

Proactive Release

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Listed below are the most commonly used grounds from the OIA.

<u>Section</u>	<u>Description of ground</u>
6(a)	as release would be likely to prejudice the security or defence of New Zealand or the international relations of the New Zealand Government
6(b)	as release would be likely to prejudice the entrusting of information to the Government of New Zealand on a basis of confidence by <ul style="list-style-type: none">(i) the Government of any other country or any agency of such a Government; or(ii) any international organisation
6(c)	prejudice the maintenance of the law, including the prevention, investigation, and detection of offences, and the right to a fair trial
9(2)(a)	to protect the privacy of natural persons
9(2)(b)(ii)	to protect information where the making available of the information would be likely unreasonably to prejudice the commercial position of the person who supplied or who is the subject of the information
9(2)(ba)(i)	to protect information which is subject to an obligation of confidence or which any person has been or could be compelled to provide under the authority of any enactment, where the making available of the information would be likely to prejudice the supply of similar information, or information from the same source, and it is in the public
9(2)(ba)(ii)	to protect information which is subject to an obligation of confidence or which any person has been or could be compelled to provide under the authority of any enactment, where the making available of the information would be likely otherwise to damage the public interest
9(2)(f)(ii)	to maintain the constitutional conventions for the time being which protect collective and individual ministerial responsibility
9(2)(f)(iv)	to maintain the constitutional conventions for the time being which protect the confidentiality of advice tendered by Ministers of the Crown and officials
9(2)(g)(i)	to maintain the effective conduct of public affairs through the free and frank expression of opinions by or between or to Ministers of the Crown or members of an organisation or officers and employees of any public service agency or organisation in the course of their duty
9(2)(h)	to maintain legal professional privilege
9(2)(i)	to enable a Minister of the Crown or any public service agency or organisation holding the information to carry out, without prejudice or disadvantage, commercial activities
9(2)(j)	to enable a Minister of the Crown or any public service agency or organisation holding the information to carry on, without prejudice or disadvantage, negotiations (including commercial and industrial negotiations)

Auckland Light Rail

Affordability analysis (Volume 2)

17 May 2023

Draft for discussion

Purpose and scope

Purpose

The purpose of this report is to outline the approach and methodology for assessing organisational affordability in the context of the Auckland Light Rail project (ALR or “the Project”), including establishing the ‘baseline’ financial environment for each of the key organisations, identifying the potential impacts of overlaying different cost and funding assumptions, and identifying potential financial levers (funding and balance sheet) to assist with managing affordability.



The report is intended to be an interim deliverable, used to inform the preferred funding and financing solutions, and associated sources and settings.

Scope of this report

This report is the second report in the affordability series, and should be read in conjunction with the Affordability Analysis (Volume 1) report which focuses on beneficiary affordability. This specific report covers affordability considerations associated with key stakeholders organisations to the project. These include:



Organisational affordability

- Auckland Council (**focus**)
- Waka Kotahi / NLTF
- the Crown
- Kāinga Ora

This report builds upon the Detailed Funding Report prepared as part of the supporting advice for the 2021 Indicative Business Case (IBC). Where possible, the underlying assumptions have been updated to reflect the current Project and organisational context. However, as per the Funding Sources and Settings report, key inputs from the technical workstreams (costings, patronage, growth/development, benefits) weren’t available during the drafting of this report. The IBC assumptions have been used as placeholders where assumptions were unavailable.

This report is intended to be read alongside the **Affordability Analysis (Volume 1) report** (dated 9 May) and **Funding Sources and Settings report** (dated 3 May 2023).

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1. Executive summary

Summary of organisational capacity

Organisational capacity has been assessed for the key funding agencies likely to be involved in ALR, including assessing the current capacity under financial constraints and identifying potential levers to increase this.

Organisations assessed	Introduction, context and constraints	Measures	Potential capacity to fund capital expenditure	Potential capacity to fund operating expenditure	Levers tested
Auckland Council	<ul style="list-style-type: none"> Overview of sources of funding. Development of financial 'baseline'. Overview of financial conditions (e.g. inflation impacts, revenue highlights). Overview of constraints (legal, financial and political). 	<ul style="list-style-type: none"> Debt-to-revenue 270% long-term target. Debt-to-revenue 290% internal debt ceiling. Balanced budget requirement. % of depreciation funded. 	Limited Primary constraint is the operating impact of the debt (i.e. higher borrowing costs), rather than capacity under debt limits. Reducing borrowing costs is a core part of the Council's current financial strategy.	Limited Operating budget pressures are acute, with the Council considering (~\$295m budget 'shortfall' contained in its Consultation Document). Asset sales, cuts to operating expenditure and a ~4.7% rates increase being considered.	Balance sheet lever <ul style="list-style-type: none"> Asset sales (AIAL, land holdings). Increase borrowing. Funding lever <ul style="list-style-type: none"> Increase rates. RFT/Congestion Charge. Development Contribution. Reprioritise funding.
Waka Kotahi / NLTF		<ul style="list-style-type: none"> 'PAYGO' - revenue compared to expenditure. GPS activity class range. 	Recommendation from the Revenue Review was that the NLTF should not contribute capital funding to 'mega projects'. Acute financial pressures, with the Fund unable to fund its Continuous Programmes and debt repayments by FY28 without changes to its revenue settings		Balance sheet lever <ul style="list-style-type: none"> Increase borrowing. Funding lever <ul style="list-style-type: none"> Increase FED/RUC. Alternative revenue streams. Reprioritise funding.
The Crown	<ul style="list-style-type: none"> Overview of appropriations. Overview of 'baseline'. Overview of constraints. 	<ul style="list-style-type: none"> Net Crown debt-to-GDP (30% debt ceiling). OBEGAL to GDP. 	Capacity under debt ceiling, however, competing investment priorities.	NLTF funding assumed for Crown contribution to operations.	Balance sheet lever <ul style="list-style-type: none"> Increase borrowing. Funding lever <ul style="list-style-type: none"> Additional GST revenue. Reprioritise funding.
Kāinga Ora	<ul style="list-style-type: none"> Given the focus of this Report is on the potential capacity of organisations to fund the transport component of ALR, Kāinga Ora's capacity has not been assessed. This analysis will be undertaken once the scope and roles for the urban development strategy have been determined. 				

Auckland Council: Affordability assessment 1 of 2

Auckland Council has capacity under its internal borrowing limits, however, the associated interest costs would exacerbate the already acute operating funding challenges. Capacity is also required for CRL cost overruns, flood recovery and other investment.

Form of funding	Capex contribution	Potential under current baseline	No	Potential with funding levers	Yes
Financial conditions / capacity					
Auckland Council's debt-to-revenue ratio is currently ~250% ¹ , which is below the 270% long-term target and 290% debt ceiling. This implies the Council has ~\$1-2bn of debt capacity under its internal borrowing constraints (excluding the impacts of Water Reform), noting that a portion of this is required for CRL, flood recovery and other investment. The operational impact of higher debt levels (i.e. funding the associated interest payments) is currently a larger constraint (than internal debt limits) on increasing borrowings, with the Council facing significant operating funding challenges through its 2024 Annual Plan. A key part of the Council's strategy to reduce its ~\$295m operating budget deficit ² is to apply proceeds from the sale of its Airport shares to reduce annual interest payments (~\$87m annual interest saving ³). The annual interest costs required to service a \$1-2bn debt-funded Council contribution (i.e. consuming the existing capacity) would be \$45-\$95m , which is equivalent to \$75-\$155 per rating unit (2.5-4.5% of the 2022/23 average rates invoice) .					
Balance sheet levers					
Asset sales: Council has a large asset base that could be applied to support a funding contribution, either through an 'in-kind' contribution or the proceeds of a divestment. Key opportunities are AIAL (\$1,887m to \$2,330m), land holdings such as golf courses (\$2,900m+). Borrowing: As above, the Council has \$1-2bn of headroom under its internal debt constraints, which could be used to finance the Council's contribution. However, this would ultimately have to be funded through other sources (rates, development contributions) and would have a significant operational impact.					
Wider policy considerations					
				<ul style="list-style-type: none"> Maintaining headroom for other investment: Cost overruns for City Rail Link (~\$526m additional cost) and flood recovery (\$900m to \$1,200m) will require the Council to raise substantial borrowings over the next couple of years. As such, the current headroom is not fully readily available for use to finance ALR. Increasing debt levels (breaching LGFA covenant): Auckland Council's internal debt ceiling is aligned to the LGFA financial covenants (290% for FY24), and therefore, any increase above the debt ceiling would result in a covenant breach. The LGFA can exclude councils from the LGFA and require them to repay outstanding borrowings for non-compliance. While the Council has the capacity to access debt capital markets directly (i.e. domestic and foreign DCM issuance comprises ~69% of its total borrowings), there would be an additional cost associated with raising the debt to repay the \$3,597m of LGFA borrowings. From an LGFA, and therefore, wider local government sector perspective, there would be a direct impact of the Council leaving the LGFA. Increasing debt levels (lower credit rating): Auckland Council currently scores a '5' for its Debt Burden, which is the lowest score. Accordingly, the credit rating risk is a qualitative notching downgrade from having an "excessively high debt burden", rather than a mechanical reduction from lower financial ratios. The key issues associated with a credit rating downgrade are: <ul style="list-style-type: none"> triggers a repayment of EUR denominated borrowings under the terms of the bonds higher borrowing costs (10-15 basis points), which on an \$11.8bn debt programme is equivalent to \$10-15m p.a. or \$15-\$25 per rating unit. borrowing costs would likely increase for the LGFA/other councils. 	

Auckland Council: Affordability assessment 2 of 2

Auckland Council is currently using a number of financial levers to manage its ~\$295m operating deficit, which is likely to constrain its ability to make a substantial contribution to the operating expenditure of ALR, especially the depreciation expense associated with asset ownership.

Form of funding	Opex contribution	Potential under current baseline	No	Potential with funding levers	Yes
Financial conditions / capacity					
<p>Auckland Council's capacity to contribute funding for operating expenditure is directly related to its ability to increase rates (i.e. ratepayer affordability). High levels of housing expenditure are currently constraining ratepayer capacity, which is outlined in the supporting Volume 1: Beneficiary Affordability Report.</p> <p>The Council's operating position has deteriorated since the IBC, with high inflation and interest rates placing significant pressure on the Council. The focus of the Consultation Document for the next Annual Plan is significantly reducing the operating deficit. Increased costs are being partially offset through increasing rates (4.7%) and public transport fares (6.5%), with cost reduction being achieved through high efficiency targets, reducing service levels and decreasing community grants and other funding.</p> <p>While the Council is compliant with the Balanced Budget requirement, it has committed to fully funding depreciation by 2028, which is exacerbating operating funding pressures. Deferring the internal targets would have implications on the Council's credit rating, which was noted during the preparation of the 2021-31 LTP.</p>					
Funding levers					
<p>General rates increase: Increasing general rates by an additional 2.0% in FY24 would result in an additional \$1,556m of funding over the period between FY24 and FY50.</p> <p>Regional fuel tax: The current RFT is set to end in 2028, extending this to 2050 and including a 2c increase in FY24 could provide additional funding of \$1,721m.</p> <p>Reprioritising expenditure: Total intended operating expenditure reduction detailed in the FY24 Consultation Document amounts to \$125m p.a. This has been considered as a proxy for the possible magnitude of an operational funding contribution.</p>					
Wider policy considerations					
<ul style="list-style-type: none"> Funding the depreciation associated with ALR: If Auckland Council became the asset owner for the ALR assets, it would be required to fund the depreciation expense. Assuming a total replacement cost of \$15b and a weighted average asset life of 50 years, the annual depreciation expense would be ~\$300m p.a., which equates to ~\$500 p.a. per rating unit. The impact of funding depreciation for CRL, where the Council's asset ownership is likely to be approximately a third (or less) of ALR is clear from the 2022/23 Annual Plan (depreciation funding percentage falls by 5% between FY25 and FY26 as a result of CRL). Increase in charges: Ratepayer capacity is likely to be constrained for many households in the current environment, as a result of the significant increase in housing related expenditure over the past 18 months (higher mortgage costs, inflation, etc.). Accordingly, the ability to increase rates to fund the operating expenditure and depreciation associated with ALR is likely to be challenging. Especially when overlaying a possible IFF (or other property charge) levy. Reducing/reprioritising expenditure: As evident from the Council's Consultation Document and recent headlines in relation to staffing reductions highlight the extent to which the Council is in the process of making significant reductions to operating expenditure. An additional requirement to reduce/reprioritise operating expenditure is unlikely to be feasible, without serious adverse impacts on service levels and the social license for the Project. Balancing rates increases with other sources: As outlined in the Funding Sources and Settings report, while there is an opportunity for the Council to raise other revenues to reduce the impact on ratepayers (congestion charge, RFT, etc.), there are social equity and access issues that would need to be worked through. 					

