizon") and then proceed to acquire Hydro One Brampton Networks Inc. ("Hydro One Brampton"), subject to the identical conditions set out by Vaughan Holdings Inc. as further described in this communication;

2. That the City of Vaughan agree to subscribe for equity common shares in Vaughan Holdings Inc. in the maximum amount of $45,600,000 to partially fund Vaughan Holdings Inc.'s portion of the acquisition of Hydro One Brampton;

3. That the City of Vaughan's investment in such common shares be made consistent with the timing and amounts deemed necessary by Vaughan Holdings Inc. in order to complete the merger and acquisition transaction;

4. That the City of Vaughan authorize Vaughan Holdings Inc. to pursue a sale from treasury of up to 10% of its shares related to its PowerStream interests to substantially recover the City's portion of the required equity investment and that a report on the process and recommendations be provided prior to completing the merger;

5. That the Mayor, together with the City Clerk, are hereby authorized to execute all documents and agreements on behalf of the City with respect to the proposed merger and acquisition, in a form satisfactory to the City Solicitor, and that City staff be authorized to take such steps as may be necessary (and substantially in accordance with the terms set out in this communication and its related report) to give effect to the proposed merger and acquisition;

6. That staff report to Council if it appears that transaction negotiations could result in agreements which deviate substantially from the principles set out in this communication and its related report; and

7. That, within 60 days of executing the agreements and documents required to finalize the merger and acquisition, staff provide Council with an update.

Purpose

The purpose of this communication to provide the outcome of the Vaughan Holdings Inc. meeting held September 16, 2015.

This memorandum supplements the information contained in the September 22, 2015 Committee of the Whole (Working Session) meeting report ("the report") pertaining to the proposed PowerStream Merger and Acquisition.

The purpose of this memorandum is:

- to inform Council and the public of the September 16, 2015 Vaughan Holdings Inc. (VHI) Board recommendations and approved resolution to move forward with the proposed PowerStream Merger and Acquisition proposal;
- to request that Council adopt recommendations and conditions in support of VHI's endorsement of the PowerStream Merger and Acquisition plan;
- to provide an update on the upset limit amount of equity investment required; and
- to provide assurances from the City's external Legal Counsel with regard to the governance issues associated with the transaction (Attachment 1 – Memorandum from Gowlings LLP, dated September 17, 2015)

Background – Analysis and Options

On September 16, 2015, Vaughan Holdings Inc. (VHI) Board met to consider the proposed three way merger between PowerStream, Enersource, and Horizon and their subsequent acquisition of Hydro One Brampton. The proposed transaction was approved by the PowerStream Board on September 11, 2015. Details of the proposed transaction can be found in the report related to this communication. The result of the VHI Board meeting on September 16, 2015 was to approve the PowerStream Board's resolution to enter the three way merger and subsequent acquisition of Hydro One Brampton, subject to certain conditions as further detailed below.

Maximum Investment Threshold

Since the release of the September 22, 2015 Committee of the Whole (Working Session) report one notable change has been made to the amount required to fund the equity needed to acquire Hydro One Brampton. The report described "$56M, subject to closing costs" as the amount required for equity injection. Since the release of that report a contingency of up to 10% has been identified as reasonable to fund the closing costs and therefore the new total amount of funding required has been revised to $61.6M. Setting the maximum amount of the equity injection as $61.6M was one of the conditions set by the VHI Board. Table 1 below shows the new funding plan and is consistent with the recommended common share purchase of VHI found in the recommendations section of this report.

Table 1 – Funding Plan for Merger and Acquisition Proposal - VHI/City Portion Only ($M)

Purchase Price of Hydro One Brampton	$56.0
Add: Contingency for Closing Costs @ 10%	$5.6
Total Funding Required for Transaction	**$61.6**
From Available VHI Cash Balance	$16.0
Issuance of New Common Shares to the City	$45.6
Proposed Funding Available for Transaction	**$61.6**

It should be noted that consistent with the report and the recommendations set out in the communication, it is expected that a substantial portion (estimated at $40M) of the City's commitment to invest in VHI and VHI's corresponding commitment to invest in the merged company will be recovered through a 10% sale of VHI's common shares from treasury. As discussed in the report this is deemed to be the most financially advantageous option permitting the City of Vaughan to take advantage of very favourable market conditions, which help minimize the City's financial requirement, while benefiting from improved net 10 year cash flows and equity value. It also ensures that cash is available in the long term for the purposes of future City capital programs or alternative high yield investments.

Commitment to Cash Flow Expectations

As a result of the closing cost adjustment noted above, the cash flows associated with the transaction were revised. The second condition set out by the VHI Board details a minimum level of cash flow expectation, projections presented in Table 2, as the basis for which the transaction would proceed. Any substantial change to these projections would require a new approval by both the VHI Board and the City of Vaughan before the close of the transaction.

Table 2 – Forecasted Cumulative 10 years Cash Flow (VHI Specific)

Cashflow to VHI (10 Years Forecast) - All values in 000's	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	Total
Status Quo											
Equity Injection	(6,797)										(6,797)
Dividends - regulated	6,313	6,672	7,373	8,038	8,668	10,639	11,273	11,907	12,409	13,161	96,453
Interest on shareholder loans	4,718	4,718	4,718	4,718	4,718	4,718	4,718	4,718	4,718	3,505	45,967
Subtotal	4,234	11,390	12,091	12,756	13,386	15,357	15,991	16,625	17,127	16,666	135,623
Solar Dividends	4,576	4,803	4,622	4,169	3,670	3,172	2,719	2,583	1,994	1,541	33,847
TOTAL	8,810	16,193	16,712	16,925	17,056	18,529	18,710	19,207	19,120	18,206	169,469
Cumulative 10 Yr Cashflow excl equity injection											176,267
MergeCo - funded by cash (100% OPEX and 100% CAPEX synergies)											
Equity Injection	(56,000)										(56,000)
Closing adjustments (up to)	(5,600)										(5,600)
Dividends - regulated	8,483	11,707	14,005	16,065	16,560	16,730	17,103	17,010	18,331	19,877	155,872
Interest on shareholder loans	3,505	3,505	3,505	3,505	3,505	3,505	3,505	3,505	3,505	3,505	35,053
Subtotal	(49,612)	15,212	17,511	19,571	20,066	20,236	20,608	20,516	21,836	23,383	129,325
Solar Dividends	4,576	4,667	4,486	3,942	3,262	2,900	2,447	2,356	1,858	1,450	31,944
TOTAL	(45,036)	19,879	21,996	23,512	23,328	23,135	23,055	22,872	23,694	24,832	161,269
Cumulative 10 Yr Cashflow excl equity injection											222,869
MergeCo - funded by 10% sale											
Proceeds from sale	39,948										39,948
Equity injections	(50,979)										(50,979)
Closing adjustments (up to)	(5,600)										(5,600)
Dividends - regulated	7,634	10,536	12,605	14,459	14,904	15,057	15,393	15,309	16,498	17,890	140,285
Interest on shareholder loans	3,505	3,505	3,505	3,505	3,505	3,505	3,505	3,505	3,505	3,505	35,053
Subtotal	(5,491)	14,041	16,110	17,964	18,410	18,563	18,898	18,814	20,003	21,395	158,707
Solar Dividends	4,576	4,667	4,486	3,942	3,262	2,900	2,447	2,356	1,858	1,450	31,944
TOTAL	(915)	18,708	20,596	21,906	21,672	21,462	21,345	21,171	21,861	22,845	190,650
Cumulative 10 Yr Cashflow excl equity injection											207,281

Source: Navigant Model forecast for regulated dividends; PowerStream forecast for Solar dividends

Execution of Solar Management Term Sheet Key Principles

The third condition added by the VHI Board to minimize transaction uncertainty was to ensure that a management agreement for the Solar business be executed in a form substantially acceptable to the VHI Board (a draft "Solar Term Sheet" outlining key principles was created that is currently acceptable to the VHI Board). Further assurances regarding the Solar issues are provided through the Gowlings LLP memorandum as attached.

Finalization of the MergeCo Dividend Policy

The last condition was to protect VHI's and the City of Vaughan's interest in the Dividend Policy currently being finalized. The VHI Board approved an amended resolution to ensure that a finalized Dividend Policy be in a form acceptable to City of Vaughan before it approves the recommendations of this communication and the report at a City Council meeting on a date yet to be determined. The Dividend Policy is substantially complete with a few clauses under final revision. Given that the City relies on dividend cash flow to support operations it is prudent to ensure the Dividend Policy is satisfactory to the City before formally endorsing the merger and acquisition proposal. The impetus towards this is intended to provide more cash flow certainty to VHI and in turn the City and to decrease the discretionary powers of the new MergeCo Board of Directors with regard to the Dividend Policy to ensure these cash flows are further protected. This Dividend Policy excludes the Solar dividends, which have its own dividend policy.

Assurances and Governance

Gowlings LLP has reviewed several governance issues on behalf of the City of Vaughan to provide assurances from a legal perspective on these matters. As part of Attachment 1 some of the issues considered include; Corporate Structure, Board of Directors, Special Approvals, Post-Closing Adjustments and Dividend Policy, Liquidity Conditions, Financing MergeCo, Future Reorganization and the PowerStream Solar Business.

Conclusion

On September 16, 2015, the Board of VHI approved the PowerStream Board's resolution to enter the three way merger and acquisition of Hydro One Brampton.

As wholly owned by the City of Vaughan, VHI's decision to adopt and approve the resolution and recommendation as detailed above are submitted to the September 22, 2015 Committee of the Whole (Working Session) meeting for further consideration by Council.

Attachments

1. Memorandum from Gowlings LLP, dated September 17, 2015

Respectfully Submitted,

John Henry
Commissioner of Finance and City Treasurer

Heather A. Wilson for
Interim Commissioner of Legal and Administrative Services/City Solicitor

Copy to: Steve Kanellakos, City Manager
Lloyd Noronha, Director of Development Finance and Investments

gowlings montréal · ottawa · toronto · hamilton · waterloo region · calgary · vancouver · beijing · moscow · london

Paul H. Harricks
Direct 416-369-7296
paul.harricks@gowlings.com

Memorandum

To: Mayor and Members of Council for the City of Vaughan
Date: September 18, 2015
Re: Project Aura Interim Report
File Number: T1003698

A. Introduction

I have been retained by the shareholders of PowerStream Holdings Inc. ("**PHI**") to provide independent legal advice to them and their municipal shareholders on:

1. The legal risks and considerations related to the merger (the "**Merger**") of PHI, Enersource Holdings Inc. ("**Enersource**") and Horizon Holdings Inc. ("**Horizon**");
2. The corporate structure and governance arrangements of the new corporation resulting from the Merger ("**MergeCo**"); and
3. The legal risks and considerations related to MergeCo's purchase of Hydro One Brampton Networks Inc. ("**HOBNI**").

The Merger and the acquisition by MergeCo of HOBNI are referred to in the report as the "**Transactions**".

As part of my engagement I have met on several occasions with the boards of directors of each PHI shareholder, including Vaughan Holdings Inc. ("**VHI**"), and have been involved in providing instructions to PHI and its legal advisors on issues that were of concern to the PHI shareholders.

B. Scope of Review

In the course of my engagement I have reviewed successive drafts of each of the following (collectively, the "**Documents**"):

1. the Merger Participation Agreement ("**MPA**") pursuant to which the Merger will be completed;
2. the Unanimous Shareholders Agreement ("**MergeCo Shareholders Agreement**") which, as of the effective date of the Merger, will govern the relationship between the shareholders of MergeCo and its subsidiaries;

3. the Share Purchase Agreement pursuant to which MergeCo will acquire all of the issued and outstanding shares of HOBNI;

4. the proposed dividend policy for MergeCo (the "**Dividend Policy**"); and

5. the term sheet (the "**Solar Term Sheet**") for the operation and management by MergeCo and its subsidiaries of the current solar power business of PHI which, pursuant to the MergeCo Shareholders Agreement, will be owned by a subsidiary of MergeCo but operated for the exclusive benefit of the PHI shareholders.

Each of the Documents is, as of the date of this report, still under negotiation between the relevant parties although, as I have been advised by PHI and its advisors, almost all of the major commercial issues have been settled as between PHI, Enersource and Horizon.. Consequently, I will be preparing and providing to the PHI shareholders a subsequent report once all of the Documents have been settled to the satisfaction of the negotiating parties.

C. Summary of Conclusions

Consistent with the mandate that I was given by the PHI shareholders, and based upon my review of the current versions of the Documents that have been provided to me, my conclusions are as follows:

1. All of the Documents are in a form that are typical for transactions such as the Transactions.

2. The legal risks to VHI and the City of Vaughan associated with the Transactions are within the range of what is typical in similar transactions.

3. The Documents are drafted in a way that, from a legal perspective, adequately protects the interests of VHI and the City of Vaughan.

4. While the Dividend Policy is still under discussion, if it is adopted by all the parties in substantially the form being proposed, and while the payment of dividends can never be guaranteed, it will provide considerable assurance that the Shareholders of MergeCo will receive the level of cash flows (as a percentage of net income) that they are expecting. In this regard, we understand that the resolution approving the Transaction passed by the Board of Directors of VHI includes a condition that the Dividend Policy will be in a form acceptable to the City of Vaughan Council.

5. Similarly, if the Solar Term Sheet is finalized in the form currently being proposed, it will provide the PHI shareholders, including VHI, with satisfactory legal protections. In this regard we similarly understand that the VHI board resolution approving the Transactions includes a condition to the effect that the definitive management agreement will be executed and substantially a form contemplated by the Solar Term Sheet.

