SUPPLEMENTARY AGENDA

Ordinary Council meeting

Monday, 9 December 2024

Date:	**Monday, 9 December 2024**
Time:	**9.30am**
Location:	**Bay of Plenty Regional Council Chambers Regional House 1 Elizabeth Street Tauranga**

Please note that this meeting will be livestreamed and the recording will be publicly available on Tauranga City Council's website: www.tauranga.govt.nz.

Marty Grenfell

Chief Executive

Order of Business

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11.15 2025/26 Annual Plan Key Financial Update, Draft Capital Programme and LGFA Bespoke Borrowing Covenant Option 4

11 BUSINESS

11.15 2025/26 Annual Plan Key Financial Update, Draft Capital Programme and LGFA Bespoke Borrowing Covenant Option

File Number: **A17048563**

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PURPOSE OF THE REPORT

1. The purpose of this report is to provide an update of Key Financials, a draft capital programme and consideration of the option of a bespoke covenant from Local Government Funding Agency (LGFA) to provide council with debt capacity and debt headroom to achieve the capital investment programme.

RECOMMENDATIONS

That the Council:

(a) Receives the report "Annual Plan Key Financial Update, Draft Capital Programme and LGFA Bespoke Borrowing Covenant Option".

(b) Directs staff to develop the draft 2025/26 Annual Plan for consideration in February 2025 with options to ensure that:

(i) The total rates increase does not overall exceed $12.5% net of growth.

(ii) Depreciation is fully funded except for roading depreciation, where the funded depreciation should reflect only the TCC share of renewals.

(iii) Operational costs proposed to be loan funded are separately reported for specific council approval.

(iv) The capital programme as prioritised in Attachment 1 forms the basis for the draft budget subject to any changes to projects or levels of service agreed by Council prior to adoption for consultation in March 2025.

(c) Agrees that Council should apply to LGFA for a bespoke covenant up to a limit of 350% debt to revenue ratio from June 2025, with a draft application to be considered by Council at its meeting on 9 February 2025.

(d) Approve the ordering of city operations plant budgeted at $2.03m in 2025/26 to enable delivery within Council of four further areas of work currently undertaken under contract from 2025/26.

EXECUTIVE SUMMARY

2. This report provides key financial information based on initial budgeting from activity managers, and a first draft prioritised capital programme for 2025/26 totalling $515m. The revised key financials and capital programme reflect changes from the LTP due to:

(a) Funding Te Manawataki o Te Papa (TMoTP) through LGFA borrowing rather than off Council's balance sheet under Infrastructure Funding and Financing (IFF) arrangements.

(b) Significant downward revision of NZTA capital subsidy funding leading to deferral of some transport projects and a loss of capital revenue from the early years of the LTP.

3. Operational cost changes are underpinned by debt, interest and depreciation that reflect the revised capital programme and asset revaluation.

4. Revenue requirements, primarily rates, have been increased from the LTP to reflect the decision to fund all depreciation, except the portion of transport depreciation that is covered by NZTA funding of renewals. This has been a result of moving toward a balanced budget for 2025/26.

5. There are a number of other costs categorised as “operational” which are budgeted as loan funded because they provide benefit to ratepayers over a number of years. In consideration of draft budget proposals in February, Council will specifically address whether these expenditure items should be loan funded.

6. To date there has not been a reset of other operating costs to reflect the changes to the capital programme. There has been a cost neutral adjustment to operating costs to bring in house three further maintenance contracts. Other operating cost changes from this reset are expected to be included in draft budget figures in February/March 2025. As a result, the first cut rates requirement is a higher increase than the 12.5% increase (net of growth and after IFF levy) for 2026 included in the LTP.

BACKGROUND

7. Following the reforecasting of capital budgets for 2024/25 by Council on 29 October 2024, a further report was presented to Council on 12 November 2024 outlining an approach and suggested capital project categorisation for the 2025/26 Annual Plan. Subsequently a Council workshop has been held on 4 December to consider the prioritised capital programme, key financials and borrowing covenants.

Key financials Based on $515m Capital Programme

8. The draft Annual Plan for 2025/26 updates the budget provided for year 2 of the LTP. The Annual Plan process to date has focussed on capital prioritisation to bring the capital programme within borrowing limits after two significant changes to assumptions in the LTP as follows:

   (a) Council decision to fund Te Manawataki o Te Papa (TMOTP) through LGFA borrowing rather than off Council’s balance sheet under Infrastructure Funding and Financing (IFF) arrangements.

