

16 OPTIONS FOR THE USE OF UNITEDNETWORKS LIMITED SHARE SALE PROCEEDS

**PURPOSE OF THE REPORT**

The purpose of this report is to present various options associated with the use of proceeds received from the early release of UnitedNetworks Limited shares, and to recommend to the Finance and Operational Performance Committee the best immediate use of the funds.

**BACKGROUND**

**Borrowing and Investment Policy**

The Council has adopted a Borrowing and Investment Policy, which contains provisions for the use of surplus funds.

Under section 4.3 Debt Repayment the policy states:

*The Council will manage debt on a netting basis at all times with the exception of sinking funds relating to debt raised pre 1 July 1998 as provided under legislation. From 1 July 1998, the Council will only make the statutory minimum contributions to these sinking funds. Additional exemptions apply to funds vested to the Council for specific purposes as dictated by legislation.*

*The funds from all asset sales and operating surpluses will be applied to the reduction of debt and/or a reduction in borrowing requirements, unless the Council specifically directs that the funds will be put to another use.*

Further to this, within section 5.0 Risk Recognition/Identification/Management, under the term Shares, the policy states:

*Council will consider selling its non-strategic share holdings where the rate of return from owning the asset is lower than the financial benefit to ratepayers of selling and of using the proceeds of sale to repay debt. In its considerations the Council will take into account the risks associated with continuing to own the asset and the risks associated with the Council's total debt.*

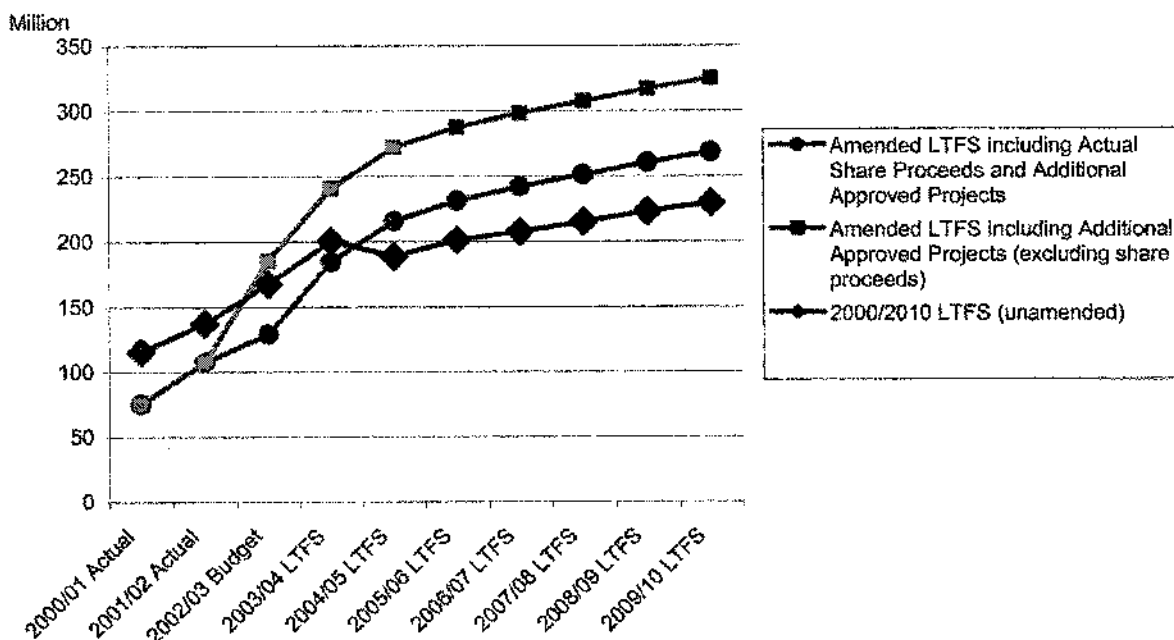
*Proceeds from share sales will go to repay existing debt, unless the Council specifically directs that the funds be put to another use.*

**Long Term Financial Strategy**

The Councils 2000/2010 Long Term Financial Strategy contains provision for the ultimate sale of the UnitedNetworks shares during the 2004/2005 year at a value of \$36.1 million. Subsequent Annual Plans have continued to factor the proceeds from the shares, into the 2004/2005 year, with the only change being the expected valuation increasing to \$51.775 million in the 2002/2003 Annual Plan, based on a discounted average valuation completed during the planning exercise.

Based on the debt position published in the 2002/2003 Annual Plan, up dated to reflect both the actual 2001/2002 year end net debt position and the inclusion of other approved projects, the following trend is predicted in net debt levels over the term covered by the current Long Term Financial Strategy.

Projected Net Term Debt to 2010



A59 - A60

During the course of the 1998 year a similar position occurred with the sale of Auckland International Airport Shares. The agenda item for the then Finance, Policy and Property Committee, dated 15 June 2000, is attached at pages A59 to A60. This shows how those funds were used to repay debt as it matured. At that time, the process took almost two years to complete.

The Annual Plan for 2002/2003 has applied an interest rate of 7.5% for loans to be refinanced and new loans. For every \$1 million of loan funds approved, there is \$75,000 added to the interest expense requirement in future years.

**WINDFALL**

The early distribution of UnitedNetworks share sale proceeds has been reported as a "windfall". By definition, a windfall is an unexpected financial gain, or other piece of good fortune. When considering the application of this definition against the distribution, the value of the windfall could only be the variance between the last recorded valuation of \$51.775 million and the actual proceeds received of \$56.354 million, a favourable variance, of \$4.579 million. A further favourable variance would be the difference between the present value (PV) and the discounted future value (FV) of the expected proceeds of \$51,775 million.

However, the use of the term windfall in its present context suggests that the distribution came as a complete surprise to Council. This is clearly not the case, and such rhetoric has only served to generate concerns amongst ratepayers as to the possible use of the funds.

