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Financial Strategy

Christchurch City Three Year Plan
Christchurch Ōtautahi

Photo: City Care – 'Paving the way'

Christchurch City Council

Financial Strategy

Introduction

This section explains the financial strategy included in the Three Year Plan for the Council to manage its share of the costs of the earthquake rebuild (consisting of operating deficits, response costs, infrastructure rebuild and anchor projects) as well as continue to provide its levels of service to the community. The strategy builds on the previous strategies adopted by Council as part of the 2011/12 and 2012/13 Annual Plans and contains the latest-available information on cost forecasts, government subsidies and insurance proceeds. The strategy also takes into account the latest-available information on the Crown's recovery plans and its commitments to cost sharing for the rebuild.

Background

Council's financial strategy for funding its share of the earthquake recovery costs was adopted during the Annual Plan deliberations in June 2012 and June 2013.

The strategy comprised three main elements:

- Council Operating Deficits.
  Forecast operating deficits of $83.4 million for the three years to June 2014 (largely the result of reduced operating revenue and the impact on the Council's rating base) was funded by a special earthquake charge for five years. The 1.76% charge was increased to 1.82% in 2012/13 when Council resolved to increase its rates remissions. This charge was intended to raise sufficient funds over five years to repay the borrowing and interest on three years of operating deficits. After the five-year period of the charge, the increase in rates revenue from this special rate will be used to contribute towards the repayment of the earthquake response and recovery costs outlined below.
- Earthquake Response and Recovery Costs.
  Total earthquake response and recovery costs were estimated to be $3.373 billion. Funding for these costs is expected to come from a combination of insurance, government subsidies (NZTA, MCDEM and CERA), deferral of a portion of the Council's renewals programme and the special rate mentioned above.
- Major Community Facilities Rebuild.
  The Council made a commitment to the community to repair or rebuild ten major community facilities. The cost of these rebuilds was largely insurance funded with improvements planned for the facilities funded through the Council's Improvement Allowance and a one-off 1.84% major community facilities rebuild charge. This charge raises sufficient additional rates to ensure the incremental debt required to build improved facilities is repaid over 30 years.

Financial Strategy for 2013-16 Three Year Plan

Council will continue to fund its normal activities and capital works programme in accordance with its existing Revenue & Financing and Liability Management Policies.

These policies provide as follows:

- Total operational costs of $410 million in 2013/14 are funded by $122 million of fees, charges and operational subsidies with the residual funded through rates, reserves and investment income. Cost and revenue projections are provided in the detail of the Three Year Plan.
- Renewal of existing Council assets of $188 million over three years (excluding earthquake damage) is funded through NZTA subsidies on roading projects and rates.
- Capital projects either for growth, or for new or enhanced Council services, are funded through borrowing. Debt servicing (interest plus debt repayment over 30 years) on growth projects is funded through development contributions and on other projects by rates. The Three Year Plan forecasts $389 million of growth and aspirational projects over three years (excluding earthquake recovery projects outlined below). The majority of these projects provide infrastructure required for the growth of the city, in particular new subdivisions.

In addition to these operating and capital costs, Council faces significant costs for its share of the earthquake response and recovery costs and the costs of rebuilding its major community facilities. Funding for these costs are outlined below.

Council Operating Deficits

The table below shows the actual and projected Council operating deficits as a result of the earthquakes. In 2012/13 Council projected that operating deficits as a result of the earthquakes would persist for three years. The annual deficits incurred are not as large as was predicted, however are now expected to last five years.

$ million	11/12 Actual	12/13 Forecast	13/14 Plan	14/15 Plan	15/16 Plan
Interest Costs	-0.2	-1.2	-1.2	-1.0	-0.5
Rates Remissions / Growth	-5.6	-4.5	0	-1.6	-0.8
Dividends	-10.5	-6.0	0.0	0.0	0.0
Parking Revenue	-8.1	-6.7	-5.9	-4.5	-3.0
Rental Revenue	-0.9	-0.9	-0.9	-0.9	-0.9
Facilities Operating Savings	5.5	4.2	0.9	0	0
Insurance Costs	-0.8	-4.8	-5.9	-5.9	-5.9
Council Costs / Savings	6.7	-8.6	-3.1	-1.0	-1.0
Total Operating Deficit	**-13.9**	**-28.5**	**-16.1**	**-14.9**	**-12.1**
2012/13 A/P Forecast	**-30.2**	**-29.1**	**-20.9**	**-2.2**	**-0.9**

After updating the forecasts, the cumulative deficits of $85.6 million over the five-year period are projected to be slightly higher than previously estimated ($83.4 million).

Council resolved to fund these deficits through a Special Earthquake Charge. A charge of 1.76% in 2011/12 and 1.82% from 2012/13 to 2015/16 raised sufficient revenue to repay the borrowing and interest on the three years of operating deficits.

The Three Year Plan includes an increase in the Special Earthquake Charge to 1.93% for its three remaining years

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(though until 2015/16). This ensures that enough revenue is raised to repay the forecast operating deficits (including interest) by the end of 2015/16.

Response and Recovery Costs

Response and Recovery costs encompass costs incurred by the Council in the immediate emergency response after the earthquake, the ongoing maintenance of temporary infrastructure and the cost of rebuilding Council's infrastructure (roads, water and wastewater networks) and buildings. These costs also include an allowance of $225 million for improvements to assets the Council approves during the rebuild process. This estimate has also been updated to include the Council's share of the costs of the Anchor Projects contained in the Central City Recovery Plan.

Over the past 12 months the Council, together with its funding partners (CERA and NZTA), has worked to update the previous work done to provide a better estimate of the total cost of rebuilding the city's damaged infrastructure and facilities.

The 2012/13 Annual Plan acknowledged that further investigation was required to the previous estimate of the response and recovery costs and that the final costs would vary. This is because the 2012/13 estimate was based on visually-observed damage and level of service deterioration rather than the more intensive asset investigation and planning that's now been possible. Notwithstanding this, this asset investigation is still only 50% complete so there remains a level of uncertainty around the final quantum of damage, which will further affect the final overall costs. The cost sharing agreement with the Crown provides that the final Council and Crown contributions could change as a result of further independent estimation, due for completion by 1 December 2014.

