



**Report of the Auditor General
of the Ville de Montréal**
to the City Council and to the
Urban Agglomeration Council

For the Year Ended December 31, 2014

4.3

**PARTICIPATION OF THE
SOCIÉTÉ DE TRANSPORT
DE MONTRÉAL IN THE
SOCIÉTÉ DE GESTION
ET D'ACQUISITION
DE VÉHICULES ET DE
SYSTÈMES DE TRANSPORT**



Table of Contents

1. Introduction	67
2. Purpose and Scope of the Audit.....	70
3. Summary of Findings	71
4. Detailed Findings and Recommendations	72
4.1. Legal Compliance of the Partnership Agreement to Form AVT.....	72
4.2. AVT's Management Mandate	75
4.3. Proposed Amendment to the <i>Act Respecting Public Transit Authorities</i>	81
4.4. Governance and Accountability Reporting.....	85
5. General Conclusion.....	92

List of Acronyms

APTA	<i>Act respecting public transit authorities</i>	MAMOT	Ministère des Affaires municipales et de l'Occupation du territoire
ATUQ	Association du transport urbain du Québec	MTQ	Ministère des Transports du Québec
BD	Board of Directors	STM	Société de transport de Montréal
CCQ	Civil Code of Québec		
GUAA	Gestion unifiée des acquisitions d'autobus		

4.3. Participation of the Société de Transport de Montréal in the Société de Gestion et d'Acquisition de Véhicules et de Systèmes de Transport

1. Introduction

The Société de transport de Montréal (STM) is part of the reporting entity of Ville de Montréal (the City) and therefore, in keeping with the *Cities and Towns Act*, falls within the scope of the Bureau du vérificateur général as a legal person that must be audited. The City controls the appointment of all members of the STM's Board of Directors (BD) and is responsible for losses generated by the STM in its operation.

Under section 107.8 of the *Cities and Towns Act*, we conducted a compliance and management audit of the STM's participation in the Société de gestion et d'acquisition de véhicules et de systèmes de transport S.E.N.C. (AVT).

Background

AVT was created on April 1, 2010 by Quebec's nine public transit corporations "the partners". They ratified both AVT's partnership agreement and a management mandate entrusting AVT with responsibility for various activities. The STM holds 20% of the voting rights for decisions made within AVT.

AVT's partnership agreement is in force for the period from April 1, 2010 to January 1, 2020, after which it will be renewed automatically for another 10-year term, and so on. The contract specifies that part of its mandate is to:

- develop and share expertise in public transportation with the partners, in particular by conducting any studies that will be of benefit to them, by managing bus purchase contracts and by developing the technical and contractual documentation necessary for awarding purchase contracts;
- acquire all services and goods associated with all modes of public transportation;
- carry out, for the benefit of its members, any commercial activity related to public transportation.

The current management mandate entrusted to AVT focuses mainly on the following three areas:

- **Contract management**, which in particular involves monitoring compliance with delivery schedules, the final inspection of buses before they are delivered to public transit

corporations and processing of non-compliances. AVT manages four bus purchase contracts that were ongoing when the mandate was signed. AVT also manages tendering contracts for the unified acquisition of urban buses for the 2012-2015 period;

- **Management of tendering activities leading to the acquisition of urban buses by the partners for the 2012-2015 period**, which in particular involves preparing the documents required for calls for tenders, conducting the analyses required for awarding contracts and testing pre-series buses;
- **Technology watch and technical studies**, which are aimed at sustaining the progress achieved by the partners and improving vehicle performance, reliability and safety for buses and other transportation vehicles.

This new general partnership offers partners the services that were previously offered by the STM through two administrative units, namely the Gestion unifiée des acquisitions d'autobus (GUAA) team and the Bureau de projets.

In the past, the STM created the GUAA team within its organization to represent the nine partners when dealing with bus manufacturers throughout the bus manufacturing process and the ensuing warranty period to ensure both the quality of the buses manufactured and compliance with bus manufacturers' obligations.

In addition, the STM set up a Bureau de projets mandated to prepare documentation for the purchase of articulated buses and to carry out a technology watch. The activities of the Bureau de projets ended on December 31, 2008.

Governance of AVT is assured by a BD consisting of five members elected every year by the general meeting of partners, which is attended by the nine partners' directors general or their designated representatives. The administrative power of AVT's BD is limited to simple administrative decisions. Partners are responsible for all full administrative decisions, such as disposal of assets and certain other decisions expressly referred to in the partnership agreement (the partners' BD or the general meeting of partners).

Each partner's BD:

- approves, prior to publication of a call for tenders, criteria for evaluating and weighting the call for tenders, duration and renewal options, the quantities of vehicles purchased by its corporation and the maximum authorized amount for the contract;
- mandates the BD of another partner to award the contract to a supplier in accordance with the contract awarding rules provided for in the call for tenders. AVT does not award contracts on behalf of partners;
- authorizes loan by-laws for its corporation.

The contributions made by the STM to AVT are accounted for in the STM's financial statements as investments in AVT under the item "Other receivables". These contributions, totaling \$719,000 per year, are authorized by a resolution of the STM's BD on the same budget basis for the years 2011 to 2015.

Any AVT surplus or shortfall is prorated and allocated to each partner based on each partner's contribution during the fiscal year in question. This division affects the cost of the investment in AVT presented in the STM's financial statements. As of December 31, 2013, the STM's investment was \$395,000.

Furthermore, the partnership agreement provides that contributions are adjusted periodically to take into account buses that were actually purchased. At the end of the five-year term ending on December 31, 2015, the adjusted contributions will be paid to or recovered from AVT.

The minutes of both AVT's BD meetings and its general meeting of partners for the years that we examined, namely 2012, 2013 and the first half of 2014, show that several discussions focused on the "mandate improvement" issue concerning the mandate granted by the partners to AVT. The purpose of the proposed amendments is to broaden AVT's mandate.

