



**ROBINS APPLEBY**  
BARRISTERS + SOLICITORS

# MEMORANDUM

**reqTO:** Blue Mountains Attainable Housing Corporation  
**FROM:** Robins Appleby LLP  
**SUBJECT:** Governance in Housing Corporations  
**DATE:** March 26, 2021  
**FILE NO.:** 2000775

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Blue Mountains Attainable Housing Corporation ("**BMAHC**") is a Municipal Services Corporation, incorporated by the Town of The Blue Mountains (the "**Town**"). You have tasked us with canvassing the drivers for the creation of a housing subsidiary and review the governance structure in place for BMAHC outlining the legal relationship with the Town and the benefits it serves.

This memorandum outlines some of the factors that municipalities consider in establishing independent housing corporations, especially as it relates to managing development projects similar to the Gateway project contemplated by the Town and BMAHC.

## **RECOMMENDATIONS**

Based on our review, we make the following recommendations, which are discussed in further detail in the memorandum:

1. Amend the Letters Patent and the By-laws of BMAHC to contemplate rental housing;
2. Review the requirement of being a member as a result of being a director of BMAHC;
3. The Gateway Project should be managed through BMAHC based on the advantages outlined in this memorandum, including liability protection for the Town, and lowering of risk resulting from an independent skill-based board of directors and holding its interest through BMAHC; and
4. Re-evaluate the governance structure to minimize risk of perception that the two entities are not independent, including potential revisions of the by-laws and the Memorandum of Understanding.



## **CURRENT GOVERNANCE STRUCTURE**

### ***Incorporation***

Town Council authorized the creation of BMAHC as a Municipal Services Corporation in its March 25, 2013 Council meeting.<sup>1</sup> The Letters Patent to incorporate BMAHC under the *Corporations Act* (Ontario)<sup>2</sup> were approved by the Ministry of Government Services on September 4, 2013. The Letters Patent provides that the objects of the corporation are to “augment the supply of healthy, affordable and sustainable ownership housing units in the Town of The Blue Mountains which are affordable to a larger portion of the population.”<sup>3</sup> It is noted that the Letters Patent specifically contemplates ownership and does not address rental units. It is recommended that the Letters Patent be amended to allow for rental housing to address the future needs of the organization.

### ***Municipal Services Corporation***

As mentioned above, BMAHC is a Municipal Services Corporation. Section 203 of the *Municipal Act*<sup>4</sup> gives municipalities the power to establish subsidiary corporations referred to as Municipal Services Corporations, which include non-share capital corporations.

Generally, a Municipal Services Corporation can only be established to provide a system, service or thing that the municipality itself could provide, however, section 9 of *Ontario Regulation 599/06* (“**O. Reg. 599/06**”) specifies a list of permissible economic development services. These services include, amongst other things, the acquisition, development and disposal of sites in the municipality for residential, industrial, commercial and institutional uses and the provision of residential housing.

The activities of a Municipal Service Corporation are restricted by Section 18 of O. Reg. 599/06. A key restriction for BMAHC is that Subsection 18(1) of O. Reg. 599/06 provides that the Municipal Services Corporation cannot incorporate another corporation. Thus, BMAHC is restricted from creating subsidiaries, which means that BMAHC will not be able to shield itself from liability from development activities by creating subsidiaries. The Town, though, is shielded from liability via BMAHC, as further discussed later in this memorandum.

### ***By-law 1***

By-law 1 provides the governance framework for BMAHC. This By-law also includes the same objects of the corporation as the Letters Patent. Thus, this By-law should also be updated to allow for rental housing.

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<sup>1</sup> Town of the Blue Mountains Staff Report CAO.13.01, *Creating the Non-Profit TBM Housing Corporation*, dated March 25, 2015.

<sup>2</sup> *Corporations Act*, R.S.O. 1990, c. C.38.

<sup>3</sup> See Section 4 of Letters Patent for Ontario Corporation Number 1899457, The Blue Mountains Attainable Housing Corporation, dated September 4, 2013.

<sup>4</sup> *Municipal Act*, 2001, S.O. 2001, c. 25.



