

Staff Report

Statutory Closed Meeting Criteria:

This report meets the following statutory closed meeting criteria:

90(1)(g) - litigation or potential litigation affecting the municipality; and

90(1)(j) - information that is prohibited, or information that if it were presented in a document would be prohibited, from disclosure under section 21 of the Freedom of Information and Protection of Privacy Act.

Recommendation on Disclosure

Report to be released for public disclosure.

Origin

Richmond Olympic Oval Corporation (ROOC) management recently presented a closed Report to the ROOC Board of Directors which provided an in-depth update on VROX Sport Simulation Ltd (VROX) - a company for which ROOC is holding 50% of the shares. The Report addresses a number of important issues and contemplates either dissolving the partnership or reaching agreement on new terms on how the two parent companies will operate VROX, if the partnership is to continue. As VROX is a subsidiary of the ROOC, which in turn is a subsidiary of the City, it is important to ensure that Council are brought up to date on this latest development regarding VROX and that relevant background information on VROX be made available to the public.

Analysis

The Richmond Olympic Experience (ROX) was created in response to the City's desire to establish an exhibit which would commemorate Richmond's role as an official venue City for the 2010 Olympic Winter Games and celebrate the history of sport in Richmond. Council stipulated that the ROX should not be a traditional museum with static exhibits. The content should be highly interactive and include realistic sport simulations. A ski jump simulator operating in Japan was referenced as an example of the type of device that would meet Council's expectations.

VROX Sport Simulation Ltd (not to be confused with the ROX) was established to produce the sport simulators referred to above and to provide ongoing technical and maintenance support for the ROX.

VROX is the most recent business established amongst the City's various enterprises and it is unique in that it is a partnership, as opposed, to a wholly owned subsidiary-municipal corporation, as are both ROOC and Lulu Island Energy Company (LIEC).

In 2014, Richmond Olympic Oval Corporation entered into a partnership with VRX Ventures Ltd. to develop prototype sport simulators for installation in The Olympic Experience (ROX) at the Richmond Olympic Oval.

VROX Sport Simulation Ltd (VROX) - was established with each partner holding 50% of the company's shares, respectively. VROX is governed by a board consisting of eight director positions. ROOC has four directors and one technical advisor - all are Senior Staff members of either the Oval Corporation or the City. Staff who are involved with VROX are:

- John Mills, COO, Richmond Olympic Oval Corporation;
- Shana Turner, Director, Finance & Corporate Services, Richmond Olympic Oval Corporation;
- Robert Gonzalez, GM, Engineering & Public Works, City of Richmond; and
- George Duncan, CAO, City of Richmond; President & CEO, Richmond Olympic Oval Corporation

Technical Advisor to the Board

- John Irving, Director of Engineering, City of Richmond

VROX Board Directors receive \$1 per year in remuneration for serving on the Board. None of the ROOC or VRX Ventures Ltd senior personnel who are board directors and/or who have management roles and responsibilities associated with VROX receive any compensation for their service. Neither ROOC or City Staff perform work on behalf of or receive any form of compensation from or through the partner company, VRX Ventures Ltd.

VROX has one regular full-time employee (RFT) - an engineering design technician. The technician has considerable experience designing and building sport simulators and she is a graduate of the Camosun College Program, with which VROX has retained to assist in the development of VROX products. A temporary fulltime (TFT) Oval employee is seconded to VROX as needed to coordinate operations and oversee maintenance and installations. Various other Oval Staff contribute to VROX in minor roles on an as needed basis. VROX is charged-back for the cost of seconded Oval personnel.

The primary tasks for which VROX Sport Simulation Ltd was contracted by ROOC to complete are as follows:

- conduct the necessary research and development to produce prototype sport simulators for installation in the Richmond Olympic Experience (ROX) at the Richmond Olympic Oval;
- provide ongoing technical and maintenance support for the interactive and sport simulation devices operating in the ROX;
- utilize the ROX to showcase both VROX Sport Simulation and VRX Ventures products to potential commercial or retail purchasers; and
- conduct research and development needed to produce alternative and/or next generation sport simulators needed to refresh the ROX on an approximately two to three-year cycle.