In this regard, according to information that we obtained on May 1, 2014:

- No amendment will be made to the mandate that the partners granted to AVT without the prior authorization of each partner's BD;
- On December 5, 2013, the directors general of the nine partners confirmed the amendments that they propose to make to the mandate;
- AVT wants the subcommittee on AVT's mission and responsibilities to hold an initial meeting before finalizing the mandate improvement process to ensure that no new issues will arise in connection with the mandate. Should any new issues arise, they must be the subject of new discussions within this committee.

Furthermore, before AVT's partnership agreement came into force, a request for an amendment to the *Act respecting public transit authorities*¹ (APTA) was sent to the Ministère des Transports du Québec (MTQ) on February 15, 2010 by the Association du transport urbain du Québec (ATUQ) on behalf of the nine partners. The purpose of the request was to specify and clarify the legislative provisions that expressly permit the nine partners to

¹ CQLR, chapter S-30.01.

constitute a legal person that can render services to third parties for remuneration, thereby facilitating a decrease in costs associated with services rendered to partners.

AVT's minutes highlight a potential impact on Transgesco Limited Partnership, which was incorporated by the STM, since the wording of the section of the act proposed by the Ministère des Transports du Québec and by the Ministère des Affaires municipales et de l'Occupation du territoire (MAMOT) could cover any entity incorporated by a public transit authority.

2. Purpose and Scope of the Audit

The purpose of this audit was twofold: first, to ensure that the processes associated with the STM's participation in AVT and in Transgesco Limited Partnership are consistent with the legal foundations established and, second, to ensure that an adequate governance and accountability reporting process was introduced and put in place at the STM with respect to its participation in AVT.

More specifically, our audit was aimed at evaluating the following criteria for the STM's participation in AVT:

- AVT's partnership agreement is legally compliant;
- The risks associated with AVT's management mandate are properly evaluated;
- The impact of the proposed amendment to the APTA has been evaluated;
- The STM has provided for an effective governance structure for its participation in AVT.

Our audit was conducted from July to November 2014 and focused chiefly on the years 2012, 2013 and the first half of 2014 but includes references to previous years as well.

Our audit focused on the STM, mainly its Direction générale and its Direction executive – Affaires juridiques. Some of the information on AVT was also obtained during the audit made of the STM's financial statements on December 31, 2013 to help confirm our understanding.

At the end of our audit, a draft report was submitted for discussion purposes to the acting Director General, the Secretary General and Executive Director – Legal Affairs and the representative designated by the STM to deal with AVT. A final report was subsequently submitted to both the acting Director General and the Secretary General and Executive Director – Legal Affairs to obtain an action plan and timeframes for its implementation for each of the recommendations addressed to them.

3. Summary of Findings

Our audit work revealed that improvements need to be made in the following areas:

- The legal compliance of AVT's partnership agreement (section 4.1):
 - The APTA does not expressly provide that public transit corporations are entitled to join forces to form a general partnership for contract management purposes;
 - AVT has ratified contracts with third parties even though questions remain about its legal capacity to contract on behalf of partners.

- AVT's management mandate (section 4.2):
 - The APTA does not expressly provide that the partners, including the STM, are authorized to award mandates to AVT without calls for tenders;
 - No presentation on any formal process for determining risks associated with the STM's participation in AVT, especially risks associated with the continuation of contracts already awarded to third parties by AVT, was given to the STM's BD or any of its committees;
 - AVT's partnership agreement allows it to carry out, for the benefit of its members, any commercial activity related to public transportation. At present, only four of the nine public transit corporations, including the STM, are permitted under the APTA to offer services for remuneration to third parties. Since there are certain requirements for a general partnership in its operating rules, one of which is that a partner does not have the right to compete with the corporation of which it is a member, the STM's participation in AVT prevents it from offering services for remuneration to third parties, which in turn prevents it from being allowed to increase its non-tariff revenues, until such time as the APTA authorizes the other five partners participating in AVT to exercise this power;
 - The interpretation of contractual clauses governing the lending of STM employees to AVT raises questions.

- Proposed amendment to the *Act respecting public transit authorities* (section 4.3):
 - Transgesco Limited Partnership does not apply in full the contract rules provided for in the APTA.

- Governance and accountability reporting (section 4.4):
 - No structured mechanism is in place for:
 - identifying and updating the background information on the STM's participation in AVT (main issues, accountability reporting to the STM's director general and to the STM's BD or one of its committees, STM resolutions, etc.),

- monitoring the STM's participation in AVT,
- maintaining and keeping up to date comprehensive documentation on the governance tools provided for in both AVT's partnership agreement and its management mandate.

4. Detailed Findings and Recommendations

4.1. Legal Compliance of the Partnership Agreement to Form AVT

4.1.A. Background and Findings

As stated in the partnership agreement, the nine partners formed AVT, a general partnership, in order to:

- develop and share expertise in public transportation;
- acquire services and goods associated with any mode of public transportation;
- carry out, for the benefit of its members, any commercial activity related to public transportation.

The law establishing these nine public transit corporations, namely the APTA, sets out the rules governing their engagement in all the activities that they may wish to consider. A general partnership such as AVT, without being a legal person within the meaning of the law, acts in its own name and owns property in its own right, which is separate and distinct from that of the corporations that constitute it.

Because of its legal form (general partnership), AVT's legal capacity has been challenged regularly since its creation by several stakeholders, as reflected in legal opinions dealing specifically with this issue, and by the fact that its Board of Directors set up a study committee on AVT's legal status and role.

In this regard, the minutes of the general meeting of AVT's partners, in connection with the meeting of February 21, 2013, state:

[TRANSLATION] [...] that it would be appropriate to embark on a reflection process to ensure that AVT, with its legal form and mandate, is able not only to fulfil its current role, but also can get to where the corporations want to see AVT in a few years.

We noted that the APTA does not expressly grant to public transit corporations the power to join forces to form a general partnership for contract management purposes.

In fact, according to a law firm we consulted, a literal, restrictive interpretation of section 89 of the APTA would make it possible to claim that the mandate entrusted to AVT by the nine partners would exceed the powers that are conferred on it by the law, because AVT is not a legal person established in the public interest within the meaning of this provision.