## OPTIONS CONSIDERED

### Opportunity Cost

When any decision is made on the use of a particular resource, it is generally at the expense of other possible projects competing for the same resource. This is referred to as the opportunity cost. Therefore, the best use of a resource should be the project that guarantees the most valuable outcome. A minimum return on an investment should be greater than or equal to the organisations weighted average cost of capital, otherwise (in financial terms) the organisation simply should not pursue the investment.

### Early Settlement of Existing Debt

This is a case of buying back debt that has been issued prior to its maturity. Additional costs can be incurred by such a strategy, as original investors would seek compensation for the difference in the issuing interest rate and the current interest rate achievable for a similar instrument. This is much the same as an individual, with a fixed interest mortgage, would expect to pay a penalty to break the contract short of its maturity. It is not recommended that this approach be taken, as current interest rates are not favourable for a repurchase strategy.

### The Retirement of Existing Debt on Maturity and Funding Future Expenditure

Past Annual Plans have "netted" the proceeds of the share sale against the debt portfolio. In the 2002/2003 Annual Plan gross term debt was reported as being \$223.270 million by July 1, 2004, but decreasing to \$189,177 by June 30, 2005. Effectively, debt and the new loan funded capital works programme are offset by the share proceeds.

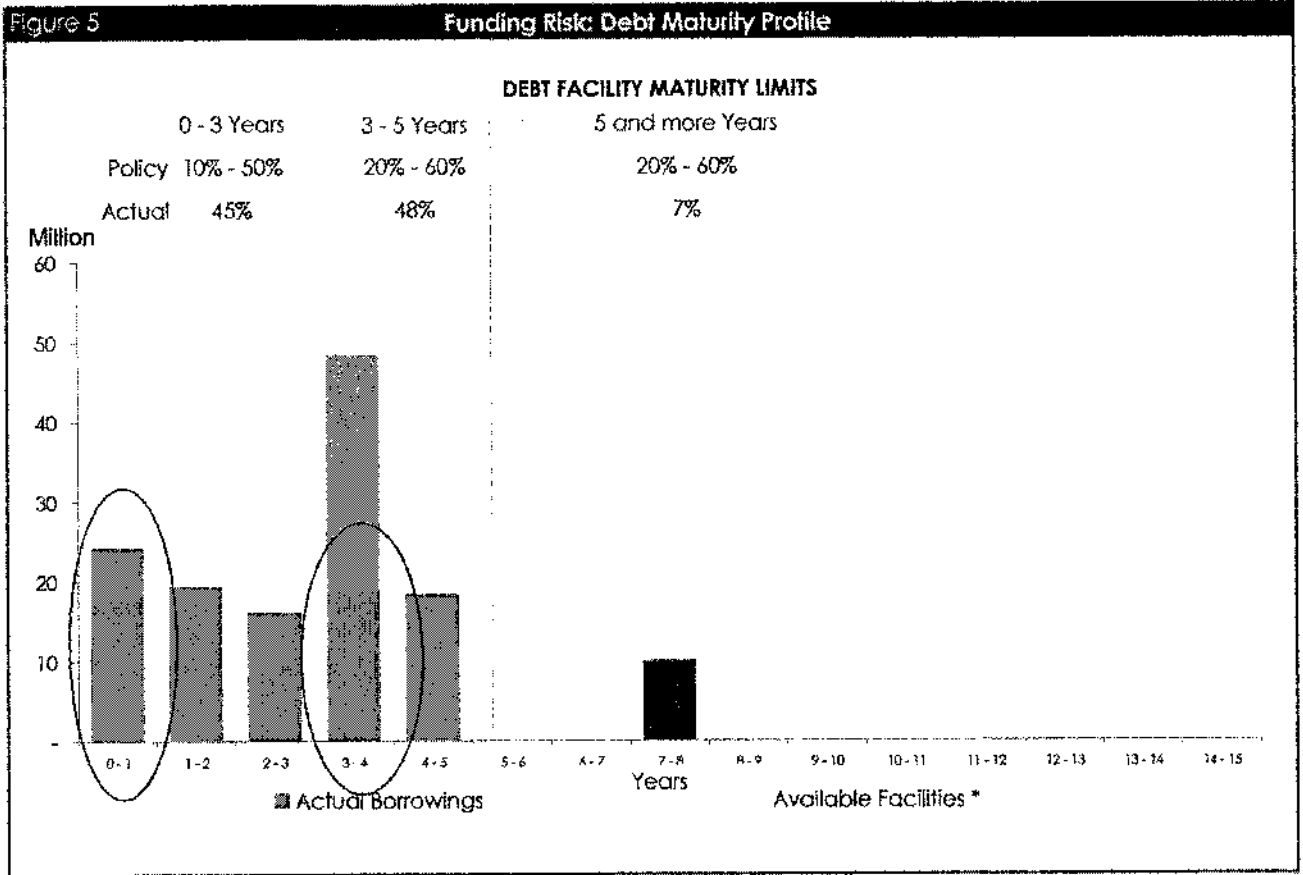
A61 - A62

During the course of the 2002/2003 Annual Plan process, an agenda item was presented discussing the future borrowing capacity of the city. This is attached at pages A61 to A62. The thrust of the report was to inform the Annual Plan Special Committee of the future restraints that Council will face. The Borrowing and Investment Policy includes some ratios as a guide to its borrowing capacity. These are as follows:

Ratio	
Net debt as a percentage of equity	<20%
Net debt as a percentage of income	<150%
Net Interest as a percentage of income	<15%
Net Interest as a percentage of annual rates income	<20%

