

**UNCONFIRMED MINUTE EXTRACT FROM THE NON-PUBLIC MINUTES OF THE COUNCIL MEETING  
HELD ON MONDAY 6 APRIL 2020**

**1 DCHL MATTERS**

A report from Finance appended a report from Dunedin City Holdings Ltd (DCHL) on the future of Dunedin Railways Ltd (DRL).

The Chairperson, DCHL (Keith Cooper) and General Manager DCHL (Jemma Adams) spoke to the report and responded to questions from Councillors.

There was a lengthy discussion on the different options available and the repercussions of each. It was agreed that this matter be treated with sensitivity and the utmost confidence and compassion.

Moved (Mayor Aaron Hawkins/Cr Christine Garey):

That the Council:

- a) **Instructs** Dunedin City Holdings Ltd (DCHL) to mothball Dunedin Railways Limited (DRL); and
  - i) Where possible, redeploy employees made redundant across the DCHL Group and elsewhere; acknowledging that
  - ii) Has no view on what a permanent outcome might look like; and
  - iii) Will provide up to \$1.05m for the mothballing costs from July 2020 - December 2021, noting that any investment in future options would need to be subject to a separate business case and approval process.
- b) **Requests** a report from DCHL, as soon as is practicable detailing:
  - i) Options for DRL's operating and governance structure in the interim; and
  - ii) An asset management schedule to protect current assets.
- c) **Requests**, in time for Long Term Plan deliberations; an update report outlining the longer term options for DRL and its assets.

**Division:**

The Council voted by division

For: Crs Sophie Barker; David Benson-Pope; Rachel Elder; Christine Garey; Doug Hall; Carmen Houlahan; Marie Laufiso; Mike Lord; Jim O'Malley; Jules Radich; Chris Staynes; Andrew Whiley and Mayor Aaron Hawkins

Against: Cr Lee Vandervis

The motion was **carried** 14 votes to 1.

**Notice of Meeting:**

I hereby give notice that an extraordinary meeting of the Council will be held on:

**Date:** Monday 6 April 2020  
**Time:** 2.00 pm  
**Venue:** Via Audio Visual Link

Sue Bidrose  
Chief Executive Officer

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**Extraordinary Council**  
**CONFIDENTIAL AGENDA**

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**MEMBERSHIP**

**Mayor** Mayor Aaron Hawkins  
**Deputy Mayor** Cr Christine Garey

<b>Members</b>	Cr Sophie Barker	Cr David Benson-Pope
	Cr Rachel Elder	Cr Doug Hall
	Cr Carmen Houlahan	Cr Marie Laufiso
	Cr Mike Lord	Cr Jim O'Malley
	Cr Jules Radich	Cr Chris Staynes
	Cr Lee Vandervis	Cr Steve Walker
	Cr Andrew Whiley	

**Senior Officer** Sue Bidrose, Chief Executive Officer

**Governance Support Officer** Lynne Adamson

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Governance Support Officer

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**Note:** Reports and recommendations contained in this agenda are not to be considered as Council policy until adopted.

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## **DECLARATIONS OF INTEREST**

Members are reminded of the need to stand aside from decision-making when a conflict arises between their role as a representative and any private or other external interest they might have.

## **DCHL - MATTERS**

Department: Finance

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### **REASONS FOR CONFIDENTIALITY**

Grounds:	S48(1)(a) - The public conduct of the part of the meeting would be likely to result in the disclosure of information for which good reason for withholding exists under section 7.
Reason:	<p>S7(2)(b)(ii) - The withholding of the information is necessary 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.</p> <p>S7(2)(h) - The withholding of the information is necessary to enable the local authority to carry out, without prejudice or disadvantage, commercial activities.</p> <p>S7(2)(i) - The withholding of the information is necessary to enable the local authority to carry on, without prejudice or disadvantage, negotiations (including commercial and industrial negotiations).</p>

### **EXECUTIVE SUMMARY**

- 1 A confidential report from Dunedin City Holdings Limited (DCHL) is attached which outlines the future of Dunedin Railways Limited ("DRL").
- 2 DCHL have previously advised Council of the commercial position of DRL and work being undertaken on a recovery plan. That position has worsened significantly as a result of the Coronavirus 19 and the report provides three options for Council to consider.