Waka Kotahi: Affordability assessment 1 of 2

The Land Transport Revenue Review and Rapid Transit Funding & Financing Papers have highlighted the extent of the NLTF's funding constraints and recommended that alternative sources of Crown funding are used for 'mega projects', rather than the NLTF

Form of funding	Capex contribution	Potential under current baseline	No	Potential with funding levers	Yes
Financial conditions / capacity					
<ul style="list-style-type: none"> Recommendations from the LTRR and Rapid Transit Funding & Financing Paper have suggested that alternative Crown sources are used for to fund capital expenditure associated with 'mega' projects. One of the key drivers of those recommendations is that the Fund's long-term revenue and expenditure profile highlight the scale of the funding challenge for the NLTF to simply continue funding its Continuous Programmes, debt repayments and Emission Reduction Initiatives. While not set up to be a 'borrowing entity' (i.e. PAYGO principle), the NLTF has had to use debt to manage its cash flows over the past couple of years, largely as a result of Covid. In its most recent quarterly report, Waka Kotahi noted that if the NLTF continued to draw on its \$2bn Crown facility it would consume its remaining capacity. 					
Balance sheet levers					
<p>The following balance sheet levers have been considered:</p> <p>Borrowing: Establishing a borrowing programme against the Fund's long-term revenues was considered at the IBC stage and has been the focus of subsequent reviews. However, this option was not progressed.</p> <p>Crown appropriations/MoT: A regular Crown appropriation (via the Ministry of Transport's appropriation pathway) could be used to enable the NLTF to contribute further funding and/or support a borrowing programme. However, this is likely to be less efficient than a direct Crown appropriation to the Project.</p>					
Wider policy considerations					
<p>The NLTF is not expected to provide a capital contribution to ALR. However, potential considerations regarding any potential capex contribution include:</p> <ul style="list-style-type: none"> Increased borrowing: The NLTF has recently taken on a borrowing facility, given lower-than-forecast NLTF revenue. The impact of any additional NLTF borrowing would need to be considered in terms of debt serviceability, as well as the NLTF's borrowing measures and risk management. Capacity under debt measures: The NLTF manages and reports against three debt measures and currently has headroom under all three. This additional capacity could support additional borrowing to provide a capital funding contribution. Crown appropriation: In the case of a Crown appropriation, consideration would need to be given to external fiscal measures such as the Crown's financial metrics (e.g. net debt-to-GDP) when considering the quantum of a potential appropriation. While financial support from the Crown would help to ease some short-term funding pressures, this support would not address ongoing funding requirements. Precedent setting: As discussed in this Report, NLTF revenue, under current settings, will be insufficient to meet the NLTF's ongoing work programmes. Any level of funding that the NLTF contributes to ALR, either as a direct contribution or via a Crown appropriation (MoT), may set a precedent for funding future rapid transport projects, which would likely be unsustainable for the Fund given such constraints. 					

Waka Kotahi: Affordability assessment 2 of 2

Analysis from the LTRR highlights the pressures for the NLTF to fund ALR. The NLTF is under considerable financial pressure due to reduced revenues and increasing expenditure requirements. Consistent with guidance from the Minister, the analysis on the NLTF and FED/RUC changes has been kept to a high level.

Form of funding	Opex contribution	Potential under current baseline	No	Potential with funding levers	TBC - depends on size
Financial conditions / capacity			Wider policy considerations		
<ul style="list-style-type: none"> Post COVID-19 impacts and the Government's Cost of Living Package continue to impact NLTF revenue, which is ~\$300m below budget for the first half of the 2023 financial year. Modelling from the LTRR indicates that the NLTF revenue, under current settings, will not be sufficient to fund its continuous programmes and debt commitments. The modelling indicates that FED would need to increase ~11.2 Cpl. p.a. over 2025-2034 to fund its Emission Reduction Initiatives and maintain the same level of capital investment in transport across New Zealand. When overlaying the potential contributions with LGWM, WHC, etc. the implied funding gap increases further. Without significant changes to the NLTF's revenue settings and/or scope (i.e. reducing its scope to be a maintenance/renewal fund) the Fund is unlikely to have capacity make an operating funding contribution. 			<ul style="list-style-type: none"> GPS-LT/NLTP constraints: NLTF spend must be applied within the activity class bands outlined in the GPS-LT; ALR operations would need to fit within these definitions to be eligible for funding. Geographic equity: While not a legal/policy requirement, the equitability of different levels of investment across the country should be considered. NLTF Funding Capacity: Funding pressures will increase over time if FED/RUC is not anchored to movements in underlying cost indices. Increasing investment requirements, e.g. to enable 'mode shift', will place further strain on the Fund, unless there is a shift to a long-term, sustainable revenue setting, or the scope of the Fund is reduced. Scope for EVs: Extending the scope of RUCs to include EVs would reduce the incentive for private vehicle users to switch from ICE to EV. However, the revenue impact of continuing the exemption for EVs would materially impact NLTF revenue. FED/RUC charges: Higher FED/RUC charges need to be considered alongside other funding sources that target motor vehicle users e.g. congestion charging and RFT. Customer affordability considerations need to be managed in relation to future FED, RUC and MVR increases (as these charges are typically regressive in nature, they can directly impact equitable access). Increasing investment need: Investment in public transport will have a critical role in supporting the transition to a lower carbon transport network and supporting growth/urban development aspirations. This is likely to translate into sustained increases in demand for NLTF funding, which will exacerbate funding pressures. Cost inflation: FED/RUC are not annually adjusted to reflect cost indices, which means there will inherently be a decline in affordability over time. 		

Crown: Affordability assessment

The size and scale of the Project means that Crown support in some form is likely to be required. There are a number of options for structuring Crown support for ALR, the preferred approach will depend on a number of factors, including the Crown funding requirement and form of the Delivery Entity.

Form of funding	Capex contribution	Potential under current baseline	Yes	Potential with funding levers	Yes
Financial implications					
<ul style="list-style-type: none"> The Crown currently has significant headroom under its 30% (of GDP) net debt ceiling, which could be used to provide capital funding for the Project through a Crown appropriation. The impact of using a Crown apportion to fund the Project on Debt to GDP is 0.8% to 2.1% (35% contribution through to a 100% contribution), which would still leave headroom significant headroom under the debt ceiling. However, the impact would be magnified if a similar funding arrangement was used for the other 'mega' projects. While there is headroom under the debt ceiling, like with Auckland Council, the additional finance costs associated with any new borrowings flows through to the operating balance. The current Government is working towards a return to an operating surplus and signalled an expectation for reduced spending. 					
Associated funding levers					
<p>The following levers could be used to provide upfront capital funding:</p> <p>Borrowing: Potential Crown appropriation ranging from 35% to 100% of the estimated proportion of costs would have an impact on net debt-to-GDP ranging from 0.8%-2.1% over the 10 years to 2033/34. The OBEGAL-to-GDP ratio would only be marginally affected by increased interest costs. The total impact on OBEGAL-to-GDP would range from -0.2% to -0.5% over the 10-year period to 2033/34.</p> <p>Increase in GST revenue: The Project will deliver significant additional GST revenue that is not included in the current baseline (e.g. Construction related GST of ~\$1,905m, \$25-30m of GST revenue per annum based on the assumed IFF levy settings under the Modified Status Quo funding scenario.)</p> <p>Reallocation of funding: The potential funding magnitude is uncertain. The extent of funding is dependent on the extent of possible reallocations.</p>					
Wider policy considerations					
<ul style="list-style-type: none"> Fiscal metrics: Crown finances, such as debt levels and operating balance, must be managed when considering the quantum of Crown appropriations. Opportunity cost: A capex contribution from the Crown to ALR would need to be considered/balanced against other core Government priorities and the funding/investment needs of other such priorities. Reallocation of funding: Any capex contribution arising from the reallocation of existing Crown funding could (adversely) affect the level of service of other areas provided to the public, which would impact the Project's ability to achieve social license. Precedent setting: Providing a Crown appropriation for ALR may set a precedent for funding other major infrastructure projects regarding the proportion of a project's capex that is provided by the Crown. There is an associated 'layering' impact (i.e. capex contribution to a number of projects) of significant Crown appropriations to the Crown's finances. 					
Crown operating expenditure contribution					
<p>This report has not considered the impact of a Crown operating contribution, given the NLTf is expected to fund the Crown's portion. A contribution would directly impact OBEGAL and the Crown's Operating Balance.</p>					

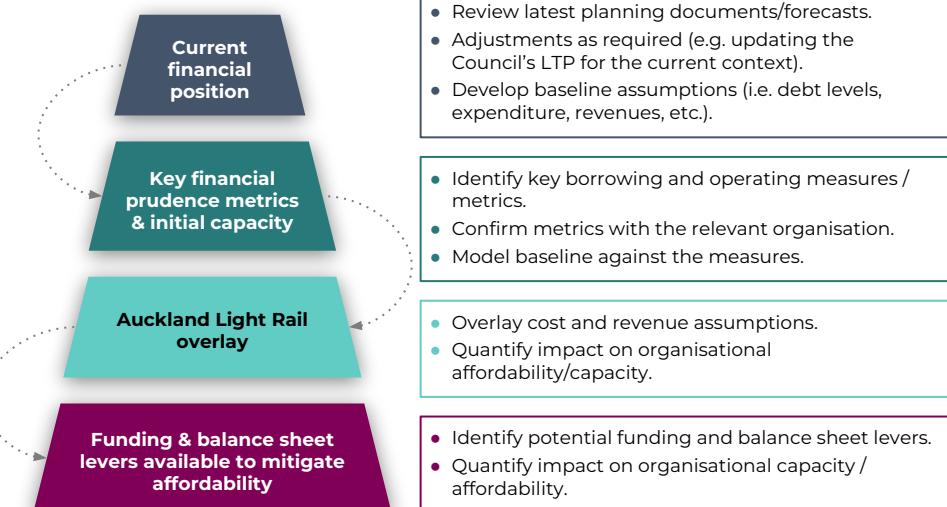
2. Introduction and approach

Scope and approach

Organisational affordability considers the capacity of the different organisations that could provide funding for the Project.

As each organisation has its own set of financial prudence metrics, a separate framework was required to assess each one. Unlike Volume 1: Beneficiary Affordability, the affordability caps operate more like 'hard caps', given the potential impact of a breach is more severe (e.g. a credit rating downgrade, breach of a financial covenant, etc.)

We have used the following approach to assess affordability for the relevant organisations:



Scope of the report

This report outlines the proposed framework for assessing affordability, which has been developed to address the issues outlined in the Sponsoring Minister's guidance.

This report covers the following:



The analysis in this report focuses on the affordability of the ALR **transport** solution, given the uncertainty over the costs associated with the urban interventions and funding contributions for other investment (e.g. Waitematā Connections (WHC)).

3. Volume 2: Organisational capacity

Overview and general principles

Organisations considered in this Report

The organisational capacity/affordability has been considered for the following organisations, with the associated measures and levers reflecting the relevant prudential/financial framework and characteristics of the organisation.

The following organisations have been identified as having potential capacity to fund/finance the ALR Project for the following reasons:

Auckland Council (Page. 15-26)

As the representative for Auckland ratepayers and constitutes that will be the primary beneficiaries of the Project. We have not considered Auckland Transport separately, given Auckland Council is the primary funder of Auckland Transport and the financial impacts consolidate up to the Council.

Waka Kotahi/National Land Transport Fund (Page. 27-32)

As the manager of the NLTF/NLTP, Waka Kotahi's organisational capacity has been considered in this Report. The focus of the analysis is on the capacity of the NLTF. Commensurate with the IMS Letter from the Minister, this analysis is relatively 'light touch', given other work currently underway/recently completed (e.g. Land Transport Revenue Review).

Crown (Page. 33-38)

Due to the size of the ALR project, Crown support through funding and financing arrangements is likely to be required. The wider economic benefits of the Project can justify Crown support, as was seen with the CRL project.

Kāinga Ora

Affordability to Kāinga Ora has not been considered in this report, as the role of Kāinga Ora is still being defined and costs for urban development are currently unknown, but will be considered once this is confirmed.

Structure of the section

An individual sub-section has been drafted for each of the organisations and aims to be somewhat standalone, with cross-referencing back to the relevant sections/reports. Each sub-section follows the below structure:

Introduction, context and constraints	Measures	Levers tested
Auckland Council Financial, legislative and political constraints	<ul style="list-style-type: none">Debt-to-revenue 270% long-term target.Debt-to-revenue 290% Internal debt ceiling.Balanced budget requirement.% of depreciation funded.	Balance sheet lever <ul style="list-style-type: none">Asset sales (AIAL, land holdings).Increase borrowing. Funding lever <ul style="list-style-type: none">Increase rates.RFT/Congestion Charge.Development Contribution.Reprioritise funding.
Waka Kotahi NLTF funding and revenue stream constraints	<ul style="list-style-type: none">'PAYGO' - revenue compared to expenditure.GPS activity class range.	Balance sheet lever <ul style="list-style-type: none">Increase borrowing. Funding lever <ul style="list-style-type: none">Increase FED/RUC.Alternative revenue streams.Reprioritise funding.
Crown Fiscal measures, appropriation quantum and precedent setting constraints	<ul style="list-style-type: none">Net Crown debt-to-GDP (30% debt ceiling).OBEGAL to GDP.	Balance sheet lever <ul style="list-style-type: none">Increase borrowing. Funding lever <ul style="list-style-type: none">Additional GST revenue.Reprioritise funding.

3.a. Auckland Council

Introduction to Auckland Council capacity

Auckland Council sources most of its revenue from rates (36%), fees and charges (24%) and subsidies and grants (18%), which includes funding from the NLTF.

Overview

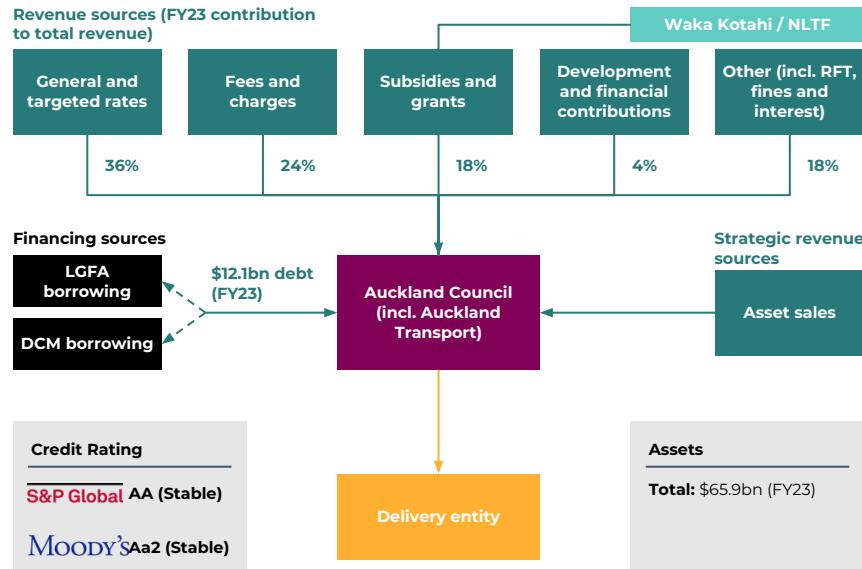
- Auckland Council's sources of funding, outlined in its Revenue and Financing Policy, are limited to those set out under section 103 (2) of the LGA 2002.
- Council funds ~60% of its operating expenditure through general and targeted rates, and fees and charges.
- Capital expenditure is largely financed through borrowing, with costs spread over time and recovered through revenue sources such as rates and development contributions.
- Auckland Council is the only New Zealand council to maintain an international debt capital markets (DCM) borrowing programme.
- Transport investment and services are primarily funded through general rates and fare revenue, as well as the NLTF subsidy (51% FAR).
- Maintains a dual credit rating (S&P AA and Moody's Aa2).