C2
CW (Working Session) - September 22, 2015
Item 1

Vaughan Committee of the Whole (working session)

PowerStream Update

September 22, 2015

Agenda

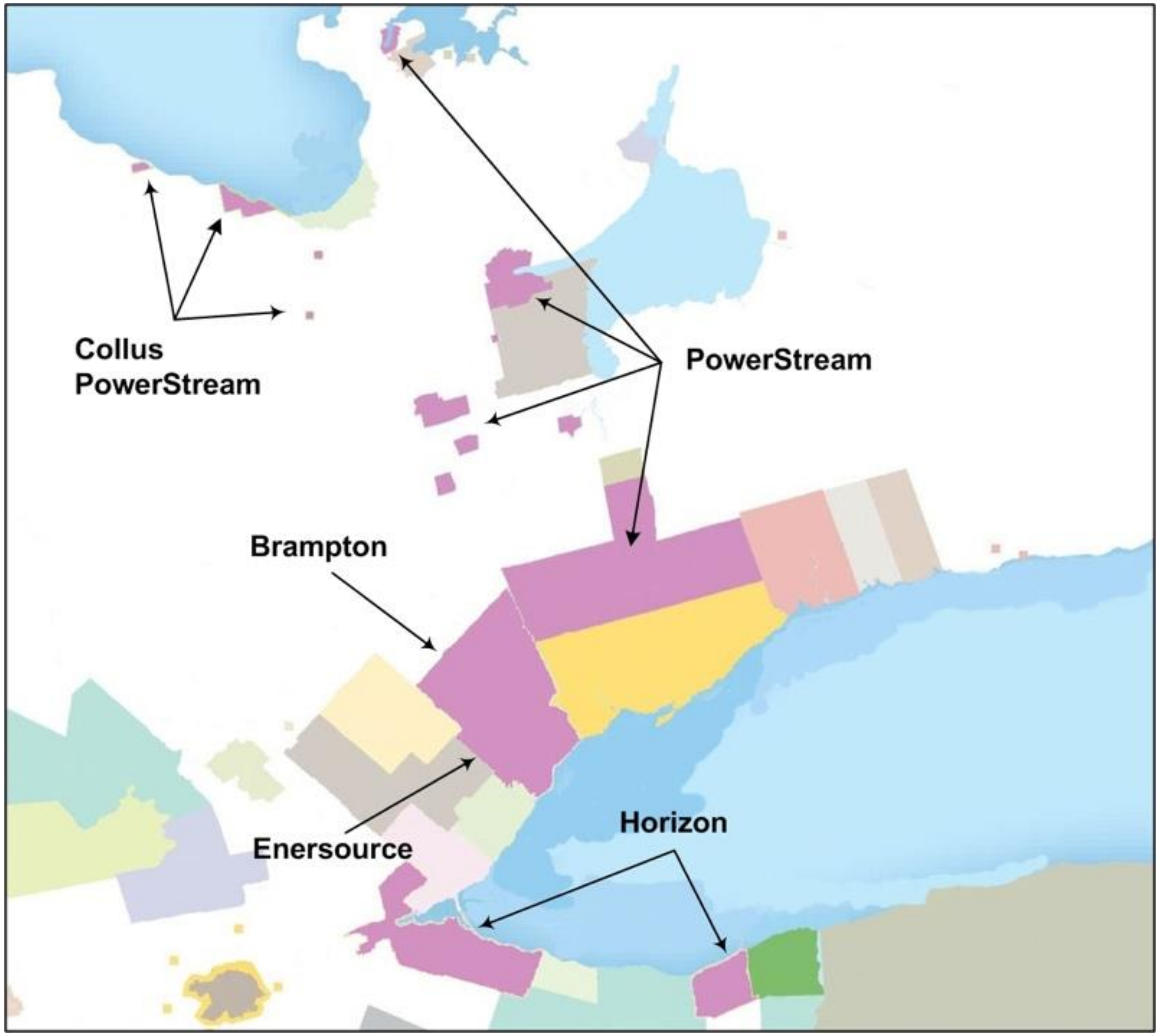
- ✓ Value Proposition
- ✓ Key Aspects of Transaction
    - Corporate Structure
- ✓ Business case
    - Synergies
    - Value to Shareholders & Customers
    - Relative Value
    - Acquisition Financing
- ✓ Key Legal Documents
- ✓ Conclusion

Second Largest Electricity Distribution Company in Ontario

- 1 million customers

- $2.7 billion in assets

- $2.5 billion rate base



Value Proposition

Improved Financial Returns to Shareholders

- *Steady and growing dividend stream at a level higher than the Status Quo*
- *$125M investment has nominal payback of 11 years*
- *$125M investment will increase in value to $230 - $300 million, due to synergy savings and Brampton dividends*

Cost Savings for Customers Compared to Status Quo

- *Rates will be lower than expected in the Status Quo*
- *Customers will save an average of approximately $40-$50/year over 25 years*

Stronger Platform for Growth in the Future

- *Much larger utility with a bigger geographic footprint, more diversification, and greater capital resources and opportunities to finance expansion*

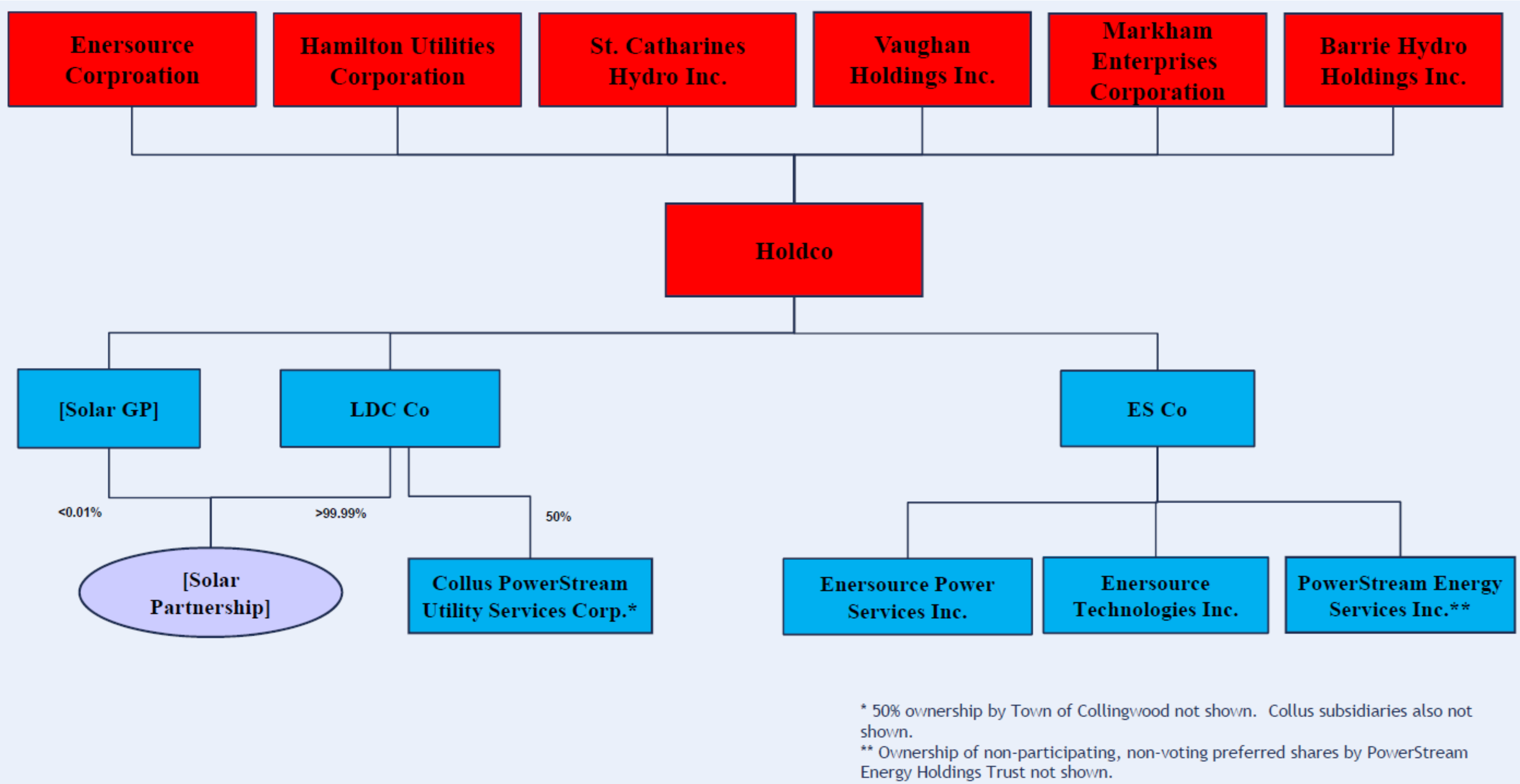
Greater Influence on Government Policy

- *MergeCo will be in a key position of leadership to influence government and regulatory energy policy for the benefit of customers and shareholders*

Key Aspects of Transaction

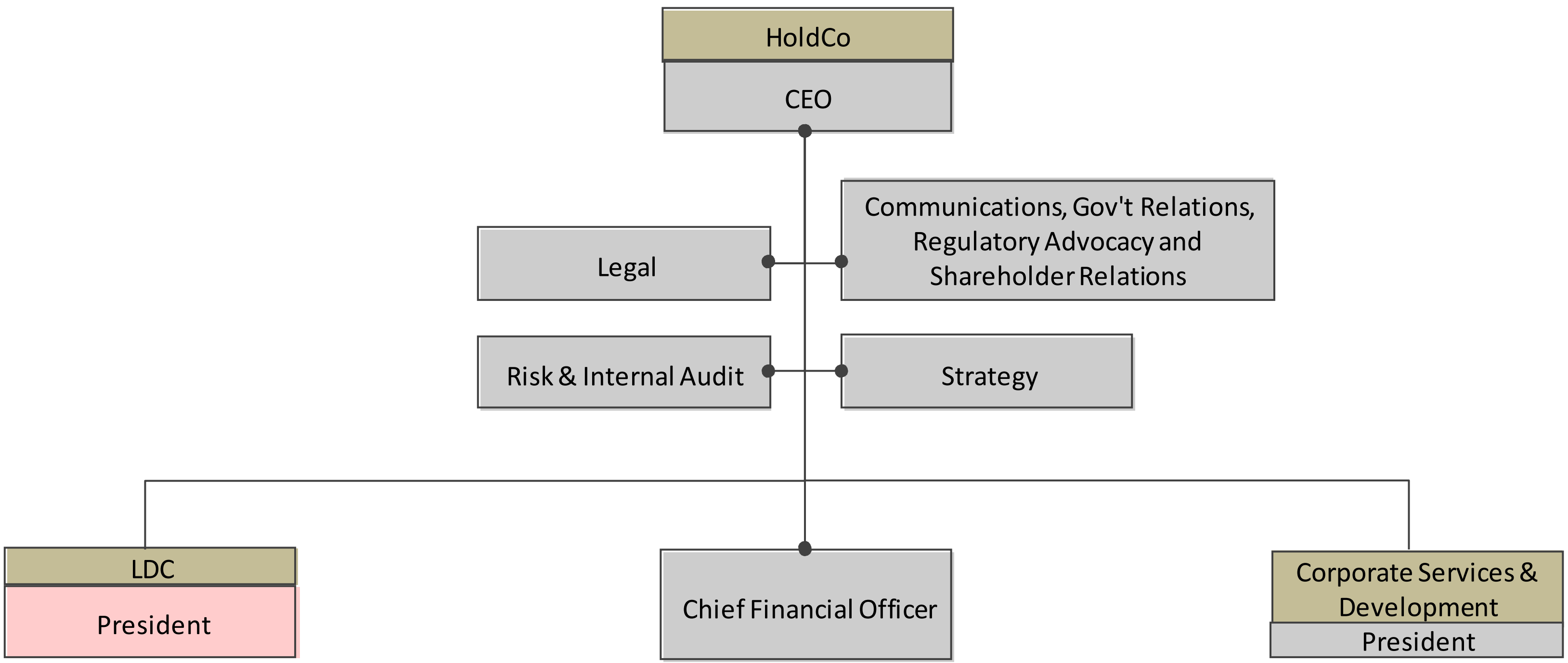
Issue	Result
Relative Value	PowerStream @ 46%
Local Presence & Facilities	Maintain existing facilities
Solar Carve Out	Maintain solar cash flows through special shares
Governance	6 of 13 Board Members to be appointed by PS shareholders
Executive	Significant presence in Executive for current PS Staff
Liquidity Rights	Improved rights to raise capital for growth, or to monetize existing investment

MergeCo Structure will Enable Execution of Strategy



- *Municipal Holding Companies are 100% owned by Municipalities, with the exception of Enersource Corporation (90% City of Mississauga, 10% Borealis)*
- *PowerStream Solar will reside in a segregated component of the LDC entity or a downstream partnership to preserve a full separation from the regulated LDC interests of MergeCo.*

