



Statement of Expectations - Bay of Plenty Regional Council

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Tēnā koe Sir Rob

Statement of Expectations for 2022 to 2025

Summary of Key Expectations

This Statement of Expectations (SoE) sets out the Bay of Plenty Regional Council's (Council) priorities and expectations to inform the development of Quayside Holdings Limited's (Quayside) draft Statement of Intent (SOI) for the year ended 30 June 2023.

I express our appreciation and thanks for the contribution of Quayside to this process. Council acknowledges the success and ongoing contribution of Quayside and looks forward to working together. For ease of reading the key expectations are presented below and overall themes thereafter.

1. Primary function of Quayside

As a CCO of the Regional Council, Quayside's primary function is being an investment entity and is principally charged with maximising sustainable returns, once Council has decided with its community, through its adopted Long Term Plan and Financial Strategy, how to balance and consider intergenerational equity and affordability issues.

In this regard, we understand that Quayside are currently discussing and working towards preparing information on "sustainable distribution". The Council expects Quayside to be cognisant of the Long Term Plan 2021 - 2031 commitments when discussing any future model. It also expects that actual financial performance is a strongly weighted factor in any finally agreed methodology.

As considered in the Council's Financial Framework Review, Council acknowledges that its distribution expectation will have an impact on, and lead to, trade-offs with other important financial objectives of Quayside. Quayside is expected to manage the effects of these trade-offs over the longer term, through setting appropriate strategies and policies to manage those trade-offs within the broad range of financial levers available to Quayside and Council.

2. Socially Responsible Investing (SRI) and Environmental, Social, and Corporate Governance (ESG) Principles

The Regional Council expects Quayside to continue to champion SRI and ESG principles, including demonstrating best practice in its approach to complying with mandated climate-related disclosures. This commitment should be reflected in Quayside's SOI and Statement of Investment Policy and Objectives (SIPO). The principles of a CCO are set out in Section 59 of the Local Government Act - to exhibit a sense of social and environmental responsibility by having regard to the interests of the community in which it operates.

This also supports the approach to achieving Regional Benefit, discussed later in this Statement.

3. Port Equity and Ownership

The equity held by Quayside in the Port of Tauranga is a Strategic Asset, as defined by Section 5 of the Local Government Act 2002. Any proposed transfer or sale of such assets requires Regional Council approval, and community consultation through the *Special Consultative Procedure* set out in Section 93 of the Act.

Overall themes

This SoE has been informed by the Financial Framework that was adopted through the Long Term Plan 2021-31 (LTP) process, as well as a workshop run with Councillors in November 2021 as part of the Annual Plan 2022/23 process. The work on the Council's financial framework and analysis to support the Annual Plan 2022/23 has been shared with Quayside through several interactive engagements and those discussions have also informed the development of this SoE.

The Annual Plan 2022/23 is being prepared at a time of significant uncertainty. In addition to the current issues and risks related to COVID-19 and the Local Government reforms (e.g. Resource Management Reforms and Future for Local Government Review), there are also significant changes in the financial environment. These include the economic impact of COVID-19, strong inflationary pressures, a rising interest rate environment, growing pressures on housing affordability, and ongoing supply chain disruption. Some of these impacts were anticipated and reflected in the LTP forecasts, however others were unexpected, and will need to be addressed through the Annual Plan 2022/23.

Further, long-term pressures continue to influence Council's underlying operating and cost environment. This includes protecting and improving the environment, responding to climate change, addressing strong growth in parts of the region, lifting social and economic outcomes, and responding to changes in community and central government expectations.

In this context, Council has carefully considered the key funding and balance sheet levers available, which it can use to achieve the best possible outcomes for the community and the region. The distributions received by Council from Quayside are a vital component of these levers, enabling Council to fund and deliver its Community Outcomes now and into the future. Council supports the development of a formulaic distribution policy and would like to remain involved in the design and implementation of this policy.

This SoE is not intended to be a comprehensive list of expectations but rather guidance and direction to Quayside on key matters where Council's expectations may have further developed compared to those reflected in the previous SoE and Quayside's current SOL.

Strategic Direction

Quayside has described the endowment model as reflecting the protection and growth of a portfolio of assets that will provide a continuous income over time. Council endorses that endowment model approach.

Overall Relationship with Quayside

Quayside is an expert investor and manager of financial assets and has strong commercial expertise. Council enjoys and values a strong and transparent relationship with Quayside. Council expects Quayside to continue to improve Council's visibility of the overall group financial position and issues.