Role in funding ALR

- Represents Auckland's beneficiaries (i.e. ratepayers/developers).
- Funding responsibilities in relation to the Regional Land Transport Plan (RLTP) and Regional Public Transport Plan (RPTP).
- Responsible levy authority for an IFF levy.

General constraints

- **Financial:** Debt-to-revenue ratio to meet LGFA covenants and maintain credit rating.
- **Legislation:** Auckland Council is required under the LGA to ensure it maintains a balanced budget, acts in a prudent manner and acts in the interests of the community and ratepayers
- **Political:** Revenue setting requires regular approval by the Governing Body following engagement with constituents, including annual rates resolutions as part of the annual planning process.



Source: Auckland Council Annual Budget 2022-2023

Introduction and context

Auckland Council is a key stakeholder in the Project, and in the overall funding solution. Current economic conditions and recent events are constraining Council's capacity and levels of affordability.

Introduction and context

Commensurate with Sponsoring Minister guidance, a key driver of the funding and financing solution is the 'beneficiary pays' principle, where the costs of a project are allocated to the beneficiaries.

Critically, the focus for the beneficiary analysis is on the final beneficiary (i.e. ratepayer, transport user, etc.) rather than the organisation. Accordingly, from a beneficiary pays perspective, the Council's funding/financing role is as the representative for Auckland. The indicative beneficiary analysis suggests that ~65% of the benefits will accrue in Auckland, which implies Auckland beneficiaries should provide a substantial funding contribution to the project.

The Council has limited capacity under its Debt-to-Revenue ratio and is not currently fully funding depreciation. The severity of its capacity constraints are highlighted in the 2024 Consultation Document for its next Annual Plan, which outlines the key financial challenges:

- Funding flood recovery investment
- City Rail Link cost overruns
- Rising interest rates
- High inflation (i.e. cost of delivering services)
- Rates affordability.

Financial 'levers' being considered

To manage these impacts, the Council is considering a mix of different levers, including: reducing operating spending, increasing rates (~4.7%, noting an additional 1% increase may be required to fund the Council's flood response), divesting its Airport shares, and repaying debt.

- **Water Services Reform:** Uncertainty around the timing and impacts of Water Reform, however, given the current levels of leverage for the three waters, the expectation is that the Reform will deliver additional borrowing capacity for the Council.

- **Flood response:** The Council is facing significant additional costs as a result of the 2023 Auckland flooding events, including higher insurance premiums, direct costs associated with repairing and replacing Council-owned assets, and increases to operational budgets to better prepare for future storm events.

- **City Rail Link:** CRLL has submitted a formal funding request to its Sponsors, reflecting the revised costs and timelines associated with completing the project.

Economic conditions have further constrained financial capacity:

- **High inflation:** The costs of delivering the same level of service and capital investment have increased significantly over the past 12-18 months, with inflation indices running at multi-decade highs. For example, The Capital Goods Price Index (CGPI) shows a 15.4% annual increase in Civil Construction costs (19.1% for the 'Transport Ways' sub-category).¹

- **Rising interest rates:** The RBNZ has increased the Official Cash Rate (OCR) by 3.75% in the past 12 months, which flows through to higher borrowing costs². The Council's Annual Plan 2023 assumed a finance costs for FY2023 would be 5.6% higher than the LTP assumption for that year³. The impact is likely to be even more pronounced for FY2024.

Water Services Reform debt settlement
~\$3.6bn⁴

Additional flood related expenditure
\$900m to \$1,200m⁵

CRL cost overruns to be funded by the Council:
~\$500m⁶

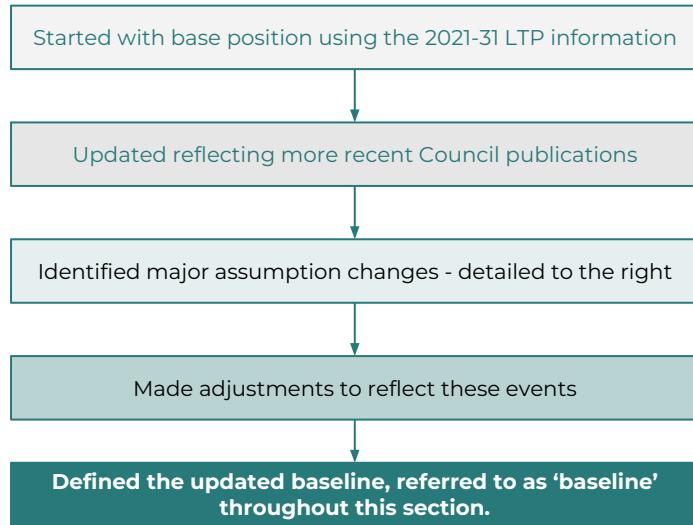
CGPI (Civil)
Dec 2022
15.4%¹

OCR increase
April 2022 - 2023
+3.75%²

Auckland Council: Approach to determine baseline

There have been a number of changes to the financial conditions for Auckland Council, including the response to the major flooding events, City Rail Link cost overruns and developments in relation to the Water Services Reform, which mean that some of the assumptions underpinning the 2021-31 LTP require updating.

The following approach has been used to update the Auckland Council LTP figures, to ensure analysis undertaken reflects key updates and changes in Auckland spend since the LTP's publication.



Adjustment	Quantum	Details
FY31-FY50	na	<ul style="list-style-type: none"> 2.0% in inflation post-LTP
Updated data	na	<ul style="list-style-type: none"> Replaced FY23 forecast with Annual Plan 2022/23* Replaced FY24 forecast with 2023/24 Consultation Document¹
CRL	\$526m ² additional cost	<ul style="list-style-type: none"> 50% in FY25 50% in FY26
Flood and cyclone recovery	\$1,050m ³ additional cost	<ul style="list-style-type: none"> Split: 80% capex, 20% opex 16.7% from FY24 to FY29
Watercare Water Services Reform	\$2,584m ⁴ debt reduction	<ul style="list-style-type: none"> Remove Water Supply and wastewater revenues and expenditure from FY25. Debt settlement payment in FY24.
Stormwater Water Services Reform	\$1,000m ⁵ debt reduction	<ul style="list-style-type: none"> Removed Stormwater from FY25 revenues and expenditure from FY25. Debt settlement payment in FY24.

* Auckland Council debt to revenue ratio includes certain leasing arrangements, which cannot be directly calculated from publicly available information. Accordingly, an adjustment in FY23 was used to align the debt to revenue ratio to what was presented in the Annual Plan 2022/23.

¹ We have modified the movement in debt from the Consultation Document to 'back out' the sale of AIAL shares and repayment of debt (\$1,887m).

² City Rail Link website - <https://www.cityraillink.co.nz/city-rail-link-cost-timeline>.

³ Auckland Council - <https://ourauckland.ckan.aucklandcouncil.govt.nz/news/2023/03/financial-update-city-rail-link-and-storm-impacts/>

^{4,5} The debt settlement figure is based upon Watercare's published reports and a high-level assumption for Stormwater (\$1bn).

Auckland Council: Baseline capacity (operational)

Under the baseline, Auckland Council has limited capacity to contribute funding to the Project. Auckland Council's operating deficit has increased since the IBC, further constraining the capacity of the council to support the funding solution.

Contributions to operational expenditure

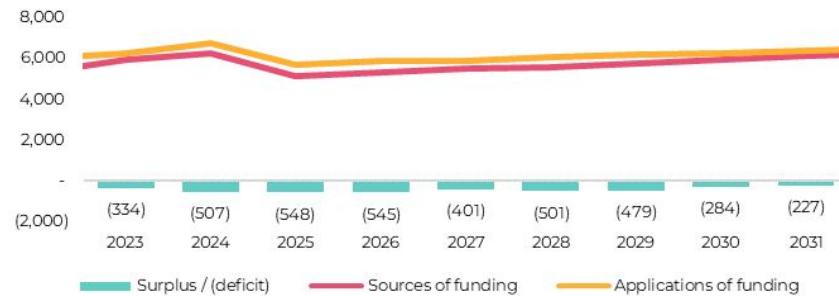
Auckland Council is required to maintain a balanced budget under the LGA (\$100), unless it is deemed financially prudent not to do so. A 'balanced budget' involves setting each year's project operating revenues (rates, subsidies and grants for operating purposes, and fees and charges) at a level sufficient to meet that year's projected operating expenses (payments to staff and suppliers, finance costs and other operating funding applications).

Auckland Council's capacity to contribute funding for operating expenditure is directly related to its ability to increase rates (i.e. ratepayer affordability). The IBC noted that the Council was moving towards fully funding depreciation by 2028 and rebalancing the rating burden between residential and business ratepayers, both of which were exacerbating affordability pressures. Since the IBC, the operational deficit has increased, indicating pressures have become more acute.

The Council is seeking to address these issues as part of its 2024 Annual Plan, which is outlined in its 2024 Consultation Document. The Council is engaging with its community on lowering operating expenditure through repaying debt through proceeds from the divestment of its Airport shares, cutting unnecessary and inefficient expenditure and seeking further operating efficiencies.

Planned operating expenditure for FY24 is ~\$1,180m, which includes ~\$600m on public transport contracts¹. The IBC estimated that the annual operational expenditure on ALR services would be ~\$135m (excluding any depreciation funding), with the Council funding ~\$33m (50% farebox recovery and 51% FAR)² a ~6% increase. Auckland Transport is seeking an additional \$21m of cost reductions³ and planning to increase fares by 6.5% to meet budget pressures, which is likely to further stretch affordability pressures.

Baseline



Note, the current baseline scenario takes account for a series of key expenditure adjustments, listed in Appendix 1, and assumes the application of the 'modified statu quo' funding scenario - ensuring alignment with the beneficiaries affordability analysis completed previously. It excludes the reduction in finance costs associated with the reduction in debt through divesting the Airport shares that the Council is currently consulting on (estimated net impact of \$39 million reduction).

Key observations

- Financial conditions for the Council have deteriorated since the IBC analysis, which has exacerbated funding/financing pressures.
- The Council is having to use its financial 'levers' (e.g. asset sales, rates increases) just to deliver its current investment and services.
- In the absence of using a financial 'lever', the Council is likely to have limited capacity to contribute to the capital costs of the Project.

Auckland Council: Baseline capacity (borrowing)

The Council's key borrowing capacity metric is a debt-to-revenue ratio, which aligns to its credit rating and LGFA borrowing covenants. The Council has more headroom under this metric than assumed in the LTP due to under-delivery of its capital programme (~250% compared to ~270%). However, reducing debt is a key focus for its 2024 Annual Plan to reduce the associated finance costs.

Borrowing capacity

Auckland Council is currently operating near its internal borrowing limits (~250% compared to its debt limit of 290% and 270% long-term target)¹. When overlaying its large capital programme, including the additional costs associated with the flood recovery and CRL, there is limited capacity to contribute to the Project.

As part of its Annual Plan 2024, Council is considering reducing its debt levels through applying proceeds from a sale of its Airport shares. Rather than debt capacity, the decision to reduce debt levels is based on a desire to address operating funding constraints through reducing finance costs (i.e. the repayment of debt is estimated to generate ~\$87m in finance cost savings p.a.)². This highlights that while the debt-to-revenue ratio is one constraint on borrowing, the consequential impact of higher finance costs is currently more of a driver of the Council's decision making.

The Water Services Reform is expected to further reduce the Council's leverage (debt-to-revenue), with the future Water Services Entity making a settlement payment based in the Council's outstanding three waters debt. The analysis in this Report assumes a ~\$3.6bn settlement payment is made in FY24³.

At ~250%, the Council's debt-to-revenue ratio already scores the lowest 'outcome' under the Debt Burden assessment⁴. Accordingly, the key risk of a higher debt-to-revenue ratio is a notching downgrade for "an excessively high debt burden". For illustrative purposes, a debt-to-revenue ratio of 400% has been assessed, which if pursued would result in a credit rating downgrade (refer to page 6 for discussion on the potential implications of a credit rating downgrade).

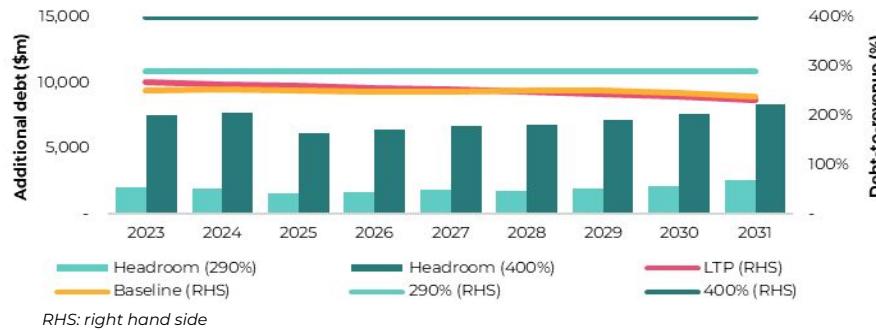


¹ Auckland Council Consultation Document 2024 Budget.

² Auckland Council Consultation Document 2024 Budget.

³ Watercare Annual Reports and high-level assumption for Stormwater.

Baseline (excluding the sale of AIAL shares)



	Baseline FY23	Baseline FY31	Change
Debt-to-revenue ratio	250%	240%	-10%
Headroom 290% ratio	\$2,016m	\$2,600m	+\$584m
Headroom 400% ratio	\$7,561m	\$8,320m	+\$758m

Note, the current baseline scenario takes account for a series of key expenditure adjustments, listed in Appendix 1, and assumes the application of the 'modified status quo' funding scenario - ensuring alignment with the beneficiaries affordability analysis completed previously.

