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25 May 2015

Dear Sirs

**Addendum to our report in connection with the New Zealand International Convention Centre**

**1. Background**

The Ministry of Business, Innovation and Employment ('Ministry'), on behalf of the Crown, and SkyCity Entertainment Group Limited ('SkyCity') (together 'the parties') have agreed the basis on which SkyCity will design, develop, construct, maintain and operate the New Zealand International Convention Centre ('NZICC'). In exchange, the Crown will provide certain concessions (including regulatory changes) to SkyCity (the 'proposed transaction').

KordaMentha provided a report to the Ministry and SkyCity on our independent and impartial assessment of the reasonableness of the financial evaluation of the proposed transaction and the methodology applied to valuing it, dated 10 May 2013 ('the Report').

At the time of the Report, it was envisaged that the total project cost for acquiring land and constructing the NZICC would be \$402 million.

As a result of detailed design plans and further discussion between the Ministry and SkyCity, over the last two years, both parties have agreed to some further variations to the proposed transaction. The specific amendments are identified in a letter from SkyCity to the Ministry dated 13 May 2015 ('the Letter'). The Letter sets out the agreed position of SkyCity and the Ministry as to the assessed quantum of the changes to the proposed transaction.

**2. The Letter**

The Letter sets out the Ministry and SkyCity's view that the net result of the specific changes identified is that SkyCity will be making a further contribution totalling \$27.4 million. In return, no additional concessions are being provided to SkyCity.

The assessed further contribution is summarised at Table 1.



**Table 1: Basis for SkyCity’s proposed increase in contributed amount**

	2015 Value		2013 Value	
	Detail	Total	Detail	Total
Hobson Street site (2,821m <sup>2</sup> )	\$17.5 million		\$13.3 million	
Less: Wellesley Street site (1,030m <sup>2</sup> )	(\$5.7 million)		(\$5.2 million)	
<b>Valuation difference</b>		<b>\$11.8 million</b>		<b>\$8.1 million</b>
<b>NPV of non-gaming on-spend due to hotel and laneway</b>		<b>\$4.4 million</b>		<b>\$3.8 million</b>
Laneway construction	million		million	
Shell fit out for food and beverage, retail and excess office space in the NZICC perimeter and laneway	million		million	
Additional contribution to car park construction	million		million	
Project Director cost allowance	million		million	
Other (non-cash) contribution by SkyCity including artwork	million		million	
<b>Other additional contribution by SkyCity</b>		<b>\$11.2 million</b>		<b>\$11.2 million</b>
<b>Total additional contribution by SkyCity</b>		<b>\$27.4 million</b>		<b>\$23.1 million</b>

Key components of the additional contribution are:

- A reallocation of land to be utilised by the NZICC. As a result of the latest designs, additional land at Wellesley Street (valued at \$5.7 million) will now be utilised but land at Hobson Street (valued at \$17.5 million) will no longer be used by the NZICC. Instead, SkyCity intends to build a hotel on this site as well as a laneway for the NZICC.
- The net present value ('NPV') of the benefit to SkyCity from the hotel and laneway generating additional on-spend at restaurants and facilities estimated by the parties at \$4.4 million.
- Other additional contribution agreed at the Concept Design stage includes additional contributions by SkyCity to the NZICC construction as well as artwork, valued by the parties at \$11.2 million and summarised above.

Other key issues to note in the Letter are:

- SkyCity and the Ministry have agreed that the hotel which may be built by SkyCity is peripheral to the proposed transaction and that any NPV benefit to SkyCity from building the hotel is not relevant to the assessment of the benefits of the proposed transaction because it is an optional project to be fully funded by SkyCity, except to the extent that hotel guests contribute to the on-spend for SkyCity as discussed below.
- SkyCity and the Ministry have agreed that the value of the gaming concessions has already been assessed as part of the original evaluation of the proposed transaction and the reallocation of land to be utilised the NZICC has no impact.

In addition to the information in the Letter, we understand that SkyCity has agreed to meet a project cost (land and building the NZICC) of \$430 million with any cost over-runs being met by SkyCity.

### 3. Scope of work

The Ministry and SkyCity have asked KordaMentha to prepare a short-form letter as an addendum to the Report ('the Addendum').



The Addendum is to set out our findings of an independent review of the assessed quantum of the specific changes to the proposed transaction identified in the Letter.

KordaMentha have specifically not been asked to address any other issues or revisit our earlier analysis. Specific areas excluded from our scope include the NPV benefit of the possible hotel and any impact to SkyCity from reallocating land utilised by the NZICC.

We also note that we have focussed our review of the NPV benefit to SkyCity from on-spend due to the hotel and laneway. We are not qualified to opine on the value of land, construction activities and artwork and reviewing the Ministry and SkyCity's assessment of the value of these contributions is outside the scope of our work.

