Absolutely Positively
Wellington City Council
Me Heke Ki Pōneke

Extraordinary Meeting of Te Kaunihera o Pōneke | Council

Rārangi Take | Agenda

1:30 pm Rāpare, 10 Whiringa ā-nuku 2024
1:30 pm Thursday, 10 October 2024
Ngake (16.09), Level 16, Tahiwi
113 The Terrace
Pōneke | Wellington

MEMBERSHIP

Mayor Whanau (Chair)
Deputy Mayor Foon (Deputy Chair)
Councillor Abdurahman
Councillor Apanowicz
Councillor Brown
Councillor Calvert
Councillor Chung
Councillor Free
Councillor Matthews
Councillor McNulty
Councillor O'Neill
Councillor Pannett
Councillor Randle
Councillor Rogers
Councillor Wi Neera
Councillor Young

Have your say!

You can make a short presentation to the Councillors, Committee members, Subcommittee members or Community Board members at this meeting. Please let us know by noon the working day before the meeting. You can do this either by phoning 04-499-4444, emailing public.participation@wcc.govt.nz, or writing to Democracy Services, Wellington City Council, PO Box 2199, Wellington, giving your name, phone number, and the issue you would like to talk about. All Council and committee meetings are livestreamed on our YouTube page. This includes any public participation at the meeting.

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1. Meeting Conduct

1.1 Karakia

The Chairperson will open the hui with a karakia.

Whakataka te hau ki te uru,
Whakataka te hau ki te tonga.
Kia mākinakina ki uta,
Kia mātaratara ki tai.
E hī ake ana te atākura.
He tio, he huka, he hauhū.
Tihei Mauri Ora!

Cease oh winds of the west
and of the south
Let the bracing breezes flow,
over the land and the sea.
Let the red-tipped dawn come
with a sharpened edge, a touch of frost,
a promise of a glorious day

At the appropriate time, the following karakia will be read to close the hui.

Unuhia, unuhia, unuhia ki te uru tapu nui
Kia wātea, kia māmā, te ngākau, te tinana, te wairua
I te ara takatū
Koia rā e Rongo, whakairia ake ki runga
Kia wātea, kia wātea
Āe rā, kua wātea!

Draw on, draw on
Draw on the supreme sacredness
To clear, to free the heart, the body
and the spirit of mankind
Oh Rongo, above (symbol of peace)
Let this all be done in unity

1. 2 Apologies

The Chairperson invites notice from members of:

1. Leave of absence for future hui of the Wellington City Council; or
2. Apologies, including apologies for lateness and early departure from the hui, where leave of absence has not previously been granted.

1. 3 Announcements by the Mayor

1. 4 Conflict of Interest Declarations

Members are reminded of the need to be vigilant to stand aside from decision making when a conflict arises between their role as a member and any private or other external interest they might have.

1. 5 Items not on the Agenda

The Chairperson will give notice of items not on the agenda as follows:

Matters Requiring Urgent Attention as Determined by Resolution of the Wellington City Council

The Chairperson shall state to the hui.

1. The reason why the item is not on the agenda; and
2. The reason why discussion of the item cannot be delayed until a subsequent hui.

The item may be allowed onto the agenda by resolution of the Wellington City Council.

Minor Matters relating to the General Business of the Wellington City Council

The Chairperson shall state to the hui that the item will be discussed, but no resolution, decision, or recommendation may be made in respect of the item except to refer it to a subsequent hui of the Wellington City Council for further discussion.

1. 6 Public Participation

A maximum of 60 minutes is set aside for public participation at the commencement of any hui of the Council or committee that is open to the public. Under Standing Order 31.2 a written, oral or electronic application to address the hui setting forth the subject, is required to be lodged with the Chief Executive by 12.00 noon of the working day prior to the hui concerned, and subsequently approved by the Chairperson.

Requests for public participation can be sent by email to public.participation@wcc.govt.nz, by post to Democracy Services, Wellington City Council, PO Box 2199, Wellington, or by phone at 04 499 4444 and asking to speak to Democracy Services.

2. General Business

NOTICE OF MOTION: WELLINGTON INTERNATIONAL AIRPORT SHARE SALE

Kōrero taunaki | Summary of considerations

Purpose

1. This report provides advice on the Notice of Motion related to the sale of the Council's shareholding in Wellington International Airport Limited (WIAL).

Strategic alignment

2. The most relevant community outcomes, strategic approaches, and priorities for this paper include social and economic wellbeing, value for money and effective delivery, making our city accessible and inclusive, and, given the implications for the 2024-34 Long-term Plan (LTP), the full range of identified priorities.
3. The full sale of the shares and establishment of the investment fund is in line with the Council's financial strategy. No sale is inconsistent with the Council's current financial strategy.

Relevant previous decisions

4. Previous decisions relevant to this paper include:
   - On 21 October 2021, the Finance and Performance Committee considered a paper recommending the sale of the airport shareholding and establishment of a new investment fund to diversify the Council's investment portfolio and reduce its exposure to natural hazards. This Committee voted not to proceed with the recommendations.
   - On 9 November 2023, the Kōrau Tōtōpū | Long-term Plan, Finance, and Performance Committee noted the outcome of a review of the Council's balance sheet and agreed to consult with the public through the LTP on a proposal to establish a perpetual investment fund, funded through sale of the airport shareholding and selected ground leases, to:
     - Ensure sufficiently liquid funds are available to mitigate losses or contribute to recovery from natural disaster;
     - Reduce the Council's geographic concentration of assets (meaning not all assets are subject to the same critical risks);
     - Address the Council's large and growing insurance risk (currently $2.6B, up 14-fold from 2021);
     - Improve intergenerational wellbeing through the building of investment wealth and reduced reliance on future borrowing;

    - Better achieve social or environmental outcomes as the Council sets parameters for what the perpetual investment fund will invest in; and
    - Introduce new revenue sources.

- On 11 April 2024, the Kōrau Tōtōpū | Long-term Plan, Finance, and Performance Committee adopted the audited LTP Consultation Document and draft Financial Strategy and agreed to proceed to public consultation on the plan, with a preferred option to establish a perpetual investment fund using the proceeds from a sale of the Council's full airport shareholding.
- On 30 May 2024, following public consultation which supported a share sale and establishment of an investment fund, the Kōrau Tōtōpū | Long-term Plan, Finance, and Performance Committee agreed to proceed with the Council's preferred option and include this in the LTP. The Committee also directed officers to seek independent advice and begin developing a sales strategy for the share sale and report back to Council with a recommended sales approach by December 2024.
- On 26 June 2024, the Kōrau Tōtōpū | Long-term Plan, Finance, and Performance Committee recommended to Council to adopt the audited LTP and noted that officers were bringing back advice on a sale strategy by December 2024 and that an agreement to sell the Council's shareholding would be subject to the advice in that sales strategy.
- On 27 June 2024, the Council adopted the 2024-34 LTP, including the proposal to sell the full airport shareholding to establish a new perpetual investment fund.

Significance

5. The decision is **rated high significance** in accordance with schedule 1 of the Council's Significance and Engagement Policy. The proposal meets the following criteria: Importance to Wellington City, Community Interest, Consistency with Existing Policy and Strategy, and Impact on Council's Capacity and Capability.

