CITY OF MISSISSAUGA JUDICIAL INQUIRY

Phase I: Written Submissions

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1. What was the context in which the City entered into a Shareholders Agreement with OMERS/Borealis?

The context in which the City entered into a Shareholders Agreement with OMERS/Borealis was a transaction being negotiated as a result of Ontario's deregulation of the electricity sector.

Legislative changes recommended by the Macdonald Report and introduced in the *Electricity Act, 1998*[1] gave Ontario's municipalities ownership of their municipal electrical utilities ("MEUs") and required them to transform their MEUs from local Boards to corporations incorporated pursuant to the *Business Corporations Act (Ontario)*, R.S.O. 1990, c. B. 16. It was under this mandatory legislative framework that the City incorporated Hydro Mississauga Corporation ("HMC") and transferred to it the majority of the assets of the former Mississauga Hydro Electric Commission.[2]

The City hired TD Securities and Fraser Milner to advise it with respect to the restructuring process. Based on the recommendations of TD Securities, the City made a voluntary decision to monetize HMC first by recapitalizing it to be held by the City as 60% debt / 40% equity and second through a sale that proceeded by way of an RFP process.[3] Borealis/OMERS was the successful party in the RFP process.

2. Was the City adequately aware of the nature of the deal with OMERS from the outset?

It is important to note that the idea of a negative veto was first introduced by OMERS/Borealis near the outset of the deal, but was subsequently rejected by the City.[4] More particularly, the negative veto was proposed in Mr. McGrath's March 7, 2000 correspondence to Mr. Toll, but ultimately rejected in the Strategic Alliance Agreement presented to the City on March 29, 2000. In other words, the negative veto formed no part of the materials provided to City Council on March 29, 2000. There is, in fact, no record of the negative veto ever being brought to the attention of City Council prior to the closing of the deal on December 6, 2000.

City Council was aware of the deal with OMERS/Borealis that was presented at the March 29, 2000 City Council meeting. At that meeting, the Mayor and members of City Council were provided with a copy of

the Strategic Alliance Agreement and attachments thereto along with TD Securities' presentation.[5] In advance of this meeting, details of the deal with OMERS/Borealis were provided to City Council in David O'Brien's March 25, 2000 in-camera corporate report. Both Mr. O'Brien's report and the TD Securities presentation recommended that the City select the OMERS/Borealis proposal as the winning bidder in the RFP process.[6]

City Council was also aware of the parameters of the deal as set out in the final transaction documents that were before them and that they approved by enacting by-law 0600-2000 at the November 29, 2000 meeting of City Council.[7]

Although it is fair to conclude that the City was adequately informed of the deal that was presented to it, City Council was not informed about the insertion of the negative veto into the final version of the Shareholders Agreement with OMERS/Borealis. The negative veto was not part of the Agreement presented to, and approved by, City Council.

3. Was an appropriate level of negotiation authority delegated to David O'Brien?

It is impractical for the Mayor and Members of City Council to negotiate directly with OMERS/Borealis as to the details of such a complex transaction. Following its customary practice and consistent with general municipal practice, the City delegated negotiation authority to senior staff, in this case the City Manager.

Pursuant to Resolution 0091-2000 enacted by City Council at its March 29, 2000 meeting, Mr. O'Brien, with the assistance of the City's external consultants TD Securities and Fraser Milner, was provided with authority to negotiate a final agreement with Borealis/OMERS, subject to bringing any changes to the documents approved by City Council in April 2000 back to City Council for its ratification.[8]

At the time authority was delegated to Mr. O'Brien, there was no contemplation that he would be seconded to Enersource before the agreements, including the Enersource Shareholders Agreement, were finalized.

After Mr. O'Brien was seconded to Enersource on November 27, 2000, he continued to be involved in and maintained responsibility for certain aspects of City business, including the negotiation of the agreements with Borealis respecting Enersource.[9] Because of this, after his secondment, Mr. O'Brien still had an obligation to act in the best interests of the City, while at the same time, he had an obligation to act in the best interests of Enersource. Those obligations were not entirely convergent.

Enersource is an *OBCA* corporation with two shareholders and operates to generate profit for its shareholders. The City is a municipality that is motivated by an entirely different set of objectives – its primary objective is operate in the best interests of the residents of the Mississauga, not for return on investment.