By-law 1 also provides the rules related to the board of directors and members. Specifically, it is stated that:

- The Board of Directors consist of seven (7) directors, two of whom shall be any of the Mayor, Deputy Mayor or any Councillor of the Town;<sup>5</sup> and
- There are two classes of membership:
  - Municipal Member, being the Town, who shall be entitled to forty-five (45) votes at members' meetings; and
  - Members, being the directors of the board, and each having a single vote at members' meetings, with a maximum of twenty (20) such members ("**Board Members**").<sup>6</sup>

It is noted that by-law 1 specifically addresses the need for political appointments to the board, but is silent with respect to non-political appointments. This issue is discussed further later in this memorandum.

By-law 1 provides for two classes of membership, with the Town having a super majority (i.e. more than two-thirds) of voting rights. Thus, the Town has effective control over BMAHC as it can, amongst various other rights, dictate the composition of the board.

The twenty Board Members spots are reserved for those that are appointed as directors of the corporation, which also include the politicians on the board. The only requirement outlined to qualify as a Board Member is what is prescribed under the *Corporations Act*, i.e. the individual must be 18 years of age or older and must not be an undischarged bankrupt.<sup>7</sup> It is recommended that this definition be reviewed to determine if there are other requirements (e.g. living in Grey County) that should be included.

## ***By-law 2***

A second By-law (By-law 2) was enacted on December 12, 2013 that provides the board of directors with borrowing powers.

## ***Memorandum of Understanding***

There is also a Memorandum of Understanding between BMAHC and the Town<sup>8</sup> (the "**MOU**") that provides for certain services and support (e.g. human resources, IT, financial services, etc.) from the Town to BMAHC.

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<sup>5</sup> See article 5 of By-law 1 of The Blue Mountains Attainable Housing Corporation ("**By-law 1**").

<sup>6</sup> See article 28 of By-law 1.

<sup>7</sup> See section 286 of the *Corporations Act*, R.S.O. 1990, c. C.38.

<sup>8</sup> Memorandum of Understanding between the Blue Mountains Attainable Housing Corporation and the Corporation of the Town of Blue Mountains, dated October 19, 2020 (the "**MOU**").



The MOU also contains language in multiple sections<sup>9</sup> to acknowledge that the Town and BMAHC are separate and independent entities. Specifically, with respect to the BMAHC, paragraph 5(a) of the MOU provides that:

*The BMAHC is a separate and independent corporate entity of the Town with independent corporate status from the Town and has been established by the Town to provide attainable housing and related services in the Town.*<sup>10</sup>

Although this statement is clear in its intent to treat the entities as separate, there are aspects of the MOU that would suggest that the entities are very intertwined. As examples:

- BMAHC is required to present an annual statement of activities and budget to Council each year;<sup>11</sup>
- BMAHC's Executive Director must work in co-ordination with the Town's budget planning process to assist the Town in providing a consolidated budget to Council;<sup>12</sup>
- BMAHC is to provide yearly audited financial statement to the Town;<sup>13</sup>
- BMAHC must follow some of the Town's policies (e.g. POL IT Infrastructure Acceptable Use Policy); and
- BMAHC is to jointly defend the Town's decision in support of an attainable housing proposal at any future LPAT hearings.<sup>14</sup>

It should be noted that Memorandums of Understanding of this type are difficult to enforce if one party decides to not be bound by it as neither side is likely to take disputes to Court. The MOU, though, does contain a dispute resolution mechanism where the disputes are resolved through a committee consisting of two members of Council, two Directors of BMAHC who are not also Councillors, the Chief Administrative Officer of the Town and the Executive Director of BMAHC.<sup>15</sup> This committee is to determine the process to resolve the dispute, which may include third-party mediation. This type of dispute resolution mechanism does contemplate a collaborate approach of discussion amongst equals, but there is no mechanism outlined in the MOU on what happens if the committee is unable to decide on the process to resolve the dispute or if the process is unsuccessful. It would seem that the main option at that point would be to terminate the agreement, which either party can do by providing three months' notice.<sup>16</sup>

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<sup>9</sup> For example, see sections 5(a) and 5(b) of the MOU.

<sup>10</sup> Section 5(a) of the MOU.

<sup>11</sup> See section 5(d) of the MOU.

<sup>12</sup> See Schedule "B" of the MOU.

