<u>Summary of Shareholder Rights and Directors' Obligations under OBCA After IPO</u>

By owning shares in a corporation, a shareholder owns an interest in the assets of the corporation, and may have a voice in how the corporation operates. The rights of share ownership differ depending on the types of shares that the shareholder owns and the terms of any shareholders' agreement that may exist.

Currently, as the sole shareholder of Hydro One Inc., the Minister can exercise immediate and direct authority over Hydro One through unanimous shareholder agreements (OBCA s. 108, OBCA s.115 fiduciary duty limited by Unanimous Shareholder Agreement).

Shareholder and Directors Rights After IPO of Hydro One Inc.

After the Initial Public Offering (IPO), the Minister will no longer have the rights of a sole shareholder, and will not have the tool of a unanimous shareholder agreement available. Theoretically, Government could work with all other shareholder groups to reach an agreement. (OBCA 108(1), 108(2)). However, the exercise is no longer as direct or immediate and will likely involve negotiations, concessions and hard-bargaining.

After the IPO, however, the Minister will still have the general rights of a shareholder under the OBCA, as modified by the Governance Agreement and the proposed legislation**.**

Shareholder's rights under the OBCA include:

<u>Voting Rights</u>:

- Shareholders who hold voting shares have the right to be informed of and to vote at meetings of shareholders called by the directors.
- Annual General Meeting (AGM): shareholders with voting shares can vote at the AGM (elect directors, approve current financials and appoint auditor for corporation).
- Preference shares may entitle shareholders to receive dividends, but may or may not allow them to vote.
- Normally shares include one vote per share.

<u>Other Rights</u>

In the event that a shareholder determines the conduct of the corporation has prejudiced them unfairly, a shareholder has certain remedies available under the OBCA including**:**

Oppression Remedy

- Shareholders may seek relief in court if there has been corporate conduct that is "oppressive or unfairly prejudicial to, or that unfairly disregards the interests of any shareholder (or director or creditor of the corporation)."

Derivative Action

- Shareholders may bring a derivative action where the directors will not authorize the corporation to participate in a lawsuit, the shareholders are acting in good faith, and it appears to be in the corporation's best interests to bring or defend the lawsuit.

Appointment of Inspector

- Shareholders may bring an application to court for the appointment of an inspector, if they can show that there has been serious mismanagement by directors or officers.

Appraisal Remedy

- Shareholders can apply for a court order requiring the corporation to buy the shareholder's shares if any of the following fundamental changes occur:
  - Change in any restrictions on the issue, transfer or ownership of shares
  - Change in any restrictions on the type of business the corporation may carry on
  - Corporation amalgamating or merging with another corporation
  - Corporation being continued under the laws of another jurisdiction (note this is currently prohibited in the case of Hydro One under the proposed legislation)
  - Selling leasing or exchanging substantially all of the corporation's assets (note this is currently prohibited in the case of Hydro One's transmission and distribution businesses under the proposed legislation)

Publicly traded corporations (including Hydro One, post IPO) are also subject to requirements for disclosure in management circulars (including information about senior management, such as share ownership, any indebtedness to the company and any interest in material transactions) as well as compensation circulars (executive compensation disclosures including shares awarded, perks and incentives; as well as compensation objectives, benchmarks and targets).

Changes to Shareholder Rights through Governance Agreement (Province's ownership interest between 85% and 40%)

As of the IPO, there will be a governance agreement between the Corporation and the Province which sets out additional requirements, which may change depending on the circumstances and the Province's ownership in the corporation. Please see the attached chart entitled "Rights of the Province Affected by Changes in Ownership".

So long as the Province holds at least 40% of the shares of Hydro one, it will be entitled to nominate 40% of the directors to be included in the management slate. Other than the CEO who will be a director, all other nominees must be acceptable to the Province acting reasonably. The Province's Board nominees would be sufficient to block the appointment of the Chair or CEO of the corporation and to block any proposed change to the Corporation's governance standards.

In the usual course, where a Board election is uncontested, the Province will vote for the management slate of directors. Should the Province disagree with a proposed management slate, it can vote against all of the directors (other than the CEO, or at its option the Chair), but cannot vote against individual directors on the slate. Should the Province reject a slate of directors, it will be entitled to nominate 40% of the new proposed slate, the CEO will be on the slate, and the balance will be nominated by a shareholder committee.

