City of Richmond

Report to Committee

To:	Finance Committee	**Date:**	December 15, 2023
From:	John Irving, P.Eng., MPA General Manager, Engineering and Public Works Chief Executive Officer, Lulu Island Energy Company Jerry Chong, CPA, CA Acting General Manager, Finance and Corporate Services Chief Financial Officer, Lulu Island Energy Company	**File:**	01-0060-20-LIEC1/2023-Vol 01
Re:	**2023 Q3 Financial Information for the Lulu Island Energy Company**		

Staff Recommendation

That the Lulu Island Energy Company report titled "2023 Q3 Financial Information for the Lulu Island Energy Company", dated December 15, 2023, from the Chief Executive Officer and Chief Financial Officer, be received for information.

John Irving, P.Eng., MPA
General Manager, Engineering and Public Works
Chief Executive Officer,
Lulu Island Energy Company
(604-276-4140)

Jerry Chong, CPA, CA
Acting General Manager, Finance and Corporate Services
Chief Financial Officer,
Lulu Island Energy Company
(604-276-4064)

REPORT CONCURRENCE	
CONCURRENCE OF GENERAL MANAGER	
REVIEWED BY SMT	INITIALS: BA
APPROVED BY CAO	

Richmond

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RICHMOND, BC V6Y 2C1

Report

To: Board of Directors **Date:** November 20, 2023

From: Jerry Chong, CPA, CA,
Chief Financial Officer

Re: Lulu Island Energy Company – 2023 3rd Quarter Financial Information

Staff Recommendation

That the 3rd Quarter Financial Information as presented in the report titled "Lulu Island Energy Company – 2023 3rd Quarter Financial Information", dated November 20, 2023, be approved.

Background

Lulu Island Energy Company (LIEC), a corporation wholly-owned by the City of Richmond, was established to provide district energy services on behalf of the City. Information regarding LIEC's district energy utility (DEU) operations can be found in Attachment 1. All capital and operating costs are recovered through revenues from user fees, ensuring that the business is financially sustainable. City Council is the regulator and thus sets customer rates.

This report provides pre-audited financial information to the Board of Directors and LIEC's shareholder, represented by Richmond City Council.

Analysis

The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS). LIEC's pre-audited Q3 financial information consists of the interim statement of financial position as of September 30, 2023 (Attachment 2) and the interim income statement for the period ended September 30, 2023 (Attachment 3). Year-to-date budget to actual numbers are shown in Attachment 4.

On September 22, 2022, LIEC entered into the City Centre District Energy Utility (CCDEU) Project Agreement with City Centre Energy Limited Partnership, a wholly owned subsidiary of Corix Utilities Inc.(Corix). The agreement replaces the previous concession agreement with Corix, the Oval Village District Energy Utility (OVDEU) concession agreement. The CCDEU agreement was approved by the LIEC Board and LIEC's shareholder, Richmond City Council, and includes a defined delivery model structure, initial setup costs and lower financing costs which is necessary for the ongoing project infrastructure expansion and operations. Due to the new agreement being in place, year over year results may not be comparable.

Financial Position

The interim statement of financial position provides a summary of assets, liabilities and shareholder's equity. Total assets are comprised of current assets (cash, investments and receivables) $16,379,800 and non-current assets (plant and equipment) $48,325,773. The total assets are $64,705,573. The total liabilities of $28,106,228 include outstanding invoices, deferred contributions and Project Agreement liabilities. The shareholder's equity represents the net worth of the company. It is equal to the total assets minus its total liabilities and measures the company's financial health. As of September 30, 2023, LIEC's shareholder equity is $36,599,345, showing good financial health of the company.

Revenues

The metered billing revenue is the total energy sales of ADEU, and City Center District Energy Utility (CCDEU) service areas (OVDEU is now combined under the CCDEU service area). The year to date metered billings revenue is $2,170,586 from the ADEU and $3,441,487 from the CCDEU. Overall, the cumulative nine months of metered billing revenue of $5,612,073 increased by 18% over 2022. This reflects the addition of one new building connection, increased energy use from customers due to increased occupancy, and the approved 2023 rates.