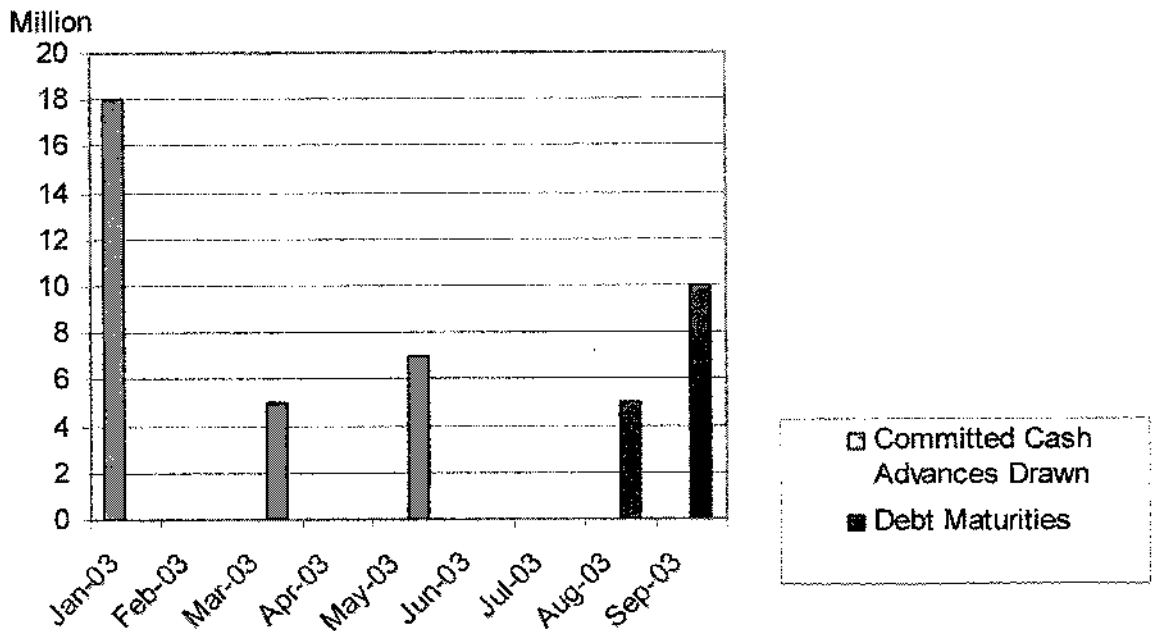
The nature of these ratios is that they indicate to Council the currently accepted prudent financial management philosophy. Further to this, they give a guide as to when the financial markets may perceive that debt levels are too high, which increases the possibility of default, resulting in an increase in borrowing costs as compensation for the increased risk.

The monthly Borrowing and Investment Report presents to Council the future debt raising and refinancing expectations. The following graphs represent the 31 October 2002 position.



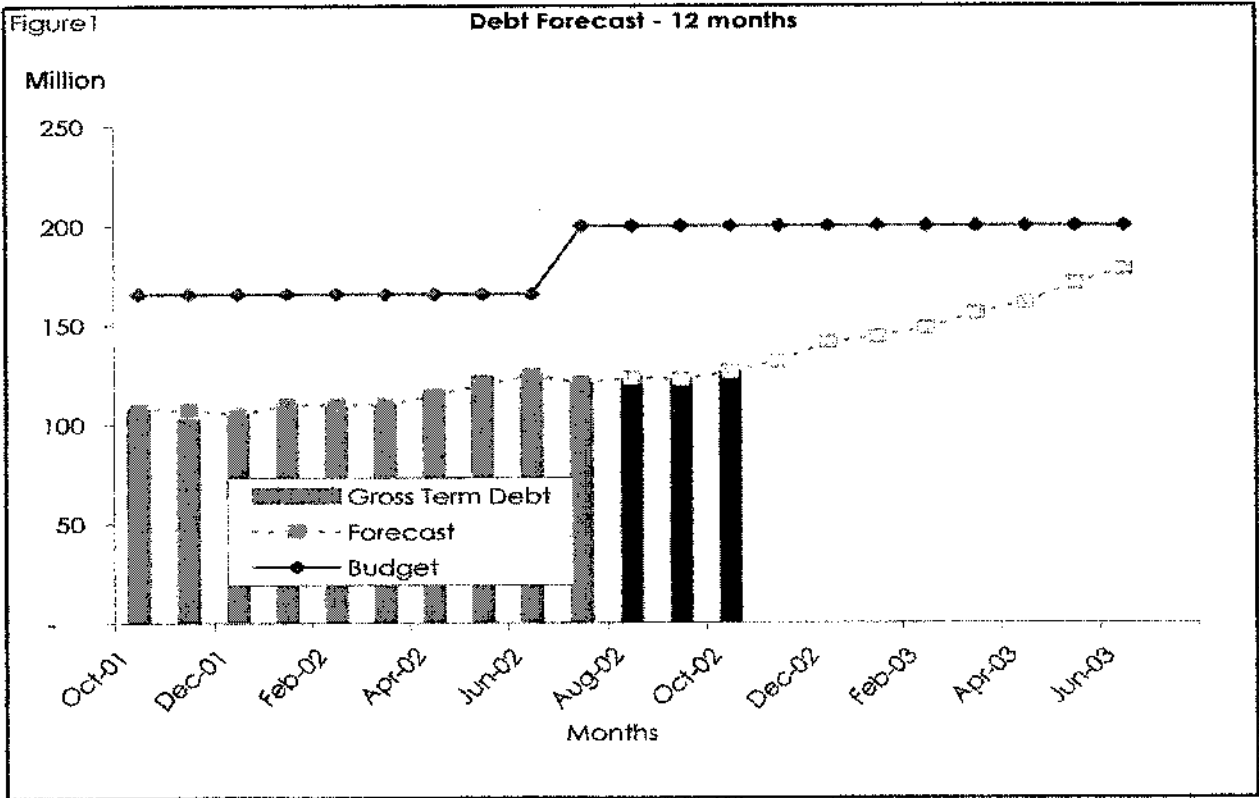
A more detailed analysis of this position is reflected as follows.