Long Term Plan 2021 - 2031

The following is a list of relevant assets that Council needs to retain, if it is to maintain its capacity to achieve or promote any outcome that it determines to be important to the current or future wellbeing of the community. Assets that Council considers to be strategic assets are:

- Council's shareholding in Quayside
- Council's shareholding in POTL which is held through Quayside

Port of Tauranga

Council treats the shareholding in the Port of Tauranga (POTL) as both a strategic asset and endowment asset. Council acknowledges that this shareholding represents over 80% of the Quayside asset base, and that there may be benefits from diversifying investment. However, to reflect the strategic importance of POTL, Quayside must as a minimum maintain a majority shareholding in the POTL.

If Quayside was to seek to reduce its shareholding in the POTL, Council approval would be required, and consultation with the community. Council expects that engagement would be sought at the earliest opportunity. Council's expectation is that if approval were to be given it would be provided within a set of defined parameters.

Historically, Quayside has been able to retain a portion of dividends to invest in growing its Non-Port Assets. While Council acknowledges that the process of distribution and use of the POTL ordinary dividends is best managed by Quayside, it expects that the ordinary dividends will be used to pay distributions to Council and to the Perpetual Preference shareholders.

Council expects Quayside will seek Council guidance on how any special dividends (or other unexpected returns) from the POTL are used. These options include a mix of special dividends to Council, and retention by Quayside for investment.

Regional benefit, SRI and ESG Principles

Council expects Quayside to continue to champion socially responsible investing, including demonstrating best practice in its approach to complying with mandated climate-related disclosures. This commitment should be reflected in Quayside's SOI and Statement of Investment Policy and Objectives (SIPO).

In developing its SIPO, Council would like Quayside to investigate the new *Crown mandate* within its Responsible Investment Framework for the Super Fund, National Providence Fund and ACC to reduce carbon dioxide emissions from their portfolios in the coming decades. Please note that at this stage, Council only seek that Quayside investigate this mandate to reduce carbon dioxide emissions from the portfolio, and determine through the SIPO process what change and impact it may have.

As part of this commitment, Council expects Quayside to consider regional benefits and socially responsible investing principles (amongst other things) when evaluating its investment options in relation to Non-Port Assets. Where Quayside sees an opportunity for an investment that may not meet its investment mandate and could adversely impact the value of future distributions, but is likely to deliver material regional benefits, Council encourages Quayside to present a business case to demonstrate wider community benefits and an updated long term financial forecast for consideration. Council defines regional benefits as helping to deliver on our Community Outcomes.

Council considers that the strongest regional benefits will flow over the term of the LTP from a sustained and increased Quayside distribution, supporting Council's planned spending on and investment in our Community Outcomes. As such, Council expects that while regional benefit should be a focus of Quayside (where practical and viable), it is not the primary consideration to delivering the distribution expectation to Council.

Partnership with Māori

Māori make up almost a third of the region's population and Council is working to significantly enhance how we work with Māori.

Council expects that Quayside will actively consider investments that provide well-being benefits for Māori and constructively engage with any Māori groups that have an interest in Quayside investment projects: including, but not limited to, Māori input on Quayside resource consents and the use of Mātauranga. Quayside may request Council staff to assist with this.

Council distribution expectations

The Financial Framework Review set the guiding principles for Council's requirement to balance revenue streams, including rates revenue and Quayside distributions. This has been incorporated into the LTP Financial Strategy and is reflected in this SoE. Council has a general expectation that Quayside will continue to support strong regional benefits through sustainably increasing Quayside's distribution to Council.

Ratepayer affordability and intergenerational equity is a key consideration for Council through the drafting of the Annual Plan 2022/23, as this is a requirement on Council from the LGA, with financial pressures increasing the cost of planned investment, and COVID-19 continuing to affect ratepayers. In the Draft Annual Plan 2022/23, Council will be required to continue to use its general reserves as well as other financial levers and run an operating budget deficit. Quayside's distributions are a key financial lever available that will enable Council to deliver its planned spending and investment in Community Outcomes, without compromising ratepayer affordability.

Interim distribution expectations beyond 2021/22 were agreed with Quayside as part of the LTP, which were intended to act as placeholders until a distribution policy was agreed and implemented. As mentioned, Council expects that this policy will have a mechanism that recognises Quayside's actual financial performance as well as its forecast performance.

Considering Quayside's and POTL strong financial performance in FY21 and the identified ratepayer affordability constraints it is anticipated that Council can justifiably anticipate that any adopted policy, incorporating the Council's desire to recognise actual performance, would lead to an increased adjustment to dividend levels from 2022/23 onwards. Council also expects that distributions will continue to grow over the remainder of the LTP period.

