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Report PE98.446
16 September 1998
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Report to the Policy and Finance Committee
from Greg Schollurn, Chief Financial Officer

Holding Company Restructure

1. Purpose

To seek the Council's approval to the sale of Council's interest in Port Wellington Ltd to Port Investments Ltd (a 100% owned subsidiary company).

2. Public Excluded

Grounds for the exclusion of the public under the Local Government Official Information and Meetings Act 1987 are:

so as not to unreasonably prejudice the commercial position of the person who supplied the information.

3. Background

At the Policy and Finance Committee meeting on 2 October 1996 Council considered report PE96.268 and agreed in principle with restructuring the ownership of the Port Company shares, subject to a positive binding ruling being received from the IRD.

Since then officers have been working to put into effect the restructuring as outlined in report PE96.268, which essentially involves the Council selling its interest in Port Wellington to Port Investments Ltd (a 100% owned subsidiary company).

Various update reports have been prepared since October 1996 and in July 1998 a Council workshop was held to bring Councillors up to date with the restructuring plans.

Recapping the underlying reasons for the restructuring, I see the following benefits associated with the sale to **Port Investments Ltd**:

- It is consistent with the concept of commercial disciplines being exercised over commercial assets (by assigning debt to an otherwise debt free investment).
- It provides the Council with the opportunity to obtain input from external directors in exercising its governance responsibilities.
- It provides increased certainty to the rates line via interest flows on a bank deposit as opposed to dividends from shares.
- It provides the Council with increased liquidity through having a bank investment. This term deposit investment will be able to be utilised in future.
- It should provide enhanced ratepayer benefit with interest income from the term deposit exceeding Council's budgeted income from dividends and convertible note interest.

It is important to understand that the positive binding ruling received from the IRD confirms the commercial substance of the transaction.

Another important consideration in respect of the sale is the Council will remain in ultimate control of the shareholding in Port Wellington via the constitutions' of WRC Holdings Ltd and Port Investments Ltd.

The Directors of the WRC Holdings Group considered the proposed transaction at their meeting on 16 September 1998 and agreed to proceed subject to Council approval and approval of the final documentation (including the bank funding facility).

It is now an appropriate time to seek formal Council approval of the sale.

4. Comment

In terms of the original key milestones established in report PE96.268 the following progress has been made:

(i) Council agreement in principle to the structures

Such agreement was received on 2 October 1996 subject to the officers confirming that the Council has the legal power to undertake the transaction. Such legal advice was received on 22 November 1996 which provided the necessary comfort that the Council has the legal power to undertake the transaction.

(ii) Company name changes agreed

All three companies were reregistered under the Companies Act 1993 using their new names.

(iii) Agreement on Statement of Corporate Intent

The draft 1998/99 Statement of Corporate Intent has been prepared on the basis of the current structure. However, I expect that a modified 1998/99 Statement of Corporate Intent will be prepared once the sale has been effected and the impact on the WRC Holdings Group of interest costs, dividend income, convertible note interest and subvention payments are reliably estimated.

(iv) Agreement on new Constitutions

The constitutions of WRC Holdings, Pringle House and Port Investments were revised with this transaction in mind at the time the companies were reregistered as noted in (ii) above.

(v) Appointment of Directors

The size and composition of Boards of Directors of the three companies has not yet been formally considered. Given the election cycle which is now upon us it makes sense that the matter of the size and composition of the Boards of Directors should be considered by the incoming Council.

(vi) Agreement by Port Wellington Directors

The Directors of Port Wellington have approved the entry into a subvention agreement (termed "Tax Loss Sharing Agreement") after receiving the consent of the minority shareholder, the Manawatu-Wanganui Regional Council. (Refer report 98.444 on this order paper)

(vii) Receipt of positive binding ruling from IRD

The positive binding ruling which was received in February 1998, reaffirms that the sale transaction does not constitute tax avoidance. It also confirms the deductibility of interest incurred by Port Investments Ltd (as purchaser of Council's interest in Port Wellington) and WRC Holdings Ltd, while confirming Council's interest income will be exempt.

In addition to the original key milestones set in October 1996, the following progress has been made by officers:

(viii) Valuation of Port Company Shares

Officers have arranged for the Council's interest in Port Wellington to be independently valued by Credit Suisse First Boston for the purpose of establishing an arms length sale price.

The current value of the equity in the Port Company (i.e. the shares) is estimated by Credit Suisse First Boston to be \$43,000,000. This excludes the value of convertible notes.