Auckland Council balance sheet levers

The Council has a number of balance sheet levers available, including increasing its borrowing capacity, changing to prudential limits, and asset disposals.

Balance sheet lever	Description	Additional debt capacity	Change from IBC	Considerations and trade-offs
Asset sales	Sale of Auckland Council's 18.1% shareholding of Auckland International Airport (NZSE:AIA).	\$1,887m to \$2,330m ¹	Yes, increase of 23%	<ul style="list-style-type: none"> Implementation requirements (e.g. consultation requirements for strategic assets). Loss of control of asset and outcomes it can derive. Loss of potential future revenue, e.g. dividends. Trade-off of spending the proceeds rather than paying down debt.
	Sale of land holdings within the Corridor (e.g. golf courses).	\$2,900m+ Refer to page 24	na	<ul style="list-style-type: none"> Legislative restrictions (e.g. disposal of reserves, zoning/planning restrictions) RFR and other title/land impediments. Community/political opposition Loss of control of asset, outcomes and future revenue it can derive.
Increase internal debt to revenue limits	Increasing the debt-to-revenue ratio to 270%.	\$1,008m (FY24)	Yes, p.a. increase at FY24 of 10%	<ul style="list-style-type: none"> Risk of a credit rating downgrade, particularly if increasing the debt-to-revenue to 400% (discussion of impacts provided on page 6). Increased annual finance costs (i.e. for every \$100m of borrowings, the annual increase in finance costs is ~\$4.7m p.a.).
	Increasing the debt-to-revenue ratio to 290%.	\$1,910m (FY24)	na	<ul style="list-style-type: none"> LGFA covenant breach, which would require the Council refinanced its LGFA borrowings (\$3,597m outstanding, 28.9% of LGFA guarantee). These impacts would manifest with both the Council and the rest of the local government sector.
	Increasing the debt-to-revenue ratio to 400%.	\$7,693m (FY24)	na	<ul style="list-style-type: none"> Risk of non-compliance with financial prudence obligations in the LGA.

¹ Based on Auckland Council Annual Budget Consultation Document and CapIQ market equity value as at 8 May 2023.

Auckland Council funding levers

Auckland Council has a number of funding levers that could be used to support a capital or operating contribution. The balance sheet impact of the funding/financing structure would need to be considered.

Funding lever	Description	Additional revenue FY24 to FY50	Change from IBC	Considerations and trade-offs
Increase - revenues RFT	Extend RFT beyond FY28, until 2050, and increase by 20%.	\$1,721m (total) \$29.5m to \$7.4m ¹	No p.a. change at FY24	<ul style="list-style-type: none"> Legislative limits on the maximum of any RFT, requiring adjustment, and the associated political appetite required to implement. Long-term transition away from ICE means revenue reduces over time.
Reprioritise expenditure	Reallocation of currently planned expenditure across the Auckland Council portfolio, with funding originally planned for other projects and services now allocated.	\$125m p.a. Total stated target for operating expenditure reduction to achieve a balanced budget, detailed in 2024 budget Consultation Document - considered as a proxy for potential operational contribution to the Project.		<ul style="list-style-type: none"> Current Council policy of reducing operating spend. In parallel with current inflationary pressures this is expected to add to constraints on operating budgets. Reprioritisation or allocation of expenditure has the potential impact of further reducing operating budgets. Potential reduction the level of service of Council services.
Increase revenues - Rates	Increase general rates by an additional 2.0% in FY24.	\$1,556m (total) \$39.4m to \$76.2m	Yes, p.a. increase at FY24 of 2.5%	<p>Specific trade-offs covered through the beneficiary affordability report (8 May 2023) in greater detail.</p> <ul style="list-style-type: none"> Current economic conditions (high inflation and increasing interest rates) leading to reduction in discretionary spend and capacity to spend.
Development Contributions	Imposing a development contribution for Auckland Light Rail investment	Not calculated at this stage		<ul style="list-style-type: none"> Reduces the incentives for developers in the corridor, and the type of developments. Limited to funding the 'growth' component the Council's capital contribution, likely capped based on contribution from other funding sources (i.e. using an IFF levy would materially reduce the ability to impose a development contributions). Requires significant debt capacity.

Regional fuel tax and asset sales

Regional Fuel Tax and Asset sales are two of the four funding ‘levers’ to Auckland Council considered in this illustrative scenario testing.

Regional Fuel Tax

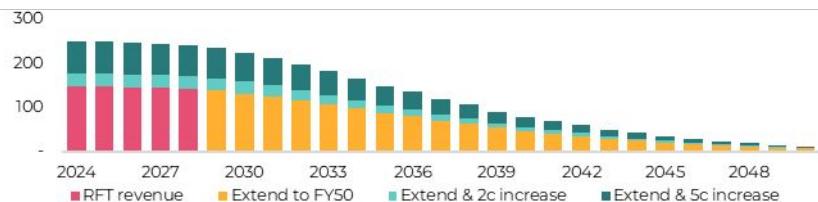
Auckland's RFT is legislated to continue to 2028, and generates approximately \$150m p.a. of funding to a dedicated group of Auckland transport projects.

The analysis below considers extending the RFT term (from FY29 to FY50), and increasing the RFT rate (by 20% and 50% resulting in RFT levies of 12c and 15c). RFT revenues have been adjusted down over time to reflect the Climate Change Commission's (CCC) estimates on Electric Vehicle (EV) uptake.

Increase in RFT	Annual incremental revenue	Total
Extend to FY50 & no change in rate	\$0m (FY24) to \$6.2m (FY50)	\$1,314m
Extend & 2c increase	\$29.5m (FY24) to \$7.4m (FY50)	\$1,721m
Extend & 5c increase	\$73.7m (FY24) to \$9.3m (FY50)	\$2,333m

The CCC estimates that the EV portion of vehicle kilometers travelled in FY24 will be 1.7%, and 95.9% in FY50, hence the decreasing quantum of the annual incremental revenue.

Incremental revenues generated through RFT (\$m)



Asset sales

Auckland Council has a significant asset portfolio, including assets in airport, port, landholdings and housing assets. The recent valuation of Auckland Council's holding is such assets are detailed in the table below.

Asset	Value
Auckland International Airport (AIA)	\$1,887m to \$2,330m ¹
Ports of Auckland	\$1,570m to \$1,910m ²
Parks and reserves	\$2,250m ³
Golf courses	\$2,900m ³
Pensioner housing	\$225m ³

Based upon the sample assets detailed in the table, the full funding opportunity to the Project through asset sales is between **\$8,832m to \$9,615m**.

Although theoretically a substantial funding opportunity to the Project, there are significant limitations regarding the extent of asset sales, where specific governing body approval and possible consultation with communities is required.

Realising value from landholdings

Auckland Council has a number of land holdings within the ALR corridor and across the wider Auckland Region that could potentially support ALR upfront capital requirements.

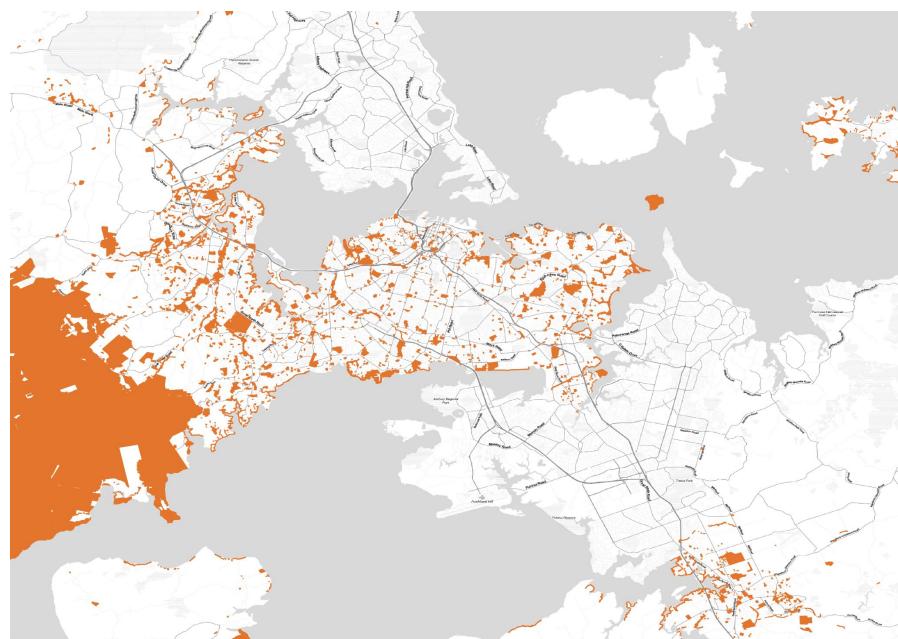
Land holdings

Auckland Council has a number of land holdings within the ALR corridor and across the wider Auckland region, as indicated in the figure to the right.

Based on 2017 land values, Auckland Council has land and capital values of **\$3,998m** and **\$5,266m** respectively.

Land holdings	Within corridor	Total Auckland
Number of holdings	285	4,164
Total area¹ (m²)	1,373m ²	318,772m ²
Land Value	\$647m	\$3,998m
Capital value	\$881m	\$5,266m

Although a significant funding opportunity, land sales need to be considered against other interests, such as maintaining parks, green space and other public realm spaces.



Increasing borrowings and general rates

Auckland Council has limited funding levers at its disposal. Currently has a debt-to revenue ratio of ~250% and the Council is limited in the ways it can increase revenue.

Increasing debt levels (breaching LGFA covenant)

Auckland Council's internal debt ceiling is aligned to the LGFA financial covenants (290% for FY24), and therefore, any increase above the debt ceiling would result in a covenant breach. The LGFA can exclude councils from the LGFA and require them to repay outstanding borrowings for non-compliance. While the Council has the capacity to access debt capital markets directly (i.e. domestic and foreign DCM issuance comprises **~69% of its total borrowings**), there would be an additional cost associated with raising the debt to repay the **\$3,597m of LGFA borrowings**. From an LGFA, and therefore, wider local government sector perspective, there would be a direct impact of the Council leaving the LGFA.

Increasing debt levels (lower credit rating)

Auckland Council currently scores a '5' for its Debt Burden, which is the lowest score. Accordingly, the credit rating risk is a qualitative notching downgrade from having an "excessively high debt burden", rather than a mechanical reduction from lower financial ratios. The key issues associated with a credit rating downgrade are:

- **triggers a repayment** of EUR denominated borrowings under the terms of the bonds
- **higher borrowing costs** (10-15 basis points), which on an \$11.8bn debt programme is equivalent to \$10-15m p.a. or \$15-\$25 per rating unit.
- borrowing costs would likely increase for the LGFA/other councils.

Increasing revenue through general rates

Council is limited in the ways it can increase revenue. These include rates increases and charge increases, e.g. increase to general rates; increases to existing, or introduction of, new targeted rates; and the extension of existing, or introduction of, regional fuel taxes.

Specific details regarding the impact of rate increases to residential landowners is covered in depth in the beneficiary affordability document. As part of this analysis a 1% and 2% increase in general rates has been considered. As reference, the 2021-31 LTP estimates that general rates revenue will be \$2,083m in FY24.

General rates	Annual incremental revenue	Total
Increase of add. 1.0% in FY24	\$19.7m (FY24) to \$38.1m (FY50)	\$778m
Increase of add. 2.0% in FY24	\$39.4m (FY24) to \$76.2m (FY50)	\$1,556m

Significant increases in charges expected from residents within the context of current economic conditions (high inflation and increasing interest rates) is likely to have material impact on affordability of charges to the end payer, e.g. ratepayers or motor vehicle users.

Development contributions and reprioritisation

Reprioritisation of planned expenditure and development contributions are two other funding ‘levers’ for Auckland Council to consider, but the Council may be limited in their ability to use either of them.

Development contributions

Under the LGA, Auckland Council has the capacity to charge development contributions to fund the portion of Council’s capital contribution that can be fairly allocated to growth.

Auckland Council currently has two development contributions in place for City Rail Link, which are summarised in the table below. The split between the two relates to investment already partially delivered and investment that is yet to be incurred.

Development contribution	Capital Expenditure	DC revenue	DC funded proportion
City Rail Link 1 (to be incurred)	\$1,168m	\$269m	23%
City Rail Link 2 (already incurred)	\$1,019m	\$172m*	23%
Total	\$2,187m	\$441m	23%

*excludes DC revenue already collected.

Auckland Council has recently changed its DC Policy to enable the collection of DCs for investment outside of the typical ten year investment horizon. A similar logic could be used to maximise the DC revenue that can be collected.

Further, Council allocated the cost between funding areas based on beneficiary analysis, which enabled it to more effectively target growth (i.e. a smaller funding area is likely to have a higher growth proportion, which supports a higher cost allocation to growth).

However, Council can only charge DCs on capital expenditure that it is legally obligated to fund, and the growth proportion applies to the Council funded proportion, rather than the total proportion. The potential impact on development incentives would also need to be worked through.

Reprioritisation of planned spend

In order to maintain currently forecasted operating expenditure, Auckland Council can reprioritise planned expenditure. As detailed previously, reductions in operational spend and current economic conditions are constraining the capacity of operational budgets across key Council services.

A reallocation of funding from important and key services could possibly lead to the reducing the the level of service provided by Council to the community, residents and ratepayers. As a result, reprioritising funding from other Council services to the Project will require sufficient political support and appetite to do so.

For context, the current Council budget for FY23/24 being publicly consulted on, is proposing operational budget reductions are \$125m, per year. This is equivalent to approximately 5.4% of the NPV of the Project’s opex.

3.b. Waka Kotahi/NLTF

Introduction and context

Waka Kotahi is responsible for managing the National Land Transport Fund (NLTF), which is currently a significant funding contributor for Auckland's public transport network and wider transport system. Under the current revenue settings, Waka Kotahi is unlikely to have capacity to make a substantial funding contribution to the Project.

Overview

Waka Kotahi is responsible for managing the NLTF, which is a hypothecated transport fund that provides funding to enable investment across New Zealand. Waka Kotahi only has control over the NLTF's expenditure, with the Minister of Transport responsible for setting its revenue structures (i.e. FED/RUC).

