## 18. CHRISTCHURCH CITY FACILITIES – ACQUISITION OF SHARES IN NCC (NZ) LIMITED

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| **Manager responsible:** | Director of Strategic Investment |
| **Officer responsible:** | Chairman, Christchurch City Facilities Limited |
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### PURPOSE OF REPORT

1. The purpose of this report is to obtain approval of the Council for the acquisition of shares in NCC (NZ) Ltd by Christchurch City Facilities Limited (CCFL) and to explain the circumstances which have led to this needing to be a retrospective approval.

### EXECUTIVE SUMMARY

2. CCFL have negotiated a purchase of 50% of the shares in NCC (NZ) Ltd which is a special purpose company with a management contract over the assets of CCFL. This contract has been consummated without the required approval of CCC and retrospective approval is now being sought.

3. The purchase of the shares is beneficial to CCFL and CC in the relatively short term.

4. The failure to obtain prior approval of the Council is the result of an oversight and not a deliberate action on the part of any party.

### FINANCIAL AND LEGAL CONSIDERATIONS

5. CCFL will have improved cash flows as a result of this arrangement and expects to recoup the outlay on the shares within one year.

6. CCFL is required by its Statement of Intent to obtain the approval of the Council to any acquisition of shares and this is the purpose of this report.

### STAFF RECOMMENDATIONS

It is recommended that the Council:

(a) Approve the acquisition of 50% of the shares by in NCC (NZ) Ltd by CCFL.

(b) Accept the explanation for the need to obtain retrospective approval from the Council.

### BACKGROUND ON CHRISTCHURCH CITY FACILITIES – ACQUISITION OF SHARES IN NCC (NZ) LIMITED

7. When CCFL was established in 1996 it contracted the management of the three venues to NCC (NZ) Ltd which was a company jointly owned by NCC Management and Development Co Ltd (Bangkok) and Addington Raceway Limited.

8. This contract was initially for a 10 year term and then had two five year rights of renewal. In October 2004 NCC (NZ) Ltd gave notice to CCFL that it wished to renegotiate a further extension of the contract for effect on renewal at 30 June 2006.

9. CCFL entered into the renewal negotiations with a desire to obtain a greater involvement in the management of the facilities and sought to negotiate some changes in the contract. CCFL had authority to conclude the renegotiation of the contract without reference to the Council as this was an operational issue. However, the outcome of these negotiations was an agreement that CCFL would obtain that greater involvement through purchasing the shares held by NCC (Bangkok) and this shifted the form of contract to require approval of the Council.

10. The Council was informed of the commencement of the renegotiation process with NCC (NZ) Ltd in a report to the Council in October 2004 as part of a comprehensive report regarding the proposed merger of CCFL and JSL. However, this was before the acquisition of shares was contemplated by the parties as a likely solution.

11. On 31 August 2005 a press release was prepared to announce the details of the arrangements entered into regarding the purchase of the shares in NCC (NZ) Limited. The press release was sent by email to Councillors individually before it was released to the media as CCFL wanted Councillors to know the details first. For completeness a copy of that press release is attached also to this report as Appendix 1.

12. The Statement of Intent for CCFL has a requirement that:

    *"No acquisition of shares in a company will take place without the prior approval of the Council."*

    Unfortunately this requirement was overlooked and therefore it is now necessary to seek retrospective approval for the purchase of these shares.

**Relationships**

13. CCFL is a company which is directly owned by the Council and therefore shareholder issues relate directly to the Council and so the Statement of Intent requires reporting of acquisitions to the Council. This is different to companies which are owned directly by CCHL. Where there is a requirement for the CCHL subsidiaries to obtain approval from CCHL (not required of all of them) the obligation is to CCHL and not to the Council. Where the issue is material, then CCHL would report that matter to CCC as a routine 'for information', but not 'approval'.

14. CCFL is monitored by CCHL on behalf of the Council. This monitoring involves regular quarterly reporting by the company to CCHL who report to the Council as deemed appropriate.