### **RECOMMENDATIONS**

That the Council:

- a) **Considers** the Report, and associated recommendations, from DCHL regarding the options for the future of Dunedin Railways Limited.

### **Signatories**

Author:	Dave Tombs - General Manager Finance and Commercial
Authoriser:	Sue Bidrose - Chief Executive Officer

**Attachments**

	<b>Title</b>	<b>Page</b>
A	DCHL Report	



DUNEDIN CITY HOLDINGS LIMITED

# Report

**TO:** Dunedin City Council

**FROM:** Keith Cooper, Chair  
Jemma Adams, General Manager

**DATE:** 2 April 2020

**SUBJECT:** Options for future of Dunedin Railways Ltd

**SENSITIVITY** **IN CONFIDENCE**

## SUMMARY

Dunedin Railways Ltd has had business sustainability issues for some time. These have been exacerbated by Covid-19 impacts on the tourism industry, and Council decisions are now required about the future of the company and its assets. This report sets out Dunedin City Holdings Ltd's (DCHL's) recommendation for the company's future and two alternatives for Council consideration.

## BACKGROUND

1. Dunedin Railways Ltd (DRL) is a Council Controlled Trading Organisation (CCTO) owned by Dunedin City Holdings (DCHL) (72.03% shareholding) and the Otago Excursion Train Trust (OETT) (27.97% shareholding).
2. DRL has had business sustainability issues for some time. These have been previously signalled to Council and other stakeholders, including in DRL's 2019 Annual Report which reported a \$1 million equity injection by shareholders DCHL and OETT, and noted that further equity would be required to ensure ongoing viability of the business.
3. The DRL Board were nearing completion of a business turn-around plan when Covid-19 started impacting on the company. Covid-19 has not only had an immediate detrimental impact on the company; it has also thrown into doubt many of the assumptions on which the turn-around plan was based.

## Current status

4. DRL's current year performance was running approximately 10% behind budget to February 2020 due to poor spring/summer tourist numbers (we understand this result was consistent with other Dunedin tourism providers).
5. DRL closed its doors on Monday 23 March as a non-essential service, in accordance with the New Zealand Government placing the country at Level 4 Alert for Covid-19.
6. All employees are at home, with most on special leave (a very small number are able to work from home). DRL has agreed with its union (RMTU) that staff will be paid at 80% for the duration of the lockdown. DRL has applied for the Government's wage subsidy, which is expected to result in a one-off payment of approximately \$350,000 (covers the programme's 12 week period)<sup>1</sup>. The subsidy amount should be considered in context of the company's current (i.e. 80%) monthly wage cost of \$320,000.

<sup>1</sup> The subsidy would be passed on to employees as required by the scheme. In the event that staff were not employed for the full 12 weeks of the programme, DRL would refund any unutilised portion of the subsidy to government.



7. April is traditionally the end of DRL's core passenger season. Over autumn and winter the company incurs considerable holding costs without revenue, and typically increases its debt accordingly. Under the status quo, DRL's debt would increase from \$2.28m to \$3.7m over the 2020 winter. DRL's costs are usually recovered and debt repaid over the following summer cruise ship season. This will not occur in the coming year.
8. The table below shows movement in DRL's financial forecasts over the past 9 months.

*DRL financial forecasts for the year ending 30 June 2020*

	<b>SoI forecast</b>	<b>Pre-Covid revised forecast</b>	<b>19 Updated forecast – including Covid-19 impacts*</b>
EBITDA	623,964	(192,387)	(1,202,488)
Net profit before tax	57,198	(803,582)	(1,838,697)
Net profit after tax	41,183	(578,579)	(1,323,862)

\*This forecast assumes staff are paid at 80%, but does not account for the wage subsidy of \$350,000 which DRL hope to receive.

9. As noted above, the business has a current wage expense of approximately \$80,000 per week (with staff paid at 80%) or \$320,000 per month, with no offsetting revenue.