MergeCo Organizational Structure



Business Case

Estimated Synergy Savings

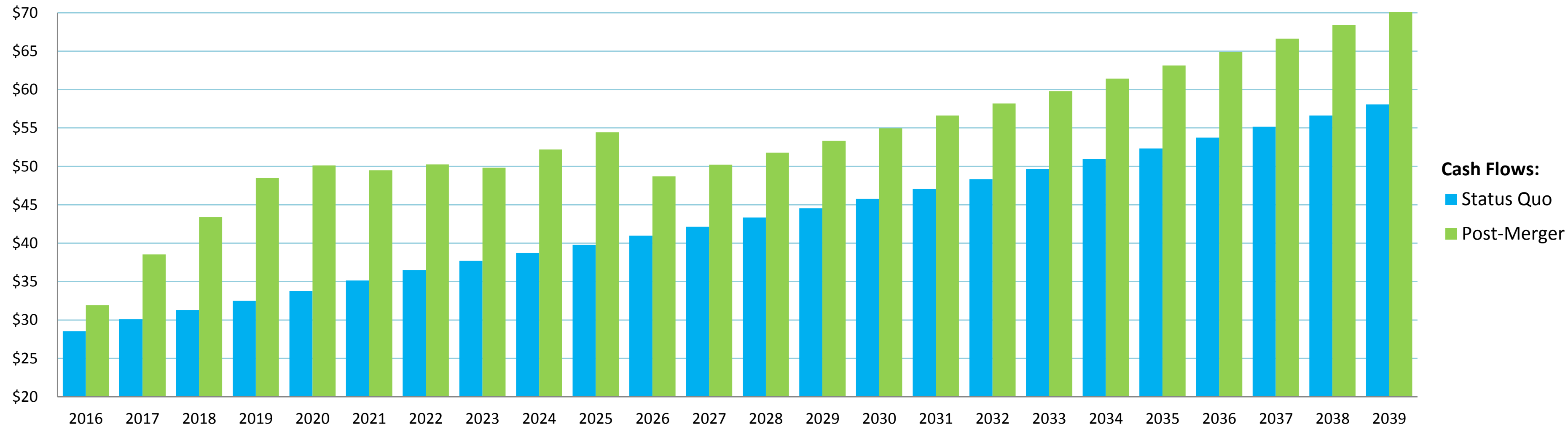
	2016 – 2020
Estimated OM&A Synergy Savings	$167 Million (approx)
Estimated Capital Savings	$ 127 Million (approx)
Estimated Transition Costs (Includes Severance)	$ 96 Million (approx)
(Approx 45% OM&A; 55% Capital)	

- Synergies of approximately $47.5M/year after 2020

- **Pace/timing of achieving synergy savings is very important**
  - balancing financial need with HR/LR and broader cultural impact along with operational requirements.

Value to Shareholders

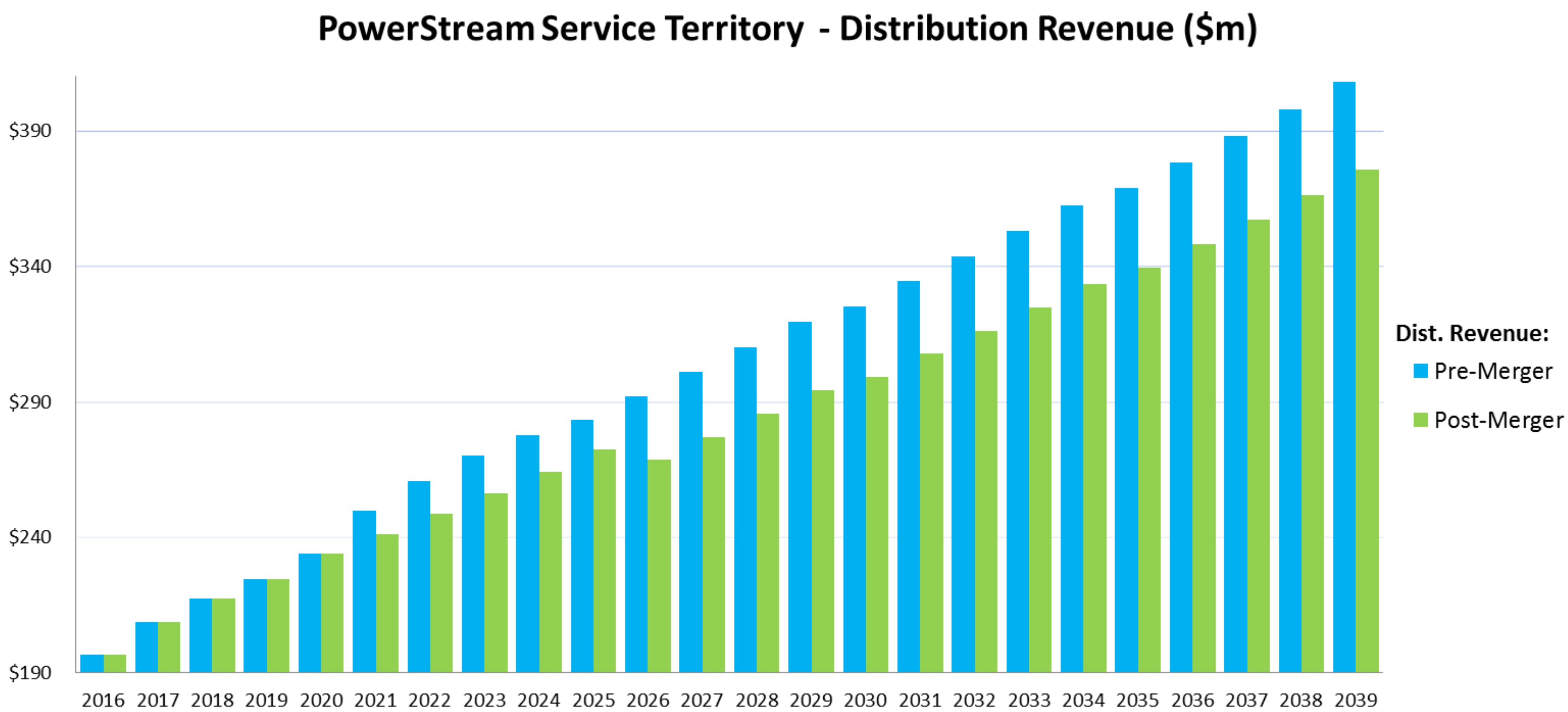
Core Business Cash Flows ($m)



*Updated to assume Promissory Notes and Deferred Interest are at 4.77% (long-term OEB rate); stand alone cash flows are amended to reflect impact of 2021-2025 rebasing that would occur if merger does not happen

Average Annual Increase in Cash Flows	**1 - 5 Years**	**6 - 10 Years**	**11 - 15 Years**	**16 - 20 Years**	**21 - 24 Years**	**Total Increase of Cash Flows**
	$11.2	$13.7	$8.4	$10.2	$11.6	$264.1

Value to Customers



- *Customers will share in merger efficiencies and will save approximately $450M over 25 years, or approximately $40-$50/customer annually*

- *Better ability to serve customers through enhanced and shared systems and range of products/services available ,with increased resources to respond to reliability issues*

- *Investment in new business opportunities improves economic development in our communities*

Value to Customers (cont.)

Typical Monthly Bill

	PowerStream	Enersource	Horizon	Hydro One Brampton
Residential	$ 131.47	$ 133.97	$ 138.15	$ 133.05
GS<50	$ 318.47	$ 335.93	$ 329.27	$ 325.12
GS>50	$ 12,971.56	$ 13,480.01	$ 13,227.02	$ 12,996.53

- PowerStream is currently undergoing a custom IR rate submission and new rates will be set for 2016:

	Proposed 2016 Rates PowerStream
Residential	$ 143.82
GS<50	$ 363.46
GS>50	$ 13,141.40

Distribution Revenue with Merger Transaction

- From 2026 onward, annual Distribution Revenue is approximately 8% lower as compared to PowerStream status quo

Community Impact

York Region Municipalities of Vaughan and Markham, as well as the City of Barrie are expected to see significant benefits on electricity bills for municipal buildings

Annual Total Bill Savings ***($ thousands)***

Municipality	Stand Alone Utility	Merged Utility	Cost Difference
Barrie Municipal Buildings	$ 17,829	$ 17,521	-$ 308
Markham Municipal Buildings	$ 11,497	$ 11,296	-$ 202
Vaughan Municipal Buildings	$ 12,498	$ 12,275	-$ 223

Large accounts in York Region and Simcoe County, as well as in Markham, would see savings on their total bills. For example, annual total bill savings after 10 years would be over:

- $10,000 for Markham Campus of Seneca College
- $11,000 for Markham-Stouffville Hospital
- $43,000 for Royal Victoria Hospital
- $9,000 for Vaughan City Hall

- The same savings can be seen at a number of other large facilities in PowerStream’s current service territory.

Valuation & Business Case Summary

Valuation model and Business Case model was reviewed, stress tested, and negotiated over 6 months by consultants representing each Shareholder's interests:

VALUATION

(including unregulated and PowerStream Solar)

Valuation	**Enterprise Value**
PowerStream	49.1%
Enersource	29.2%
Horizon Utilities	21.7%

BUSINESS CASE

(excluding PowerStream Solar)

Business Case	**Enterprise Value**
PowerStream	46.0%
Enersource	31.0%
Horizon Utilities	23.0%

Closing Adjustments:

- Closing adjustments for each LDC determined prior to merge and leveraged accordingly by MergeCo
- Purchase price is subject to certain limited price adjustments i.e. for working capital and fixed assets

PowerStream Solar

PowerStream Shareholders continue to benefit from the economics of the underlying solar assets

- PowerStream Solar will remain in LDC company
- Ring-fenced, similar to current structure, to comply with OEB requirements
- PowerStream Shareholders receive 100% of the dividends of the Solar business
- Revised dividend policy for PowerStream Solar is being developed and will provide a dividend stream similar to the one currently forecasted
- PowerStream Shareholders will indemnify the other Shareholders for risks associated with Solar business

PowerStream Solar - forecasted dividends

Factors not related to the merger transaction

- The refinancing of IO Ontario debt; IO financing can only be used if PowerStream is 100% municipally owned ; given that it is expected that PowerStream would obtain Private Equity financing even on a stand alone basis, it is not possible to use IO financing anymore. For 2016-2025 the total impact of increased interest cost and refinancing cost is approx. $1.7M
- Updating the SLA to include markup; for 2016-2025 the total impact is about $0.1M
- **Overall impact on dividends: reduction of $1.8M (2.3%)**

Factors related to the merger transaction

- The increased spread on long-term debt ; at 50 bps for 2016-2025 the total impact of increased interest cost and refinancing cost is approx. $2.9M
- Updating the SLA to 10% markup; for 2016-2025 the total impact is less than $0.1M
- Changing the dividend policy to 80% of net Free Cash Flow - for 2016-2025 the total impact is about $1.2M . This effect is due to the timing only; at the end of 20 year period it will be reversed.
- **Overall impact on dividends: reduction of $4.2M (5.5%)**

HOBNI Acquisition Financing

Purchase price - $607M

- Option to finance the purchase HOBNI with 70% - 75% debt
- Shareholder equity requirements to purchase HOBNI will be subject to closing adjustments
- Debt/equity adjustments, working capital adjustments and other assets adjustments to be based on pre-merger financial statements
- Bridge financing of up to $625M to purchase HOBNI, and $500M revolving credit will be available for MergeCo

($ millions)	**City of Vaughan**	**City of Markham**	**City of Barrie**	**PowerStream Total**
	45.315%	*34.185%*	*20.50%*	
Ownership in MergeCo (Excl. Solar)	20.8%	15.7%	9.4%	46.0%
Equity Required (Excl. Solar)	$56.5	$42.6	$25.6	$124.7

Sources of equity contribution:

- Debt conversion pre-merger
- Municipal support
- Private Equity funding

Key Legal Documents

Key Legal Documents

The terms and conditions for the proposed transaction are accomplished primarily through three key agreements:

- *Share Purchase Agreement* (SPA) for the purchase of Brampton;
- *Merger Participation Agreement* (MPA) to give effect to the 3-way merger;
- *Shareholders Agreement* (SA) to govern the rights of the shareholders in the future

All key aspects of the legal documents have been negotiated and the agreements are now substantially final and complete;

Details are summarized as follows:

Share Purchase Agreement ("SPA")

Share Purchase Agreement

- Purchase price – the purchase price is $607M.

- Adjustments – the Purchase price is subject to certain limited price adjustments i.e. for working capital and fixed assets.

- Closing conditions – the Agreement will provide for limited closing conditions, including closing of the Merger, Competition Act approval, and OEB approval. The purchase is not subject to a financing condition. All requisite Shareholder and Municipal approvals will have been obtained prior to signing the Agreement(s).

Share Purchase Agreement Cont'd

- Closing date – the target closing date is March 31, 2016.

- Anti-Flip – the Province has insisted on the inclusion of anti-flip provisions that would (a) prohibit the purchasers from selling all, or substantially all the shares or assets of Brampton without the consent of the Province for a period of 5 years, and (b) prohibit the sale of more than 49% of the equity of the entire merged entity (MergeCo) for a period of 3 years (except as between the current owners).

- Indemnification – the Agreement will provide for indemnification by the Province, on certain matters, i.e. environmental, and include thresholds and cap on claims.

Merger Participation Agreement ("MPA")

Merger Participation Agreement

- Parties – the Parties to the Merger Participation Agreement (MPA) and the Shareholder Agreement (SHA) will be all of the municipal holding companies, their respective municipalities, the three merging utilities (PowerStream, Enersource and Horizon) as well as BPC Energy Corporation (Borealis/OMERS).

- Shareholders – the shares of MergeCo would be held directly by each of the municipal holding companies. There will be one or two indirect shareholdings; in the case of Enersource 10% of their interest owned by Borealis or in the case of the PowerStream's or Horizon's shareholders a sale of 10% would result in 10% indirect ownership by a major pension fund such as Borealis or Teachers'.

