



## memorandum

C 1  
Communication

**CW (WORKING SESSION)**  
**September 22, 2015**

**DATE:** SEPTEMBER 18, 2015

**TO:** MAYOR AND MEMBERS OF COUNCIL

**Item- 1**

**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 is 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%	<u>\$5.6</u>
<b>Total Funding Required for Transaction</b>	<b>\$61.6</b>
From Available VHI Cash Balance	\$16.0
Issuance of New Common Shares to the City	<u>\$45.6</u>
<b>Proposed Funding Available for Transaction</b>	<b>\$61.6</b>

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)*

<b>Cashflow to VHI ( 10 Years Forecast)</b> - All values in 000's											
	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	Total
<b>Status Quo</b>											
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
<b>TOTAL</b>	<b>8,810</b>	<b>16,193</b>	<b>16,712</b>	<b>16,925</b>	<b>17,056</b>	<b>18,529</b>	<b>18,710</b>	<b>19,207</b>	<b>19,120</b>	<b>18,206</b>	<b>169,469</b>
Cumulative 10 Yr Cashflow excl equity injection											176,267
<b>MergeCo - funded by cash (100% OPEX and 100% CAPEX synergies)</b>											
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
<b>TOTAL</b>	<b>(45,036)</b>	<b>19,879</b>	<b>21,996</b>	<b>23,512</b>	<b>23,328</b>	<b>23,135</b>	<b>23,055</b>	<b>22,872</b>	<b>23,694</b>	<b>24,832</b>	<b>161,269</b>
Cumulative 10 Yr Cashflow excl equity injection											222,869
<b>MergeCo - funded by 10% sale</b>											
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
<b>TOTAL</b>	<b>(915)</b>	<b>18,708</b>	<b>20,596</b>	<b>21,906</b>	<b>21,672</b>	<b>21,462</b>	<b>21,345</b>	<b>21,171</b>	<b>21,861</b>	<b>22,845</b>	<b>190,650</b>
Cumulative 10 Yr Cashflow exd 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**

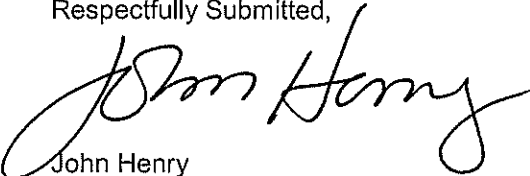
On September 16, 2015, the Board of VHI approved the PowerStream Board's resolution to enter the three way merger and acquisition of Hydro One Brampton.

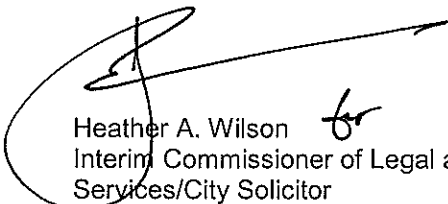
As wholly owned by the City of Vaughan, VHI's decision to adopt and approve the resolution and recommendation as detailed above are submitted to the September 22, 2015 Committee of the Whole (Working Session) meeting for further consideration by Council.

### **Attachments**

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

Respectfully Submitted,

  
John Henry  
Commissioner of Finance and City Treasurer

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

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



montreal • 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.