

4. Public Excluded Financing Consideration: Ferry Precinct Development (iReX) Business Case

(Clr Peters) (Report prepared by Martin Fletcher)

S400-004-001-21

Purpose of Report

1. To consider Port Marlborough NZ Ltd's (PMNZ) proposal to spend up to \$110M on the iReX Picton Ferry Terminal Redevelopment and how the transaction should be financed.

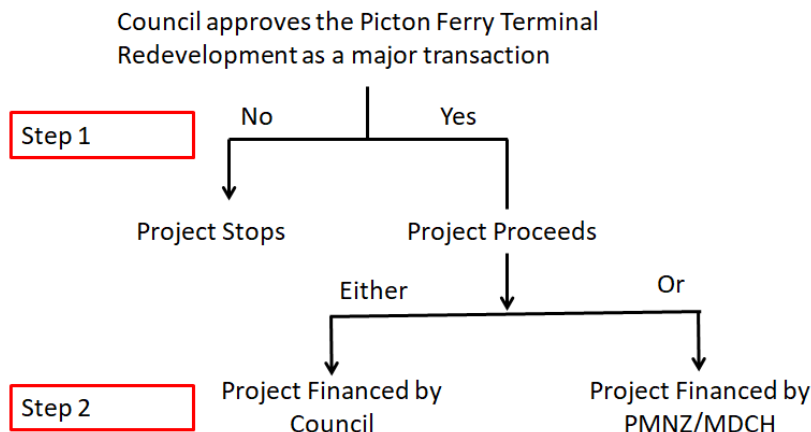
RECOMMENDATIONS

That Council:

1. agree to MDC Holdings Ltd (MDCH) and PMNZ proceeding with the iReX project as a major transaction subject to the outcome of consultation; and
2. agree to consult on raising \$110M of debt to finance PMNZ's share of the iReX project.

Background/Context

2. The decisions being asked of Council are a two-step decision process. The first is whether or not Council agrees to MDCH and PMNZ proceeding with the redevelopment of the Picton Ferry Terminal Redevelopment as proposed in the **separately attached** Business Case. If Council agrees to the first recommendation, the second decision is how the project should be financed. The two options are either:
 - a. Council raises the finance from the Local Government Funding Agency (LGFA) and on lends to MDCH and PMNZ; or
 - b. PMNZ raises the finance directly.



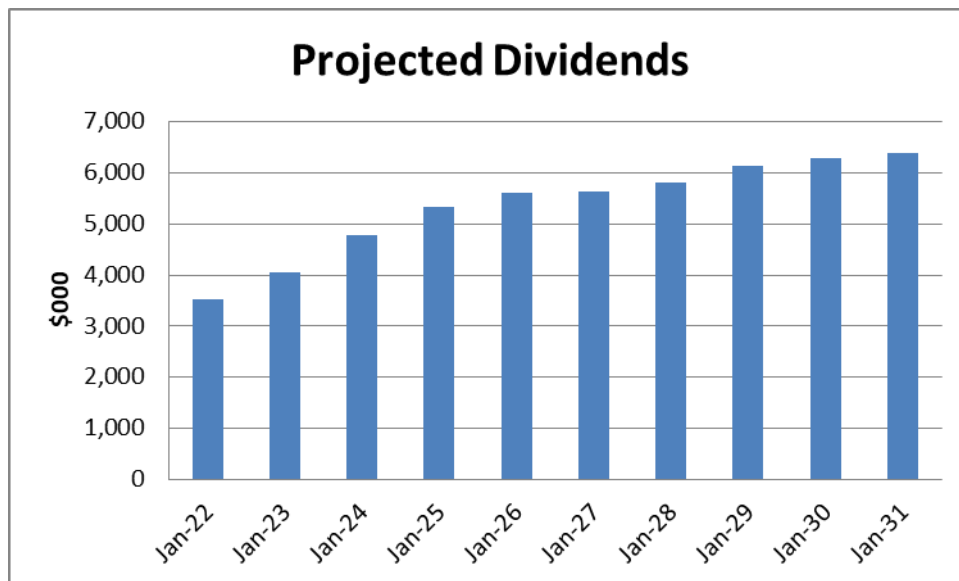
3. What follows is a description of the progress made to date, a description of the project from PMNZ's perspective and the Companies Act 1993 requirements relating to a major transaction.
4. After extensive negotiations with KiwiRail, PMNZ has reached agreement on how the Picton Ferry Terminal redevelopment should proceed. This agreement includes:
 - a. the principles under which the redevelopment will occur;
 - b. preliminary design;
 - c. the assets to be owned by PMNZ;