**Debt Maturities and Renegotiations by Month**

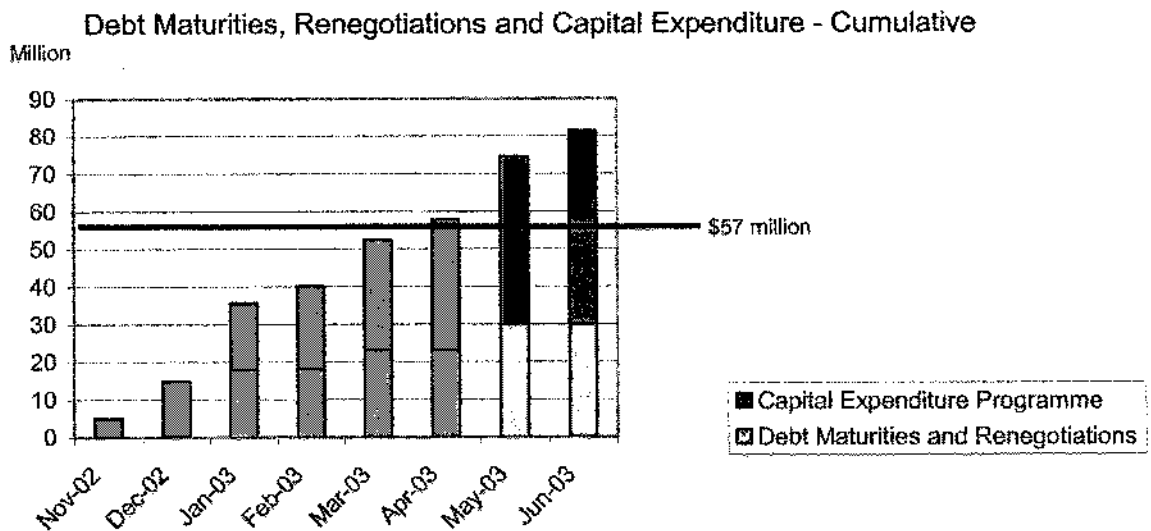


Forecasted debt requirements for approved loan funded capital works is considered in the following graph, which is also copied from the Borrowing and Investment Report, contained within this agenda.

Debt Forecast



By adding debt maturities and forecasted capital expenditure on an accumulative basis, the following borrowing programme is implied.



If no new loans were raised, under the October 2002 forecasted capital expenditure programme, the entire proceeds from the sale of the UnitedNetwork shares would be absorbed against the existing and future borrowing programme by May 2003.

### **Investments and Diversified Portfolios**

There are several different liquid investment strategies that could be initiated. Generally these can be classed as debt, equity, cash deposits or a combination of the three. Debt relates to investing in securities that principally return interest income during the course of the investment, and the principle on maturity. This is also the case of cash deposits. Excluding cash deposits, debt instruments generally offer security. Equity investments relate to the purchase of shares, with little or no guarantee of any return. The investor seeks a return through dividends and the capital growth of the share value. The more diversified position would be a combination of equities, debt instruments and cash deposits.

When considering investment strategies, the investor should always look for a diversified portfolio. Investing in one class of asset is considered risky. Investing in a number of different equity or debt instruments in different sectors within the economy, a portfolio is referred to as diversified. A portfolio is further diversified if assets are purchased from offshore markets, something that Council has not approved in the past.

Counterparty credit risk is measured by an investors analysis of the organisation in which they intend to invest. Alternatively, a Standard and Poor's credit rating is an indication by a third party of the underlying strength and ability to repay debt by an organisation when debt falls due. A credit rating is not an indication of the future strength of the companies share price, however a change in credit worthiness maybe viewed by the market as an indication of how risky that organisation is, which maybe reflected in its share price.

From an equity perspective, to mitigate unsystematic risks in shares, risks associated with sudden changes in a single organisations operation, an investor should purchase 20 - 40 different shares such as those companies listed within the NZSE40 index. More technically, the investor would consider a company's equity beta coefficient, the measure of that company's market or systematic risk when compared against the market portfolio, before adding those shares to their own portfolio. Furthermore, this measure would be used to optimise an equity based investment, meaning that by investing in more of one equity over another, a better return is expected, without increasing the portfolios risk.

It is simply not sensible to invest in one or two securities, that are considered "safe" and expect to achieve a return. With all things, the greater the risk that is taken, the greater the return is expected. However, the nature of risk is that by taking a greater risk does not mean that a greater return is guaranteed.

Investing in such instruments cannot be regarded as a core Council activity. Further to this, the return on investment must be greater than the Councils weighted average cost of capital, which is reported at 7.44% at 31 October 2002. In saying this however, interest streams or dividends could be used to progress new Council initiatives or increasing the original investment. However, over the past year, favourable interest rates have been targeted to hedge future borrowing requirements. Investments in interest bearing instruments over long terms would require this position to be unwound to some degree. This position would then add additional risks to future borrowing requirements.

### **New Fixed Asset Creation or Operational Spending**

Based on the forecasted Long Term Financial Strategy debt position, it appears to be inappropriate to channel the majority of the proceeds to new initiatives, without first either reprioritising or reviewing approved expenditure. The argument is that under the approved Long Term Financial Strategy and the inclusion of new projects, some pressure begins to appear on possible breaches of the Borrowing and Investment Policy ratios. Remembering that these ratios are adopted in order to demonstrate prudent financial management to the market in general, which in turn, reduces our cost of borrowing.

Large scale increases to the approved financial strategy only serve to limit Councils future options. The full funding of depreciation has initially generated a cash surplus that was intended to be used to mature debt. This was also included within the 2002/2003 Annual Plan. Such a position is necessary in order to minimise the possibility of breaching policy ratios, while also affording Council the freedom to move forward with its desired initiatives.

Any consideration of new capital projects and operational activities should be considered on an individual basis with the relevant research undertaken.

### **Distributions**

When considering a distribution to a shareholder or a ratepayer in this case, Council should consider the best use of the funds. A corporate that intends to present a large distribution to shareholders, either by dividends or share buy backs, actually is saying to the market "we have no future investment initiatives". Council will always have future investment initiatives, and will require funds accordingly. A distribution to Ratepayers now, only results in greater future costs associated with future expenditure programmes.

### **Loans to Organisations**

When considering giving loans to individuals or groups, a lender would question the feasibility of the action that is intended to be undertaken, and the likelihood of the loan and interest being repaid at some future time. Furthermore, a lender would not likely lend at an interest rate lower than their own weighted average cost of capital. In doing such a thing, the underlying value of the loan is diminished over the term of the loan. The intention of interest is to compensate the investor for the risk undertaken in granting the loan, and the loss in value of the principle over the duration of the loan.

