

PowerStream's Response to COLLUS Power Corp Request For Proposal



STRATEGIC PARTNERSHIP Section 3.1 – Purchase of Shares

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November 16, 2011

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This document contains PowerStream’s response to Section 3.1 of COLLUS Power Corp’s Request for Proposal - Strategic Partnership, and addresses matters directly related to purchase of shares.

The remaining sections (3.2 - 3.7) of PowerStream’s proposal are submitted under separate cover, as required by the RFP.

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A INTRODUCTION

PowerStream is pleased to respond to the Request for Proposal document issued by COLLUS Power Corp (“COLLUS Power”) on October 4, 2011.

On September 19, 2011 the PowerStream team made a presentation to the COLLUS Power Strategic Partnership Task Team. The PowerPoint presentation made at that time is attached as an appendix to PowerStream’s response to the RFP in Section B.

PowerStream Inc. is the second largest municipally-owned electricity distribution company in Ontario, serving more than 330,000 customers in nine municipalities located in Simcoe County and York Region that have a combined population of approximately 1,000,000.

Created on June 1, 2004, following the merger of three York Region-based utilities (Markham Hydro, Richmond Hill Hydro and Vaughan Hydro), PowerStream Inc. is jointly owned by City of Vaughan, the Town of Markham and the City of Barrie. PowerStream’s unprecedented and unrivaled expansion of its customer base from just over 192,000 in 2004 to 334,472 (as of October 31, 2011) is a result of serving an area of the province that continues to experience tremendous population growth in combination with the company’s own pursuit of forming strategic partnerships and relationships with other utilities. PowerStream has successfully completed the voluntary merger of four utilities and the acquisition of another in less than five years.

Although for most companies the transitional challenges that usually follow a merger or acquisition can often impede the achievement of other corporate goals and objectives, PowerStream through these consolidations has continued to demonstrate its industry leadership in customer service, innovation and environmental stewardship.

Several major projects completed by PowerStream since its merger with Barrie Hydro Distribution Inc. on January 1, 2009, such as bringing into service the company’s 11th transformer station directly connected to the provincial transmission grid and the incorporation of several smart grid features to its own distribution system, along with some impressive customer and employee satisfaction figures, are indicative of the company’s ability to transition, move forward and lead at the same time. This is further evidenced by the number of awards the company has earned over in recent years including Greater Toronto’s Top Employers (2012), Electricity Distributors Association’s Performance Excellence Award (2011), United Way of Great Simcoe County’s Campaign Merit Award (2010), Ontario Energy Association’s Company of the Year Award (2010), Ministry of the Environment’s Ontario Environmental Leader (2010), Vaughan Chamber of Commerce Business of the Year (2010), Electricity Distributors Association’s Environmental Excellence Award (2009) and Smart Commute Employer of the Year for North Toronto, Vaughan (2009 and 2011).

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PowerStream's commitment to the environment and sustainable growth has been demonstrated in several areas and on a number of occasions. The company has built two work location buildings that have been certified by the Canada Green Building Council as LEED® (Leadership in Energy and Environmental Design) Gold. No other company in Simcoe County or York Region, and no other electricity distribution utility in Ontario, operates out of multiple LEED® gold certified facilities. Further to this, PowerStream has an active solar PV generation business and is an industry leader in the delivery of conservation and demand management programs to its customers.

PowerStream believes that COLLUS Power and PowerStream share the same values which are critical to making the proposed Strategic Partnership successful. In fact, COLLUS Power's inspirational and forward-thinking value statement that the organization values "the entrepreneurial spirit to responsibly and decisively challenge the conventional" aligns well with PowerStream's vision statement of being "a socially responsible company, committed to the environment and sustainable growth, leading the way into the future with boldness, innovation, and industry best in class performance." Moreover, COLLUS Power's stated values of "trust, responsibility, sustainability, people, partnerships & collaboration and continuous improvement" are similar in intent and spirit to PowerStream's values of "respect, teamwork, performance, accountability and initiative."

PowerStream is proposing a structure which will satisfy the objectives of both COLLUS Power and the Town of Collingwood and create a partnership which will continue to operate in the best interests of the customer, employees and Shareholders in all the service territories currently served by both entities. This structure recognizes the importance of municipal ownership, growth and community involvement, principles that are held in high regard by both organizations and the customers they serve. The model, articulated to the COLLUS Power Strategic Partnership Task Team by Brian Bentz, President & CEO of PowerStream on September 19, 2011, is transferable for future regional growth with other communities and we believe that this will provide a model for further consolidation.

