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June 13, 2016

VIA EMAIL

Attn: Sue Oberg, Assistant County Manager/CFO
Westlock County
10336 - 106 Street
Westlock, AB T7P 2G1

Dear Madam:

Re: Peter Kelly

This letter is a companion to our letter of the same date regarding the Horizon North Project.

As a result of certain failures to follow the proper procedures with respect to Horizon North and the Horizon North project on the Lands, you have requested our opinion with respect to available remedies against Mr. Kelly.

Mr. Kelly was an employee of Westlock County under two consecutive employment agreements. The first employment agreement is dated August 21, 2014, wherein Mr. Kelly was employed in the fulltime position as Chief Administrative Officer ("CAO") for the County of Westlock. Upon Mr. Kelly completing a 6 month probationary period, a second employment agreement, dated April 28, 2015, was entered into between Westlock County and Mr. Kelly. The second employment agreement was for a one year term, effective March 1, 2015 to February 28, 2016, and replaces all previous agreements.

Mr. Kelly's last day of employment with Westlock County was March 24, 2015, as his employment agreement was extended for one month. From March 1, 2016 to March 24, 2016, Mr. Kelly was not appointed CAO nor interim CAO. After March 24, 2016, Mr. Kelly was not an employee of the County.

Unlike the first employment agreement, which attached a job description outlining the responsibilities of the position of CAO, the second employment between Westlock County and Mr. Kelly does not expressly set out his duties or responsibilities.

Fortunately, the *Municipal Government Act* ("MGA") provides some assistance in that regard. Sections 207 and 208 of the MGA set out the Chief Administrative officer's responsibilities and major administrative duties as follows:

Chief administrative officer's responsibilities

207 The chief administrative officer

- (a) is the administrative head of the municipality;
- (b) ensures that the policies and programs of the municipality are implemented;
- (c) advises and informs the council on the operation and affairs of the municipality;
- (d) performs the duties and functions and exercises the powers assigned to a chief administrative officer by this and other enactments or assigned by council.

Performance of major administrative duties

208(1) The chief administrative officer must ensure that

- (a) all minutes of council meetings are recorded in the English language, without note or comment;
- (b) the names of the councillors present at council meetings are recorded;
- (c) the minutes of each council meeting are given to council for adoption at a subsequent council meeting;
- (d) the bylaws and minutes of council meetings and all other records and documents of the municipality are kept safe;
- (e) the Minister is sent a list of the councillors and any other information the Minister requires within 5 days after the term of the councillors begins;
- (f) the corporate seal, if any, is kept in the custody of the chief administrative officer;
- (g) the revenues of the municipality are collected and controlled and receipts are issued in the manner directed by council;
- (h) all money belonging to or held by the municipality is deposited in a bank, credit union, loan corporation, treasury branch or trust corporation designated by council;
- (i) the accounts for authorized expenditures referred to in section 248 are paid;
- (j) accurate records and accounts are kept of the financial affairs of the municipality, including the things on which a municipality's debt limit is based and the things included in the definition of debt for that municipality;
- (k) the actual revenues and expenditures of the municipality compared with the estimates in the operating or capital budget approved by council are reported to council as often as council directs;
- (l) money invested by the municipality is invested in accordance with section 250;
- (m) assessments, assessment rolls and tax rolls for the purposes of Parts 9 and 10 are prepared;
- (n) public auctions held to recover taxes are carried out in accordance with Part 10;
- (o) the council is advised in writing of its legislative responsibilities under this Act.

(2) Subsection (1)(a) to (d) and (o) apply to the chief administrative officer in respect of council committees that are carrying out powers, duties or functions delegated to them by the council.

As explained in the accompanying letter regarding the Horizon North Project, there were a number of unusual procedures followed by Mr. Kelly with respect to his dealings with Horizon North and the Horizon North Project. In summary, it appears Mr. Kelly undertook to negotiate the enhancement and leasing of the Lands to Horizon North, with an option to purchase, mainly on his own without input from Finance or others in Administration and without seeking the prior approval of Council when required or appropriate.

This approach has resulted in Westlock County spending approximately \$375,706.52 on the Horizon North Project, which amount was not budgeted for or otherwise authorized by Council. The Lease Amendment Agreement negotiated with Horizon North by Mr. Kelly provides for payment of a portion of the project costs incurred by the County by way of a \$56,000 plus GST upfront payment, followed by increased lease payments over a 3 year term. The shortfall is approximately \$194,000.00.