Merger Participation Agreement Cont'd

- Amalgamation – PowerStream, Enersource, and Horizon would amalgamate with each other and continue as a new corporation ("MergeCo").

- Closing Date – the Merger would close up to 30 days prior to the closing of the purchase of the shares of Brampton.

- Representations & Warranties – the Agreement provides for customary Representations and Warranties between the Parties, with respect to; financial matters, material contracts, corporate status, condition of assets, full disclosure, environmental, and tax matters.

- Indemnification – each of the Parties agree to indemnify one another for claims, with thresholds and caps.

- The SPA and SHA will provide for the payment of the Share purchase of Brampton. Debt financing for this purchase has been arranged.

Shareholders Agreement

Overview

- The SHA between the Parties will come into effect upon Closing of the Merger.

- The draft SHA is similar to PowerStream's existing SHA in terms of structure, and incorporates the matters agreed to in the 3-way/purchase LOI.

- The Agreement will define the "Business", governance, composition of the Board of Directors.

- Composition of the Board of Directors: Total of 13 directors; 6 of 13 PowerStream appointments; Vaughan 3, Markham 2, and Barrie 1. As part of their respective allotment of board seats, each municipality may appoint 1 non-independent board member.

- The Agreement will set out the Guiding Principles, which will also help inform the initial Strategic Plan.

Shareholders Agreement Cont'd

Overview

- The Agreement sets out the unanimous approval matters and matters that require 66 2/3rds (Supermajority) approval. There is a much shorter list of the Unanimous and Supermajority matters than in PowerStream's current SHA, resulting in a greater delegation to the Board.

- The Agreement deals with the transfer of Shares and Liquidity Rights. The Agreement will provide, with 66 2/3rds approval, the ability to bring in third party capital in order to fund growth, and also with 66 2/3rds approval, the ability to monetize in whole or in part, with a mechanism to deal with the allocation of taxes.

Risk Management

Risk	Response
Synergies may not be achieved	PowerStream has a track record of meeting or exceeding its targets
Integration challenges	This is our fourth transaction in 10 years: experience counts
Unidentified expenses/liabilities	Extensive due diligence already, and specific contractual protection
Transaction financing in a rising interest rate environment	Bridge financing for two years is secured; flexibility to arrange capital details after closing
Regulatory uncertainty affects business plan going forward	A larger, more prominent utility will carry more weight in the industry and have a greater role in policy

Next Steps

PowerStream

PowerStream Board – September 11th

BHHI – September 14th**, City of Barrie** September 21st or 28th**,** Oct 5th TBC

VHI – September 16th**, City of Vaughan** September 22nd**,** Final Approval TBD

MEC – September 16th**, City of Markham** September TBD

Horizon

City of St. Catharines – TBD

City of Hamilton – September 2nd and 23rd

Enersource

Board – September 3rd

City of Mississauga– September 16th

Borealis – by September 16th

Conclusion

By pursuing the merger transaction, we will be stakeholders of the most dynamic utility in Canada

- ✓ *The 2nd largest LDC in Canada, serving 1 million customers*
- ✓ *Reduced upward pressure on distribution rates for our customers*
- ✓ *Scale and opportunity to innovate and grow*
- ✓ *Strategically positioned to take advantage of opportunities in a changing industry landscape*
- ✓ *Increased Shareholder value and cash flows*

C3
CW (Working Session) - September 22/15
Item #1

PowerStream Merger and Acquisition: Decision Support

Prepared for the City of Vaughan

September 22, 2015

Proposed Transaction

- The transaction has two major components
  - Three-way merger between PowerStream, Enersource, and Horizon
  - Joint acquisition of Hydro One Brampton
- Would create the second largest regulated electricity distribution utility in Ontario by the number customers, nearly one million, and the third largest by regulated asset value

Navigant was retained to provide decision support to PowerStream's shareholders

Navigant's analysis addresses five critical questions

1. Value and risks: What is the value of the transaction to PowerStream shareholders and what are the associated risks?
2. Cash flow: What are the expected cash flows to PowerStream shareholders under the status quo and the proposed transaction?
3. Liquidity: What flexibility is there for PowerStream shareholders (jointly and individually) to divest their holdings and what is the associated impact of such divestment under the status quo and the proposed transaction?
4. Acquisition price: Is the purchase price for Hydro One Brampton consistent with market value?
5. Merger relative value: Are PowerStream shareholders receiving an appropriate share of the equity in the new company ("MergeCo")?

Navigant is a global provider of specialised professional services

Navigant Consulting Ltd. is the Canadian operating company and a wholly owned subsidiary of Navigant Consulting, Inc. (together "Navigant"). Navigant is a specialised global expert services firm that helps clients create and protect value in the face of critical business risks and opportunities. Our experts have deep industry knowledge in energy, healthcare, construction, and financial services. Navigant has over 5,000 professionals located in more than 50 cities around the world, serving clients in more than 70 countries. Navigant is traded on the New York Stock Exchange and had revenue of US $860 million in 2014.

Client Profile

- Nearly 300 financial services companies including many of the largest banks in the U.S.
- Over 80% of AMLAW 100 firms
- 50 of the largest electricity and natural gas utilities globally
- Over 300 hospitals, health systems & academic medical centers, and global life sciences companies
- Federal, state and local government departments and agencies

Geographic Profile

Talent Profile

- 5,000+ employees as of Dec. 31, 2014
  - 1,700 expert / consulting professionals
  - 2,700 business process management services professionals
- Credentials include CFAs, CPAs/CAs, economists, engineers, physicians, PhDs, and attorneys
- Niche areas of expertise combined in unique ways
- Broad networks of experts and affiliates
- Collaborative and nimble resource management

NAVIGANT

Navigant's Energy practice has the depth of knowledge and breadth of capabilities to solve the most complex energy sector challenges

Navigant Energy offers a full range of advisory services specifically targeted to the power and utilities and oil and gas industries. Navigant's Energy practice has over 400 consultants around the world and a breadth of capabilities to solve the most complex energy sector issues. Our consultants have substantial hands-on industry experience with unmatched expertise across the entire energy value chain. Our experts combine their business strategy knowledge with exceptional operational experience to deliver solutions that are technically and financially viable.

Market Intelligence

1. Research
2. Benchmarking
3. Modelling

Strategy, Technology, and Organization

4. Business strategy, planning and implementation
5. Technology, strategy assessment, and advisory
6. Due diligence and M&A support
7. Innovation and R&D management
8. Technology and appliance standards, codes and testing
9. Reverse engineering and test facilities

Markets, Customers

10. EE/DSM Market research and characterisation
11. EE/DSM evaluation, measurement, and verification
12. EE/DSM program design

Operations & Asset Management

13. Energy markets advisory
14. Utility contracting support
15. Energy project development support
16. Integrated resources planning 2.0
17. Electric transmission planning and operations
18. Electric distribution planning and operations
19. End user energy strategy

Financial, Risk and Regulatory

20. Retail regulatory support
21. Energy SME litigation support

Sample Engagements

Merger of PowerStream and Barrie Hydro

The City of Barrie retained Navigant to serve on the Joint Steering Committee to negotiate a merger agreement between Barrie Hydro and PowerStream. As part of this engagement, Navigant explored the potential savings, rate, and reliability impacts of the potential merger and made numerous presentations to Barrie City Council and senior staff regarding the implications of the potential merger. The merger was ultimately approved by the three municipal shareholders of the two utilities.

Transaction advisor to Constellation Energy merger of Constellation Energy and Exelon

Navigant was engaged by Constellation Energy to provide transaction due diligence and advisory assistance in support of the company's proposed merger with Exelon which would result in one of the nation's largest competitive energy products and services suppliers with 64 terawatt-hours of load per year delivered to over 100,000 businesses and approximately 1 million residential clients.

Navigant mobilized a cross functional team of transaction and energy professionals from its corporate finance and energy practices to perform a comprehensive due diligence process that focused on identifying any strategic, financial, or operating issues with the potential to affect the valuation/stock price of the combined entity post-close. Navigant's process and findings were delivered in a summary report identifying any potential red flag issues and recommendations on mitigation strategies for any key risks identified.

Transmission utility transaction diligence

Navigant provided technical, financial and due diligence support to the a large utility investment holding company in its pursuit of the acquisition of AltaLink, an Alberta Transmission Facility Operator. Navigant's support included a review of the regulatory framework and ratemaking process for transmission facilities, a comparison of the Alberta regulatory framework with other jurisdictions globally and an assessment of the key risk factors related to the business.

Technical advisor to the Distribution Sector Review Panel

Navigant provided technical consulting services to the Ontario Distribution Sector Review Panel. As part of this engagement, Navigant provided insight on previous local distribution company mergers and quantification of associated savings, trends in LDC spending and implications on the potential for further efficiencies, cost drivers for local distribution companies and potential efficiencies, and areas where local distribution companies are currently sharing common infrastructure, systems, and processes, and the potential for further efficiencies in these areas.

NAVIGANT

Key aspects of the business case are reasonable

- Navigant ***reviewed, analysed, and tested*** the business case assumptions, and revised as appropriate

- Hydro One Brampton purchase price
  - Price for Hydro One Brampton ***in within, but at the high end of, the valuation range***

- Relative valuation of PowerStream, Enersource, and Horizon
  - Relative valuation of PowerStream is ***reasonable***
  - PowerStream Solar is ***likely undervalued***
    - As a result, management successfully negotiated that the PowerStream Solar assets be carved out and earmarked for only the existing PowerStream shareholders
    - Small negative impact to the expected PowerStream solar cash flows, up to $1.7M for Vaughan

- Synergies
  - Synergies were ***reviewed and determined to be reasonable*** and achievable
    - Roughly half of the functional area synergies are likely conservative (i.e. synergies may be greater)
    - There are risks associated with the Synergies, but PowerStream has a track record of delivering

NAVIGANT

Proposed transaction creates value for the City of Vaughan, but comes with risk

1. Transaction ***requires ~$56M investment*** from the City of Vaughan, plus or minus closing adjustments (10%)

2. The transaction is ***expected to create between $71 and $102M of shareholder value***, approximately 30% to 80% more than the $56M initial investment, representing a 6 to 9% return on investment

3. Vaughan's initial investment is expected to be ***recovered through increased dividends over 10 years***, if ratepayer benefits are also considered, the simple payback period is reduced to seven years

4. Over 25 years, the present value of the ***projected benefit to Vaughan electricity customers is $61M***, equivalent to an **average of $40 per year for all customers** *and $25 per year for residential customers*

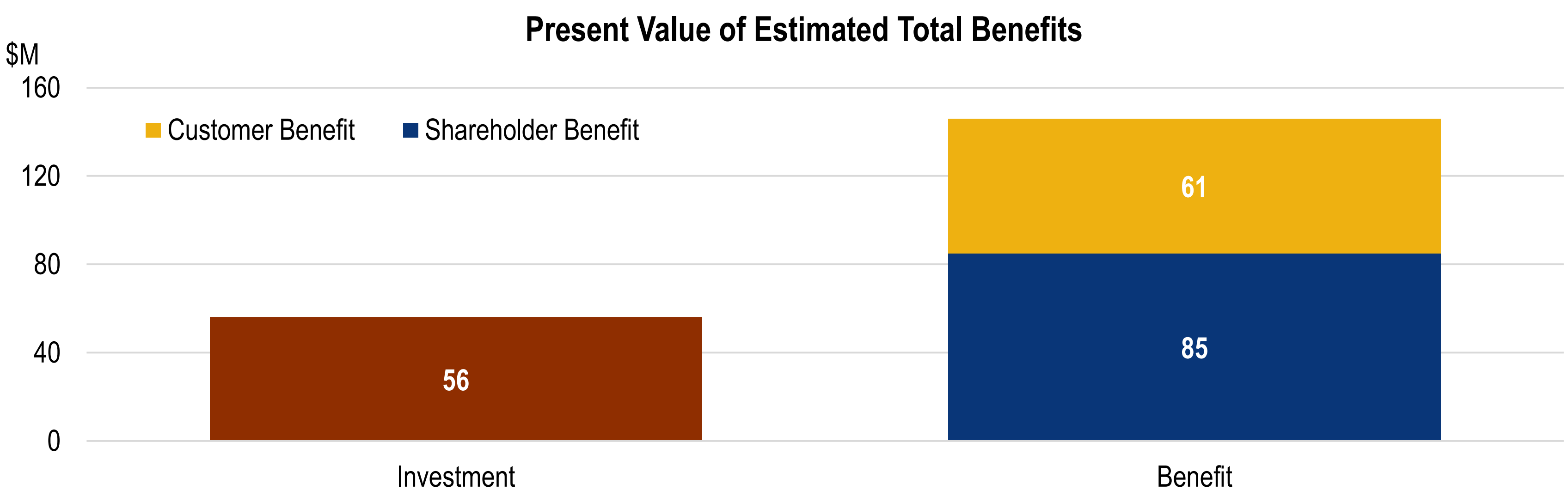
5. The transaction can be ***funded with limited or no cash*** if the City of Vaughan (i) sells 10% of PowerStream and reinvests the proceeds, or (ii) swaps its shareholder loans for equity; the former also ***mitigates risk associated*** with the *transaction*

6. The investment has ***more risk and is expected to provide a lower return*** than investments made to-date in PowerStream, although under certain reasonable conditions the return could be higher

7. The transaction is expected to ***have a limited impact on the liquidity*** of Vaughan's existing investment, and could result in a small improvement