VROX was needed due to both the ROX project teams and the design consultant's inability to find suitable commercial interactive digital and sport simulation products on the retail market. The option to commission the design consultant to develop prototype sport simulators was presented to the ROX project team at a cost that the project budget could not accommodate.

Although cost estimates as presented by the consultants appeared to be excessive, research verified that the referenced costs fell within industry standards for the necessary combination of research, development and manufacturing of sophisticated prototype devices. The team; however, also had other reservations and as a result, the ROX consultants were not retained to develop the custom designed prototype sport simulation products. The ROX team identified a potential partner with who the prototype sport simulator products could be developed at lower cost. It was also evident that the partnership option (VROX) would entail less risk and provide greater control over the choice of sport to be represented and the aesthetic appeal of the products.

Although entering into a partnership with a private sector company was not a typical option for the City or Oval, and was undertaken with considerable reservation, it was the only viable option at the time.

ROOC also had the option to retain the partner company to develop the prototype products at a targeted, but not fixed cost. The products would likely have been acquired at a lower cost than the consultant's estimates, but at higher cost than through the VROX partnership. ROOC, however would still have had to pay 100% of the cost while carrying all of the risk, and with the supplier owning all of the intellectual property rights (IP) to the new products. Under this option, the ROOC would have had to pay all costs, including assured profit for the supplier; and carried all of the risk, yet not have any rights to share in the proceeds of future sales in the event units would be sold to customers other than the Oval. Consequently, establishing the partnership, ROOC achieved five significant strategic advantages:

- Ensure the sport simulators would be delivered in time for the opening of the ROX;
- Enabled ROOC to acquire the prototype sport simulators at the lowest possible cost (cost incurred) to develop them exclusive of any mark-up or profit that would typically have had to be paid to the supplier; and/or consultants;
- ROOC, through VROX, would share ownership of the IP rights and/or patent, if applicable and be assured that ROOC would receive 50% of the net profit earned on any future sale of the products to customers other than the Oval;
- ROOC would have a high degree of influence, if not control over warranty and post warranty maintenance programs, costs and contracts; and
- ROOC would be in a position to ensure that any future investment in product development would be toward products that would meet ROX's future needs.

The Basis for the Partnership

The partnership was established based on the following arrangements:

- Partner company would provide the technical expertise; oversee VROX operations, including design, manufacturing, assembly, product consumer safety certification, and testing.
- ROOC would be the funding partner within budget parameters stipulated by ROOC Board.

- ROOC would commission VROX to develop a minimum of three prototype sport simulators at the prescribed standard and at a cost not to exceed the amount approved by the ROOC Board and/or referenced by the ROX professional design consultants.
- ROOC would provide access to the Oval and/or ROX, as needed to showcase the VROX prototype products and the Oval's partner's products, to prospective purchasers.
- VROX would only manufacture products ordered or commissioned by ROOC and/or for sale to other customers, with external orders supported by a cash deposit. VROX will not produce products on speculation; however, sport simulators produced for the Oval may, with approval from ROOC, be utilized at trade shows or other relevant venues for retail sales and promotional support purposes.
- Both partners will receive a 50% share of net profits on any simulators sold to purchasers other than those built specifically for the Oval.
- ROOC will market the products and make best efforts to introduce the VROX products to other high performance sport related agencies.

Summary:

The arrangements on which the partnership was based more than adequately served ROOC's needs as demonstrated in the following summary:

ROOC would acquire sport simulation products it needed for installation in the ROX at a cost that is significantly lower than estimated by the project consultants; within a time frame needed to meet the scheduled opening date for the ROX; have direct control over both the budgets and choice of sports to be simulated; and retain the right to receive 50% of the net profit earned on the future sale of any VROX products to customers other than the Oval. As a result, any net revenue earned from future sales would reduce/offset the cost incurred to develop the first generation prototype sport simulators needed for the ROX.

