



SUBJECT: 2024 Hydro Business Plan

TO: Committee of the Whole

FROM: Finance Department

Report Number: F-02-24

Wards Affected: Not applicable

Date to Committee: February 5, 2024

Date to Council: February 13, 2024

Recommendation:

Receive and file finance department report F-02-24 regarding the Hydro 2024 business plan.

PURPOSE:

This report is to provide committee with an overview of the 2024 Hydro business plan on the following key areas:

- 10-year forecast of net income
- Capital expenditures
- Balance sheet
- Dividend flow
- Shareholder risks

Vision to Focus Alignment:

- Support sustainable infrastructure and a resilient environment

Background and Discussion:

The shareholder direction to BEC (Burlington Enterprises Corporation) is a document that sets out the accountability, responsibility and relationship between the Board and the Shareholder. Article 6 of the direction details reporting requirements to the shareholder. Specifically, section 6.1 requires that “not later than 45 days prior to the end of each fiscal

year, the Board will approve and submit to the Chief Financial Officer of the shareholder a business plan for the next five fiscal years.”

The business plan is to include;

- a) The strategic direction and any new business initiatives which Burlington Hydro or its subsidiaries will undertake;
- b) An operating and capital expenditure projection for each fiscal year thereafter, including the resources necessary to implement the Business Plan;
- c) Pro forma unconsolidated Financial Statements for each fiscal year, including projected dividend payments to the shareholder;
- d) An acquisition budget setting forth the nature and type of capital expenditures proposed to be made in the following fiscal year, supported by explanations, notes and information upon which the budget was based;
- e) Energy conservation programs and environmental plans; and
- f) Any material variance from the Business Plan then in effect.

This information is important to the City as it assists the City, as shareholder to understand the financial and operational aspects of the distribution business and other businesses of the corporation. The City is in receipt of the following financial information, including 10-year forecasts, with regards to BHI (Burlington Hydro Inc.) and BESI (Burlington Electricity Services Inc):

- Business Assumptions
- Balance Sheet
- Statement of Changes in Cash Flow
- Profit & Loss Statement
- Capital Forecast

Each year the Board of Directors conducts a strategic planning process which helps formulate company objectives and strategic goals for the coming year. Risk management is a primary focus across BEC and is incorporated into their annual strategic planning process. The following prioritized strategies have been set as key objectives in 2024:

- Responsible Financial Management
 - Meet financial metrics related to LDC (Local Distribution Company) Scorecard.
 - Generate cost savings through partnership in the GridSmartCity Cooperative.
- Customer and Community commitment
 - Conduct customer satisfaction and public safety awareness surveys.
 - Implement corporate communications campaigns.
 - Hold a public open house.

- Promote GridSmartCity.
- Internal process and Operational effectiveness
 - Meet performance metrics referenced in LDC Scorecard.
 - Continue to expand implementation of secure document technology.
 - Integrate and implement a new Outage Management System.
- Learning and Growth - Employer of choice
 - Meet safety metrics referenced in OEB Scorecard
 - Continue towards safety excellent.
 - Develop and implement an ambassador program.

Guiding these objectives are the strategic principles of the organization:

- Customer focus.
- Operational effectiveness.
- Public policy responsiveness.
- Strong and sustainable financial performance.

BEC remains focused to meet the needs and priorities of the community into the future. It strives to contribute to the quality of life in the community, aligning its business strategies to support the City's sustainable growth.

BURLINGTON HYDRO INC.