The updated financial forecasts for the response and recovery costs have been developed jointly by Council, NZTA and CERA based on information provided by SCIRT and a team of independent reviewers. The overall estimate includes a provision of $398 million for savings to be agreed with the Crown and subject to the independent estimation mentioned in the paragraph above.

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($ million)	Estimated Cost	Insurance Cover	Government Subsidy	Other Contributions	Net Cost to Council
Infrastructure (Below Ground)					
Roads	758	-	526	-	232
Sewer	1,450	140	870	-	440
Water	106	28	64	-	14
Stormwater	334	13	200	-	121
Savings to be agreed with Crown	(398)	-	(239)	-	(159)
	2,250	**181**	**1,421**	**-**	**648**
Buildings, Facilities and Other Assets					
Buildings and Facilities	276	266	-	-	10
Anchor Projects	783	370	-	-	413
Sewer above-ground assets	139	139	-	-	-
Water above-ground assets	20	20	-	-	-
Stormwater above-ground assets	2	2	-	-	-
Park Facilities	2	2	-	-	-
Council Buildings / Infrastructure - improvement allowance *	160	-	-	-	160
Increased Costs of Working	21	4	9	-	8
Uninsured Assets (Parks, Stormwater)	94	-	-	7	87
Insurance Excesses	29	-	-	-	29
	1,526	**803**	**9**	**7**	**707**
Emergency & Response Costs					
Roading Emergency Work	96	-	68	-	28
Welfare and other emergency work	68	-	54	-	14
Other response costs	50	2	36	1	11
Maintenance of Temporary Services	335	18	187	1	129
Demolition Costs	11	-	11	0	(0)
Rockfall	84	-	14	-	70
Unbudgeted Staff Costs	11	-	-	-	11
	655	**20**	**370**	**2**	**263**
Total Costs	**4,431**	**1,004**	**1,800**	**9**	**1,618**

* The total allowance is $225 million of which $65 million is included in the Anchor projects

Council will continue to work with CERA to ensure both Council and the Government receives value for money in the rebuild of infrastructure and facilities.

The previous table shows that Council's estimated contribution to the earthquake response and recovery costs is $1.618 billion. Of the total costs of $4.431 billion, $1.004 billion is covered by insurance and $1.800 billion is covered by the Crown's expected contribution to the response and recovery costs under the cost sharing agreement. The total does not include further Crown contributions of $1.088 billion to the jointly-funded Anchor Projects.

The cost recoveries assume:

- Underground Assets. Council has already settled for $201 million of insurance cover from the Local Authority Protection Programme (LAPP) for the repair of its underground assets. The total amount paid by the LAPP programme is the maximum amount possible due to the reinsurance taken by the programme. NZTA subsidies for eligible roading have been assumed at 83% as approved by the NZTA Board. Crown Subsidies of 60% on underground assets are based on the cost sharing agreement.
- Buildings, Facilities and Other Assets. The forecasts assume Council secures insurance settlement for rebuild/repair of its facility assets on a like-for-like basis (less a 2.5% excess). Any improvements or strengthening of Council assets in excess of their pre-earthquake strength is assumed to be funded through a $225 million "improvement allowance" in these estimates. This category of costs includes $94 million of estimated costs for remediating assets that were not possible to insure such as parks, riverbanks and riverbeds (dredging). The Council share also includes $11 million for repairs to the composting plant, which was not insured, and the 2.5% excess on buildings claims.

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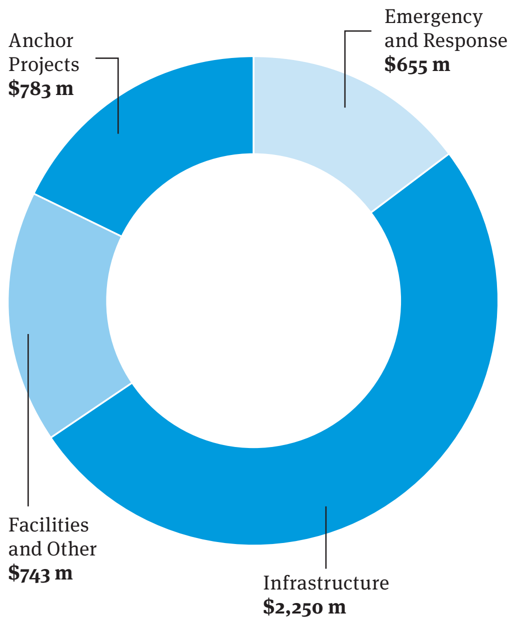
- Emergency & Response Costs. Of the $654 million expected to be incurred for emergency and response costs, $335 million relates to maintaining temporary infrastructure (such as above-ground water supply lines and temporary stopbanks) until permanent repairs are completed and/or the residential red zones are vacated. Government subsidies are expected as follows: NZTA subsidies for roading work of 75% for 2010/11 and 83% subsequently, 100% for eligible Welfare costs, 60% for ongoing maintenance of temporary works (100% for the February 2011 emergency period), 60% for rockfall and demolition costs. The rockfall costs include a 50% Council contribution to the Crown's purchase of properties threatened by rock roll or mitigation costs.

The financial strategy in this Three Year Plan and budget is based on the assumption the Council receives its full insurance entitlement. The Council has not factored in a possible shortfall from re-insurance "challenges". The quantum (if any) of the shortfall should be known by October 2013. A shortfall would put pressure on the budget and could lead to the Council reviewing this plan and making adjustments in the second and third year of the plan.