As considered in the Council's Financial Framework Review, Council acknowledges that its distribution expectation will have an impact on, and lead to, trade-offs with other important financial objectives of Quayside including:

- the growth in Non-Port Assets;
- the diversification of income away from the current reliance on the POTL dividend;
- the growth in the overall net asset value of Quayside;
- the ability to pursue new projects of regional benefit; and
- the need to manage liquidity and the consequential influence on investment decisions.

Quayside is expected to manage the effects of these trade-offs over the longer term, through setting appropriate strategies and policies to manage those trade-offs within the broad range of financial levers available to Quayside and Council.

Quayside's ongoing advice in relation to the distribution policy and trade-offs of different expectations is sought and valued by Council.

Working with Quayside

In determining its 2022/23 SOI, Council would like Quayside's expert advice on the matters that it considers relevant to the operation of Quayside but in particular:

1. The appropriate rate of investment return it would target for the Non-Port Asset portfolio, considering current and forecast market conditions, and the liquidity necessary to support Council's expectation for distributions.
2. The level of financial resilience that needs to be held in reserves between Council and Quayside and appropriate investment/liquidity, to allow for unpredictable major events that could drive large one-off expenditure needs or materially reduce income (such as events affecting the dividend stream from the POTL).
3. Appropriate strategies to ensure that the value of Quayside is protected for the region and whether there are any potential risks/opportunities arising from local government reforms/reviews.
4. The appropriate target growth rate for the Non-Port Assets portfolio to protect the long-term purchasing power per capita of the fund, reflecting the current and forecast market conditions, the

fact that the Non-Port Asset portfolio is a mid-life endowment fund, and Council's expectation that POTL dividends are paid to Council and PPS shareholders.

To support the above, Council expects Quayside to continue to work with Council staff to improve visibility and a co-ordinated approach to cash-flow management, investment, borrowing, tax, and commercial matters. This would include a long term (e.g. 10 year) forecast of key financial information and risks, and be timed to keep Council informed around major financial decisions for Quayside, such as the use of POTL special dividends, or taking on additional debt.

In addition, Council wishes to meet, at least half yearly, with the Quayside Board, and where appropriate POTL representatives, to facilitate a strong understanding of the relevant operating environments and circumstances of each entity in keeping with publicly available information.

Perpetual Preference Shares (PPS)

The Council expects Quayside to actively engage with Council on the strategy regarding the PPS investment in the future.

Rangiuru Business Park and Tauriko Estate

Council has identified the development of Rangiuru Business Park as a regional benefit asset that is strategically important to the region. Council supports Quayside progressing this investment and has budgeted to provide Quayside with on-lending to support the development.

Council also has an interest in the Tauriko land, which Quayside currently holds on behalf of the Council. The expectation is that Quayside will continue to hold the land for future strategic benefit and or Council initiatives, noting that divestment of this land must only occur with the agreement of Council. Council will continue to work with Quayside on the strategy for this investment.

Council accepts that these assets may not generate the same level of return for Quayside, which may affect Quayside's ability to meet its other investment targets. Accordingly, Council is comfortable with regional benefit assets being specifically identified and reported separately to the main portfolio. The expectation is that a bespoke set of performance objectives will be agreed for each Regional Benefit Asset, which Quayside will be monitored against. Different ownership options for these assets may also be considered where there is a strong case for Council to own the asset.

Toi Moana Fund

Notwithstanding that the Toi Moana Trust (TMT) is a separate CCO, Council recognises that this is a significant fund that Quayside manages on our behalf.

Current interest rate settings mean that there is unlikely to be a material financial advantage from pre-funding capital expenditure through debt and holding it in reserves. However, Council has identified the Toi Moana Trust as a viable alternative for investing accumulated reserves. This is reflected in Council's draft Treasury Strategy 2022/23, which recommends an additional \$20 million of reserve funds are invested in the Toi Moana Fund.

Council expects Quayside to continue managing the Toi Moana Fund in a prudent manner, reflecting Council's level of risk appetite and performance objectives included in the Toi Moana Trust's SOI.

Council recognises that as the size of the fund grows Quayside may wish to consider the best and most efficient vehicle and structure for the TMT. Council expects that Quayside will work with council staff to bring forward options in the development of a TMT Statement of Intent for 2022/23.

Finally, Council again acknowledges the success and ongoing contribution of Quayside and looks forward to working together to reflect the expectations in this SoE in developing Quayside's 2022/23 SOI.

Nā to rourou, nā tāku rourou, ka ora ai te iwi. With your contribution and mine, the people will prosper.
Ngā mihi nui



Doug Leeder

Chairman

Toi Moana Bay of Plenty Regional Council