Cost of Sales

The cost of sales is the accumulated total expenses attributable to the metered billing revenue, which includes contract services, utilities (electricity and natural gas), and amortization expenses. The contract expense increased by 78% over 2022 due to the additional operations and maintenance work as a result of more buildings being serviced, including two on-site low carbon energy plants (LCEP); compared to budget, the contract expense actual is 3% below the budget. The increased energy demand due to the addition of more buildings and operation of the first two on-site LCEP's, paired with electricity and gas rate increases caused the utility expense to increase 7% compared to 2022, but 7% below the budget. The amortization expense decreased due to a change in the accounting estimate, where LIEC is matching the amortization life of the assets to be the same as in the CCDEU Project Agreement and the financial model. The year-over-year cost of sales has increased by 15%, but 14% below the budget. The gross margin as a percentage of revenue is 43% for 2023 compared to 42% in the first nine months of 2022.

General and Administration Expenses

General and administration (G&A) expenses are expenditures that LIEC incurs with respect to supporting operations which includes salaries and benefits, administration expenses, professional fees, etc. Salaries and benefits are 22% higher than last year and 4% higher than the budget due to the filling of one new position earlier this year and benefits associated with an approved leave of absence and extra support during the year-end audit from City staff. The administration expense increased compared to the prior year mainly due to an increase in the CCDEU Project Agreement related administration expenses which include: overhead costs to administer Corix's special purpose entity, LIEC reporting, and CIB reporting and financial administration requirements. This increase was expected; compared to the budget, the administration expense is 15% below budget. The administration expense also includes the overhead allocation paid to the City of Richmond for the day-to-day support that LIEC receives from City staff. Insurance expenses increased compared to the prior year, but is below the budget, due to: the general insurance rate increase; additional assets being insured; additional comprehensive environmental liability insurance coverage; and deductions required under the CCDEU Project Agreement. Professional fees have increased compared to the prior year, but are below budget, mainly due to the cost for updating technical guidelines, as well as due to the audit, bank account, collateral agent and insurance trustee fees for the special purpose entity necessary to deliver the CCDEU Project Agreement. LIEC audit fees also increased due to additional audit work surrounding the CCDEU project and increase in the financial position.

Overall, the G&A expenses as a percentage of revenues is 22% compared to 15% in 2022. This is due to the first year of implementation of the CCDEU. As with the ADEU and OVDEU projects, the CCDEU initial years' general and administration expenses are projected to increase in relation to the revenue received from customers. This is due to the initial project operation and administration setup costs necessary for the infrastructure expansion and operation for a project of this scale, as well as the costs required to administer low-interest financing from CIB. As more customers are connected to the utility, the general and administration expenses in relation to the revenue will decrease.

Contributions and Financing Expenses

The contributions and financing expense section represents other sources of income and costs for the business. The developer contributions are lower compared to Q3 2022 and below budget due to a change in the amortization rate and adjustment for values in 2023 to match it with the CCDEU Project Agreement, as well as the adjustment between estimated and actual value of the equipment. Developer contributions are recognized as revenue over a longer period as the rate matches the amortization rate and adjustments are required to recognize the actual value of the equipment contributed by developers.

Other income is made up of energy model review fees. The energy modeling review fee revenues are lower than 2022 due to lower than projected building permit reviews. The net finance cost is the result of year-to-date finance costs on project agreement liabilities, offset by interest income. Interest income has exceeded the full year budget for 2023, because LIEC has taken advantage of the higher interest rates by investing in short-term term deposits which have yielded much higher returns compared to 2022 and budget. This has resulted in a variance in the net financing costs in both year-over-year and actuals to budget comparison, which is positive for LIEC.

LIEC's earnings before interest, tax, and amortization (EBITA), used as a proxy to measure the company's financial performance, as a percentage of revenue decreased to 41% compared to 56% in Q3 2022. This is due to the initial operation and administration setup costs necessary for the CCDEU project infrastructure expansion and operation. This is expected and has been encountered in the past with the existing OVDEU and ADEU projects. As more customers are connected to the system, revenues and EBITA will increase. EBITA has exceeded the budget by 3%.

The year-to-date net income of $1,571,188 has exceeded the prior year (Q3 2022 - $1,467,148) and the budget. Consistent with the company's financial plan objectives, any net income will be maintained in LIEC's equity in order to fund future capital projects and infrastructure replacements.