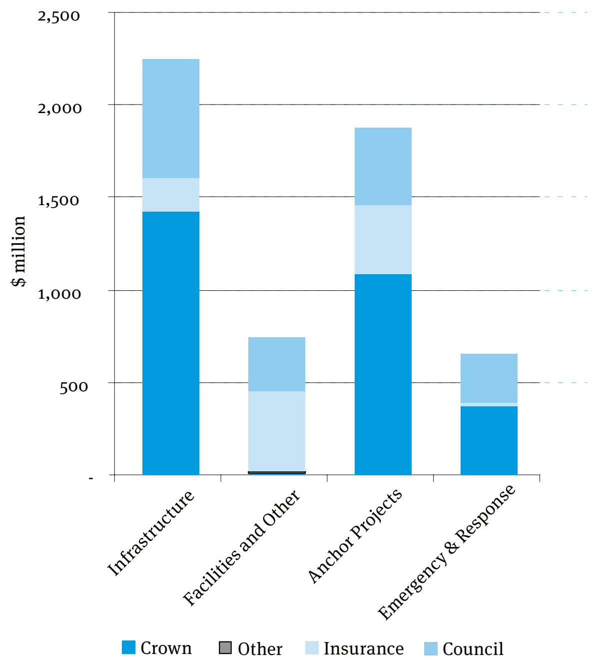
The Council acknowledges that it has signed a binding agreement on funding the re-build with the Government and this has been committed to and cannot be changed (unless agreed by both parties).

The charts below illustrate how the total response and recovery costs are split between emergency & response costs, costs of rebuilding key infrastructure, and costs associated with repairing and rebuilding the Council's facilities. The costs for facilities includes the Council's contribution to joint projects with the Crown. The chart on the right shows the assumptions made with respect to funding and is consistent with the cost sharing agreement. It includes the $1.088b Crown funding of Anchor projects.

Total Response and Recovery Costs
$4,431 million



Relative Funding Shares



Consistent with the financial strategy adopted by Council last year, Council will fund its share of the response and recovery costs through a combination of its asset renewal budget and the increase in rates revenue available from the Special Earthquake Charge after the operating deficits are repaid in 2015/16.

The infrastructure rebuild programme is expected to rebuild up to 40% of the city's infrastructure; assets that would have been replaced by Council's normal asset renewal programme over the next thirty years or longer for some assets. For this reason, it is possible for the Council to use part of its asset renewal budget over that period to repay the debt it takes on to fund its share of the rebuild. The financial strategy includes debt repayments from rates of $50 million for 2013/14 (in addition to $150 million from the period 2010/11 – 2012/13), $40 million per annum for the following five years and $25 million per annum for the following thirteen years (plus inflation). This provides over $900 million towards the repayment of the required debt.

[1] *The actual proportion differs according to asset class and value. The most significant portion of the rebuild by proportion is the sewer network with an estimated 41% damage by length. The roading network has an estimated 11% damage by length.*

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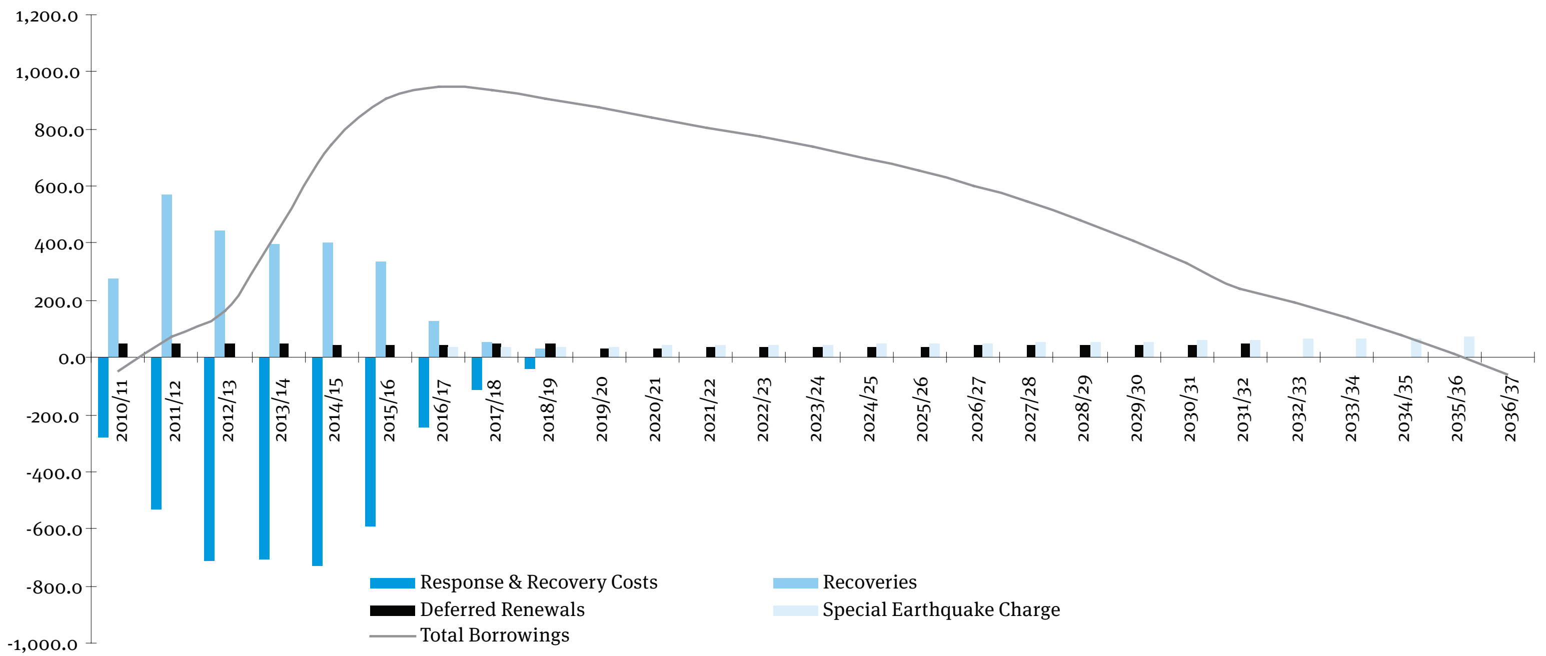
Combined with the additional rates revenue forecast to be available from the Special Earthquake Charge from 2016/17 onwards, the renewals saving will repay the response and recovery costs in 24 years (2036/37), well within the 30-year limit in the Council's Liability Management Policy.

The next chart shows that Council borrowings for response and recovery costs increase as the rebuild progresses and peaks at $946 million in 2016/17. As the upfront costs of the rebuild subside, the borrowings are then repaid during 2036/2037 (24 years).

