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M E M O R A N D U M

TO: Cheryl Carson, Legal Services Branch, Ministry of Energy, Ministry of Economic Development, Employment and Infrastructure, and Ministry of Research and Innnovation

FROM: Crown Law Office – Civil

DATE: April 7, 2015

RE: Applicability of the Procurement Directive on the Divesture of Hydro One Brampton Networks Inc.

I. INTRODUCTION

We are responding to your request received on April 5, 2015 for urgent advice in relation to the applicability of the Ontario Public Service Procurement Directive issued by Management Board of Cabinet on December 2014 (the "Directive") on the Transaction, as defined below.

II. BACKGROUND

Her Majesty the Queen in right of Ontario, as represented by the Minister of Energy (the "Shareholder") is a registered holder of all of the issued shares of Hydro One Inc. (the "Corporation"). The Corporation is the sole shareholder of Hydro One Brampton Networks Inc. (the "Subsidiary").

On December 12, 2014, a press release, attached as Appendix A, was issued by the Shareholder encouraging ideas related to the consolidation of the Subsidiary and the distribution business within Hydro One Networks. In response to such release, three distribution companies (collectively, the "Distribution Companies") approached the Premier's Advisory Council on Government Assets. They have made an offer to purchase the Subsidiary and necessary steps are being taken to affect the divestment of the Subsidiary (the "Transaction").

III. ISSUES

1. Is the Corporation subject to the Directive?

2. Is the Transaction subject to the Directive?

IV. CONCLUSION

1. Yes, the Corporation is subject to the Directive. The Corporation is designated as an "Other Included Entity" for purposes of the Directive.

2. No, the Transaction is not subject to the Directive.

V. ANALYSIS

1. Is the Corporation subject to the Directive?

Under Section 3(1) of the *Management Board of Cabinet Act* (Ontario) (the "MBC Act"), the Management Board of Cabinet has a number of powers and duties including policy and directive making authority over the "public service". The term "public service" is defined in Section 1(1) of the MBC Act to include "every corporation, with or without share capital, that is not a Crown agency but is owned, operated or controlled by the Crown, …". Such definition would capture the Corporation. However, each directive has an application and scope section which further sets out which entities are captured by such directive.

The Directive provides that it applies to all Ministries and, in part, to Other Included Entities. The term "Ministries" is defined to include "all ministries, Clusters,[1] advisory, adjudicative and regulatory agencies and any other agency, as classified under the Agency Establishment and Accountability Directive, that is required by a Memorandum of Understanding to comply with the [Directive] or its predecessors in its entirety". The Corporation is a non-Crown agent,[2] share capital corporation established under the *Business Corporations Act* (Ontario) [3](the "OBCA") with its mandate and duties stated under the *Electricity Act, 1998* (Ontario). The Corporation is not classified under the Agency Establishment and Accountability Directive. Accordingly, the Corporation is not within the definition of "Ministries" for purposes of the Directive.

The term "Other Included Entity" is defined to include "…non-classified entities where the Chair and/or Chief Executive Officer is directly or indirectly appointed by Ontario" and such entities must not be required by a memorandum of understanding to comply with the Directive in its entirety unless approval from the Management Board of Cabinet (the "MBC") has been received for such entity to be treated as an Other Included Entity.

Under the OBCA,[4] the Minister of Energy, as the sole shareholder, appoints the board of directors, including the chair.[5] Pursuant to the memorandum of understanding between the

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[1] The term "Cluster" is defined in the Directive as "Information and Information Technology clusters as defined by the Information and Information Technology Strategy 1998".

[2] See Section 48(2) of the *Electricity Act, 1998* (Ontario).

[3] See Section 1(2) of the *Electricity Act, 1998* (Ontario).

[4] See Section 119(4) of the OBCA.

Shareholder and the Corporation with an effective date of March 25, 2015 (the "MOU"), the MOU requires the Corporation to comply with the Directive. However, on July 16, 2009, MBC designated the Corporation as an "Other Included Entity" for purposes of the Directive.[6]

Based on the above, the Directive should apply to the Corporation and the Corporation should be an "Other Included Entity" for purposes of the Directive.

2. Is the Transaction subject to the Directive?

The purpose of the Directive is to ensure that goods and services (including, construction, consulting services, and information technology) are acquired through a process that is fair, open, transparent, geographically neutral and accessible to qualified vendors. The Directive provides that the overall objective is to ensure that Ministries and Other Included Entities acquire goods and services required to meet government needs in the most economical and efficient manner, through procurement processes that conform to the following principles: (a) value for money; (b) vendor access, transparency, and fairness; (c) responsible management; and (d) geographic neutrality and reciprocal non-discrimination. Where the entity is within the definition of "Other Included Entity" for purposes of the Directive, Sections 3 and 8 of the Directive apply. In general, such sections allow the entity to establish and follow its own procurement policy and related processes and procedures while ensuring that such policies, processes, and procedures adhere to the abovementioned procurement principles. (We note that Section 7.14 of the Directive addresses the disposition of government-owned computers and all other assets and consumable supplies except motor vehicles. However, as the Corporation is an Other Included Entity, Section 7.14 is inapplicable.)