Financial considerations

☐ Nil	☒ Budgetary provision in Annual Plan / Long-term Plan	☐ Unbudgeted $X

Risk

☐ Low	☐ Medium	☒ High	☐ Extreme

Author	Katherine Meerman, Chief Advisor
Authoriser	Andrea Reeves, Chief Strategy and Finance Officer

Motion

That Te Kaunihera o Pōneke | Council:

1. **Agree** to commence a process to amend the 2024-34 Long-term Plan (LTP) with Council's objective being No Sale of any of its shareholding in Wellington International Airport Limited
2. **Agree**, while the Council is progressing an LTP amendment to remove the share sale from the LTP, to:
   a. Direct officers and relevant contractors to cease all work to progress the share sale including the currently scheduled report for December 2024;
   b. Suspend any committee or individual from taking any steps or spending money to progress the share sale pursuant to any delegations made to that committee or individual; and
   c. Direct that no further money is spent on establishing a Perpetual Investment Fund (PIF) through the share sale
3. **Agree** to suspend any delegations to any committee or sub-committee of Council relating to the development of the Council's draft and final LTP amendment
4. **Note** it is likely that an LTP amendment will be required as part of the Government's Local Water Done Well reforms.

Whakarāpopoto | Executive Summary

6. The sale of the Council's 34% shareholding in Wellington International Airport (WIAL) and the establishment of a new perpetual investment fund is a major component of the 2024-34 LTP and financial strategy the Council adopted in June 2024.
7. The Notice of Motion (in resolutions 1 to 4) proposes to initiate an LTP amendment process to reverse this core component of the LTP and stop all work on the share sale and fund establishment until this LTP amendment is completed (likely June 2025).
8. The plan to sell the airport shares and establish a fund was agreed as part of the LTP because the Council faces serious risks to its balance sheet, including:
   - A large and growing insurance risk – we do not have sufficient insurance to respond to future financial and natural hazard risks. Currently our underinsurance is estimated at $2.6B and expected to grow as the costs of insurance rise and the availability of insurance continues to be challenging.
   - An undiversified investment portfolio – 93% of the Council's portfolio is held in airport shares and ground leases. This means that all the portfolio is exposed to the same kinds of risks – both sudden and unforeseen catastrophes, and also slower moving climate and market risks.
9. These risks have been identified by external financial advisers and ratings agencies over the last few years, including two separate external balance sheet reviews by EY in 2021 and KPMG in 2023. Both reviews identified selling the airport shareholding and establishing a new investment or insurance fund as an effective way to resolve these financial challenges.
10. The LTP consultation showed that the majority of the community support this approach – with 52% of submitters supporting a full or partial sale, and 63% of representative survey respondents supporting a full or partial sale.

11. The Council is not alone in facing these financial resilience pressures; many local authorities are seeking to address similar risks through their latest LTPs and are likewise seeking to establish long-term investment funds. There are notable examples of similar funds that have been established.

12. Officers recommend that the Council proceeds as planned in its LTP, and does not support the Notice of Motion, for the following reasons:

    - A full sale of the airport shareholding and establishment of a new investment fund is the most effective way to address the Council's financial risks, as evidenced by the recommendations of external reviews and ratings agency feedback;
    - A full sale and fund establishment meets the requirements for prudent financial management under the Local Government Act 2002 (LGA);
    - A full sale and fund establishment avoids future calls on the Council to further invest significant capital funding in the airport to deliver on its $1B long-term growth agenda; and
    - The LTP's current plan for a sale of WIAL shares and the establishment of a perpetual investment fund is supported by the community.

13. The 'no sale' option proposed in the Notice of Motion does not address the Council's underlying financial risks – it does not address the lack of diversification in the Council's investments and it will not address the Council's increasing underinsurance problem. Unless accompanied by significant reductions in debt (and increasing requirements for debt headroom), which would need to be achieved through cuts to the capital programme, it will be unlikely to meet the LGA's requirement for prudent financial management.

14. Officers recommend the Council does not support the proposal in the Notice of Motion to suspend the delegations of the Kōrau Tōtōpū | Long-term Plan, Finance, and Performance Committee to develop and hear the LTP amendment and instead refer the amendment to the Council. This resolution is inconsistent with the Council's Tākai Here partnership agreement as it would mean that the Council's mana whenua partners cannot fully participate and vote in the amendment process and is also inconsistent with the Council's standard practice.

15. If the Council supports the Notice of Motion and agrees to initiate an LTP amendment process, this paper provides some initial advice about the approach to assessing the capital programme and the scope for cost reductions. The paper identifies two scenarios for increases in headroom – a doubling of current headroom to $500m and a tripling to $750m – to respond to the large increase in insurance risk since the 2021-31 LTP when the current $272m was last set. These scenarios would require a $400m or $600m cut to the capital programme respectively from an "available" capital programme of approximately $1.95B. Any LTP amendment would need to be integrated with the Annual Plan process and consider the implications of water reform and changes to transport funding.

16. If the Council supports the Notice of Motion, the following next steps would apply:
    - all work on the airport share sale and PIF establishment would cease;
    - officers would bring back further advice to the Council by November on the timeline and process for the amendment;
    - the Council would need to develop its options for consultation (including detail of capital programme changes). These options would need to include a full sale, partial sale and no sale options (as per the previous LTP consultation);
    - consultation material would be prepared and the preferred option would be audited prior to consultation;
    - a full programme of community engagement would be required, followed by oral hearings;
    - post-deliberation, the amended LTP would be audited prior to final adoption by June 2025.
17. If the Council does not support the Notice of Motion, officers will continue work on the share sale and PIF establishment project and, as previously directed by the Council, bring back advice on a sales strategy and design options for the PIF by December 2024. This advice would include (amongst other things):
    - Market feedback from potential buyers that indicates the number of possible bidders and strength of interest;
    - Estimated valuation range (i.e., sales price range) determined by market interest, other comparable sales transactions, listed airport peer benchmarking, and assessment of WIAL business plan and forecasts;
    - Options on the sales strategy for the Council to consider based on market feedback, and a detailed execution plan for the options;
    - Alternatives for mana whenua participation in any sale process, including alongside other investors;
    - Advice on the merits of a full sale compared to a partial sale, including based on market feedback;
    - Early options for the objectives and design of the PIF, including mechanisms to protect the fund, and case studies from other similar investment funds that demonstrate the value of such funds for a local authority’s financial strategy; and
    - Advice on whether to proceed with the sale of airport shares to establish the PIF based on the development of the above.

Takenga mai | Background

18. In 2023, the Council commissioned KPMG to undertake an independent review of its balance sheet which identified significant issues with the Council's long-term financial resilience and risk – in particular, a significant insurance risk associated with underinsurance ($2.6B) and a lack of diversification in its investment portfolio.

19. The review strongly recommended that the Council take action to address these risks, noting the Council's exposure, through the extent of its underinsurance, would be an unacceptable risk for most governing bodies. To address these risks, KPMG recommended a sale of the full WIAL shareholding and establishment of a perpetual investment fund.

20. EY and PwC undertook similar work for the Council in 2021 which recommended diversifing the Council's investment portfolio to reduce geographic concentration to Wellington and exposure to natural hazard risk. This work also identified the opportunities in selling the airport shareholding and investing in other diversified funds.

21. In the 2024-34 LTP, the Council consulted with the community on the sale of its full Wellington airport shareholding to establish a new investment fund to provide funds for future disaster recovery. There was a majority of community support for either a full or partial share sale:

    - 28% of submissions supported a full share sale and 24% submissions supported a partial sale; a total of 52% compared to 28% for no sale
    - 27% of respondents to the representative survey supported a full share sale and 36% supported a partial sale; a total of 63% compared to 19% for no sale.