## **Outlook**

10. DRL's outlook is very uncertain. Cruise traffic is a significant portion of DRL's customer base. The cruise industry is largely US/European-owned and will take some time to recover, both in terms of global Covid-19 restrictions lifting, and also in consumer appetite returning for international travel in general and cruise products in particular. At this stage, DRL's best guess is that cruise seasons in New Zealand may start to rebuild from the summer of 2021/2022 at the earliest.
11. Aside from the cruise market, inbound international tourism is significant for DRL and with borders likely to remain closed for the foreseeable future, passenger numbers will be significantly reduced.
12. A surge in domestic travel is very unlikely to match the business that DRL would otherwise have enjoyed from the international market.

## **DISCUSSION**

13. In this context, DRL and DCHL have been identifying and evaluating options for DRL's future. We outline three options in this report:
  - a. Close the business (DCHL's recommended option)
  - b. Mothball the business for ~18 months (or until tourism market recovers), with a view to re-opening train services on the Taieri Gorge line
  - c. Mothball the business with a view to exploring feasibility of a small number of alternative options for the company's assets.
14. These options are presented to Council because of the significance of the company to the community and because two of the three options presented would require financial contribution from Council.
15. DCHL acknowledges this will be a difficult decision to make. All of these options involve the loss of a large number of jobs, and significant change to – or potential loss of – a long-standing and iconic Dunedin tourist attraction. We acknowledge the significant community affection for the company and the Taieri Gorge service.

16. Continuing with the business at status quo, however, would cost approximately \$750k per quarter ongoing through winter with little hope of significant revenue for the next 18 months at least. The company is not able to sustain this cost and would quickly become insolvent without shareholder support.
17. Any future option will need to be discussed with the company's other shareholder, the OETT. The OETT are represented by directors on the DRL board, who have been exploring options, but we have not yet held a shareholder to shareholder discussion. DCHL has approached Council first as DCHL is the majority shareholder of DRL. We intend to engage with the OETT as the next step following Council consideration of this report.

### **Option 1: Close the business (DCHL's recommended option)**

18. Under this option, Dunedin Railways Ltd would be wound up over the next quarter. All 74 staff would be made redundant and assets disposed of.
19. [REDACTED]
20. Estimated costs of this option are set out below:

	<b>Quarter to Jun 2020</b>	<b>18 months to Dec 2021</b>	<b>Years 3-10</b>	<b>Total</b>
DRL Cost	\$1.63m	-	-	<b>\$1.63m</b>
DCHL cost to clear DRL debt	\$2.28m	-	-	<b>\$2.28m</b>
<b>Total</b>	<b>\$3.91m</b>	-	-	<b>\$3.91m</b>

21. The \$1.63m cost to DRL in the next quarter comprises redundancy costs, holiday pay and booking refunds. This figure is subject to some change depending on the balance of the company's debtors and creditors, GST and tax (etc) at the time of closure.
22. There is a further impact on DCHL's balance sheet, as equity in DRL (currently \$1.52m on DCHL books) would be written off.
23. DCHL and DRL are able to fund the costs associated with Option 1.
24. DCHL recommend this option because it presents the lowest financial impact to the Group overall. DCHL also believe this option is best given the poor outlook for DRL in the medium to long term.

25. [REDACTED]