BHI Net Income Forecast 2024-2033

Forecasted net income ('000 millions) before tax for the next ten years is presented as follows:

2023 Update	2023 Budget	2024 Budget	2025 FCST	2026 FCST	2027 FCST	2028 FCST	2029 FCST	2030 FCST	2031 FCST	2032 FCST	2033 FCST
5.636	4.022	4.588	4.482	8.114	8.330	8.213	8.231	8.436	10.283	10.685	11.058

The 2023 update of \$5.636 million presents a positive variance of approximately \$1.614 million from the 2023 budget of earnings before tax of \$4.022 million. Factors affecting the 2023 update are as follows:

Distribution Revenue	\$(172)K	Unfavourable variance primarily driven by lower demand for large commercial customers. This was slightly offset by a higher number of residential customers and higher consumption for small commercial customers.
Other Operating Revenue	\$1,508K	Favourable variance due to management fees for the Metrolinx GO Corridor Electrification Project and interest on regulatory balances.
Operating Expenses	\$(581)K	Unfavorable variances in operations and maintenance costs of \$303K and Administration Department of \$350K. These are slightly offset by favorable variance for Billing & Collection of \$72K.
Net Finance Costs	\$554K	Favourable variance due to higher interest rates on cash balances and interest on long term debt.
Depreciation Expense	\$305K	Favourable variance due to timing of capital projects taking place.

The results achieved by BHI are of importance to the shareholder as the dividends flowing to the shareholder from BEC are composed of earnings from BHI and BEI.

TEN-YEAR CAPITAL BUDGET AND FORECAST

In keeping with BHI's Asset Management strategy the capital budget and forecast identifies projects that are part of its sustaining capital budget as well as ensuring that Burlington has an adequate supply of electricity. These include:

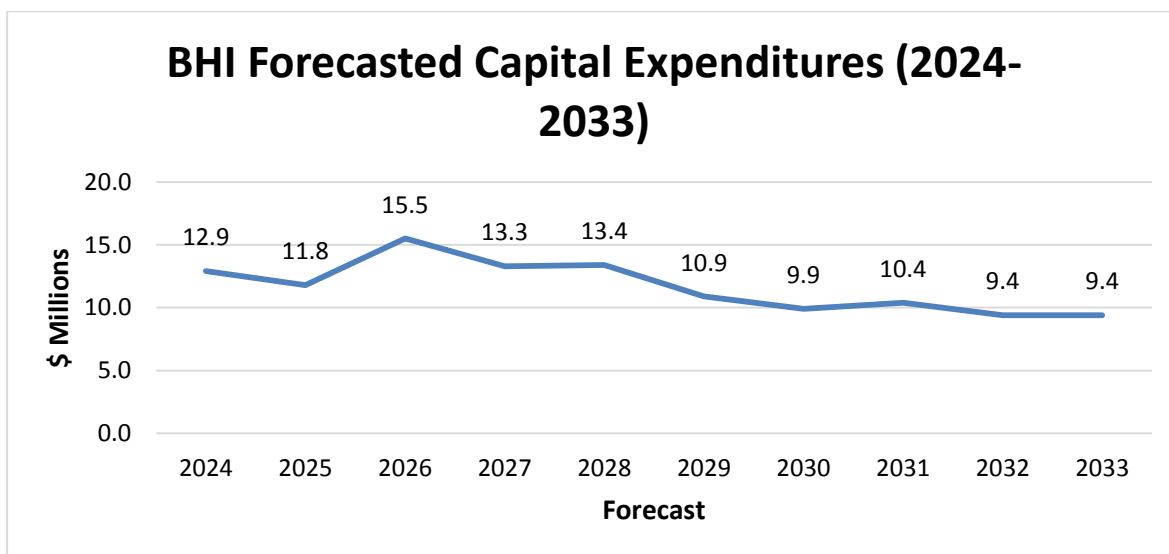
- Customer demand projects including connecting new customers, building new subdivisions, and relocating system plant for roadway construction work.
- Renewal which focuses on replacement of assets that have reached end of useful life. New assets require less maintenance, deliver better reliability, and reduce safety risks to the public.
- Security which could include adding switching devices or creating a backup feeder supply to reduce the risk to typical restoration times.
- Reliability which supports maintenance of or improvement to the Service Quality indices measured and submitted to the OEB each year.
- Substations which are invested in to improve or maintain reliability to large numbers of customers and to maintain security and safety at the substation sites. The renewal or retirement of Burlington Hydro's 4.16 kV substations is part of the annual review undertaken as part of the Asset Management strategy.

