Report 11.58
Date 28 March 2011
File CFO/09/02/01

Committee Council
Author Mike Timmer, Treasurer

WRC Holdings Group 2011/12 draft Statement of Intent

1. Purpose

To receive the 2011/12 draft Statement of Intent (SOI) of the WRC Holdings Group (refer **Attachment 1**) and to identify any matters for consideration by the directors of WRC Holdings.

2. Significance of the decision

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

3. Background

WRC Holdings Ltd and its 100% owned subsidiary companies, Port Investments Ltd (PIL), Pringle House Ltd (PHL), and Greater Wellington Rail Ltd (GWRL) are Council Controlled Trading Organisations (CCTOs) as defined under the Local Government Act (LGA) 2002. Greater Wellington Transport Ltd and Greater Wellington Infrastructure Ltd are not included in the SOI as they have no business activity and have been expressly exempted by Council resolution on 11 February 2011 to produce an SOI.

The companies noted above, together with CentrePort, form the WRC Holdings Group. A single SOI (incorporating the CentrePort Statement of Corporate Intent (SCI)) is prepared for the group and provided pursuant to section 64 (5)(b) of the Local Government Act (LGA) 2002.

The LGA 2002 requires that a draft SCI for CentrePort and a draft SOI for WRC Holdings is provided to the shareholder by 1 March, covering the projected results for the three financial years from 1 July 2011.

The directors of WRC Holdings Ltd considered the draft SCI for CentrePort and draft SOI for WRC Holdings on 24 February 2011. A letter enclosing the draft WRC Holdings SOI (incorporating the CentrePort SCI) was sent to the Chair of Greater Wellington on 24 February (refer **Attachment 2**). Greater

Wellington, as the shareholder, is now required to note the draft WRC Holdings Ltd SOI that incorporates the CentrePort SCI), and where it considers necessary, provide comments back to WRC Holdings Ltd directors. This meeting is to receive the draft and invite comments. The final version must be passed by Council on or before 30 June 2011.

4. Statement of Intent

As noted in section 1 of this report the draft SOI (incorporating the CentrePort SCI) for 2011/12 and the following two years is attached (refer **Attachment 1**).

The following is a summary of the financial results for the 2011 SOI incorporating the 2010 SOI figures for 2010/11 year and the 2011 SOI projections for the next three years.

	2010/11 $000	2011/12 $000	2012/13 $000	2013/14 $000
Net profit (deficit) before tax (NPBT)	11,4718	14,466	14,937	15,133
Net profit (deficit) after tax (NPAT)	6,983	9,847	10,250	10,482
Return on total assets	4.81%	4.46%	4.04%	3.79%
Return on shareholders equity	3.09%	4.81%	4.43%	4.24%
Shareholders equity to total assets	23.9%	22.33%	22.25%	22.07%
Dividends	940	2,257	2,538	2,793

The following analysis compares last year's SOI to this year's draft SOI followed by a commentary on the significant variances.

Contrasting these figures with last year's SOI, the changes in the key lines are as follows:

	2011/12 $000	2012/13 $000
NPBT (2010/11 SOI)	12,928	13,608
NPBT (2011/12 SOI)	14,466	14,937
Increase (Decrease)	1,538	1,329
Dividends (2010/11 SOI)	1,022	1,210
Dividends (2011/12 SOI)	2,257	2,538
Increase (Decrease)	1,235	1,328

The increase in profitability in both years is due to a reduction in interest cost of $875,000 in 2011/12 and $600,000 2012/13 in CentrePort and flowing through to WRC Holdings. CentrePort's interest reduction is being driven by the Guarantee from Greater Wellington. CentrePort's other operations expenses have also reduced by $390,000 in 2011/12 and $120,000 in 2012/13 both driving an increased profit before tax.

The sharp increase in dividend is stemming from increased profit before tax and a reduction in taxation paid due to CentrePort being able to pay a subvention[1] payment to PIL (and hence reducing its tax liability.

The dividend policy for WRC Holdings Group (excluding CentrePort) is to pay out 100% of net profit after tax (NPAT) but excluding revaluation gains and losses, CentrePort's current policy is to payout 40-60% of NPAT, with dividends forecast at the 40% level in this plan.

