
TO: GENERAL COMMITTEE

SUBJECT: MERGER OF ALECTRA AND GUELPH HYDRO

PREPARED BY AND KEY CONTACT: C. MILLAR, DIRECTOR OF FINANCE/TREASURER, EXT 5130
D. MCALPINE, GENERAL MANAGER OF COMMUNITY AND CORPORATE SERVICES, EXT 4421

SUBMITTED BY: D. MCALPINE, GENERAL MANAGER OF COMMUNITY AND CORPORATE SERVICES

GENERAL MANAGER APPROVAL: D. MCALPINE, GENERAL MANAGER OF COMMUNITY AND CORPORATE SERVICES

CHIEF ADMINISTRATIVE OFFICER APPROVAL: M. PROWSE, CHIEF ADMINISTRATIVE OFFICER

RECOMMENDED MOTION

WHEREAS Barrie Hydro Holdings Inc., the Municipality's subsidiary (the "Subsidiary") and The Corporation of the City of Barrie (the "Municipality") are parties to the Unanimous Shareholders Agreement for Alectra Inc. ("Alectra") dated January 31, 2017 (the "Current Alectra Shareholder Agreement");

AND WHEREAS the Board of Directors of the Subsidiary will consider the purchase by Alectra of all of the issued and outstanding shares of Guelph Hydro Electric Systems Inc. ("GHESI") from Guelph Municipal Holdings Inc. ("GMHI") in consideration for the issuance to GMHI of Class G Common Shares in the capital of Alectra, and the amalgamation of Alectra Utilities Corporation ("AUC") with GHESI, both of which at such time will be wholly-owned subsidiaries of Alectra, under Section 174 of the *Business Corporations Act* (Ontario), to continue as one local distribution company to be called Alectra Utilities Corporation, all conditional upon the completion of a merger participation agreement to be entered into between Alectra, AUC, GHESI and GMHI, in accordance with the conditions set out therein;

AND WHEREAS it is desirable to amend the Current Alectra Shareholder Agreement to add GMHI and The Corporation of the City of Guelph as parties thereto (the "New Alectra Shareholder Agreement");

AND WHEREAS the form of New Alectra Shareholder Agreement has been provided to the Municipality;

AND WHEREAS management of Alectra and staff of AUC, and their advisors, have provided a review of the key aspects of the New Alectra Shareholder Agreement;

NOW THEREFORE IT IS RESOLVED THAT:

1. Subject to approval of the Board of Directors of the Subsidiary, the City of Barrie authorizes and approves the New Alectra Shareholder Agreement, substantially in accordance with the form presented to the Municipality, subject to any non-material modifications or amendments as approved by the President, CEO and General Counsel and Secretary of Alectra and authorizes the Municipality to enter into and deliver the New Alectra Shareholder Agreement in a form satisfactory to the President, CEO, General Counsel and Secretary, and to perform, observe and comply with its obligations under such Agreement.
2. The Mayor and City Clerk of the City of Barrie are hereby authorized and directed to execute and deliver the New Alectra Shareholder Agreement in accordance with the foregoing resolutions.

3. The Mayor and City Clerk of the City of Barrie are hereby authorized and directed to sign and/or dispatch and deliver all other documents, notices, articles, certificates to be signed and/or dispatched or delivered under or in connection with the New Alectra Shareholder Agreement or to take any action deemed necessary in respect of any of the foregoing.

PURPOSE & BACKGROUND

4. In February, 1999, City Council directed that the City of Barrie retain ownership of the assets of the Barrie Public Utilities Commission and incorporate a Holding Company and other Affiliate corporations under the Ontario Business Corporations Act to operate Barrie's electrical distribution corporation (the Corporation) for the benefit of the citizens of Barrie.
5. In October, 2000, City Council directed, through Resolution 00-G-291, the establishment of a Holding Company and its related subsidiaries in accordance with the requirements of The Electricity Act, 1998. The Holding Company was named "Barrie Hydro Holdings Inc." and the subsidiaries were named "Barrie Hydro Distribution Inc." and "Barrie Hydro Energy Services Inc."
6. In 2008 City Council approved the merger of Barrie Hydro Holdings, with PowerStream. PowerStream is owned, through their holding Companies by the Cities of Vaughan, Markham and Barrie. In 2015, City Council approved the merger of PowerStream, Enersource, and Horizon Utilities as well as the acquisition of Hydro One Brampton. Alectra Incorporation was formed as a result of the merger. The City of Barrie owns 8.78% of the shares of Alectra.
7. Alectra is the second largest municipally owned electrical distribution company in North America, with over 960,000 customers, serving 15 communities from Penetanguishene to St. Catharines.
8. Alectra's Strategic Plan endorsed by Barrie Hydro Holdings Inc. in October of 2016 identified a Strategic Pillar entitled Growing the Business. The goal of growing the core business through mergers and acquisitions of Local Distribution Companies (LDCs) and regional and community planning initiatives. The objective was to explore and pursue merger and acquisition opportunities that were value accretive with a preference to greater urban density and geographic contiguity, and expand the Alectra service area to the full extent of the respective municipal boundaries
9. The City of Guelph owns 100% of Guelph Municipal Holdings Inc., which in turn owns 100% of the electricity distribution company Guelph Hydro Electric Systems Inc. ("GHESI") and Envida Community Energy Inc.
10. Guelph Hydro is regulated by the OEB, and provides electrical power to approximately 56,000 residential, commercial and industrial customers in the City of Guelph and the Village of Rockwood. Its corporate direction is similar to that of Alectra.
17. The City of Guelph undertook an asset review of Guelph Hydro over the past year. In June, Guelph Council voted to continue exploring possible merger opportunities with other publicly owned utilities and on October 5th, Alectra was chosen as Guelph's preferred partner.
18. As part of the proposed transaction, the parties undertook a due diligence review. Legal counsel, tax and accounting firms together with other advisors were retained to assist with the due diligence review. Deloitte performed financial and tax due diligence through review of financial statements, accounting records and tax filings on Guelph Hydro. Vanry + Associates performed a review of the asset condition assessments and capital investment planning process to determine the health of the electrical distribution assets of Guelph Hydro. Alectra engaged Gowling WLG (Canada) LLP to undertake the legal due diligence review Guelph Hydro Electricity Services Inc.