Financial Impact

None.

Conclusion

The pre-audited financial information shows that LIEC's financial position is positive. This report will be presented to Council for information.

Helen Zhao
Controller
(604-204-8699)

Cody Lan
Cody Lan
Assistant Controller
(604-247-4698)

Att. 1: District Energy in Richmond
2: Interim Statement of Financial Position as of September 30, 2023 (unaudited)
3: Interim Income Statement for the period ending September 30, 2023 (unaudited)
4: Year-To-Date Budget vs. Actual Comparison (unaudited)

District Energy in Richmond

Richmond's 2041 Official Community Plan (OCP) establishes a target to reduce greenhouse gas (GHG) emissions 50 per cent below 2007 levels by 2030 and 100 per cent by 2050. The City identified district energy utilities (DEUs) as a leading strategy to achieve the City's GHG reduction goals and incorporated Lulu Island Energy Company Ltd. (LIEC) in 2013 for the purposes of carrying out the City's district energy initiatives on the basis of the following guiding principles:

1. The DEU will provide end users with energy costs that are competitive with conventional energy costs, based on the same level of service; and
2. Council will retain the authority of setting customer rates, fees and charges for DEU services.

The City established three DEU service areas: ADEU, OVDEU, and CCDEU. Table 1 below provides a summary of the developments connected under the DEU service areas to-date.

Table 1 – DEU Service Areas - Current and Projected Connected Space

	Buildings To-Date	**Residential Units To-Date**	**Floor Area**	
			To-Date	**Build-out**
Alexandra DEU	13	2,200	2.4M ft^2	4.4M ft^2
Oval Village DEU	14	3,174	3.7M ft^2	6.4M ft^2
City Centre DEU	3	1,082	1.2M ft^2	48.0M ft^2
Total	**30**	**6,456**	**7.3M ft^2**	**58.8M ft^2**

The ADEU provides heating and cooling services to ten residential buildings, the large commercial development at "Central at Garden City", the Richmond Jamatkhana temple and Fire Hall No. 3, comprising of 2,200 residential units and over 2.4 million square feet of floor area. While some electricity is consumed for pumping and equipment operations, most of this energy is currently produced locally from the geo-exchange fields in the greenway corridor and West Cambie Park, and highly efficient air source heat pumps.

The OVDEU services 14 buildings, containing 3,174 residential units. Energy is currently supplied from the three interim energy centres with natural gas boilers which provide 16 MW of heating capacity. LIEC received a $6.2 million grant from the CleanBC Communities Fund for the design and construction of the sewer heat recovery technology and a permanent energy centre for the area. This project is in the preliminary design stage and is expected to be completed in 2028. Once completed, the system will be able to produce up to 80% of low-carbon energy from the Gilbert Trunk sanitary force main sewer.

The CCDEU currently services three buildings, comprised of 1,082 residential units and approximately 1.2M ft^2 of floor area. To-date, developments in the City Centre service area have already committed 5.5M ft^2 of building floor area for future connection. While permanent energy centre progress through development, CCDEU utilizes on-site low carbon energy plants as a source of energy production. At full build-out, 176 developments, 28,000 residential units and approximately 48M ft^2 of floor space will be serviced by 5 permanent energy centres with over 130 MW of heating and 115 MW of cooling capacity. The built out system is estimated to reduce over one million tonnes of GHG emissions compared to conventional service.

Interim Statement of Financial Position (Unaudited)

	As of September 30 2023	As of December 31 2022
Assets		
Current assets:		
Cash and cash equivalents	$ 968,448	$ 3,191,380
Accounts receivable	2,574,762	2,240,807
Investments	12,836,590	12,324,233
	16,379,800	17,756,420
Non-current assets:		
Plant and equipment	48,325,773	45,745,053
	$ 64,705,573	$ 63,501,473
Liabilities and Shareholder's Equity		
Current and non-current liabilities:		
Accounts payable and accrued liabilities	$ 1,623,879	$ 3,852,889
Deferred developer contributions	12,719,403	13,017,815
Government grants	264,742	241,051
Project Agreement liability	13,498,204	11,361,558
	28,106,228	28,473,313
Shareholder's equity:		
Share capital and contributed surplus	27,397,115	27,397,115
Retained earnings	9,202,230	7,631,045
	36,599,345	35,028,160
	$ 64,705,573	$ 63,501,473