As the new President and C.E.O. of Enersource, Mr. O'Brien focused on getting the transaction completed as quickly as possible before the transfer tax exemption expired on December 31, 2000. This is consistent with the City's objectives. As the only staff person of the City with full knowledge of all aspects of the deal between the City and Borealis/OMERS, he should have also been focusing on ensuring that the agreements ensured that the City, being the 90% shareholder, had its interests fully protected.

The agreements entered into provided significant benefits to Borealis/OMERS, well in excess of those normally enjoyed by a 10% shareholder.[10] There may have been proper business reasons for this however, when these changes appeared at the very last second, it raises issues about their propriety. City Council should have been provided with a proper briefing concerning all of the last minute changes to the deal, including the changes that added negative veto, and should have held a formal Council meeting to decide whether or not to approve them.

Although it is fair to conclude that Mr. O'Brien was provided with an appropriate and customary level of negotiation authority, Mr. O'Brien exceeded this authority by failing to bring back to City Council for its ratification important changes that were made to the final agreement with Borealis/OMERS, including the changes that added the negative veto. Wearing the two hats that he was, as City Manager and as President and C.E.O. of Enersource, Mr. O'Brien's judgment may have been clouded. Focused as he was on closing the deal and getting the new Enersource Corporation up and running in accordance with the objective of the Strategic Alliance Agreement, his obligation to the City and City Council to have the final agreement ratified by City Council was not met.

City Council at all times reserved its authority to approve and authorize the agreements related to this transaction, including the Shareholders Agreement. City Council exercised that authority on November 29, 2000 but was not given a further opportunity by Mr. O'Brien thereafter, despite the material change of adding the negative veto to the agreement.

4. Was it appropriate for Dave O'Brien to continue to give instructions after he was seconded to Enersource on November 27, 2000?

No. For the reasons discussed in #3 above, it would have been appropriate for the City to have in place a successor for Mr. O'Brien, who was knowledgeable with all aspects of the City's deal with Borealis/OMERS and who could have acted for the City in lieu of Mr. O'Brien after he was seconded to Enersource. Mr. O'Brien was conflicted in acting in both of these roles, and his judgement respecting what was in the best interests of the City may have been clouded by his desire, as C.E.O. and President of Enersource, to ensure that the Enersource transaction was completed.

In the course of the Inquiry, little attention was paid to the issue of secondment and the process for making a secondment, however where applicable we have made comments in the recommendations section in #13c below.

5. Was Bill Houston authorized to take instructions regarding changes to the Shareholders Agreement from Dave O'Brien?

Yes. Mr. Houston was authorized to take instructions from Mr. O'Brien on all issues regarding changes to the documents for the transaction with OMERS/Borealis including the changes to the Shareholders Agreement. Mr. O'Brien's testimony and Mr. Houston's testimony support this conclusion.[11]

6. Did the Mayor know that s. 2.15(t)(i) of the Shareholders Agreement had been amended to include the phrase "and a nominee of Borealis is among those directors approving" prior to its execution on December 6, 2000?

No. The Mayor did not know that s.2.15(t)(i) of the Shareholders Agreement had been amended to include the phrase "and a nominee of Borealis is among those directors approving" prior to its execution on December 6, 2000.

The Mayor testified that she was not made aware of this change until the fall of 2007 when the City and OMERS/Borealis were engaged in a dispute over compensation for Enersource's directors.[12] Though Mr. O'Brien testified that he thought he had made the Mayor aware of this change, he was unable to pinpoint exactly where and when this had done so, and his answers on this issue were unclear, contingent and in some cases nonsensical.[13]

7. Did City Council know that s. 2.15(t)(i) of the Shareholders Agreement had been amended to include the phrase "and a nominee of Borealis is among those directors approving" prior it its execution on December 6, 2000?

No. See answer to #6 above.

