## 5. JADE STADIUM LIMITED - PROVISION OF DEBT FINANCE

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| Corporate Plan Output: Financial Advice | |

The purpose of this report is to advise the Council on a suitable method of providing the debt finance for Jade Stadium Limited (JSL) to fund the balance of the development project.

**BACKGROUND**

At the February 2000 meeting of the Council the business plan of JSL for the development of the stadium was approved. The Council also resolved that:

> *"The Director of Finance be requested to further investigate the most appropriate lending mechanism to provide the debt finance to Jade Stadium Limited and report back to Council as soon as possible."*

The Board of JSL have requested that the Council provide the loan finance on the assumption that the Council can borrow the funds and on-lend to JSL more readily than if JSL sought to borrow directly from a commercial source. This is particularly the case given the high gearing level of JSL in the early years of the project. This was recognised by the Council in the report on the proposed redevelopment and was the reason for the recommendation noted above requesting this report.

Victory Park Board (VPB) currently has debts of $5.5 million (including the CCC lights loan of $1.6 million) which are being serviced by JSL on behalf of VPB. For the purposes of this report the debt of both bodies will be treated as debt of JSL as all debt will be serviced from the same revenue stream and if the project is to go ahead it will be necessary for VPB to agree to be wound up and all assets and liabilities will be vested in JSL (apart from the land asset which will vest in the Council and be leased back to JSL).

**LOAN REQUIREMENT**

Assuming that all stages of the project proceed as currently planned and agreed to by Council, JSL intend to borrow progressively over the period of the building programme an additional sum which will peak in the year ending September 2001 at $39.53 million. At the time that this additional borrowing peaks JSL will still have debts to other parties totalling $3.43 million. Thus at the peak borrowing point the maximum sum required could be up to $42.96 million.

It is uncertain at this stage whether the existing loans will be repaid and refinanced but provision for this possibility is sought as an option for JSL to take up if it is practical and expedient.

**LEGAL ISSUES**

The Local Government Act makes provision in Section 601 for CCC to make advances for the purposes of recreation and community development. This clearly applies to this situation and is the legal authority on which a loan to JSL would be made.

There is also a requirement in section 594ZPA of the Local Government Act which effectively restricts any loans to a LATE to an interest rate which is not less than the open market costs of funds to the Council. The section specifically requires that the interest cost charged must not be more favourable than what the cost to the Council would be if it had borrowed without giving a rating security.

The investment of Council funds is also governed by the Council's Investment Policy. While this policy clearly provides for the lending of funds to LATEs and community organisations it is silent as to whether it is in order for the Council to borrow to on-lend to LATEs, which will be necessary in this case. It will therefore be appropriate for a suitable amendment to be made to the Investment Policy when it is next reviewed.

**BORROWING FACILITY**

The Council does not currently have any source of uncommitted reserve funds which it could use to fund a loan to JSL of this magnitude. While a possibility does exist that when the capital from the sale of the Orion gas networks is available some of this could be used to fund the loan (as an investment) it is currently too early to assume that possibility because no strategic planning for the use of those funds has been carried out. Therefore, at least in the interim, a source will need to be identified for the Council to borrow the funds to on-lend to JSL.

The JSL business plan provides for the progressive draw-down of funding as the progress payments on the project proceed and also only allows for the payment of interest during the construction period. A very flexible borrowing facility is therefore needed.

The Council has an established facility in place with CCHL whereby CCC can borrow through CCHL by CCHL either issuing bonds (fixed long term) or by the issue of commercial paper (flexible short term). Both facilities have adequate uncommitted capacity for a such a loan.

An alternative would be for CCC to borrow in its own right either by the direct issue of its own bonds, from a bank or through the Local Government Finance Corporation facility.

In view of the need for flexible finance during the construction period I consider that the most suitable arrangement will be for CCC to borrow from CCHL using the short term commercial paper facility. This will involve borrowing for periods of 90 to 180 days on a basis which can be rolled over on each maturity until the project is complete. This also has the advantage that in the current interest rate environment interest costs are lower on short term borrowing. This matter has not yet been discussed by the Board of CCHL but as it fits within the established facility I would anticipate that agreement could be reached for CCHL to provide this facility.