However, it could be argued that the general rules of civil law allow public transit corporations to constitute a general partnership. In fact, under section 300 of the Civil Code of Québec (CCQ), the APTA, as the incorporating law, governs the activities of public transit corporations; the CCQ provisions, if any, will be applicable as a supplement to the APTA provisions. Others might argue that AVT is only a grouping together or extension of the partners in their capacity as legal persons established in the public interest.

It should be recalled that section 89 of the APTA reads as follows:

A transit authority may give any other legal person established in the public interest the mandate to acquire property or any service on its behalf.

The transit authority may accept such a mandate from the legal person where it intends to acquire property or any service for itself.

The mandates given under this section shall be given by gratuitous title. The Minister may authorize the transit authority to make a purchase referred to in this section without any formal contract awarding procedure.

At present, some uncertainty remains that the interpretation of section 89 of the APTA might be prejudicial to the security of the STM's commitments arising directly or indirectly from AVT activities.

Consequently, it is our opinion that, because of AVT's legal form and the nature of its current management mandate, AVT should refrain from awarding any contracts as the partners' agent until its legal capacity is clarified with respect to its power to contract on behalf of partners.

Certain legal opinions expressed in 2010 and 2012 diverge as to AVT's legal status and as to whether it has the legal capacity to conclude contracts independently of its partners. In our opinion, the senior management of the STM, as a partner of AVT, must decide upon and agree upon the STM's position and vision concerning its participation in AVT. This lack of a clear position makes it difficult for the STM to determine risks arising from its participation in AVT and to establish procedures in an informed manner that will enable it to mitigate such

risks. The positioning would also help the partners set clear guidelines for AVT's senior management regarding the limits of its activities.

Moreover, a document entitled "Rôle et mission d'AVT" [TRANSLATION: "Role and Mission of AVT"], which AVT's director general submitted to the presidents of the transit corporations on February 13, 2014, specifies that [TRANSLATION: "all activities are always carried out jointly with the corporations"] and that services provided to third parties are among AVT's main activities. The document specifies the three conditions that must be present in order for AVT to be able to provide services to third parties:

- Must be approved by AVT's BD;
- Ancillary activity (priority given to partners);
- Minimum profit of 15%.

Moreover, AVT's 2013 annual management report states that:

[TRANSLATION] AVT's main clients are Quebec public transit corporations. However, AVT also offers its services to other public transit organizations and public bodies [...] As a result of our business development efforts, AVT has exceeded its objectives in the area of obtaining external contracts.

While the concentration of expertise in public transportation in AVT may well be a sound practice in terms of management and use of the STM's and the other eight partners' resources, the vehicle chosen to do this raises questions.

4.1.B. Recommendation

We recommend that the Direction générale of the Société de transport de Montréal:

- **decide upon the legal compliance of AVT and agree with both its senior management and the other eight partners upon the position and the vision of the Société de transport de Montréal concerning its participation in AVT;**
- **set clear guidelines for AVT regarding the limits of its activities, particularly in the area of services offered to third parties.**

Business unit's response:

*[TRANSLATION] Compile various legal opinions about the incorporation of AVT.
(Planned completion: June 2015)*

Obtain from AVT's BD the revised mandate that will be entrusted to AVT to follow up on the legislative amendments under way. (Planned completion: following the coming into force of the legislative amendment)

Have this mandate approved by the STM's BD. (Planned completion: following the coming into force of the legislative amendment)

4.1.C. Recommendation

We recommend that the Direction générale of the Société de transport de Montréal ensure that AVT does not conclude contracts on behalf of partners until AVT's legal capacity to contract on behalf of partners is clarified.

Business unit's response:

[TRANSLATION] Obtain confirmation from AVT that no contracts were concluded on behalf of transit corporations. (Planned completion: June 2015)

4.2. AVT's Management Mandate

4.2.1. AVT Partners' Compliance with Rules for Awarding the Management Contract

4.2.1.A. Background and Findings

Sections 93 and 95 of the APTA provide that any contract for the supply of material or materials involving an expenditure of \$100,000 or more may be awarded only following a call for tenders issued through an advertisement published in a newspaper distributed on the territory of the corporation.

However, under paragraph 2 of section 101.1 of the APTA, a public transit authority is not required to follow the rules for awarding contracts provided for in sections 93 and following for contracts concluded with a public body within the meaning of the *Act respecting access to documents held by public bodies and the protection of personal information*.²

Monetary contributions other than seed capital are paid by the partners to AVT under mandates entrusted to AVT and are determined on the basis of the number of buses that each partner plans to purchase in the course of a year. These biannual contributions, provided for in AVT's partnership agreement as well as in the management mandate entrusted by the partners to AVT, serve to finance the duties provided for in the management mandate.

² CQLR, chapter A-2.1.

We observed that these contributions were made by partners to AVT without any form of tendering process, considering that AVT would qualify as a public body within the meaning of the *Act respecting access to documents held by public bodies and the protection of personal information*, given its legal nature.

According to some legal opinions, AVT is authorized to carry out mandates on behalf of partners without these mandates first being subjected to a tendering process.

However, a report produced by the Auditor General of the Ville de Lévis in March 2014 calls this conclusion into question.

While this observation concerns the Société de transport de Lévis, we believe that it also applies to the STM, as shown by this excerpt from the report:

[TRANSLATION] The argument advanced to explain this absorption is as follows: AVT, through its general partnership status, constitutes an outgrowth, in other words a prolongation or extension of the transit corporations that incorporated it. To summarize this argument, AVT does not constitute an entity separate from the corporations that created it.