- d. PMNZ's financial contribution;
 - e. financial returns; and
 - f. a number of risk mitigations. The risk mitigations include reducing the level of capital investment to acquire new ferry precinct assets from an earlier contemplated \$150M+ to \$110M.
5. The agreement was approved by the PMNZ Board on 12 November 2021 contingent on:
- i. approval by special resolution of MDC Holdings Ltd as a major transaction under Section 129 of the Companies Act 1993; and
 - ii. approval of funding by Marlborough District Council.
6. The agreement was approved by the MDCH Board on 2nd December 2021 contingent on:
- i. approval by Council for MDC Holdings Ltd to undertake the financing of the project as a major transaction under Section 129 of the Companies Act 1993; and
 - ii. approval of funding by Marlborough District Council.
7. Rhys Welbourn, Chief Executive, PMNZ will provide a presentation on the key terms contained in the PMNZ/KiwiRail agreement and resulting business case approved by the PMNZ Board.
8. At \$110M the transaction is defined as a **major transaction** in accordance with S129(2)(a) of the Companies Act 1993 (\$110M / total PMNZ assets of \$217M = 50.7%). As such the transaction must be approved by a special resolution. The Companies Act 1993 defines special resolution as “a resolution approved by a majority of 75% or, if a higher majority is required by the constitution, that higher majority of the votes of those shareholders entitled to vote and voting”.
- As MDCH is the only, i.e. 100% shareholder of PMNZ a simple majority of the MDCH Board was required, which occurred on 2 December 2021.
9. In regard to MDC Holdings Ltd, the transaction represents 47.5% of its consolidated asset value. As such while not strictly required, it would be prudent for Council to approve the transaction by way of special resolution.

Assessment/Analysis

10. As identified earlier, Rhys Welbourn, PMNZ's Chief Executive will provide a presentation on the project. Also **separately attached** are PMNZ's Business Case and Risk Mitigation Schedule which were considered by the PMNZ Board.
11. While the Business Case covers the proposal in more detail, the key points of the Business Case are:
- a. It secures Picton's position as the gateway to the South Island for at least the next 30 years;
 - b. It facilitates KiwiRail operating significantly improved ferries from not only an environmental, but also a wake reduction perspective;
 - c. The funding being sought is \$110M and for that Port will provide the following non InterIslander specific facilities:
 - i. a new 264 metre wharf;
 - ii. provision for a possible cruise berth;
 - iii. linkspan, seawalls, revetments and scour protection; and
 - iv. improvements to access, parking, landscaping storm water treatment and connections with the town centre and foreshore.
 - v. Also, while not part of the Business Case, KiwiRail will build an overbridge at Dublin Street and make a significant contribution towards upgrading the Waitohi Culverts. Other intersection improvements are also possible on State Highway One in Picton. These projects are ranked first in the Regional Land Transport Plan, but the timing for them proceeding is Waka Kotahi's decision.

- d. A return on capital of 6.1% post tax leading to increased dividends to MDC Holdings Ltd and in turn Council.



In addition to increased dividends, the benefit to the MDC group from this project is far greater in cash terms as there is also the cash represented by depreciation and the % of Post Tax Profits retained by PMNZ. The total benefit is over \$7.5M per annum (2027).

- e. Numerous risk mitigations, including:
- i. locking in whole of life design principles to ensure quality of the whole development is maintained;
 - ii. KiwiRail taking the construction cost and timing risk;
 - iii. Only agreeing to provide generic non KiwiRail specific assets, which PMNZ can use for other purposes should the lease not be extended for its second 30 year term;
 - iv. frontloading of lease payments which enables an acceleration of debt repayment on a fixed fee basis, which means that PMNZ is not exposed to KiwiRail's volume risk;
 - v. a balloon payment of 39% of the depreciated value of Port's assets should KiwiRail not exercise its renewal option at the end of the first 30 year lease term. This together with iv) and PMNZ adopting the strategy of committing project free cash to debt repayment will mean that the \$110M advance will be repaid before the end of the first lease term; and
 - vi. agreeing to pay the cost of debt in the event of a force majeure event occurring that doesn't reduce PMNZ's ability to operate, e.g. Wellington is unable to operate.