Combined shareholder and customer benefit is substantial

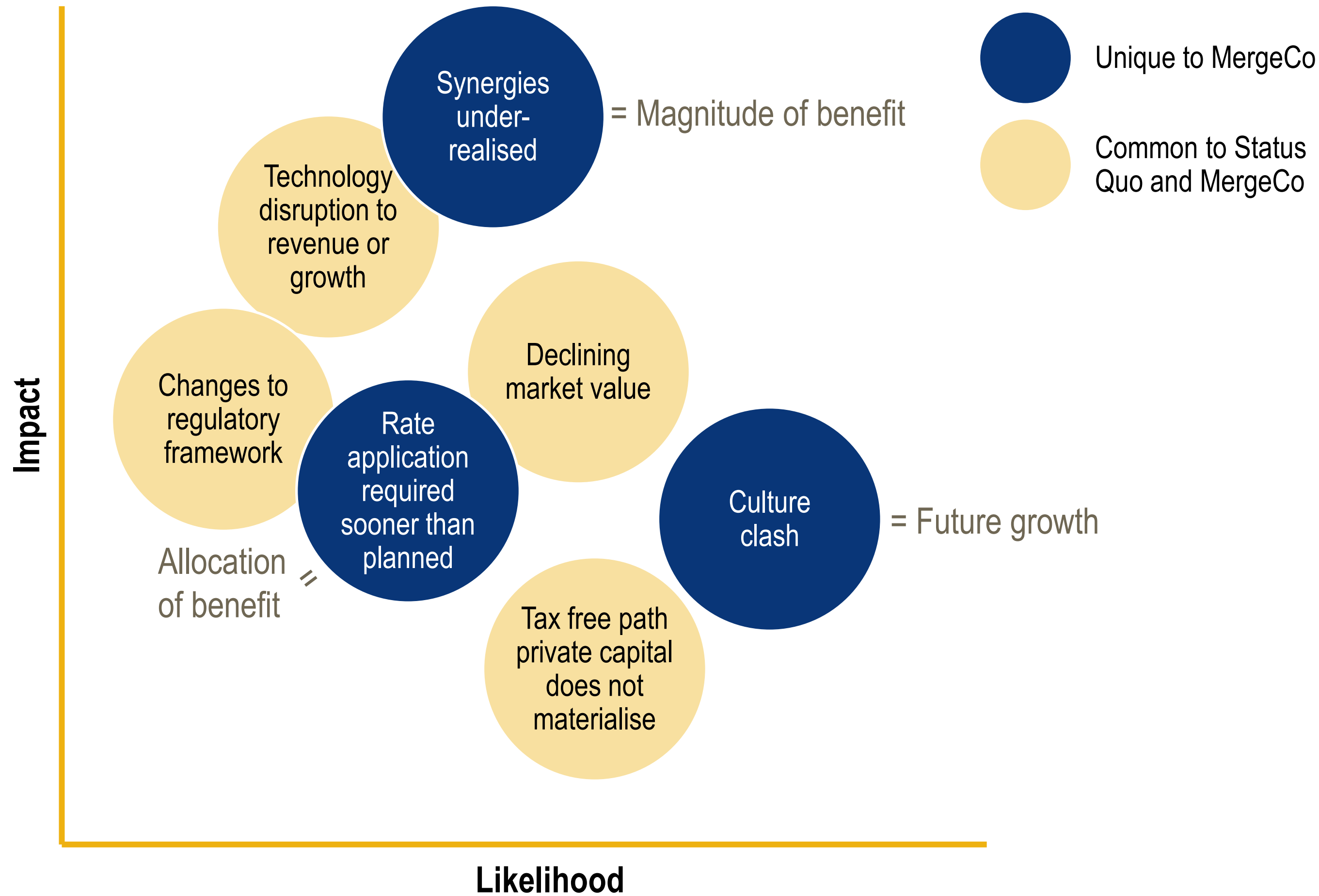
» $146M of total benefit (present value) for $56M investment
  › $85M of benefit is realised through increased dividends and equity value to Vaughan
  › $61M of benefit is realised through lower electricity rates than would otherwise



Source: Navigant. "Decision support for the proposed three-way merger between PowerStream Holdings Inc., Enersource Corporation, and Horizon Holdings Inc., and the joint acquisition of Hydro One Brampton Networks Inc.". September 18, 2015.
Notes:
1) All values discounted at 5%

NAVIGANT

Navigant assessed the risks associated with the transaction based on (i) likelihood of occurrence and (ii) impact on value



NAVIGANT

Four considerations on funding options; 10% sale provides second highest cash flow, but mitigates risk

Consideration	Status Quo	100% Cash	Convertible Note	10% Sale
1. Cash flow magnitude				
Investment required	$7M	$56M	$0	$11M
Net present value (10-years)	$101M	$87M	$126M	$122M
2. Cash flow risk	--	Neutral	Increase	Neutral
3. Investment exposure	--	Increase	Neutral	Neutral
4. Liquidity	--	Decrease	Decrease	Neutral

NAVIGANT

Disclaimer

No Warranties or Representations, Limitation of Liability

THIS REPORT (THE “REPORT”) WAS PREPARED FOR VAUGHAN HOLDINGS INC. ON TERMS SPECIFICALLY LIMITING THE LIABILITY OF NAVIGANT. NAVIGANT’S CONCLUSIONS ARE THE RESULTS OF THE EXERCISE OF ITS REASONABLE PROFESSIONAL JUDGMENT. USE OF THIS REPORT BY THE READER FOR WHATEVER PURPOSE SHOULD NOT, AND DOES NOT, ABSOLVE THE READER FROM USING DUE DILIGENCE IN VERIFYING THE REPORT’S CONTENTS.

NAVIGANT DOES NOT MAKE ANY REPRESENTATIONS OR WARRANTIES OF ANY KIND WITH RESPECT TO (I) THE ACCURACY OR COMPLETENESS OF THE INFORMATION CONTAINED IN THE REPORT OR IN ANY OF THE OTHER DOCUMENTS, (II) THE PRESENCE OR ABSENCE OF ANY ERRORS OR OMISSIONS CONTAINED IN THE REPORT, (III) ANY WORK PERFORMED BY NAVIGANT IN CONNECTION WITH OR USING THE REPORT, OR (IV) ANY CONCLUSIONS REACHED BY NAVIGANT AS A RESULT OF THE REPORT, AND (E) ANY USE WHICH YOU MAKE OF THIS REPORT, OR ANY RELIANCE ON IT, OR DECISIONS TO BE MADE BASED ON IT, ARE THE RESPONSIBILITY OF YOU. NAVIGANT ACCEPTS NO DUTY OF CARE OR LIABILITY OF ANY KIND WHATSOEVER TO YOU, AND ALL PARTIES WAIVE AND RELEASE NAVIGANT FOR ALL CLAIMS, LIABILITIES AND DAMAGES, IF ANY, SUFFERED AS A RESULT OF DECISIONS MADE, OR NOT MADE, OR ACTIONS TAKEN, OR NOT TAKEN, BASED ON THIS REPORT.

POWERSTREAM MERGER AND ACQUISITION

Recommendation

The Commissioner of Finance and City Treasurer, and Interim Commissioner of Legal and Administrative Services and City Solicitor, in consultation with the Director of Development Finance and Investments recommend:

1. That the presentation by PowerStream Inc. on the merger and acquisition proposal be received;

2. That the presentation by Navigant Consulting Ltd. on the proposal's financials be received;

3. That the presentation by Gowlings LLP on the proposal's governance topics be received;

4. That such resolutions or recommendations as may be submitted by Vaughan Holdings Inc. be considered; and

5. That the City Clerk be requested to schedule a Special Meeting of Council between September 23, 2015 and October 9, 2015 to consider the recommendations of Committee of the Whole (Working Session) in this matter.

Contribution to Sustainability

Additional revenue opportunities provide support and financial sustainability to the City of Vaughan. Therefore investment opportunities must be considered and evaluated to determine if they present investment value and are aligned with the City's investment principles.

Economic Impact

Vaughan Holdings Inc. (VHI), which is wholly owned by the City of Vaughan, has been presented with a new investment opportunity for a three way merger between PowerStream Holdings Inc., Enersource Corporation and Horizon Holdings Inc. and subsequent acquisition of Hydro One Brampton. The proposed transaction would require an equity cash injection of approximately $56M from VHI, subject to closing costs. There is a potential for increased dividend income for the City and synergy savings are expected to result in reduced upward pressure on future hydro rates to the average rate payer. As discussed in detail further in this report several funding options were considered for the estimated $56M cash injection, including a combination of using funds accumulated within VHI and available funds within the City's investment portfolio, or a conversion of the City's promissory note with PowerStream, or 10% sale of equity in PowerStream. A combination of using funds accumulated within VHI and the 10% equity sale is deemed the preferred funding option as it allows the City to benefit from the proposed transaction with minimal cash injection. However, available funds within the City's investment portfolio will be leveraged until a sale is finalized.

Several key economic impacts are discussed in further detail throughout the body of this report.

Communications Plan

On April 16, 2015, the Premier of Ontario made several announcements with respect to recommendations received from her Advisory Council of Government Assets including the initiation of negotiations with PowerStream, Enersource, and Horizon on a transaction that would see the three local distribution companies merge and also acquire 100 per cent of Hydro One Brampton Networks Inc. to create the second largest local distribution company in Ontario.

Negotiations have been ongoing over the last several months. Given the imminent shareholder decisions expected on the proposal, communications has been an important consideration, which is why the Communications teams from Vaughan, Markham, Barrie and PowerStream have had meetings and ongoing discussions to develop a collaborative approach to informing stakeholders about the proposal.

The first phase of the communication approach was the issuance of a news release by the City of Vaughan on August 24, 2015. It cited the status of the ongoing negotiations of the merger and acquisition, background on the proposal, benefits to the community, a quote from the Mayor and expected decision timelines. This release was posted on the City of Vaughan's website. PowerStream has also created a webpage with information on the proposal at www.PowerStream.ca/Merger.

The next phase in the approach was promoting this at the September 22, 2015 Committee of the Whole Working Session and informing members of the public that they are welcome to attend and make a deputation. This was done with advertisements in four local newspapers – Vaughan Citizen, Thornhill Liberal, Lo Specchio, and Corriere Canadese, posts on the City's corporate social media sites, and through promotions on Vaughan TV, the City's blog and an eBlast to subscribers of the City's eNewsletter. The City contacted local reporters directly to ensure they were aware of this meeting.

MergeCo is considering issuing a joint news release prior to the first Committee or Council meeting Working Group of any shareholder among the shareholder cities. If this release is issued, the City will promote it via Vaughan's website, social media accounts and eNewsletter.

If all the PowerStream shareholders approve the merger proposal, MergeCo will issue a joint news release after final shareholder approval has been completed. Subsequently, MergeCo may also place advertisements in several dailies. The City will support these activities and promote them via Vaughan's website, social media accounts and eNewsletter.

Purpose

The purpose of this report is to inform Council and the public on the proposed three way merger and subsequent acquisition of Hydro One Brampton.

PowerStream, Enersource and Horizon utilities are working to finalize details of their proposed merger and joint proposal to purchase Hydro One Brampton from the Government of Ontario. This proposal is the result of many months of effort and negotiation between the parties, and is currently at the critical phase of PowerStream's Board approval. Once endorsed by PowerStream's Board recommendations will flow to the shareholder's holding companies and subsequently to their respective municipal Councils for consideration.

Subject to PowerStream's Board meeting on September 11, 2015 and Vaughan Holdings Inc. (VHI) Board meeting on September 16, 2015, a written communication will follow this report outlining VHI Board's recommendation.

The attached Business Case and Navigant Consultant report provides full details of the proposed Merger and Acquisition.

The contents of this report are based substantially on the investment proposal negotiated to date and business case provided and highlights key areas for consideration. Given the size of the documents, for the reader's reference, the MergeCo Business Plan from PowerStream (Attachment 1), the MergeCo Business Case from PowerStream (Attachment 2) and the written consultant report from Navigant Consulting (Attachment 3) are available for viewing in hard copy at the Office of the City Clerk located on the 1st floor of Vaughan City Hall at 2141 Major Mackenzie Drive, Vaughan, ON L6A 1T1.

Given the complexity of the report, the contents are reported in the following format:

Executive Summary
A. Background on PowerStream
B. Local Distribution Company's (LDCs) mergers in the Provincial context
C. History of current merger and acquisition proposal
D. Shareholder due diligence
E. Context for evaluation of proposal
F. Benefits and Risks of proposal
G. Governance issues associated with proposal
H. Funding options for acquisition
I. Financial impacts to the City
J. Benefits to the rate payer from merger and acquisition

Background - Analysis and Options

Executive Summary

On April 16, 2015, four of Ontario's largest electricity distribution companies (LDCs) announced they would work together to form a new utility that would serve almost a million customers in York Region, Simcoe County, Peel Region, Hamilton and St. Catharines.

The proposed merger transaction comprises the following:

- A merger of the regulated and non-regulated business activities of: PowerStream, Enersource, and Horizon (individually, a 'Party' and collectively, the 'Parties').
- An acquisition by the Parties of the regulated electricity distribution business of Hydro One Brampton Networks Inc. (HOBNI) for gross proceeds of $607M, net of any purchase price adjustments

The combined entities described above are referred to as "MergeCo" and the corresponding transactions are referred to as the "Transaction". The creation of MergeCo must be approved by all shareholders and is subject to regulatory approvals.