<sup>13</sup> See Schedule "B" of the MOU.

<sup>14</sup> See Schedule "C" of the MOU.

<sup>15</sup> See section 19 of the MOU.

<sup>16</sup> See section 20 of the MOU.

## **MANAGING DEVELOPMENT RISK**

### ***Development risks***

In order to assess the merits of an arm's length corporation, it's worth setting out the kinds of risks any public or quasi public body faces when undertaking development:

- **Cost over-runs** – Cost over-runs can be generated in several ways. The most frequent being unexpected increases in input costs, delays, and design related delays.
- **Procurement** – We note three distinct procurement risks.
  - First, there is a risk with contracting improperly – a reason that a municipality might prefer to retain control - and which must be clear regardless of who is controlling purchasing.
  - Second, There is a risk of contracting with vendors who are bad actors. The application of standard price based procurement practice in development is dangerous given the extent of the unknowns and reliance on good judgement.
  - Third, there is the risk of being over-prescriptive in procurement and disincentiving participation.
- **Design Risks** – Flaws in the design can delay projects and add costs to rectify. Being directly involved in the design process can alleviate this risk.
- **Utility to the end user** – A project can be great on paper, but it is useless unless it meets the needs of the end user. Continuous engagement with the end user is necessary to mitigate this risk.
- **Tortuous Liability** -- Lawsuits may arise at any point during the project, thus subjecting the owner to risk of damage awards. Corporate structures are created to shield the Owner from such liability.
- **Political Risk** – Development requires a decision-making timetable that is driven by the circumstances of construction. A stand-alone entity can be made to be more flexible and responsive than a political structure. Further, everyone is in favour of affordable housing until it is too big, too near, too noisy, too dusty and, as always, generating too much traffic. As political pressure mounts, a political “board” may be hard pressed to champion a development.

Different Municipalities, all sharing the goal of building housing, have elected to manage these risks differently. The creation of a subsidiary is a powerful way of addressing these risks.

### ***Control***

Before addressing the factors favouring an independent housing subsidiary, it is important to acknowledge why municipalities may prefer to have housing managed and operated internally. The main advantage of direct management of the housing stock versus managing through a arms-length corporation is the control that the municipality can have over the operations of affordable or attainable housing. Without a intermediary board, the municipality is in direct control of the



decision-making process. Such a structure has many risks, especially when dealing with development projects and the municipality retains all liability.

## **RATIONALE FOR A HOUSING CORPORATION**

### **1. Liability Protection**

In general, the use of a subsidiary allocates development risk to the subsidiary and therefore protects the Town's core assets should something go wrong during the development process.

In the event that development occurs under the Town's umbrella, its core assets are exposed. While we would expect that loans would be secured against development sites only, the borrower would still be the Town. A lender – or any other claimant – would be able to look to the land and the covenant of the Town to satisfy its debt or make claims.

In the event that development occurs under the subsidiary umbrella, the Town's assets would not be directly exposed. Notwithstanding the foregoing, there may be circumstances, such as financing, in which the Town may have to directly guarantee the obligations of the subsidiary, thereby exposing the Town to that specific liability of the subsidiary. However, the extent of the guarantee can be negotiated and limited.

### ***Following the Private Sector***

It is normal course for private development companies to use subsidiary corporations to isolate themselves from development risk. In the event a project becomes unviable, the project can be abandoned and sold by its creditors, with the developer's loss generally limited to its investment in that project (absent any other independent covenants, like a guarantee). Should something go wrong, it would be a fair question to ask why the Town had not used this mechanism.

The answer we hear most frequently to this question is that the municipality should stand behind its developments. We recognize that due to local politics and optics, it could be difficult for the Town to abandon the subsidiary were it to incur obligations that it cannot meet. However, this does not reduce the benefit of the subsidiary as it allows the Town more options in the event of a serious problem. Without the protection of the limited liability of a separate entity, creditors can impose enforcement processes or coercive terms. With the protection of limited liability, the Town is in a stronger position. The Town would be forced to defend litigation or other claims if the Town's assets are exposed. In contrast, because the subsidiary would be a separate corporate entity and the Town's liability is limited, the Town may adopt a different strategy for disputed claims because its assets are not exposed.