From our review of the relevant documents and information gathered during the investigation by Westlock County, we conclude that Mr. Kelly has breached his duties to Westlock County as CAO. The following is a summary of the most significant breaches:

- a. Negotiated the sale of a lot within the Industrial Park for \$30,000 per acre without Council approval, which is also potentially less than market value and requires advertising of same.
- b. Breached s. 248 of the MGA and directed the expenditure of unbudgeted municipal resources and money for the project without prior Council approval up to a value of approximately \$375,706.52.
- c. Negotiated and executed on behalf of the County a Lease dated April 1, 2015 between Westlock County and Horizon North without prior Council approval.
- d. Negotiated a Lease Amending Agreement, including an option to purchase, with Horizon North without prior Council approval.
- e. Breached County Policy 5.10 Purchasing Policy with respect to the expenditure of any non-budgeted amounts of \$10,000 or greater without prior Council approval.
- f. Withheld from Council information with respect to the cost update for the Horizon North Project.
- g. Authorized and directed work on the Horizon North Project which exceeded the amount Horizon North was willing to pay and the value of the Lands without Council approval.

- h. Failed to follow proper procedure with respect to invoicing of Horizon North.
- i. Failed to follow proper procedure with respect to tracking expenses for the Horizon North Project.
- j. Continued to represent to Horizon North that he was CAO after his appointment as CAO ended.
- k. Continued to deal with Horizon North on behalf of Westlock County, reportedly as CAO, by text after the termination of his employment.
- l. Failed to maintain appropriate paperwork.

An employee owes a contractual duty to take care of his or her employer. The breach of that duty founds an action for damages in tort or in contract and an employer is entitled to recover damages caused by the breach of duty provided that the damages are not too remote and are sufficiently proved.

There is no doubt Mr. Kelly owed a duty of care to Westlock County to perform his duties as CAO with reasonable care and skill. By approving expenditures by Westlock County which were not approved by Council (either by inclusion in the budget or otherwise authorized), Mr. Kelly breached his employment contract and the relevant provisions of the MGA and is liable for the damages that reasonably flow from the breach.

In addition, it was an implied term of Mr. Kelly's employment agreement that he would perform his duties in a professional, competent manner and in compliance with Council's direction, the relevant provisions of the MGA and Westlock County policies. Mr. Kelly breached the terms of his employment agreement for the reasons set out above.

While we are relatively confident the County would be able to establish a breach of Mr. Kelly's employment duties, the question remains to what extent damages suffered by the County can be proved. Theoretically, the damages suffered by the County would be the expenditure of funds which were not approved by Council and in compliance with the MGA which the County has not been able to recoup from Horizon North. That difference is approximately \$194,000.00.

However, a Court would also take into consideration that this expenditure most likely resulted in the increase in the value of the Lands as a result of the Horizon North Project. If the County proceeds with the agreement with Horizon North which contains an option to purchase the Lands at \$30,000 per acre, and the option is exercised by Horizon North, the potential to prove the damages is improved as the difference between the purchase price and the value of the Lands would crystallize the loss to the County. At the same time, Mr. Kelly could claim that Council approved this "loss" by approving the sale at that value. For these reasons, the likelihood of establishing damages is difficult to determine. Damages are necessary for a successful claim.

Since Mr. Kelly's employment was in Alberta, an action could be commenced in the Alberta Court of Queen's Bench by the County. The claim would be for the breach of the contractual duty of care to Westlock County and would be framed in an action for damages in tort and in contract. An action of this nature could easily take a number of years to proceed to trial, at significant expense.

In addition, the *Limitations Act* would apply to this claim, meaning the claim would need to be commenced within two years of the date the County knew or ought to have known of the claim against Mr. Kelly. Since most of Mr. Kelly's actions were in 2015 and 2016, the most conservative approach would be to view the two year limitation period as beginning to run in spring of 2015 when Public Works was first directed by Mr. Kelly to commence work on the Horizon North Project. This means a claim would need to be commenced prior to the spring of 2017.

An added wrinkle is the possibility the limitation period comes to an end before Horizon North exercises its option to purchase. Damages would not yet have been determined, but a claim would need to be filed.

Taking this into account, we are of the opinion that it is far from clear that the County would be successful in an action seeking to recover damages. Anytime there is litigation, there is no certainty of success. While the County has been able to deduce much of what occurred, the County does not have an original Horizon North file and Mr. Kelly may present a very different version of events. Given the challenges with the evidence and the issue with establishing damages, we believe the likelihood of success is less than 50%. This suggests that it may be impractical to proceed with litigation.

Furthermore, as result of his status as a designated officer, Mr. Kelly would have available to him certain defences under the MGA which other employees would not have.

Section 558 of the MGA provides as follows:

Offences applicable to officials

558 No chief administrative officer or designated officer may

- (a) fail to discharge the duties of office imposed by this or any other enactment or bylaw,
- (b) sign any statement, report or return required by this or any other enactment or bylaw knowing that it contains a false statement, or
- (c) fail to hand over to a successor in office, or to the persons designated in writing by the council or the Minister, all money, books, papers and other property of a municipality.

