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**DELIVERED BY EMAIL**

Mr. Dan Chapman  
City of Kitchener  
200 King Street West  
Kitchener, ON N2G 4G7

Dear Mr. Chapman

**Re: Amalgamation of Kitchener Power Corp. and Waterloo North Hydro Holding Corporation**

The City of Kitchener (the “**City**”) retained Borden Ladner Gervais LLP (“**BLG**”) to provide legal advice with respect to a proposed merger between Kitchener Power Corp. (“**KPC**”) and Waterloo North Hydro Holding Corporation (“**WNHHC**”) (the “**Proposed Transaction**” or “**New Holdco**”). Specifically, New HoldCo will own 100% of the issued and outstanding shares of the newly amalgamated electricity local distribution company (“**New LDC**”), which will be regulated and licensed by the Ontario Energy Board (the “**OEB**”), along with other existing subsidiary corporations.

**Due Diligence Report**

As part of BLG’s mandate, the City instructed us to carry out legal due diligence as more particularly described in Section IV of our due diligence report. Extensive legal due diligence was undertaken and our due diligence report was delivered to the City on August 9, 2021. Since the due diligence report is a confidential document which is subject to solicitor-client privilege, this letter has been prepared at the City’s request to provide a public summary of the relevant legal documents based, in part, on our due diligence.

**Amalgamation Related Legal Agreements**

The proposed mergers constitute legally binding commercial transactions. Two legal agreements have been developed and negotiated over the past several months that prescribe and chart the future relationship between the various municipal shareholders and the proposed merged companies. These agreements are known as the Merger Participation Agreement and the Unanimous Shareholders’ Agreement. BLG provided advice to the City on both Agreements.

## **The Merger Participation Agreement**

The Merger Participation Agreement (the “MPA”) is the agreement that describes key elements of the amalgamation mechanics and the rights and responsibilities of the municipal shareholders and the companies pertaining to the implementation of the mergers. Among other things, the MPA sets out the equity ownership between the five municipal shareholders at the New Holdco company level as follows:

Kitchener	53.39%
Wilmot	4.49%
Waterloo	30.83%
Woolwich	8.51%
Wellesley	2.78%

A number of months will pass after all the municipal councils approve the legal agreements and before the mergers actually close. For example, Ontario Energy Board approval is required before the distribution company mergers can take place and this regulatory process will take several months. Accordingly, the financial position of each of the companies involved in the transactions will change over this period. To manage these typical financial fluctuations the MPA includes price adjustment mechanisms to ensure that these changes are accounted for. The net result will be an additional dividend payment to the Kitchener-Wilmot municipalities or to the Waterloo et al municipalities depending on the net gain or loss arising from these adjustments. The payment will be made through a special share class dividend. Note that these closing adjustments are typical for utility mergers of this type and will have no impact on the equity allocations set out above.

The MPA also sets out the representations, warranties and covenants of the parties addressing issues such as confirming the municipal ownership of shares in the existing companies, the absence of undisclosed liabilities, compliance with laws, statements about environmental conditions of the businesses, disclosure of material contacts, carrying on business in the normal course and other typical and traditional vendor representations and covenants.

The location of the head office and executive functions is also mandated in the MPA. This includes the requirement that the new merged holding company and distribution company maintain its administration and operations buildings, including executive functions, at 301 Victoria Street South, Kitchener. This location will be for an indefinite period and can only be changed with Kitchener’s approval.

Under the MPA, the signatories agree to indemnify each other against violations of promises made such as representations, warranties and covenants. The maximum exposure has been capped at \$15 million (pro-rated to reflect the ownership level of each municipality) which can only be triggered if a claims threshold of \$250,000 has been met.

As directed by Kitchener Council, the MPA also includes a section on regulatory approvals that mandates that the Ontario Energy Board will be asked to approve, as a separate and distinct head of relief sought, that legacy distribution rate classes be maintained for a minimum period of 20 years

after closing to ensure that Kitchener's electricity distribution rates are comparable to status quo rates if no merger had occurred.