   (b) Significant downward revision of NZTA capital subsidy funding leading to deferral of Cameron Road Stage 2 and a loss of revenue.

9. Based on a draft capital programme of $515m the following key financials have been modelled for 2025-26.

Key Financial Metric	**2024/25 LTP $m**	**2025/26 (Year 2) LTP $m**	**2025/26 Annual Plan $m**
Total Rates $m	333	373 Increases to 375 including IFF levy	Target maximum 375
Rates Increase % after growth and adjusting for IFF debt retained in-council *($3.3m is 1% rates increase)*	15.9%	12.5%	Target maximum 12.5%
Funded Depreciation $m	72	82	113
Unfunded depreciation $m ($21m is NZTA share of transport depreciation)	32	34	21
Net savings required to remain within 12.5% rates limit after growth			**25**
Capital and operational projects of a capital nature $m	510	544	515
Capital Subsidies $m	119	161	81
Net Debt $m	1,450	1,639	1,666
Debt to Revenue Ratio per Financial Strategy *excluding IFF & Tauriko West "grants" as revenue*	277%	272%	296%
Debt to Revenue ratio per LGFA calculation *including IFF & Tauriko West "grants" as revenue*	234%	223%	255%

10. At this first iteration of financials, the modelled rates increase for 2025/26 is significantly above the limit set in the LTP. This is primarily due to the higher depreciation costs and proposal to fully fund all depreciation except the NZTA share (51%) of renewals.

11. Further work is required to find operational savings to offset these increases and limit the rates increase to 12.5% (after growth & IFF levy adjustment) or less. Other operating cost changes from this reset are expected to be included in draft budget figures in February/March 2025. The 12.5% increase is identified as a target maximum.

12. There has been a cost neutral adjustment to operating costs to bring in-house four areas of work that were previously contracted out. As part of bringing this work into City Operations, Council needs to purchase a range of plant (vehicles, mowers, tractors, etc). Previously Council has purchased all plant. However, given current borrowing constraints, the intention is to purchase smaller bespoke plant that would not be readily leased, and lease the larger plant such as vehicles. A total budget to purchase all of the plant is $6,4m. This has been reduced in the draft Annual Plan to $800k opex p.a. for lease costs (still within the net neutral requirement) and $2.03m capex. To have plant available to commence work on the 1 July, Council needs to place orders prior to Christmas. This paper seeks approval to order, but not incur costs of purchase or lease until the 2025/26 financial year.

Balanced Budget

13. Council has indicated a balanced budget requirement where operational revenue is sufficient to cover operational costs. In the Statement of Comprehensive Revenue and Expense, Tauranga City Council (TCC) reports revenue for day-to-day operations under a subtotal called Total Operating Revenue, which is separated from Total revenue which includes all other revenue which TCC categorises as Asset Development Revenue. This is an indicative rather than absolute classification. For example, development contribution revenue covers both annual interest and principal repayment on growth debt. Also challenging a balanced budget calculation are various transactions to fund asset development not owned by TCC which are recorded and operating expenditure and revenue.

14. A report to the Accountability Performance and Finance Committee on 8 October 2024 - Report 9.1 Accounting and Funding Operational Expenditure and Implications for Balanced Budget - outlined the reasons for loan funding certain expenditure items where there was a longer-term benefit, so that future ratepayers should also cover a share of the costs. For example, development contribution revenue covers repayment of both interest and capital for growth projects.

15. The following table outlines the areas where operating revenue has not been sufficient to cover expenditure leading to a deficit before asset development revenue. Where expenditure is proposed to be covered by loans, debt is retired over the expected number of years that expenditure is expected to provide benefit. All occasions where operating expenditure is proposed to be loan funded or unfunded would be brought to Council for approval as part of the Annual Plan process.

Item	Rates-funded	Should not be rate-funded	Other net loan-funded	Justification
Unfunded depreciation				Now funded
Depreciation - Transport				Assume 51% subsidy from NZTA for renewals
Tauriko West - timing of expenditure and funding				Capex spend, funded in an unusual way
Waters CCO establishment costs				Costs would be transferred to CCO as part of Waters debt should this option be chosen
Capitalised interest costs (DCs and Te Tumu)				Growth pays for growth. Capital revenue funds repayment of principle and capitalised interest
Grants for delivery of capital				Payments made to third parties for delivery of community assets not owned by Council
Net reserve movements				For 2025/26 these are net favourable
Digital SaaS net of repayments				Capital in nature with benefit of investment over time
City development costs net of repayments				Costs only incurred in support of the City Centre capex programme
Cash activity surplus/deficits				Net position of user fee funded activities
New growth areas planning, net of repayments				Initial planning costs for future capital-intensive development areas