I disagree with this interpretation. First, aside from any legal argument, this concept is difficult to imagine [...], mainly for the following reasons:

- *the STL [and the STM] has practically no control over this corporation; as a partner, it has only two votes out of fifty for the STL and ten votes out of fifty for the STM;*
.....
- *each and every partner of AVT, namely the nine transit corporations governed by the APTA, the STL [and the STM] falls under a municipal auditor general's jurisdiction, is subject to accountability requirements and a public decision-making process and, finally, is administered mostly by elected officials of its City, which is manifestly not the case with AVT.*

Second, it is worth recalling that, in 1997, a similar case was the subject of a judgment involving the Montreal airport. Without going into details, what emerges from this judgment is that an organization may be declared "public" only on the condition that the law declares it public, or that this status is derived from the law by necessity in view of its intended purpose. In other words, it is not because public bodies have decided to acquire the status of a general partnership that they acquire this status de facto.³

In view of the uncertainty surrounding the public body status attributed to AVT, we think that there is a risk that a court may conclude that AVT does not have all the necessary characteristics to qualify as a public body. If the interpretation adopted by the STM and its

³ *Rapport occasionnel 2014 à la Société de transport de Lévis*, Auditor General of Lévis, p. 30-1.

partners is not likely to stand up in court, some contracts awarded by the partners to AVT might be terminated by a court of competent jurisdiction if they are contested.

4.2.1.B. Recommendation

We recommend that the Direction générale of the Société de transport de Montréal ensure that AVT qualifies and is recognized as a public body in order to reflect the spirit of sections 93, 95 and 101.1 2 of the *Act respecting public transit authorities*.

Business unit's response:

[TRANSLATION] Pending developments in the legislative amendment proposed by the MTQ. Obtain from AVT follow-up on the legislative amendments under way. (Planned completion: May 2015)

4.2.2. Risks Associated with the Participation of the Société de Transport de Montréal in AVT

4.2.2.1. Financial Risk

4.2.2.1.A. Background and Findings

AVT's partnership agreement concluded among the nine partners contains certain financial rights and obligations for AVT and the nine partners.

In particular, the agreement provides that each partner must make a cash contribution every year as payment of AVT's obligations; the amount paid is determined in proportion to the number of buses that each partner plans to purchase during the year. The amount payable is determined every year by AVT's BD.

The agreement also provides that AVT's profit or shortfall is prorated and allocated to each partner based on each partner's contribution during the fiscal year in question. Similarly, if AVT's financial situation requires it, its treasurer might request an additional special contribution from the partners.

Moreover, according to a law firm we consulted, non-compliance with the contract awarding rules that may be applicable, according to the legal status to be defined by AVT involves certain risks, which are explained in this excerpt from a legal opinion we received:

[TRANSLATION] When a non-profit corporation or a legal person is constituted by a public body for the purpose of entrusting it with some of its duties, this corporation

might be required to comply with contract awarding rules, which are public. In concrete terms, a supplier who is dissatisfied with the awarding of a contract by mutual agreement to a competitor could support the application of tendering rules by relying on the principle that no one is supposed to do indirectly what he or she does not have the right to do directly.

We did not track down any risk analysis prepared by the STM with respect to its participation in AVT. Consequently, it appears that no formal presentation on risks faced by the STM and steps taken to mitigate them, if any, was made to the STM's BD or one of its committees.

Furthermore, we noted that the minutes of AVT's BD produced following the meeting held on June 13, 2014 report the following:

[TRANSLATION] Based on the secretaries' committee's recommendations, the presidents remarked that AVT should not accept new external contracts until the Act respecting public transit authorities is amended [...] Nonetheless, the presidents accept nonetheless that the corporation [AVT] is continuing contracts that are already under way.

We were not able to find any evidence that members of the STM's BD or one of its committees are truly aware of the risks the STM would face if any irregularities arise in connection with ongoing contracts with third parties or in connection with all completed contracts that have been awarded to third parties by AVT and for which the STM might be a stakeholder.

In our opinion, a thorough knowledge of the issues and the associated past, present and future risks is essential in order for the members of the STM's BD to be able to make informed decisions about AVT.

It is our opinion that determination of the major risks and the steps taken to mitigate them would provide reassurance to the STM officers responsible for governance concerning its participation in AVT. These governance mechanisms will be discussed in greater detail in section 4.4 of this audit report.

4.2.2.1.B. Recommendation

We recommend that the Direction générale of the Société de transport de Montréal determine the main risks associated with its participation in AVT, including those associated with the continuation of contracts already awarded to third parties by AVT, and present, to its Board of Directors or one of its committees, the steps taken to mitigate these risks.

Business unit's response:

[TRANSLATION] Evaluate the advantages, disadvantages and risks of participating in the new entity that will be created. (Planned completion: following the coming into force of the legislative amendment)

Recommend that the STM's BD create a framework for the delegation of its representative's powers to AVT's BD (i.e., monetary limitation of commitments). (Planned completion: following the coming into force of the legislative amendment)

Presentation of this governance to AVT's BD by the STM representative. (Planned completion: following the coming into force of the legislative amendment)

4.2.2.2. Risks of Losing Business Opportunities for the Société de Transport de Montréal

4.2.2.2.A. Background and Findings

[TRANSLATION] The nine transit corporations formed a general partnership for the purpose of "carrying out, for the benefit of its members, any commercial activity related to public transportation".⁴

The minutes of the meeting held on June 13, 2014 by AVT's Board of Directors indicate the following:

[TRANSLATION] Based on the secretaries' committee's recommendations, the presidents remarked that AVT should not accept new external contracts until the Act respecting public transit authorities is amended to allow the nine corporations to render services to third parties for remuneration [...] The members discuss possible options available to help corporations avoid losing contract opportunities while ensuring that AVT does not go against the will expressed by presidents.

At present, the APTA permits only four public transit corporations, including the STM, to offer, as of December 31, 2001, certain goods and services associated with public transportation for remuneration.

In February 2010, the partners made a request for a legislative amendment so that the five other corporations that formed AVT can benefit from the same privilege of being allowed to offer their services for remuneration to third parties.

⁴ Section 1.03 of AVT's partnership agreement.

Since a general partnership contains certain requirements in its operating rules, one of which is that a partner does not have the right to compete with the corporation of which it is a member, the STM's participation in AVT prevents it from offering services for remuneration to third parties and from being able to increase its non-tariff revenues until the APTA grants this same privilege to the other five partners participating in AVT.

One way in which the STM could exercise the right that is conferred upon it under the APTA would be to request an amendment to this end to the law establishing AVT.

4.2.2.2.B. Recommendation

We recommend that the Direction générale of the Société de transport de Montréal, pending a favourable outcome of the request for a legislative amendment, explore other avenues for enabling the Société de transport de Montréal to offer its services for remuneration to third parties and thereby increasing its sources of non-tariff revenues.