Response and Recovery Costs and Council Borrowing



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Major Community Facilities / Anchor Projects

As part of the 2012/13 Annual Plan, the Council resolved to rebuild or repair ten major community facilities, those being:

- Christchurch Convention Centre
- Former AMI Stadium
- Lichfield and Manchester St Carparks
- Central City Multi-Sport Facility
- Christchurch Town Hall for the Performing Arts
- Central Library
- Christchurch Art Gallery
- South-West Library and Service Centre
- Eastern Aquatic Facility
- Athletic Track Replacement

The Council also made a $6.4 million commitment to the Avon River Park.

As part of the cost sharing agreement, the Council agreed to increase its contributions to the anchor projects included in that Plan. The table below summarises the Council's agreed position with the Crown.

		Council Funding Source:			
	Council Contribution	**Insurance**	**Land**	**Imprvmt**	**Borrowing**
Convention Centre Precinct	0.0	30.6	10.8		-41.4
Stadium	253.0	143.0			110.0
Carparking	70.0	41.7	15.0	12.9	0.4
Metro Sports Facility	147.0	77.6			69.4
Town Hall / Performing Arts	157.5	68.9		51.3	37.3
Memorial	0.0				0.0
Central Library	60.0	8.2	27.2	0.5	24.1
Avon River Park	6.4				6.4
The Square	4.6				4.6
Transport Interchange	39.9		39.9		0.0
Transport Plan - Phase 1	27.0				27.0
Escalation	17.5		0.9		16.6
Total	**782.9**	**370.0**	**93.8**	**64.7**	**254.4**

The total Council contribution to these projects is estimated to be $783 million and is partly funded by insurance proceeds on damaged facilities of $370 million. The strategy assumes that land sales of former sites will contribute $94 million to the costs, leaving Council to borrow a total of $319 million to fund its share.

This residual cost to Council results from recommendations to strengthen or significantly improve these assets. Some of the projects, such as the proposed Hornby Service Centre, Central City Multi-Sport Facility or Stadium, represent substantial new facilities, while others, such as the Town Hall or Art Gallery projects represent major improvements to the pre-earthquake facility.

The Council will fund the $319 million net cost partly through the response and recovery infrastructure / buildings improvement allowance ($64.7 million) with the remainder funded through borrowings, to be repaid over 30 years in line with the Council's Revenue & Financing Policy. As well as the improvement allowance, Council had allowed for borrowing capacity in its 2009/19 Long Term Council Community Plan, (LTCCP) to fund growth and aspirational projects. These projects include a number which are replaced by the anchor projects in this Three Year Plan.

To fund part of the borrowing required, the Council introduced a 1.84% charge as a one-off increase in the 2012/13 Annual Plan. This Major Community Facilities Rebuild Rates Charge will raise sufficient additional rates to ensure the incremental $163 million of debt required to rebuild these facilities is repaid over 30 years. For the average ratepayer, the cost of servicing this additional debt represents $3 per month in rates

The assumptions above assume that insurance settlements on the Council facilities will be concluded as outlined. Council staff and advisors have been working with our insurer's loss adjustors to quantify the damage, repair or reinstatement costs and to establish agreement on Council's insurance entitlement against each facility.

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Under its policy wording, Council is entitled to claim for the repair or rebuild of damage to a facility to the greater of 33% of the New Building Standard or its pre-earthquake strength and up to scheduled value (adjusted for cost escalation to 110%). The estimates of insurance proceeds presented reflect the best advice the Council has to date, but have not yet been agreed to by the Council's insurers. Council staff are continuing to work with its insurers to present and settle its insurance claims. These will be brought back to Council for final approval.

Rating Base Growth

Prior to the earthquakes, Christchurch City Council enjoyed steady growth in its ratepayer base of around 1% per annum, resulting in a $3 million increase to rates revenue each year. However, this growth declined in recent years due to slower natural population growth (ie. subdivisions, residential and commercial building activity) and the demolition of earthquake-damaged properties. As at June 2013, the city's capital value is forecast to have reduced by $1.549 billion since 2010/11 as a result of 2200 residential (value $536 million) and 1300 commercial demolitions (valued at $1.013 billion). This is partially offset by subdivision and building activity of $841 million during the same period. Further demolitions to the value of $1.5 billion are expected until 2014/15, including the final demolitions within the CBD cordon and the residential red zones ($50 million commercial and $1.45 billion residential).

Through an Order in Council, the government has allowed Council the ability to decrease rates when a property is demolished and to increase rates when a property is rebuilt. This removes the ongoing need to grant remissions for demolished properties, because rates on those properties would immediately revert to land value only.

Over the past three years, the capital value of the city has declined as a result of the demolitions of residential and commercial properties in the city. The land value has remained intact because, until the next revaluation is completed at the end of 2013, Council continues to use 2007 valuations. Immediately following the earthquakes, there was a decrease in subdivision and building activity, which resulted in fewer new ratepayers in the city. Combined with the impact of demolitions on capital value, this meant that existing ratepayers faced a higher rates increase than if there had been normal growth.

The budgets in the Three Year Plan assumes this trend reverses for several reasons. Firstly, the majority of the residential and commercial demolitions will be nearing completion by the end of 2013/14. Council has already removed as many properties as possible from its valuation roll. Secondly, the level of subdivision activity has increased as has both residential and commercial building activity. The financial strategy assumes that net growth returns to historical levels in 2013/14 and then accelerates in the following four years before returning to historical levels in 2018/19 and beyond. An offsetting reduction in capital value is assumed in 2014/15 and 2015/16 to reflect possible future decisions on rezoning land purchased by the Crown.

Total Council Borrowing

The magnitude of the costs faced by the Council means that if it is to keep rate increases to an affordable level and deliver the rebuild within an acceptable period of time, it must increase its debt levels. However, as is outlined above, the increase in debt required over the next eight years will be repaid by Council within 30 years thereby returning the Council to a financial position similar to where it would have been prior to the earthquakes.

The chart below demonstrates this. The black dotted line represents Council's ratepayer-funded debt (ie. excluding debt required for the rebuild). This is the debt projected to be incurred for aspirational and growth projects on the basis that rates in future years, received from those ratepayers who are benefiting from those new assets, are servicing the debt on those new assets. This is known as intergenerational equity. The level of this debt continues to grow with the size of the city so the relative cost per ratepayer decreases.