NLTF funding can only be provided to projects that are included in the National Land Transport Programme (NLTP) and deliver against the GPS outcomes (e.g. emissions reduction).

The Ministry of Transport (MoT) is responsible for the Government Policy Statement - Land Transport (GPS-LT), which sets the strategic direction and priorities for transport investment, as well as the activity classes and associated funding ranges for the NLTF.

Commensurate with the decisions from the Land Transport Revenue Review (LTRR), the NLTF is not expected to provide any funding for the construction of ALR (or other 'mega' projects), however, operational funding may be available.

- NLTF funding is constrained by the 'PAY-GO' principle, where annual expenditure is expected to be aligned to the Fund's annual revenues.
- Recent (post-COVID-19) loans have been provided by the Crown to the Fund to manage an operating deficit, however, this is expected to be addressed through the LTRR.
- The Fund is required to manage within prudential debt metrics, however, given the Fund is not expected to contribute to the capital cost, there is unlikely to be Project-related debt.

Role in funding ALR

General constraints

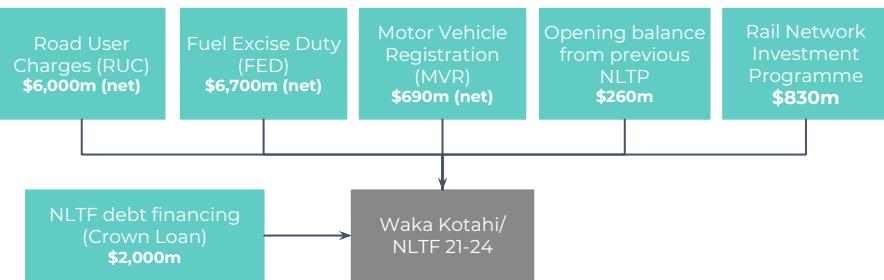
Context:

Since the IBC, the NLTF has been impacted by lower FED/RUC revenue as a result of the impact of COVID-19 and the Government's reduction in FED, lower farebox recoveries (i.e. higher operational subsidies for public transport), and higher demands on expenditure (strong investment pipeline and high inflation).

To fund the resulting operating deficit, the Crown provided Waka Kotahi with a \$2bn loan facility, which has been used to maintain current investment levels. These borrowings will, ultimately, need to be repaid through operating surpluses over the medium term.

A key focus of the LTRR was reviewing the long-term revenue and expenditure profile of the Fund, and working through how it would be able to repay the loans.

Funding for the National Land Transport Fund (NLTF) for 2021-24 will come from:



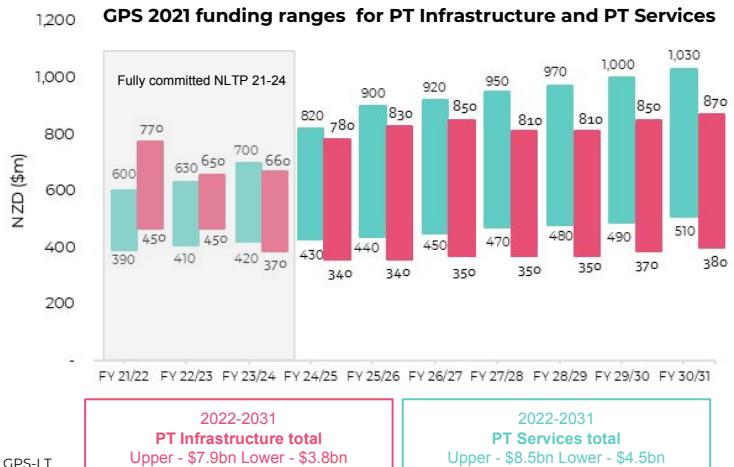
Introduction and context

The funding ranges outlined in the 2021-31 GPS-LT imply the Fund should have the capacity to make a funding contribution to ALR. However, analysis from the LTRR indicates that the NLTF's revenue settings are unlikely to generate sufficient revenue to deliver the level of investment contemplated in the GPS-LT.

Context: Current GPS-LT constraints

There is, theoretically, significant funding for ALR within the 'PT Infrastructure' and 'PT Services' funding ranges from the GPS-LT. However, when overlaying the long-term revenue settings for the Fund and NLTF PAY-GO requirements, the capacity pressures become more acute.

Further, one of the key decisions from the LTRR, which was post the GPS-LT 2021-31, is that the NLTF should not provide capital funding for 'mega' projects.



Context: NLTF PAY-GO model

The NLTF is managed based on the 'PAY-GO' principle, where the Fund's annual expenditure is limited to its annual revenues. The PAY-GO requirements have been softened in recent years to manage post COVID-19 impacts and reduced revenue from the Government's Cost of Living Package.

Key constraints on the NLTF's ability to contribute funding include:

- **Constrained NLTF fund:** The NLTF remains under "considerable financial pressure"¹ due to the number of committed projects in the NLTP 2021-24, reduced revenues, and cost increases. Waka Kotahi has submitted a number of budget bids to help manage the liquidity risks for the NLTF.
- **Decreased revenues:** NLTF revenue during FY22 was ~\$205m (5%) below budget, which reflected the ongoing disruption from COVID-19². The pressures have been further amplified in FY23, with revenues ~\$300m below budget for the first six months of the year (July to December)³. Reductions to fares and FED as part of the Government's Cost of Living Package have contributed to the lower revenues. However, this has been partially offset by expenditure tracking below budget (\$156m)⁴.
- **Increasing investment need:** Investment in public transport will have a critical role in supporting the transition to a lower carbon transport network and supporting growth/urban development aspirations.
- **Cost pressures:** As outlined in the Auckland Council section, inflation drivers have been very high over the past 12 months, with the 'Transport Way' sub- index of the CGPI showing a 19.1% annual increase⁵. Accordingly, it is more expensive to maintain the same levels of service/investment.

1 Waka Kotahi Performance Report Q2 - 1 Oct to Dec 2022

2 NLTF Annual Report 2022

3 Waka Kotahi Performance Report Q2 - 1 Oct to Dec 2022

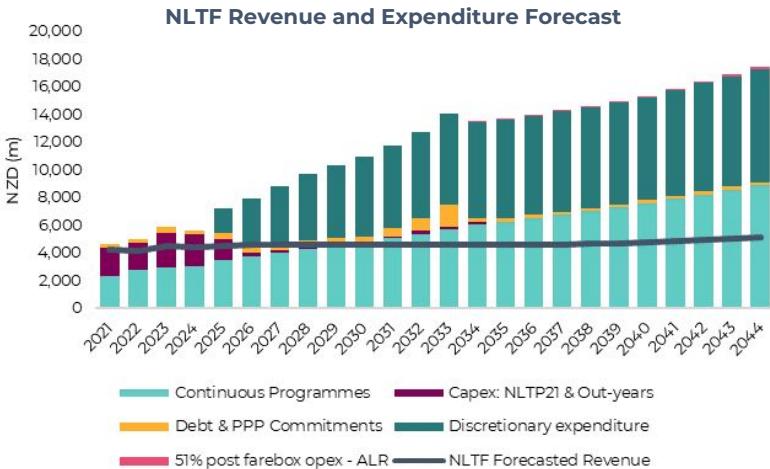
4 Waka Kotahi Performance Report Q2 - 1 Oct to Dec 2022

5 StatsNZ - Business Price Indexes - December 2022 quarter -

Capital Goods Price Index

Introduction to NLTF capacity

The long-term revenue and expenditure profile for the NLTF was reviewed as part of the LTRR, which concluded that in the absence of significant changes to the NLTF revenue settings there would be insufficient revenue to fund just continuous programmes.



Total NLTF forecasted revenue includes Fuel Excise Duty, Road User Charges, Motor Vehicle Registration and Track User Charges revenues.

Continuous programmes include Public Transport Services, State Highway Maintenance, Location Reference Method, road policing, emergency works, and investment management.

Debt & PPP commitments includes Transmission Gully and Puhoi to Warkworth available payments and service charges, and additional and existing debt.

Discretionary expenditure is all expenditure that is not essential expenditure. It includes Emissions Reduction Initiatives for opex and capex, high level estimates, and capex capacity. Forecasted capital expenditures are for illustrative purposes and show amounts aligned with historical levels inflated at the appropriate index through time.

Capex NLTP relates to actual and committed capex from the 2021 NLTP.

NLTF funding capacity

Analysis of the Fund's long-term revenue and expenditure profile indicates that under the current settings, the NLTF's revenues will be insufficient to fund continuous programmes (i.e. State Highway maintenance and keeping the network running) and debt obligations by the late 2020s.

Accordingly, without material changes to FED/RUC (e.g. extending it to include electric vehicles), the NLTF is unlikely to have capacity to fund even an operational subsidy (i.e. 51% of the post-farebox operating expenditure associated with ALR).

The NLTF's revenue profile is constrained by the decarbonisation of the transport system (i.e. uptake of EVs, which don't currently pay FED or RUC). This relationship is ultimately contrary to emissions reduction, which is the "overarching focus" for the GPS-LT 2024. Further, there is currently no annual inflation adjustment to FED or RUC, which, given the costs funded by the NLTF increase annually in line with inflation, means that the NLTF's funding gap will continue to widen.

One of the options considered as part of the LTRR was reducing the scope of the Fund to cover only operations/maintenance and renewals (rather than capital investment), which would significantly reduce discretionary expenditure.

Key observations

- Without significant changes to FED/RUC, the NLTF will not have sufficient revenue to fund its continuous programmes and debt commitments, irrespective of its role in funding ALR.
- There is unlikely to be sufficient funding available through the NLTF for the assumed 51% (post-farebox) operating subsidy for ALR.

Waka Kotahi funding levers

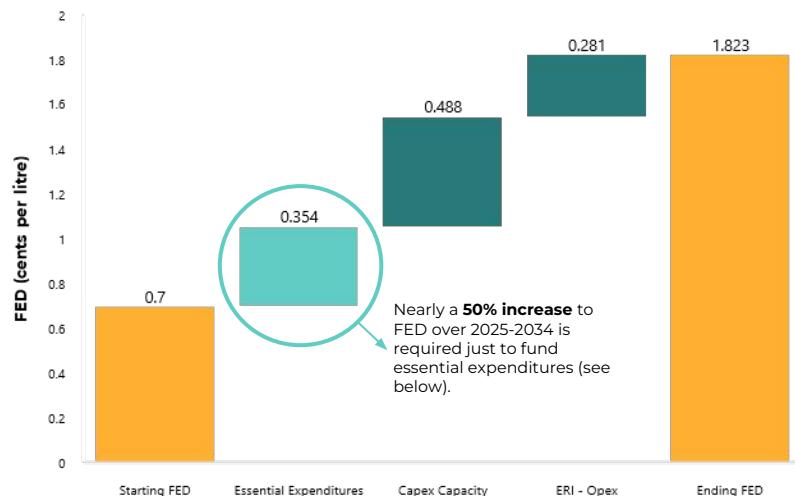
The NLTF is currently facing increasing pressure and uncertainty of future revenue sources. Waka Kotahi is limited in the ways it is able to increase its revenue, as most funding levers are controlled by Central Government.

Funding lever	Description	Indicative magnitude of funding	Change from IBC?	Considerations and trade-offs
Borrowing	Borrowing could be used to support ALR and bridge the investment gap between the NLTP and the forecast land transport revenue.	There is precedent for Waka Kotahi borrowing outside of the NLTP for PPPs. However, a corresponding revenue stream would need to be agreed with the Crown to support this quantum of debt. Further, as noted in the Waka Kotahi's Quarterly Performance Report, "continuation of the trend would mean [the NLTF] would exhaust all [its] facilities".		<ul style="list-style-type: none"> Requires Ministerial approval to undertake borrowing. Dependent on how increased finance costs are planned to be serviced. The impact on the NLTF's debt management ratios would need to be considered.
FED/RUC adjustments	Increasing the charges associated with RUC and FED. Additionally, considering introducing a charge associated with EVs.	An 11.2 Cpl increase to FED over the 2025-2034 period would allow Waka Kotahi to close the funding gap and fund capex to a level aligned with historical investment.	The IBC identified a (nominal) indicative magnitude of \$317m to \$634m for a 5c/l or 10c/l increase to FED (and equivalent to RUC) (refer Appendix 3).	<ul style="list-style-type: none"> Increases in FED and RUC are controlled by Central Government. Changes in FED would need to be in accordance with the Customs and Excise Act 2018, while changes to RUC would need to be undertaken through an Order in Council. Large increases would be needed in order to raise the necessary money to fund ALR.
Alternative revenue streams	Revenue streams such as MVR, tolling and road pricing could be added to the NLTF to reduce the revenue gap.	This will be assessed as part of the Future of the Transport Revenue System Review.		<ul style="list-style-type: none"> Need to be considered alongside other funding sources that target motor vehicle users e.g. congestion charging, RFT.
Reprioritise expenditure	Reprioritise investment to create capacity for ALR.	The only lever directly available to Waka Kotahi is to manage its expenditure profile. Not quantified, due to uncertainty surrounding specific areas for reallocation of NLTF spend.		<ul style="list-style-type: none"> Due to current inflation levels, it is expensive to maintain the same levels of service/investment.

Waka Kotahi: funding levers

A significant increase in FED/RUC revenue is required for the NLTF to simply continue funding its essential expenditure, let alone provide a funding contribution for ALR or investment to support decarbonisation of the transport system.

Cumulative increases in FED (CpL) over 2025-2034 to close funding gap



- Essential expenditures** include continuous programmes, debt obligations including PPPs, committed capex projects, emergency works and regulatory topslice.
- Capex capacity** represents inflated historical investment levels. Forecasted capital expenditures are for illustrative purposes only and show amounts aligned with historical levels inflated at the appropriate index through time.
- Emissions Reduction Initiatives (ERI) Opex** represents additional public transport service costs likely to arise due to VKT reduction and 'mode-shift' ambitions

FED/RUC revenue scenarios:

FED and RUC are the main funding levers for the NLTF. Waka Kotahi is limited in the ways it is able to these rates as increases in FED and RUC are controlled by Central Government.