### ***Maintaining the Corporate Veil***

It should also be noted that to maintain liability protection via creation of a subsidiary, it is important to ensure that the corporate veil is not pierced. Courts have concluded that piercing of corporate veil is very difficult to do as “[t]ypically, the corporate veil is pierced when a company is



incorporated for an illegal, fraudulent or improper use.”<sup>17</sup> Having said that, where there is lack of independence in decision-making in the subsidiary, a perception is created that the parent and subsidiary are not independent. Such perception can lead to lawsuits against the parent company, which may ultimately be unsuccessful, but still require Town resources to defend. Thus, it is advisable to maintain separation between the parent and subsidiary.

With respect to BMAHC, we have not identified any risks of the corporate veil being pierced by a Court, thus the Town would be protected from liability from development risks if the development were to be at the BMAHC level. It is, though, advisable to consider the perception of independence of BMAHC in light of the control that the Town has through its voting rights under By-law 1 and the intertwining of the entities described in our discussion on the MOU.

It is worth noting that BMAHC ability to follow private sector arrangements to the logical conclusion of incorporating a subsidiary for each project is thwarted by Subsection 18(1) of O. Reg. 599/06.

## **2. Political Participation**

The range of opinion as to how much political participation is to be included in a development subsidiary’s decision-making processes is remarkable and points to the conclusion that municipalities have different tolerances for allowing unelected board members to control how housing is delivered. Some subsidiaries have boards entirely composed of elected officials (e.g. Housing York), some of have no elected officials (e.g. London HDC) and others have some elected officials (e.g. Toronto Community Housing). Entities such as BMAHC follow the hybrid model, where they are overseen by independent board of directors that have members of the community and politicians on their boards appointed by the municipality.

The advantage of having decisions made by politicians is that these individuals represent the community and have an understanding of the priorities of their constituents and the accountability lines are very clear. Such understanding is especially important where taxpayer funds are used for a project as any monies used for one purpose means that the same monies cannot be used elsewhere.

The challenge with having all decisions go through the political prism is that =it is often difficult to construct a skills-based board capable of governing a development enterprise which requires experience in pro formas, managing real estate portfolios, executing development projects and administering tenancies.

In the case of BMAHC, there currently are both political and non-political perspectives at the board level, thus providing for both political and non-political matters to be more easily brought forward. At the board level, the directors, whether Councillors or Citizen Members, all have the same powers and obligations, including fiduciary duties to the corporation.

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<sup>17</sup> 642947 Ontario Ltd. v. Fleischer, 2001 CanLII 8623 (ON CA) at para. 68.





Although not involved in the board decision-making, the Town also exerts significant control over the board of director through its appointment powers as it controls the majority of votes via its membership class.

It should be noted that the board composition is dictated by By-law 1. As mentioned previously, By-law 1 is silent with respect to the number of non-politician board members there should be. It is recommended that the By-law be amended to specifically provide for citizen members to be on the board of directors.

### ***Councillor and Director***

One caution that we would point out is that it is sometimes difficult for politicians to wear two hats – that of the director with a fiduciary duty to the corporation and that of the politician who is accountable to their constituents. In such cases, the director has to be cognizant of the hat they wear at the board level, and the fiduciary duties that come with the role. At the council level, when issues related to BMAHC are debated, the Councillor is not considered to be in a conflict of interest merely as a result of a being on the board of BMAHC. In *Aurora (Town) v. Ontario*,<sup>18</sup> the Ontario Superior Court concluded that a council-appointed director of a non-share capital corporation is not deemed to have an indirect pecuniary interest under the *Municipal Conflict of Interest Act*<sup>19</sup> when council is considering a matter related to the corporation.

### **3. Risk Aversion of Municipalities**

Municipalities are risk averse by design. Municipalities are used to being regulators and the decision-making process is legislative in nature, rather than transactional. It is not to say that municipalities cannot develop as both Peel and Toronto, for example, manage aspects of housing development internally. However, a subsidiary offers some useful advantages.

#### ***Faster Decision Making***

A board of directors can make decisions faster because it is not bound to a council cycle and can meet quickly, if needed. It also operates on a much narrower group of issues than a municipal council. Having fewer items to manage allows the board of directors to be more focused on the development project and make decisions more expediently.