19. On November 30th, Alectra Inc.'s Board of Directors – approved the Guelph Hydro – Alectra transaction. The merger of Alectra and Guelph Hydro requires the unanimous consent by all shareholders (Mississauga, Vaughan, Hamilton, Markham, Barrie, St. Catharines, OMERS Infrastructure, and Guelph). The matter will be considered by each of the shareholders and their respective municipalities in December and early January of 2018.

ANALYSIS

20. Alectra has provided Guelph Hydro – Alectra Merger presentation attached as Appendix “A” to this staff report.
21. The proposed merger of Alectra and Guelph Hydro is a less complex transaction than the previous merger of PowerStream, Enersource and Horizon and the acquisition of Brampton Hydro One. Guelph Hydro would be accepting all of Alectra’s systems, processes and procedures. This will reduce the transition costs and integration risks for Alectra. The Alectra Unanimous Shareholder Agreement has been accepted as the base document with minor adjustments required related to governance. The timeline for the merger discussions has been relatively compressed with the intent to conclude the approval process in early 2018.
22. The relative ownership of the merged company would be:

Alectra Inc. – 95.37%
Guelph Hydro – 4.63%

The chart below shows the relative ownership of each municipality in the proposed Alectra/Guelph merger. The City of Barrie’s ownership is 8.37%.

Ownership	Pre-merger	Post-merger
City of Mississauga	27.90%	26.61%
City of Vaughan	21.49%	20.49%
City of Hamilton	18.15%	17.31%
City of Markham	15.73%	15.00%
City of Barrie	8.78%	8.37%
City of Guelph	0.00%	4.63%
St. Catharines	4.85%	4.63%
OMERS Infrastructure	3.10%	2.96%

23. The Alectra/Guelph merger is expected to achieve 1.5% in operating cost savings in first eight to ten years. Approximately \$23.9 to \$32.5 million in savings for operating expenses and approximately \$5.9 million for capital expenditures are forecasted due to the merger. These are partially offset by transition costs. In total, over the eight to ten years, Alectra/Guelph merger is forecast to achieve net aggregate cash synergy savings of \$18.0 to \$26.6 million. Annual ongoing cash synergies of \$4.3 million are projected post deferral period (net of transition costs).
24. Dividends are forecasted to increase 0.9% to 1.1% on average for current Alectra shareholders or \$0.9 to \$1.1 million per year over status quo during the deferral period. A \$6.9 to \$11.3 million total increase in Alectra’s dividend is projected during the deferral period.

25. Governance

The transaction would result in one additional shareholder and an independent representative on the Board of Directors. Currently, the City of Barrie, through BHHL, has one board member out of 13 on the Alectra Board. Under the proposed transaction, BHHL would have one board member out of 14 on the Board.

26. Impacts on Customers

According to Ontario Energy Board (OEB) policy, all of the savings resulting from LDC consolidations are transferred to customers at its first rate re-basing following a merger. The maximum length of time post-merger that a utility can wait to re-base is no later than 10 years. The period prior to such first re-basing is defined as the Re-basing Deferral Period.

The information provided by Alectra identifies that Alectra legacy customer rates will not be affected by this merger as they are following the original deferral period of 10 years. Legacy customers continue to benefit from lower rates as compared to the rates that would have existed if the original Alectra merger transaction had not occurred.

Upon rebasing, the incremental on-going synergies from this merger will be added to those of the original Alectra merger. Over 20 years, it is projected that average annual distribution rates will be 0.5% - 0.6% lower. An aggregate customer benefit of \$70 to \$85 million is projected over 20 years.