While Councillor Mahoney testified that she recalled being advised by Mr. O'Brien on these changes in an informal briefing session held in the caucus room prior to the closing on December 6, 2000, she could not recall specifics of this briefing session including exactly when it took place, who was present (although she was positive that the Mayor was not present and that Mr. O'Brien and the acting City Manager Angus McDonald were present)[14], nor could she substantiate her recollection with any

documentary evidence.[15] The formal records of the City as maintained by the Clerk's office do not support that such a meeting took place.[16] Also, her recollection in this regard is challenged by the sworn evidence of five of the other City Councillors in office at the time – all who say that they recall no such briefing taking place.[17]

In any event, Councillor Mahoney agreed that the City could not undertake formal decision making in an informal briefing session and no formal Council action to ratify the changes ever occurred.[18] The *Municipal Act*, R.S.O. 1990, which was law at the time, did not authorize, in any way, informal briefing sessions and the Council Procedural By-law No.272-92 at that time was consistent with the legislation. The Procedure By-law does provide for the calling of special meetings of Council to deal with matters on 48 hours notice, and it would have been possible to call a special meeting to ask Council to approve the changes to the Shareholders Agreement.[19] Also, while it was important to all parties that the agreements be executed before December 31, 2000 transfer tax exemption deadline, had the City Manager requested an extension of time for a few days to obtain Council's approval for the changes made on December 4th, that request would have been accommodated by Borealis.[20]

8. Should the Mayor and/or Council have been advised that s. 2.15(t)(i) of the Shareholders Agreement had been amended to include the phrase "and a nominee of Borealis is among those directors approving"?

Yes. The changes made to s. 2.15(t)(i) of the Shareholders Agreement were a material change to the structure of the deal between the City and OMERS/Borealis. Resolution 0091-2000 enacted by City Council at its March 29, 2000 meeting required that this change (along with the other material changes to the Shareholders Agreement that were made following the November 29, 2000 City Council meeting), to be brought back for ratification by the Mayor and City Council.[21]

Jeffrey Singer (the City's current external counsel who conducted a 2007 investigation into the circumstances surrounding the insertion of the negative veto) testified that as this change was a material change to the Shareholders' Agreement, the Mayor and Council should have been advised of it by Mr.

Houston - whose role was to make sure that his client (City Council) fully understood the agreement and any proposed material changes to the agreement.[22]

9. Whose responsibility was it to ensure that the Mayor and/or Council knew that s. 2.15(t)(i) of the Shareholders Agreement had been amended to include the phrase "and a nominee of Borealis is among those directors approving"?

Both Mr. O'Brien and Mr. Houston were responsible for bringing to the City's attention the changes that were made to section s. 2.15(t)(i), as well as the other last minute changes that were made to the Shareholders Agreement (i.e. changes to the directors' compensation and quorum requirement) after the final documents were presented to City Council at its November 29, 2000 meeting. Although Mr. O'Brien testified that he held the ultimate responsibility for doing so, he also testified that he relied on Mr. Houston to advise him of the legal consequences of any changes being made.[23] As the City's external counsel responsible for the transaction, Mr. Houston should have explained to Mr. O'Brien the significance of these changes.

It is likely that neither Mr. Houston nor Mr. O'Brien fully understood the impact of the changes made to section 2.15(t)(i) of the Shareholders Agreement. The lack of any correspondence on this issue between the time the change was made and the closing justifies this conclusion. Moreover, as noted in #2 above, both Mr. Houston and Mr. O'Brien, as the City's representatives, were aware that the negative veto was proposed in Mr. McGrath's March 7, 2000 correspondence to Mr. Toll, but ultimately rejected in the Strategic Alliance Agreement presented to the City on March 29, 2000. Notwithstanding this knowledge, when the negative veto was re-introduced into the Shareholders Agreement by OMERS/Borealis on December 3-4, 2000, neither Mr. Houston nor Mr. O'Brien took proper or adequate steps to ensure that City Council was made aware of this change and given the opportunity to ratify or reject the revised agreement as it was entitled to do.

It is likely that even after the closing, Mr. Houston was not fully aware nor did he understand the impact of these changes. The fact that the December 19, 2000 "Brief for Directors" that he prepared for the directors of Enersource Corporation, does not mention the negative veto justifies this conclusion.[24]

10. Did Borealis/OMERS act properly throughout the transaction?

There appears to have been no impropriety on the part of Borealis/OMERS concerning the sequence of events leading to changes made to section 2.15(t)(i) of the Shareholders Agreement on December 3, 2000.