Therefore translating this valuation of the entire Port Company into the value of Council's 76.9% interest:

• value of shares \$43,000,000	
@10/13ths	\$33,076,923
• value of convertible notes (1)	<u>\$ 7,692,305</u>
	<u>\$40,769,228</u>

(1) valued at book value on the basis of advice from Credit Suisse First Boston

On the basis of the independent advice received I am proposing that the sale price be set at \$40.8 million, subject to the price adjustment noted in section (ix) below.

(ix) Preparation of sale/purchase agreement

A sale and purchase agreement has been prepared to document the sale between the Council and Port Investments Ltd (Refer **Attachment 1**). Due to the significance of the unresolved Tranz Rail issue at Port Wellington and the potential impact on the valuation of the company I have instructed our legal advisors (Chapman Tripp) to include a "purchase price adjustment" clause within the sale and purchase agreement.

The adjustment clause is seen as necessary as the independent valuation report has been prepared on the conservative but reasonable assumption that the Tranz Rail revenue to Port Wellington will be lost with effect from the year 2001.

The clause provides that in the event that this assumption is incorrect and results in a net positive revenue stream for the Port Company beyond 2001, this will have a positive impact on the value of the Port Company and this value should be reflected in an adjusted purchase price. (The adjustment clause provides that 50% of the value increase should be translated to an adjustment to the sale price.)

The existence of the price adjustment clause is seen as commercially sound in that without it Council (as the seller) could be seen to be

acting imprudently by selling at an inappropriate time (with the uncertainty over Tranz Rail having such a large potential impact on value). By setting the adjustment at 50% of any value increment it effectively reflects a negotiated position between the seller and purchaser.

(x) Agreement with the National Bank of New Zealand

The restructuring plans are dependent on having access to the appropriate banking facilities. I have been in discussions with the National Bank with a view to finalising the appropriate banking facilities, subject of course to the approval of both the Directors of the WRC Holdings Group, and of the Council. The high level terms and conditions have been agreed and we are now reviewing the detailed documentation (with the assistance of our legal advisors).

Essentially, the terms of the banking arrangements are as follows:

(a) *WRC Investment with NBNZ*

(WRC is to invest the sale proceeds from the sale of its interest in Port Wellington with the National Bank)

The key conditions are as follows:

- Interest will be earned on a floating rate (BKBM bid rate + .35% pa). (BKBM is a standard banking pricing benchmark.)
- The term deposit can only be broken without cost at the end of each 90 or 180 day term. (whether the term is 90 or 180 days has not yet been set)
- The investment amount cannot exceed the WRC Holdings loan amount. (Refer (b) below.)
- Normal “set off” clause between WRC/NBNZ will apply.

An investment of approximately \$41 million with one financial institution (National Bank) will be a breach of Council’s current Treasury Management Policy of \$10 million with each financial institution. Given National Bank’s credit rating of AA- (the same as the Council) this is seen as an acceptable risk for Council to take. Further, our legal advisors advise that in the extremely unlikely event of the National Bank finding itself in financial difficulty, the Council would have the legal right to set off all our borrowing obligations to the bank (e.g. \$25 million Stadium funding) with the bank’s investment obligations to us. Notwithstanding this, the credit risk of the National Bank will need to be closely monitored for as long as the Council has the investment.

(b) *WRC Holdings Ltd Loan from NBNZ*

(WRC Holdings is to borrow from the National Bank in order to be able to fund Port Investment Ltd's purchase of the Council's interest in Port Wellington.)

The key conditions are as follows:

- Facility limit of \$55 million drawn in two tranches (to cover purchase and purchase adjustment, if needed). The initial tranche will be for \$40.8 million, the initial purchase price.

Whether this is increased, and if so by how much, will depend on the outcome of Port Wellington's negotiations with Tranz Rail over the coming months.

- Interest rate will be paid on a floating rate (BKBM bid rate + .45% pa).
- The loan will be secured by a first charge registered debenture over the assets and undertakings of WRC Holdings Ltd (but excluding the shares WRC Holdings holds in its subsidiary companies) and security over unpaid share capital held by WRC in WRC Holdings equating to 120% of the loan amount.
- Events that will cause review of the facility include:
 - WRC's S & P credit rating falling to A- (currently AA-)
 - WRC's General rating level exceeding 60% of its rating capacity (currently < 10%)
 - WRC losing the power to levy general rates

These are all seen as reasonable events of review for the National Bank to require, and are consistent with those imposed on the Stadium funding facility.

In addition there are enforcement events such as the normal "default" clause and a "material adverse change" clause which will enable the bank to terminate the facility if they are not satisfied with explanations received should these events occur.