A new policy regarding mergers and acquisitions was recently announced by the Ontario Energy Board (OEB). All of the savings resulting from LDC consolidations are maintained by Shareholders for the first five years and for years six through ten, half of the earnings above 300 basis points (or 3%) above regulated rate of return are transferred to customers.

Service levels and response times are not anticipated to be affected by the merger.

27. Facilities

The information provided by Alectra in support of the merger identifies that the Alectra utility administration offices, call centres and control rooms will remain in their existing locations. The existing operations service centres will continue to serve communities from Hamilton, St. Catharines, Mississauga, Brampton, Barrie, and Markham. Guelph's operations centre will continue for a minimum of 10 years.

ENVIRONMENTAL MATTERS

28. There are no environmental matters related to the recommendation.

ALTERNATIVES

29. The following alternative is available for consideration by General Committee:

Alternative #1

General Committee could choose to not approve the Merger between Alectra and Guelph Hydro.

This alternative is not recommended as the Merger transaction improves net income and dividends. Approval of the transaction is a unanimous shareholder item for Alectra shareholders. If the City of Barrie does not approve the transaction, the merger will not proceed, even if the other shareholders are in favour of the merger.

FINANCIAL

30. Neither the City of Barrie nor Barrie Hydro Holdings Inc. are required to provide any funds/equity toward the merger.
31. Dividends are forecasted to increase 0.9% to 1.1% on average for current Alectra shareholders or \$0.9 to \$1.1 million per year over status quo during the deferral period. A \$6.9 million to \$11.3 million total increase in Alectra's dividend is projected during the deferral period.
32. The forecasted benefit to Barrie for its portion of the total increase in dividends during the deferral period would be \$577,530 to \$945,810.

LINKAGE TO COUNCIL STRATEGIC PLAN

33. The recommendations included in this Staff Report support the following goals identified in the 2014-2018 Strategic Plan:
- Responsible Spending
34. Responsible spending includes the prudent investment of City funds, to generate a return on investment which can be used as a source of financing for City projects and infrastructure.



APPENDIX "A"

GUELPH HYDRO – ALECTRA MERGER PRESENTATION PROVIDED BY ALECTRA INC.

Guelph Hydro – Alectra Merger

December 2017 – Council [Public]

PUBLIC

Executive Summary

Overview

Anticipated Benefits of Amalgamation

Shareholder	Customer
<ul style="list-style-type: none">✓ Net aggregate cash synergies of \$18.0MM - \$26.6MM in first 8-10 years<ul style="list-style-type: none">~ \$23.9MM – \$32.5MM for operating expenses~ (-\$5.9MM) for capital expenditures	<ul style="list-style-type: none">✓ 0.5% - 0.6% lower average annual distribution rates over 20 years
<ul style="list-style-type: none">✓ Annual ongoing cash synergies of \$4.3MM post deferral period (net of transition costs)	<ul style="list-style-type: none">✓ Aggregate customer benefit of \$70MM - \$85MM over 20 years
<ul style="list-style-type: none">✓ Annual operating expense synergies are consistent with prior merger experiences of PowerStream and Horizon	<ul style="list-style-type: none">✓ Fully supported distribution capital plans and investment in local communities
<ul style="list-style-type: none">✓ 10-year synergy retention allowed under OEB consolidation policy	<ul style="list-style-type: none">✓ Expectation for improved customer service levels and system reliability
<ul style="list-style-type: none">✓ Improvement in net income and dividends	

Executive Summary

Overview

Customer Benefits of this Merger:

- Alectra legacy customer rates will not be affected by this merger as they are following the original deferral period of 10 years
- Upon rebasing the incremental on-going synergies from this merger will be added to those of the original Alectra merger
- Service levels or response time unaffected
- Local service centres and administration facilities unaffected
- 1.5% operating cost savings in first 8 to 10 years due to this merger
- \$18.0MM to \$26.6MM of net cash savings from operating and capital costs in the first 8 to 10 years due to this merger
- Approximately \$4.3 MM of sustained net cash savings thereafter per year

Community Benefits of this Merger:

Facilities unaffected by this transaction

- Utility administration offices remain in Hamilton, Vaughan & Mississauga
- Call centres remain in St. Catharines & Vaughan
- Control rooms remain in Hamilton & Vaughan

Existing operations service centres will continue to serve communities from:

- Hamilton, St. Catharines, Mississauga, Brampton, Barrie, and Markham
- Guelph's operations centre will continue for a minimum of 10 years

Executive Summary

Overview

Shareholder Benefits of this Merger:

