



STAFF REPORT ACTION REQUIRED

Participation in Consultation for Proposed Development of Corporate Governance Guidance for Ontario Energy Board Rate-Regulated Utilities

Date:	July 5, 2016
To:	City Council
From:	City Manager
Wards:	All
Reference Number:	

SUMMARY

On June 22, 2016, the Ontario Energy Board (the "**OEB**") published a draft report (the "**Draft Report**"), prepared by Elenchus Research Associate Inc., entitled: *Corporate Governance for Regulated Natural Gas and Electricity Utilities* (http://www.ontarioenergyboard.ca/oeb/Documents/EB-2014-0255/Elenchus_Draft_Report_Corp_Governance_20160622.pdf). The stated purposes of this report include:

- Discuss the context for the OEB's past, current and future interest in utility corporate governance
- Present the fundamentals of good corporate governance
- Set the framework for stakeholder consultations on the OEB guidance, and the monitoring and assessment tools
- Present recommendations for the OEB guidance, monitoring and assessment (including a *Preliminary Draft* of the OEB guidance)

The OEB has stated that the Draft Report is draft because the OEB and Elenchus want to gain insight from Utilities and other stakeholders before it is finalized. To this end, OEB and Elenchus staff will be holding targeted meetings with selected stakeholders to discuss the principles and recommendations set out in the Report. The OEB has not yet announced timing for these consultations.

The OEB requested that stakeholders interested in participating should indicate their intent by filing a letter with the OEB by July 11, 2016. As the sole shareholder of THC, there is a potential that the recommendations in the Draft Report may have an impact on the relationship between the City and THC.

This report outlines the recommendations in the Draft Report and seeks City Council's ratification of the actions taken by the City Manager in submitting a letter (dated July 8, 2016) to the OEB, expressing an interest in participating in the consultations. This report seeks further authorization for staff to participate in these consultations in order to ensure that the City's interests, as shareholder, are represented.

Further analysis of the preliminary guidance and recommendations in the Draft Report and its implications for the relationship between the City and Toronto Hydro Corporation will be undertaken prior to the consultations.

Following participation in the consultations, the City Manager will report back to Council on the outcomes of the consultation process and any finalized reports from the OEB.

RECOMMENDATIONS

The City Manager recommends that:

1. Council ratify the actions taken by the City Manager expressing an interest in the City of Toronto, as shareholder of the Toronto Hydro Corporation, participating in the stakeholder consultations to develop guidance on corporate governance for Ontario Energy Board rate-regulated utilities.
2. Council authorize staff to participate in the OEB stakeholder consultations to ensure that the City's interests are represented.
3. Council request that the City Manager report back on the results of the consultation, when the consultations are complete.

Financial Impact

There are no financial implications associated with the recommendations in this report.

As of the writing of this report, the financial implications to the City of the draft guidelines for OEB rate-regulated utilities is not known. An in-depth analysis will be undertaken and included in a report back to City Council upon completion of the consultations.

The Deputy City Manager and Chief Financial Officer has reviewed this report and agrees with the financial impact information.

ISSUE BACKGROUND

Relationship between the City and Toronto Hydro Corporation

The Toronto Hydro Corporation (THC) is incorporated under the Business Corporations Act, with the City of Toronto as its sole shareholder. THC is the sole shareholder of the Toronto Hydro-Electric System Limited (THESL), which is the electricity distribution company that would be subject to the proposed new OEB guidelines.

Pursuant to City Of Toronto By-Law No. 374-1999 City council authorized the transfer of the employees, assets, liabilities, rights and obligations of the Toronto Hydro-Electric Commission and the City of Toronto associated with the generation, distribution, transmission and retailing of electricity and associated business activities to Toronto Hydro Corporation, Toronto Hydro-Electric System Limited (THESL) and Toronto Hydro Energy Services Inc. (THESI), as Business Corporations Act (Ontario) corporations incorporated under Section 142(1) of the Electricity Act, 1998 and Sections 71 and 73 of the Ontario Energy Board Act, 1998. Shares of each of the corporations were issued to the City.

The City transferred all of the voting securities in THESL and THESI which were issued to the City pursuant to the By-law, to Toronto Hydro Corporation in consideration of the issuance to the City of voting securities by Toronto Hydro Corporation.

The following is a link to the 2015 annual report of the parent company

http://www.torontohydro.com/sites/corporate/InvestorRelations/FinancialReports/annualReportProject2015/Documents/PDFs/AR2015_e-Report.pdf

THC Governance

THC is managed by a Board of Directors consisting of 11 members and composed of:

- The Mayor, or a Council Member who the Mayor recommends as a designate and is appointed by City Council;
- 2 Council members;
- 8 citizen members.

City Council appoints one of the citizen members of the Board to be the Chair.

Members are appointed according to the policies and procedures in the City's Public Appointments Policy by a Corporation Nominating Panel appointed by the Mayor.