12. There is significantly more detail on the project's scope, financials and risk mitigations in the **separately attached** Business Case.

13. Conversely if Council decided not to agree to the project, then Government would be required to take over the project and part of PMNZ's area. The consequences of that are that some of benefits that have been secured as part of the negotiation may be lost. Certainly what would be lost are not only the increased dividends, but also a reduction of approximately \$1M of existing dividends. The current wharf and terminal are ending their economic life and in the near future will no longer generate revenue. As a result, the loss in cash terms to the MDC group is far greater as there is also the cash represented by depreciation and the % of Post Tax Profits retained by PMNZ. The total loss is over \$3M.

Summary

14. The iReX project is the biggest project undertaken in Marlborough's history. The Port Marlborough team has negotiated extremely well on our behalf, achieving good financial returns while also minimising/mitigating project risks.

15. As a result it is recommended that Council agree to MDCH and PMNZ proceeding with the iReX project as a major transaction.

Financing Options

16. On the assumption that Council agrees that PMNZ should proceed with the project, the two financing options are:
 - a. Council raises the finance from the LGFA and on-lends to MDCH and PMNZ; and
 - b. PMNZ raises the finance directly.
17. The advantages of option, “a” are:
 - a. The LGFA has been expressly established to provide low cost finance to Council's. As a result, Council will be able to finance at a lower cost than PMNZ.
 - b. As a result of “a.” above, this will increase profits and dividends to ratepayers, thereby reducing future rates.
 - c. The debt raised does not impact on the calculation of Council's “Debt Cap” as the “Cap” is net debt and the additional debt is offset by the loan made to MDCH.
18. Council should also note that S&P Global has very recently reviewed Council's credit rating. On 30 November 2021 S&P decided Council should retain its AA+ Long term rating. This is an excellent result that Marlborough retains its place as one of the top rated local authorities in New Zealand, only just below the New Zealand Government's AAA rating. S&P also because of the “larger infrastructure program at both Council and Subsidiary level”, revised Council's outlook from stable to negative. Council should note:
 - a. this rating applies to the whole Council Group and that S&P were copied the IREX Business Case to assist in their evaluation;
 - b. S&P's “base case excludes the potential effect of the Crown government's proposed "three waters" reforms. The reform program, as currently envisaged, could see responsibility for drinking water, wastewater and stormwater assets taken away from councils and amalgamated into four new regional water service entities from mid-2024. The reforms are still under development”
 - c. S&P went on to say “If the "three waters" reforms proceed, it is possible that Marlborough will offload a significant proportion of its debt (and related water assets and revenues) to one of the proposed water service entities. This could improve its group debt burden. It isn't yet clear if the reforms will be enacted in their current form, or when they may take effect. The reform program faces hurdles in the form of resistance from many council sector representatives and the national opposition party”.
 - d. the change in outlook has no impact on the cost of debt finance to Council. In fact even if Council's rating was reduced to AA, (still an excellent rating that's better than that held by New Zealand's four major trading banks), it still wouldn't have any impact on the cost of Council debt.
19. The minor disadvantage is that the increased debt appears on Council's “parent” balance sheet.
20. In addition, there is a Matched Funding Facility Agreement in place between MDCH and PMNZ dated 1 April 2011. The agreement stipulates that PMNZ will not create any security interest over any part of its assets and that on the occurrence of a number of default events any advances made to PMNZ become immediately repayable. There is a matching agreement between MDCH and Council dated 30 August 2017 when Council took over responsibility for debt financing its subsidiaries.
21. There is no real advantage of PMNZ raising the finance for the project directly as provided by option “b”.

22. The disadvantages are:
- a. Advice has been received that the interest PMNZ would have to pay a bank is 1 to 1.5% higher than the interest rate Council would pay. This reduces dividends to Council and reduces the margin between the fee paid by KiwiRail and the cost of interest, i.e. increases the project's risk.
 - b. Banks would require security, initially from MDCH and then Council. These securities could take the form of subscribed uncalled capital or Council guarantee.
 - c. On preparing Council's consolidated financial statements, PMNZ's debt would appear on the Consolidated Balance Sheet of the MDC Group.

Summary

23. The advantages of Council raising the finance needed for this project significantly outweigh the disadvantages especially in regard to financial benefits to ratepayers from increased dividends. As a result it is recommended that Council agree to consult on it raising \$110M of debt to finance PMNZ's share of the iReX Picton Ferry Precinct Development Project.