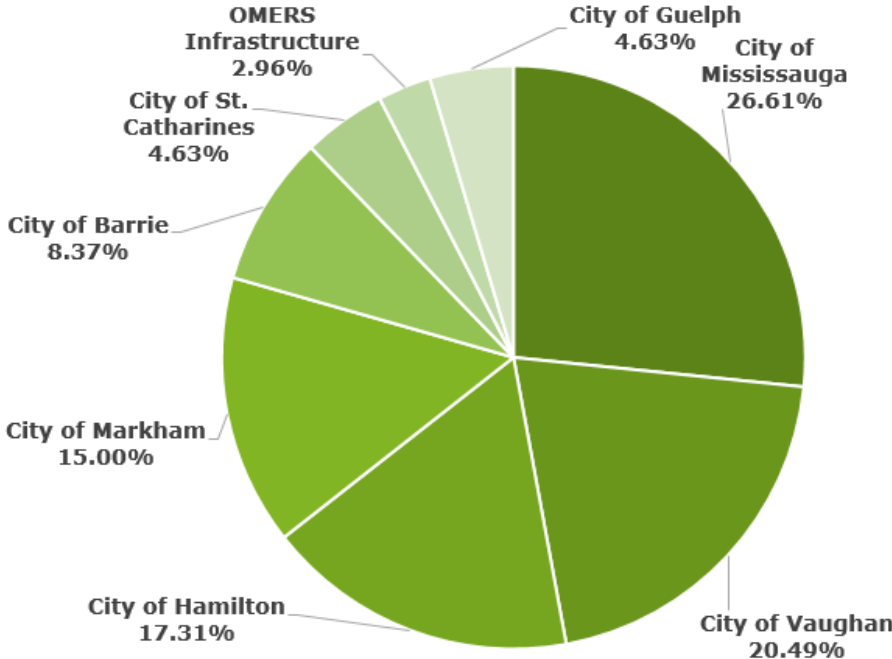
- Maintain existing municipal ownership
- One additional shareholder and an independent representative on the Board of Directors
- During the deferral period, the following benefits would accrue to the Alectra shareholders:
 - 0.9% to 1.1% average increase in dividends for Alectra shareholders or \$0.9MM to \$1.1MM per year over status quo
 - \$6.9MM to \$11.3MM total increase in Alectra’s dividend.

In summary of the proposed merger:

- Shareholder
 - Enhanced dividend revenues
 - No acquisition costs or transaction premium
 - No change in Board Representation

Individual Shareholder Ownerships:

The allocation of shareholdings under the Enterprise Value approach.



Executive Summary

Customer Benefits

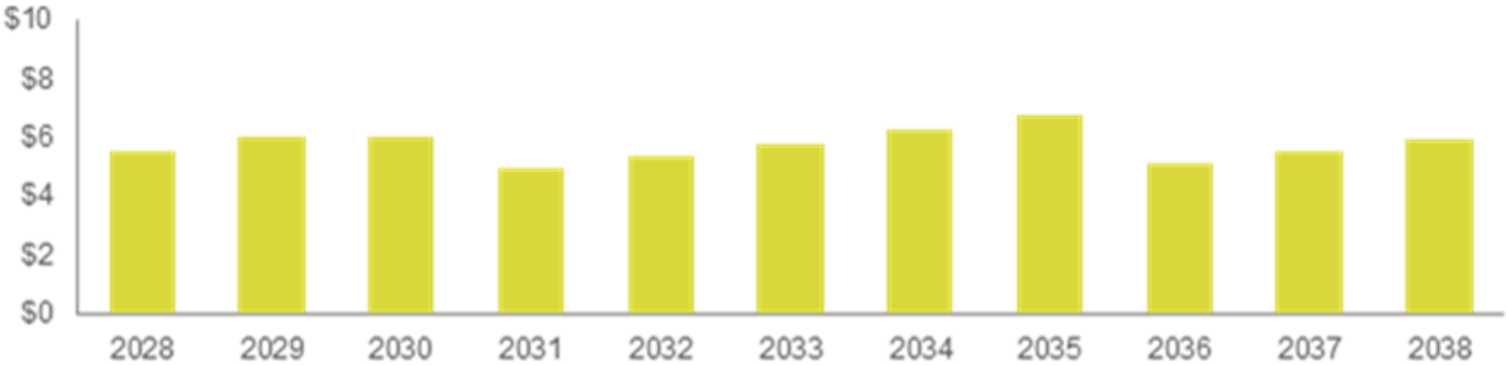


Figure 1.1 – Customer Benefits: Post Deferral Period Average Distribution Revenue per Customer (incl. ICM)

Transaction is expected to deliver lower distribution costs to MergeCo customers averaging an aggregate of \$3.5MM to \$4.3MM per year, or 0.5% to 0.6%, through the entire Forecast Period (2019 -2038)

The deferral period is up to 10 years but 8 years may be desirable to coincide with the next re-basing of Alectra

Legacy customers continue to benefit from lower rates as compared to the rates that would have existed if the original Alectra merger transaction had not occurred