22. Following consultation, the Council adopted the LTP, including agreeing to proceed with the preferred option (a full share sale and establishment of a fund) and directed officers to seek independent advice on a sales approach and valuation and bring back a recommended sales strategy to the Council by December 2024.

23. Following the adoption of the LTP, a Notice of Motion was brought to initiate an LTP amendment to reverse the decision to sell the shareholding and to make the necessary consequential changes to the Council's financial strategy and plan. The Notice of Motion also proposes that all matters relating to the LTP amendment be considered by Council rather than the delegated committee. This has implications for mana whenua as set out later in the report.

24. This paper provides advice on the implications of the proposed change to the LTP, and seeks the Council's decision on whether to initiate the LTP amendment or to proceed based on the current LTP and Council resolutions, with the next step being advice on a sales strategy in December.

Kōrerorero | Discussion

Why was the airport sale and perpetual investment fund included in the LTP?

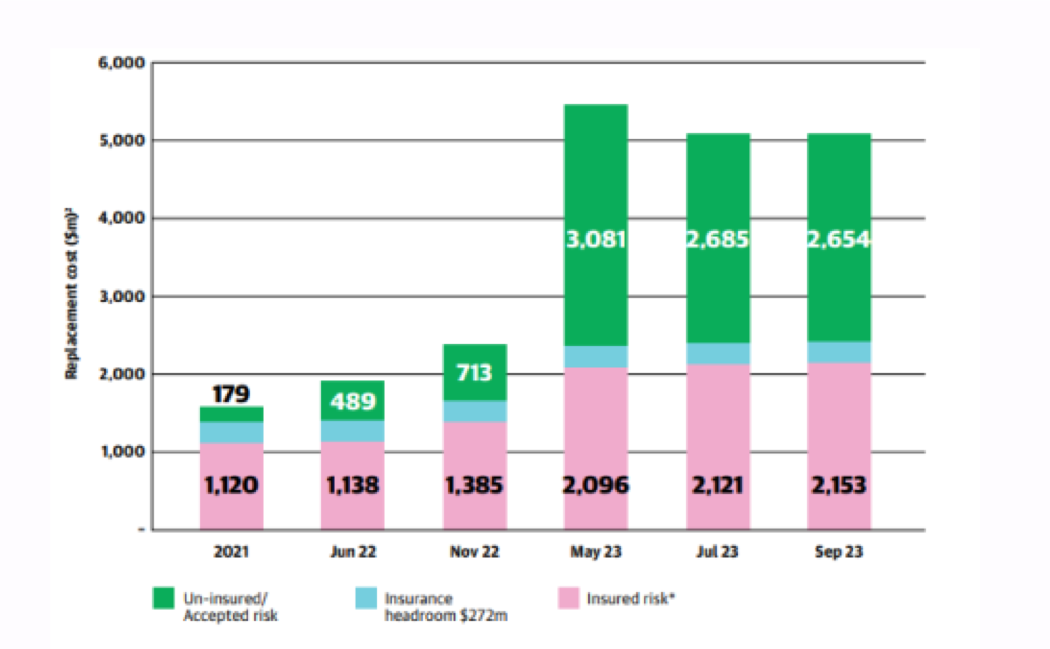
<u>The Council is facing serious financial challenges…</u>

25. The Council is facing serious financial issues which the 2024-34 LTP addresses through its intention to sell the airport shares and use the proceeds to establish a new investment fund:

- We do not have sufficient insurance to respond to future financial and natural hazard risks – the value of this underinsurance is growing and is currently estimated to be at $2.6B, far more than the $272m debt headroom the Council had previously held in the 2021/31 LTP to cover these risks (see Figure 1). The Council's uninsured, or accepted risk, has grown 14-fold since the 2021-31 LTP. The costs of insurance are expected to continue to rise and the availability of insurance to continue to be challenging – this means the Council needs to consider new solutions to address this problem.
- There is a lack of diversification in the Council's investment portfolio with 93% of the Council's portfolio held in airport shares and ground leases. This means that all of the Council's portfolio is exposed to the same kinds of risks (i.e., all our eggs are in one basket) – not just the risk of a sudden and unforeseen catastrophe, but also longer-term climate and market risks. This means the Council could face significant financial losses if one or more of these was to eventuate and/or that it is more difficult to release capital, if required, when such an event occurred.

26. The result of these issues, combined with significant Council investment through a large capital programme, means the Council's current balance sheet does not support the outcomes the Council is seeking – without change, it is not possible to continue to invest in ageing infrastructure as well as manage pressure on borrowing and rates and mitigate future risks.

Figure 1: Funding sources for 1-1,000 year loss



27. The decisions the Council takes in response to the government's Local Water Done Well reform may exacerbate these balance sheet risks, making the decision about whether or not to sell the airport shares and establish the fund more critical. This is discussed further in paragraphs 70 to 72 below.

28. As well as KPMG and EY, these issues have been identified by Standard & Poor's S&P) in the Council's November 2023 and August 2024 reports.

- In November 2023, S&P maintained the Council's negative watch position and noted the Council would need to make significant changes to its financial strategy in its upcoming LTP to return to a stable outlook – as part of these changes, they identified the sale of relevant assets. The commentary identified the extent of the Council's insurance risk, a lack of insurance market capacity, and the Council's unique risk profile as reasons why traditional insurance options are no longer sufficient and alternative options will be required.
- In August 2024 S&P downgraded Wellington City because its "financial outcomes are weaker than previously expected" and because "the Council's additions to its capex programme in its 2024-34 LTP will weigh on its fiscal performance over the next three years". S&P noted the Council's financial management is strong within a global context but that the "rapid accumulation of debt in the last five years is an outlier among similarly rated peers globally" which, combined with a weak fiscal outlook, has "drive(n) our lower assessment of Wellington City's financial management". Again, the assessment notes the Council's increasing insurance risk, the fact that "traditional insurance solutions are becoming increasingly impractical" and notes that the planned airport share sale and investment fund establishment would help "diversify the Council's investment sources and ensure funding is available to support a recovery from natural disasters, by narrowing the insurance gap."

29. It is important to note that this latest S&P assessment and downgrade has occurred based on the financial strategy and forecasts in the LTP (i.e., assuming a full sale of the shareholding takes place and an investment fund is established). The review notes the uncertainty about whether the sale will now go ahead, the upcoming impact of water reform, and wider pressure on the local government sector as factors that are likely to influence their future reviews.

<u>Wellington is not alone in risks faced or response proposed…</u>

30. Most local authorities in New Zealand are facing considerable financial pressure and balance sheet risk – which is a result of a combination of factors, including a lack of funding tools, deferred maintenance liabilities, cost increases and population growth. These generally-felt pressures are in addition to Wellington's regional specific factors including exposure to natural disasters (and resulting insurance impacts) and diffcult current local economic conditions.

31. The effect of all this has been difficult decisions made through the latest LTP processes – including significant rates rises, material increases in borrowing, putting pressure on balance sheets and LGFA and credit rating covenants, and/or deferral of captial expenditure, cost and service cutting, and consideration of asset sales.

32. Auckland, Bay of Plenty, Dunedin and Southland all consulted on asset sales in the most recent LTP, Christchurch and Hawke's Bay have undertaken strategic investment reviews and Napier consulted on the establishment of a CCTO for the management of its investment assets.

33. In many cases, Councils have responded to these challenges by proposing to establish new investment funds with the proceeds of asset sales (e.g., Auckland Council, Hawke's Bay Regional Council), and/or in the past have established investment funds with such proceeds (e.g., Bay of Plenty Regional Council, New Plymouth District Council, Southland Regional Council).