Mr. Lever, counsel to OMERS/Borealis, communicated directly with Mr. Houston, outside counsel to the City, generally with respect to the ongoing negotiations relating the Shareholders Agreement and, in particular, with respect to the insertion of the negative veto on December 4, 2000. As noted in #9 above, the failure to so advise City Council of the negative veto was the responsibility of one or both of Messrs. Houston and/or O'Brien and not the responsibility of either OMERS/Borealis or its counsel.

11. Did the Mayor act properly throughout the transaction?

Yes. The Mayor approved the final transaction documents that were before her and members of City Council at the November 29, 2000 City Council meeting. It was the responsibility of Mr. Houston and Mr. O'Brien to carry out the necessary due diligence to ensure that the final documents were consistent with what City Council had approved, to advise the Mayor of any subsequent changes to the agreements including the changes to section 2.15(t)(i) of the Shareholders Agreement and to seek the approval of the Mayor and City Council before agreeing to such changes.

12. When concerns about clause 2.15(t)(i) arose, was there an adequate investigation of the transaction?

In 2007, City Council considered the issue of Enersource directors' remuneration. When the City and Borealis/OMERS as Enersource shareholders could not agree on the amount of directors' remuneration, City Council learned for the first time about the negative veto in the Enersource Shareholders Agreement.

Upon learning about the negative veto, the City conducted an adequate investigation. At the time, the City Solicitor and the Mayor made appropriate inquiries to those who were involved in the transaction, as well as retaining outside counsel to conduct an investigation.[25]

Unfortunately, the answers provided by the key figures - Mr. Houston and Mr. O'Brien - were inconsistent, full of contingent or hypothetical answers, and in some cases were nonsensical.[26] In late 2008 and into early 2009, the City sought further answers, only to be provided with more inconsistent, unclear and nonsensical answers from those who were involved.[27]

As a result, it was appropriate for the City to call for a judicial inquiry on the Enersource Transaction in order to fully investigate the circumstances surrounding the addition of the negative veto into the Enersource shareholders' agreement.

13. What recommendations should the Commissioner consider with respect to:

a. minute-taking and note-keeping during *in camera* sessions of Council;

Subsections 239(7) and (8) of the *Municipal Act, 2001*[28] require that the City Clerk must take minutes of in-camera meetings of City Council. Though these sections represent an improvement over the old *Municipal Act*, R.S.O. 1990, c. M. 45. (the legislation in force in 2000), which contains no such requirements, they still would have not provided a complete and comprehensive picture of the business that City Council conducted in the various in-camera sessions that were considered in this phase of the Inquiry.

The difficulty is that minutes are a high level recording of a discussion, but do not present all of the details of the discussion. The *Municipal Act, 2001* does not contain any provisions requiring detailed note taking in an in-camera session.

What may have benefitted the City in this case is an obligatory note taking policy, procedure or legislative requirement establishing a permanent record of what took place during an in-camera session. In addition

to providing details of what was discussed, the record should describe who was present during the in-camera session, what materials were distributed, what confidential instructions were provided to City staff, and any resolutions that were to be announced in a public session.

Concomitant with the establishment of an obligatory note taking policy, procedure or legislative requirement would be to designate under the City's records retention by-law how long such notes should be kept. Currently, the City's record retention By-law requires that minutes of City Council meetings and General Committee meetings be kept for 2 years in active storage and to be archived permanently thereafter. Currently, when the City Clerk takes notes, these notes are only kept for one year. Arguably they should be kept for the same time period as the minutes of City Council meetings referenced above.

b. "informal briefings" of City Council;

The Corporation of the City of Mississauga acts by By-Law through the Mayor and Members of Council. There neither is, nor should there be, any mechanism for informal decision making by City Council.

Both the *Municipal Act, 2001* and the old *Municipal Act* (the legislation that was in force in 2000) govern the calling, place and proceedings of City Council meetings. Under neither statutory scheme could City Council conduct official business without adhering to the requirements of the legislation. Subsection 55(2) of the old *Municipal Act* required the passing of a procedural by-law setting out the exact procedure that the City would follow in regards to the calling, place and proceedings of City Council meetings.[29] In 2000, the City's procedural by-law was 272-92.[30] Under that by-law, "Meeting" is defined to include all regular, special or other meetings of Council. Essentially, any time Council gathers together and discusses City matters, a meeting is constituted. There was, and is, no legislative provision allowing for informal meetings of Council.