Business unit's response:

[TRANSLATION] Verify the appropriateness of amending the agreement to form the general partnership to ensure that AVT has no exclusive rights in this area, in view of the future legislative amendment and given the fact that, for the moment, AVT may not sell its services to third parties. (Planned completion: June 2015)

4.2.3. The Lending of Employees by the Société de Transport de Montréal to AVT

4.2.3.A. Background and Findings

Our audit revealed that there were agreements both between the unions of the STM and AVT and between the STM and AVT concerning invoicing for the use of the STM's staff by AVT.

Section 2.03 of AVT's contract provides as follows:

[TRANSLATION] [...] The Partner that lends an employee to AVT shall continue to pay the employee their salary and assume any other expenses incurred by the contract of employment associated with the lending of the employee, such as costs associated with fringe benefit programs, which amounts, salaries and other costs, shall be reimbursed by AVT to the Partner. Throughout the period in which they perform duties for AVT, employees on loan shall maintain their employment relationship with the Partner as well as the working conditions they had with the Partner, and they may return to work at any time for the Partner [...]

We noted that the interpretation of contract clauses associated with the lending of the STM's employees to AVT raises certain questions concerning both AVT and the STM.

Correspondence exchanged between AVT managers and STM managers in March 2013 and September 2014, shed light on such questions as whether or not employees on loan to AVT from the STM are included in the authorized staff in STM budgets, and whether or not they maintain their employment relationship with the STM if they stop working for AVT.

The correspondence also shows that there is no clear dividing line between the STM and AVT concerning management of STM staff working for AVT.

Consequently, even though AVT was created on April 1, 2010, questions were still being asked in September 2014 about interpretations regarding the management and invoicing of employees on loan from the STM to AVT.

4.2.3.B. Recommendation

We recommend that the Direction générale of the Société de transport de Montréal establish a clear policy or guideline regarding management of the human resources covered by the agreement between the Société de transport de Montréal and AVT in order to provide a better management framework for the managers concerned.

Business unit's response:

[TRANSLATION] Check the existing management frameworks. (Planned completion: June 2015)

4.3. Proposed Amendment to the Act Respecting Public Transit Authorities

4.3.1.A. Background and Findings

In its preamble, AVT's partnership agreement states that its chief mission is to provide services to the partners that formed it.

Nonetheless, according to the information that we gathered, the partners expressed the intention to request that AVT be allowed to provide services for remuneration to third parties (namely, clients other than the partners that created it).

One of the arguments advanced is that AVT has cutting-edge expertise that could be of interest to other public transit corporations or public bodies, either inside or outside Quebec.

At the request of the nine partners, the ATUQ sent a letter to the MTQ on February 15, 2010, to request that the APTA be amended so that it specifies and clarifies the legislative provisions that would expressly permit the nine partners to constitute a legal person that can offer services and goods to third parties for remuneration.

The APTA provides that only four public transit corporations (RTC, RTL, STL⁵ and STM) have the power to constitute a legal person to provide their corporate expertise to third parties for remuneration.

The result is that the other five partners that make up AVT cannot use it to sell their expertise to third parties. In fact, this would amount to allowing them to do indirectly what the APTA prevents them from doing directly.

The minutes of the general meeting of AVT's partners, held on March 7, 2014 show that AVT's BD wants to ensure that the legal status and role currently conferred on AVT adequately meet the partners' needs.

The minutes of the meeting of AVT's BD, held on June 13, 2013, show that the MTQ agreed to the request for an amendment to the APTA, but on the condition that the APTA provide that any entity constituted by a public transit authority be subject to the same acquisition rules as public transit corporations and to the *Act respecting access to documents held by public bodies and the protection of personal information*.

Yet the minutes of AVT bring to light the fact that the amendment, such as it is proposed, might be restrictive for the activities of the STM's commercial subsidiary, Transgesco Limited Partnership, because it does not follow the same acquisition rules as corporations governed by the APTA; instead, it is subject to the rules set out in the Agreement on Internal Trade.

A document entitled *10 ans de développement commercial [TRANSLATION: 10 Years of Commercial Development]*, produced in 2013 for the tenth anniversary of Transgesco Limited Partnership, outlines the reasons why it was created:

⁵ RTC: Réseau de transport de la Capitale.
RTL: Réseau de transport de Longueuil.
STL: Société de transport de Laval.

[TRANSLATION] On May 30, 2003, in accordance with the Act respecting public transit authorities, which, since December 31, 2001, has authorized it to offer certain goods and services associated with public transportation for remuneration, the STM adopted a resolution ratifying the creation of Transgesco Limited Partnership that allows it to:

- *make use of a corporate vehicle that gives it flexibility for its business activities;*
- *be protected from contractual and commercial liability;*
- *participate in the orientations and management of subsidiaries;*
- *keep its tax status.*⁶

Its mission is defined in this document as follows: *[TRANSLATION: "To generate revenue, other than tariff revenue, from the commercial potential, assets and resources of the Société de transport de Montréal, while staying true to the STM's mission and improving its customers' transportation experience."]*

The agreement to form Transgesco Limited Partnership defines its purpose as follows:

[TRANSLATION] The purpose of the Transgesco will be to pursue activities that involve managing, administering, operating and developing various partnerships with private sector stakeholders in order to practise all commercial activities related to the enterprise of public transportation pursued by the Société de transport de Montréal and in order to offer, for remuneration, all services and all goods required for the purposes of construction, layout and repair of infrastructures, equipment and rolling stock for all modes of public transportation. In addition, Transgesco will practise any other activity that is supplementary, ancillary or intrinsic to the pursuit of these activities.

Our understanding of section 160 of the APTA is that it explicitly allows the STM itself to provide the goods and services in question or requests the constitution by articles of a legal person in order to offer them. This section stipulates that:

The Société de transport de Montréal is authorized to furnish, for remuneration, all services and goods for the purposes of the construction, laying out or repairing of infrastructures, equipment and rolling stock relating to the subway network and to their management and administration.