On completion of the project it would be appropriate to establish a more permanent long term funding facility with provision for repayment by JSL as envisaged in their business plan. This could be by the issue of longer term bonds by either CCHL or the Council or through the utilisation of CCC or CCHL capital funds from the Orion gas sale. As noted elsewhere it will be necessary for some re-investment of these funds to take place to protect the revenue streams of the Council and this could be one possibility. A decision on the long term funding arrangements is best left at this stage to assess in the light of the markets available at the time. Suffice to say there are several options available.

**SECURITY**

The loan agreement already in place between CCC and CCHL means that no further security will be necessary between CCC and CCHL.

Security will be necessary, however, to secure the lending between CCC and JSL. This should take the form of a debenture over all the assets of JSL so that any additional borrowing by JSL cannot take place without the approval of CCC.

Some enhancement will also be needed to the succession agreement between JSL, VPB and CCC pending the vesting of the land in the Council and the formalisation of a lease of the land to JSL. Currently there is a mortgage over some of the VPB assets to secure the action taken to date and this should be extended on appropriate conditions to ensure that there is adequate security for the Council lending from the outset. Some interim advice has been sought from Denis Sheard of Buddle Findlay on this matter and this will need to be worked through in detail.

A delegated authority from the Council jointly to the Director and Finance and the Director of Business Projects to approve the detail is requested.

**INTEREST COST**

In view of the restrictions of the Local Government Act on the terms of lending to LATEs it is necessary to charge a commercial interest rate. The utilisation of the CCHL commercial paper programme will ensure that this section of the Local Government Act is complied with.

CCHL will borrow at on the commercial paper market. It will be necessary for an on-cost to be placed on the market rate of approximately 30 basis points to cover CCHL costs of arranging the funding and to contribute to the facility establishment costs. These costs should be added to the interest cost charged to JSL. A further 10 points should also be added as a margin for CCC. This on-cost should be reviewable when the log term funding is established at the end of the construction period.

The actual interest cost will depend on the commercial rates chargeable at the times of borrowing and could change over the term of the arrangement. However as an indication based on today's market conditions (i.e. 29 March 2000) The rate chargeable to Jade Stadium would be as follows:

| Term | Rate |
| --- | --- |
| 30 days | 6.45% |
| 90 days | 6.81% |
| 180 days | 7.06% |

Market projections are that interest rates will increase over the balance of this year and a further 100 basis points could be added. The JSL business plan is based on interest rates of 8% during the construction period rising to 8.5% for the long term funding arrangements. Interest rate management using swaps where necessary will be negotiated with JSL if they require.

**IMPACT ON ANNUAL PLAN CHANGE**

The impact on the annual plan of this arrangement is fiscally neutral. However, it needs to be noted that the draft annual plan has been developed without reflecting the borrowing by Council to fund this on-lending to JSL. While there will be an increase in the level of gross and net debt there will be a compensating debt security as an asset on the CCC Statement of Financial Position.

It will however be appropriate to reflect this arrangement in the final annual plan once the details are finalised. It is not practical to reflect the change in the draft version of the plan as it will be with the printer before the lending arrangements are finalised.

**Recommendation:** 1. That the Council agree to lend to Jade Stadium Limited a sum of up to $43 million ($39.5 million for the project and $3.5 million for possible refinancing) on the following basis and subject to the following conditions:

(i) Prior approval of the CCHL board to borrowing the amount required under its commercial paper programme and to on-lend to CCC in accordance with the existing loan agreement.

(ii) An interest margin being charged of 30 points for CCHL and 10 points for CCC.

(iii) No repayment of principal to be required until a certificate of practical completion has been issued in respect of the project.

(iv) On practical completion of the development the Council negotiating a long term funding arrangement with JSL and CCHL to replace the short term funding arrangements.

(v) A debenture security over all the assets of JSL being provided to the Council.

(vi) An amendment to the succession agreement between JSL, VPB and CCC being made to provide for a second mortgage over the land as an interim measure to better protect JSL's position.

2. That the Director of Finance and Director of Business Projects be delegated joint authority to approve the final detailed arrangements.

3. That a loan resolution be submitted to the April meeting of the Council authorising the borrowing of a loan to fund this financial arrangement. Note: The resolution to be passed by the Council is contained in clause 2 of the report of the Chairman of the Strategy and Resources Committee.

4. That the final Annual Plan be amended to reflect the borrowing arrangements.

5. That the Investment Policy be amended to clarify the ability of the Council to borrow to on-lend to a LATE on a commercial basis.