#### ***Understanding Risk***

As a board of directors can be more focused on a development project than a Town Council, the board of directors would have a better understanding of the overall risk profile of the project. We elaborate on governance below. Such understanding of the risk allows the board to make more informed decisions on risk, which usually results in it being less risk averse.

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<sup>18</sup> *Aurora (Town) v. Her Majesty the Queen in Right of Ontario*, 2013 ONSC 6020 (CanLII).

<sup>19</sup> *Municipal Conflict of Interest Act*, RSO. 1990, c. M50.





A risk-averse decision-making process does not bode well in the development context where decisions need to be made quickly and often involve taking on calculated risks. Delays in decision-making can directly lead to slippage of project timelines and extra costs.

### ***A natural tension with the Regulator***

A municipality governing its own development is faced with having to approve its own projects from a planning perspective. The result in our experience tends to be the undervaluation of land. All developments require unabashed champions to promote their cause and push the regulators within the municipality to understand their vision. This is a more natural fit where the development champion is not on the same organizational chart as the planning regulator.

## **4. Governing Development and Construction: A Skill-Based Board**

Focused governance is one of the most often cited advantages to a development subsidiary. The Town can determine the number of directors for the board of the subsidiary and can tailor its composition.

A diverse composition of the board of directors can be a strength in that diverse perspectives are applied to the challenges of the subsidiary. Development is its own discipline and decisions can be material financial commitments. A board of directors geared to development could be more weighted to development expertise allowing more focussed and knowledgeable attention on such matters. Expertise in the following areas should be considered for such a board:

- Real Estate Development;
- Real Estate Finance;
- Planning and Design; and
- Attainable and Affordable Housing.

Having a separate board does not mean that the Town will not have control and oversight over the entity. As can be seen through the BMAHC governance structure, the Town, through the members, has the power to appoint and to remove the board of directors.

By contrast, a Town Council as a governing body will only have the requisite expertise to govern if, by chance, a slate of councillors are elected with similar skill-sets.

When we speak of governance, consider two roles that a governing body ought to be able to play. First, a governing body ought to be able to set direction for the organization (i.e. establish its vision and mission). Town Council is clearly able to do that and can continue to set out general parameters through the mechanisms below. A second important function is more defensive: it must be able to identify risks the management team is missing or assumptions that may be incorrect. A skills-based board will usually be better placed to fulfill this function.

Once appointed to the board, each individual director owes a fiduciary duty to the corporation which requires directors to act in good faith and in the best interests of the corporation at all times and, to this end, must act reasonably with the skill and diligence of a reasonable person, and to



avoid conflicts of interest.<sup>20</sup> While it is expected that the interest of a corporation would align with the Town, on rare occasion that could not necessarily be the case. In the rare event that a conflict happens, the director is required to side with the interests of the corporation and not its members.

### **3. Ability to Mortgage**

One concern with the municipality managing development directly is that regulations passed pursuant to the *Municipal Act* explicitly prohibit a municipality from mortgaging its land.<sup>21</sup> While the municipality is restricted from mortgaging land, nothing in the *Municipal Act*, its regulations, or the various legal texts on municipal law in Ontario state that a subsidiary corporation is bound by the same restrictions.

We have attached our analysis, including limitations, as Appendix A to this memorandum.

### **4. Land Ownership and Financing**

Development projects often require financing from third parties. The ownership of land can determine the type of financing available. As a general principal it is easier to obtain financing against a freehold parcel of land, then one that is leased. The reasons for that are that lenders do not have to understand the lease and they know that. Also, should they have to sell the property to recover their debt, they do not have to worry about a tenant. They also know that in the event of tenant getting into financial difficulty, there will not be competing claims between the Town as landlord and the lender as mortgagee.

However, there is no question that it is legally possible to borrow money based on the security of a long term lease. The matter of competing claims is resolved through a “Three Party Agreement”, which includes the Landlord, Tenant and Mortgagee. Indeed, we can point to several examples of that arrangement. The arrangement also has the added benefit of not having the land sold out of the public sector on a default. Rather the lender takes over the leasehold interest and can only sell the balance of the tenancy to a third party.

It is not difficult to see why lending underwrites will prefer a freehold arrangement.