#### *Option 1: Advantages*

26. Lowest cost to DRL, DCHL and Council
27. Best match for DRL's outlook going forward

#### *Option 1: Disadvantages*

28. Loss of 74 jobs

29. Removes an iconic tourist attraction and an object of city pride

**Option 2: Mothball the business for future re-opening of train services on the Taieri Gorge line**

30. Under this option, DRL would be “mothballed”. That is, its operations would be ceased, but assets would be kept and minimum maintenance completed so that the company could operate in some shape or form at some point in the future.
31. If DRL were to operate trains on the Taieri Gorge line again in future, the DRL board recommend that all but seven staff be made redundant. Those seven staff would continue to undertake maintenance on the company’s track and rolling stock assets and would maintain licences and intellectual property (IP), at a cost of approximately \$0.9m per year. There would be no revenue to offset this cost so ongoing shareholder support would be required.
32. We believe the company would spend at least 18 months in mothball, before the tourism market recovered sufficiently to warrant re-opening of any or some train activity.
33. Once re-opened, the company’s operating model would need to change. Its current model is unsustainable and this would likely be highlighted further in a market recovering from the global shock of Covid-19.
34. When developing their turn-around plan, the DRL board only identified one potentially sustainable Taieri Gorge operating model. The model entails:
- a. [REDACTED]
  - b. [REDACTED]
  - c. [REDACTED]
  - d. [REDACTED]
35. This model is not aimed at making a profit or providing a return to shareholders, but would hopefully break even and perhaps allow for some income to offset capital expenditure or deferred maintenance costs.
36. It must be noted that this model was developed in a pre-Covid-19 context. Many of the assumptions it is based on are now in doubt (for example, cruise numbers and timing of industry re-start, tourism numbers in general, [REDACTED] [REDACTED] [REDACTED] [REDACTED] [REDACTED] general employment and economic landscape post Covid-19).
37. The primary reason DCHL do not recommend this option, however, is the significant deferred maintenance required on the Taieri Gorge line. The line from Wingatui to Middlemarch will require an estimated \$10 million over the next ten years (including \$3m in the short term) for repairs and upgrades of track, sleepers, bridges, tunnels, etc. This work is considered essential for ongoing safety of rail operations on the line.

38. Estimated costs of Option 2 are set out below:

	<b>Quarter to Jun 2020</b>	<b>18 months to Dec 2021</b>	<b>Years 3-10</b>	<b>Total</b>
<b>DRL Cost</b>	\$1.43m	\$1.35m	Re-start investment: \$0-1.5m Short term def mtce: \$3m Med term def mtce: \$5m-7m Sub-total: \$8m-11.5m	<b>\$10.78m to \$14.28m</b>
<b>DCHL cost to clear DRL debt</b>	\$2.28m	-	-	<b>\$2.28m</b>
<b>Total</b>	<b>\$3.71m</b>	<b>\$1.35m</b>	<b>\$8m to 11.5m</b>	<b>\$13.06m to \$16.56m</b>

39. The \$1.43m cost to DRL in the next quarter comprises redundancy costs, holiday pay and booking refunds. Again, this figure is subject to some change depending on the balance of the company's debtors and creditors, GST and tax (etc) at the time of closure.
40. The cost to December 2021 is based on estimated mothball period costs (primarily staff costs) of \$0.9m per year.
41. Re-start investment of \$1.5 million is an estimate of costs such as recruitment and increased overheads required at point of re-opening the business.
42. Clearing of DRL's debt has been included, although in theory this debt could remain with DRL while in mothball.
43. While DCHL's equity in DRL (currently \$1.52m) would remain on DCHL's balance sheet under this option, it would be negatively impacted by a highly likely ~\$3.2m-4.2m impairment of assets that DRL will face at the end of FY2020.
44. Council would need to provide funding for mothballing costs, re-investment and deferred maintenance costs (estimated total \$9.35 to \$12.85m) if it wished to pursue this option.

*Option 2: Advantages*

45. Maintains train service on the Taieri Gorge line
46. Retains seven jobs, with potential new hires when company brought out of mothball

*Option 2: Disadvantages*

47. Very high cost – significant shareholder support required over many years
48. Uncertain future sustainability of business
49. Loss of 67 jobs

**Option 3: Mothball the business with a view to exploring feasibility of alternative options for the company's assets**

50. Under this option, DRL would again be "mothballed", but the possibility of operating train services on the Taieri Gorge line in future would be removed.
51. As in option 2, the majority of DRL's staff would be made redundant and some assets would be divested. Approximately five staff would be retained, at least initially, to maintain assets.

52. DRL could be maintained as a stand-alone entity, or the remaining five staff and assets could be transferred into Dunedin Venues Management Ltd (DVML). This would offer reduced costs by leveraging DVML's current cost base and governance, and DVML have existing expertise in the tourism sector and marketing. This would need to be carefully considered and more analysis undertaken to ensure it did not impact negatively on DVML's business.
53. Mothballing would significantly reduce DRL's current costs and retain the company's assets in the short term, while DRL/DVML and DCHL explored alternative uses for those assets. Alternative uses might include:
- a. [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]
  - b. [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]
  - c. [REDACTED]