The blue line on the graph shows Council's total debt projection as a result of the infrastructure rebuild and facilities rebuild borrowing required.

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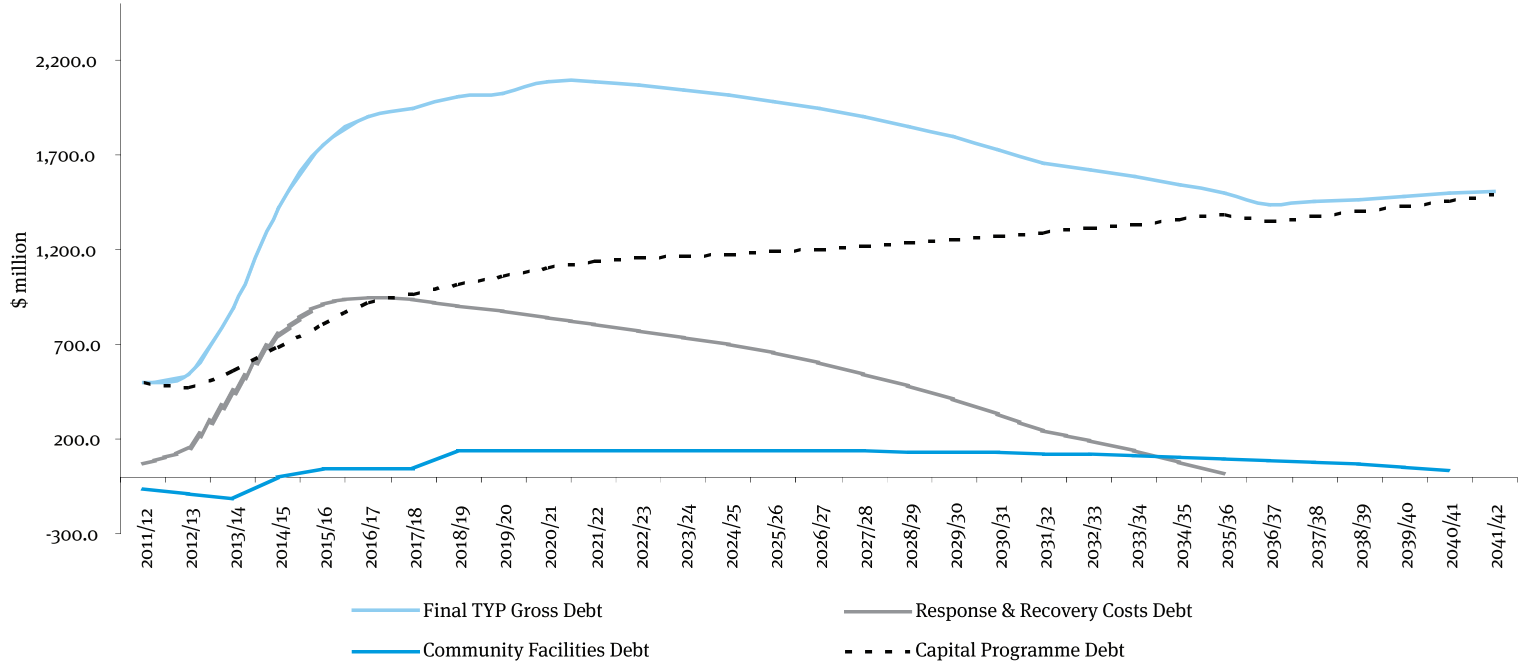
CCC Total Projected Debt



The graph shows that to fund its share of the rebuild, Council needs borrow more funds over the first eight years than would have been the case in the absence of the rebuild. However, as explained in the previous sections, the debt required for the rebuild is repaid within a 30-year period, which returns Council to a level of debt that is affordable to its ratepayers.

Council is conscious both of the amount of debt it needs to take on, as well as the affordability of that debt. In its foundation policies, the recently-established Local Government Funding Agency (LGFA) established debt covenants that govern the total amount of debt a local authority may borrow from the Agency. Council has ensured that it remains within both the affordability (net interest as a proportion of rates) and quantum ratios (net debt as a proportion of total revenue). Council's Liability Management Policy limits have been amended to align them with the LGFA's foundation policy limits.

Compared with the LGFA's limit of 250% for net debt to total revenue and 30% for net interest to rates income, Council's debt is forecast to increase with the ratios peaking in 2016/17 at 236% and 19% respectively.

The charts below demonstrate that although Council's total debt levels climb over the next eight years as a result of the rebuild, the strategy for repaying this debt ensures the city's total debt declines over time. In addition, because the city continues to grow, so does its rates and total revenues. By controlling the increase of debt following the rebuild process, Council's key debt covenants decline to conservative levels, which will in turn restore Council's high credit rating.

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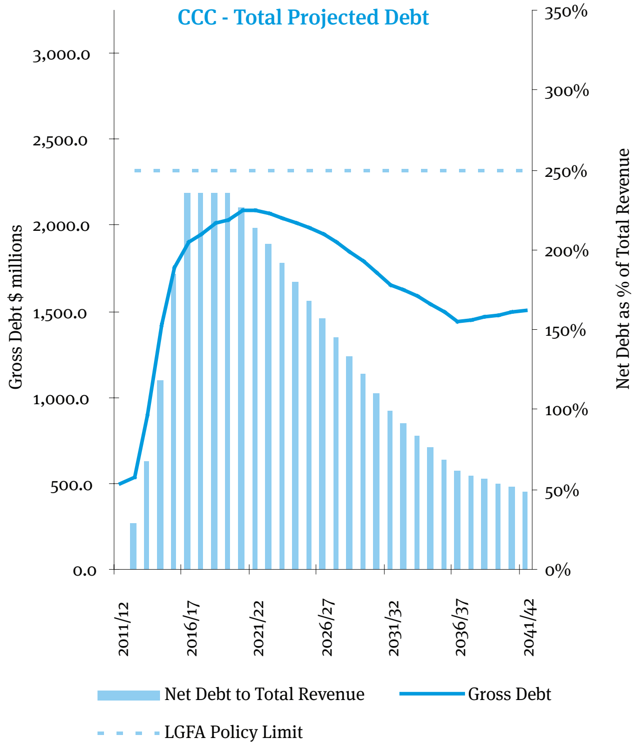