It can therefore be said that a prudent financial strategy with any loan granted by Council should have an interest rate equal to weighted average cost of capital plus a margin associated with the risk of default. Further to this any loan should have some security and be related to a Council core community strategy. The Councils Community Assistance Policy provides for loans to various organisations.

### **CONCLUSION**

The Borrowing and Investment Policy has clearly stated that if Council does not specifically direct that the funds be used for other purposes, then the funds will be used to repay debt. Under the current Long Term Financial Strategy with the inclusion of other new projects not included in the Long Term Financial Strategy, the Councils borrowing ratios become challenging in future years. Adding new expenditure to this position accelerates possible ratio breaches. The Long Term Financial Strategy has netted the proceeds of the UnitedNetworks share sale against debt. Investing the proceeds would require a guaranteed return greater or equal to the cost of borrowing, in order for a netting position to break even or be favourable. Investments carry greater levels of risk, while greater risk does not guarantee greater returns.

A strategy of offsetting new borrowing requirements and repaying maturing debt with the share sale proceeds provides a saving of over \$4 million, reduces pressure on future borrowing ratios and does not introduce additional risks to the treasury portfolio. It therefore follows that the strategy that is adopted should not introduce additional risk over and above those that already exists. A long term investment strategy may require that interest rate risk management instruments that have been transacted over the past year, which will eventually lower the overall cost of borrowing, would need to be unwound. This would incur future interest rate risks to the portfolio. The least disruptive and most prudent strategy is to repay debt as it matures and offset the requirement to borrow funds in the short term, dependent on what future borrowing opportunities are presented.

### **RECOMMENDATIONS**

1. That the information be received.
2. That the \$56,353,589.60 received from the sale of the UnitedNetworks Limited shares be applied in accordance with the Borrowing and Investment Policy to repay debt.

Report prepared by: Bruce Wilkin, Funds Accountant.



**14 STATUS OF SPECIAL FUNDS**

3609/2002

MOVED by Cr Battersby, seconded Cr Presland:

That the information be received.

**CARRIED**

**15 BORROWING AND INVESTMENT REPORT**

3610/2002

MOVED by Cr Battersby, seconded Cr Fenton:

That the information be received.

**CARRIED**

12.35 pm Cr Fenton left the meeting.

**16 OPTIONS FOR THE USE OF UNITEDNETWORKS LIMITED SHARE SALE PROCEEDS**

3611/2002

MOVED by Cr Battersby, seconded Cr Nash:

That the information be received.

**CARRIED**

3612/2002

MOVED by Cr Nash, seconded Cr Brady:

That the \$56,353,589.60 received from the sale of the UnitedNetworks Limited shares be applied in accordance with the Borrowing and Investment Policy to repay debt.

**CARRIED**

12.40 pm Cr Presland left the meeting.

3613/2002

MOVED by Cr Stone, seconded Cr Brady:

1. That a copy of the options for the use of UnitedNetworks Limited Share Sale Proceeds report be referred to the four Community Boards, Te Taumata Runanga, Pacific Island Advisory Board and to Waitakere Ranges Protection Society.
2. That there be a formal response to the letter received from the Waitakere Ranges Protection Society regarding the UnitedNetworks Limited Share Sale Proceeds.

**CARRIED**

12.42 pm Cr Presland returned to the meeting.

# **Siting of New Lynn Boost Pump Station in Margan Ave, New Lynn**

## **Report to Waitakere City Council Community Board**

**Report No 2603**

**By**

*Design Services*

**6 February 2003**



# Siting of New Lynn Boost Pump Station in Margan Ave, New Lynn

## Report to Waitakere City Council Community Board

**Issue:** Final

**Prepared by:** John Parker  
Senior Civil Engineer.....

**Reviewed by:** Rob Porazinski  
Project Manager.....

**Approved by:** Don Berry  
Planning Manager.....

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**Appendix** \_\_\_\_\_ **Site Plan & Outline Design**

## **1 INTRODUCTION**

The purpose of this report is to seek approval from the Waitakere City Council Community Board for the siting of a pump station that would encroach into the Margan Green Reserve in Margan Ave, New Lynn (refer to the appendix for plan details of location). This is referred to as Site 1 in the following discussion.

Watercare is the supplier of bulk water services to Waitakere City. It has a responsibility for supplying drinking water to the Auckland Region and must do this in a cost effective, environmentally sound and socially responsible manner. It is these basic responsibilities, which are behind the need for this pump station.

## **2 REASONS FOR THE PUMP STATION**

The primary purpose of the pump station is to boost pressures and flows in Watercare's 1360mm diameter Huia No 2 watermain in order that water can be pumped to key reservoirs in Waitakere City.

The pump station will:

1. Provide security of supply to those areas of the water reticulation network that are presently supplied by the Huia Water Treatment Plant. The pump station would protect consumers against supply loss should the treatment plant and its reservoirs (the Titirangi Reservoirs) be damaged by an earthquake or other natural disaster; and
2. Maintain consumer supply in Waitakere City when the Huia Water Treatment Plant is taken out of service for essential maintenance and upgrading purposes. The upgrading works are required to meet higher drinking water standards that come into effect on 1 January 2005.

## **3 SITING OPTIONS CONSIDERED**

An investigation was carried out by Watercare to choose a suitable site for the proposed pump station. A number of sites in the New Lynn area were considered. Sites identified in Margan Ave were, however, considered most suitable for both engineering and site availability reasons. Four sites in Margan Ave were identified as being possibly suitable (refer Figure 1). Site 1 is Watercare's preferred location.

A secondary use for the pump station is that in the future it would be connected to the North Harbour Main (that supplies the North Shore). In this case it would be necessary to lay a new watermain in Margan Ave, which would travel in a westerly direction from the pump station and along Margan Ave. It therefore follows that pump station sites closer to the western end of Margan Ave are advantageous in that they reduce the amount of pipelaying required and hence cost.