Official City business, now and in 2000, must be and must have been conducted in accordance with the City's procedural by-law. Therefore, the issue is not whether official City business can be conducted in

meeting of City Council not in adherence with the City's by-law – clearly it cannot. The issue is whether such informal briefings should be taking place at all.

Councillor Mahoney testified that informal briefings occurred when Mr. O'Brien was City Manager (and under his predecessor) but "not very often" and she referred to such meetings as "education sessions". She also testified that changes that occurred as a result of the enactment of the *Municipal Act, 2001* have significantly reduced informal briefings that were held as part of what were known as "education sessions".[31]

In fact, as noted above, there was and is no legislative mechanism allowing for informal briefings to City Council. There was, prior to the enactment of the *Municipal Act, 2001*, also no such thing as "education sessions". "Educational sessions" are something quite specific and it was the *Municipal Act, 2001* (s. 239(3.1)) that authorized "educational sessions". Importantly, the *Act* requires these to be formally scheduled and placed on the agenda. Educational sessions are significantly restricted in terms of what they can cover. Further, such sessions cannot advance the decision-making process of City Council.

To the extent informal briefings were used in 2000 it was clearly a feature of Mr. O'Brien's informal management style and practice as City Manager and not one allowed by law. Accordingly, if the provisions of the *Municipal Act, 2001* and the current procedural by-law are followed no recommendation is necessary or required.

c. instructions and chains-of-command when counsel negotiates a deal on behalf of a municipality; and

The City's policies and procedures presently in place regarding these issues are significantly different than what was the norm in 2000. When Mr. O'Brien was City Manager, the City was operating very informally and paper trails were discouraged. Today, confidential instructions to City staff, as authorized by s.239(6) of the *Municipal Act, 2001*, are recorded by the City Clerk and distributed to City staff involved a particular matter. In addition, outside consultants and counsel retained by the City are required

to execute comprehensive retainer agreements setting out the terms of their engagement and whom at the City they are to take instructions from. For example, outside counsel to the City take their instructions from the City Solicitor who is accountable to City Council.

What may have been helpful in this case is if upon Mr. O'Brien's secondment as President and C.E.O., there was a by-law enacted clearly setting out what authority Mr. O'Brien was to retain at the City and what authority was to be delegated to Angus MacDonald when he assumed the role of acting City Manager. Indeed, such detailed by-laws should also apply to appointments of secondment for all senior staff at the City.

It may also be of assistance for the City to develop a formal policy and/or guidelines for best practices regarding secondment of City employees, ideally including a requirement that secondments are subject to the review of City Council. Such policy/guidelines should provide that senior staff should not be seconded without City Council having the opportunity to fully explore the impact of the secondment on the corporation, and make necessary arrangements to ensure that provisions are in place to ensure that the best interests of the City are properly protected. Secondments should never put City staff in a potential conflict of interest situation, and should only happen when the best interests of the City can be achieved through authorizing the secondment.

Lastly, the *Municipal Conflicts of Interest Act*, R.S.O. 1990, c. M.50 does not specifically deal with secondments and possible conflicts that might arise in that context, accordingly consideration could be given to expanding the *Act* to include this type of conflict.

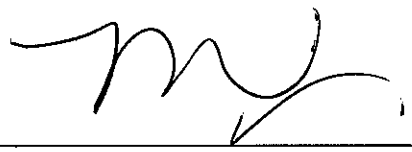
d. the appropriateness of requiring the Mayor to sign a document attesting to her familiarity with a document if she may not have personal familiarity with it.

The City's policies and procedures presently in place regarding this issue are significantly different than what was the norm in 2000. The Mayor testified that in a typical City Council meeting dozens of by-laws may be enacted and hundreds of documents may be before City Council for their approval. With such a

high volume of paper, the Mayor, the City Councillors and the City Clerk must be able to rely on City Staff to ensure that the form of the documents placed before the Mayor and City Clerk to execute accurately reflect the substance of what was agreed to.

In this case, Fraser Milner provided a comprehensive closing opinion stating, among other things, that all necessary City approvals had been obtained. Arguably in those circumstances, having the Mayor sign a certification of familiarity was neither necessary, appropriate and did not provide any further protection to the City.