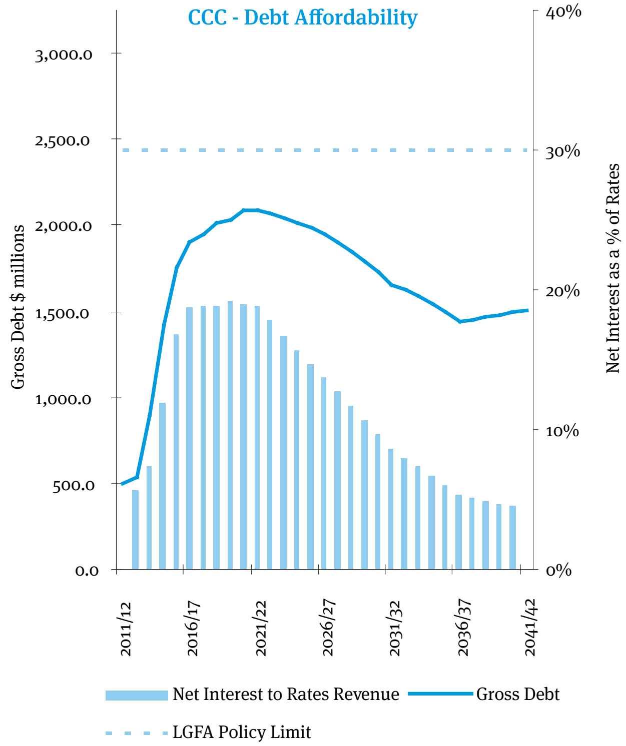

The increase in debt in the short to medium term may lead to a further decrease in the Council's credit rating. In its most recent review, Standard & Poors commented that while they consider the Council's financial strategy to be prudent, Council's credit rating would likely be reviewed if its net debt exceeded 180% of revenue or net interest 9% of revenues. Council debt ratios peak in 2016/17 as a result of the rebuild borrowing; if the rebuild programme proceeds as forecast, Council will exceed these two ratios, but not the LGFA's covenants. In addition, Standard & Poors focuses on total Council group revenues and debt (ie. including CCHL), which improves the ratios due to CCHL's strong operating revenues. This will have a marginal impact on interest rates, which are built into the existing budgets. Notwithstanding this, it is expected the Council's credit rating will be restored over time as the certainty around Crown contributions increases and the debt returns to LTCCP levels.

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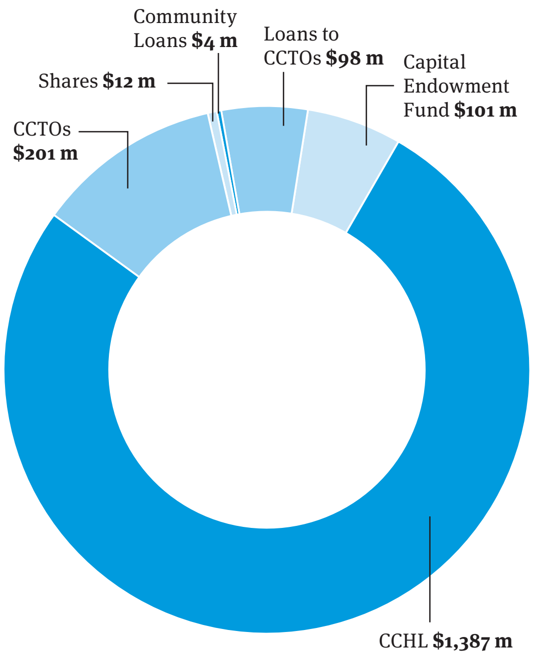
Investments

Excluding short-term cash balances, Council holds $1.8 billion of investment assets made up as follows

Total Council Investments at 30 June 2012 - $1,804 million



In considering its financial position during the development of the Three Year Plan, the Council discussed its ongoing ownership of these investment assets. As a result, the financial strategy does not propose that any Council investments are sold during the life of the TYP. The financial returns from the investments are built into the forecast revenues in the financial strategy.

Council's objectives for holding and managing these investments are as follows:

- Christchurch City Holdings Ltd (CCHL). CCHL is the holding company for the Council's trading assets. The Council's objective for owning CCHL is that the company monitors the Council's existing investments, which largely service the city's infrastructure assets. Including the appreciation in the capital value of its investments, CCHL has achieved returns over the past five years, which average in excess of 9% per annum; 15.6% per annum since its inception in 1995. The Council is targeting annual dividend payments from CCHL of between $46 million and $48 million over the three years of the TYP. Further information on CCHL's subsidiary companies is provided in the TYP and in the companies' statements of intent.
- Capital Endowment Fund. In April 2001 Council set up the Capital Endowment Fund using the proceeds from the sale of Orion's investment in a gas company. The Fund provides an ongoing income stream which is applied by Council to economic development and to community events and projects. The fund is invested according to the Council's Investment Policy and is projected to make returns averaging 5.02% over the life of the TYP.
- Share investments. The Council has made several equity investments in companies that provide services to local government or to facilitate economic development. These companies and the target investment returns are as follows:

Share Investments	Target Investment Returns
New Zealand Local Government Funding Agency	Target returns are 2% above the LGFA's cost of funds
New Zealand Local Government Insurance Corp	No investment return forecast in current SOI
Transwaste Ltd	Transwaste target returns are 9% return on its capital (as per Transwaste SOI).
Endeavour Icap	No financial return expected; investment is for economic development

- Council-controlled Trading Organisations. Council has made equity investments in Vbase Ltd, Tuam Ltd, Civic Building Ltd and Canterbury Development Corporation Holdings Ltd and from time to time extends loans to these organisations at market rates. The CCTOs are established to enable administrative efficiencies to be achieved, for example as property owner for Council assets where a commercial business model is appropriate. No financial return is expected from these equity investments during the life of the Plan.
- Community Loans. From time to time the Council makes loans to community groups to enable them to pursue their stated objectives. The return on these loans ranges from interest free through to 8% depending on when they were granted and the conditions imposed on them at the time.