<u>Central government is considering its future role in helping to manage insurance and natural hazard risk…</u>

34. It is not just the Council (or local authorities) that are exposed to natural hazard and resilience risks. Severe weather events are becoming more common across New Zealand and understanding of underlying natural disaster risk (and resulting financial consequences) around the country is continually improving and sharpening.

35. As a result the Crown's exposure to natural hazard risk is also growing, putting pressure on the government's balance sheet – with the implication that future Crown responses to natural disasters will not necessarily be the same as responses in the past. Recent Treasury advice released to Radio New Zealand under the Official Information Act makes this clear when it says

    So far, the Crown had been able to weather "overwhelming events" like Cyclone Gabrielle, the Christchurch earthquakes and the Kaikōura earthquake, using its borrowing discretion to support councils and asset owners.

    Those events had been large enough to affect net debt and GDP, but not so much that they had challenged the government's ongoing fiscal sustainability.

    However, modelling from 2021 suggested that larger and more frequent extreme weather events would create additional Crown costs equivalent to 0.54 percent of GDP by 2061."

36. The report signals that Treasury work is ongoing on these issues but indicates that they see these past events as large but discrete (and able to be dealt with on an as-needed basis with one-off borrowing) compared to upcoming costs of climate-related risks which may need to be managed differently.

<u>A new investment fund (achieved via a full share sale) was included in the LTP because it addresses the risks the Council faces…</u>

37. The option the Council consulted on as its preferred option in the LTP is to sell the Council's full 34% shareholding in Wellington International Airport Limited (WIAL) and invest the funds in a new, publicly owned perpetual investment fund with a clear purpose to invest to manage the Council's future financial risks.

38. With an assumed initial investment of $492m, plus the addition of $50m of ground lease sales in the early years of operation, and an assumed growth rate of 7% a year, the fund would be expected to grow to $2.8B within 50 years. The fund could grow to $6.4B within 50 years, if an 8% return was achieved (refer Figure 2). A 7% return is based on returns from balanced and growth-focused KiwiSaver funds over the last 10 years and an 8% return is based on growth-focused KiwiSaver funds – based on these benchmarks, the Council could expect the fund to grow to a sufficient level to manage its insurance exposure.

39. The Council could continue to receive a dividend stream from the fund, as it does currently from the airport. This would mean the fund could be established without any impact on rates because the new dividend stream could offset rates in the same way the airport dividend does now. The scenarios modelled in Figure 2 assume a dividend stream to the Council from the fund which matches the forecast WIAL dividend stream over the 10 years of the LTP[1] – this means the Council will be no worse off from a revenue perspective than it would be had it retained the shares. If the Council chose a different dividend level (and therefore a different reinvestment rate back into the fund), this would also have a strong influence on the fund's value over time – higher reinvestment levels lead to accelerated growth (refer Figure 3).

Figure 2: Investment fund value under different return assumptions

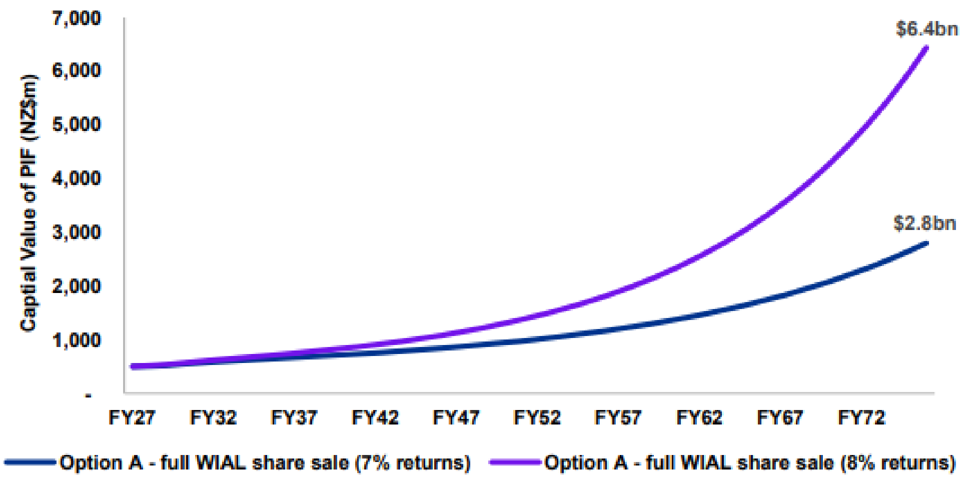
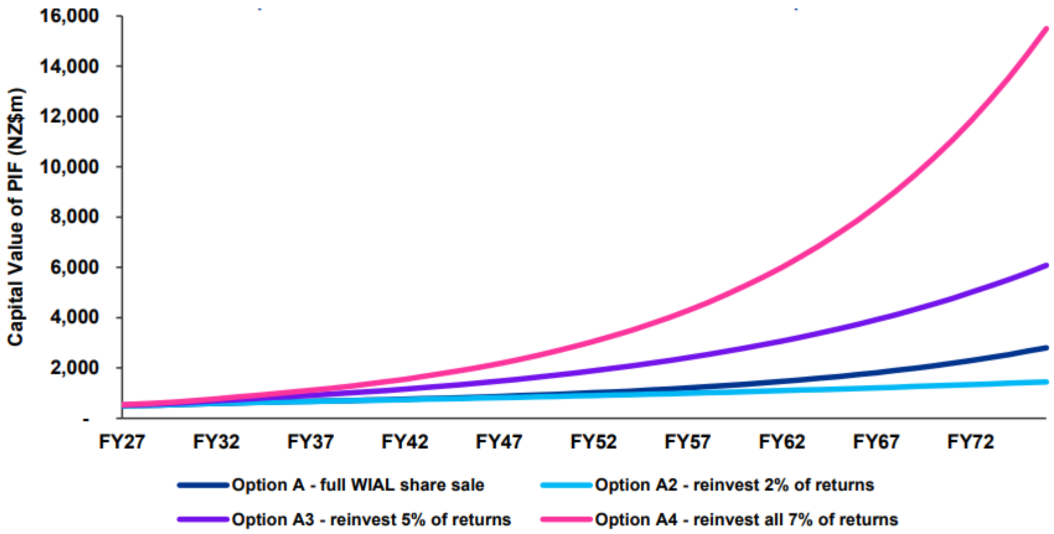


Figure 3: Investment fund value under different dividend and reinvestment assumptions



[1] The dividend to the Council is then assumed to be capped after year 10 – including in Option A in Figure 3 below.

40. Importantly, the forecast of financial outcomes of the investment fund (and its impact on rates), depend on details of its design. These include its form (e.g., CCO, Trust), investment mandate (including ESG and resposible invesment policy), reinvestment rate and tax status as well as the proceeds from the WIAL sale. The Council would receive further advice on these aspects as part of the December report back, if the Council agrees that this will go ahead.

41. The fund would be set up to be well protected, meaning the funds could not be withdrawn by the Council unless it was for the specific purposes for which the fund was established (e.g., for disaster recovery). All proceeds from the sale would go into the fund and would not be used to pay down Council debt or fund services or pay for other Council projects.