The Transaction will create the second largest electricity distribution company in Ontario with almost 1 million customers, 2.7 billion in assets, and 2.5 billion rate base. In total, MergeCo is expected to deliver approximately **$427M of net cash savings (pre-tax) through synergies** in the first 10 years following the merger thereafter sustained at approximately $51M per year ($310M in operating synergies + $111M of capital synergies, net of transition costs).

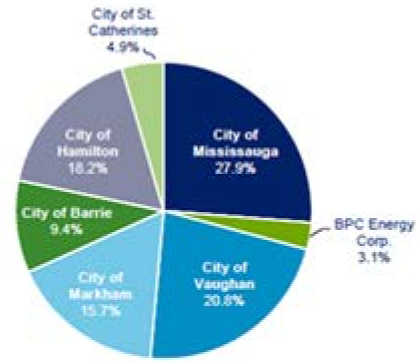
The City of Vaughan holds 45.31% of PowerStream via its holding company VHI. Under the merger, the City's ownership of MergeCo will be approximately 20.80% (second largest shareholder in the proposed MergeCo). Figure 1 below illustrates the pre and post ownership shares involved in the Transaction.

The City of Vaughan receives regular dividend and interest revenues from PowerStream, estimated to be approximately $16M in 2015. The equity investment required from the three PowerStream shareholders is expected to be $125M, while Vaughan's portion of this is approximately $56M.

Figure 1: Individual Shareholder Ownerships

Pre-Merger Shareholding	
Enersource	
City of Mississauga	90.0%
BPC Energy Corp. (Borealis)	10.0%
	100.0%
PowerStream	
City of Vaughan	45.3%
City of Markham	34.2%
City of Barrie	20.5%
	100.0%
Horizon Utilities	
City of Hamilton	78.9%
City of St. Catharines	21.1%
	100.0%

Potential Merge Co Shareholding Contribution



Key Aspects of the Merger

Following months of negotiation with merger partners, PowerStream, on behalf of its shareholders, has reached substantial agreement on a number of key aspects.

1. Relative Value: PowerStream Shareholders will own 46% of the new company, (Vaughan's portion will be 20.8%)

2. Solar "Carve Out": PowerStream's Solar business is expected to be kept as a separate operating subsidiary under MergeCo; the dividend stream from existing PowerStream solar investments will be maintained through special shares

3. Local Presence & Facilities: all of PowerStream's existing facilities will be maintained following the merger

4. Governance: Six of 13 board members are to be appointed by PowerStream Shareholders, (Vaughan will have 3 representatives)

5. Executive: significant Executive presence of current PowerStream staff

6. Liquidity Rights: improved rights to raise capital for growth, or to monetize existing investments

Managing the Risks of the Transaction

The key risks to the Transaction may be seen as follow:

- Synergies (cost savings) may not be achieved
- Integration challenges
- Unidentified expenses / liabilities
- Regulatory uncertainty affects business plan going forward
- Shared ownership and a greater investor focus

Many of the risks identified above are seen to be mitigated through PowerStream's history of achieving synergy and integration post-merger/acquisition. PowerStream has entered four transactions of a similar nature in the last ten years. Additionally, the consolidation of these smaller LDCs will produce a larger and presumably more prominent corporation that will have the ability to exert more influence on the industry and related policy. The new MergeCo will also see greater independence on the Board of Directors with more powers delegated to that Board to steer the corporation in its pursuit to create value for the shareholders and bring savings to the electricity consumer. PowerStream was more closely held by its shareholders whereas MergeCo will see many more shareholders providing a greater deal of autonomy to its Board to steer the organization to a larger corporation mentality. This risk is mitigated by the fact that current PowerStream shareholders are still represented by 6 of the 13 Board members, of which Vaughan has 3 representatives. Effectively, Vaughan will need to focus its attention towards being an investor rather than the operations of the corporation.

Key benefits of the Transaction

Improved Financial Returns to Shareholders

- Steady and growing dividend stream at a higher level than the current arrangement; Vaughan can expect dividends to increase in the first 10 year post transaction by $62M
- Payback of equity investment for Hydro One Brampton of approximately ten years; Vaughan's $56M equity investment expected to increase to a value of approximately $90M – $135M over 10 years

Reduced upward pressure on future hydro rates for customers compared to the current arrangement

- Overall, approximately 8% decrease in future distribution rates (e.g. mitigates future increases). Customers will benefit through the savings of $450M over 25 years or an average of $40 annually. This will help reduce upward pressure on future rates.

Stronger Platform for Growth in the Future

- Much larger utility with a bigger geographic footprint, more diversification, and greater capital resources and opportunities to finance expansion

Greater Influence on Government Policy

- Merged utility will be in a key position of leadership to influence government and regulatory energy policy for the benefit of customers and shareholders

Part A - Background on PowerStream

PowerStream is the second largest municipally owned LDC in Ontario, serving over 370,000 residential and commercial customers. PowerStream is regulated by the Ontario Energy Board (OEB).

The principal activity of PowerStream is the distribution of electricity within Alliston, Aurora, Barrie, Beeton, Bradford West Gwillimbury, Markham, Penetanguishene, Richmond Hill, Thornton, Tottenham and Vaughan, as well as Collingwood, Stayner, Creemore and Thornbury through its strategic partnership with Collus PowerStream.

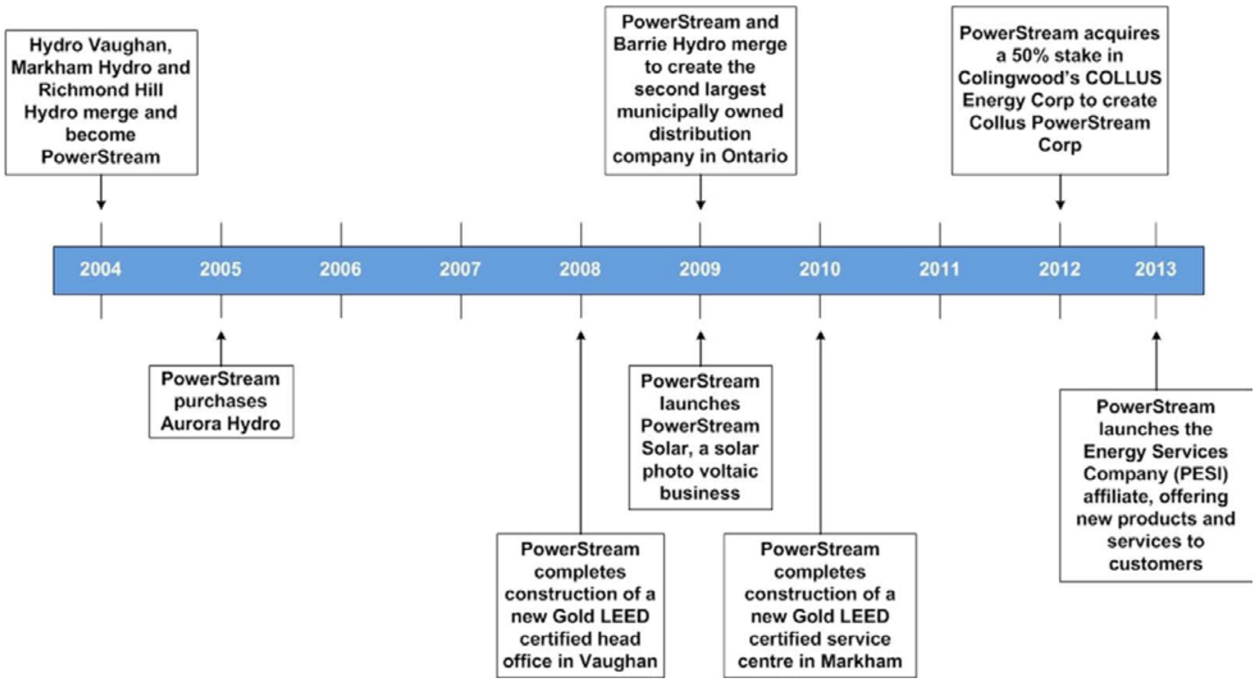
PowerStream encompasses an 854 sq. km service territory and delivers over 8,384 GWh of electricity to customers annually.

Growth is a key performance driver for PowerStream

PowerStream's strategy is to build on its core distribution business to become Ontario's premier integrated energy service provider. PowerStream's aim is to be a leading utility with respect to size, scale and scope, enabling the Corporation to realize the potential synergies and efficiencies that come with growth.

PowerStream has led the industry with successful mergers, improving service reliability, reducing upward pressure on rates, and has been an active member that supports its local communities. A few of PowerStream's recent business activities are illustrated below.

Figure 2: PowerStream 10 Year History



Part B - LDC mergers in the Provincial Context

LDCs in Ontario operate in a complex regulated environment highly responsive to shifts in Ontario government policy. The current distribution sector makeup is a product of a number of pieces of legislation and is summarized below.

Up until 1996 most municipalities in Ontario had their own Municipal Electricity Utility or MEU. These MEU's were governed similar to any other municipal department such as water or sewage and were not revenue generating. This changed in 1996 when the Macdonald Commission suggested significant changes to the structure of MEUs. Legislation enacted by the Ontario government in 1998 confirmed that municipal governments should continue to own electric utilities, but required that they be transformed into business corporations under the Ontario Business Corporations Act (OBCA).

The City's existing PowerStream assets (Principal Investment) were inherited

The incentive to structure sustainable corporations, or LDCs, in a deregulated market contributed to the initial wave of consolidation in the sector. This brought the number of MEUs in the province from 307 to around 89 by 2001. Since then, government policy surrounding a transfer tax holiday have led to a handful of LDC consolidations, (with PowerStream in a notable leadership position) and acquisitions by Hydro One which have brought the number of utilities currently operating in the province down to 66. There has also been some private equity participation in LDCs, although these have been by and large limited to 10% due to prohibitive tax treatment.

The Province of Ontario has endorsed LDC consolidation

The policy rationale for LDC consolidation (for the benefit of ratepayers and shareholders) has been well established and consistently advanced from multiple sources over the past few years.

In 2012, the Ontario government created the multi-partisan Distribution Sector Review Panel to provide expert advice to the government on how to improve efficiencies in the electricity sector with the aim of reducing costs for customers and increasing efficiencies. The Panel strongly endorsed industry consolidation and noted the following:

Regarding Consolidation:

"...LDCs in Ontario should be consolidated into eight to twelve larger regional distributors...six to ten regional distributors would be located in southern Ontario and typically have a minimum of 400,000 customers..."

"...regional distributors must be contiguous and stand shoulder to shoulder."

Regarding New Investment:

"New investment in the distributor sector, notably from pension funds, should be encouraged. The report recommends that the Ontario Government enter into negotiations with the Federal Government on a tax agreement which would facilitate the removal of the transfer tax on the sale of LDC assets."

Regarding Governance:

"The membership of the boards of directors of regional distributors should have at least two thirds independent directors..."

Part C - History of Current Merger and Acquisition Proposal

LDC consolidations reduce upward pressure on hydro rates

In the spring of 2014, the Ontario government, seized with the issue of seeking efficiencies out of publicly-owned assets, began the review of government-owned assets. The review was specifically geared towards the optimization of government-owned assets including Hydro One and Ontario Power Generation (OPG). PowerStream was actively engaged in the review headed by former TD Bank Chair, Ed Clark. Although not originally tasked with the issue of LDC consolidation, the Clark panel quickly determined that the potential savings to ratepayers were too significant to not address. The panel released their final report in the spring of 2015.

The report stated the following with respect to Hydro One Brampton and utility consolidation:

1. The Province should proceed immediately with a sale or merger of its interest in Hydro One Brampton Networks Inc. to or with Enersource Corporation, PowerStream Holdings Inc. and Horizon Holdings Inc., intended to catalyze consolidation in the Greater Toronto and Hamilton Area and to strengthen competition in the electricity distribution sector by increasing the number of LDCs with the capacity to drive further consolidation.

2. The Province should amend the transfer tax rules and departure tax rules that apply when municipal electricity utilities leave the payment-in-lieu of taxes regime both on a time-limited basis and implement these changes as quickly as possible.

3. The mandate and powers of the Ontario Energy Board should be strengthened to ensure that changes in industry structure do not put upward pressure on rates.

Through the passing of the 2015 budget and ongoing efforts with the OEB, the government has effectively endorsed all of the Clark panel's recommendations with respect to electricity distribution. Refer to Attachment 4, Province of Ontario press release on April 16, 2015, for a description of the relationship of these recommendations to this Transaction.

At the May 1, 2015 PowerStream Board Strategic Planning Session options were discussed and it was resolved that the preferred option to be executed was a 3-Way Merger acquiring Hydro One Brampton.

The proposed merger transaction comprises the following:

- A merger of the regulated and non-regulated business activities of: PowerStream Inc., Enersource Corporation, and Horizon Holdings Inc. (individually, a 'Party' and collectively, the 'Parties').
- An acquisition by the Parties of the regulated electricity distribution business of Hydro One Brampton Networks Inc. (HOBNI) for gross proceeds of $607M net of any purchase price adjustments

Merger Synergy Savings benefits customers in the form of reduced upwards pressure on rates

As a result of the merger, MergeCo expects to generate the following material savings (values are pre-tax):

- Aggregate gross operations, maintenance and administration expenditure (OM&A) savings of $355M over the first 10 years, or 14% of total OM&A expenditures, thereafter continuing at a savings rate of approximately 15% annually, (i.e., not cumulative).
- Aggregate gross capital expenditure savings of $168M over the first 10 years, thereafter continuing at a sustained level of $8M annually.