[REDACTED]
54. We anticipate these options could be explored within 3-4 months.
55. A key component of this option is to discontinue rail activity on the Taieri Gorge line in view of the cost of deferred maintenance.
56. If those alternative uses were not feasible, and if no other options were identified, then (in consultation with Council) plans may revert to Option 1, with remaining assets divested and staff made redundant.
57. Estimated costs of Option 3 are set out below:

	Quarter to Jun 2020	18 months to Dec 2021	Years 3-10	Total
<b>DRL (or DVML) Cost</b>	\$1.53m	\$1.05m	[REDACTED] [REDACTED] [REDACTED] [REDACTED] [REDACTED]	[REDACTED] [REDACTED]
<b>DCHL cost to clear DRL debt</b>	\$2.28m	-	[REDACTED]	[REDACTED]
<b>Total</b>	<b>\$3.81m</b>	<b>\$1.05m</b>	[REDACTED]	[REDACTED] [REDACTED]

58. The \$1.53m cost to DRL in the next quarter comprises redundancy costs, holiday pay and booking refunds. Again, this figure is subject to some change depending on the balance of the company's debtors and creditors, GST and tax (etc) at the time of closure.
59. The cost to December 2021 is based on estimated mothball period costs (primarily staff costs) of \$0.7m per year. Depending on decisions about sub-options, that cost may be further reduced after several months (for example, if train operation possibilities were ruled out).

60. [REDACTED]  
[REDACTED]  
[REDACTED]
61. Clearing of DRL's debt has been included, although in theory this debt could remain with DRL (or DVML) while in mothball.
62. If DRL was maintained as a stand-alone entity then \$1.522m equity remains in DCHL's accounts. If DRL was transferred to DVML, this equity investment would add to the investment in DVML in DCHL's accounts. Either way this equity would be affected by impairment of assets noted under Option 2.
63. Council would need to provide funding for mothballing costs (estimated \$1.05m to December 2021) if it wished to pursue this option. Any investment in future options [REDACTED] would need to be subject to a separate business case and approval process.

#### *Option 3: Advantages*

64. Allows more time for consideration of alternative use of DRL's iconic assets without high ongoing staff cost
65. Retains five jobs, at least short term

#### *Option 3: Disadvantages*

66. Potential additional 3-4 months of cost if options are explored and found unfeasible
67. Loss of 69 jobs
68. Further options identified would require their own cost/benefit analysis.

#### *Comparison of options*

69. The total estimated costs of the three options are summarised below for reference:

	Quarter to Jun 2020	18 months to Dec 2021	Years 3-10	Total
<b>Option 1:</b> Close the business	\$3.91m	-	-	<b>\$3.91m</b>
<b>Option 2:</b> Mothball for future re-opening of train services on the Taieri Gorge line	\$3.71m	\$1.35m	\$8m to 11.5m	<b>\$13.06m to \$16.56m</b>
<b>Option 3:</b> Mothball to explore feasibility of alternative options (excluding Taieri Gorge line)	\$3.81m	\$1.05m	[REDACTED] [REDACTED] [REDACTED] [REDACTED]	[REDACTED] [REDACTED]

### **DUNEDIN CITY HOLDINGS RECOMMENDATION**

70. As noted above, DCHL recommends Option 1: close the business.
71. DCHL appreciates that its shareholding in DRL is not a commercially driven investment, or one that is focussed on financial returns or dividends. DRL makes a valued contribution to Dunedin in other ways, including adding to the city's tourist offering, delivering economic benefit and as a part of the city's heritage.
72. However, DCHL expects subsidiary and associate companies to at least be sustainable. Option 1 is the only option that delivers that. Option 2 and Option 3 will both require

ongoing shareholder support which DCHL is not in a position to provide without compensation from Council.

## **NEXT STEPS**

73. We would appreciate the opportunity to discuss our recommendation with Council.
74. Following that, DCHL will engage with OETT as the company's other shareholder.
75. Once a path forward has been agreed between shareholders, DCHL will report back to Council. DRL will lead planning for implementation, including (among other things):
  - a. Union engagement and human resources activity
  - b. Relevant arrangements for assets
  - c. Relevant companies office requirements
  - d. Communications planning.
76. DCHL will work closely with DRL during this time and will keep Council briefed as required.

Keith Cooper  
Chair

Jemma Adams  
General Manager