### **5. Contracting confidence in the private community**

A subsidiary focused on development may be better able to attract high-quality developers and partners in the private sector than a municipality, which has many ongoing pursuits.

Partnership with the private sector has been used by other housing providers to develop land and build more affordable housing. The advantages of using private-sector partners include leveraging their expertise, borrowing capacity, and relationships.

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<sup>20</sup> There are no statutory provisions in the *Corporations Act* which parallel the fiduciary duty provisions contained in the *Business Corporations Act* (Ontario). However, Section 71(4) of the *Corporations Act* refers to this duty in an indirect manner. We are of the view that similar duties apply to directors under both acts, but have not completed fulsome research into this point.

<sup>21</sup> O.Reg 276/02, Bank Loans, s. 4(2).



## **6. Debt Consolidation**

Ontario municipalities are subject to debt and financial obligation limits under *Ontario Regulation 403/02*. All debt for the development project will be consolidated in the subsidiary, making it easy to account for and separate, where permissible under accounting rules. However, in the event that the subsidiary raises funds through secured lending against its real property and the commercial lender is not solely satisfied with the subsidiary's covenant, the Town may be required to guarantee the subsidiary's debt. Such guarantee will likely impact the debt limits of the Town, if any.

## **7. Accounting Convenience**

Different corporations will maintain separate balance sheets for the assets and liabilities of the entities. Of course, they can also be stated on a consolidated basis. A subsidiary focused on development allows for easy segregation of expenses and capitalizing costs where possible.

Keeping separate balance sheets and/or separate bank accounts for the subsidiary can also negate arguments that the subsidiary is not a separate entity from the Town. Such arguments may arise if a third-party in litigation with the subsidiary is trying to "pierce the corporate veil" of the subsidiary to attempt to include the Town as a party to said litigation.



## APPENDIX A

### 1. The Statutory Powers of a Non-Share Capital Corporation allow Mortgaging

The ability to incorporate is derived exclusively from statute as it does not exist at common law. Furthermore as a creature of statute, a corporation's powers must be set out in its incorporating legislation.

Section 118 of the *Corporations Act* allows for the incorporation of a non-share capital corporation in the Province of Ontario and pursuant to section 126.1, a non-share capital corporation is granted with "the capacity and, subject to this Act, the rights, powers and privileges of a natural person" [emphasis added]. As the powers of a natural person include the ability to mortgage one's property, such ability can only be limited by a restriction contained in the *Corporations Act*.

Upon review, the *Corporations Act* includes one restriction with respect to granting a mortgage over the corporation's property. In order to mortgage a corporation's property, the directors must first pass a by-law authorizing such borrowing powers. This statutory limit is in addition to any restrictions which may be found in the letters patent of a non-share capital corporation.

A review of BMAHC's by-laws confirms that it has the borrowing authority via By-law 2.

### 2. Municipal Service Corporations and Mortgaging

As mentioned previously, the activities of a Municipal Service Corporation are restricted by Section 18 of *Ontario Regulation 599/06*. After reviewing this regulation, which contains restrictions on the actions of a Municipal Services Corporation including that it cannot act as an incorporator of another corporate body and it may only invest in prescribed securities, we are able to conclude that Section 18 does not prohibit a Municipal Services Corporation from mortgaging its land.

In addition to our review of the legislation and its regulations, we reviewed textbooks and other secondary resources respecting the Municipal Act. While there was not an express statement that a municipal subsidiary can mortgage property, the restrictions discussed in these texts did not reference a prohibition on mortgaging property. In fact, these textbooks state that a Municipal Services Corporation is entitled to borrow money and that one of the underlying policy objectives of a Municipal Services Corporation is to increase opportunities for public/private partnerships and to involve private sector partners in the financing and undertaking of public projects through business corporations.

Based on our review of the above-noted legislation, regulations and secondary resources, we are not able to identify a restriction on the right of an subsidiary to mortgage property.

Please note that the issue of whether a Municipal Services Corporation can mortgage, while the municipality cannot, has not been tested by the Courts, who may consider the limitations on the



municipality to mortgage in relation to delegating this authority to a subsidiary. Thus, our interpretation does not have the benefit of judicial review.