MergeCo will incur transition costs of approximately $95M in the first three years with respect to systems and process integration and human resource costs.

In total, MergeCo will deliver approximately $427M of net cash savings (pre-tax) in the first 10 years following the merger thereafter sustained at approximately $51M per year.

Part D - Shareholders Due Diligence

To determine if the Transaction is in VHI's and in turn the City's best interest, due diligence has been undertaken on the valuation, level of investment and financing options. To ensure independent advice and recommendations are provided; the shareholders of PowerStream have jointly retained industry experts Navigant Consulting, Ltd. and BDR North America Inc. In addition, Gowlings LLP has been jointly retained for legal advice. PowerStream Inc. agreed to pay for the Consulting fees incurred. Furthermore, each utility company in the Transaction have secured their own independent advisor to perform due diligence work.

Navigant (NYSE: NCI)

Navigant is a specialized, global professional services firm dedicated to assisting clients in creating and protecting value in the face of critical business risks and opportunities. Navigant Consulting services include a wide range of financial management services, investigation services, litigation support services, and business management consulting services, as well as software programs for use in database management, analysis and benchmarking.

Through senior level engagement with clients, Navigant professionals deliver expert and advisory work through implementation and business process management services. The firm combines deep technical expertise in Disputes and Investigations, Economics, Financial Advisory and Management Consulting, with business pragmatism to address clients' needs in highly regulated industries, including Construction, Energy, Financial Services and Healthcare.

BDR North America Inc.

BDR is a Toronto-based consulting firm of seasoned professionals specializing in the energy sector in terms of mergers and acquisitions, business and strategic planning and regulatory.

BDR has for many years managed and advised regarding the process of merger, acquisition and divestment of both generation and "wires" facilities in the electricity industry and related affiliates. Key to these assignments is the development of appropriate valuations for the businesses in the context of the relative risks.

Gowlings LLP

Gowlings is a leading Canadian and international law firm, with over 700 legal professionals serving clients in 10 offices across Canada and around the world.

Process Approach and Roles for Merger and Acquisition Proceedings

The Transaction is the result of many months of effort and negotiation between the Parties.

*Working Groups - w*orking groups were established and comprised of representatives from each LDC's departments to determine synergies and transition costs

Deloitte - Deloitte was engaged to provide a third party valuation of PowerStream, Enersource, and Horizon*.* Deloitte produced a business case model to assess the merger and purchase transaction, considering net synergies, capital structure, financing, and regulatory impacts

The Valuation model and Business Case model were reviewed, stress tested, and negotiated over six months by each of the following parties:

Navigant Consulting, Ltd. - representing PowerStream Shareholders

Morrison Park Advisors Inc. – providing advisory services to PowerStream

PricewaterhouseCoopers LLP – representing Enersource Shareholders

Ernst & Young Global Limited – representing Horizon Shareholders

CFO & Supporting Management Teams – of each LDC

The Business Plan (Attachment 1) which described comprehensive details of the proposed transaction and the Business Case (Attachment 2) are both available for viewing at the Office of the City Clerk.

Part E - Evaluation of the proposed transaction

The City's Investment Policy is a good context for evaluating the opportunity

The City's Investment Policy lists three investment objectives in priority order:

1. Preservation of principal investment
2. Maintenance of adequate level of liquidity
3. Earning a competitive rate of return

Based on the order priority from the above list it can be seen that certain risk "trade-offs" may occur between the items. While preservation of principal is the number one priority, investment in a utility corporation does not come with the same guarantees that might accompany a bond transaction for instance. Furthermore, due to prohibitive tax consequence as discussed further below in this report, the ability to withdraw the investment based on cash needs is minimal at best pointing to a very low level of liquidity. In turn, these two items must be weighed against the opportunity for a rate of return that is not available under virtually any other investment opportunity that a municipality is able to enter within the City's existing portfolio and legislation. The City does, however, have legal authority to enter this proposed transaction as set out in the Ontario's Electricity Act, 1998 and Ontario's Municipal Act. Some of these elements are discussed further throughout this report.

Since the City's investment in PowerStream is different than a traditional municipal investment (i.e.T-bill, bonds, etc.), there are other factors that also need to be taken into consideration. These other factors may include governance/control, impact on customer hydro rates, and utility market trend and risks.

The written report by Navigant, the shareholders financial consultant, provides professional and independent analysis on the proposed transaction.

Staff and consultants have been in frequent discussions with PowerStream to assess the proposed transaction. The written Navigant report is based on these discussions and the business case provided to the shareholders by PowerStream. Information discussed in the report is based on a variety of topics, but most importantly the following key areas of consideration:

- Is the PowerStream's relative valuation in MergeCo reasonable?
- How much equity investment is required by the City of Vaughan?
- What are areas to maximize value in the transaction?
- What is the treatment for Solar shares?
- What are the benefits and risks to City of Vaughan?
- How does the City fund its share of the acquisition of Hydro One Brampton?
- What are the governance issues to consider?

Further details on these key areas are discussed below and in subsequent parts of the report, but a more fulsome discussion from the consultants may be found in their written analysis.

Is the PowerStream's relative valuation in MergeCo reasonable?

The proposed relative valuation of PowerStream Inc. under the merger is approximately 46% (excluding the Solar Class A shares) based on enterprise values using discounted cash flows of the three utilities. Reasons to exclude Solar Class A shares are discussed in more detail below.

The City owns 45.315% of PowerStream and based on the relative valuation, the City's ownership of MergeCo will be approximately 20.80%. The 20.80% represents the proportional market value of PowerStream in the combined market value of MergeCo.

Navigant Consulting Ltd., the shareholder's financial consultant, had review the valuation model and did an independent standalone valuation of the PowerStream relative valuation. Navigant's assessment is that the relative valuation of PowerStream is reasonable and fair.

How much equity investment is required by Vaughan?

The proposed acquisition of Hydro One Brampton is priced at $607M. The rate base valuation is approximately $404M. The equity injection required from the three PowerStream shareholders is expected to be $125M, while Vaughan's portion of this is approximately $56M, subject to closing costs. The closing costs are uncertain at this time, however it is expected that a contingency of up to 10% of the equity injection ($5.6M) will be requested in order to cover these expenses. Additionally, the transaction costs may also have an effect on the 2015/2016 dividend payouts by PowerStream. The acquisition price of Hydro One Brampton has been set at 1.5 times the rate base valuation of approximately $404M. The market valuation (premium) for utilities companies has increased due to the current low interest rate environment.

What are areas to maximize value in the transaction?

There are two areas that were substantially agreed to in the negotiation that maximize value in the transaction for Vaughan, which include: 1) Separation of PowerStream's Solar business Class A shares under MergeCo, and 2) Favourable Transfer tax treatment for the Brampton purchase.

1) Separation of PowerStream's Solar Business Class A Shares

Based on Navigant's analysis, keeping the Class A shares of Solar business separate in the merger transaction is preferred. Solar would be kept as an operating subsidiary of MergeCo and existing PowerStream shareholders would retain ownership of economic interests of those assets. There are three advantages to this:

- Undervalued - the Solar business is undervalued in the relative valuation. Separating it out through Special Class shares maximize value.
- Certainty of cash flow the Solar business is based on fixed contracts and provides a predictable income stream. Table 1 below provides the Solar cash flow forecast provided by PowerStream under the MergeCo Transaction.
- Liquidity – The Solar program provides a repayment of the initial investment providing greater financial flexibility and access to cash.

Table 1 – Solar Dividends 10 year forecast

Solar Dividends (10 Years Forecast) - All values in $'Mil	**2016**	**2017**	**2018**	**2019**	**2020**	**2021**	**2022**	**2023**	**2024**	**2025**	**Total**
Status Quo											
Dividend - Total	10.10	10.60	10.20	9.20	8.10	7.00	6.00	5.70	4.40	3.40	74.70
Dividend - Vaughan 45.31%	4.58	4.80	4.62	4.17	3.67	3.17	2.72	2.58	1.99	1.54	33.85
MergeCo											
Dividend - Total	10.10	10.30	9.90	8.70	7.20	6.40	5.40	5.20	4.10	3.20	70.50
Dividend - Vaughan 45.31%	4.58	4.67	4.49	3.94	3.26	2.90	2.45	2.36	1.86	1.45	31.94
Variance: Status Quo vs. MergeCo*	-	(0.14)	(0.14)	(0.23)	(0.41)	(0.27)	(0.27)	(0.23)	(0.14)	(0.09)	(1.90)

Source: PowerStream's forecast

* Variance of the Solar Dividend under MergeCo due to service management fees, financing costs, and dividend policy

While the dividends are tracking slightly less under the merger scenario it should be noted that this is mainly attributable to interest rate adjustments resulting from a planned debenture renewal and the management services cost recovery to MergeCo for the management of these assets. These are costs that were previously covered through PowerStream overhead and are therefore now affecting the dividends in a more direct manner. Combined with the increased dividends for MergeCo as a whole, this dividend schedule forecast is still deemed reasonable in the context of the overall transaction.

The terms and conditions of keeping the Solar business separate from MergeCo will be based on the draft Solar term sheet. The draft Solar term sheet outlines the nature of the agreement including management services, cost recovery, ownership principles, dividend policy and intercompany financing.

Although the final form will not be ready until transaction closing, addressing the terms above provide a good basis for assurance to the current PowerStream shareholders that the segregation of the Solar business continues returning an expected high level of value while being fully incorporated in to the merger and acquisition transaction. Additionally, it is important to note that PowerStream shareholders are still able to participate and benefit from any **new** solar asset projects under MergeCo.

2) Reducing future Tax obligation for the Brampton Purchase

The Transfer Tax on Hydro One Brampton is 33% of the sale price, which translates to approximately $200M. PowerStream negotiated with the Province for the removal of this tax. Through discussion with the Province has not removed this tax, they have agreed to provide a PILs tax credit of approximately $60M, which can be used to partially offset the future transfer taxes.

This will help with liquidity concerns, but the full departure and transfer tax would be applied to PowerStream or MergeCo sale transactions above 10%. To assist with future growth, limited partnerships are being proposed, which effectively permits growth capital investment without triggering tax liabilities. This will be determined through future tax rulings before closing the Brampton purchase.

To further illustrate the severity of the tax consequence, if PowerStream shareholders were to receive an equity value of $900M for their current holdings in PowerStream then approximately $350M in tax would be owing, which equates to approximately 40% of the value.

Part F - Risks and Benefits

What Are the Benefits and Risks to the City of Vaughan?

Figure 3 below illustrates the benefits and risks to the City of Vaughan of a potential merger.

Figure 3: Benefits and Risks of Merger

Benefits

- Potential net synergies of $427M
- Potential average rate of return of 6.3%
- Consistent with Provincial mandate for consolidation
- Future utility rate reductions of $40 per customer per year
- Potential for increased cash flow and equity growth over forecast
- Provide economies of scale for growth and innovation
- Platform to expand in to new lines of business
- Greater opportunity for alternative equity funding
- Retain the value of Solar business

Risks

- Payback period is long term if funded by cash
- Forecasted synergy, returns, and equity growth lower than expected
- Purchase price of Hydro One Brampton on the high end
- Burdensome tax treatment on ownership changes
- Disruptive technologies could impact value
- Regulatory changes could affect future value
- Less direct control in terms of governance
- Growth strategy will require undetermined additional future equity investment

Part G – Governance issues associated with proposal

Gowlings LLP will provide a memo to speak to many of the governance issues cited and this memo will be attached to a communication to Committee of the Whole (Working Session) subsequent to the VHI Board meeting, however below is a list of the issues for consideration.

- Board Composition
- Independent vs. Non-Independent Members
- Proposed Management Structure
- Special Approvals
- Dividend Policy
- Agreement Structure

Part H - Funding options

How does the City fund its share of the acquisition of Hydro One Brampton?

The proposed transaction would require an equity investment of approximately $56M, subject to closing costs, from Vaughan.

The three funding options identified in order of preference are:

- Sell 10% of existing PowerStream shares
- Use City cash reserves
- Convert promissory note in PowerStream

Selling 10% of PowerStream to fund transaction is the recommended funding option

The sale of 10% of PowerStream Inc. is expected to bring in approximately $40M to Vaughan specifically. This cash can be used to fund most of the equity investment required at approximately $56M, with the remainder coming from funds retained in VHI for investment opportunity.

Based on Navigant's analysis, the sale of 10% is preferred for the following reasons:

- Provide higher dividend cash flow with minimal equity investment
- Lock in the current market value
- Minimize risk on liquidity and preservation of capital with no tax consequence
- Hold City's cash reserve for future investment opportunities
- May attract a strategic private partner that could influence tax rule change and increase internal competition on future divesture
- Selling 10% effectively transfers a portion of the risk
- 10% sale aligns with Provincial mandate
- Allows the merger to move forward which will ultimately benefit utility users

On August 12, 2015, VHI Board approved the potential sale of 10% of existing PowerStream shares as a source of funding for the approximately $56M equity investment required from Vaughan. The acquisition will be initially funded by funds retained within VHI of $16M and the remaining $40M funded through the City's investment portfolio. It is anticipated that the City's portion will be recovered by the sale of the 10% shares of PowerStream.