In the event of a contested board election, the Province would be entitled to vote how it wishes for individual directors, and would have sufficient votes to elect the Board so long as its ownership remained greater than 50%.

<u>Additional Shareholder Rights/Restrictions in the Governance Agreement</u>

Rights of Province Unaffected by Changes in Ownership

- Province will identify the initial members of the Board, the initial Chair and the initial CEO.
- Province will approve the initial governance standards of the Company. According to the term sheet for the Governance Agreement, certain aspects of the Government's shareholder rights would be modified (see attached Chart under the heading "Restrictions while Province holds more than 10%", rights granted to shareholders pursuant to the OBCA would be restricted. In accordance with the term sheet, the province would not exercise its right to requisition a shareholder meeting and to vote its shares on fundamental changes to the Company (e.g., amendment to articles, amalgamation, continuance, arrangement etc.).

Restrictions on Board Nominees Unaffected by Changes in Province's Ownership

- All nominees to the Board must be approved by the Nominating and Governance Committee, except in the circumstance where the Board is being reconstituted after Province has successfully voted for the removal of all directors.
- All nominees to the Board should be high-quality, reputable business leaders with the requisite skills, (including integrity, expert knowledge, finance, industry or other relevant experience), board experience, time and motivation for an

operation of the Company's size and scope, and having regard to the Company's core operating principles.
- The majority of the Board at all times must be composed of Canadians.

Restrictions while Province holds more than 10%

- The CEO will be on the Board.
- Nominees to the Board cannot be current officials or employees of Province subject to an exception related to the directors on the current, pre-IPO Board which the Government decides to appoint.
- Nominees to the Board cannot be former officials or employees of Province unless such nominee has not been an official or employee of Province for at least three years prior to the date of their nomination to the Board.
- Each nominee to the Board will be "independent" of Province (independence will be determined pursuant to Ontario securities laws, including any regulatory instrument promulgated by the Ontario Securities Commission ("OSC")).
- The Nominating and Governance Committee must satisfy itself that each nominee will exercise his or her judgment independent of Province.
- Province will not requisition a meeting of shareholders to initiate any fundamental change described in Part XIV of the OBCA (e.g., amendment to articles, amalgamation, continuance, arrangement etc.).
- Each nominee to the Board must receive a majority (50% +1 vote) of the votes cast with respect to his or her election other than at contested meetings.
- Upon a Board vacancy, Province can nominate replacements for directors Province nominated.

Changes to Legislation Which Affect Shareholder Rights

OBCA Shareholders are normally able to purchase and sell shares without restrictions in general. The new legislation would limit this ability to not more than 10% of shares of post IPO Hydro One.
- Government would be required not to take steps which reduce its share position to less than 40%.
- Government would be limited to the "10%-threshold" if its ownership interests reach or drop below 10%.
- Between 11% and 39%, Government could buy back to re-attain 40%.

Other Statutory Restrictions
- The Company cannot sell substantially all of the transmission or distribution business regulated by the OEB.
- The Company's jurisdiction of incorporation may not change from Ontario.
- The Company must maintain its executive head office in Ontario.
- The CEO and substantially all the officers with strategic decision-making or management authority must work and reside in Ontario

- o Province and Auditor General have rights to gain access to records to permit the preparation and auditing of Province's financial statements.

Directors Duties Under OBCA

- The HONI board of directors have a <u>fiduciary duty</u> to the corporation (134(1)), and must act in the best interests of the corporation. Directors must at all times act independently of the interests of shareholders, and owe their primary fiduciary responsibility to the Corporation
    - ▪ S.134(1) reads as follows (1) "Every director and officer of a corporation in exercising his or her powers and discharging his or her duties to the corporation shall,
        - (a) act honestly and in good faith with a view to the best interests of the corporation; and
        - (b) exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances.

- o The effect of this is that the board may make decisions related to Hydro One that will be ll be other than what Government would want;

- Directors must declare when they are in, or perceive that they are likely to be in, a position of conflict on a matter brought or to be brought before the board of directors for approval. In these instances, directors will normally be expected to recuse (absent) themselves from voting on an item with which they are in conflict.