42. A range of measures could be put in place to protect the fund, which could include the following – officers would provide the Council with further advice on these as part of the December report back:

- **Establishing a new entity/unit to manage the fund** – the new entity could be a new CCO, Council-owned holding company or Trust, and the Council would be involved in setting its constitution and objectives – the new entity would then need to operate in accordance with these parameters;
- **Reflecting the fund in Council's policies and reporting requirements** – the fund would likely be identified as a strategic asset in Council's significance and engagement policy requiring public consultation in order to make any changes;
- **Exploring legislative protection** – the fund might be established under an Act of Parliament which could set out key objectives and investment principles and could set safeguards for withdrawals;
- **Other commercial or financial mechanisms** – there may be other commercial incentives that could be designed into the fund (e.g., material break fees) that have implications for the ability to liquidate the fund in the future; and
- **Other legislative and regulatory reporting requirements** that are relevant for managed funds.

What objectives is the Council seeking to address?

43. In considering whether or not to support the Notice of Motion, the Council needs to consider the objectives it is seeking to address and how effectively various options deliver on those objectives. These objectives include:

- Address underinsurance risk resulting from increasing cost and lack of traditional insurance availability
- Improve the balance sheet resilience by addressing the lack of diversification in the Council's investments
- "manage its … assets, liabilities, investments, and general financial dealings prudently and in a manner that promotes the current and future interests of the community", as required by section 101(1) of the Local Government Act.

44. In seeking to achieve these objectives, the Council is required under the LGA to operate in accordance with a number of principles, the following being the most relevant to this issue:

    - A local authority should give effect to its identified priorities and desired outcomes in an efficient and effective manner
    - A local authority should have regard to the views of all of its communities
    - A local authority should take account of the interest of future as well as current communities
    - A local authority should periodically assess the expected returns from investing in a commercial activity and satisfy itself that the expected returns are likely to outweigh the risks inherent in the investment or activity
    - A local authority should ensure prudent stewardship and the efficient and effective use of its resources in the interests of its district or region, including by planning effectively for the future management of its assets.

45. The Council has been previously provided with advice on how the options perform against these principles (refer to LTP Committee paper from 30 May 2024).

<u>What is prudent financial management?</u>

46. In adopting the LTP, the Council set the foundation for prudent long-term financial management and sustainability – the Independent Auditor's Opinion recognises that the 2024-34 programme has struck the necessary balance providing a "reasonable basis for long-term integrated decision making and coordination of the Council's resources".

47. In amending the LTP, any new option would need to also meet the legal requirement for prudent financial management. At this point it is difficult to be clear on what would or wouldn't be acceptable, particularly given the combined effect of the aiport decision, water reform and transport funding changes. However, the conclusions of the KPMG balance sheet review and feedback from S&P both suggest that simply removing the airport sale and PIF establishment from the LTP with no consquential mitigating action would not be financially prudent – in this situation, the Council would have seen its insurance risk increase 14-fold over the previous LTP period and have not taken any action to manage that increased exposure. On this basis, officers have modelled two scenarios that double and triple the existing headroom allocation to demonstrate a meaningful step towards mitigating the increasing insurance risk.

48. Officers noted in the recent 26 September Annual Plan paper that it will be challenging over the next few years for Annual Plans to maintain the requirement for prudency while balancing significant infrastructure investment, operational costs, and rates affordability. Achieving this balance becomes significantly more difficult over the short and longer-term if the Council's balance sheet risks remained largely unaddressed as a result of a decision not to sell the airport shareholding and establish an appropriately-sized investment fund.

Assessing the options against objectives

49. Table 1 provides a summary assessment of the options against these objectives, with further discussion below. Officers continue to recommend that the Council pursues a full sale and PIF establishment on the basis of its performance against these fundamental objectives.

Table 1: Considering options against the objectives

	Option1: Full sale/PIF establishment	Option 2: No sale/LTP amendment	Option 3: Partial sale/PIF establishment
Address underinsurance	✓✓	✗	✓
Improve diversification	✓✓	✗	✓
Prudent financial management	✓✓	?✓	✓

50. **Option 1 (full sale/PIF establishment)** was included as the preferred option in the LTP consultation on the basis that it most clearly and strongly delivers on the Council's objectives to address its insurance and diversification risks. It also clearly meets the LGA requirement for prudent financial management for current and future generations.

51. This option also has other signficant advantages over the other options, particarly a no sale/LTP amendment option, including:

- It responds directly to the concerns raised by credit rating agencies and external financial advice over the last few years;
- It best provides the Council with liquid assets that are available for rebuilding or providing financial relief after a natural disaster;
- It enables the Council to more explicitly invest in line with its values and objectives; and
- Given the airport's proposed growth plans, it avoids the Council being called on to provide significant capital contribution to fund growth or risk diluting its shareholding.

52. **Option 2 (no sale/LTP amendment)**, as sought by the Notice of Motion, does not adequately address the objectives. On this basis, officers recommend the Council does not support the Notice of Motion.

- No Sale does not address the financial risks the Council currently faces – it does not improve lack of diversification in the Council's investment portfolio and would leave the Council (and future ratepayers) with an increasing underinsurance problem that cannot be adequately addressed through capital cost reductions and increasing debt headroom;
- No Sale with no reductions in the capital programme (or insufficient reductions) would not meet the LGA's requirements for prudent financial management; and
- No Sale with large reductions in the debt-to-revenue ratio (or increased requirements for debt headroom), while likely to meet the immediate requirement for a prudent budget, will come at a cost of investments in the city.

53. Retaining the shareholding would also mean that the Council could be called on to provide funding for the airport's growth plans, during a period where its own financial position continues to be constrained. If the Council does not provide funding when called on, its shareholding will likely be diluted and its influence (to the extent it currently has any) will diminish.

54. The airport's 2040 masterplan anticipates a $1B capital investment plan for new and expanded terminals, land acquistion, relocation of and new freight facilities, additional aircraft hangars, resilience projects and potential runway extension. The airport could fund this programme either via debt or shareholder contributions. If no debt financing was available, the Council's contribution could be up to $340m; if half the programme was debt funded, the Council's contribution could be up to $170m.[2]

55. Further implications on the 'no sale' option are included at paragraphs 61 to 69.

56. **Option 3 (partial sale/PIF establishment)** better achieves the objectives than option 2 (no sale), but is less effective than option 1 (full sale) at addressing the Council's fundamental financial risks. It would likely meet the requirement for prudent financial management, assuming other components of the financial strategy are retained (e.g., 225% ratio and $272m debt headroom) but will result in a fund that cannot grow as large or as quickly as needed to be truly effective in achieving financial resilience and helping future ratepayers manage risk (refer Figure 4).

57. Given its slower growth, the Council should consider whether it wanted to take other steps to bolster the fund or adjust its financial strategy as compensatory measures (depending on what the measures are, they may trigger an LTP amendment but that would need to be assessed at the time).

58. A partial sale also leaves the Council with the same risks around funding the airport's growth or having its shareholding diluted – in this situation there would be up to two other shareholders who could provide necessary capital and the new shareholder (or shareholders) would have bought in knowing the likely funding requirement (and presumably therefore being prepared to provide the necessary capital).

59. Critically, there may well be significant challenges in successfully executing a partial sale transaction. The demand for a partial sale is likely to be much less than for the Council's full shareholding which means there would be a meaningful discount applied to any transaction (i.e., it will sell for much less than half the value of the full sale, assuming half the shareholding is sold). The resultant shareholding Council would retain would also be significantly less marketable than the full shareholding is currently, and would likely be subject to pre-emptive rights which would reduce the ability to achieve fair value for the sale of the remaining shareholding in the future, should the Council choose to do so. Given the size of the financial risks the Council is facing, the Council should carefully consider whether the benefit it sees in retaining a smaller shareholding outweighs the loss of higher proceeds from a transaction under Option 1.