16. The indicative 2026 model produces the following calculation.

	2026 $m	
Operating deficit per Annual Plan	**(68)**	
Items that do not require funding in 2026:		
Tauriko West Funding Transactions (net - timing)	1	
Waters CCO establishment costs loan funded	7	If Council chooses to create a Waters CCO establishment costs would be transferred as part of waters debt
Depreciation cost related to NZTA funding of renewals	21	51% NZTA subsidy
Capitalised interest costs (DCs and te Tumu)	26	DC revenue (capital revenue) of $35m budgeted in year
Adjustment to operating deficit	**55**	
Residual loan funding items:	**(13)**	
Digital SaaS net loan funded	5	
City Development net loan funded	7	
New growth areas planning net loan funded	0	Offset almost in full by debt retirement
Grants for delivery of capital net loan funded	2	Assets not owned by Council
Cash activity (surplus)/deficits	(2)	User fees to be considered in February
Other net reserve movements including opex loans repaid	1	Balance of revenue collected to fund reserves over reserves used to fund activities e.g. Kerbside, Waste Levy, Biosolid reserve. Plus debt retirement for opex loans from previous years.
	0	

Prioritised capital Programme

17. The capital programme has been prioritised for 2025/26 to **$515m** in the light of revised borrowing capacity and decisions of Council. This follows on from the reforecast reduced budget for 2024/25. The draft capital budget for 2025/26 is set out in **Attachment 1.**

18. In proposing a draft budget for 2025/26, consideration has been given to the deliverability of a programme of work beyond the 2025/26 year within borrowing limits. Under a bespoke covenant most of the current LTP programme of work could be delivered (based on assumed subsidies being confirmed in later years for projects such as Cameron Road Stage 2 and TMOTP). It is recognised that large programmes of work could be better phased across the next ten from the current timing, which would avoid exceeding the 320% limit in early years. Phasing should also reflect cost effective resourcing arrangements over time to deliver the programme. Further work on projects to be phased will be considered as part of future work to inform the annual plan for 2026/27 (year three of the LTP) as well as the 2027-37 Long-term Plan.

Borrowing Limits and LGFA Bespoke Covenants

19. TCC along with other growth councils has taken on significant amounts of debt over the last 20 years primarily to meet infrastructure requirements for growth. Government has worked with LGFA to look at ways to better enable councils to continue to invest by providing greater borrowing capacity. A proposed mechanism to improve capacity is bespoke borrowing covenants set by the LGFA Board for growth councils. Bespoke covenants can be set to a maximum limit of 350% debt to revenue, noting that Councils would be expected to maintain adequate debt headroom within this limit.

20. Borrowing from LGFA offers relatively low-cost debt, and for most councils the most competitive interest rates and reliable borrowing that Councils could access. The LGFA, as a large institution with a strong credit rating, can also provide strong credit certainty to councils.

21. Under standard LGFA borrowing limits, if Council's debt to revenue ratio exceeds 280% it would be required to repay all LGFA debt and would not be eligible for further LGFA borrowing. The LGFA covenants calculate revenue generously, including all capital revenues as well as IFF and Tauriko West revenues.