Finally, Kitchener and Wilmot's tree reforestation grants program will continue post-merger consistent with past practice. Kitchener Council also will be consulted with respect to the new merged company name.

The MPA will be executed after this agreement has been approved by all municipal shareholders. Thereafter the MPA will be filed with the Ontario Energy Board as part of the supporting evidence for the New LDC and New Holdco mergers.

### **The Unanimous Shareholder's Agreement**

Where the MPA focuses largely on merger implementation, the Unanimous Shareholder's Agreement (the "USA") sets out the relationship between the municipal owners and the new companies. The USA includes various corporate governance requirements including the composition of the new 13 member parent holding company board (7 directors to be appointed by Kitchener with a minimum of 4 independent Kitchener directors) and the new 9 member distribution utility company board (2 directors to be appointed by Kitchener both of whom may be non-independent). The majority of the New LDC board will be comprised of independent directors.

Under Ontario law, shareholders can remove certain decision-making powers from the board of directors in order for the municipal councils to decide these matters. Special Majority Shareholder Approval (66 2/3) will be required for changes such as new auditors, buying or selling assets or other transactions with an economic value greater than 10% of the consolidated book value of parent holding company and its subsidiaries. Super Majority Shareholder Approval (90%) will be required for any action that would dilute a shareholder's ownership percentage, changing the debt/equity rate beyond certain levels and changing the geographic extent of the distributors operations.

The USA also includes various rights and duties with respect to conveyance of a municipalities interests in the company including pre-emptive rights for new share offerings, a right of first refusal if another shareholder receives an offer on their shares, piggy back rights to allow other shareholders to require their shares to be acquired as part of an offer to another shareholder, drag along rights and options with respect to the sale of surplus assets.

The USA also contains a non-competition clause designed to allow the municipalities to continue to own and operate separate existing businesses (such as Kitchener's natural gas franchise) and other designated activities on municipal owned sites (such as district energy and solar panels ) within the municipality. The newly merged companies agree not to pursue a current designated business activity within a municipal shareholder's borders without first obtaining that municipality's written consent. Prior to a municipality undertaking a new energy-related venture within its borders, that municipality agrees to explore, on a good faith basis, possible collaboration on such ventures with the appropriate merged utility company.

Finally, the USA includes a dividend policy including target dividend payments for the first three financial years of the new companies' existence, including a target dividend of 50% payout of the net operating income of the merged companies.

### **Ontario Energy Board Approval**

If all municipal shareholders of KPC and WHNHC approve the MPA and USA, an application must be made to the Ontario Energy Board to approve the merger of the Kitchener-Wilmot and Waterloo electricity distribution companies. This approval is required before the New LDC amalgamation can be completed. The Ontario Energy Board filing is known as a MAADs application (MAAD stands for Mergers, Amalgamations, Acquisitions and Divestitures).

In deciding whether to approve the merger of the two electricity distribution companies, the Board applies what is known as the "no harm" test. This test is articulated in the OEBs *Handbook to Electricity Distributor and Transmitter Consolidation* and associated MAADs Filing Requirements issued January 19, 2016. This Handbook is intended to provide guidance to applicants and stakeholders on MAADs applications. In order to demonstrate "no harm", the distributor applicants must show that there is a reasonable expectation based on underlying cost structures that the costs to serve customers following a consolidation will be no higher than they otherwise would have been. In other words, customers cannot be made worse off than compared with the status quo (i.e. if no merger would have taken place). It is anticipated that the OEB regulatory process will take approximately 6 months to complete.

If the OEB approves the merger, then the amalgamation transactions will close, generally within 60 days from the date of such approval. At closing, Articles of Amalgamation will be filed with the Province to create the new companies that shall bring the new corporations into effect.

Yours Very Truly,

**Borden Ladner Gervais LLP**

*original signed by Mark Rodger*

J.Mark Rodger\*

\*Jonathan Rodger Professional Corporation