60. For these reasons, officers and the Council's sales advisers continue to recommend against a partial sale and can provide further advice on this in December, if that report back progresses.

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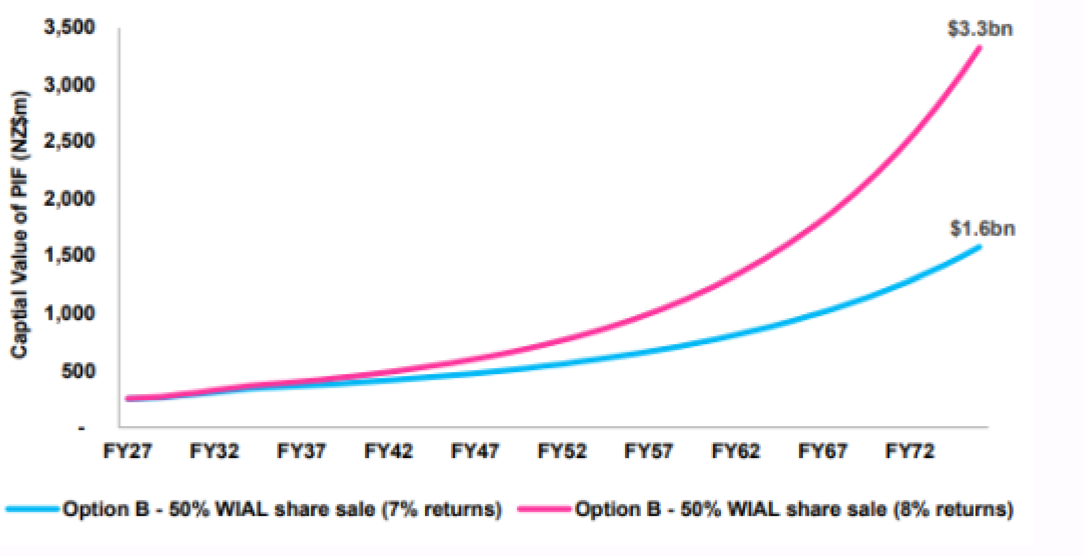
[2] A similar scenario occurred when Auckland Airport raised $1.2B from shareholders in 2020 (related to COVID). Auckland Council did not participate and, as a result, its shareholding was diluted.

Figure 4: Partial sale fund value under different return scenarios



Implications of 'no sale'

61. If the Council resolved to initiate an LTP amendment process with the objective that 'No Sale' of the airport was the Council's preferred option, officers recommend that the Council determines a programme of debt reduction (or new debt-to-revenue ratio), which would be achieved through cuts to the current capital programme. The purpose of these cuts would be to create some additional debt headroom to respond to insurance risks, and to ensure the Council continues to have a financially prudent budget.

62. As discussed above, these cuts will only be a risk mitigant; it is not possible to sufficiently reduce debt to address the insurance risk through creating headroom. It is also important to note that these cuts will do nothing to address the diversification risk and the lack of of resilience in the Council's balance sheet from the natural hazard exposure – both of these risks would remain.

63. Once the Council had agreed in principle on a set of changes, it would need to consult via a Special Consultative Procedure as part of an LTP amendment. This process would follow the same steps as the process to develop the LTP and include production of consultation material with a set of options identified, audit of the consultation document and preferred option prior to consultation, a full community engagement process, oral hearings and audit of the final proposal.

64. The options for consultation would include:

    - No Sale plus a package of capital programme changes (identified as the Council's preferred option)
    - Full sale/investment fund establishment
    - Partial sale/investment fund establishment (plus identified debt changes, if required).

65. The details of capital programme changes would need to be worked through by the Council, following further officer advice, if the Council voted to support the Notice of Motion. This advice would also need to take into account the impact of transport funding cuts, water reform options, and other priorities previously identified for the upcoming 2025/26 Annual Plan.

66. However, at a high level, officers' advise that the following principles should guide the consideration of capital programme cuts:

    a. The capital programme should prioritise the maintenance and renewals of existing assets over upgrading or building new. Under the current LTP, renewals expenditure is already set at 75% of unconstrained renewal funding (apart from water) for the first ten years of the plan, and this is subject to a matter of emphasis by the auditor; any cuts to the captial programme should avoid further reducing renewals expenditure;

    b. Projects that are substantively in train (i.e., contractually committed and spend well advanced) should continue;

    c. The capital programme should ensure the Council meets its legislative and regulatory requirements;

    d. Changes/reductions are required over the full term of the LTP, however, savings that can be found early should be prioritised as they have more significant impacts on operating costs and capital savings required over the later years of the programme; and

    e. Projects part funded from development contributions could move to later in the LTP period, but if removed from the plan entirely, development contributions would need to be returned and/or the DC policy amended.

67. Currently the LTP's capital programme over years two to ten of the LTP equates to $4.2B; if renewals and major projects that are substantively in-train (e.g., Te Matapihi, sludge, Town Hall) are exluded from consideration for an LTP amendment, the remaining capital programme over years two to ten is approximately $1.95B – this could be considered to be the indicative available programme within which to fund cuts.

68. Table 2 shows the capital programme reductions that would be needed under different scenarios. As discussed above, if the Council wanted to remove the sale and mitigate its financial risks via debt headroom, officers' advise that the Council seeks a meaningful increase in the headroom to reflect the large, and growing, insurance exposure – a doubling to $500m and tripling to $750 are shown below. Given the scale, these would likely need to be phased in over the first half of the LTP period (as shown in Figures 5 and 6).

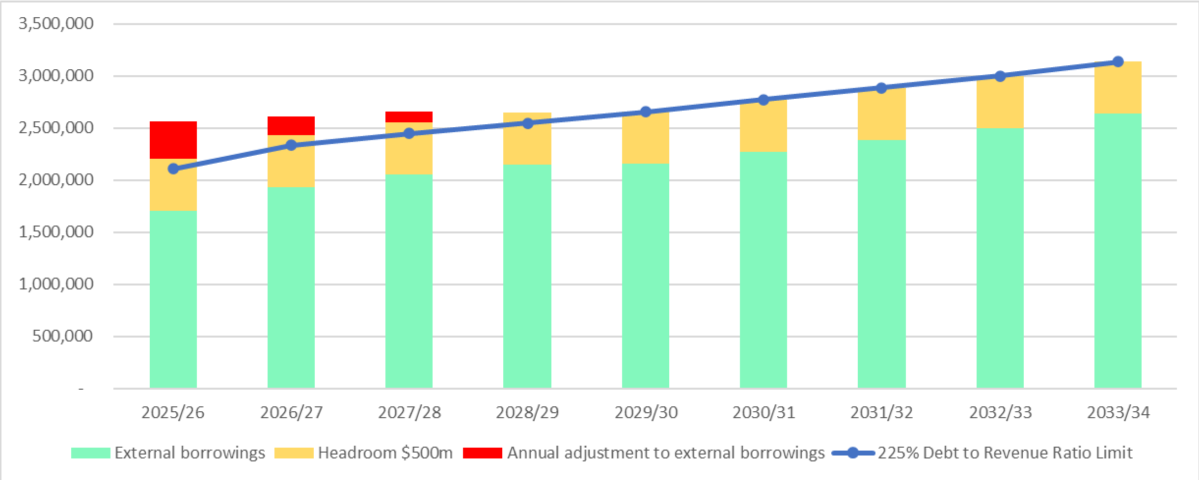
Table 2: Capital programme and reductions[3]