Section 535 of the MGA provides as follows:

Protection of councillors and municipal officers

535(1) In this section,

(a) “municipal officers” means

(i) the chief administrative officer and designated officers, and

(ii) employees of the municipality;

(b) “volunteer worker” means a volunteer member of a fire or ambulance service or emergency measures organization established by a municipality, or any other volunteer performing duties under the direction of a municipality.

(2) Councillors, council committee members, municipal officers and volunteer workers are not liable for loss or damage caused by anything said or done or omitted to be done in good faith in the performance or intended performance of their functions, duties or powers under this Act or any other enactment.

(3) Subsection (2) is not a defence if the cause of action is defamation.

(4) This section does not affect the legal liability of a municipality.

Earlier versions of these two MGA provisions were considered by the Alberta Courts in *Vogel v. Hall*, 2001 ABCA 188.

In *Vogel v. Hall*, the treasurer of the Municipal District of Bighorn invested the municipality’s money in ways that were not authorized by the MGA. The investments failed and were not recoverable. A group of ratepayers sued several defendants, including the treasurer’s supervisor (the CAO) and members of Council. The municipal Council declined to initiate or join the lawsuit as Plaintiffs.

The trial judge found that the CAO had been grossly negligent in failing to supervise the treasurer and awarded damages against him in his personal capacity. A central issue in this lawsuit was whether the rate payers had standing to sue; the Court concluded they did have standing because they had suffered special damages. The Court of Appeal has upheld this decision and dismissed the appeal.

The trial judge exercised his discretion to permit standing because the issues raised were serious, the question of the CAO’s gross negligence was justiciable, the Respondent rate payers had a genuine issue in the recovery of the funds and there was no other reasonable way to bring the suit (because the municipality had declined to bring the action).

Since this case was decided, s. 535 of the MGA (which is the section that provides limited protection from liability for councillors, municipal officers and volunteer workers) has been amended. Currently, it provides that councillors, municipal officers and volunteer workers are not liable for loss or damage caused by anything said or done or admitted to be done in good

faith in their performance or intended performance of their functions, duties or powers under the MGA or any other enactment. Previously, this section provided that councillors, municipal officers and volunteer workers are not liable for loss or damage caused by anything said or done or admitted to be done in their performance or intended performance of their functions, duties or powers unless the person was dishonest, grossly negligent or guilty of willful misconduct.

In *Vogel v. Hall*, the Court concluded the CAO had been grossly negligent (very negligent) and therefore did not fall within the protection of s. 535. Since s. 535 has been amended, in order to overcome its protection in an action against Mr. Kelly, the evidence would need to establish that Mr. Kelly was not acting in good faith in the performance or intended performance of his functions, duties or powers.

While there is significant case law on the concept of bad faith, at its core bad faith implies malice or ill will, intentionally attempting to deceive or mislead another in order to gain some advantage. While it is difficult to see what advantage Mr. Kelly derived from his dealings with Horizon North, many of his decisions may demonstrate the elements of unreasonableness, discrimination or arbitrariness frequently associated with bad faith conduct.

The protection provided by s. 535 is a high hurdle to overcome. It is arguable that Mr. Kelly's actions were evidence of bad faith in that it appears he took steps on a number of occasions to hide what he was doing from Council and Administration, misrepresented the extent of his authority to Horizon North and, allegedly, destroyed or did not keep a Horizon North file. All of these factors would be evidence of bad faith in the performance of his duties with respect to Horizon North, but are not a guarantee that a Court would find the necessary elements of bad faith in the conduct.

Another reason *Vogel v. Hall* is relevant to Westlock County's current situation is that it demonstrates the willingness of the Courts to allow taxpayers to proceed with litigation against municipal employees and elected officials for misconduct which results in loss to the municipality when the municipality chooses not to do so. Admittedly, it is a rare situation where tax payers will take on this type of litigation personally, but it has happened.

One final option available to the County would be to commence a prosecution against Mr. Kelly. Section 557 of the MGA provides that a person who contravenes or does not comply with s. 558 is guilty of an offence. Where a person is guilty of an offence under the MGA, a prosecution may be commenced within 2 years after the date of the alleged offence and a person who is found guilty of an offence under the MGA is liable to a fine of not more than \$10,000 or to imprisonment for not more than one year, or to both fine and imprisonment. This, of course, would require the Government of Alberta to make the decision to prosecute. It may be difficult to obtain the province's agreement to take this step. A prosecution of this type would also require proof to the higher standard of beyond a reasonable doubt.

Conclusion

We trust the foregoing will assist Council in determining next steps. We would be happy to discuss any aspect of this opinion with you in greater detail or answer any questions or concerns you may have.

Yours truly,

REYNOLDS MIRTH RICHARDS & FARMER LLP

PER:



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