With regards to CCHL's subsidiary companies, Council considers that the strategic reasons for ownership combined with the total shareholder returns outweigh the risk of continued Council ownership. Therefore there is greater value for Council to retain ownership than to sell any of these companies. The table at appendix 1 outlines key advantages and counter-arguments of continued Council ownership of these companies.

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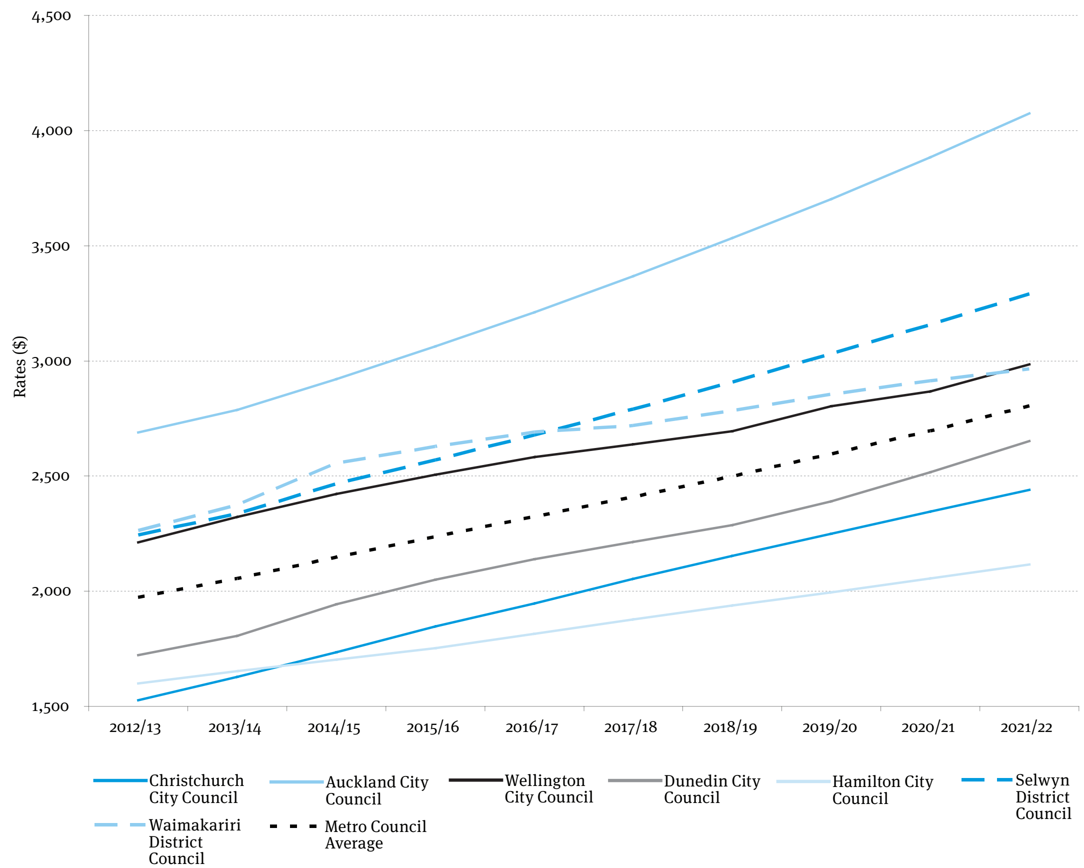
Christchurch City Council Rates Compared with other Metropolitan Councils

Similar to the relatively low levels of existing debt, Christchurch's rates levels remain low when compared with other metropolitan (and neighbouring) councils. The chart below shows that despite the special rates charges for funding community facilities and Council's short-term operating deficits, Christchurch's rates remain more than 15% lower than the forecast average of these other metro Councils, surpassing only Hamilton.

Estimated Average Residential Rates By Metro and District Council



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Summary

The table below provides a summary of the Council's financial strategy:

Funding required for	Consisting of	External Sources of Funds	Council Share Funded by
Council Activities - Operating Costs	Operational costs of $1.275 billion over three years.	• Fees and Charges under the Revenue & Financing Policy cover 32% of operating costs • NZTA subsidies available for eligible roading works (approx $44 million over three years)	• Rates including Special Earthquake Charge • Interest and dividends
Council Activities - Capital Renewals	Capital costs of $188 million over three years	• NZTA subsidies on eligible works	• Rates
Council Aspirational & Growth Projects	Aspirational and growth capital programmes of $389 million over three years	• NZTA subsidies on eligible works	• Borrowing per Liability Management Policy • Growth Projects funded by Development Contributions
Earthquake Response & Recovery Costs	Total costs of $4.431 billion, with a net cost to Council of $1.618 billion	• Government subsidies estimated at $1.800 billion subject to review by 1 December 2014 • Insurance proceeds of $1.004 billion	• Deferral of $943 million of capital renewals over 20 years • Increased rates revenue from Special Earthquake Charge from 2016/17 ($32.8 million per annum)
Anchor Projects (included in above line)	Total Council contribution of $783 million	• Insurance proceeds ($370 million)	• Council Infrastructure / Buildings Shortfall Allowance ($65 million) • Proceeds from land sales of $94 million • Borrowing of $254 million funded by Major Community Facilities charge and rates over 30 years

The strategy requires Council to increase its borrowings over the next five years to fund its share of the emergency costs and the costs for rebuilding its infrastructure and facilities. The increased borrowing is repaid through a combination of a Major Community Facilities Rates Charge, savings of $943 million through the capital renewals programme and higher rates revenue after five years of the Special Earthquake Charge.