Next step

24. The next step is to undertake formal consultation in terms of the Local Government Act 2002. Please see the next Agenda item with a proposed consultation document and consultation plan.

Presentation

25. A presentation on the business case will be given by Rhys Welbourn – Chief Executive Port Marlborough NZ Ltd.

Attachments

- Attachment 4.1 – Covering letter from Keith Taylor – Chairman, Port Marlborough New Zealand Limited Page 16
Attachment 4.2 – Ferry Precinct Development Business Case separately attached
Attachment 4.3 – Waitohi Picton Port Access Single Stage Business Case - Update Page 17

Author	Martin Fletcher, Chief Financial Officer
Authoriser	Mark Wheeler, Chief Executive



26 November 2021

Attn: Marlborough District Council Holdings Ltd

Dear Directors

Subject Reference – Letter Subject name

The board of Port Marlborough last week considered the business proposal to invest \$110 million into port developments as part of KiwiRail's iRex project.

As you are aware this follows a very protracted process, discussions and negotiations with KiwiRail. The board are unanimously of the view that the finally negotiated position is a positive one for Port Marlborough and appropriately balances risk, return and capital availability. Our management team have done excellently in bringing this proposal together.

Therefore the board have approved the business proposal subject to:

Your approval of the proposed major transaction and capital investment of \$110 million to acquire new ferry precinct assets

The securing of debt funding for the project from our ultimate shareholder Marlborough District Council (MDC) which requires your support.

Rhys, his senior team and I look forward to discussing this with you next week.

Sincerely



Keith Taylor
Chair – Board of Directors
Port Marlborough New Zealand Limited

WAITOHI PICTON PORT ACCESS SINGLE STAGE BUSINESS CASE

Background

The draft Waitohi Picton Access single stage business case (SSBC) has been developed collaboratively by Waka Kotahi, Marlborough District Council, KiwiRail, Port Marlborough, and Marlborough Roads. It recommends a package of transport network investments for Picton to enable the introduction of two larger capacity ferries by KiwiRail through the Inter-island Resilience Connection project (iRex).

The SSBC aims to:

- improve experience and access within Picton, while allowing the Port operations to handle current and future passenger and freight movements
- improve transport safety amongst the community and visitors by managing conflicts at key points, and
- avoid severance of the community and disruption of local and regional access while allowing longer trains.

Recommended programme

The recommendations in the draft SSBC were developed together with the project partners, and with input from key stakeholders. Figure 1 below summarises the recommended programme of infrastructure activities including the expected funding and delivery owners, and indicative timing of delivery.

Figure 1: Project Delivery

Activity	Funding source(s)	Delivery owner	Timing
Dublin St Walking and Cycling	MDC + Waka Kotahi	MDC	Operational before Day one 2024.
Dublin St Overbridge	TBD	KiwiRail	Operational before train arrives - Day one 2024
Auckland St Footpath improvements	MDC + Waka Kotahi	MDC	Implement at the same time as cul-de-sac due potential safety issues
Dublin / Auckland signalised intersection	Waka Kotahi	Waka Kotahi	By 2029 - Predicted gap in LOS
Wairau / Broadway Level crossing safety improvements and Broadway cul de sac	KiwiRail + Waka Kotahi	KiwiRail	Level crossing and cul-de-sac operational Day one 2024

Kent / Wairau Roundabout	Waka Kotahi	Waka Kotahi	Operational before Day one 2024
Wayfinding	Waka Kotahi	Waka Kotahi	Operational before Day one 2024
Kent St Safety improvements	Waka Kotahi	MDC	Operational before Day one 2024
Lagoon / Dublin Roundabout upgrade	Waka Kotahi	Waka Kotahi	Operational before Day one 2024
Kent St Footpath improvements	Waka Kotahi	MDC	Operational before Day one 2024

In addition to the above infrastructure interventions, the draft SSBC recommends Auckland Street be revoked to local road and Kent Street reverts to State Highway. Kent Street currently functions as a State Highway with the bulk of inter-regional traffic using this to access the Port. The SSBC also recommends a truck parking strategy be developed.

Business case completion

The draft SSBC is yet to be finalised and the recommended programme, costs and funding sources are therefore still indicative until it is finalised. The key outstanding elements of the business case are the financial case (who pays for what) and management case (how / when improvements are to be delivered). These elements require coordination and agreement between Marlborough District Council, KiwiRail and Waka Kotahi prior to the business case being completed.