- Customer Connections and metering include meter installations, meter upgrades and the capital components of wholesale and retail meter verification activities.

There are also special projects which are outside the sustaining capital program. These are:

- Capacity improvements for new customer connections and increased demand of existing customers.
- Developer Buybacks which involve BHI purchasing new subdivision assets as they are put in place by developers.
- Regulatory Requirements which are system capital investments driven by regulatory requirements. These directions may come from the OEB, IESO (Independent Electricity System Operator), the Ministry of Energy or the Ministry of the Environment.
- The Metrolinx Go Transit electrification project is a cost recovery project which will allow BHI to recover costs of staff and resources deployed to the project.

Forecasted capital expenditures from the Business Plan are presented as follows:



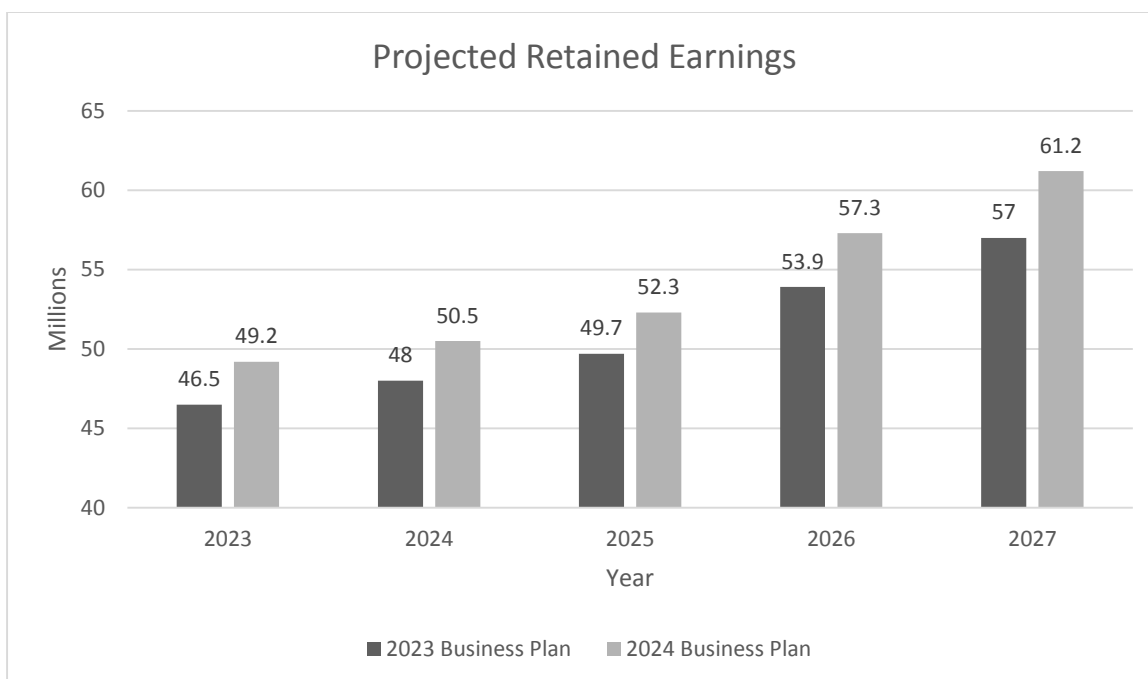
The 2023 capital budget has been developed using data from the asset management plan. The focus on maintaining the distribution system remains.

BALANCE SHEET

(i) Retained Earnings:

BHI continues to forecast retained earnings growth that represents value of increased ownership in a larger company. The following chart illustrates

retained earnings growth forecast in the first five years of the 2024 business plan:



(ii) Long Term Debt

- Financing the Smart Meter program (2010) with Infrastructure Ontario, loan has a 15-year amortization period at a fixed rate of 4.51% maturing in 2026.
- Financing the Hydro One Transformer Station capital contributions has a 25-year amortization period at a fixed rate of 4.02% and maturing in 2038.
- Loan matching long-term funding against BHI capital expenditures including the true-up payment for the Tremaine transformer station and the two Tremaine breakers. 15-year amortization period at a fixed rate of 3.63% maturing in 2033.
- \$5M of long-term debt is planned for 2024 to assist in financing the 2024 capital program.
- Total outstanding debt at the end of 2024 is forecast to be \$18.7M.