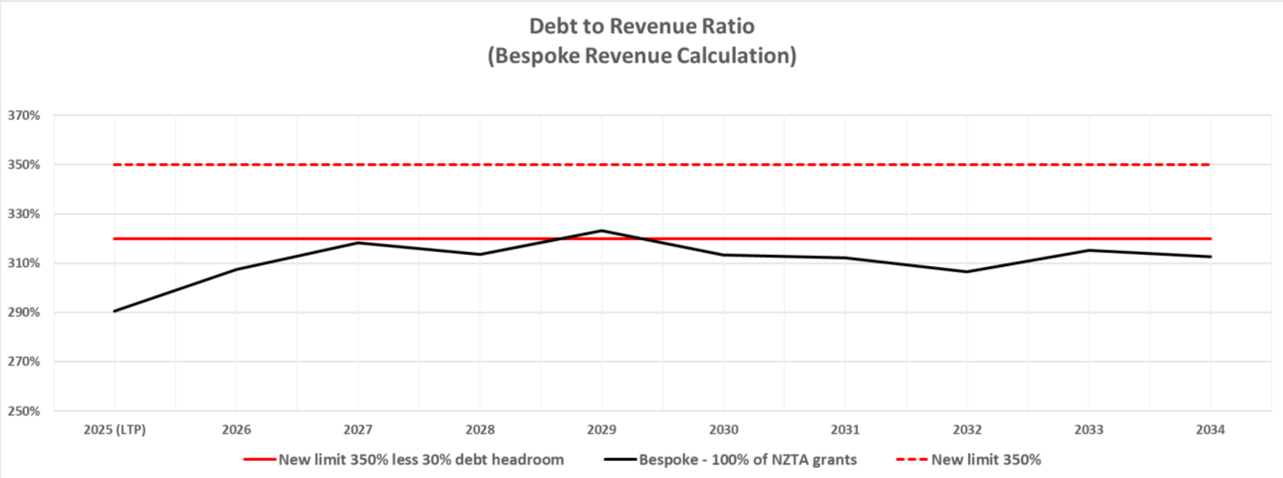
22. Even with these revenue sources included, Council is forecast to exceed borrowing limits in the next few years. This is because since the LTP two significant assumptions have changed the debt position of council relative to the capital expenditure planned in the LTP. These are that borrowing for TMoTP has remained on council balance sheet ($151.5m) and NZTA subsidies for transportation projects has been significantly reduced. From 2027/28 the project-specific Tauriko West and IFF payments to TCC would not continue, reducing calculated revenue and producing a sudden increase in the debt to revenue ratio.

23. In response to the above changes since the LTP, Council has reprioritised the timing of the capital programme for 2024/25 and 2025/26. However, even with this prioritisation an annual capital spend averaging $520m ongoing, would result in the current LGFA borrowing limits being exceeded in the next few years as shown in the graphs in **Attachment 2 – Graph 2**.

24. Under a bespoke LGFA covenant, and the assumed calculation methodology, Council could largely remain within a 320% internal borrowing limit, well within the LGFA 350% limit, and therefore providing sufficient debt headroom for Council to respond to unforeseen events.

25. The Bespoke Covenant graph below (also included in **Attachment 2 – Graph 3)** shows the debt to revenue ratio as it would be expected under a bespoke covenant, noting that the 2029 result is likely to be avoided through phasing of the capital programme as would occur in the next LTP process.

26. **Graph 1: Debt to Revenue Ratio Under a Bespoke Covenant**



27. An alternative to a bespoke covenant would be to reduce the capital programme each year from an average of $520m per annum to an average of $450m. This would enable council to remain within standard debt to revenue ratio limits with LGFA. It also could reduce rates revenue requirements by reducing interest rates and depreciation, reducing the increase in rates by 1% to that assumed in the key financials for 2025/26. A further 1-2% reduction in a later year would be expected depending on timing and amount of depreciation removed with the reduction in projects. The results of a $450m capital programme on debt to revenue are shown in **Attachment 2 - Graph 4**.

STATUTORY CONTEXT

28. The development of draft budgets and consideration of limits on borrowing and rates form part of the requirements of the Annual Plan process under the Local Government Act 2002.

STRATEGIC ALIGNMENT

29. This contributes to the promotion or achievement of the following strategic community outcome(s):

	Contributes
We are an inclusive city	✓
We value, protect and enhance the environment	✓
We are a well-planned city	✓
We can move around our city easily	✓
We are a city that supports business and education	✓

30. The Annual Plan updates LTP budgets which have been set to work towards strategic community outcomes.

OPTIONS ANALYSIS

31. Council has options regarding the direction to staff to prepare an application for a bespoke covenant to LGFA and the decision whether or not to approve the ordering of City Operations plant required for 2025/26 before finalisation of the 2025/26 Annual Plan. These options are discussed below.

32. Decision 1: direct staff

	Advantages	Disadvantages
Option 1 Approve application for a bespoke borrowing covenant	• Council can achieve the infrastructure required for the city more quickly with benefits therefore flowing more quickly from these investments • Council has prudent headroom to respond to unforeseen events • Council can continue to borrow from LGFA which has advantages for borrowing costs and reliability relative to direct council borrowing	• Higher borrowing will increase costs to ratepayers from interest and depreciation associated with the higher capital programme (estimate 8% increase once depreciation commences (delayed impact)
Option 2: do not approve a bespoke covenant application and instead reduce the capital programme further to remain within existing borrowing limits.	• Operating costs flowing from capital investment will be reduced with lower debt and less investment in new assets, primarily from interest and depreciation (estimate 8% of capital expenditure over time, noting the delayed impact of depreciation).	• Infrastructure and community investment will be deferred resulting in a worsening of the deficit of Housing supply required under the NPS on Housing supply, with flow on impacts to housing and rental costs to people living in Tauranga. • Other non-growth capital will be deferred with potential impacts on traffic congestion,