It may also request the enterprise registrar to constitute, by articles, a legal person having as an object the providing, for remuneration, of the goods and services referred to in the first paragraph for any mode of shared transportation [...]

This power is conferred primarily on the STM. It can choose to exercise this power through a legal person for which it has requested constitution by articles.

⁶ Transgesco Limited Partnership, *10 ans de développement commercial* [TRANSLATION: *10 YEARS OF Commercial Development*], p. 1.

⁷ *Ibid.*

Consequently, it is our opinion that the services and goods that it is authorized to provide, as well as the issues related to sources of revenue other than tariffs, are an integral part of a transit corporation's operations and that Transgesco Limited Partnership was created in order to protect the STM from contractual and commercial liability.

Moreover, according to the principles established by the Civil Code of Québec, this separate legal personality means that a contract awarded by such a legal person should not be considered a contract awarded by a transit corporation. However, there are exceptions to this general statement. Under some circumstances, as a result of proximity between two organizations it may be concluded that one is in fact the *alter ego* of the other.

Indeed, in the STM's financial statements, Transgesco Limited Partnership is designated as an entity under the STM's control. Consequently, it would be inconsistent, to say the least, for the STM to maintain that:

- AVT, a general partnership, is an extension of the STM and, as such, it could be associated with part of a legal person established in the public interest;
- Transgesco Limited Partnership is a legal person separate from the STM to the extent that it must not be subject to the same tendering rules as the STM.

Therefore, when Transgesco Limited Partnership concludes a contract for the purpose of acquiring goods and services that otherwise should be acquired by the STM for the purpose of meeting its objectives, according to these principles, it may be subject to the obligations pertaining to calls for tenders applicable to public transit corporations provided for in the APTA.

Consequently, it is our opinion that the outcome of the proposed legislative amendment will perhaps not be what some stakeholders expect. The proposed legislative amendment would simply reflect what the current legal reality of Transgesco Limited Partnership appears to be.

We believe that reasonable doubt remains that the rules for awarding contracts followed by Transgesco, which are different from those followed by the STM, cannot be consistent with its legal reality.

Under section 94 of the APTA, any contract involving an expenditure of less than \$100,000, from among the contracts referred to in the second paragraph of section 93, may be awarded only following a call for tenders, by way of written invitation, to at least two insurers, contractors or suppliers, as the case may be.

In creating Transgesco Limited Partnership, the STM entrusted to it certain commercial activities associated in particular with advertising that the STM would itself be authorized to carry out under section 160 of the APTA. In our opinion, in this context, Transgesco Limited Partnership should be subject to the same rules for awarding contracts as the STM. Instead, Transgesco Limited Partnership follows the rules of the Agreement on Internal Trade, which are less demanding since, for expenditures of less than \$100,000, contracts may be awarded by mutual agreement.

For expenditures of less than \$100,000, the creation of Transgesco Limited Partnership would allow the STM to do indirectly what the law prohibits it from doing directly.

4.3.B. Recommendation

We recommend that the Direction générale of the Société de transport de Montréal re-evaluate the interpretation adopted on the contract rules applicable to Transgesco Limited Partnership.

Business unit's response:

[TRANSLATION] Compile legal opinions and management frameworks for the awarding of contracts by Transgesco. (Planned completion: June 2015)

4.4. Governance and Accountability Reporting

4.4.1. Governance Mechanisms at the Société de Transport de Montréal

4.4.1.A. Background and Findings

In this section, we took an interest in the existence and adequacy of governance mechanisms established by the STM to monitor the activities of AVT. It may be worth noting that half the members of the STM's BD, as presented in the 2013 annual financial report, came into office in 2013.

The minutes of AVT's general meeting held on December 5, 2013 report a proposal for a presentation on AVT and its mission to be given to the boards of directors of each of its partners.

According to the information we gathered from STM managers in September 2014, this proposal was not acted on. However, AVT's director general made a presentation to the presidents of the nine partners at a meeting organized by the ATUQ on February 13, 2014.

The annual activity report produced by AVT for the year 2013 is another source of information. The AVT website also contains information on certain indicators under the "espace client" tab reserved for the nine partners.

Notwithstanding the existence of these information tools and documents, we believe that the members of the STM's BD do not have sufficient documentation on the specific nature of the STM's participation in AVT and the monitoring of its activities.

We are of the opinion that it would be appropriate for members of the STM's BD to have a "personalized" presentation portfolio at their disposal. This document could describe more specifically the main issues faced by AVT, compile a history of the main resolutions voted on by the STM's BD concerning this partnership and draw up a history of accountability reporting by AVT to management and to the STM's BD.

This presentation portfolio could also prove very useful when a new designated representative of the STM is appointed to sit on AVT's BD as well as of its general meeting of partners.

4.4.1.B. Recommendation

We recommend that the Direction générale of the Société de transport de Montréal look into the possibility of preparing and keeping up to date an AVT presentation document for stakeholders within the Société de transport de Montréal involved in the monitoring the Société de transport de Montréal's participation in AVT so that they will have a thorough knowledge of the background of the participation of the Société de transport de Montréal in AVT and as a result be able to make a meaningful evaluation of the issues involved and fully exercise their role with respect to the decisions to be made.

Business unit's response:

[TRANSLATION] Prepare a collection of documents:

- *Agreement creating AVT;*
- *Mandate entrusted to AVT;*
- *STM resolution on these documents;*
- *STM resolution on contributions;*

- STM resolution on the STM representative's powers;
- Summary of the STM representative's powers;
- And any other relevant document issued by the STM. (**Planned completion: July 2015**)

4.4.2. Accountability Reporting to the Société de Transport de Montréal

In this section, we took an interest in the existence and quality of an accountability reporting process regarding the STM's participation in AVT.

4.4.2.1. Expectations Concerning Accountability Reporting

4.4.2.1.A. Background and Findings

We examined reporting between the STM's designated representative and its director general. We also reviewed the required reporting process between the STM's BD and the STM's director general in connection with the STM's participation in AVT and its activities.

