

3. CHRISTCHURCH CITY HOLDINGS LTD - APPOINTMENT OF DIRECTORS

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The purpose of this report is to set out some options and make recommendations regarding the future size and composition of the CCHL Board, and also to make some recommendations regarding transitional arrangements for both the CCHL Board and subsidiary boards.

This report reflects earlier discussions by the CCHL Board, and has been seen and approved by the Board.

BACKGROUND

Following the recent announcement that the number of Councillors will be reduced to 12 (plus the Mayor) in the forthcoming elections, the CCHL Board has considered the impact that this may have in terms of governance and the effective operations of the company.

Currently the CCHL Board comprises nine directors – six Councillors (including the Chairperson) and three “commercial” directors appointed on the basis of their business expertise.

The question arises as to whether it would be appropriate to reduce the number of Councillor directors on the CCHL Board to reflect, at least partially, the reduced numbers of Councillors. At the same time, the Board has also considered whether its performance could be enhanced by the appointment of one or two additional commercial directors.

The CCHL Board is aware that the Council has initiated its own internal structure review to address the consequences of the reduced size of the Council, and wishes to participate in this process to the extent that it is relevant to CCHL and the operating subsidiaries. In the meantime, this report sets out CCHL’s views.

Before the detail of this issue is examined, it is worth noting the following factors:

- One of the strengths of the current arrangements is the trust that exists between CCHL and the Council. A significant element of this is the number of Councillor directors on the CCHL Board.
- The Councillor directors on the CCHL Board are all relatively senior or longstanding Councillors.
- The Councillor directors all have some exposure to business practice or professional expertise even if it is not always as directors of large businesses.

CCHL BOARD SIZE AND STRUCTURE

The CCHL Board has considered a number of options for the size and structure of the Board, and their potential advantages and disadvantages are addressed below

Scenario 1 – four Councillor directors, four commercial directors

The first scenario assumes that there is a reduction in the number of Councillor directors. Additionally, as there has been a degree of consensus in recent deliberations of the Board that the appointment of an additional commercial director would contribute to the quality of the Board and reduce the workload on the existing commercial directors, the scenario also assumes on extra commercial director.

Issue	Four Councillor directors, four commercial directors	
	Arguments in favour....	But.....
Efficiency, governance	Most commercial boards would have fewer than nine directors (eg the draft IOD Board Charter refers to a board size of six to eight). Fewer directors in total can lead to more efficient meetings, and fewer Councillor directors may reduce the risk of straying into Council matters. Also easier to organise meetings and reduced paperwork.	Arguably CCHL is not a typical board, and a greater number of directors may be appropriate given the need for a mix of political representation and commercial expertise.

Council trust in CCHL	Although under this proposal, there would be one fewer Councillor director, a greater proportion of the elected members would be on the CCHL Board. Including the Mayor, the four Councillor directors would represent 31% of the elected members, whereas currently the six Councillor directors represent 24% of the elected members).	The additional commercial director would mean that there was a 50:50 split between Councillor and independent directors, as opposed to the current 67:33 split. Potentially, there could be a perception that Council influence over key regional assets was reduced. (This, however, would be mitigated if the Chair, who has a casting vote, remained a Councillor.)
Calibre of directors	The retirement of several experienced Councillors together with the smaller size of the new Council could reduce the pool of appropriately-experienced Councillor directors, and the risk of less experienced Councillors being appointed becomes more significant. (ie excluding the Mayor, selecting five from 24 potential directors is easier than selecting three from 12).	An extra independent director would compensate for less experience in Councillor directors if that eventuates.
Council workload	The 12 Councillors are likely to have a high workload at Council level, and it may be inefficient to have four Councillors – ie including the Mayor, 31% of the Council – tied up in non-core business for at least one three hour meeting every two weeks, plus meeting preparation time and Board committee work.	If fewer Councillors were appointed to subsidiaries this may not be such a problem.
Representation at political level.	Political party ties may weaken following the downsizing, and hence the perceived requirement for a larger board to more accurately reflect political representation at Council level may reduce.	
Business environment	The business environment is becoming increasingly complex and challenging, with new issues confronting CCHL (eg public/private partnerships, company restructuring proposals, new international accounting standards). A fourth commercial director will assist CCHL in meeting these challenges.	
A more proactive CCHL approach	The CCHL Board is taking a more proactive approach to its governance role. This will demand more time, energy and resource from the Board, and the appointment of a fourth commercial director will assist in this regard.	

Scenario 2 – five Councillor directors, four commercial directors

This scenario results in the same number of directors as at present, but with one fewer Councillor director and one additional commercial director.

Many of the advantages and disadvantages referred to above would be applicable to this scenario.

A major issue, however, could be the potential difficulty of selecting a sufficient number of Councillor directors with appropriate business experience from the small pool available. It would also eliminate the opportunity to streamline the Board.

Scenario 3 – three or four Councillor directors, three commercial directors

An alternative option might be to keep the same number of commercial directors (three) and reduce the number of Councillor directors to three or four.