The 10-year time horizon forecasts additional borrowings of \$15 million until BHI's next rebasing application in 2026 and \$80 million over the forecast period. The company's capacity to borrow for capital projects is sound with a debt/capital structure within lender covenants.

The forecast also includes the costs of maintaining a \$20 million operating line of credit for working capital needs and an \$18 million letter of credit facility to cover prudent requirements related to the monthly power bill with the IESO.

BURLINGTON ELECTRICITY SERVICES INC. (BESI)

BESI is the sister company to the distribution company BHI. Unlike BHI, which is closely regulated by the OEB, BESI operates as an unregulated business. Its divisions include:

Festival of Lights Division: This division contains the annual costs of operating the Festival of Lights net of any sponsor donations.

Region Billing Division: Provides water billing services for the Region of Halton. The contract continues to contribute net income to the company.

Solar Array Division: Its revenues are derived from a solar array which was connected in 2012 to the City's Fire Hall 8. General maintenance of the array is the division's operating costs.

Electric Vehicle (EV) Charging Station Division: Installs charging stations for electric vehicles and achieves rental revenue from the stations. The program paves the way for key information on homeowner interaction with EV's and the electricity grid.

Mobile Turbine Co-Generator Division: This division holds the Mobile Turbine Co-Generator situated in the South Parking Lot of the Brant Street Office.

Control Room Division: This division provides control room monitoring for Milton Hydro.

Suite Metering Division: Provides suite metering services.

1328 Brant Street Building Rental: Leased office space to the city.

Operating expenses for BESI cover salaries and benefits, consulting services, legal services, promotion, and marketing costs. These are forecast to be unfavourable by \$19K.

Overall net income after tax is forecast to have a negative variance of \$60K. Unfavourable variances in the Regional Billing Division are only slightly offset by favourable variances in the other divisions.

Dividends

Annual dividends paid to the shareholder are composed of dividends from BHI operations, BHI working capital and BESI net income.

(in \$ Millions)	2024 Budget	2025 FCST	2026 FCST	2027 FCST	2028 FCST	2029 FCST	2030 FCST	2031 FCST	2032 FCST	2033 FCST
Dividends - BHI	2.7	2.2	2.2	3.5	3.6	3.6	3.6	3.7	4.5	4.7
Dividends - BESI	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.4
Total Dividends declared to Shareholder	3.1*	2.6*	2.6*	3.9	4.0	4.0	4.0	4.1	4.9	5.1

*Dividends declared are inclusion of special dividends not paid to the city. Included in the budget for 2024-2026 is a special dividend equivalent to the property lease with BEC for 1340 Brant as approved in report CM-27-22.

The increase in dividends starting in 2027 reflect expected revenues based on a cost-of-service application. The increase is not guaranteed and will be adjusted based on actual approval.

Shareholder Risks and Opportunities

- (I) **Regulatory/Political Risk:** As a regulated business, BHI is subject to the direction of Government legislated boards and committees. The 2018 provincial change in government has impacted the utilities particularly in conservation demand management programs which have been centralized under the IESO. Incentives related to the demand management program are no longer paid to the local utilities. Issues related to electricity are expected to remain in the public view.
- (II) **Cost of Service Review:** The OEB has established a five-year cycle in which the local distribution companies must undergo a full “cost of service” review. As a result of the 2014 cost of service review, the city was impacted by having the interest rate on the promissory note dropped from 5.87% to 4.88%. With the most recent rate application, the interest rate on the promissory note has reduced from 4.88% to 2.85% effective May 1, 2021. The original interest rate on the note was 7.25%. The following outlines actual cash flow received by the City from BEC;