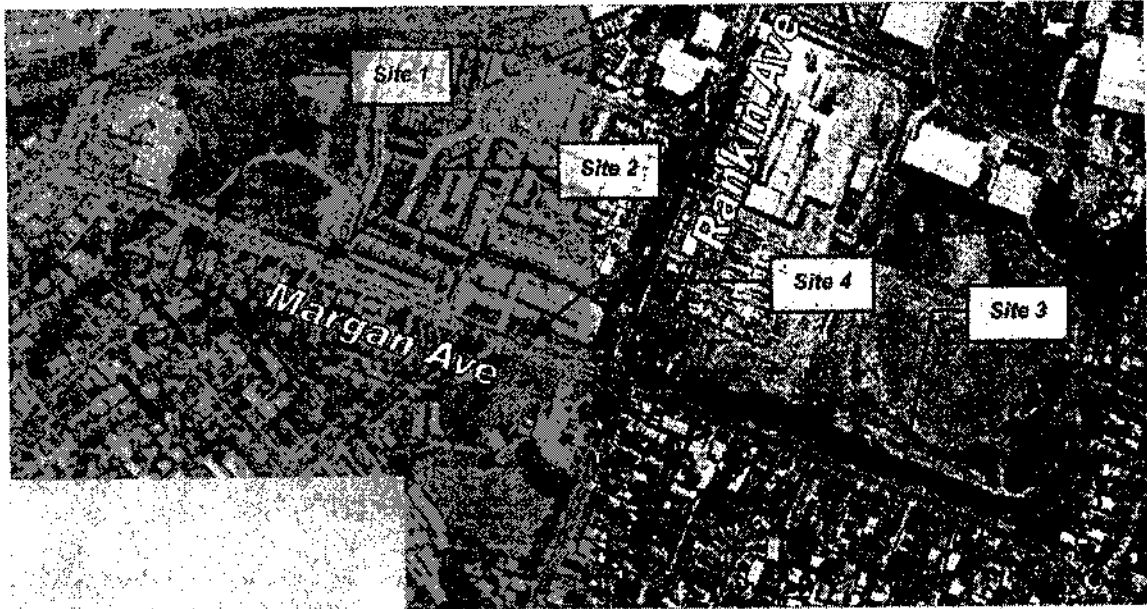


Figure 1, Aerial View of Margan Ave

The following photographs are of Site 1 showing the approximate location of the pump station and the surface mounted boxes that would be removed if the pump station were located at this site.

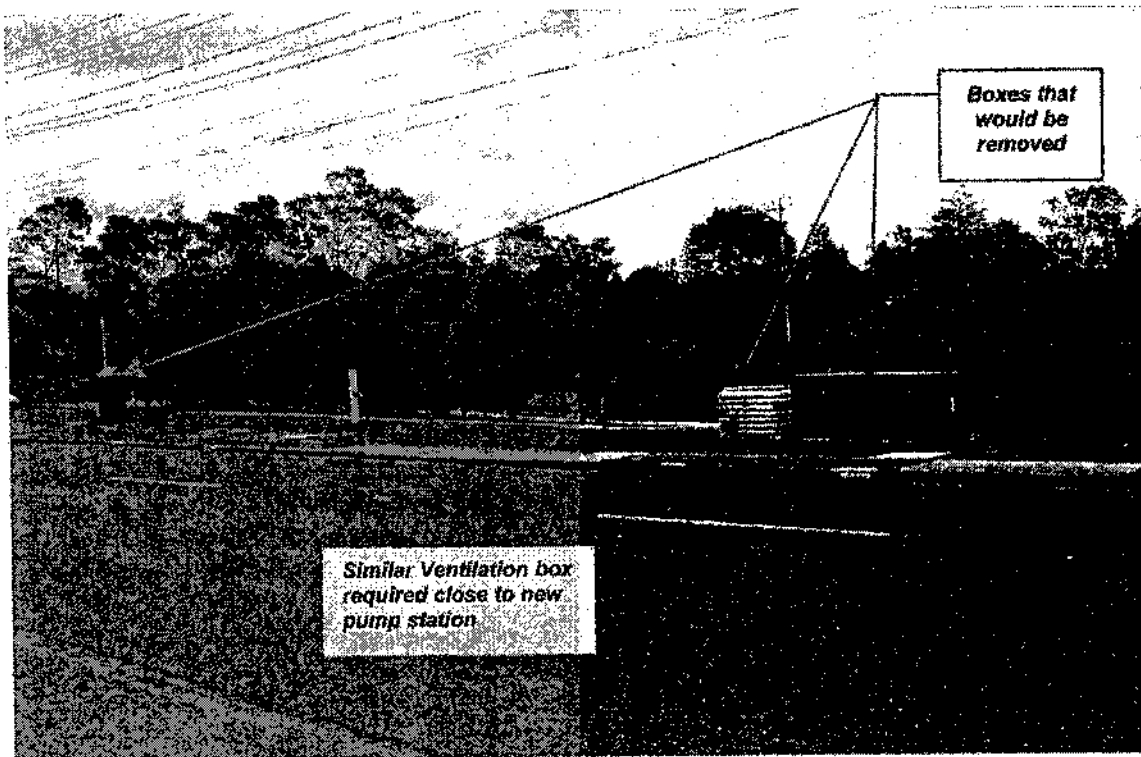


Figure 2 – Pump Station Site viewed towards Manawa Reserve (Site 1)

