

15. REPORT FROM CHRISTCHURCH CITY HOLDINGS LIMITED

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The purpose of this report is to

- (a) Provide information to the Council on recent activities of Christchurch City Holdings Limited ('CCHL'); and
- (b) Recommend to the Council a process for appointment of Councillors to company boards following the forthcoming elections

LYTTELTON PORT COMPANY LIMITED ('LPC')

Financial Statements for the year ended 30 June 2001

LPC has recently announced its results for the year ended 30 June 2001. While gross revenue was more or less unchanged at \$58.3 million, the net profit after tax was \$13.7 million, compared with \$14.9 million in the previous year. The reduction in profit reflected a number of factors, including dredging costs in the first half of the year, higher fuel costs, pressures on margins and higher financing expenses. While there was a decrease in profit compared with last year, it should be borne in mind that last year was a record one in many respects.

Container trade volumes through the Lyttelton Container Terminal were slightly down on last year, and there is increasing pressure on margins. On the other hand, there were significant increases in coal volumes (up 23%) and cars (up 7%). A memorandum of understanding with Solid Energy for a long term coal supply agreement was signed earlier in the year. The diversity of trades through the port is a significant advantage for the company.

SELWYN PLANTATION BOARD LIMITED ('SPBL')

Financial Statements for the year ended 31 March 2001

SPBL recorded a net surplus before tax for the year of \$2.5 million, compared with \$0.9 million in the previous year. This improvement is a direct result of an increase in production which, at 139,000 tonnes, is now considered to be at or slightly under a sustainable level. After tax, the net surplus was \$2.1 million (2000: \$1.5 million) – the earlier year contained some one-off tax adjustments that make direct comparison difficult.

Notwithstanding the increase in production, the company continues to face a difficult trading environment, with flat or falling world prices.

In addition to the ordinary dividend, the company paid a special dividend of \$1 million in March 2001 (CCC share \$0.39 million). This was possible as a result of a favourable cash position arising from a taxation refund and a low level of capital expenditure required.

APPOINTMENT OF COUNCILLOR DIRECTORS TO SUBSIDIARY BOARDS

Background

Most of the companies in which the Council has an interest currently have at least one Councillor appointed to the Board of the company. It has been normal practice for these appointments to terminate following the triennial elections and for reappointments or new appointments to be made.

In September 1998 the Council agreed on the following structure for the review of the Councillor appointments to the Boards:

- Councillor representatives on CCHL appointed by the Council in November, immediately following the local body elections.
- A subcommittee of the Council established as an appointment panel to recommend to the Council the appointment of Councillor directors to subsidiary company boards. It was agreed that appointments would be made in the February following the triennial elections

- The membership of this appointment subcommittee was the Chair of the Strategy and Resources Committee, the Chair of CCHL, one other Councillor and a non-Councillor. (Mr Murray Rodgers, Management Consultant, was employed to work with the subcommittee.)

The subcommittee developed a process which included:

- seeking expressions of interest from interested Councillors, including incumbent directors
- discussions with the Chairpersons of the various Boards to determine the skills and experience needed on each board
- interviews of individual Councillor applicants by a management consultant and reporting on their suitability to the subcommittee
- consideration of the most appropriate appointments by the subcommittee and formulation of a recommendation to the Council.

Current Position

The following table lists and analyses according to appointment source the current directors appointed to each of the companies:

Company	Number of Directors	CCC appointed Councillor/Staff	CCC appointed External	Appointed by Other shareholders
Christchurch City Holdings	9	James (C) Austin Close Harrow Moore Stewart	Stock Taylor Boyce	
Orion	7 (Note: Constn allows for 8)		Carter Constable (C) Gray Laurie (MD) Rae Vacancy	Gould
Christchurch International Airport	6	O'Rourke Sherriff	Bradley Sheldon	Lyll Thomas
Lyttelton Port Company	7	Howell	Layton (C) McCormack Grant Sundstrum Stewart Viles (MD)	
Redbus	4 (Note: Constn allows for 6)	Ganda	Urlwin (C) Frew McFedries	
Selwyn Plantation Board	6	Buist	Coakley Berge	Marsh (C) Heenan Vacancy
City Care	5	Wright	Spence (C) Marsh Foster Young	
Christchurch City Facilities	4	Condon Corbett	Taylor (C) Sheard	
Jade Stadium	7	Austin Baker Wright	Irvine (C) Buck Johnstone Prendergast	
Travis Group	3	Lineham	Russell Taylor	