(xi) **Review of capital structure of companies**

As noted in section (x) above the National Bank requires Council to increase the level of uncalled capital in WRC Holdings Ltd from its current level of \$25 million to approximately \$66 million. (Uncalled capital needs to remain at least 120% of the loan facility amount.)

To ensure that WRC Holdings Ltd has sufficient uncalled capital to call on if necessary (eg to increase its loan to Port Investments Ltd in the event that the adjustment clause is triggered) I am recommending total uncalled capital be increased further to \$75 million.

In turn, I am recommending to the Directors that they increase the level of uncalled capital held by WRC Holdings Ltd in Port Investments Ltd to provide comfort that if necessary additional capital can be provided to Port Investments Ltd at a later date. Currently there is only \$100 of capital in Port Investments, with all of this being uncalled. (i.e. there is effectively no capital.) Also, as Port Investments is to fund its purchase of Council's interest in Port Wellington via an intercompany loan from WRC Holdings Ltd the Council will need to approve the establishment of a new Advances Facility Agreement to cover this intercompany loan. This Advances Facility Agreement will be based on the standard Advances Facility Agreements which already exist between group companies.

(xii) Review of proposed structure by Standard and Poor's

Preliminary discussions have been held with Standard and Poor's to ensure the planned sale by Council to Port Investments Ltd will have no adverse impact on Council's credit rating.

Advice received to date suggests that it will not, but I wish to undertake more formal consultation with Standard and Poor's before finally proceeding with the transaction.

(xiii) Final review by IRD

As Councillors are aware we have received a positive binding ruling from the IRD on the proposed transaction. However, our advisors have suggested that it would be prudent to provide the IRD with copies of the final documentation to ensure that we have carried out the restructuring as we had indicated in the ruling application. (If the IRD subsequently discovers that the implementation of a transaction is materially different from that proposed in the binding ruling application the binding ruling can be deemed to be invalid.)

This will be done after the meeting on 22 September if the Council approves the sale transaction.

5. Recommendations

- (i) *That the report be received and the contents noted.*
- (ii) *That the Committee recommend to Council that:*
 - (a) *Council approve the sale of Council's 76.9% interest in Port Wellington (shares and convertible notes) to Port Investments Ltd at a price of \$40.8 million subject to the Chief Financial Officer receiving the necessary comfort from Standard and Poor's that the sale will not adversely impact Council's credit rating and receiving the necessary confirmation from the IRD that the transaction proposed materially reflects the contents of the binding ruling application.*
 - (b) *Council approve the sale and purchase agreement (Attachment 1 of this report) which incorporates a purchase price adjustment clause, and authorise the execution of the agreement and associated share and convertible note transfer forms, by affixing the Council's common seal.*
 - (c) *Council agree that the matter of size and composition of the Boards of Directors of WRC Holdings Ltd, Pringle House Ltd and Port Investments Ltd be considered at the appropriate time by the incoming Council.*
 - (d) *Council approve the deposit facility to be provided by the National Bank of New Zealand for the investment of Council's sale proceeds on such terms and conditions to be determined by the Chief Financial Officer in conjunction with the General Manager and Chairman.*
 - (e) *Council authorise the Chief Financial Officer in conjunction with the General Manager and Chairman to negotiate, approve and agree the precise terms and conditions of the banking facility with the National Bank of New Zealand and that the Chief Financial Officer, in conjunction with the General Manager and Chairman, be authorised to execute such documentation on behalf of the Council or cause such documentation to be executed by the Council under its common seal as the case may be.*
 - (f) *Council approve the purchase by Port Investments Ltd of Council's interest in Port Wellington and the entry by WRC Holdings Ltd into a borrowing facility with the National Bank of New Zealand (secured by a debenture over certain of its assets and undertaking) to enable the WRC Holdings Group to fund the purchase on such terms and conditions as are agreed by the Directors of the WRC Holdings Group.*

- (g) *Council's Treasury Management Policy (section 7) be amended to reflect an on-balance sheet credit exposure to the National Bank of New Zealand of up to \$50 million, subject to the Council entering into the banking facility with the National Bank of New Zealand noted in resolution (ii)d above.*
- (h) *Council approve the increase in uncalled capital held by the Wellington Regional Council in WRC Holdings Ltd from \$25 million to \$75 million and authorise the entry into and execution under its common seal the necessary shareholders' resolutions and other documentation which are considered to be necessary for the increase in capital.*
- (i) *Council approve the increase in uncalled capital held by WRC Holdings Ltd in Port Investments Ltd from \$100 to \$10 million and authorise the entry into and execution under its common seal the necessary shareholders' resolutions and other documentation which are considered to be necessary for the increase in capital.*
- (j) *Council approve the passing of the shareholders' special resolution approving WRC Holdings Ltd's entry into the Advances Facility Agreement with Port Investments Ltd.*
- (k) *Council authorise the Chief Financial Officer, in conjunction with the General Manager and Chairman, to negotiate, approve and agree the entry into and execution by the Council of such other documents, resolutions and other matters as they may consider necessary to give effect to the transactions described above.*