		safety, travel times, loss of economic and wellbeing benefits of community expenditure. • Potential loss of subsidy if transport or other subsidised projects are deferred. • Potential breach of consent conditions • Potential higher maintenance or operational costs to deliver agreed level of service if further investment in some assets is deferred • Loss of reputation with other parties from not undertaking projects or taking advantage of an option to enable required investment • No available headroom to respond to unforeseen events • Requirement to repay loans to LGFA if limits are breached and need to refinance elsewhere at higher costs.

Option of approving or not approving ordering of plant to support additional in-housed city operations in 2025/26

Option	Advantages	Disadvantages
Option 1 Agree to ordering plant for in-housing further contracts	City Operations will be resourced to undertake these new contracts from the beginning of 2025/26 when the contract with external providers ceases	A commitment is made to purchase plant ahead of final annual plan adoption.
Option 2 Do not agree to ordering plant for in-housing further contracts	No commitment is made prior to 2025/26 Annual Plan commencing	City Operations will not be resourced to undertake these new contracts from the beginning of 2025/26 when the contract with external providers ceases and transitional arrangements will be needed at additional cost.

FINANCIAL CONSIDERATIONS

33. Financial considerations form the basis of this report and are discussed in the sections above.

LEGAL IMPLICATIONS / RISKS

34. There are no direct implications arising from consideration of priorities and borrowing covenants.

CONSULTATION / ENGAGEMENT

35. This report forms part of the Annual Plan process under which a consultation document will be prepared and consulted on in March/April 2025.

SIGNIFICANCE

36. The Local Government Act 2002 requires an assessment of the significance of matters, issues, proposals and decisions in this report against Council's Significance and Engagement Policy. Council acknowledges that in some instances a matter, issue, proposal or decision may have a high degree of importance to individuals, groups, or agencies affected by the report.

37. In making this assessment, consideration has been given to the likely impact, and likely consequences for:

    (a) the current and future social, economic, environmental, or cultural well-being of the district or region

    (b) any persons who are likely to be particularly affected by, or interested in, the decision.

    (c) the capacity of the local authority to perform its role, and the financial and other costs of doing so.

38. In accordance with the considerations above, criteria and thresholds in the policy, it is considered that the decision is of high significance.

ENGAGEMENT

39. Taking into consideration the above assessment, that the decision is of high significance, officers are of the opinion that consultation will be undertaken on the Annual Plan for 2025/26 in accordance with the requirements of the Local Government Act 2002.

NEXT STEPS

40. Staff are undertaking an organisational reset in response to the change in focus from the LTP and will identify savings in expenditure to remain within the 12.5% rates increase limit.

41. Draft Annual Plan budgets will be prepared for consideration by Council in February 2025.

ATTACHMENTS

1. **Draft 2026 Annual Plan Capital Budgets - Detailed - A17251072** ⇩
2. **Debt to revenue ratio charts - A17251177** ⇩