The funding deficit identified in the final LTRR paper in November 2022 is \$27-39bn for the 10-year period between 2025-2034, assuming no changes to FED and RUC. In order to understand the impact of increases in FED and RUC on revenue, the following options have been assessed by Waka Kotahi.

These options have been assessed for the purposes of the LTRR, and have excluded the deficit needed to fund ALR.

Increase to FED (and RUC equivalent) over 2025-2034 period	Average 3.5 CpL p.a.	Plus incremental average 2.8 CpL p.a.	Plus incremental average 4.9 CpL p.a.
Result	Repay debt obligations and fund continuous programmes	Enable estimated ERI opex to be funded	Fund capex to a level aligned with historical investment levels

Key observations:

- An 11.2 CpL p.a. increase to FED (and RUC equivalent) over the 2025-2034 period would be needed to enable Waka Kotahi to close the funding gap and fund capex to a level aligned with historical investment. These increases do not consider funding ALR.

3.c. Crown

Introduction and context

Given the size and scale of the Project, a significant Crown contribution is likely to be required to address affordability constraints at the beneficiary and organisational level. The contribution may include direct grant funding (i.e. via an appropriation) or indirect support (e.g. guarantee, underwrite, etc.).

Overview

Crown funding is accessed through an appropriation and governed by the Public Finance Act (PFA). Appropriations must be administered by Departments (i.e. MoT), however, the appropriation can authorise expenditure for a Non-Departmental organisation. A 'Capital Expenditure' appropriation is likely to be used for ALR, and could take the form of an annual or multi-year appropriation. Typically, projects of the size and scale of ALR require a multi-year appropriation to provide the necessary revenue certainty.

The size and scale of the Project means that Crown support in some form is likely to be required. The NLTF is expected to fund the Crown's portion of the operating expenditure.

- Fiscal measures:** Key Crown financial metrics including total core Crown debt, net debt-to-GDP, operating surplus and OBEGAL (operating balance before gains and losses)-to-GDP.
- Appropriation quantum:** Crown may also consider the quantum of appropriation required in a given year or period, and competing government funding priorities.
- Precedent:** Precedent setting will also be a consideration i.e. future financial obligations based on the approach to ALR.

Context and current economic conditions

Current Crown fiscal strategy is built on a long-term objective to reduce debt and a short term objective to return operating balances to surpluses. Crown considerations include the following fiscal measures:

Measure	Net Crown debt-to-GDP	OBEGAL/Operating balance to GDP
Goal	The long-term prudential objective is to maintain net debt below 30% of GDP.	In the short term, return to a surplus with a long-term objective to maintain an average OBEGAL in the range of 0-2% of GDP.

Example appropriation pathway

Borrowing expenses would be covered in the "Vote for Finance" administered by the Treasury on behalf of the Minister of Finance.

Parliament	Minister of Transport	Ministry of Transport	Delivery Entity	Contractors
Approves the Budget, which allocates expenditure between different investment and services	Designated Minister with the delegations to control the right to use the appropriation within pre-agreed limits	Department assigned responsibility for administering the appropriation. ALR would be packaged in the Transport "Vote"	Non-departmental that can receive the appropriation administered by MoT	Invoices and receives payment from the Delivery Entity for works

Overview of Crown appropriations and lending

There are many viable options for structuring Crown appropriations to support ALR. The preferred approach will depend on the appropriation type, appropriation pathway, and borrowing options.

Structuring Crown appropriations and lending

There are a number of options for structuring Crown support for ALR. Key considerations for each of the structuring options are outlined below:

• Appropriation type

- Quantum of Crown support required
- Crown preference for higher upfront versus lower over time payments
- Transparency around repayment of capital costs
- Administrative burden
- Consideration of how underwriting certain risks could support Project outcomes

• Appropriation pathway

- Form of the Delivery Entity
- Extent of Urban Development activity and role of the Delivery Entity
- Governance and reporting arrangements

• Borrowing options

- Implementation and deliverability
- Value for money
- Flexibility
- Impact on Crown balance sheet
- Risk transfer
- Wider considerations.

1. Appropriation structure	2. Appropriation pathway	3. Borrowing option
<ul style="list-style-type: none"> • Capex (pay as you go): Appropriation covers capital funding shortfall as it is incurred (i.e. expenditure incurred minus value capture funding sources and any other funding). • Capex (financed): Debt covers capital funding shortfall as it is incurred, with an appropriation used to service debt and repay principal over time. • Opex: Appropriation covers operating funding shortfall as it is incurred. • Underwrite: May be required to underwrite value capture funding sources in case they are not realised at the time or quantum expected. An underwrite could also be considered to facilitate Transit Oriented Development (TOD) development. • Pre-delivery: Support for pre-delivery ALR costs may also be required if funding allocated in the NLTF/NLTP is insufficient. 	<ul style="list-style-type: none"> • Direct to Delivery Entity: Appropriation paid directly to the Delivery Entity. • Via Waka Kotahi: Appropriation paid to Waka Kotahi (as per the NZ Upgrade Programme) which would fund the Delivery Entity. <i>Still requires the Ministry of Transport's appropriation pathway.</i> • Via NLTF: Appropriation paid into the NLTF (which would fund the Delivery Entity) and subject to NLTF requirements. <i>Still requires the Ministry of Transport's appropriation pathway.</i> • Via Kāinga Ora: Appropriation paid to Kāinga Ora (as per HAF) which would fund the Delivery Entity. <i>Would require the Ministry of Housing and Urban Development's appropriation pathway.</i> 	<ul style="list-style-type: none"> • Central: Crown manages cash flow timing centrally (i.e. outside of ALR project). • DMO: Borrowing is undertaken through the DMO (as per Waka Kotahi/NLTF). • Debt Capital Markets: Borrowing is undertaken through the Debt Capital Markets (as per Kāinga Ora).

Impact on net debt-to-GDP

The impact on net debt-to-GDP has been assessed, assuming under each scenario the ALR Project cost is funded by additional Crown debt. The total impact of funding ALR through debt has a minimal impact on the net debt-to-GDP ratio, ranging from 0.8% for a 'full cost allocation' Crown contribution to 2.1% for an 100% Crown contribution.

Crown appropriation: impact on net debt-to-GDP

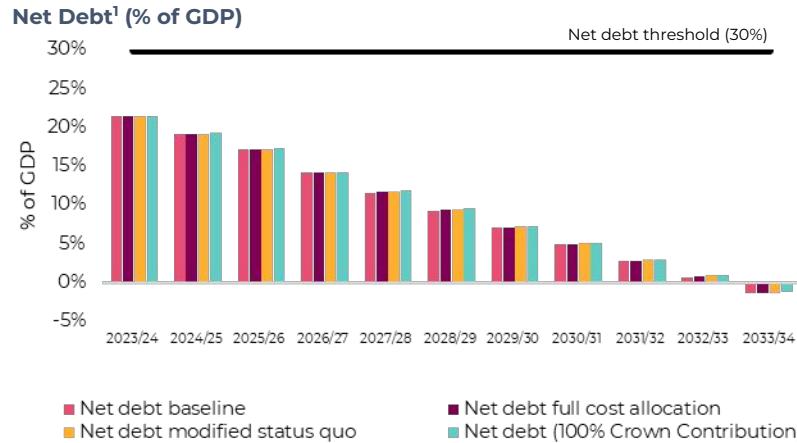
Three scenarios have been considered:

- 1) Total Project capex has been used to conservatively show the maximum impact the Project could have on the Crown's balance sheet, noting multiple funding sources are expected to form the overall funding mix.
- 2) The 'modified status quo' funding scenario assumes Crown appropriation is expected to fund ~75% of capex.
- 3) The 'full cost allocation' scenario aligns the funding split between local / regional and national beneficiaries to their share of benefits (65% v 35% split) reflecting the theoretical application of a pure 'beneficiary pays' approach.

The total impact on Crown net debt-to-GDP ranges from 0.8% - 2.1% over the 10 years to 2033/34. This results in minimal change to the net debt (as a % of GDP) measure and leaves more than sufficient headroom below the 30% threshold.

Key observations

- There is significant headroom for a Crown appropriation for ALR costs.
- Crown support ranging from 'full cost allocation' to 100% of costs will impact net debt-to-GDP ranges from 0.8% - 2.1% over the 10 years to 2033/34.



Scenario	ALR cost profile		
	Costs %	Total Appropriation amount (NPV \$m)	Total Increase in Debt-to-GDP ratio (%)
Baseline	0	0	0%
Full cost allocation	\$3,863		0.8%
Modified status quo	\$8,052		1.6%
100% of capex costs	\$10,679		2.1%

Impact on operating surplus and OBEGAL-to-GDP

The impact of interest associated with increased debt on operating surplus and OBEGAL (as a % of GDP) has been assessed as a result of the debt scenarios outlined on the previous page.

Operating Balance and OBEGAL (As a % of GDP)

The current Crown policy forecasts returning to an operating surplus by FY24/25, and maintaining an OBEGAL in the range of 0% to 2% of GDP over the long run.

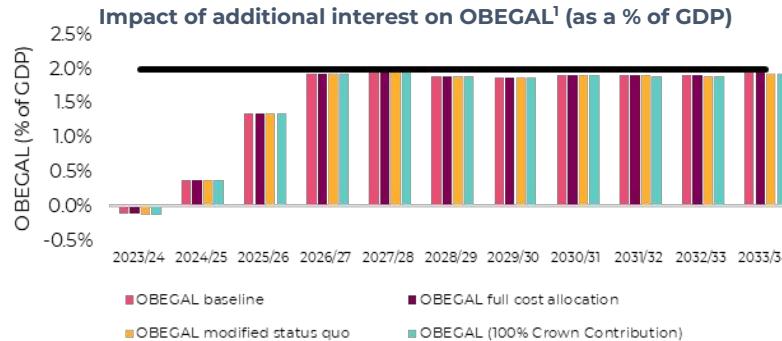
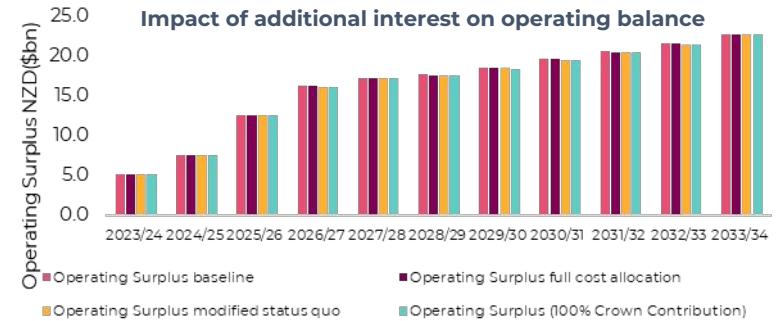
A Crown appropriation to the Project through debt will increase Crown operating costs (e.g. finance costs), impacting OBEGAL-to-GDP.

Assuming the Crown borrows to fund an appropriation, the OBEGAL as a percentage of GDP is marginally affected by increased interest costs and remains within target 0-2% range. The total impact on OBEGAL (as a % of GDP) ranges from -0.2% to -0.5% over the 10-year period to 2033/34. The Crown is still able to return to an operating surplus from 2024/25, in line with current strategy.

Additional finance costs as a result of increased debt would decrease the operating balance by a total of \$156m under the 'full cost allocation' Crown contribution scenario, \$326m under the 'modified status quo' Crown contribution scenario, and \$432m under the 100% Crown contribution scenario.

Key observations

- Crown appropriation via debt would have limited impact on Crown operating balance metrics, ranging from -0.2% to -0.5% over the 10 years to 2033/34. Expected operating costs would remain within the current financial strategy.



¹ Operating Balance Before Gain and Losses, represents Crown revenue less total Crown expenses excluding minority interest share.

Crown balance sheet levers

There are a range of levers the Crown could employ to fund its contribution to ALR, such as increase borrowing, allocation of GST, and reallocation of funds

Funding lever	Description	Indicative magnitude of funding	Change from IBC?	Considerations and trade-offs
Increased Borrowing	The Crown has the ability to provide funding through a Crown appropriation from increased borrowings.	~\$3,863m to \$10,679m	n/a - different debt measure utilised by the Crown since IBC.	<ul style="list-style-type: none"> Balancing the competing priorities for funding across other government investment areas. Setting a precedent of the magnitude of financial support to other major infrastructure projects, and associated 'layering' impact of these costs to Crown finances to support similar public transport projects throughout the country.
Allocation of GST on a geographical basis	Allocation of tax revenue, e.g. GST, within geographical proximity of the Project.	~\$8,250m to \$9,500m (calculated in funding sources report)	Lever was not assessed in IBC	<ul style="list-style-type: none"> Acts as a reallocation of revenues, based on the assumption of increased commercial activity as a result of the Project. Establishes precedent for funding other major infrastructure projects - and as a result not considered within the modified status quo funding scenario.
Reallocation of funds	The Crown could reallocate funds from other government activities to raise further revenue for the ALR project.	n/a	n/a	<ul style="list-style-type: none"> Not quantified, due to uncertainty surrounding specific areas for potential reallocation of government spend. Specific considerations and trade-offs associated with the impact to different public services if funding is reallocated or reprioritised towards the Project.

Appendices

Appendix 1 - Auckland Council baseline adjustment assumptions

Appendix 2 - Illustrative funding scenarios

Appendix 3 - Background from the IBC

Appendix 4 - Glossary of terms and abbreviations

Appendix 1 - Auckland Council baseline adjustment assumptions

Updated baseline capacity

Given Council's 2021-31 LTP is the most recent available source of long-term financial projections, using this data source requires a number of adjustments to more accurately reflect the current environment and financial constraints. The table below outlines these adjustments and any associated assumptions.