One of the major principles of governance we were particularly interested in is transparency, which is reflected in the agent's accountability and accountability reporting resulting from delegation of power by the principal. We would like to point out that elected officials' decisions rely partly on the quality of the information relayed.

The following statements, which describe one of the responsibilities of a BD, are excerpts from a report entitled *Evaluation des pratiques de gouvernance de la STM* [TRANSLATION: *Evaluation of the STM's Governance Practices*], produced by the École nationale d'administration publique in response to a mandate that the STM had given to the BD:

[TRANSLATION] For this purpose, the Board of Directors has at its disposal monitoring instruments and all the information necessary to assess the organization's performance from time to time.

.....
The director general, in return for greater responsibility, must submit to the BD a statutory report on its decisions and important issues. It must bring to the BD's attention any situation that presents a problem or is of interest to the organization.⁸

⁸ École nationale d'administration publique, *Evaluation des pratiques de gouvernance de la STM* [TRANSLATION: *Evaluation of the STM's Governance Practices*], July 2012, pp. 16 and 20.

According to the information we compiled, reporting is done orally by the representative designated by the STM to AVT in order to inform the director general of issues considered important by the designated representative.

We were also informed that accountability reporting is done by the director general of the STM to the STM's operational committee (which in 2013 became the assets monitoring committee) or to the BD when the director general considers it necessary.

Nonetheless, it is necessary to go back to May 2011 to find the most recent accountability reporting documents submitted by the STM's director general to the STM's BD in connection with AVT. At that time, the BD was informed of changes in the AVT dossier on a monthly basis.

It should be stressed, however, that contributions paid periodically by the STM to AVT are still authorized by the STM's BD.

We understand that the assets monitoring committee is a technical committee that was set up by the STM's BD to contribute to the good governance of the STM and assist it in the exercise of its functions and responsibilities, including the STM's participation in AVT.

During our audit, we noted the existence of two major challenges related to AVT's mandate. One was to broaden the activities of the initial mandate, and the other was to amend the APTA so that the nine partners can constitute a legal person that can provide services to third parties for remuneration.

However, in order for AVT to be able to offer these new activities resulting from these improvement projects, the APTA must first be amended. Amendments must also be made to both AVT's partnership agreement and to the management mandate entrusted to it by the partners.

The report produced by the École nationale d'administration publique, quoted above, specifies: *[TRANSLATION: "The first responsibility of a BD is to ensure that the corporation's mission and objectives are pursued; for a public organization, these are set out in its incorporating law."⁹]*

⁹ École nationale d'administration publique, *Evaluation des pratiques de gouvernance de la STM [TRANSLATION: Evaluation of the STM's Governance Practices]*, July 2012, p. 15.

We were unable to determine whether these important issues were reported to the STM's BD or one of its committees in connection with the STM's participation in AVT.

As mentioned in section 4.2.2.1., it was only at the meeting of AVT's BD, held on June 13, 2014, that the decision was made to stop accepting new contracts until the APTA is amended. Previously, AVT executed contracts with third parties for remuneration even though the APTA did not allow this since five partners did not have this power.

Adequate accountability reporting to the STM's administration could have enabled it to prevent AVT from overstepping its powers, in view of legislative constraints.

According to Resolution CA-2010-060, adopted by the STM's BD for the purpose of creating AVT, one of the BD's resolutions was *[TRANSLATION: "to designate the director general and the secretary of the Société de transport de Montréal to sign the contract creating the general partnership, for which they can agree to any amendment that is not incompatible with this resolution."]*

It is our understanding that any major change made to AVT's partnership agreement or to its management mandate must ultimately be approved by the STM's BD. The discussions on proposed improvements to AVT's mandate began in 2010. However, we understand that the STM's BD was not fully informed of these projects.

Informing the STM's BD right from the outset of such discussions would have provided assurance that the BD agreed with these orientations and enabled it to avoid putting effort into a project that was ultimately unlikely to be ratified by the BD.

We noted that the process by which the STM's director general reports to the STM's BD or assets monitoring committee is not formally defined according to criteria specifying what is expected of it.

Moreover, a document produced by the Direction exécutive – Affaires juridiques of the STM, in May 2014, compiles the comments and recommendations of the partners' secretaries in response to the observations of the Auditor General of the Ville de Lévis in its March 2014 report addressed to the president of the Société de transport de Lévis.

One of these recommendations, which concerns the accountability reporting section, reads as follows: *[TRANSLATION: "It might be worthwhile to provide for annual accountability reporting by the Société's designated representative with AVT regarding the use of its contribution."]*

In our opinion, a committee designated by the STM's BD could play an important role in issues related to the STM's participation in AVT while ensuring that effective methods and tools are in place to enable the STM's management to provide the BD with a formal accounting process concerning how the STM's contribution is used at AVT as well as other important issues. A supporting document specifying the criteria for accountability reporting should support this process.

Moreover, according to the STM's 2013 activity report, one of the main topics discussed during the operational committee's meetings was the indicators and highlights for the STM concerning the metro, buses and adapted transportation. A similar topic could be considered with respect to the STM's participation in AVT.

Through one of its existing committees, the STM's BD would be able to monitor the emergence of new problems stemming from the STM's participation in AVT and be made aware of and prepare for any problems it might face.

We were unable to track down any directive describing guidelines providing the STM's BD with a clear framework for monitoring issues related to the STM's participation in AVT.

In brief, our audit revealed that no reporting is done by the STM's designated representative to the director general, and the reporting done by the director general to the STM's BD or one of its committees is not carried out:

- on the basis of formal criteria;
- regularly and as part of a structured framework.

4.4.2.1.B. Recommendation

We recommend that the Direction exécutive – Affaires juridiques of the Société de transport de Montréal, because of its role in supporting executive administrations in the development of various management frameworks, in collaboration with the Direction générale of the Société de transport de Montréal, determine, for purposes of accountability and accountability reporting:

- what it expects from the Board of Directors of the Société de transport de Montréal or one of its committees concerning the monitoring of activities resulting from the Société de transport de Montréal's participation in AVT, set forth in a formal manner;
- the accountability reporting mechanisms expected from the Société de transport de Montréal's designated representative when the Board of Directors or its delegate designates or appoints a representative to sit and vote on AVT's Board of Directors and at the general meeting of AVT's partners.