The relationship between the City and THC is set out in the Shareholder Direction, which includes: the structure and responsibilities of the Board of Directors, matters regarding THC subsidiaries, remuneration, matters requiring shareholder approval and reporting requirements.

COMMENTS

The Ontario Energy Board (OEB) is currently in the process of establishing a performance based regulatory framework, and has indicated that it views good corporate governance as a significant element to the performance of utility companies.

As part of the process to develop a new regulatory framework, the OEB retained KPMG to conduct a jurisdictional review of leading corporate governance practices by other energy and non-energy regulators, and corporate governance structures currently in place for Ontario electricity distributors. This review resulted in an April 2015 report, Review of Corporate Governance of Electricity Distributors (http://www.ontarioenergyboard.ca/oeb/Documents/EB-2014-0255/KPMG_Report_Corporate_Governance_20150429.pdf), which provided recommendations for the OEB to consider in order to assist electricity distributors in achieving good corporate governance.

These recommendations include:

- establishing guidance for electricity distributors to achieve corporate governance standards that reflect best practice;
- identification of indicators for the ongoing monitoring of the effectiveness of good corporate governance; and,
- developing an approach (eg. periodic audits) to provide evidence that distributors' corporate governance reflects leading practice.

In a June 22, 2016 letter inviting stakeholders to consult, the OEB indicated that it intends to accept the recommendations in KPMG's report and retained Elenchus Research Associate Inc. (Elenchus) to build on these recommendations to develop draft guidance on good corporate governance.

As THC may be subject to any new guidelines and/or requirements, it is important that the City participate in these consultations to represent the City's interests as shareholder of THC. A copy of the letter sent to the OEB expressing an interest in participating in the consultations is attached in Appendix 1.

Elenchus Report

In the Draft Report, *Corporate Governance for Regulated Natural Gas and Electricity Utilities*, Elenchus put forward draft, principles-based guidance and recommendations intended to apply to all OEB rate-regulated utilities. This report has been released as a draft so that OEB and Elenchus can consult with stakeholders, with the feedback of these consultations being used to inform the final guidance for corporate governance of rate-regulated utilities.

The following is a summary of the Preliminary Draft Guidance and Elenchus' recommendations to the OEB that will be the focus of the stakeholder consultations:

Preliminary Draft Guidance – Appendix 1 of Elenchus Report

1. Section 1 outlines the responsibilities of the board of directors and recommends a clear delineation of responsibilities for the Chair of the Board, the Chair of each Board committee and the CEO.
2. Section 2 makes recommendations concerning the composition of the Board, recommending that the majority of Board members be independent, "to provide an appropriate balance between strong corporate governance and reasonable flexibility for utilities". Further recommendations include the imposition of term limits for directors, regular meetings between independent directors and the adoption of policy or targets relating to the identification and consideration of women as directors.
3. Section 3 provides guidance for the creation of Board committees to fulfill its responsibilities, recommending that Board's appoint an Audit Committee, Human Resources Committee, Nominating Committee, Governance Committee and Risk Committee.
4. Section 4 sets out recommended practices for Board's to develop, adopt and uphold a written code of business conduct, which should address a number of matters including conflict interest, protection of corporate assets, confidentiality of corporate information and compliance with laws, rules and regulations. The draft also recommends that Boards develop practices to avoid conflicts of interest, mitigate risk, formalize a corporate strategy and promote effective communication between the board, management and the shareholders.

Elenchus Recommendations to OEB – Appendix 2 of Elenchus Report

The following is a high-level summary of the Elenchus' recommendations to the OEB, which are grouped in three categories: guidance, monitoring and assessment.

1. **Guidance:** Recommends high-level principles that form the basis for the Preliminary Draft Guidance in Appendix 1, including that guidance should be based on financial and securities regulator guidance, and be consistent with best practices in corporate governance in Canada.
2. **Monitoring:** Recommends specific disclosure requirements aligned with the OEB's guidance, as well as more detailed disclosure in key areas, such as Board responsibilities, Director independence, Director selection and assessment, risk management, stakeholder interests, conflict of interest, Board assessment, key regulator issues, significant Board events. The report indicates that Elenchus intends on discussing these recommendations further with stakeholders. This section also recommends specific requirements concerning self-assessment, and a disclosure framework with respect to reporting.

3. **Assessment:** Makes specific recommendations with respect to assessing Board governance practices and periodic audits of Board disclosures to the OEB.

City Response to Draft Preliminary Guidance and Recommendations

In preparation for the consultation, a more fulsome analysis of the potential impacts of the draft Preliminary Guidance and recommendations on the City and its relationship with THC will be undertaken. The consultation will provide the City the opportunity to represent its interests as shareholder and to identify opportunities to support and strengthen the City's relationship to THC and its role as shareholder.

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SIGNATURE

Peter Wallace
City Manager

ATTACHMENTS

Appendix 1: Letter of Interest to Participate in OEB Consultations