Current LTP capital programme (years 2-10)	$4.2B
Adjusted/indicative available capital programme	$1.95B
Savings required: $500m debt headroom, 225% debt to revenue ratio	$400m
Savings required: $750m debt headroom, 225% debt to revenue ratio	$600m

69. Examples of projects included in the available programme are:

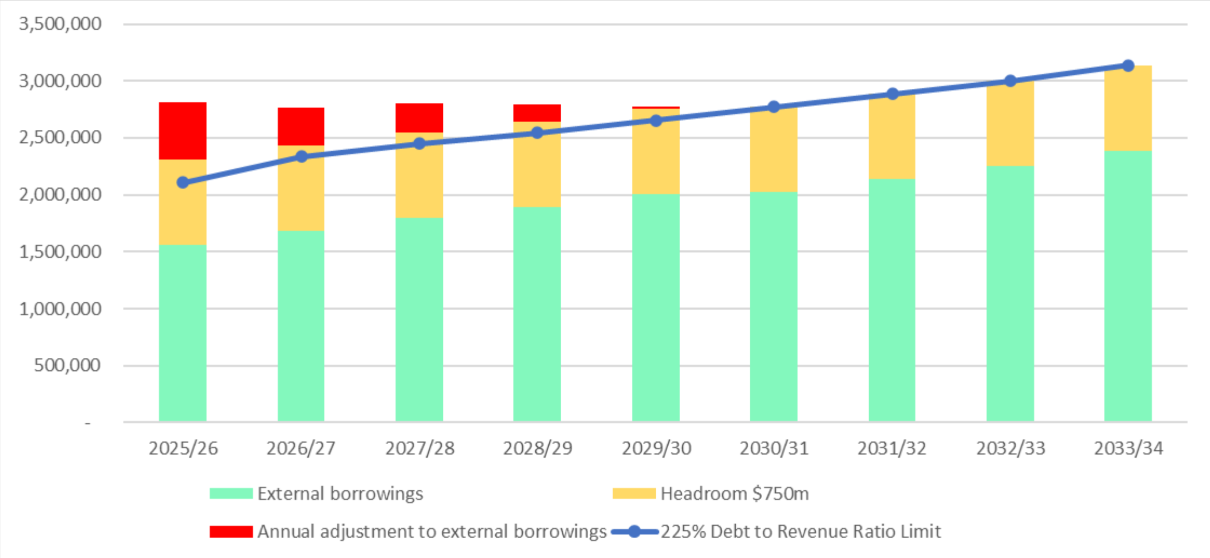
- Major initiatives: Cycleways programme, social housing upgrades, Golden Mile, City Streets programme, future provision for community new and upgraded community facilities
- Community or facility upgrades: Begonia House, Bond Store, Grenada Sports Hub, Khandallah pool, Newtown community hub, Otari landscape plan, venues upgrades
- Infrastructure upgrades: retaining wall upgrades, preseal preparations, footpath upgrades, LED streetlight transition, speed management and parking upgrades, Kiwi Point Quarry upgrade
- Services improvements: rubbish collection bin changes, library collections upgrades, zoo masterplan.

Figure 5: $500m debt headroom, $400m capital programme cut in years 2-5



[3] Note these scenarios for increased debt headroom assume all other assumptions in the capital programme remain the same e.g., revenue profile.

Figure 6: $750m debt headroom, $600m capital programme cut in years 2-6



Water reform and NLTP funding changes

70. In considering whether or not to suppport the Notice of Motion, the Council should also consider the potential impact of water reform changes on the Council's balance sheet. While there is significant uncertainty about the implications of the Local Water Done Well reforms, a transfer of the Council's water assets to a new CCO is a possible outcome.

71. In the transfer, the value of the assets (and related revenue stream) transferred will likely be higher than the value of the corresponding debt that could be transferred. The consequence of this would be that the Council's effective current debt-to-revenue ratio increases and its ability to borrow (i.e., its debt headroom) decreases. Even if there is minimal or no impact on the Council's debt-to-revenue ratio perspective (i.e., if the ratio remains the same), the reduction in revenue in nominal dollar terms will mean the nominal value of what the Council can borrow will reduce.

72. From both these perspectives, the Council's future ability to borrow to address underinsurance in the event of a disaster will be relatively more constrained than if water reform did not go ahead. While there is the net effect of the reduction in the value of the Council's insurance liability to consider (i.e., as a result of the transfer of assets), officers' view at this early stage is that water reform will be more likely to exacerbate the Council's balance sheet pressures, rather than improve them.

73. Recent changes to the National Land Transport Plan (NLTP) funding from government also need to be considered and, even in the absense of an LTP amendment, will require changes to the capital programme.

74. The NLTP has indicated the Council's expected revenue will be reduced by $70m (or one third). With lower than expected revenue, borrowings need to reduce to remain within the current debt-to-revenue profile in the LTP. Currently we anticipate the capital work programme would need to be reduced by $132.3m in years one to three, in order to remain within the current debt profile. Officers are developing separate advice on options for changes to remain within the current envelope and this will be provided to the Council on 29 October 2024.

LTP amendment process and delegations

75. The Council had advice on 26 September 2024 on the 2025/26 Annual Plan process, noting that the Annual Plan process is subject to decisions on this Notice of Motion, water reforms and NZTA transport funding changes.

76. If the Council supports this Notice of Motion, the Annual Plan process would become a full LTP amendment process and officers would bring back further advice on the implications of this for the work programme, timeframes and costs (which is expected to be approximately $150,000 for audit services).

77. Water reform does not, of itself, necessarily require an LTP amendment or the associated requirements for a Special Consultative Procedure and audit. Under the Local Water Done Well legislation, the Council is required to consult with the community on the model for the new entity, but the form of this is not specified and can be determined by each individual Council. Following consultation, if an LTP amendment is required, Councils can simply update their LTP, which would be required to be audited. However, if the Council prefers a regional approach to reform, timing of the consultation may need to consider timing of consultation being undertaken by other Councils. If the Notice of Motion passes and an LTP amendment process is commenced, then the most likely option is that the consultation for water reform would form part of the LTP amendment, including an audit and a Special Consultative Procedure.

78. The Annual Plan/LTP amendment needs to be delivered as a single intergrated package and overseen by a single decision making body. If the Council supports all resolutions in this Notice of Motion, the Annual Plan, the LTP amendment for the airport, plus any other related processes (e.g., consultation on water reform) would be brought together and run by the Council, instead of the LTP Committee. If the Council chose to support resolution 1 and 2, but did not support resolution 3, the Annual Plan/LTP amendment process, plus other associated consultations (e.g., consultation on water reform) would remain with the LTP Committee.

79. Given that mana whenua representatives are not lawfully entitled to make decisions at Council, this would mean that mana whenua are not involved in decision making in any aspects of the LTP amendment (including water reform). This would be inconsistent with both Council's delegated committee structure (where these matters are delegated to be developed by the LTP Committee) and our Tākai Here agreement.

80. If the Council chose to support resolution 1 and 2, but did not support resolution 3, the Annual Plan/LTP amendment process, plus other associated consultations (e.g., consultation on water reform) would remain with the LTP Committee.

81. Officers recommend the Council does not support resolution 3 in the Notice of Motion to suspend the delegations of the LTP Committee and refer the amendment to the Council. This resolution is inconsistent with the Council's Tākai Here partnership agreement and would mean that the Council's mana whenua partners cannot fully participate and vote in the amendment process. The resolution is also inconsistent with the Council's standard practice and Committee terms of reference, both of which would see the LTP Committee overseeing any LTP amendment as has been in the case in the past (most recently the LTP amendment for social housing in 2022).