Adjustment	Quantum	Details	Assumptions
2031-2050		2.0% in inflation post-LTP	Assumed across funding sources.
Updated data		Replaced FY23 forecasted with actual Replaced FY24 forecast with 2023/24* Consultation Document ¹	N/A
CRL	\$526m	16.7% in FY23 and FY26 33.3% in FY24 and FY25	From mid-way through FY23 to FY26 (split evenly across each of the half-year periods).
Flood and cyclone recovery	\$1,050m	Split: 80% capex, 20% opex 16.7% from FY24 to FY29	Assumed that the cost is front-loaded. Assumed as the mid-point of the cost estimate of \$900m - \$1,200m. Assumed equal split from FY24 to FY29.
Watercare	\$2,584m	Remove Water Supply from FY24 Remove Wastewater from FY24 Removed Watercare's total debt	Assumed that the full Water Supply and Wastewater FIS is removed from the Auckland Council's FIS from 1 July 2024. Assumed Watercare's total debt is removed from Auckland Council.
Stormwater	\$1,000m	Removed Stormwater from FY24	Assumed that the full Stormwater FIS is removed from the Auckland Council's FIS from 1 July 2024.

Appendix 2 - Illustrative funding scenarios

Introduction to funding scenarios

Five illustrative scenarios have been developed to show how different tools can come together to fund both capex and opex. The scenarios also draw out affordability, trade-offs and wider considerations and are summarised in the 'Funding Sources and Settings' report.

The scenarios are illustrative and not intended to reflect a 'preferred' or likely funding scenario. The following assumptions/limitations apply:

Data is based on IBC numbers, analysis will be refined and updates as underlying work, numbers and findings become available.

Costs and phasing are based on IBC tunneled light rail option:



Current opex FAR is assumed to continue to apply. i.e. NLTF funds 51% and Auckland Council funds 49% of opex, net of farebox.

No estimates have been made, at this stage, in relation to **potential urban funding sources** such as the sale of existing land or strategic land acquisition to assist with delivery phase funding.

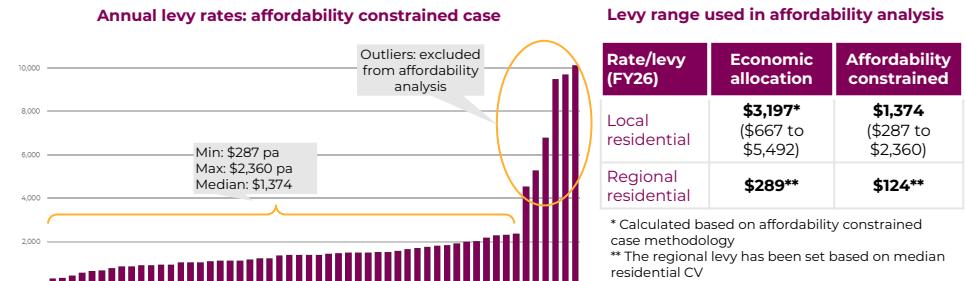
An **IFF levy** on local and regional residential and non-residential landowners is assumed as the key funding source to target Auckland beneficiaries. Two initial cases have been developed to provide indicative funding amounts:

Economic allocation	Based on the initial allocation of economic benefits which implies ~\$7bn (NPV \$5.6bn) of eligible ALR costs should be funded by Auckland regional and local beneficiaries
Affordability constrained	IFF funding scaled back to \$3bn (NPV \$2.6bn) as an initial proxy for a more affordable levy.

In both cases the local station catchments fund ~50% of the IFF funding amount with the regional catchment funding the remaining ~50%.

Levies are calculated based on proximity to stations (400m, 800m, 1,600m and >1,600m) reflecting benefit received based on existing land values (LVs). Work is underway to allocate local benefits across individual stations based on their share of the public transport and land value uplift, however, this is a work in progress.

A multiplier of 1.7x has been applied to non-residential properties. The incidence of the IFF levy on non-residential land is expected to be on business owners (rather than landowners), as most commercial leases are on a 'net' basis. Affordability analysis has focused on median levies.



Overview of the illustrative 'modified status quo' scenario

Purpose

The purpose of this scenario is to outline the potential funding implications of utilising currently available tools and relatively standard settings.

The scenario overlays practical affordability and implementation constraints over the usual funding arrangements.

The key modifications to the status quo are the use of a Crown appropriation (rather than NLTF capital contribution) and an IFF levy to minimise the impact on Auckland Council.

Funding sources: Capex

Landowners: Implementation of an **IFF levy** (in lieu of using targeted/general rates) on both local and regional **residential landowners** to ensure the associated debt is off-balance sheet solution for Auckland Council.

The IFF levies are as per the 'affordability constrained' case with differentials used to reflect the different quantum of benefits derived by each landowner beneficiary group (i.e. median local residential **\$1,374 p.a.**, median regional residential **\$124 p.a.**). All levies are inflated annually.

Under this scenario, **~\$1,505m** of funding is recovered through IFF levies (in NPV terms taking into account the drawdown profile).

Business owners: A funding contribution from businesses is collected through an **IFF levy on non-residential landowners**. This approach is based upon the levy costs being passed through to businesses through 'net' leases, where the lessee pays the taxes, insurance fees and maintenance costs.

The starting levies for local and regional non-residential land in this scenario are **\$1,784 p.a. and \$203 p.a.**, which are inflated annually. The revenue collected under this scenario is **~\$1,123m**.

No development contributions can be collected under this scenario, because Auckland Council is not liable for any share of the capital costs, which is a requirement under the Local Government Act 2002 (LGA).

Crown: A significant Crown appropriation would be required to bridge the 'funding gap' (**~\$8.1bn**).

Funding sources: Opex

Public transport beneficiaries: The standard farebox arrangements have been assumed, where users of the system are charged for using the service, with fares moderated based on wider outcomes (e.g. driving 'mode-shift') and overall network funding requirements.

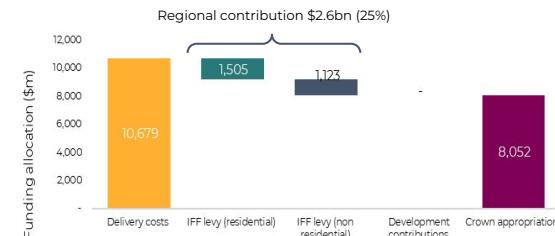
The increase in network revenue (proxy for farebox) is estimated to be **~\$0.4bn** in NPV terms under this scenario. The **implied farebox recovery is 17%**, which is well below the Auckland Transport RPTP target (47% to 50%).

Motor vehicle users (via NLTF contribution): At a system level, motor vehicle users provide a funding contribution through the **NLTF contribution**, which is funded through FED/RUC sources.

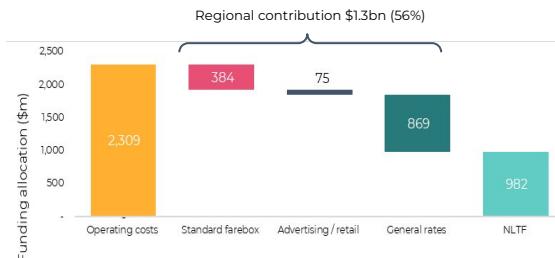
A **51% FAR** is assumed (aligned to Auckland's current FAR) and no changes to underlying FED/RUC settings. Based on these settings, the NPV of the NLTF contribution is **~\$1.0bn**, placing **considerable pressure on the Fund**.

Landowners: A one-off **1.29% increase in general rates** (at the start of operations) is assumed to assist fund Auckland Council's opex contributions generating **~\$0.9bn** (NPV).

Delivery phase funding allocations (NPV \$m)



Operations phase funding allocations (NPV \$m)



Appendix 3 - Background from the IBC

Background from the Indicative Business Case

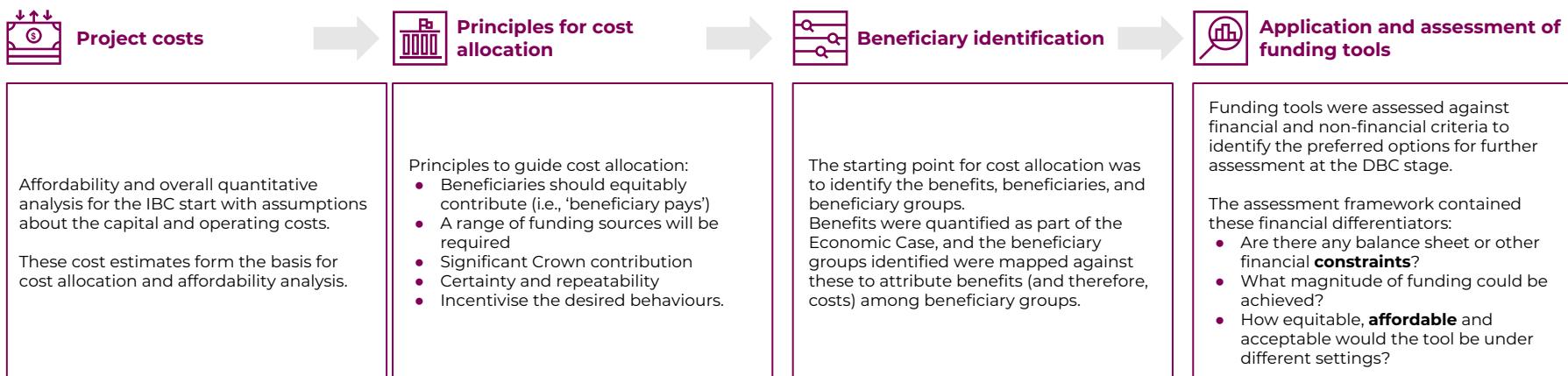
The IBC discussed that ratepayer affordability and acceptability is an important consideration in the implementation of different taxes, levies and rates, particularly in the lower socio-economic portions of the corridor.

Overview of high-level affordability analysis

The IBC identified that **overall project affordability** will be driven by the following factors:

- cost of the preferred technical option
- scope of urban development works being delivered and supporting investment
- capacity of the relevant organisations to fund and finance the Project (both upfront and ongoing costs)
- individual ratepayer affordability (to the extent funding is generated through rating based tools).

Process for analysing overall Project affordability



Assessment of funding options - financial differentiators

A high-level assessment of the different tools was completed as part of the Funding Shortlist Report. This included financial and non-financial differentiators. This page focuses on the two of the three financial differentiators that relate to affordability analysis.

Financial differentiators - IBC assessment



Equitability/affordability

The extent to which the funding option allocates the cost of the Project to its beneficiaries, including between different generations. Wider social considerations, such as affordability for the ultimate payer and socio-economic impacts were also considered under this criteria.

Application to affordability analysis

The IBC considered affordability for beneficiaries largely from a cash flow lens, recognising that income as well as other demands on cash should be considered. Beneficiary affordability was considered for the end payer of each funding tool.

Consideration was given also to other factors that affect household income, to the relative (not just absolute) increase in costs to beneficiaries, and the alignment between costs and benefits to a beneficiary.



Balance sheet impact

The potential balance sheet impact of the different funding options emerged as a key consideration for different organisations, and was therefore specifically addressed for each option.

The IBC assessed the capacity of relevant organisations to fund and finance the Project, with the relevant organisations being: Auckland Council, Waka Kotahi (the NLTF), Kāinga Ora, the Crown, and other sources including private finance.

Organisational capacity assessment summary

The IBC assessed the baseline capacity (both operating budgets and balance sheet) for the below organisations.

Organisation	Relevant funding source(s)*	Assessment approach	High-level analysis**
Auckland Council	<ul style="list-style-type: none"> Capex contribution - borrowing, asset recycling, DCs Opex contribution - general / targeted rates, regional fuel tax (RFT), reducing expenditure Payment in kind (land holdings). 	<ul style="list-style-type: none"> Council's revenue and financing sources as well as credit rating were first identified. Baseline capacity for operating expenditure and borrowing were assessed for the 2021-2031 LTP period. Potential levers included borrowing, proceeds from asset sales, rates increase, targeted rate, RFT increase, Capacity for a payment-in-kind or sale of assets and regional land holdings. 	Auckland Council is highly constrained with respect to both operating budgets and balance sheet capacity, with the ongoing impact of COVID-19 and City Rail Link costs unclear.
Waka Kotahi	<ul style="list-style-type: none"> Capex contribution - NLTF (borrowing), Crown appropriation/MoT Opex contribution - GPS-LT for public transport, FED and RUC, MVR, reduced expenditure. 	<ul style="list-style-type: none"> Consideration of ALR delivery and operating costs fitting within the scope of the PT Infrastructure and PT Services activity classes respectively, consideration of capacity of these funding allocations Considered debt headroom against credit metrics of peers Analysis of scenarios to increase ongoing revenue - affordability impacts from cash flow and equity level. 	The NLTF is fully committed in the short term, but there is opportunity undertake borrowing supported by additional revenue streams and/or Crown appropriation to fund capex. Waka Kotahi also has a number of funding levers that could be used to generate ongoing revenues to fund opex.
Kāinga Ora (KO)	<ul style="list-style-type: none"> Negotiated contribution UDA - SDPs - targeted rates, DCs, borrowing Strategic land purchases. 	<ul style="list-style-type: none"> Understanding KO's baseline borrowing capacity and credit constraints, while considering its investment programme. Assessment of KO's land holdings that fall within the corridor and could be sold/used to maximise urban development outcomes Ratepayer affordability analysis in context of an SDP. 	Kāinga Ora has debt headroom and may be able to support ALR through the acquisition, development and sale of land, reducing the burden on ALR and maximising urban development outcomes. SDP establishment is an opportunity - similar funding tools to Council without balance sheet limitations.
The Crown	<ul style="list-style-type: none"> Crown appropriation (capex, opex, underwrite, or pre-delivery costs). 	<ul style="list-style-type: none"> Consideration of fiscal measures such as total core Crown debt and core Crown debt-to-GDP Further analysis/advice needed to assess impact of underwrite support - contingent liability may arise. 	Indicative analysis with Crown support ranging from 50% to 150% of the estimated appropriation size, the impact on net core Crown debt-to-GDP ranges from 0.71%-4.64% depending on the option.
Other sources	<ul style="list-style-type: none"> Private sector capital Emissions trading scheme (ETS) Congestion charging (CC) in Auckland. 	<ul style="list-style-type: none"> General financial constraints to private sector capital Consideration of beneficiary-to-payer alignment with the ETS and CC, as well as potential baseline capacity to contribute funding. 	High-level analysis indicates the potential of the ETS and CC, under current baselines, having capacity to contribute revenue as funding for ALR, although with some misalignment of beneficiary-to-payer.