Most of the advantages and disadvantages set out in Scenario 1 would be applicable to this scenario, with the advantages becoming even more pronounced in most cases.

A downside compared to the proposed 4:4 split in Scenario 1 would be that the workload of the existing commercial directors would not be reduced (and indeed may even increase), and the capacity of the Board to meet new challenges will not be improved.

Scenario 4 – three Councillor directors, four commercial directors

Again, many of the pros and cons noted under Scenario 1 can be extrapolated to this scenario. In addition, the following factors are relevant:

Issue	Three Councillor directors, four commercial directors	
	Arguments in favour....	But.....
Council trust	<p>While Councillor directors would be outnumbered by commercial directors, the Chairperson could still be a Councillor.</p> <p>The smaller size of the Council may result in a greater focus on good governance rather than pure political representation, and therefore the relative numbers on the Board may not be such an issue.</p>	<p>A Councillor minority on the Board may not sit comfortably with some or most elected members, and with segments of the public.</p> <p>There would be less direct feedback on shareholder concerns to the CCHL Board.</p> <p>A worst case scenario would be a split between Councillor and commercial directors (eg over whether to pay a special dividend), resulting in a breakdown in trust between CCC and CCHL and the good governance arrangements that have existed to date.</p> <p>The Council would perceive the need for very careful scrutiny of the attitudes of commercial appointees. Potentially, the appointment process for independents could be politicised to a greater or lesser degree.</p>

On balance, the CCHL Board believes that Scenario 1 reflects the preferred outcome, and wishes to recommend a reduced board size following the Council elections this year, comprising four Councillor directors and four commercial directors.

Provided the Council is prepared to approve these changes in principle, the resolutions required to effect the above change will be brought to CCHL’s Annual General Meeting later this year for formal shareholder authorisation.

TRANSITIONAL ARRANGEMENTS

A significant body of knowledge and experience within the CCHL Board will potentially be lost following the next elections, particularly given that at least three senior Councillor directors, including the Chairperson, will not be standing for re-election.

It is therefore considered essential to maintain as much continuity as possible during the transitional phase to the new Board. The role of the chairperson is particularly critical in this regard.

The Board (in the absence of the current Chairperson) has discussed this issue, and recommends that the current Chairperson, even though she will not be standing for re-election to the Council, be re-appointed to the CCHL Board as Chairperson for an interim period of one year. This transitional arrangement would:

- enable a designated replacement Chairperson (preferably a Councillor) to become familiar with CCHL’s operations and be introduced to key players (eg subsidiary Chairs); and
- enable a proper induction process for new appointees to the Board, both Councillor and independent.

It is recognised that, in the normal course of events, it would be preferable for the Chairperson of CCHL to be a Councillor. However, in the circumstances, it is believed that for a transitional period the advantages of maintaining a degree of continuity and institutional knowledge on the CCHL Board outweigh this consideration. It would be appropriate in these circumstances for the Deputy Chairperson to be a Councillor.

The CCHL Board further recommends, on the assumption that the proposed four Councillor/four commercial director Board structure is accepted, that the current Chairperson be appointed as one of those commercial directors for a three year term (the first year of which would be as Chairperson).

In accordance with the Council's policy on the appointment and remuneration of directors, the CCHL Board will bring a further report to the Council with regard to the (re)-appointment of commercial directors to the CCHL Board.

PROCESS FOR APPOINTMENT OF DIRECTORS TO CCHL

Subject to the above proposed transitional arrangements in respect of the CCHL Chairperson, it is recommended that appointments to the CCHL Board be made in accordance with Section 5 of the Council's policy on the appointment and remuneration of directors, which was adopted by the Council in May 2003 in accordance with the requirements of the Local Government Act 2002. Relevant extracts from the policy are set out below:

"Identification of required skills, knowledge and experience of CCHL directors

Councillor directors of CCHL

The required skills, knowledge and experience for a Councillor appointment to the CCHL Board will be identified by a Council appointments committee, established immediately after the triennial Council election. The Council appointments committee will comprise three members.

In general terms, the Council appointments committee will apply similar criteria to potential Councillor candidates to those used by CCHL in its assessment of candidates for other CCTOs. However, the committee will also take into account a candidate's potential to quickly acquire business and financial skills, as well as his or her existing skills and experience.

The candidates' skills must be relevant to the requirements of the company in terms of its governance and financial requirements.

It is important that the Councillor directors have the confidence of the Council given the confidential and commercially sensitive nature of much of the business being considered.

The committee may use the services of a specialist consultant in making the above assessments.

External directors of CCHL

In the case of a vacancy for an external director appointment, whether it be a casual vacancy or arising from the non-reappointment of a retiring external director after the Council elections, the CCHL governance committee will identify the required skills, knowledge and experience for an external appointment to the CCHL Board. The same criteria as used by CCHL in its assessment of candidates for other CCTOs will be applied.

It is expected that all appointees to the CCHL board will undergo, or already have undergone, formal corporate governance training, or have the requisite experience in this area. CCHL will generally pay for at least part of any such training.