GREG SCHOLLUM
Chief Financial Officer

Date: 28 October 1998

Parties

WELLINGTON REGIONAL COUNCIL
(the Vendor)

PORT INVESTMENTS LIMITED
(the Purchaser)

AGREEMENT FOR SALE AND
PURCHASE OF SHARES IN
PORT WELLINGTON LIMITED

 **Chapman Tripp**
Barristers & Solicitors NEW ZEALAND

AGREEMENT FOR SALE AND PURCHASE OF SHARES

Date 28 October 1998

PARTIES

- (1) **WELLINGTON REGIONAL COUNCIL**, at Wellington (*the Vendor*).
- (2) **PORT INVESTMENTS LIMITED**, a company having its registered office at Wellington (*the Purchaser*).

BACKGROUND

- A The Vendor holds certain securities in PORT WELLINGTON LIMITED (*the Company*), in particular:
- (i) it is the registered owner of 15,384,610 ordinary shares in the Company (*the Shares*); and
 - (ii) it holds 2,634,351 unsecured convertible notes issued by the Company in accordance with the terms of a convertible note deed dated 28 June 1995 (*the Notes*),

together the Shares and Notes being *the Securities*.

- B The Vendor wishes to sell, and the Purchaser wishes to purchase the Securities for the consideration and on the terms and conditions set out in this Agreement.

TERMS AND CONDITIONS

1 DEFINITIONS AND CONSTRUCTION

1.1 Defined Terms

In this Agreement, unless the context requires otherwise:

Adjustment Event means the event described in clause 6.1;

Agreement means this Agreement and the schedule attached to it, and includes any supplementary agreement executed by the Parties;

Business Day: means any day on which banks registered in accordance with the Reserve Bank of New Zealand Act 1989 are open for general banking business in Wellington;

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AGREEMENT FOR SALE AND PURCHASE OF SHARES

Company has the meaning given to that term in Background A;

Encumbrance includes any mortgage, lien, charge and encumbrance whether equitable or otherwise over any of the Shares and includes any interest (other than any statutory or regulatory requirements of general application) adverse to the Vendor's exclusive ownership and right to transfer the Shares to the Purchaser unencumbered by any interest adverse to the Purchaser, other than as provided in the Constitution of the Company;

Notes has the meaning given to that term in Background A;

Parties means the parties to this Agreement;

Purchase Price Adjustment means the change in the value of the Shares, if any, calculated under clause 6.2;

Securities has the meaning given to that term in Background A;

Settlement Date means ^{20 November} 1998 or such other date as the Vendor and the Purchaser may agree upon in writing;

Shares has the meaning given to that term in Background A;

Warranties means the warranties and representations given by the Vendor under Clause 5.1.

1.2 Construction

In the construction of this Agreement, unless the context requires otherwise:

Background, Clauses and Schedules: references to Background, Clauses and Schedules are to background, clauses and schedules of this Agreement;

Currency: references to monetary amounts are to New Zealand currency;

Headings: the headings and sub-headings appear as a matter of convenience and shall not affect the construction of this Agreement;

Person: a reference to a person includes a reference to a body corporate and to an unincorporated body of persons;

Parties: references to any Party include the successors and any permitted assigns of that Party.

2 AGREEMENT FOR SALE AND PURCHASE

2.1 Agreement to Sell

The Vendor agrees to sell, and the Purchaser agrees to purchase, the Securities for the consideration and on the terms and conditions set out in this Agreement.

2.2 No Encumbrances

The Securities shall pass to the Purchaser free of any Encumbrances.

2.3 Entitlements with Securities

The Securities will pass to the Purchaser together with all rights attached to them at the date of this Agreement or becoming attached to them at a later date, for the consideration provided for in Clauses 3 and 6.

2.4 Waivers

The Vendor waives and will procure the waiver of any restrictions on transfer (including pre-emption rights) which may exist in relation to the Securities under the Constitution of the Company or otherwise.