(in \$ Millions)	2016	2017	2018	2019	2020	2021	2022	2023
Dividends	3.6	2.6	3.4	2.6	2.6	2.4	3.0	2.5
Interest	2.3	2.3	2.3	2.3	2.3	1.6	1.4	1.4
Interest on RESF	0.7	0.6	0.5	0.4	0.3	0.2	0.1	0.1
Total	6.6	5.5	6.2	5.3	5.2	4.2	4.5	4.0

(III) **Opportunities:** It is through BESI, the unregulated company that the shareholder has opportunities for strategic initiatives. BESI has set out as part of its overall business strategy to pursue in-scope services and new business ventures. Services that might be pursued would be intended to minimize risk to the taxpayers while representing an opportunity to establish and/or enhance existing common or shared services. Working strategically with Hydro management presents the city with an opportunity to find creative solutions that will ensure fiscal sustainability.

(IV) **ERM (Enterprise Risk Management):**

BHI employs ERM to monitor and assess risk in eight broad categories. A risk matrix is updated and reported quarterly to the BHI Board. The eight categories include:

- Operational
- Financial
- Profitability
- Reputational
- Compliance
- Regulatory
- Technology
- Strategic

BHI addresses the mitigation and impact of these risks in its Risk Management Plan and the ERM matrix.

Financial Matters:

The City's Hydro reserve fund is an integral part of the City's capital infrastructure program. It provides \$2.1 million annually to support the annual capital renewal program. Furthermore, it is anticipated over the next five years to be providing for the annual average repayment of approximately \$2.0 million in debt charges on special

circumstances debt towards major capital projects of varying types throughout the city. The reserve fund was previously relied on for City's storm allocation program until 2022 and is still relied on for direct cash contributions towards capital projects.

In 2023, Council approved an amendment to the Shareholder Direction to establish a new dividend policy (CM-03-23). This policy was intended to provide some stability to the annual dividend amount received. As per the policy regular dividends will be forecasted by the Board in an amount of, up to 50% of BEC's consolidated annual net income or \$2.4 million annually, whichever is greater. It should also be noted that BEC has declared special dividends to the city when circumstances allow. Additionally, the City receives interest on its promissory note which was reduced to 2.85% in 2021. This rate is set by the OEB.

The Hydro reserve fund is closely monitored, and adjustments are made as required to ensure a sustainable reserve fund balance.

Climate Implications:

To prepare for the transition from the use of fossil fuels to electrification in the community to mitigate greenhouse gas emissions, City Council approved a direction (EICS-11-22) requesting Burlington Hydro complete a Climate Sustainability report to prepare for increased demand. The study will assess the impacts on the local grid of the growth in electric vehicles and charging requirements, the greening of corporate fleets, bi-directional charging, thermal energy (heat for buildings), energy storage, renewable energy and, increasing use of battery electric equipment (i.e., lawn mowers, leaf blowers, etc.). Also included in the request is an assessment of climate projections and the forecasted impacts of a changing climate on the local grid and to prepare for grid resiliency. City staff are liaising with and supporting Burlington Hydro on this initiative; the report is targeted for completion by the second quarter of 2024.

Burlington Hydro is an active member of the Climate Action community stakeholder advisory committee, participates on the Climate Resilient Burlington Implementation Team, and provides regular updates to the committees on activities related to becoming a climate resilient, low carbon community.

Conclusion:

The City is appreciative of the efforts of the Board of Directors and Hydro Staff in continuing to manage this valuable City asset in a highly effective manner as reflected by the continued strong results forecast in the business plan and realized in the current year.

The City's 10-year Capital Financing Strategy is dependent on both annual dividends and interest on the note receivable.

Respectfully submitted,

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Notifications:

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Report Approval:

All reports are reviewed and/or approved by Department Director, the Chief Financial Officer and the Executive Director of Legal Services & Corporation Counsel.