General Issues relating to Director appointments

There are a number of issues which need to be considered when making appointments to the boards:

- **Skill Set** - A board is a small but critically important group of people who are responsible for the successful governance of a company. Because of the size it is essential that there is a range of skills represented on the board. However, all directors need to also be able to actively contribute to the majority of board deliberations which are primarily commercial in nature. Since the Council depends heavily on the revenue arising from its trading investments, it is essential that there be a balance of skills around the table so that the board can effectively carry out its governance role for the benefit of the Council as shareholder.
- **Diversity** - While a diversity of skills is valuable, no director should be appointed solely because of one particular attribute as contributions are needed to a wide range of issues on a regular basis. All directors would need to have as a minimum, a good general knowledge of commercial issues and be able to understand complex board papers and issues of commercial law and practice.
- **Responsible to the Company** - The Companies Act and accepted corporate governance principles make directors primarily responsible to act in the best interests of the company. The role and responsibility of directors therefore lies in a different direction to that of a Councillor who is appointed as a representative of a constituency. This does not mean a Councillor cannot fill both roles but simply that the responsibility is different in nature.
- **Reporting** - Because the responsibility of a director is primarily to the company, it is not the director's official role to report back to the Council as an individual. Protocols have been established where the companies report in writing and/or through their Chairperson and Chief Executive. This formal reporting therefore happens whether or not a Councillor is appointed.
- **Time Commitment** - While many of the companies meet only on a monthly basis there are usually some committees and a director must make a significant time commitment in order to be well-briefed and have the capacity to participate fully in all meetings. Time needs to be set aside to ensure that, as far as is reasonably possible, full attendance at board meetings is achieved.
- **Community Input** - Most of the Council's trading companies have a significant element of monopoly trading and have a significant impact on the local community. An appreciation of community values and concerns is therefore a valuable attribute to be represented on the boards of the various companies, but this needs to be enhanced by a good general knowledge of commercial issues as well. Councillors will contribute to this mix of skills because of their business experience and knowledge of public issues and shareholder expectations.
- **Size of Boards** - It will be noted from the table above that in some cases the number of directors appointed is less than that permitted in the company constitution. This is as a result of previous decisions that the boards were too large. Particularly in the smaller companies the costs of a large board is unjustified. A small cohesive board with good skill diversity is also often more effective than a large group.
- **Length of Tenure** - It is accepted practice that directors of companies should be periodically changed to ensure new ideas and challenge is introduced on a rotational basis. The Crown has a practice of replacing directors after six years. However, the Council adopted a policy some years ago that appointments should be reviewed after six and nine years and generally no director would serve for longer than twelve years under the policy.
- **Continuity** - In normal circumstances it is wise not to make radical changes to boards so that corporate knowledge is not lost on a wholesale basis. It is best to ensure that some depth of experience is retained on each board by making incremental changes.
- **Consistency of Councillor appointments** - It is noted from the above table that the number of Councillors appointed to the boards varies. In the case of Orion there are no Councillor appointments although two of the directors are former Councillors. CIAL and CCFL has two Councillors and Jade has three. In the case of Jade the third appointment arose because Councillor Austin was appointed to the initial board before she was elected as a Councillor. There is some merit in rationalising the inconsistency in Councillor numbers on the various boards.

Role of Councillor Director Appointments

The governance model established between Council, CCHL and the trading subsidiaries is not dependent on Councillor appointments to the trading subsidiaries in terms of representation and reporting as these are handled on a subsidiary to CCHL interface through formal reporting procedures. However, there is a role to ensure that each of the company boards understand community interest issues and Councillors are generally well suited to fill this role provided they can also contribute to the general commercial issues of board business.

Due to the small size of the boards and the need for a wide range of commercial and other skill sets, consideration should be given to the appointment of one Councillor only to each board.

CCHL Director Appointments

CCHL has an important but different role to fulfil as the monitoring entity which can interface with the trading subsidiaries and question their boards on the issues which require accountability to the shareholder. Many of the companies are operating in commercially sensitive areas and for a full and frank disclosure of information to take place, the companies need to be able to discuss issues in a confidential environment. CCHL is able to fulfil this role on behalf of Council. In order to have the confidence of the Council in this function it is therefore essential that there be a significant Councillor representation on the CCHL board.