One important procedural protection that is firmly in place presently (but was not consistently in place in 2000) is that all by-laws, contracts and other important documents placed before City officials for execution, including the Mayor and City Clerk, now contain a stamp from the City Solicitor's office approving them as to form. This stamp provides the Mayor and City Clerk comfort that the City Solicitor's office has checked that the form of the documents accurately reflect the substance of the agreements authorized to be entered into by City Council, and any amendments thereto.



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[1] S.O. c. 15, Sched. A, s. 142. Also see para. 29 of the Evidence of the Honourable Donald Macdonald, Exhibit 4, referring to Ontario, Ministry of the Environment and Energy, *A Framework for Competition: The Report of the Advisory Committee on Competition in Ontario's Electricity System* (Toronto: May 1996)(Chair: Donald Macdonald)("Macdonald Report")

[2] Transcript of the evidence of William Houston on May 26, 2010 ("Houston Transcript"), p. 159-160.

[3] July 14, 1999 Memo from Jonathan Toll to David O'Brien, Exhibit 7. Also see Transcript of the evidence of Jonathan Toll on May 25, 2010 ("Toll Transcript"), p. 61-64.

[4] Exhibits 9, 12 and 69.

[5] Report - Proposal to Create a Strategic Partnership with the City of Mississauga, Exhibit 13. TD Securities Presentation to the Mayor and Members of Council, Exhibit 9. Also see Houston Transcript, p. 173-175.

[6] In Camera Corporate Report from David O'Brien to Chairman and Members of the General Committee re Hydro Restructuring, Exhibit 6. Also see Transcript of the evidence of David O'Brien on May 27, 2010 ("O'Brien Transcript") at p. 417.

[7] By-law 0600-2000 authorizing the closing of the Strategic Alliance Agreement, enacted November 29, 2000, Exhibit 23. Also see O'Brien Transcript, p. 464; Houston Transcript, p. 195; Transcript of the evidence of Councillor Katie Mahoney on June 15, 2010 ("Mahoney Transcript"), p. 1103-1104; and January 22, 2009 e-mail from David O'Brien to Carol Horvat, Exhibit 17.

[8] Resolution 0091-2000, Exhibit 69.

[9] O'Brien Transcript, p. 483-484.

[10] Transcript of the evidence of Jeffrey Singer on June 1, 2010 ("Singer Transcript"), p. 786

[11] O'Brien Transcript, p. 519. Houston Transcript, p. 163.

[12] Transcript of the evidence of Her Worship Mayor Hazel McCallion on June 2, 2010 ("Mayor's Transcript"), p. 1053-1054.

[13] O'Brien Transcript, p. 464-467, 476-477, 503-505. Also see January 22, 2009 e-mail from David O'Brien to Carol Horvat, Exhibit 17.

[14] Transcript of the evidence of Councillor Kathleen Mahoney on June 15, 2010 ("Mahoney Transcript"), p. 1112-1118.

[15] Mahoney Transcript, p. 1097

[16] Mahoney Transcript, p. 1113-1119

[17] Sworn affidavits of Councillors Iannicca, Carlson, Corbasson, Mullin and Prentice, Exhibits 75-79.

[18] Mahoney Transcript, p. 1123

[19] Mayor's Transcript, p. 1000. Also see Transcript of the evidence of City Solicitor Mary Ellen Bench on June 1, 2010 ("Bench Transcript"), p. 868-869.

[20] Transcript of the evidence of Michael Nobrega on May 31, 2010 ("Nobrega Transcript"), p. 588-589

[21] *Supra* note 7.

[22] Singer Transcript, p. 801-802

[23] O'Brien Transcript, p. 474, 478

[24] Strategic Alliance Agreement and Key Related Legal Documents - Brief for Directors prepared by Fraser Milner, Exhibit 16. Also See Houston Transcript, p. 188-193.

[25] Singer Transcript, p. 770-782. Also see Bench Transcript, p. 832-858.

[26] Exhibits 21 and 33.

[27] Exhibits 17, 18 and 65. Also see Houston Transcript, p. 296-298; and O'Brien Transcript, p. 464-467, 476-477, 503-505.

[28] S.O. 2001, c. 25.

[29] Under the *Municipal Act, 2001*, subsection 238(2) governs the calling, place and proceedings of City Council meetings.

[30] By-law 272-92, Exhibit 68.

[31] Mahoney Transcript, p. 1122-1123.