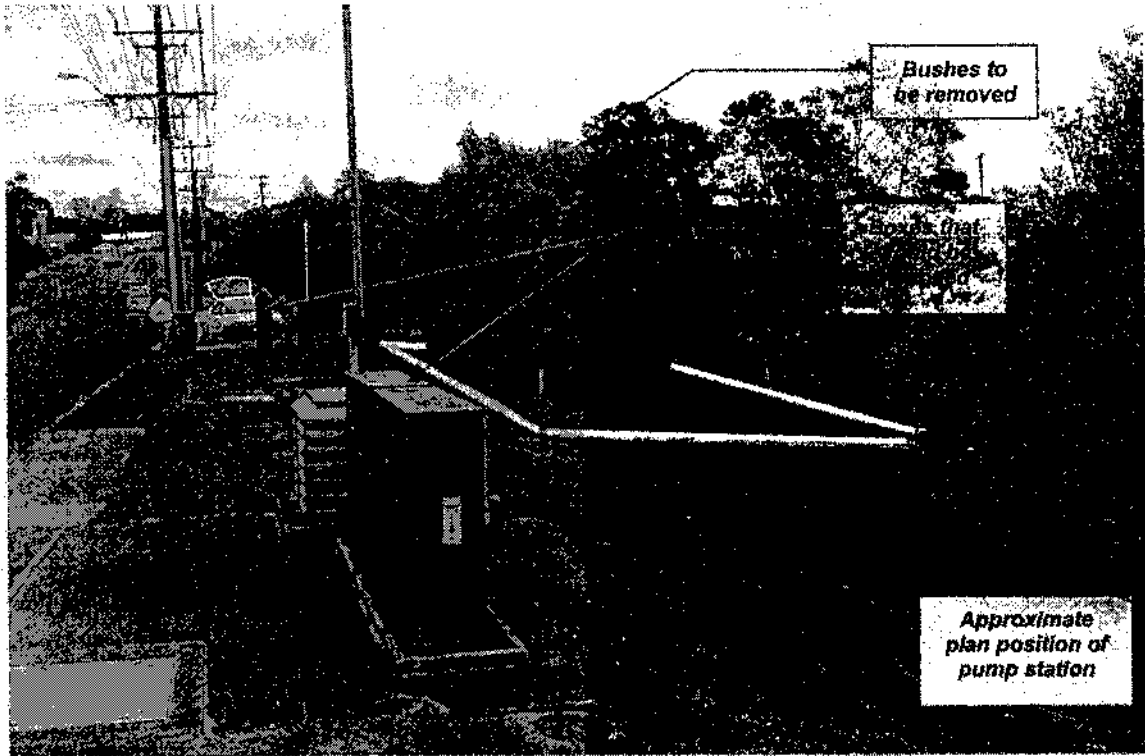


Figure 3, Close up view of pump station Site 1 showing approximate position and surface mounted boxes that would be removed.

The following table is a summary of the advantages and disadvantages of each of the sites considered.

Site	Advantages	Disadvantages	Comments
1	<ul style="list-style-type: none"> <li>▪ Makes use of an existing control valve facility on the Huia No 2 main, which is essential for the operation of the pump station. All the other sites require this facility to be duplicated at an additional cost in excess of approximately \$100,000.</li> <li>▪ Not close to any existing residences or other buildings.</li> <li>▪ Site is relatively flat</li> <li>▪ Will enable the removal of 4 kerbside utility boxes operated by Watercare, which will significantly enhance the appearance of the site from the road.</li> <li>▪ Access to the pump station would be good because site constraints are minimal.</li> <li>▪ No need to relocate any Council services.</li> </ul>	<p>A number of bushes would need to be removed to allow for the construction of the pump station. This would be compensated for with landscaping that would be undertaken as part of the works.</p>	<ul style="list-style-type: none"> <li>▪ This is Watercare's preferred site</li> <li>▪ Refer to Section 5 for discussion of features of the pump station at this site.</li> </ul>

<p>2</p>	<ul style="list-style-type: none"> <li>▪ Is not close to the Manawa Wetland Reserve.</li> </ul>	<ul style="list-style-type: none"> <li>▪ A new control valve and meter chamber would be required at an additional cost of approximately \$100,000.</li> <li>▪ Future pipeline costs for a connection to the North Harbour Main would be in the order of \$100,000.</li> <li>▪ Site is steep and it would be difficult to completely bury the pump station.</li> <li>▪ If the pump station were only partially buried a much more difficult and time-consuming consenting process would be required.</li> <li>▪ Close to existing residences.</li> <li>▪ Close to the as yet unformed end of Melview Place.</li> <li>▪ Ease of site access not good due to the relative steepness of the site.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Site not favoured because of cost and consenting issues. The use of this site would require additional expenditure of over \$200,000 compared with Site 1.</li> </ul>
<p>3</p>	<ul style="list-style-type: none"> <li>▪ Not close to any existing residences or other buildings.</li> </ul>	<ul style="list-style-type: none"> <li>▪ A new control valve and meter chamber would be required at an additional cost of approximately \$100,000.</li> <li>▪ Future pipeline costs for a connection to the North harbour main would be in the order of \$600,000.</li> <li>▪ Site is moderately steep and it would be difficult to completely bury the pump station.</li> <li>▪ If the pump station were only partially buried a much more difficult and time-consuming consenting process would be required.</li> </ul>	<ul style="list-style-type: none"> <li>▪ This site is not favoured as it would require additional expenditure of over \$700,000 compared with Site 1.</li> </ul>
<p>4</p>	<ul style="list-style-type: none"> <li>▪ Access to site is good as use can be made of the existing driveway access to the car park for the adjacent shops.</li> <li>▪ Not close to any existing residences or other buildings</li> </ul>	<ul style="list-style-type: none"> <li>▪ A new control valve and meter chamber would be required at an additional cost of approximately \$100,000.</li> <li>▪ Future pipeline costs for a connection to the North harbour main would be in the order of \$300,000.</li> <li>▪ Approval may be required to interfere with existing trees of the site.</li> </ul>	<ul style="list-style-type: none"> <li>▪ This site is not favoured as it would require additional expenditure of over \$400,000 compared with Site 1.</li> <li>▪ Site is close to the car park of a small shopping centre.</li> </ul>

## 4 TIMING CONSIDERATIONS

Essential maintenance and upgrading work at the Huia Water Treatment Plant has been programmed to commence Jan 2004 for which a shut down of that facility is required. The proposed New Lynn Pump Station will maintain supply to the areas served by that treatment plant for the duration of the upgrade work. It is therefore necessary that the New Lynn Pump Station be operational by the end of 2003.