Draft 2026 Annual Plan Capital Budgets - Detailed

Outcome Group	Client Key	Name	FY25 Budget	FY26 Budget	FY27 Budget	FY28 Budget	FY29 Budget	FY30 Budget	FY31 Budget	FY32 Budget	FY33 Budget	FY34 Budget
Transport	**N.000029.18**	PEI Phase 3 Transport	30,765,320	27,631,405	10,892,904	0	0	0	0	0	0	0
	N.000109.01	TSP009 - Tauriko West - Northern Access	19,387,145	21,071,189	23,296,618	0	0	0	0	0	0	0
	N.000109.04	TSP009 Intersection Kaweroa Dr & SH29	34,831,939	18,091,871	2,936,945	0	0	0	0	0	0	0
	N.000109.02	TSP009 Cambridge Rd Intersection Upgrade	10,481,312	17,520,753	21,918,547	0	0	0	0	0	0	0
	N.000008.17	TSP028 Bus facility imp Tga Crossing	1,289,037	16,028,966	5,680,824	5,816,898	634,150	0	0	0	0	0
	N.000001.02	TSP007 Turret Rd 15th Ave multimodal imp	2,623,341	13,728,254	37,822,213	57,571,004	18,539,698	8,553,938	0	0	0	0
	N.000089.29	TSP009 Intersection Kaweroa Dr & SH29	0	11,660,493	2,935,638	0	0	0	0	0	0	0
	N.000045.09	Road resurfacing WC212	7,380,889	9,000,000	9,732,750	9,970,250	11,019,949	11,666,445	10,629,227	10,874,037	11,241,357	11,686,870
	N.000046.47	Arterial Route Review and Implementation	800,000	6,614,107	2,463,260	840,754	0	0	0	0	0	0
	N.000045.03	Pavement Rehabilitation WC214	6,247,806	6,500,000	8,196,000	10,667,170	11,020,842	11,559,838	11,507,722	11,820,778	12,082,347	12,420,145
	N.000109.03	TSP043 - Whiore Avenue Upgrade	358,774	4,077,510	906,726	0	0	0	0	0	0	0
	N.000045.01	Pre Seal Repairs WC111	3,300,001	3,500,000	3,893,100	5,716,964	5,852,059	6,189,092	5,573,507	6,046,901	6,497,620	6,676,589
	N.000009.20	TSP032 City Centre Transport Hub	3,250,000	2,535,055	507,136	3,364,271	1,382,627	2,497,214	0	0	0	0
	N.000069.02	Streetlight WC222 Renewal	2,225,250	2,398,500	2,463,260	2,410,162	2,463,334	2,512,610	2,557,760	2,598,785	2,637,748	2,698,254
	N.000024.06	The Boulevard - Stevenson Drive to Sands Intersection	500,635	2,360,128	0	0	0	0	0	0	0	0
	N.000008.13	Wairakei Town Centre bus facility	0	2,188,749	513,037	0	0	0	0	0	0	0
	N.000024.14	Sands Avenue - The Boulevard to Te Okuroa Dr	2,200,000	2,175,395	0	0	0	0	0	0	0	0
	N.000091.01	TSP009 WC Ring Rd section within TBE (SH29 to Matakokiri Dr)	1,500,000	1,848,105	0	0	0	0	0	0	0	0
	N.000045.13	Otumoetai Railbridge Footpath Renewal	683,483	1,603,867	722,961	1,043,796	0	0	0	0	0	0
	N.000089.32	Kaweroa Dr - Taurikura/SH29 (DC funded)	1,500,000	1,500,000	0	0	0	0	0	0	0	0
	N.000009.02	Cameron Road Stage1	2,000,000	1,202,699	0	0	0	0	0	0	0	0
	IBIS:238858	Miro Street parking enhancements	0	1,200,000	0	0	0	0	0	0	0	0
	N.000029.21	The Boulevard - Between Sands Ave and Te Tumu	207,000	1,068,641	2,276,657	311,640	0	0	0	0	0	0
	N.000075.04	New Transportation Model	1,283,400	1,066,000	848,456	896,804	916,589	934,925	951,725	966,990	981,488	1,004,001
	N.000029.05	TSP013 - Te Okuroa Dr - Sands Ave to Te Tumu (Stages H and I)	5,820,736	977,704	0	0	0	0	1,630,725	0	0	0
	N.000045.04	Kerb, Channel & Sump WC231 Renewal	1,400,000	882,903	947,877	879,544	900,817	953,690	974,382	1,101,485	1,226,386	1,253,441
	N.000018.15	Chapel Street Esplanade Walkway/Cycleway	0	800,000	0	0	0	0	0	0	0	0
	N.000103.01	TSP029 - Belk Road Futureproofing	600,000	782,422	0	0	0	0	4,227,771	9,969,660	0	0
	IBIS:238863	Ngatai Rd/Bureta Rd intersection safety improvements	0	660,000	1,797,420	0	0	0	0	0	0	0
	IBIS:238857	Farm Street placemaking and accesibility improvements	0	600,000	723,100	0	0	0	0	0	0	0
	IBIS:238860	Girven Road pedestrian crossing upgrade	0	597,000	0	0	0	0	0	0	0	0
	N.000029.20	Intersection - Between Sands Ave and The Boulevard	648,333	577,589	0	0	0	0	0	0	0	0
	N.000045.08	Footpath Renewals WC225	536,402	550,000	1,613,895	1,653,277	1,692,345	1,757,090	1,795,212	1,834,594	1,863,737	1,904,853
	N.000089.38	Construction of Belk Rd RAB	500,000	503,581	0	0	0	0	0	0	0	0
	N.000012.14	City Centre Transportation Development	0	500,000	4,974,588	8,603,692	0	0	0	30,066,830	20,461,336	18,472,293