Auckland Council capacity assessment*

Auckland Council's capacity to contribute funding to ALR depends on a number of constraints - financial (debt capacity), legislative (balanced budget requirements), and political (Governing Body approvals).

Expenditure capacity

It was determined that under current baselines, Council has limited capacity to contribute funding as operating funding (e.g. rates) was fully allocated in order to achieve a **balanced budget** (as required under the Local Government Act 2002 (LGA) of the need for operating revenues to be at a level sufficient to meet that year's projected opex).

In order to contribute under current baselines it is likely that existing services, investment and/or operating expenses would need to be reduced over and above their existing post-COVID-19 opex cuts.

The chart below shows Council planning to operating at a deficit for the 2021-31 LTP period, with shortfalls made up for through borrowing.

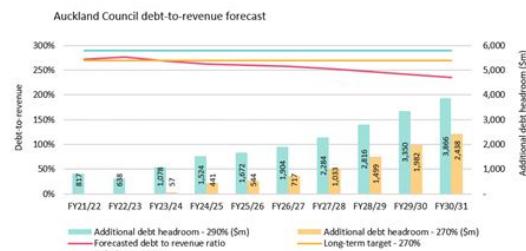


Borrowing capacity

Analysis showed that Council had limited capacity for additional borrowing in the near-term, with some debt capacity becoming available from 2024 onwards (assuming the same credit rating - S&P Global of AA (stable) and Moody's of Aa2 (Stable)).

The chart below shows Council's **debt-to-revenue** for the 2021-31 LTP period below their limit of 290% and long-term target of 270% - in line with their treasury policy and covenants from the Local Government Funding Agency (LGFA).

Further analysis would be needed to understand the sensitivity of debt capacity to credit rating and the resulting impact on cost of borrowing, as well as access to borrowing.



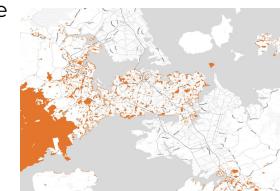
Assets and land holdings capacity

Auckland Council has a number of commercial and non-commercial assets that could be available for asset recycling. It also has a number of land holdings within the ALR corridor and across the wider Auckland region.

These assets were assessed at a high-level to explore the potential possibility of supporting ALR upfront capital requirements by either reducing land acquisition costs (if land fell within the corridor) or by contributing the proceeds of a sale.

Further analysis and due diligence would be needed to assess **Council's capacity** to either offer a 'payment-in-kind' of land to the ALR delivery entity or to contribute capital from sale proceeds. Among other factors, this opportunity would depend on:

- Trade-offs of alternative uses of the land (i.e. if the asset or land holds strategic value)
- Value for money for ratepayers
- Broader Council urban development goals.



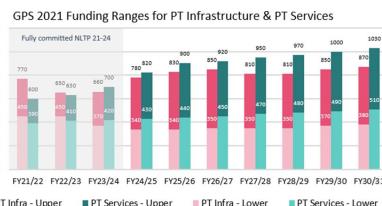
Waka Kotahi capacity assessment*

Waka Kotahi manages the NLTF (which gives effect to the GPS-LT set by MoT) but has limited control over the NLTF's revenue sources and ability to borrow. The NLTF is fully committed in the short term but there may be opportunity to undertake additional borrowing and/or Crown appropriation to fund capex.

NLTF investment constraints

Public transport investment constraints

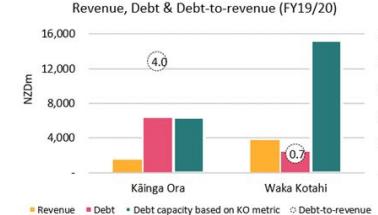
- ALR delivery activities would fit within the scope of the PT Infrastructure activity class, which is **fully committed** to June 2024 with only \$66m committed to ALR and \$39m expected for ALR.
- ALR operating costs would fall into the PT Services activity class - **significant increase** over forecast period with increased PT usage.



Additional borrowing

The NLTF can borrow to fund specific land transport activities, but has borrowed little to date and maintains relatively low debt levels. Key serviceability credit metrics suggest that the NLTF could borrow significantly more, although debt servicing costs (principal repayment and interest) would be classified in the relevant activity class which is fully committed in the short term.

Using Kāinga Ora (and others) as a peer, as the NLTF does not have an internal treasury management policy, suggests significant **debt headroom**. However, this analysis was indicative only and ALR could use up a significant proportion of available debt headroom.



Levers to increase NLTF revenue

The NLTF's revenue sources are 49% FED and 45% RUCs, with small changes to the rates on these able to drive large revenue increases. Four different scenarios were analysed to assess revenue impact and affordability - a 5c and 10c increase in FED and equivalent increase in RUC, as well as FED and RUC indexed at 1% and 2% in 2022.

New Zealand's fuel tax sits at 46% of total fuel costs (48% for Auckland), while the OECD average is 54%. A FED increase of 24c/litre would take Auckland up to the OECD average, implying relative cash flow affordability of the first two of these scenarios. It was noted that these options could still result in **cash flow affordability concerns**, particularly for vulnerable demographics and those that do not have an alternative to private vehicle transport.

There is also the consideration of **regional equity**, whereby Auckland beneficiaries, through the Project, may receive a disproportionate level of NLTF revenue despite it being a national source.

Kāinga Ora capacity assessment*

Kāinga Ora could play an important role in achieving the Project's desired urban development outcomes in the corridor. KO have a number of landholdings within the ALR corridor and has baseline borrowing capacity, although has an ambitious investment programme.

Borrowing capacity

Analysis showed that KO has baseline borrowing capacity, but also has an ambitious investment programme that is expected to require considerable capital - limits ability to invest in ALR.

KO's credit metrics, and impact on credit rating, would also need to be considered when taking on additional debt. **Constraints to borrowing** include:

- New borrowing needing to be serviced, and holding costs (e.g. rates, maintenance) if borrowing is used to purchase land
- KO bound by internal treasury policy, and by Government directed borrowing limits (the Borrowing Protocol limit)
- Impact on credit rating, although strong link to the Crown and role as critical service provider.

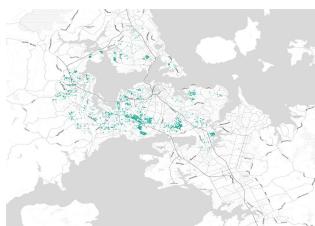


Land holdings capacity

Kāinga Ora have a number of landholdings within the ALR corridor and also across the wider Auckland Region that could potentially support ALR's upfront capital requirements by reducing land acquisition costs or contributing the proceeds from the sale of land holdings to ALR.

The size and value of KO's land holdings would need to be considered, as well as the potential further value uplift as a result of the Project.

Selection of land proposed for sale would require further due diligence to ensure alignment with both the Project's objectives and Kāinga Ora's **objectives and capacity** to divest such assets/land.



UDA - ratepayer affordability

The Urban Development Act 2020 (UDA) empowers Kāinga Ora to act as a 'one-stop-shop', delivering all elements of complex urban development. This includes the ability to implement rating and other funding tools. These funding tools, possible through SDP establishment, are largely synonymous with the powers of councils under the Local Government (Rating) Act 2002 (LGRA), however, without Council's balance sheet constraints.

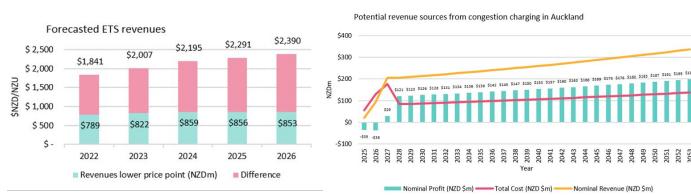
Implementation of such funding tools would require analysis of

- what Project elements could fall under the scope of the UDA/an SDP and, importantly
- **affordability to ratepayers/end payers** of these funding tools imposed under the UDA in addition to existing rating costs imposed by Council.

KO is also treated like other beneficiaries in the context of being subject to value capture tools, such as paying DCs or a negotiated contribution. Consideration of these funding tools imposed on KO would be needed; any DC/negotiated contribution higher than 'market' (i.e. what a private developer would pay) puts more cost burden on the Crown and would require further consideration.

Capacity assessment* for Crown and other sources

Initial analysis highlights a gap between ALR capital costs and funding that can be sourced through value capture and other tools, which is expected to be closed by a Crown appropriation, private sector, and other sources. It is also assumed the Crown will be required to provide an underwrite of any variable or value capture sources.

Crown capacity	Private sector capital	Other public sources																																										
<p>Initial analysis shows the likely need for a Crown appropriation to assist in funding ALR.</p> <p>Assessment of the Crown's capacity to close ALR's funding gap depends on the appropriation type, appropriation pathway, and the source of borrowing.</p> <p>Fiscal metrics to analyse Crown capacity include assessing the impact on total core Crown debt and core Crown debt-to-GDP.</p> <p>With Crown support ranging from 50% to 150% of the estimated appropriation size, the impact on net core Crown debt-to-GDP ranges from 0.71% to 2.12% for the LRT Dominion Road option and 1.55% to 4.64% for the MRT Sandringham Road option.</p> <p>Depending on the likelihood of the underwrite being required, a contingent liability may arise for the Crown. The Detailed funding advice report recommended that accounting advice is sought once the value capture tools are confirmed and scope of the underwrite is understood.</p>	<p>Private sector debt and equity might be used by the Delivery Entity in order to finance ALR.</p> <p>General financial constraints to private finance include:</p> <ul style="list-style-type: none">Initial Crown equity contribution still required.Construction debt likely to be expensive, term debt still above Crown/DMO borrowing rates. Equity likely to value revenue streams (e.g. farebox) conservatively and require any upside (e.g. if farebox is higher than anticipated).Debt tenor unlikely to match the Project life, introducing refinancing risk.Interest rate swaps will be required to mitigate base rate risk.Reporting and ongoing covenant testing will be required.There may be additional commercial terms that private lenders require as part of negotiated financing agreements.	<p>Other public funding sources that could be used to support ALR include the Emissions Trading Scheme and congestion charging applied in Auckland.</p> <p>General financial constraints to these public sources include:</p> <ul style="list-style-type: none">Potential mismatch of beneficiary to payer if using ETS revenuesCompeting projects and funding needs for both ETS and CC generated revenues i.e. other transport projects or better payer-to-beneficiary mapped projects broadly. <p>Potential revenue capacity of both sources were analysed, although it is difficult to predict the exact price and volume of NZUs from the ETS in particular. At a high level, both options were assessed as having potential baseline capacity to contribute funding.</p>  <table border="1"><caption>Forecasted ETS revenues (NZD/m)</caption><thead><tr><th>Year</th><th>Revenues lower price point (NZD/m)</th><th>Difference (NZD/m)</th></tr></thead><tbody><tr><td>2022</td><td>\$789</td><td>\$1,841</td></tr><tr><td>2023</td><td>\$822</td><td>\$2,007</td></tr><tr><td>2024</td><td>\$859</td><td>\$2,195</td></tr><tr><td>2025</td><td>\$856</td><td>\$2,291</td></tr><tr><td>2026</td><td>\$853</td><td>\$2,390</td></tr></tbody></table> <table border="1"><caption>Potential revenue sources from congestion charging in Auckland (NZD/m)</caption><thead><tr><th>Year</th><th>Nominal Profit (NZD \$m)</th><th>Total Cost (NZD \$m)</th><th>Nominal Revenue (NZD \$m)</th></tr></thead><tbody><tr><td>2022</td><td>\$100</td><td>\$100</td><td>\$100</td></tr><tr><td>2023</td><td>\$150</td><td>\$150</td><td>\$150</td></tr><tr><td>2024</td><td>\$200</td><td>\$200</td><td>\$200</td></tr><tr><td>2025</td><td>\$250</td><td>\$250</td><td>\$250</td></tr><tr><td>2026</td><td>\$300</td><td>\$300</td><td>\$300</td></tr></tbody></table>	Year	Revenues lower price point (NZD/m)	Difference (NZD/m)	2022	\$789	\$1,841	2023	\$822	\$2,007	2024	\$859	\$2,195	2025	\$856	\$2,291	2026	\$853	\$2,390	Year	Nominal Profit (NZD \$m)	Total Cost (NZD \$m)	Nominal Revenue (NZD \$m)	2022	\$100	\$100	\$100	2023	\$150	\$150	\$150	2024	\$200	\$200	\$200	2025	\$250	\$250	\$250	2026	\$300	\$300	\$300
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Appendix 4 - Glossary of terms and abbreviations

Glossary of terms and abbreviations

Term	Description	Term	Description
AIAL	Auckland International Airport Limited	KO	Kāinga Ora
ALR	Auckland Light Rail	LGA	Local Government Act 2002
ALR Ltd.	Auckland Light Rail Limited	LGFA	Local Government Funding Agency
CC	Congestion Charging	LTP	Auckland Transport Long-Term Plan
CCC	Climate Change Commission	LTRR	Land Transport Revenue Review
CGPI	Capital Goods Price Index	LVUM	Land Value Uplift Mechanism
CpL	Cents per Litre	MoT	Ministry of Transport
Council	Auckland Council	MSM	Macro Strategic Model
CPI	Consumer Price Index	MV	Motor Vehicle
CV	Capital Value	NLTF	National Land Transport Fund
DBC	Detailed business case	NPV	Net Present Value
DC	Development Contribution	NW	NorthWest Rapid Transit
DCM	Debt Capital Markets	NZSF	New Zealand Superannuation Fund
EV	Electric Vehicle	OBEGAL	Operating Balance Before Gains and Losses
ETS	Emissions Trading Scheme	PT	Public Transport
FAR	Financial Assistance Rate	PTOM	Public Transport Operating Model
FED	Fuel Excise Duty	RFT	Regional Fuel Tax
FY	Financial Year	SDP	Specified Development Project
GDP	Gross Domestic Product	TSY	The Treasury
GPS - LT	Government Policy Statement on Land Transport	RUC	Road User Charges
GST	Goods and Services Tax	UDA	Urban Development Act 2020
IBC	Indicative Business Case	VKT	Vehicle kilometres travelled
IFF	Infrastructure Funding and Financing	WHC	Waitematā Harbour Connections

Thank you



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