greater WELLINGTON
REGIONAL COUNCIL

Report 11.292
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Council
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WRC Holdings Group final Statement of Intent

1. Purpose

To receive the final Statement of Intent (SOI) of WRC Holdings Limited (WRCH).

2. Significance of the decision

The matters for decision in this report do not trigger the significance policy of the Council or otherwise trigger section 76(3)(b) of the Local Government Act 2002.

3. Background

The Council considered the draft SOI for WRCH at their meeting on 5 April 2011 after the Chair had a received a copy in late February. The Council did not request any changes for the WRC Holdings Board.

The final SOI has been updated with CentrePort's updated financial forecasts incorporating the sell down of Harbour Quays buildings. This proposed sale has yet to be approved by the shareholders.

CentrePort have advised us that a final SCI will not be available until July.

4. Changes from the draft SOI

The changes can be divided into two categories, the words and the numbers.

4.1 Changes to the words

The following notable alterations have been made to the SOI.

Activities of the Group – Section 3.2

This section has been reorganised to reflect the fact the Group is made up of a number of entities, with each entity now having a heading. The section on Greater Wellington Rail Limited has been updated to reflect the recent negotiations with KiwiRail. It now better reflects what rail stock and assets the company currently owns and may acquire.

Environment, Social and Financial Targets – Section 4.0

This section has been reorganised to include all the performance targets in a more logical order, with CentrePort's targets now included under Port Investments Limited.

Financial Information – Section 6.0

The numbers have been updated with the changes since the draft SOI. A line in the equity section of the balance sheet has been added to record an inflation component increase on the Mandatory Convertible Notes, these are discussed further under section 4.2.3 CentrePort Limited.

Assumptions in preparing the prospective financial statements – Section 6.8

A paragraph has been added – second bullet point to reflect the transfer of rail assets from KiwiRail.

Issues facing the Group – Section 7.0

The section on CentrePort and Greater Wellington Rail has been updated to reflect recent changes.

4.2 Changes to the numbers

4.2.1 Pringle House Limited

Some minor adjustments were made to rental revenue and insurance. Insurance was increased to reflect the sharp upward move in premiums which had the overall effect of reducing the subvention payment to Greater Wellington by $187,000 in 2011/12 and $118,000 in both 2012/13 and 2013/14.

4.2.2 Port Investments Limited

Some minor adjustments were made to reflect a smaller dividend from CentrePort. These were offset to some extent by increasing subvention payments from CentrePort, providing an overall favourable impact of $47,000 in the 2011/12 year and unfavourable impacts of $159,000 and $296,000 in the 2012/13 and 2013/14 years respectively. These adjustments have the impact of reducing the dividend to WRC Holding and ultimately to Greater Wellington.

4.2.3 CentrePort Limited

The updated net profit after tax has reduced as follows, $579,000, $1,144,000 and $911,000, for the three years. This has been driven by higher insurance and fuel costs, but offset to some extent by higher revenues.

Capital expenditure has been increased by $1.2 million over the 3 years along with the reduced operating profits referred to above; therefore, the dividend paid by CentrePort has been reduced by $250,000, $500,000 and $600,000. Ten thirteenths of this dividend is payable to Port Investments limited.

CentrePort has incorporated accounting entries to record the partial sell down of their Harbour Quays buildings to a Special Purpose Vehicle (SPV).

This transaction sees an immediate reduction in debt of $75 million and creation of a liability of mandatory convertible notes. The notes are inflation linked, thus the notes value increase with the rate of inflation. The notes require interest to be paid at a fixed rate of 6% per annum on the outstanding balance. As a result the note liability increases over time. This increase is recorded in non-current liabilities as an increase in the notes value as well as an offsetting inflation charge to Equity.

The offset to the above increase in equity is not recorded in the plan as it is a basic planning assumption that unrealised property valuations are not budgeted. If such valuations were to be recorded then it is expected that the Harbour Quay assets would move up in value and the offsetting entry would be to Equity, thus offsetting the inflation adjustment referred to above.

After 12 years the mandatory convertible notes convert to equity in the SPV with an adjustment in the value settled at this point.

4.2.4 Greater Wellington Rail Limited

An update on the timing of the Matangi and the Ganz Mavag trains has seen both repairs and maintenance and depreciation increase, which is offset by an increase in grants.

The loss after tax has increased as the non cash impairment has increased, due to the timing of the train purchases and the rate of the impairment in the value of the equity investment in the trains. This has had a significant adverse impact in terms of the Group's profitability.

The impairment is an accounting adjustment that recognises a reduction in the value of the equity investment in the trains. It is calculated at 20% and 40% of the depreciation amount per year on the trains respectively.

The trains have been purchased by Greater Wellington Rail Limited, via a 20% and 40% equity injection from WRC Holdings and an 80% and 60% grant from Greater Wellington respectively for the Matangi and the Ganz Mavag.

The equity contribution for the trains was previously calculated at 10% but this has been increased to 20% in the case of the Matangi to reflect the reduction in the Government contribution to the project, and 40% to the Ganz Mavag.

Over time, Greater Wellington Rail will continue to make a loss until such time as the equity contributed equals the sum of all the annual impairments and also at which point depreciation on the trains will cease.

Rental revenue received from the Matangi and the Ganz Mavags is now being recognised, reflecting the fact that the train operator, KiwiRail, will pay a market rental for use of the trains. This is calculated as an 8% return on the capital cost contribution by WRC Holdings.

4.2.5 WRC Holdings Limited

The impact of the CentrePort dividend flows through as noted above and the impairment of investment has increased due to the timing of the Matangi and Ganz Mavag projects.

Performance Targets

	2011/12 ($000)	**2012/13 ($000)**	**2013/14 ($000)**
Surplus before tax - Final	12,625	11,287	10,844
Surplus before tax – Draft	*14,466*	*14,937*	*15,133*
Surplus after tax- Final	8,692	7,427	6,715
Surplus after tax – Draft	*9,847*	*10,250*	*10,482*
Earnings before interest and tax- Final	42,475	46,340	48,513
Earnings before interest and tax – Draft	*43,471*	*48,045*	*52,481*
Return on total assets - Final	4.17%	3.64%	3.39%
Return on total assets- Draft	*4.46%*	*4.04%*	*3.79%*
Return on shareholder equity - Final	3.87%	2.60%	2.01%
Return on shareholder equity – Draft	*4.81%*	*4.43%*	*4.24%*
Dividends – Final	2,304	2,380	2,497
Dividends- Draft	*2,257*	*2,358*	*2,793*

As can be seen from the above table, profitability is down on the February draft SOI. This is being driven by an increasing impairment of investment, between the two SOIs and between years as the impairment moves up from $1,262 in 2011//12 to $4,097 in 2013/14.

The contribution from CentrePort is also down in June compared to February, deteriorating from $359,000 in 2011/12 to $898,000 in 2013/14. The key drivers for this deterioration are rising insurance and fuel costs.

5. Communications

No communications are necessary.

6. Recommendations

That the Council:

1. ***Receives** the report.*

2. ***Notes** the content of the report.*

Report prepared by: Report approved by:

Mike Timmer
Treasurer

Bruce Simpson
Chief Financial Officer

Attachment 1: Final WRC Holdings Group Statement of Intent