Other remaining tasks required to complete the business case include:

- Review of Kiwirail's revised Outline Plan of Works and Integrated Transport Assessment to ensure the recommendations in draft business case are still appropriate
- Parallel cost estimate
- Safety audit
- Waka Kotahi investment quality assurance (IQA) review

We are aiming to complete the SSBC in the first quarter of 2022.

Waka Kotahi Investment

In general, Waka Kotahi will 100% fund State Highway infrastructure that would be required regardless of the iREX programme. Other infrastructure will require co-investment, or full investment, from other partners, as indicated in Figure 1.

Funding has been signalled as 'probable' in the National Land Transport Programme (NLTP) for the Waka Kotahi improvements recommended in the SSBC. There is also an activity in the NLTP for the Dublin Street overbridge. This activity was included in the Regional Land Transport Plan and NLTP to signal that it needs to be delivered in the 2021/24 period. At the time of the RLTP being developed and the NLTP published, we hadn't confirmed who the responsible party was to fund and deliver the activities identified in the business case so had included this activity as a place holder to give it visibility for the region. Waka Kotahi is currently re-evaluating this project against the Waka Kotahi investment criteria to determine if it meets the criteria for investment from the NLTP. As noted in Figure 1, this is yet to be confirmed.

Once the business case has been completed, Waka Kotahi will request a variation to the NLTP (if required) to formalise the Waka Kotahi and Marlborough District Council activities that will be delivered in the 2021-24 NLTP period. This will unlock implementation funding.

5. Public Excluded Statement of Proposal Document: iReX Project

(Report prepared by Martin Fletcher)

S400-005-006-01

Purpose of Report

1. To consider the draft Statement of Proposal (SoP) for financing the Picton Ferry Precinct Development (iReX) Project and related community engagement plans.

Executive Summary

2. The Picton Ferry Precinct Development is a significant project requiring public consultation. **Attached** is a draft of the SoP, which is still subject to legal review by Simpson Grierson. The paper also identifies other means for providing information and receiving feedback from the community.
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RECOMMENDATIONS

That Council:

1. **adopt the draft Statement of Proposal (SoP) for the Picton Ferry Precinct Development, subject to legal review by Simpson Grierson;**
 2. **note the intention to engage directly with the community as part of the consultation process;**
 3. **agree to establish a sub-committee of the Mayor, Deputy Mayor and Councillor Peters to finalise the document post legal review; and**
 4. **agree to move this agenda item out of public excluded when the SoP is issued to the community.**
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Background/Context

3. At a value of \$110M, the Picton Ferry Precinct Development Project meets the definition of a significant transaction. While financial provision was made in the 2021-31 Long Term Plan (LTP), this project was specifically excluded from consultation on the LTP on page 4 of the Consultation Document (along with Three Waters reforms). It is now time to undertake consultation on this project, firstly on whether or not this project should proceed and secondly, on whether the project should be financed by Council or directly by Port Marlborough NZ Ltd (PMNZ).
4. The attached draft SoP:
 - a) identifies the proposal and the reasons for the proposal; and
 - b) provides an analysis of the reasonably practicable options including their advantages and disadvantages.
5. The options identified include:
 - i. proceeding with the project and financing it using funds raised by Council;
 - ii. proceeding with the project and financing it using funds raised by PMNZ; and
 - iii. not proceeding with the project.
6. The SoP also identifies when consultation will open, how a submission can be made, closing date for submissions, submission hearing dates and when Council is likely to make a decision. If the Christmas/New Year period falls in the middle of the consultation timeframe an extension on the normal one month has been provided for.

7. In addition to undertaking SoP based consultation, Council also intends to:
- provide coverage of this proposal in its Council pages.
 - provide opportunities for direct resident feedback. These opportunities may include drop-in days, public briefing/meeting, engagement with Iwi and specific interest groups and webinar. The final form and number of events has yet to be finalised. The final decision may depend on what is permissible under COVID-19 restrictions.
8. Also, because of the significance of this project, both financially and due to its impact on the District, it is proposed to have the draft SoP reviewed by Simpson Grierson for legal compliance. It was not possible to complete this step before the finalisation of this agenda item.

Attachments

Attachment 5.1 – Statement of Proposal

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Author	Martin Fletcher, Chief Financial Officer
Authoriser	Mark Wheeler, Chief Executive Officer