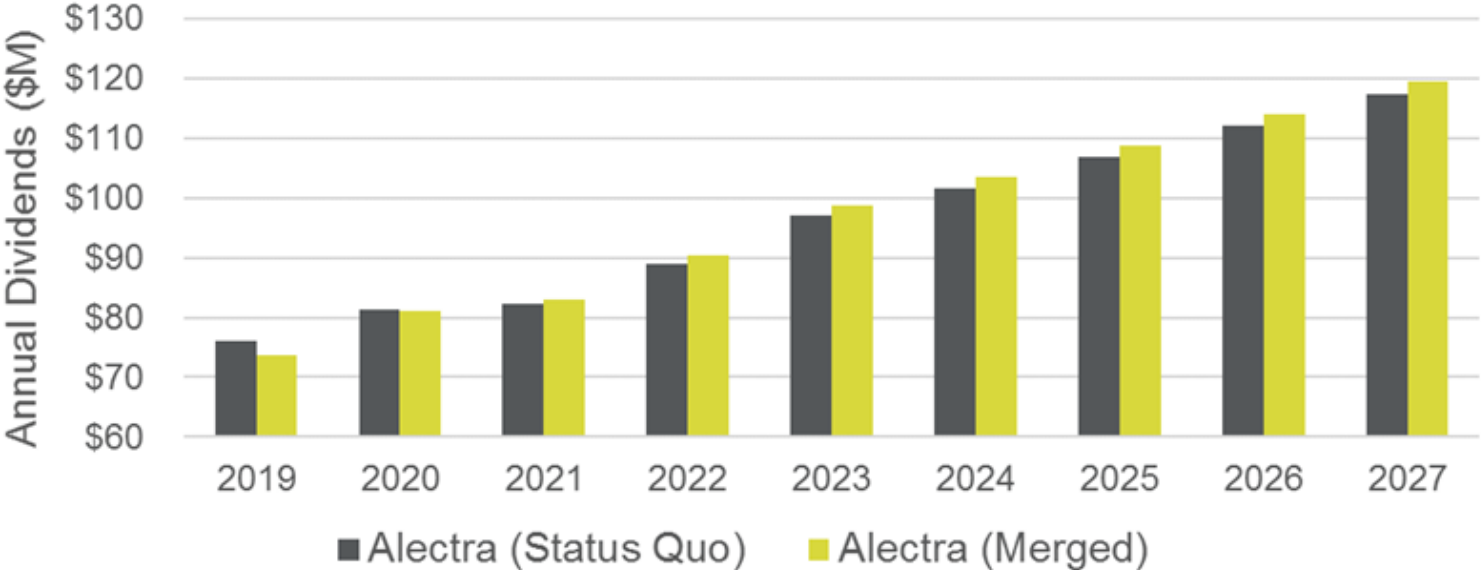
Benefit continues for the deferral period of 10 years starting in 2017

Guelph customers will benefit from lower rates as compared to the rates that would have existed if the Guelph Hydro - Alectra merger transaction had not occurred

Guelph Hydro customers avoid rate increases due to avoiding regular rate rebasing through successive Cost of Service applications in 2021 and 2026 in order to recover ongoing increases in costs

Executive Summary

Shareholder Benefits



Increase in total allocated shared dividends of:

~ \$6.9 MM to \$11.3 MM relative to the status quo over an 8 to 10 year rebasing period,

0.7% to 1.1% increase

Figure 1.2 – Shareholder Benefits – Alectra Annual Dividends (10 year deferral period)

Executive Summary

Community Benefits – Service Levels

Operating Regions

- Western Region: Legacy Horizon service territories
- Central Region: Legacy HOBNI and Enersource service territories
- Eastern Region: Legacy PowerStream service territories
- Southwestern Region: existing Guelph Hydro service territories