## 5 DESCRIPTION OF PUMP STATION

The appendix contains a plan that shows the preliminary design concept for the pump station. The main features of the pump station located at Site 1 (refer Figure 1) would be as follows:

- The structure would be underground and constructed from reinforced concrete and be approximately 22m long, 6m wide and 3.5m deep;
- The pump station will house 3 pumps with a duty loading of approximately 550KW in total. A separate underground electrical control room is appended to the main pump hall;
- The surface of structure would be covered with earth to allow for grassing and landscaping;
- Two access hatches (1.6m x 1.2m x 150mm high), a ventilation enclosure (similar to that shown in Figure 2), and a radio aerial are required. These would be the only features of the underground structure visible from the surface;
- A surface mounted transformer would be required to supply power to the pump station. This does not need to be close to the pump station and it is proposed that it be located in a position away (up to 50m) from the pump station so that does not detract from the visual amenity of the reserve;
- Future access to the pumps would be by means of removable access hatches located directly over the pumps. These hatches would be buried with earth and grassed over. If removal of a pump set were required, the grass and earth covering over the hatch would need to be removed and replaced. This is expected to be a very unlikely event (perhaps once every 25 years). The surface of the pump station would therefore need to be kept clear of any significant trees;
- Vehicular access to the pump station would be by means of a Gobi block or similar driveway that would allow the retention of a grassed appearance to the immediate environs of the pump station. A small parking area (in Gobi blocks) for maintenance vehicles would also be required; and
- Limited earthworks would be required to ensure that the works fit in with the local environment and ground contours. This would be carried out in a manner agreed with Waitakere City Council.

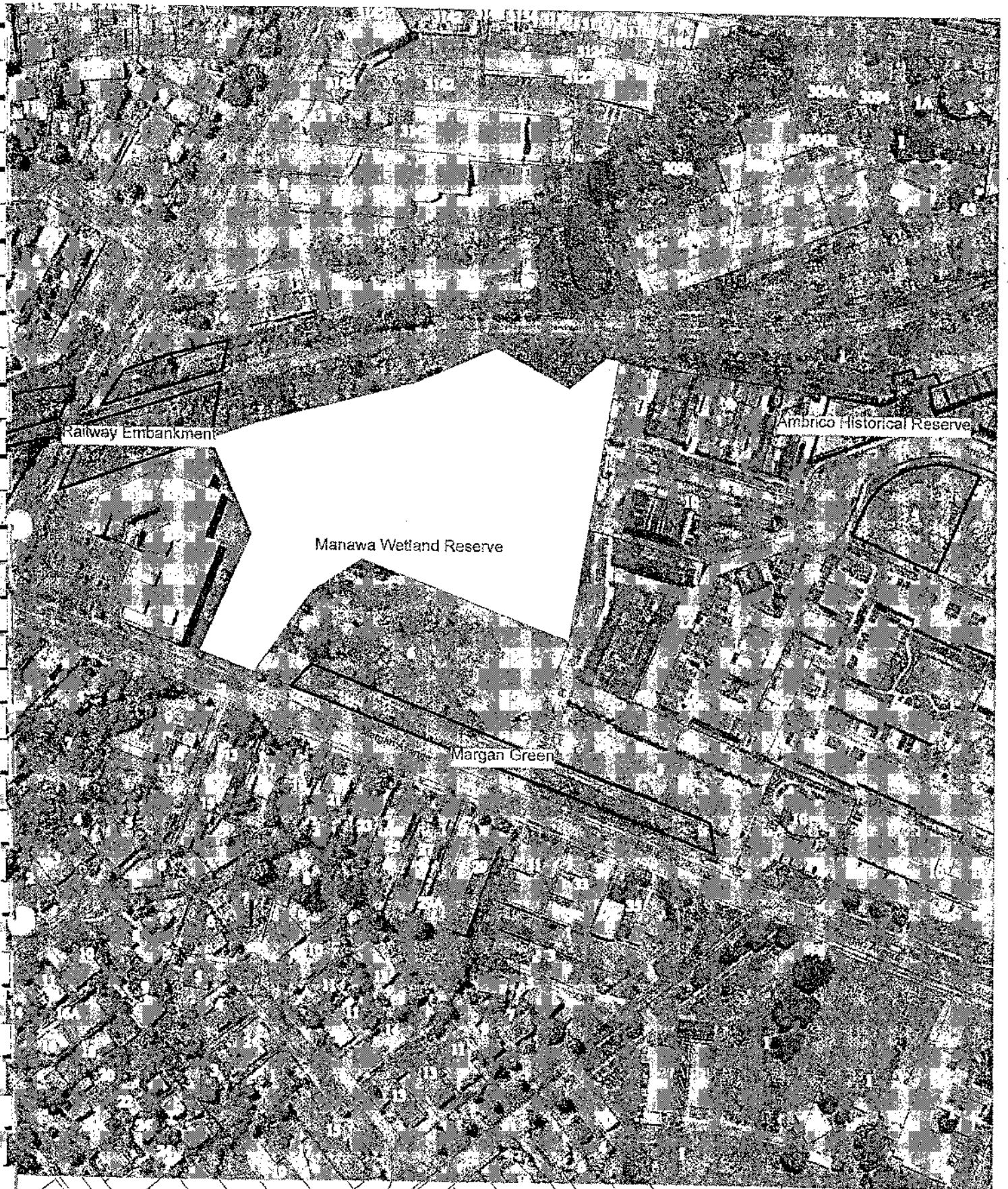
Existing kerbside electrical control and ventilation boxes would be removed if the pump station were to be built at this site (refer Figure 1 and Figure 3). We consider that this would considerably enhance the visual appearance of the site.

## 6 OTHER INFORMATION

A proposed site plan and outline design for the pump station are provided in the Appendix.

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*Appendix*  
*Site Plan & Outline Designs*



PARKS COLOUR AERIAL PHOTOGRAPHY

**Manawa Wetland Reserve**

Park Location: No Address Set



Manawatu City Council  
*Te Taiāro o Manawatu*

Map Scale 1:2,524  
Print Date 22/5/2002



The Council endeavours to provide accurate spatial data no guarantee as to the completeness and accuracy of the data shown on this plan can be given. All data should be verified on site.

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