For the Directive to apply to the Transaction, the Transaction must fit within the definition of "procurement". The Directive defines the term "procurement" as (a) "any contractual or commercial arrangement involving the acquisition of a good or service through purchase, rental, lease or conditional sale;" or (b) "where a value or benefit has been conferred by the Crown to a successful vendor in exchange for good(s) or service(s) or revenue to the Crown".

With respect to part (a) of the definition of "procurement", the Transaction does not involve the acquisition of a good or service through purchase, rental, lease or conditional sale. The Transaction is a divestment, rather than an acquisition. Accordingly, part (a) of the definition of "procurement" does not apply to the Transaction.

In interpreting part (b) of the definition of "procurement" in the context of the purpose of the Directive and Sections 3 and 8 of the Directive, part (b) captures situations where the Crown engages, for example, a software developer to develop a software program in conjunction with the Crown for a fraction of the price. The software developer is then permitted to use the know-how obtained during such development to develop other software for other parties. Furthermore, as required under part (b) of the definition of "procurement", value or benefit must be conferred by the Crown to the successful vendor. The term "vendor" is not defined in the Directive;

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[5] LSB Energy confirmed that Minister of Energy appoints the chair of the Corporation.

[6] LSB Energy confirmed that the designation of the Corporation by MBC as an "Other Included Entity" has not been, to their and their policy client's knowledge, revoked.

however, the general use of the term denotes “seller”. In the present case, the Distribution Companies are not the vendors in the Transaction, but rather they are purchasers in the Transaction. Accordingly, as the Transaction involves the divestment of assets by the Corporation, part (b) of the definition of “procurement” does not apply to the Transaction.

Based on the above, the Directive does not apply to the Transaction.

Please note that pursuant to Section 1.0.5(1) of the *Financial Administration Act* (Ontario), Treasury Board has, in general, the powers and duties to review, evaluate and approve any financial matter that affects the Crown including, but not limited to, the disposition of assets of the Crown. Accordingly, the potential divesture of the Subsidiary would require the approval of Treasury Board. We note that a submission to Treasury Board does not give rise to a basis for challenge by a third party.

As well, we note that the Minister of Economic Development, Employment and Infrastructure’s mandate, pursuant to Section 7(1) of the *Ministry of Infrastructure Act, 2011* (Ontario), is to review matters related to infrastructure and public works. We further note that we have been advised that the Minister of Economic Development, Employment and Infrastructure is aware of the Transaction.

We trust you will find the foregoing of assistance.

Crown Law Office - Civil

Per: Leila Dabir, Counsel

In consultation with Cheryl Carson and James Rehob (ENE, MEDEI, MRI LSB) and Tom Lo and Katharine Tabscott (TBS LSB)

Encl.

Appendix A

Premier's Advisory Council on Government Assets Inviting Ideas for Hydro One Electricity Distribution Assets

Council Moving Ahead with Phase Two

TORONTO, Dec. 12, 2014 /CNW/- The Premier's Advisory Council on Government Assets is now moving forward with its work to encourage consolidation in the province's electricity distribution sector for the benefit of ratepayers, while maximizing value to taxpayers.

As part of this process, the Council is now interested in receiving written ideas related to encouraging consolidation and Hydro One Brampton and the distribution business within Hydro One Networks.

As identified in its initial report, Hydro One Brampton and the electricity distribution business currently integrated within Hydro One Networks are two critical assets that could be used to encourage additional consolidation within the Province's electricity distribution industry and help support the government's infrastructure priorities while protecting ratepayer interests.

Alan Hibben, a retired senior investment banker from RBC Capital Markets, has volunteered to work with the Chair and the other members of the Council in receiving and discussing proposals, which will help the Council finalize its recommendations to the government for consideration in the 2015 Budget process and on the procurement process.

Interested parties are encouraged to contact Mr. Hibben at Alan.Hibben@ontario.ca to obtain more information and to provide an expression of interest.

Background:

- On April 11, 2014, Premier Kathleen Wynne appointed a council to review and identify opportunities to modernize the Liquor Control Board of Ontario, Hydro One and Ontario Power Generation and to recommend ways to maximize their value to the people of Ontario.
- On November 13, 2014, the Premier's Advisory Council on Government Assets released its Initial Report, *Retain and Gain: Making Ontario's Assets Work Better for Taxpayers and Consumers.* In its report, the Council took into account the government's preference to retain core assets in public ownership and in maximizing the value to the taxpayers.
- In considering Hydro One, the Council has recognized that any proposal should focus on the dual objectives of encouraging further consolidation in the Province for the benefit of electricity ratepayers and using private capital rather than taxpayer funds to accelerate that process, without reducing the value to the Province of its distribution business, and without compromising the best outcome for taxpayers.
- The Council also recommended diluting the interest of the Province in these two assets to allow taxpayers to realize the value of its assets, and to help support the government's infrastructure priorities outlined in the Ontario 2014 Budget.

SOURCE Premier's Advisory Council on Government Assets

For further information: Diane McArthur, Executive Lead, Advisory Council on Government Assets, Email: diane.mcarthur@ontario.ca