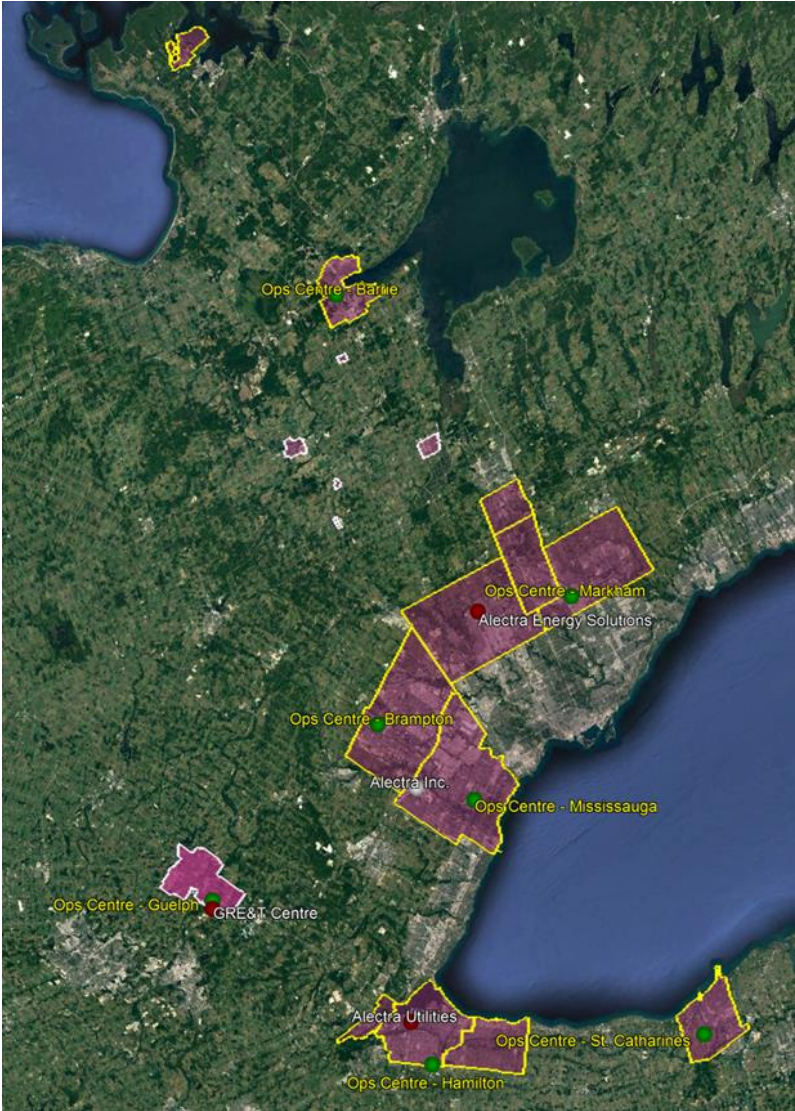
No change in facilities

- Utility administration offices remain in Hamilton, Vaughan & Mississauga
- Call centres remain in St. Catharines & Vaughan
- Control rooms remain in Hamilton & Vaughan

Existing operations service centres will continue to serve communities from:

- Hamilton, St. Catharines, Mississauga, Brampton, Barrie, and Markham
- Guelph will have a operations centre for a minimum of 10 years