Options and next steps

82. The Council has two options available:
    - Support the Notice of Motion (not recommended)
    - Do not support the Notice of Motion (recommended)
83. If the Council supports the Notice of Motion, the following next steps would apply:
    - all work on the airport share sale and PIF establishment would cease;
    - officers would begin planning an LTP amendment process and bring back further advice to the Council by November on the timeline and process for developing the amendment;
    - the Council would need to develop its options for consultation (including detail of capital programme changes) by December 2024. These options would need to include a full sale, partial sale and no sale options (as per the previous LTP consultation);
    - consultation material would be prepared and the preferred option would need to be audited prior to consultation;
    - a full programme of community engagement would be required, followed by oral hearings;
    - post-deliberation, the amended LTP would be audited prior to final adoption by June 2025.
84. If the Council does not support the Notice of Motion, officers will continue work on the share sale and PIF establishment project and, as previously directed by the Council, bring back advice on a sales strategy by December 2024. This advice would include (amongst other things):
    - Market feedback from potential buyers that indicates the number of possible bidders and strength of interest;
    - Estimated valuation range (i.e., sales price range) determined by market interest, other comparable sales transactions, listed airport peer benchmarking, and assessment of WIAL business plan and forecasts;
    - Options on the sales strategy for the Council to consider based on market feedback, and a detailed execution plan for the options;
    - Alternatives for mana whenua participation in any sale process, including alongside other investors;
    - Advice on the merits of a full sale compared to a partial sale, including based on market feedback;
    - Early options for the objectives and design of the PIF, including case studies from other similar investment funds that demonstrate the value of such funds for a local authority’s financial strategy; and
    - Advice on whether to proceed with the sale of airport shares to establish the PIF based on the development of the above.

Whai whakaaro ki ngā whakataunga | Considerations for decision-making

Alignment with Council's strategies and policies

85. The 2024-34 LTP outlines the Council's strategies, priorities and policies for the next 10 years. The proposal to sell the Council's full airport shareholding and use the proceeds to establish a new publicly owned investment fund is a central component of the LTP's financial strategy. The Notice of Motion unwinds the critical part of the financial strategy without a specified alternative plan; leaving the Council's underlying financial and balance sheet risks unaddressed.

Engagement and Consultation

86. If the Council supports the Notice of Motion, a full LTP amendment process would be undertaken which would include community consultation on options to address the Council's insurance and financial resilience risks.

Māori Impact Statement

87. Recommendation 3 of the Notice of Motion is inconsistent with the Council's Tākai Here partnership agreement in that it would mean mana whenua representatives cannot fully participate and vote on a full LTP amendment process. If the Notice of Motion passed as submitted this would mean that all matters being considered as part of the LTP amendment, (which is likely to include water reform) would be considered by Council.

88. This is a significant departure from the delegated committee structure (whereby decisions on the development of all matters relating to an LTP include mana whenua representation through Committee) and is not reflective of Council's obligations under Tākai Here.

Financial implications

89. If the Council was to support this Notice of Motion, full financial implications would be developed and brought back to the Council as part of the LTP amendment process.

Legal considerations

90. Under the Local Government Act, Councillors have a statutory duty to be prudent in its management of investments and general financial dealings (amongst other matters). These must be managed in a way that promotes the current and future interests of the community. Should Councillors support this Notice of Motion and an LTP Amendment process be commenced, it is critical that this obligation is central to any decisions made by Council as part of that process.

91. In addition, Councillors should not show (or appear to show) predetermination or bias in their decision making. If an LTP Amendment process is commenced, the proposed sale of the shares will be the subject of public consultation. Councillors have a statutory obligation to receive those views with an open mind. This does not mean that Councillors cannot have views or even strongly held views about issues. However Councillors should not commit to a particular outcome prior to the decision and should be able to demonstrate that they are open to alternatives, after listening to consultation and debate.

Risks and mitigations

92. The Council is facing major financial resilience risks, which its current 2024-34 LTP addresses via a sale of the Council's airport shareholding and establishment of a new investment fund. The Notice of Motion proposal to amend the LTP would leave these risks unaddressed and the LTP amendment process will need to consider alternative ways to mitigate the Council's financial risks.

Disability and accessibility impact

93. There are no direct disability and accessibility impacts as a result of this Notice of Motion paper. Full details would be developed through the LTP amendment process, if the Notice of Motion was supported.

Climate Change impact and considerations

94. There are no direct climate change impacts as a result of this Notice of Motion paper. Full details would be developed through the LTP amendment process, if the Notice of Motion was supported.

Communications Plan

95. Subject to the Council's decision, officers will prepare communications messages and a media statement confirming the outcome of the Notice of Motion and providing the public and other stakeholders with clear next steps on the process ahead.

Health and Safety Impact considered

96. Not applicable.

Ngā mahinga e whai ake nei | Next actions

97. If the Council supports the Notice of Motion, all work on the airport share sale and PIF establishment would cease and officers would begin planning an LTP amendment process and bring back further advice to the Council by November 2024.

98. If the Council does not support the Notice of Motion, officers will continue work on the share sale and PIF establishment project and, as previously directed by the Council, bring back advice on a sales and reinvestment strategy by December 2024.

Attachments

Attachment 1.	Notice of Motion ⇩	Page 29

Absolutely Positively
Wellington City Council
Me Heke Ki Pōneke

4 September 2024

Ms. Barbara McKerrow
Chief Executive
Wellington City Council
113 The Terrace, Te Aro
Wellington 6011

NOTICE OF MOTION

We the undersigned Wellington City Councillors formally advise that we do not support the proposed sale of the Council's shares in Wellington Airport. We therefore present the following Notice of Motion:

That Te Kaunihera o Pōneke | Wellington City Council:

1. **Agree** to commence a process to amend the 2024-34 Long-term Plan (**LTP**) with Council's objective being No Sale of any of its shareholding in Wellington International Airport Limited.
2. **Agree** that while the Council is progressing an LTP amendment to remove the share sale from the LTP, to:
   a) direct officers and relevant contractors to cease all work to progress the share sale including the currently scheduled report for December 2024.
   b) suspend any committee or individual from taking any steps or spending money to progress the share sale pursuant to any delegations made to that committee or individual: and
   c) direct that no further money is spent on establishing a Perpetual Investment Fund through the share sale.
3. **Agree** to suspend any delegations to any committee or sub-committee of Council relating to the development of the Council's draft and final long-term plan amendment.
4. **Note** it is likely that an LTP amendment will be required as part of the government's Local Water Done Well reforms.

Her Worship Tory Whanau, Mayor		**Rebecca Matthews, Councillor**	
Laurie Foon, Deputy Mayor		**Geordie Rodgers, Councillor**	
Ben McNulty, Councillor	[signature]	**Ray Chung, Councillor**	[signature]
Nīkau Wi Neera, Councillor	[signature]	**Iona Pannett, Councillor**	[signature]
Nureddin Abdurahman, Councillor (Mover)	[signature]	**Nicola Young, Councillor**	[signature]
Teri O'Neill, Councillor	[signature]	**Tony Randle, Councillor (Seconder)**	[signature]
Diane Calvert, Councillor	[signature]	**Sarah Free, Councillor**	
John Apanowicz, Councillor		**Tim Brown, Councillor**	

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