15. CCFL reported orally to CCHL on progress with the negotiations with NCC in June 2005 and again in August 2005. The board of CCHL was supportive of the conclusion which was reached in the negotiations. The report was made by the Chairman of CCFL who is also a director of CCHL. No decision was required by CCHL on the matter.

16. CCFL and Jade Stadium Limited (JSL) are separate companies in a legal sense but are in transition towards a full merger in due course. In the meantime the two companies are beginning to operate as one entity, they have mirror boards of directors and the CEO of JSL has now been appointed as the CEO of CCFL as well. However, some issues are being transferred on a progressive basis and as the issue of renegotiating the contract with NCC was commenced before this partial merger was undertaken, a subcommittee of the CCFL board took responsibility for the contract negotiation issues advised by Council staff. It is probable that these transitional arrangements contributed to overlooking the need to obtain prior approval of the Council.

**Ratification of the Share Purchase**

17. CCFL have entered into a contract with NCC (Bangkok) to purchase their 50% shareholding in NCC (NZ) Ltd. This contract was for settlement on 31 August 2005 and payment for the shares was made that day. It is therefore unrealistic for CCC to contemplate an attempt to revoke that contractual arrangement.

18. It is acknowledged that the Council's approval should have been obtained first and if the board of CCFL and the staff of CCC had realised that this was a requirement at the time, it would certainly have been sought first. However, that did not happen and the situation needs to be remedied.

19. The CCFL Board is thoroughly satisfied that acquisition of the shares is in the best interest of CCFL and CCC. This will enable the CCFL board to more actively influence the direction of the management company and obtain a better understanding of the business drivers. The management fees and profits made by the management company will now be shared with CCFL instead of going entirely outside the group.

20. In order to complete this contract, NCC (Bangkok) made it a requirement that the amount paid be kept confidential and therefore CCFL is unable to make that figure public. It was necessary for CCFL to agree to maintain confidentiality of the amount. The detail is provided in the 'public excluded' report to Council on a confidential basis. However, it can be noted that the returns forecast from this investment will provide a commercial payback for the investment.

21. Retrospective approval of the Council is now being sought in order that the earlier omission is rectified.

**Comment on the failure to obtain prior approval**

22. The failure to meet the requirement of the Statement of Intent to obtain prior approval of the Council is the result of an oversight. It was not the deliberate intention of any party to try and avoid any obligation to the Council. The oversight was only realised when an enquiry was received by staff from a Councillor and immediate action was initiated to recognise the omission and report to the next Council meeting.

23. It would appear that some confusion arose because of the transitional state of the company's management as it was an issue commenced before merger with JSL and was being handled by the board and its advisers with no expectation that the new CEO become involved.

24. Transactions involving the acquisition of shares are a rare occurrence amongst the subsidiary companies and although it should have been checked out in any event, the fact remains that it was overlooked because of lack of prior experience.

25. The Council was informed by email of the purchase prior to the completion of the issue being publicly announced and before it was realised that there was an obligation to obtain approval. This illustrates a willingness to keep the Council informed.

26. The process which resulted in the acquisition of shares commenced as the renegotiation of a contract which was within the terms of reference for the CCFL board. Although it finally evolved to become the acquisition of shares and so required approval of the Council, in essence to the company, it was a realignment of an existing structure within the CCFL framework. After all, the only purpose of NCC (NZ) Ltd is to operate a management contract over the assets of CCFL. The achievement of a significant ownership of NCC, which had control of the business operations of CCFL, was a means of bringing the CCFL business closer to the company for the benefit of the company and its shareholders.

27. Following a request by a Councillor, the CEO of the Council has asked the Office of the Auditor General (OAG) to advise whether there is a "potential breach of audit guidelines". There has been insufficient time to receive a response to that enquiry prior to finalising this report for Council. However, it is hoped that at least an oral response may be obtained before the Council meeting on Thursday. An initial reaction from the OAG is that there are no specific audit guidelines to follow in this process. However they will endeavour to advise on what they require as auditors to rectify the omission.

**Conclusion**

28. This is a disappointing failure to follow through on a Council requirement for approval. However, the most important thing to remember in all of this is that the outcome from the share purchase is for the good of CCFL and the Council and will have this effect in the short term.