Guelph Hydro – Alectra merger will not affect services levels



Executive Summary

Transaction - Structure

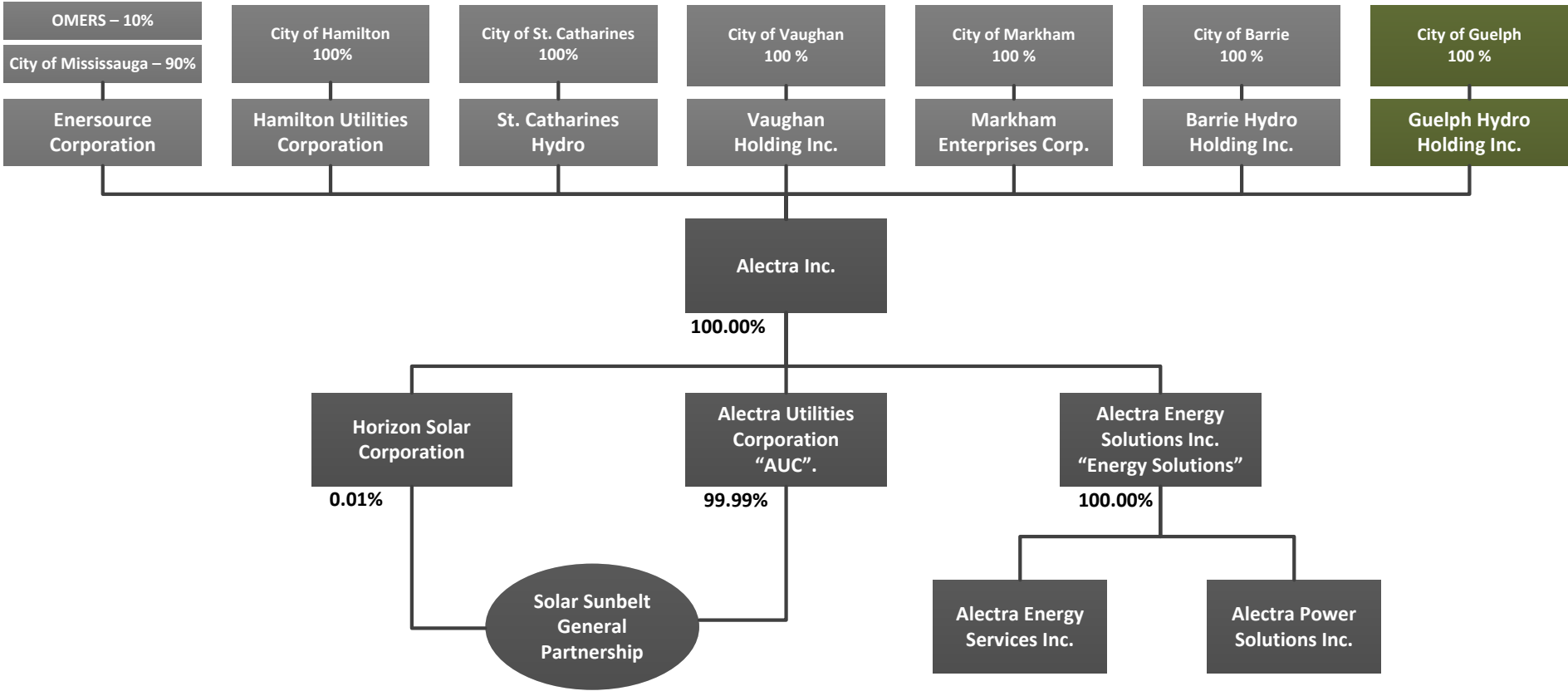


Figure 1.5 – Proposed (Legal) Corporate Structure

Executive Summary

Transaction - Valuation

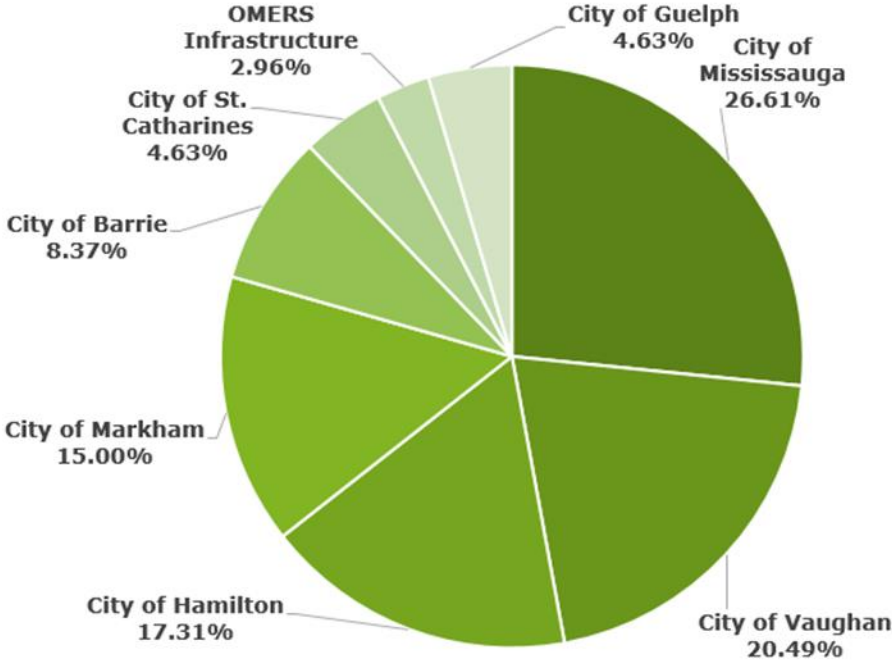
Allocation of shareholdings under the EV approach:

	Enterprise Value (EV)
Alectra Inc.	95.37%
Guelph Hydro	4.63%

Figure 1.6 – Participant Value Calculation

Ownership	Pre-merger	Post-merger
City of Mississauga	27.90%	26.61%
City of Vaughan	21.49%	20.49%
City of Hamilton	18.15%	17.31%
City of Markham	15.73%	15.00%
City of Barrie	8.78%	8.37%
City of St. Catharines	4.85%	4.63%
OMERS Infrastructure	3.10%	2.96%
City of Guelph	0.00%	4.63%
	100.00%	100.00%

Figure 1.7 - Individual Shareholder Ownerships



Executive Summary

Transaction – Regulatory Strategy

OEB recently announced new policy regarding mergers and acquisitions for utilities:

- Shareholders continue to benefit from all synergies for initial five years and, for years six through ten, must share half of earnings above 300 basis points (or 3%) above regulated rate of return
- May apply for annual incremental capital module (ICM) cost recovery to compensate for ongoing capital investments above certain thresholds

MergeCo will apply for ICM cost recover when thresholds are met

Model suggests deferring rebasing application for full 8 years

Opportunities:

Greater synergies than planned are achieved

Risks:

Synergies may not be achieved or are delayed

Transition costs are higher than expected

Regulatory uncertainty negatively impacts ICM cost recovery

2. Overview of Guelph Hydro

Transaction Participant – Guelph Hydro

Alectra and Guelph Hydro are aligned on strategic objectives

Guelph Hydro has a proud and proven history of performance and working within the community