Limited Access to Information on VROX

Due to the Oval Corporation having only 50% interest in VROX which is a private company, VROX is not subject to transparency and reporting regulations such as Freedom of Information and Privacy Act (FOI) as is the case with the City and Oval. Consequently, access to information about VROX is less readily available than would otherwise be the case.

VROX being designated as a private company and therefore not being subject to the same transparency and public reporting regulations as ROOC or the City is an unintended consequence of establishing VROX that neither ROOC or City Staff had anticipated or recognized would be the case. Consequently, the ROOC team is taking steps to address this aspect of VROX. Staff have commenced discussions/negotiations with our partner to either dissolve or change the partnership in order to address this concern.

Having acknowledged Staff's intention to negotiate changes to the partnership that will ensure that VROX will become subject to the same regulations as the Oval. It should also be noted, however, that during the interim numerous steps have been taken to ensure access is available to information about VROX. For example, through its connection to the ROOC, VROX audited financial information is presented in the Notes to ROOC's audited consolidated financial

statements. Further, the City’s and ROOC’s external auditors, KPMG, are also VROX’s auditors, thereby ensuring that all VROX financial matters and transactions must be administered to the same standards as the Oval and/or City. VROX is also required to use ROOC and/or City policies to guide VROX practices and in order to ensure consistency; the ROOC’s Financial Controller also serves as VROX’s Financial Controller. Staff also propose, through this staff report, to release background information on VROX that would otherwise not be accessible by the public.

Finally, all VROX financial documents and information are readily available and presented to the ROOC board and/or Council in a similar manner to all other City-owned enterprises.

Other Business

ROOC and VROX are also presently in the process of sales discussions with two separate customers. The potential value of these sales, if completed, will significantly offset the cost ROOC incurred to develop the prototype simulators for ROX.

ROOC received a significant benefit through establishing VROX, in the form of the delivery of three high quality, reliable, and aesthetically appealing sport simulator products that were developed through the partnership, and would not otherwise have been available. Based on the terms of our arrangement; however, ROOC’s partner will not receive any financial benefit from VROX until a sale is completed to a customer other than the Oval.

In this regard, the ROOC and VROX have been pursuing new sales leads. The details of which although having been presented to the ROOC Board and Richmond City Council will not be released at this particular time.

Business Development:

ROOC’s primary needs in regard to VROX are centred on maintenance support for ROX and periodic development of new products. External sales would also benefit ROOC because they would help to offset ROX costs for the prototype simulators; however, ROOC is not prepared to develop product on speculation or to incur costs for marketing on speculation.

VROX Financial Performance During Start-up At a Glance

2016 VROX Unaudited financials	2015 VROX Audited financials	2014 VROX Audited financials
\$ 63,248 Plus SR&ED incentive funding not yet applied for, but application pending	\$70,879 Plus awaiting SR&ED incentive funding-application value is \$115,000 for 2014 & 2015	<\$107,094> Plus awaiting SR&ED incentive funding

Note: Due to the timing of the pending approval of the SR&ED incentive funding, if approved it will impact VROX's 2017 financials.

\$1,685,000	Total ROOC authorized funding to VROX to date.
\$1,385,000	Total funding VROX has received from ROOC as of December 31, 2016
Simulators: 2 bobsleigh 1 bobsleigh (shell) 1 sit-ski 1 kayak	Total VROX products received by ROOC and/or work in progress to date.

Financial Impact

N/A

Conclusion

VROX met its first objective and priority by delivering three prototype sport simulators on schedule and under budget to the ROOC.

VROX has been an effective source for the supply of the specialty products needed for the ROX and offers alternatives which is a necessity to considerable potential to deliver additional benefits through future retail market sales.

ROOC has been moving VROX into a maintenance focused mode of operation; however, if the pending orders for VROX products are confirmed VROX will have to transition back to design and production mode in a very short time frame.

Staff should make the necessary changes to the partnership and/or Company Articles to ensure VROX will operate under the same regulations that apply to ROOC as operating as a municipal corporation.



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