Appointment of CCHL directors

Retirement after Council elections

The CCHL constitution provides that all directors must resign immediately after each triennial Council election, although they may offer themselves for re-appointment. In practice, these resignations will take effect following the appointment of replacement directors in accordance with this policy.

Councillor directors

A Council appointments committee, assisted by a specialist consultant will, after the triennial Council elections, interview all Councillors expressing an interest in appointment to the CCHL Board. This includes existing CCHL Councillor directors retiring by rotation and offering themselves for re-appointment.

Following the interviews, the committee will make its final recommendations to the Council. The report will be "public excluded" in order to protect the privacy of the individuals concerned. The Council will consider the report and make its decision.

Public announcement of the appointments will be made as soon as practicable after the Council has made its decision.

External directors

In the case of a vacancy for an external director appointment, whether it be a casual vacancy or arising from the non-reappointment of a retiring external director after the Council elections, the same procedures will be followed as apply to the appointment of a director to a CCTO."

COUNCILLORS ON SUBSIDIARY BOARDS – TRANSITION TO NEW APPOINTMENT POLICY

Currently, a number of Councillors sit on subsidiary boards. Most were appointed for terms ending in February/March 2005. In May 2003, the Council approved a new policy on the appointment and remuneration of directors, as required by the Local Government Act 2002.

The policy, amongst other things, sets out the qualities sought in directors, and moves away from the automatic appointment of Councillor directors to subsidiary boards.

Section 4 of the policy provides that:

"The required skills, knowledge and experience for director appointments to a CCTO board are assessed in the first instance by the governance committee of CCHL, in consultation with the Chairperson of the relevant CCTO. Reference is made to current governance best practice in this area, as encapsulated in Institute of Directors' guidelines and other relevant material. External assistance may be used in some cases.

The mix of skills and experience on the CCTO board will be taken into account, and consideration given to complementing and reinforcing existing skills and reducing known weaknesses where necessary.

In general terms, the following qualities are sought in directors of CCTOs:

- a) Intellectual ability*
- b) Commercial experience*
- c) Understanding of governance issues*
- d) Sound judgement*
- e) High standard of personal integrity*
- f) Commitment to the principles of good corporate citizenship*
- g) Understanding of the wider interests of the publicly-accountable shareholder*

As a general principle, the Council would seek to appoint one person who, while meeting all of the above criteria, has particular strengths in terms of attribute g).

It is expected that all appointees to CCTO boards will undergo, or already have undergone, formal corporate governance training, or have the requisite experience in this area.

Neither Councillors nor Council staff are precluded under this policy from appointment to CCTO boards."

It is anticipated that the policy may be tested if some current Councillors who are directors of subsidiary companies (excluding CCHL) do not stand for re-election as Councillors, or fail to get re-elected. Most current Councillor director positions, based on previous appointment terms, are due for review in February or March 2005. At that time, it may be reasoned by some that as those directors are no longer Councillors, they should automatically step down from their boards and be replaced by new Councillors. The CCHL Board strongly recommends that this approach **not** be taken, as it would be contrary to the Council's adopted policy and inconsistent with principles of good governance. Appointments are not made on the basis of representation.

Instead, to assist the transition to the new policy, it is recommended that in February 2005, CCHL be authorised to specifically review the positions of those directors on subsidiary boards who either are Councillors or were Councillors immediately prior to the elections, and are due to retire by rotation at that time. The review would be conducted in terms of the Council's appointment policy, and encompass such steps as identification of the required skills through discussion with the Chairperson, and identification and interview of suitable candidates using external consultants. If the incumbent, or any other Councillors at that time, wished to be considered for (re-)appointment, they would undergo the same process.

Having completed the review, CCHL would then report to the Council with its recommendations, and the Council would then make its final decisions. Appointments would then be made for terms consistent with the companies' AGM and rotation cycles, rather than the Council's election cycle.

In the case of any Councillors or ex-Councillors who are on subsidiary boards after the elections, but are not due to retire by rotation until some time after (ie they have been appointed in relation to the company's AGM cycle rather than the Council's election cycle), it is recommended that their position be reviewed at the scheduled rotation date rather than in February 2005.

The Committee concurred with the views of CCHL regarding the need to maintain continuity during the transitional phase to the new Board following the 2004 elections and supported the proposal to reappoint the current Chairperson for an interim period of one year. However, the Committee considered that the decision to reappoint the current CCHL Chairperson as an external director for a further term of three years should be made in accordance with the Council's Policy on Appointment of Directors.

- Recommendation:**
1. That the Council approve a restructuring of the CCHL Board, to be formally approved at the company's next Annual General Meeting, that would result in the Board comprising four Councillor directors and four commercial directors.
 2. That, to facilitate the transition to the new structure, the Council approve the re-appointment of the current CCHL Chairperson as an external director and Chairperson for one year, following which the Chair of CCHL be a City Councillor.
 3. That, in respect of Councillors who are directors of subsidiary companies (excluding CCHL), and are due to retire by rotation in February or March 2005, their positions be reviewed and filled in accordance with Section 4 of the Council's policy on the appointment and remuneration of directors.