Other funding options are available, but less financially advantageous

The use of available City cash in the City's investment portfolio without a subsequent sale of 10% of PowerStream for recovery is the second preferred funding option. There is approximately $16M funds retained in VHI. The additional cash required would need to come from the City's investment portfolio with no immediate recovery. Although, the City can financially manage the funding, these are earmarked for other purposes, albeit in the distant future. The use of cash investment is subject to risks, particularly liquidity constraint of the transaction. The City's cash on hand is the most liquid financial asset whether it's collecting interest in the bank or investment in low risk and high liquidity short term investments. This investment would not allow easy access to fund the City's future long-term capital program when required, hence the sale of 10% is preferred to reduce these risks. This merger transaction should be viewed as a long term income generator, with a long payback period and restricted liquidity.

Converting the promissory note to fund the transaction is the least preferred option. The City currently has an $86M promissory note with PowerStream. The promissory note has a rate of return of 5.58% on $78M and 4.03% on $8M and can be called at any time. Therefore the promissory note is a liquid asset that earns a very competitive rate in today's environment. The promissory note is not subject to other risks, namely liquidity and preservation of principal, which would exist if converted.

Part I - Financial impacts to the City

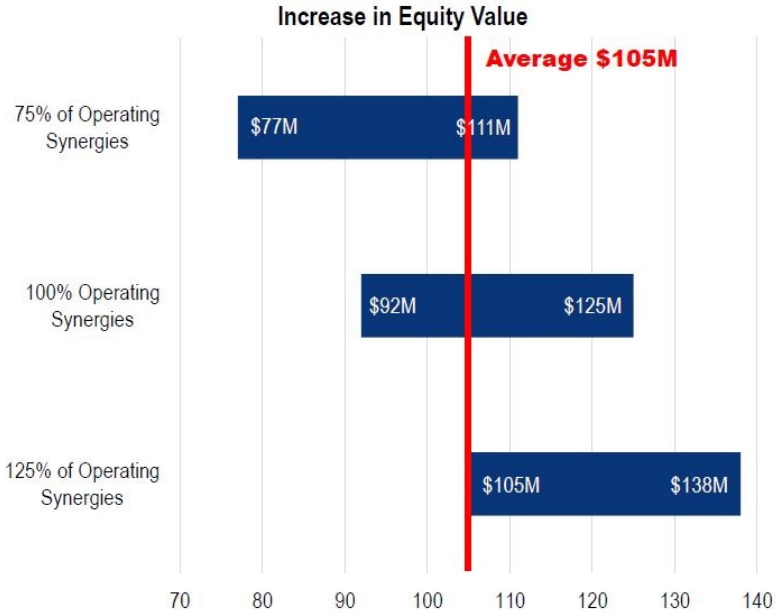
The proposed transaction is expected to increase equity value and provide a steady and growing dividend stream to shareholders

Subject to assumptions and risks described in this report and attachments, MergeCo is expected to deliver meaningful shareholder benefits both in terms of equity growth and dividend cash flow. The following assumes financing through a cash contribution and are summarized as follows:

To the benefit of City of Vaughan

- Vaughan's contribution to the acquisition of Hydro One Brampton is estimated at $56M. Vaughan's share of the $230M – $300M increase in shareholder value is approximately $90M-$135M.

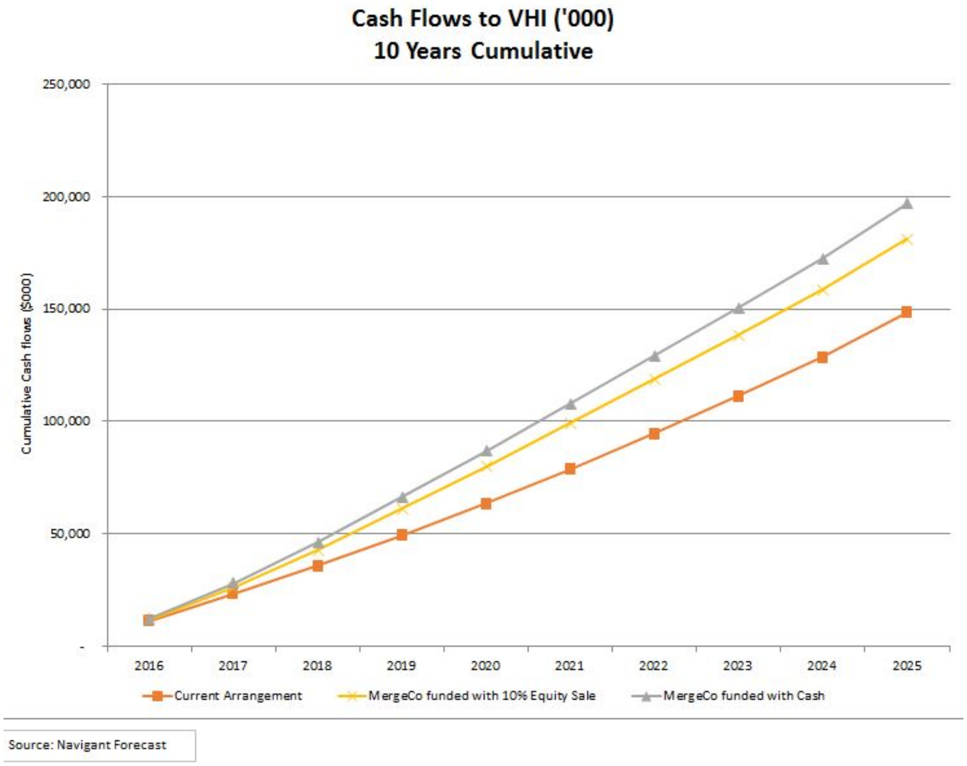
Figure 4 – Growth of equity value



Source: Navigant Project Aura Valuation and Business Case Model (August 28, 2015)
Notes:
1) Range of for each synergy scenario based on alternative terminal value calculations, e.g., perpetuity growth rate, final year cash flow, and exit multiple
2) Assumes 5% discount rate

- Vaughan can expect their dividend to increase in the first ten years post transaction by $62M.

Figure 5 – Cash flows to Vaughan



MergeCo

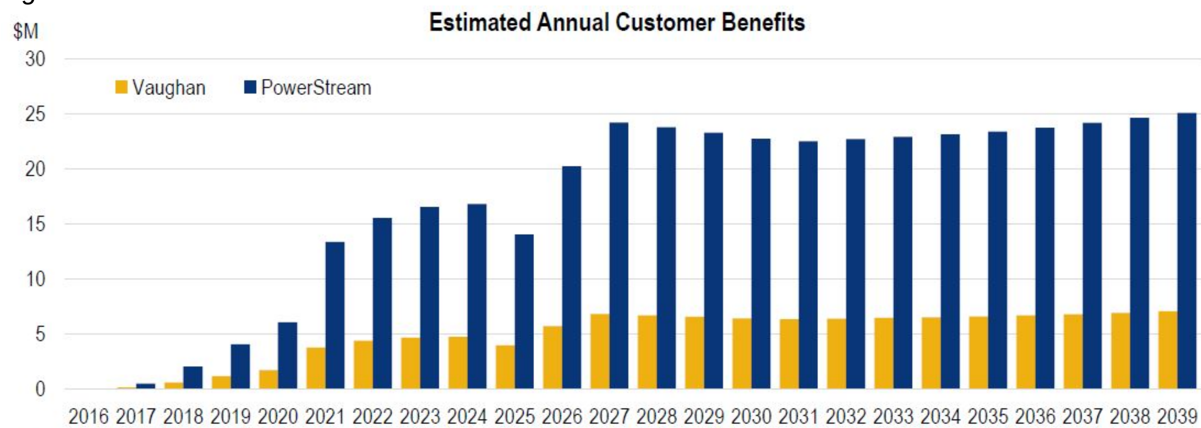
- Increase in the Net Present Value (NPV) of earnings of approximately $276M from $1,154M to $1,430M from 2016 to 2036 relative to the current arrangement, a 24% increase.
- Rates of return begin to normalize post 10 years, however projections beyond 10 years become less predictable given several uncertainties. Therefore, the focus is predominantly on the initial 10 year period.

Part J - Benefits to the rate payer

The proposed merger between PowerStream, Enersource and Horizon Utilities and the acquisition of Hydro One Brampton would bring significant value to customers. Analysis has found that customers will be able to save approximately $450 million over 25 years (an average of $40 per customer annually). Efficiencies realized as a result of the merger would reduce the upward pressure on distribution rates, allowing customers to benefit directly through lower bills than would be seen if the merger does not take place.

Figure 6 below illustrates the estimated annual customer benefits from the merger. It shows the overall savings to PowerStream customers and the Vaughan specific customer benefits. Included in these savings are also direct savings on City of Vaughan facilities, which equates to approximately $222K per annum. This results in an added benefit to City of Vaughan property tax payers in the form of reduced pressure on annual tax levy increases.

Figure 6 – Customer benefits



Source: Navigant Project Aura Valuation and Business Case Model (August 28, 2015)
Notes:
1) All values nominal
1) Customer benefits over the first 10 years are driven primarily by avoided capital expenditures
2) Customer benefits after the first 10 years are driven primarily by lower operating costs

In addition, there are numerous benefits of the merger that go beyond cost savings on customer bills. These include:

- Better ability to serve customers through enhanced and shared systems and range of products or services available.
- Increased resources to respond to reliability issues.
- Investment in new business opportunities improves economic development in the City.

Regional Implications

Residents of York and greater Toronto and Hamilton areas being served by MergeCo can expect reduced upward pressure on future hydro rates with the proposed transaction.

Conclusion

PowerStream, Enersource and Horizon utilities are working to finalize details of their proposed merger and joint proposal to purchase Hydro One Brampton from the Government of Ontario. This proposal is the result of many months of effort and negotiation between the parties, and is currently at the critical phase of PowerStream's Board approval. Once endorsed by PowerStream's Board, recommendations will flow to VHI and subsequently to City Council for consideration.

Subject to a PowerStream Board meeting on September 11, 2015 and a VHI Board meeting on September 16, 2015, a written communication will follow this report outlining VHI Board's recommendation.

The proposed transaction would require an equity cash injection of approximately $56M, subject to closing costs. There is a potential for increased dividend income for the City and synergy savings are also expected to reduce upward pressure on future hydro rates. The investment should be viewed as long term in nature. Additionally, the proposed transaction will result in more

Revised

risk, slightly less liquidity, and a transformation in the governance structure compared to current arrangement, but is still seen as favourable given the potential economic benefits.

Attachments

1. MergeCo Business Plan from PowerStream Inc. (available at the Office of the City Clerk for viewing upon receipt)
2. MergeCo Business Case from PowerStream Inc**.** (available at the Office of the City Clerk for viewing upon receipt)
3. Navigant Consulting Ltd. written analysis of Business Case (available at the Office of the City Clerk for viewing upon receipt)
4. Province of Ontario April 16, 2015 Press release on proposed transaction

Report prepared by:

John Henry, Commissioner of Finance and City Treasurer
Heather Wilson, Interim Commissioner of Legal and Administrative Services/City Solicitor
Lloyd Noronha, Director of Development Finance and Investments
Alex Ly, Senior Analyst, Development Finance and Investments

Respectfully submitted,

John Henry Commissioner of Finance and City Treasurer	Heather Wilson Interim Commissioner of Legal and Administrative Services/City Solicitor

ATTACHMENTS 1, 2, 3 available at the Office of the City Clerk for viewing

ATTACHMENT 4

Province of Ontario announcement on April 16, 2015:

In accepting the recommendation of the Premier's Advisory Council on Government Assets, the province intends to proceed with a merger of Enersource Corporation, Horizon Utilities, Hydro One Brampton Networks Inc. and PowerStream Holdings Inc. to ensure value for the province and to help catalyze Local Distribution Company (LDC) consolidation for the benefit of ratepayers.

Together, the merger of these three strong performing utilities with Hydro One Brampton will create the second-largest electricity distributor in Ontario by number of customers. The merged entity would deliver efficiencies and economies of scale while continuing to provide safe, reliable and clean electricity. This represents a major step forward in promoting LDC consolidation in Ontario, in line with the recommendations made in the 2012 Ontario Distribution Sector Review Panel Report.

The municipalities that own the three partner LDCs have all expressed support for this merger.

Enersource

Enersource Corporation serves over 200,000 residential and commercial customers across Mississauga. It is a diversified energy and technologies company that serves customers through the distribution of electricity and the delivery of services related to the design, operation and maintenance of electrical systems. Ninety per cent of Enersource Corporation is owned by the City of Mississauga, and 10 percent is owned by BPC Energy Corporation (Borealis), which is part of the Ontario Municipal Employees Retirement System (OMERS).

Horizon Utilities

Horizon Utilities Corporation provides electricity and related utility services to over 240,000 customers in Hamilton and St. Catharines. Horizon Utilities is wholly owned by Horizon Holdings Inc., a company jointly owned by the cities of Hamilton and St. Catharines through their holding companies Hamilton Utilities Corporation and St. Catharines Hydro Inc.

Hydro One Brampton

Hydro One Brampton Networks Inc. was acquired by Hydro One from the City of Brampton in 2001. It has more than 150,000 residential, commercial and industrial customers and serves an area of 300 square kilometers. In order to meet the growth of the community and needs of its customers, Hydro One Brampton continues to work with the City of Brampton and other organizations to improve Brampton's infrastructure and distribution system.

PowerStream

PowerStream Holdings Inc. is a municipally owned energy company providing power and related services to more than 375,000 customers primarily residing or owning a business in communities located immediately north of Toronto and in Central Ontario. It is jointly owned by the Cities of Barrie, Markham and Vaughan through their respective holding companies, Barrie Hydro Holdings Inc., Markham Enterprises Corporation and Vaughan Holdings Inc."