5. Detailed Operating Budgets

The draft operating budgets were provided to WRC Holdings Ltd directors. The commentary on these budgets, including the key assumptions and significant changes from last year's budgets, are discussed below.

5.1 Pringle House Ltd (PHL)

Total rental revenue is largely unchanged over the SOI period as no rental increases have been budgeted. The lease with Vector is up for renewal in 2012 and at this stage we are assuming the tenancy will continue.

Costs have been inflated by 2.5% per year.

The majority of the net profit in PHL is paid directly to Greater Wellington by way of a subvention payment as this is the most effective way to provide a return to the shareholder. The projected subvention payment to Greater Wellington in 2011/12 is $916,716.

Overall, the 2011/12 PHL budget shows a net profit of $196,174, after payment of the subvention to GWRC.

No gains/losses from the revaluation of the building have been assumed.

5.2 Port Investments Ltd (PIL)

The projected dividend from CentrePort (PIL's share) is expected to be $3.635 million for 2011/12 and increasing to $3.846 million and $4.0 million for the next two years respectively.

The dividend from CentrePort is based in the CentrePort's SCI projections of paying out 40% of net profit after tax.

[1] A subvention payment is a mechanism that allows tax loses within one company in a group of companies to be offset against profits in another company in the same group.

CentrePort is able to provide subvention payments to PIL beginning in 2011/12 and ending in 2015/16, the payments range from $616,000 in 2011/12 to $1.313 million in 2015/16. These can be directly offset against tax losses and as such has a significant cash benefit to the Group.

Interest expense on PIL's $44 million loan from WRC Holdings is projected to rise gradually over the SOI period.

5.3 Greater Wellington Rail Ltd (GWRL)

GWRL holds rolling stock and is presently in the process of acquiring the Matangi train units from Rotem Mitsui in Korea.

The units are funded by a 90% grant which is treated as revenue in advance and a 10% equity contribution from WRC Holdings, ex Greater Wellington. This is the portion funded by rate payers.

The revenue in advance is released annually equalling the annual depreciation of the trains.

All operating costs are met with a matching grant from Greater Wellington.

Changes are underway in relation to the ownership of the rail fleet; this is discussed further in the SOI under section 7.3.

5.4 WRC Holdings Ltd (WRCHL)

WRCHL is the holding company for PIL, PHL and GWRL. Income is sourced from dividends and interest income from its subsidiaries. It has a $44 million loan via commercial paper backed by a facility from the Commonwealth Bank of Australia (CBA).

Interest charged on the $44 million loan to CBA is offset by the income received from PIL on its $44 million advance.

Total revenue of WRCHL increases from $4.4 million in 2011/12 to $5.1 million in 2013/14 and reflects an increasing dividend from PIL due to rising dividends and subvention payments from CentrePort.

Costs are inflated by 2.5% and interest costs are rising gradually reflecting a general increase in base interest rates. However, $20 million of the $44 million debt is now locked in at a base funding cost of 4.03% till September 2014.

6. CentrePort

CentrePort is showing an increasing level of profitability, albeit at a reducing rate, with a projected profit after tax forecasted at $10 million for the 2010/11 year, moving to $13 million in 2013/14.

This supports a Group higher dividend which increases from $4.725 million in 2011/12 to $5.20 million in 2013/14.

CentrePort is also in a position to pay PIL subvention payments which start out at $616,000 in 2011/12 and increase to $966,000 in 2013/14.

CentrePort's draft Statement of Corporate Intent (SCI) does not contain any changes relating to the proposed restructuring of the Harbour Quays development.

7. Recommendations

That the Council:

(1) ***Receives*** *the report.*

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

(3) ***Receives*** *the draft Statement of Intent of WRC Holdings Group for 2011/12 and forwards any comments or recommendations to the directors of WRC Holdings Ltd for their consideration.*

Report prepared by:	Report approved by:
Mike Timmer Treasurer	Bruce Simpson Chief Financial Officer

Attachment 1: WRC Holdings Group – 2011/12 Draft Statement of Intent

Attachment 2: Copy of letter to Chair, Greater Wellington Regional Council