3 THE PURCHASE PRICE

3.1 The Purchase Price

The purchase price for the Securities shall be the sum of \$ 40,800,000

3.2 Payments

Subject to Clause 4.2, the Purchaser shall pay the purchase price to the Vendor on the Settlement Date by electronic funds transfer to the Vendor's account at such bank as the Vendor may notify the Purchaser prior to the Settlement Date, or in such other manner as the Vendor and the Purchaser may agree.

4 SETTLEMENT

4.1 Place of Settlement

Settlement shall take place on the Settlement Date at the Wellington office of the Wellington Regional Council or any other place agreed upon between the Parties.

4.2 Vendor's Obligations

On the Settlement Date the Vendor shall deliver to the Purchaser:

4.2.1 *Transfers*: duly **executed** transfers of the Securities to the Purchaser;

4.2.2 *Share Certificates*: the share certificates (if any) for the Shares; and

4.2.3 *Note Certificates*: the certificates (if any) for the Notes.

4.3 Purchaser's Obligations

Subject to the Vendor's compliance with Clause 4.2 the Purchaser shall pay the purchase price for the Securities in accordance with the provisions of Clause 3.

5 WARRANTIES

5.1 Warranties

The Vendor gives the warranties set out in Schedule 1 to the Purchaser.

5.2 Operation of Warranties

The Warranties shall be deemed to be repeated on the Settlement Date with reference to the facts then existing.

6 PURCHASE PRICE ADJUSTMENT

6.1 Adjustment Event

If, by the first anniversary of the date of this Agreement, the assumption which was taken into account in determining the value of the Securities (which assumption related to TranzRail New Zealand Limited's relocation or upgrade of the InterIslander ferry terminal) proves to be incorrect, then a Purchase Price Adjustment shall be calculated in accordance with clause 6.2

6.2 Calculation of the Purchase Price Adjustment

The amount of the Purchase Price Adjustment shall be 50 percent of the increase in the value of the Securities directly attributable to the Adjustment Event, such amount to **be** determined either:

6.2.1 by the written agreement of the Vendor and the Purchaser; or

6.2.2 where no such agreement can be reached within 5 Business Days of the date of the Adjustment Event, by taking the average value of valuations made by two appropriately qualified valuers, one appointed by each party, the costs of each valuer to be met by the appointing party.

6.3 Payment of the Purchase Price Adjustment

The Purchase Price Adjustment calculated under clause 6.2 shall be paid by the Purchaser in the same manner as set out in Clause 3.2.

7 PAYMENTS

7.1 No deduction or set off

All payments required to be made under this Agreement shall be paid without any set-off or counterclaim and without deduction or withholding (except as required by law) of any taxes or other governmental charges.

8 VENDOR'S INDEMNITY

8.1 Indemnity

The Vendor indemnifies the Purchaser and the Company against any loss, claim, damage, expense, liability or proceeding suffered or **incurred at any time by the** Purchaser as a direct or indirect result of any breach of any of the Vendor's obligations, undertakings or warranties contained or implied in this Agreement.

9 MISCELLANEOUS CLAUSES

9.1 Arbitration

Every dispute that arises out of or in connection with this Agreement shall be determined in accordance with the Arbitration Act 1996.

9.2 No Merger

The agreements, obligations, warranties and undertakings of the Parties shall not merge with the sale and purchase of the Securities but (to the extent that they have not been completed by performance on the Settlement Date) shall remain enforceable to the fullest extent notwithstanding any rule of law to the contrary.

9.3 costs

The Parties will meet their own costs relating to the negotiation, preparation and completion of this Agreement.


9.4 Counterparts

This Agreement may be executed in two or more counterparts, each of which shall be deemed an original, but all of which together shall constitute the same instrument.

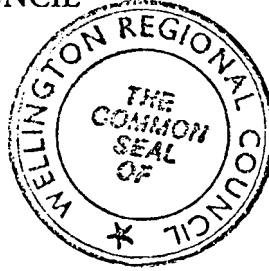
EXECUTED as an Agreement on the date first written above.

AGREEMENT FOR SALE AND PURCHASE OF SHAKES

The Common Seal of
WELLINGTON REGIONAL COUNCIL
was affixed in the presence of:




Authorised Person



Signed on behalf of
PORT INVESTMENTS LIMITED
by:



Director



Director

SCHEDULE 1

VENDOR'S WARRANTIES

(Clauses 1.1 and 5)

The Vendor gives the following Warranties (which shall be deemed to be given again on the Settlement Date) to the Purchaser:

1 Authority

The Vendor has been duly authorised to enter **into and** perform this Agreement, and has the necessary power to bind **itself in** the manner contemplated by this Agreement.

2 Unencumbered Property

The Securities will pass free of all Encumbrances.