Business unit's response:

[TRANSLATION] Once a year, present a report on AVT's activities by the STM representative on the committee on governance, ethics and sustainable development of the STM. (Planned completion: June 2015)

Once a year, submit the report on AVT's activities to the STM's BD. (Planned completion: July 2015)

Appointment by the BD of the STM representative within the new entity, in which a resolution must be provided for, if necessary, concerning the accountability reports requested, and guidelines for the powers of the STM representative within AVT. (Planned completion: when the new entity is created to replace the existing general partnership in response to legislative amendments under way)

4.4.2.2. Information to be kept to Promote Accountability Reporting

4.4.2.2.A. Background and Findings

One of the basic principles of sound management is that an organization must have continuity of operation, and survive those who manage it. According to this principle, the agent has an obligation to ensure the handover of power and everything that makes it possible to exercise the power entrusted to it so that the entity can pursue its activities without interruption. This is reflected in particular by adequate record-keeping and documentation.

Both AVT's partnership agreement and the management mandate entrusted by the partners to AVT provide that several management documents must be produced by AVT, including management charts, strategic plans, financial statements, annual activity reports and minutes. These documents must be presented to and approved by the BD or the meeting of AVT's partners.

As part of our audit, we asked the STM's designated representative with AVT to provide us with some of these documents for 2013 and 2014. The email exchanges show that it was not easy for the representative to obtain them. It should be pointed out that three representatives have held this position in turns since the establishment of AVT on April 1, 2010.

Even though we did finally succeed in obtaining most of them, the facts show that, if the STM's representatives who come and go to sit and vote at AVT maintain and keep up to date a permanent record of the history of relevant, comprehensive information on the fulfilment of their role as persons exercising powers delegated to them by the STM's director general, this would help smooth the transition when there is a change in the STM's representative at AVT, and it would also help promote optimal accounting provided to the STM's governance bodies.

4.4.2.2.B. Recommendation

We recommend that the Direction générale of the Société de transport de Montréal ensure that comprehensive documentation on the governance tools provided for in both AVT's partnership agreement and its management mandate is maintained and kept up to date by the designated representative of the Société de transport de Montréal.

Business unit's response:

[TRANSLATION] The actions provided for in recommendations 4.4.1.B. and 4.4.2.1.B. enabled us to meet this recommendation. (Planned completion: July 2015)

5. General Conclusion

In our opinion, the audit we conducted has cast light on issues of sufficient importance to cast reasonable doubt on the compliance of AVT's activities with the *Act respecting public transit authorities* (APTA).

We note that, since the coming into force of AVT's partnership agreement on April 1, 2010 and of its management mandate on May 1, 2010, a reflection process was undertaken concerning AVT's role and mission, and it is still ongoing.

This reflection process led to the creation in 2013, by AVT's Board of Directors (BD), of a committee on AVT's legal status and role to ensure that the legal status and the role currently granted to AVT adequately meet the partners' needs, considering the steps taken to improve AVT's mandate and obtain an amendment to the APTA authorizing the nine partners, and consequently AVT, to provide services to third parties for remuneration.

From the time it was created, AVT has offered its services to third parties for remuneration. Several contracts were awarded by AVT to third parties in violation of provisions of the APTA, which allows only four public transit corporations out of the nine partners to offer, for remuneration, certain goods and services associated with public transportation.

The minutes of AVT's BD meetings show that in the course of 2014, based on the recommendations of the secretaries' committee of the Association du transport urbain du Québec, AVT ceased in its efforts to obtain new external contracts until the APTA is amended in this respect.

We noted a legal uncertainty concerning the power of the Société de transport de Montréal (STM) to award mandates to AVT without a call for tenders since, in light of the information compiled, it must be established unequivocally that AVT has all the characteristics necessary to qualify as a public body.

During our audit, we were unable to find evidence that any formal procedure is followed to determine risks related to the STM's participation in AVT or to evaluate risks associated with the continuation of contracts already awarded to third parties by AVT.

Our findings highlight issues concerning management and invoicing of employees on loan from the STM to AVT.

Our audit also calls into question the contract rules currently applied to contracts awarded by Transgesco Limited Partnership.

In addition, our findings highlighted the lack of documents on analyses that would help identify and update the main risks associated with the STM's participation in AVT and provide measures to manage them adequately for either the current or the proposed management mandate.

Our findings underscore the fact that, in the area of governance at the STM, no structured accountability reporting process is in place for the monitoring of activities performed by the STM's designated representative with AVT. The STM's BD is not informed of the decisions made by AVT. No structured mechanism is in place to maintain and keep up to date comprehensive documentation on governance tools provided for in both the AVT contract and its management mandate.

In brief, not only must the STM fulfil the mission set out in the APTA, namely to ensure mobility of people on its territory through modes of public transportation, it must do this within a financial and legal framework that is not limited strictly to this objective.

It is our opinion that the Direction générale and the Direction exécutive – Affaires juridiques of the STM must make short-term adjustments in order to:

- clarify, in collaboration with the other partners, AVT's legal capacity to contract on behalf of the partners and clarify the extent of AVT's obligations with respect to the request for an amendment to the APTA;
- strengthen the STM's governance function to ensure monitoring of the contribution provided by the STM to AVT and enable members of the STM's BD to be informed of the decisions made by AVT.

We cannot overstate the fact that the implementation of measures taken to follow up on recommendations of this audit report will help clarify AVT's legal capacity to contract on behalf of the partners, clarify whether it is possible for AVT and the partners to conclude contracts by mutual agreement, clarify the contractual status of Transgesco Limited Partnership as well as strengthen the STM's governance and accountability reporting in connection with its participation in AVT.

Over and over, members of the STM administration impressed upon us that the STM took all the deficiencies that our audit revealed very seriously. Moreover, in this regard, before our findings were even published, we learned that measures had already been implemented to resolve the issues arising from our audit, and that other measures were being studied for the purpose of optimizing management with respect to the STM's participation in AVT.