This Addendum does not provide assurance that the assessed quantum of the additional contribution is reasonable. Instead, the Addendum represents the results of our indicative review, based on the limited time available, and notes whether any matters have come to our attention which impact on the reasonableness of the quantum assessed by SkyCity and the Ministry.

#### 4. Our findings

Based on the scope of work we have undertaken, matters that have come to our attention which impact on the reasonableness of the quantum of the additional contribution assessed in the Letter (i.e. \$27.4 million) include:

The reported additional contribution is based on values as at 2015. We note that it is inherently difficult to compare values assessed at 2013 in the Report with values assessed in 2015. However, unless all of the underlying analysis were updated this is necessary.

Issues with the NPV of on-spend as a result of the hotel and laneway include:

- There are cogent arguments for a range of discount rates that could be applied to assess the NPV. SkyCity and the Ministry have adopted a discount rate of 10% based on SkyCity's weighted average cost of capital ('WACC'). Arguably, the discount rate could be as high as 17% based on a hurdle rate for the NZICC, on the premise that these additional cashflows would only be earned in the event that significant convention centre business is captured. However, given the relatively small sums involved relative to the size of the proposed transaction (with a build cost of approximately \$430 million) we do not consider the approach taken to be unreasonable. It is akin to saying that the incremental cashflows are relatively small and would be valued as a bolt-on to SkyCity's existing business.
- For comparison purposes we note that NPV at 2013, which is more comparable with the calculations set out in the Report is \$3.8 million using SkyCity and the Ministry's proposed discount rate of 10%.

Other additional contribution by SkyCity includes a number of items where we are unable to review the assessed quantum. It is also unclear that the benefits are solely to the NZICC and not, at least in part, shared by SkyCity. However, the other additional contribution is in addition to the NZICC's land and building costs of \$430 million and any change to the assessed value is unlikely to affect our summary, set out below.

Rather than following the approach adopted by the parties, our preferred way of analysing the additional costs to SkyCity offset by benefits to SkyCity is set out in Figure 1 below:

**Figure 1: Cost/Benefit to NZICC and SkyCity**

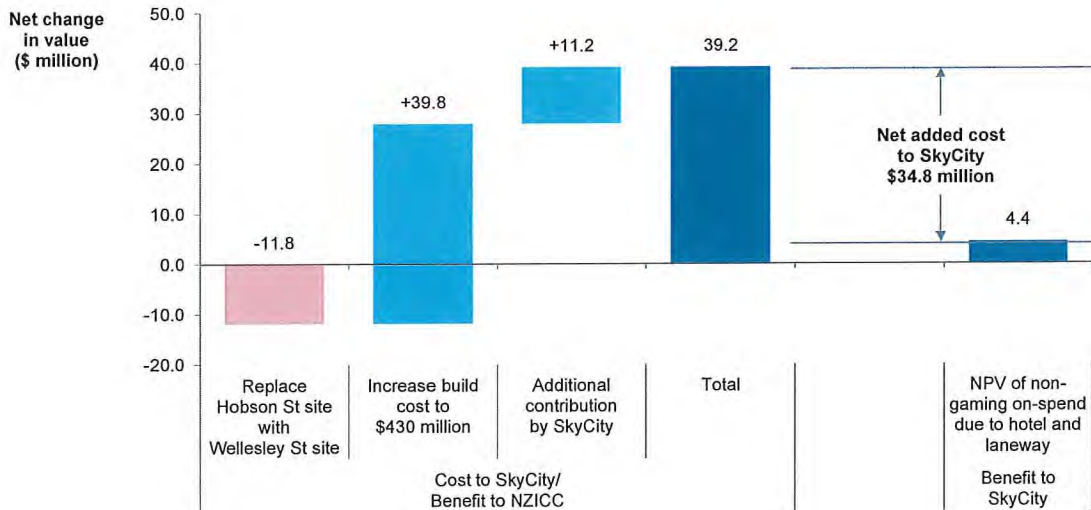


Figure 1 shows:

- Additional costs to SkyCity are:
  - the reallocation of land being used by the NZICC;
  - additional building works that result in a total project cost (land and buildings) of \$430 million (plus potential cost over-runs); and
  - other additional contribution by SkyCity (e.g. artwork).
- Additional benefits to SkyCity are:
  - the NPV of non-gaming on-spend due to the hotel and laneway.

## 5. Summary

Based on the scope of work undertaken, the impact of the changes to the proposed transaction is that the Crown is receiving more contribution from SkyCity than was envisaged in the Report.

Since we issued the Report, no additional concessions have been provided by the Crown.

We note for completeness we have not been asked to consider other events that may have changed since the Report. We have not reviewed SkyCity's reasons for increasing its investment outlay.

Yours faithfully



Grant Graham  
KordaMentha