The structure envisaged by COLLUS Power and wholly supported by PowerStream includes:

- A proposal to purchase 50% of the equity in COLLUS Power and provide an additional cash payment by facilitating the recapitalization of COLLUS Power
- A proposal to provide strategic and specialized resources to COLLUS Power while continuing to effectively engage the COLLUS Power and affiliate employees
- A proposal to support growing the COLLUS Power business both organically and through acquisition or merger
- A proposal to provide a continued and substantial presence in the communities that COLLUS Power serves

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- A proposal to provide continued and enhanced support for the interests of the communities COLLUS Power serves
- A proposal to provide continued focus on maintaining and enhancing the competitive distribution rate and cost structure of COLLUS Power

PowerStream is very pleased to have been given the opportunity by COLLUS Power to respond to the RFP and PowerStream strongly believes in the strategic, operational and financial benefits that its Proposal offers.

NOTE: In PowerStream's Response we have, assuming that we may be the successful proponent, referred to the post closing utility as "COLLUS PowerStream".

B PURCHASE OF SHARES**B.1 Proposed Payment**

Subject to the Terms and Conditions of a Share Purchase Agreement, the Town of Collingwood would receive total cash consideration of \$14,510,170 upon closing. This payment is comprised of:

Sale of 50% Equity of COLLUS Power	\$7,300,000
Recapitalization Dividend	\$5,500,000
Repayment of Town of Collingwood Note	\$1,710,170
TOTAL CASH TO TOWN OF COLLINGWOOD	\$14,510,170

Upon closing, PowerStream would pay \$7.3 million for duly-issued shares evidencing PowerStream's ownership of 50% of the outstanding equity share capital of COLLUS Power.

PowerStream would also facilitate a special recapitalization dividend to be paid immediately prior to closing to recapitalize COLLUS Power to its deemed capital structure, as determined by its Ontario Energy Board ("OEB") defined regulatory rate base, while also maintaining a deemed level of working capital based on the 2011 audited financial statements, as at December 31, 2011. We estimate the amount of the recapitalization dividend to be approximately \$5.5 million. If the 2011 audited financial statements are not final, the recapitalization dividend will be estimated based on the unaudited financial statements. If required, upon finalization of the 2011 audited and closing financial statements, a post closing adjustment would be made to reflect the difference between the estimated 2011 results and the closing financial statements.

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In addition, as part of its proposal, PowerStream is prepared to offer, if the Town of Collingwood so chooses, that the existing promissory note, payable held by the Town of Collingwood, would be repaid by third party debt facilitated by PowerStream. This would give the Town of Collingwood an additional \$1,710,170 as part of the sale of COLLUS Power for a potential total cash distribution to the Town of Collingwood of \$14,510,170.

**B.2 *Proposed Timing Considerations;* B.3 *Due Diligence Requirements;*
B.4 *Pre-Closing Conditions***

If PowerStream is the successful Proponent, a Share Purchase Agreement would be prepared to effect the transaction. Such agreement would contain customary representations and warranties for a transaction of this nature. The Share Purchase Agreement would include a new Shareholder Agreement, which would, among other things, set out the composition of the Board of Directors, Unanimous Consent Items, Objectives and Guiding Principles, and Liquidity Rights. The Share Purchase Agreement will also provide for customary due diligence including, but not limited to: financial systems and record of accounts, inspection of physical plant and related assets, review of audited financial results for the fiscal year 2011, closing financial statements and other related documents, and review of Information and Technical Systems.

B.5 *Representation on Proposed New COLLUS PowerStream Board*

As noted in COLLUS Power's RFP, its the preference is that a majority of Board members on the Board be independent. Consistent with this philosophy, PowerStream proposes the following Board structure:

- 6 person Board of Directors comprised of 3 representatives each from The Town of Collingwood and PowerStream
- 2 co-chairs to be nominated by each Shareholder
- A majority of the representatives from both Shareholders would be independent

The proposed Board of Directors structure, combined with the Shareholders Agreement, would ensure that there is significant local input over the COLLUS PowerStream operations.

B.6 *Proposed Dividend Policy*

PowerStream's Proposal is conditional upon agreement on a new Dividend Policy. In 2010, COLLUS Power did not pay a dividend to its Shareholder. Starting in 2013 COLLUS PowerStream would expect to pay a dividend to its Shareholders. The proposed Dividend Policy is consistent with other dividend policies for regulated entities in Ontario.

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Such Policy is based on the philosophy that the purpose of the dividend policy is to provide the Shareholders with a steady income stream from continuing operations while providing COLLUS PowerStream with an appropriate capital structure and working capital level in order to operate as a viable business. The Dividend Policy philosophy would be consistent with the objectives and guiding principles of COLLUS PowerStream.

It is proposed that Dividend amounts would be determined as follows:

- COLLUS PowerStream shall pay a minimum of 50% of annual net income, as dividends, with consideration given to the following:
 - Cash position at the beginning of the year;
 - Working capital requirements for the current year; and,
 - Net capital expenditures required for the current year.