The constitution of CCHL provides for nine directors, two of whom must be external to the Council. Currently there are three external directors and six Councillors.

There is considerable value in having at least three strong commercial directors on the CCHL board. A fourth would add extra value through diversity of skills. It would also boost skills in anticipation of the likely need to consider progressively retiring the longer serving external directors over the next two to four years. However, an increase in numbers would reduce the number of Councillors on the board and this needs to be balanced against maintaining the confidence of the Council.

Councillor directors on CCHL need to have a general ability to understand commercial issues and financial reports and inquire into the drivers relating to the subsidiary businesses. However, the intensity of commercial knowledge needed is generally not as great as directors who are at the coalface of operating companies. Ideally the selected Councillor directors on CCHL will be Councillors from a cross-section of the Council who have the confidence of the Council as a whole and a general commercial knowledge.

Time Frame for Appointments

Because of the importance of making the best possible appointments to boards, the Council (in 1998) adopted the practice, outlined in the background section of this report, of making Councillor appointments to subsidiary boards in the February following the triennial elections. The process allowed all interested Councillors to register interest and provided for an evaluation of the skills of Councillors seeking appointment utilising the services of a management consultant. It is proposed that a similar process is utilised again this year.

The constitution of LPC provides for director replacements to take place at the annual meeting of the company and therefore any decision made about a Councillor appointment to LPC would not be implemented until October 2002.

The Councillor directors for the CCHL Board are more appropriately selected on a representative basis and should be appointed directly by the Council at the time it appoints its standing committees.

Rotation of Commercial Directors

The constitutions of all the trading subsidiaries provide for regular rotation of directors, generally on a three yearly cycle. As noted above it is established policy to review appointments after six and nine years and generally no director would serve for longer than twelve years.

It is normal practice where CCHL has reviewed an external appointment and considers it appropriate to reappoint the director for a further term for this to be actioned by CCHL. For the sake of clarity it would be appropriate for Council to ratify this practice.

Eligibility to Vote on this Issue

The issue of whether Councillors are eligible to vote on the appointment of directors was considered in 1998 by the Legal Services Manager as in the past there has been some doubt, particularly relating to the payment of directors' fees.

The Legal Services Manager advised that all Councillors are eligible to vote on this matter including those who have applied for a position or are being appointed. Peter Mitchell's opinion is set out below.

"A Councillor who is nominated to the position of a director to a subsidiary company board can legally discuss and vote on that Councillor's nomination.

While s.6(1) of the Local Authorities (Members Interests) Act 1968 has a prohibition on a Councillor speaking or voting on a matter in which they have a pecuniary interest (as here) s.6(3) of the same statute provides:

"(3) Nothing in subsection (1) of this section shall apply with respect to any of the following matters:

*(c) An election or **appointment of a member of the local authority to any office**, notwithstanding that any remuneration or allowance is or may be payable in respect of that office".*

The words "...appointment...to any office..." includes appointment as a director to a subsidiary board so all Councillors can discuss and vote on such appointments.

For clarity, this exemption does not extend to matters such as the level of remuneration for such directors. My previous advice was that Councillors/directors cannot discuss/vote on that issue.

Here the issue is the appointment, not the remuneration."

Recommendation: That it be recommended to the incoming Council at its inaugural meeting in November 2001:

1. That five or six experienced Councillors be appointed by the Council to the Board of CCHL at the time that it appoints its standing committees.
2. That CCHL be requested to:
 - (a) Review the appointment of Councillor directors to all subsidiary boards using a process similar to that adopted in 1998.
 - (b) Ascertain and consider the skill set required for each of the subsidiary boards in determining the most suitable appointment recommendations.
 - (c) Consider recommending the appointment of one Councillor to each subsidiary board unless there are exceptional circumstances.
 - (d) Recommend appointments to Council no later than March 2002.
3. That CCHL be authorised to approve, if it is deemed appropriate, the reappointment of existing external directors to subsidiary company boards when they are due for retirement by rotation.

Chairman's

Recommendation:

1. That recommendations 1 and 2 be adopted.
2. That the opening words of recommendation 3 be amended to read:

"That CCHL be **requested to recommend to the Council**, if it is deemed appropriate, the reappointment of existing external directors to subsidiary company boards when they are due for retirement by rotation."