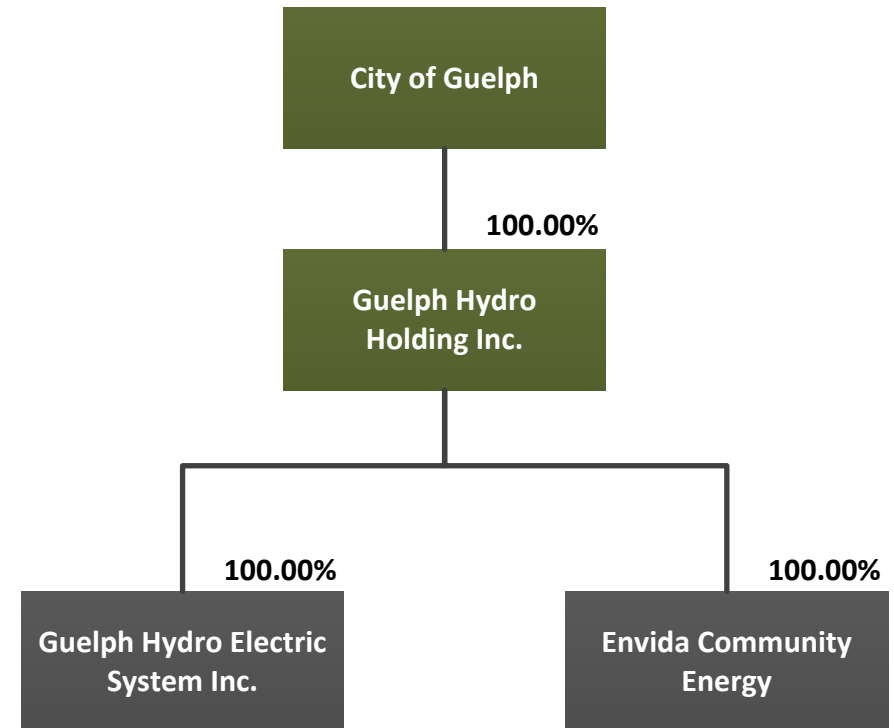
Together we bring a dynamic, forward-looking team focused on being the best in efficiency, customer service, innovation and sustainability

Guelph customers and community are committed to and focused on green energy technologies, making the regional location a strong fit for the Green Energy and Technology (GRE&T) Centre

Guelph Hydro Electric Systems Inc.

The City of Guelph owns 100% of Guelph Municipal Holdings Inc., which in turn owns 100% of the electricity distribution company Guelph Hydro Electric Systems Inc. (“GHESI”) and Envida Community Energy Inc.

Guelph Hydro is regulated by the OEB, and provides electrical power to ~ 56,000 residential, commercial and industrial customers in the City of Guelph and the Village of Rockwood



Transaction Participant – Guelph Hydro

Mission

Guelph Hydro will be ranked as one of Ontario's top electrical utilities; trusted by stakeholders to provide continually increasing value while playing a role in the rapidly transforming energy sector.

Vision

Powering community well-being.

Values

- 1) Safety, Reliability and Efficiency
- 2) Caring Relationships
- 3) Innovation and Leadership
- 4) Environmental Stewardship

Guelph Hydro Electric Systems Inc.

Serving the Township of Guelph-Eramosa, the Township of Puslinch, City of Guelph and Rockwood. The service territory covers 93 sq. km.

Infrastructure

5,903 transformers,

1 transformer station and 2 substations

10,765 poles

42 fleet vehicles

1,132 KMs of line

2 rooftop solar facilities generating 139 megawatt-hours

Facilities and Logistics

GHESI's administration functions and operations centre are located at 395 Southgate Drive, Guelph.

GHESI owns, maintains and operates an overhead primary distribution feeders and underground primary distribution circuits in the City of Guelph and in the Village of Rockwood as well as 57-13.8 kV feeders and 5-8.32 kV feeders within its service territory.

3. In Closing

In Closing

Due Diligence

As part of the proposed transaction, the merging entities undertook a due diligence review to assess among other things certain legal, financial, environmental and operational aspects prior to obtaining Board, Shareholder and Regulatory approval

No issues identified during the Due Diligence Review would prevent the proposed Transaction from proceeding

Use of Third Party Subject Matter Experts

Legal

- Gowlings WLG (Canada) LLP

Financial

- Deloitte performed financial and tax due diligence through review of financial statements, accounting records and tax filings on Guelph Hydro

Asset Management

- Vanry + Associates performed a review of the asset condition assessments and capital investment planning process to determine the health of the electrical distribution assets of Guelph Hydro

Reviewed and Recommended

On November 30th, Alectra Inc.'s Board of Directors – approved the Guelph Hydro – Alectra transaction

Executive Summary

Resolution of the Municipality

Re: Project Mercury

WHEREAS □, the Municipality's subsidiary (the "Subsidiary") and the Corporation of the City of □ (the "Municipality") are parties to the Unanimous Shareholders Agreement for Alectra Inc. ("Alectra") dated January 31, 2017 (the "Current Alectra Shareholder Agreement").

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2. The Mayor and City Clerk of the Municipality are hereby authorized and directed to execute and deliver the New Alectra Shareholder Agreement in accordance with the foregoing resolutions; and
3. The Mayor and City Clerk of the Municipality are hereby authorized and directed to sign and/or dispatch and deliver all other documents, notices, articles, certificates to be signed and/or dispatched or delivered under or in connection with the New Alectra Shareholder Agreement or to take any action deemed necessary in respect of any of the foregoing.