Based on the forecasted net income for COLLUS PowerStream, and assuming that COLLUS PowerStream earns the regulated rate of return, we anticipate that the net income in 2013 could be in the range of \$800,000 to \$1,000,000. As per the proposed Dividend Policy, COLLUS PowerStream would therefore pay a dividend of approximately \$400,000 to \$500,000.

B.7 *Other - Shareholders Agreement Matters*

PowerStream's Proposal is conditional upon the Parties agreeing upon their respective Liquidity Rights to be incorporated in the new Shareholder Agreement. As contemplated in the RFP, the new Shareholder Agreement would provide for certain buy/sell arrangements.

Such arrangements would include:

Any transfer or pledge of shares in COLLUS PowerStream would be prohibited without the written consent of the other Shareholder, provided that the Shareholders Agreement shall include liquidity provisions to be negotiated, such as:

1. In the event that either Shareholder receives a bona fide offer which it desires to accept from an arm's length third party to acquire all of the Shares owned by such Shareholder for cash (an "Offer"), the other Shareholder shall be entitled to a right of first refusal to acquire such Shares at the same price and on the same terms and conditions as set out in the Offer, failing which the Shareholder receiving such Offer shall be entitled to sell its Shares to the third party which made the Offer subject to that third party agreeing to be bound by the Shareholders Agreement;

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2. At any time after 2 years from the date of closing, either Shareholder may by written notice to the other institute a buy - sell mechanism by specifying a price per Share and requiring that the recipient Shareholder in its discretion elect either to (i) purchase all of the Shares of the initiating Shareholder, or alternatively (ii) sell all of the Shares of the recipient Shareholder, in each case at the price per Share specified in the initiating notice;
3. At any time after 2 years from the date of closing, Collingwood Utility Services Corp, as the owner of 50% of the outstanding Shares of COLLUS PowerStream, shall be entitled to Put those shares to PowerStream Inc and require that the latter acquire such Shares at a price equal to their fair market value determined by the same valuation approach as was utilized in the purchase by PowerStream Inc. of its initial 50% shareholding in COLLUS PowerStream.

B.8 *Ontario Energy Board*

It is our understanding based on Section 86(2) of the OEB Act which deals with ‘Acquisition of Share Control’ that, as a result of COLLUS Power Corp and the Town of Collingwood selling 20% or more of their equity in COLLUS Power, a MAADS (“Mergers, Acquisitions, Amalgamation and Divestitures”) application to the OEB will be required. This application will follow a process similar to that for a rate application with a newspaper notice, interrogatories from intervenors, written submissions and a written or oral hearing.

MAADs applications are evaluated based on a “no harms test”, meaning that the OEB must determine that COLLUS Power and PowerStream customers will be no worse off as a result of the transaction. Although this may appear simple, the application, the subsequent additional evidence and the Decision are very important strategic information. OEB staff and intervenors will refer back to these documents for years to come.

PowerStream staff has extensive experience in the MAADs process, most recently with the Barrie-PowerStream merger. This application was approved by the OEB at the end of an oral hearing in December 2008.

PowerStream staff will support COLLUS Power staff in the MAADs application by providing strategic advice and assisting with the compilation of evidence, interrogatory responses, submissions, witness training and hearing preparation, as necessary.

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C APPENDIX

C.1 Objectives and Guiding Principles

PowerStream proposes that the new Shareholder Agreement would set out the Guiding Principles of the Corporation, which would include the following:

- **For Profit Corporation** – COLLUS PowerStream will continue to be a for profit corporation committed to optimize its rate of return and Shareholder value. Subject to OEB approval, the maximum rate of return sought by COLLUS PowerStream from time to time will be achieved as soon as practical
- **Capital Structure** – COLLUS PowerStream will maintain a capital structure consistent with the OEB capital structure mandated by the OEB (currently 60/40 debt to equity).
- **Dividend Policy** – COLLUS PowerStream will plan to pay dividends to its Shareholders approximating 50% of the net income on an annual basis with due consideration given to the cash position at the beginning of the year, working capital requirements and net capital expenditure requirements.
- **Growth** – COLLUS PowerStream will be committed to pursuing significant growth opportunities on a prudent and profitable basis giving due consideration to the geographic footprint, size and location of LDCs in Ontario.
- **Employees** – COLLUS PowerStream will treat all employees in a fair and equitable manner. The Corporation will develop with its employees a shared commitment towards high customer service, improved productivity and workplace safety. The Corporation will ensure that all staff understand the Corporation's business plan and have the skills they require to fulfill their part in achieving those goals.
- **Customers** – The customers of the Corporation are the operational priority of the Corporation. COLLUS PowerStream will provide a reliable, effective and efficient electricity distribution system.
- **Community and stakeholders** – COLLUS PowerStream will play a significant role in the local communities in which it operates. COLLUS PowerStream will act as a good corporate citizen and a facilitator of economic development in the communities it services.