Interim Income Statement (Unaudited)

	September 30 2023	September 30 2022	$ Changes	% Change
Revenues				
Metered Billings (Quarterly)	$ 5,612,073	$ 4,773,731	$ 838,342	18%
Service fee	736,115	736,115	-	0%
	6,348,188	5,509,846	838,342	15%
Cost of Sales				
Contracts	1,327,029	747,552	579,477	78%
Utilities	1,315,099	1,229,949	85,150	7%
Amortization	1,006,602	1,208,347	(201,745)	(17%)
	3,648,730	3,185,848	462,882	15%
Gross Margin	**2,699,458**	**2,323,998**	**375,460**	**16%**
General and Administration Expenses				
Salaries and benefits	788,628	645,243	143,385	22%
Administration expenses	256,246	63,722	192,524	302%
Insurance	172,953	71,440	101,513	142%
Professional Fees	148,265	33,750	114,515	339%
	1,366,092	814,155	551,937	68%
Net Income Before Other Items	1,333,366	1,509,843	(176,477)	(12%)
Contributions and Financing expense				
Developer contributions	276,272	282,571	(6,299)	(2%)
Other income	4,232	75,825	(71,593)	(94%)
Net financing cost	(42,682)	(401,091)	358,409	(89%)
	237,822	(42,695)	280,517	
Net Income	**$1,571,188**	**$1,467,148**	**$104,040**	**7%**

Earnings Before Interest, Taxes and Amortization (EBITA)				
Net income per above	$ 1,571,188	$ 1,467,148	$104,040	7%
Net Financing cost	42,682	401,091	(358,409)	(89%)
Amortization expense	1,006,602	1,208,347	(201,745)	(17%)
EBITA	$ 2,620,472	$ 3,076,586	($456,114)	(15%)

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Notes:

	Ending September 30 2023	Ending September 30 2022
Percentage of Revenue		
Gross margin percentage	43%	42%
General and administration percentage	22%	15%
Net income percentage	25%	27%
EBITA percentage	41%	56%

Year-To-Date Budget vs. Actual Comparison (Unaudited)

	2023 Q3 Budget	2023 Q3 Actual	$ Variance	%Variance
Revenues				
Metered Billings (Quarterly)	$5,670,861	$ 5,612,073	(58,788)	(1%)
Service fee	736,115	736,115	-	-%
	6,406,976	6,348,188	(58,788)	(1%)
Cost of Sales				
Contracts	1,372,783	1,327,029	(45,754)	(3%)
Utilities	1,419,106	1,315,099	(104,007)	(7%)
Amortization	1,463,575	1,006,602	(456,973)	(31%)
	4,255,464	3,648,730	(606,734)	(14%)
Gross Margin	**2,151,512**	**2,699,458**	**547,946**	**25%**
General and Administration Expenses				
Salaries and benefits	756,412	788,628	32,216	4%
Administration expenses	301,891	256,246	(45,645)	(15%)
Insurance	251,042	172,953	(78,089)	(31%)
Professional Fees	149,250	148,265	(985)	(1%)
	1,458,595	1,366,092	(92,503)	(6%)
Net Income Before Other Items	692,917	1,333,366	640,449	92%
Contributions and Financing expense				
Developer contributions	378,813	276,272	(102,541)	(27%)
Other income	20,250	4,232	(16,018)	(79%)
Net financing cost	(778,189)	(42,682)	735,507	(95%)
	(379,126)	237,822	616,948	(163%)
Net Income	**$313,791**	**$1,571,188**	**$1,257,397**	**401%**

Earnings Before Interest, Taxes and Amortization(EBITA)				
Net income per above	$313,791	$1,571,188	$1,257,397	401%
Net Financing cost	778,189	42,682	(735,507)	(95%)
Amortization expense	1,463,575	1,006,602	(456,973)	(31%)
EBITA	$2,555,555	$2,620,472	$64,917	3%

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