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Appendix 1 - Considerations in Ongoing Council Ownership of its Trading Companies

Advantages of Council Ownership	Counter-arguments to Council Ownership
• **Synergies.** Provides opportunities for broader Council / Community objectives to be reflected in the companies' objectives. Allows companies to proactively respond to community aspirations such as climate change, energy use, sustainability, and social equity in a more direct and binding manner.	• **Synergies.** Community values should be reflected in regulation, policy and incentives that are transparent and contestable. The use of Statements of Intent to influence commercial behavior can lead to sub-optimal business performance.
• **Local control.** While operating on a commercial basis, wider economic benefits to the region are taken into account – largely through the Statement of Intent process (eg. recognition of Council strategies etc). CCHL is a successful model for ensuring that intervention is by way of guidance rather than direct lobbying or interference with recognised best practice board governance processes. The model reflects similar principles adopted for Crown commercial enterprises.	• **Local Control.** This can lead to mixed messages for the companies and reduce efficiency or returns if companies are required to compromise their potential rate of return. Companies associated or linked to Council may also perceive an inability to act as commercially as competitors.
• **Asset reliability.** A public owner of key infrastructure is more likely to accept a lower return in the short term to ensure there is sufficient investment into these assets for the long term (eg. investment in increased network resilience, or proactive asset maintenance).	• **Asset reliability.** The private sector has strong incentives to invest in asset reliability and maintain the performance of its assets to ensure it maximizes profits. Further it will not over-invest or 'gold-plate' its assets. Council-controlled companies may be less inclined to reduce services, reduce quality of assets and infrastructure due to community expectation.
• **Investment returns**. CCHL has generated greater than 15% per annum shareholder returns since inception. Current dividend forecasts ($46 million in 13/14) lower Council rates required by 15%. The total shareholder returns exceed the Council's cost of capital in investing in these companies. Independent professional directors appointed to CCTOs can be as effective at ensuring efficiency in Council-owned companies as those with private sector ownership.	• **Investment returns.** Notwithstanding that total returns to Council are higher than the cost of capital, dividends to Council are less than interest forgone on potential sales proceeds. An alternative shareholder may bring additional value to these companies and private sector ownership ensures better efficiency.
• **Pricing**. Where there is no effective competition in a market, the existence of a Council-owned company can stimulate pricing and help to ensure that pricing for CCC tenders is competitive or control pricing where there is a monopoly provider.	• **Pricing.** This is only true where markets are not mature and in most instances of monopoly, pricing is regulated.
• **Future potential.** Also known as "option value", this enables future flexibility with these assets. Eg. Port redevelopment, Orion windfall, Enable investment. If they are sold this value is gone.	• **Future potential.** Council should not be exposed to unnecessary commercial risks – for example, Council's ownership may be questioned where it owns assets that are speculative, high risk or for purposes not connected to the well-being of the community.
• **Long-term investment horizon.** Because they have an owner who is focused on long-term outcomes, the companies have a greater ability to invest in the long-term, where profitability may take some time but creates gain where aligned to the strategies (Community outcomes) of the city.	• **Long-term investment horizon.** This investment exposes ratepayers to risk that the private sector is not prepared to accept. If the investment is made by the Council, it should be sold once it becomes commercially viable to reduce the commercial risk.
• **Stability of ownership.** Strong stable ownership can create a competitive advantage for the operating companies. Private sector owners are more likely to seek profit in a shorter timeframe & not be as prepared to invest in the long-term.	• **Stability of ownership.** Stability of ownership can also be achieved through a strong private-sector parent. A private sector parent may also bring other skills and experience that add value to the companies.
• **Availability of capital.** Council decision-making to make further capital available will be moderated by how the investment contributes to commercial and non-commercial outcomes for the city. The Council could choose to allow its companies to access normal capital markets (CCTOs already raise debt capital through the normal market).	• **Availability of capital.** A wider range of capital raising options is available to privately-held companies. Exposure to capital markets places stronger commercial disciplines on businesses.

Christchurch City Council

Financial Strategy

Appendix 2 – Financial Strategy Statutory Disclosures

The requirements of s101A of the Local Government Act 2002 are met by the disclosures outlined in this Financial Strategy and elsewhere in the Three Year Plan. There are several other required disclosures, which are outlined below.

Policy on Giving Securities

When the Council's borrowings and interest rate risk management instruments are secured, they will generally be secured by way of a charge over the Council's rates revenue. Any internal borrowing against special funds / reserve funds and other funds will be on an unsecured basis. Under the Debenture Trust Deed the Council offers deemed rates as security for general borrowing programs.

From time to time, with prior Council and Debenture Trustee approval, security may be offered by providing a charge over one or more of the Council's assets. Physical assets will be charged only where:

- there is a direct relationship between the debt and the purchase or construction of the asset which it funds (e.g. an operating lease, or project finance)
- the Council considers a charge over physical assets to be appropriate

Any pledging of physical assets complies with the terms and conditions contained within the Debenture Deed

Quantified Limits on Rates, Rates Increases and Borrowing

The rates increase forecast in this Three Year Plan represent the Council's intended quantified rates amounts and increases for the life of the Plan.

Similarly, the debt projections outlined in the financial statements to the Three Year Plan and explained in the sections above, represent Council's intended total borrowing limit based on the rebuild cost recovery assumptions outlined in the Plan.

Expected Changes in Population and Use of Land

Following the 2010 and 2011 earthquakes approximately 1,667 hectares of land in Christchurch City has been 'red zoned' by the Canterbury Earthquake Recovery Authority (CERA) meaning the land is no longer suitable for urban purposes i.e. private or public, residential or commercial use.

The council has therefore had to accelerate the amount of land made available for urban purposes so that people who have had their homes and businesses destroyed and have had to relocate have alternative sites to move to. Land is also needed for the natural growth of the Christchurch population which is predicted to reach 377,000 by 2022, an increase of 3% over 2013 with the number of households increasing 6% over the same period. In addition housing is required for many of the estimated 23,000 trades people coming to the Greater Christchurch Region for the re-build over the next few years.

The supply of industrial business land (Zoned B3 – B8), and the take up of this land has remained reasonably consistent throughout the earthquake period with approximately 7 ha being taken up in each year following the earthquake. Proposed Change 1 (PC1) highlighted 603 ha business greenfield areas available for future business development. To date 218 ha is zoned and available for take up.

Approximately 23,000 potential residential sections have been identified. 3,500 are in the process of gaining resource consent or granted with the balance yet to be consented. There are 16,000 sections that do not currently have infrastructure provided for them, however 9,500 of those will gain infrastructure provision by the end 2013.

To provide infrastructure for the growth outlined above, the Plan includes growth capital expenditure of $63m, $86m and $89m for 2013/14, 2014/15 and 2015/16 respectively. For further details on the specific projects please refer to the proposed capital programme. New infrastructure required for growth have had operating and maintenance costs included and across the life of the Three Year Plan this equates to an additional $1.18 million per annum in line with growth assumptions.