THE TREASURY
Kaitohutohu Kaupapa Rawa

Reference: 20100105

21 June 2010

Dear Mr Prentice

Thank you for your Official Information Act request, received on 9 April 2010. Following consultation you agreed that the request should be as follows:

> *"This is an OIA request for all documents created by COMU, Treasury, and CCMAU since November 2008 on the subject of options for changing the ownership of Crown-owned assets by selling these assets, partially selling them, or having them issue bonds."*

As I indicated in my letter extending the deadline for responding to your request, we have interpreted your request as relating to Crown-owned agencies monitored by COMU. In the interests of clarity I should also note that this response does not cover situations involving a change of ownership between Crown agencies where the Crown remains the ultimate owner (including for example the recent transfers between electricity SOEs and the Crown) and situations involving a change of ownership in the context of Treaty of Waitangi settlements.

Information being released

Please find enclosed the following documents:

Item	Date	Document Description	Decision
1.	19.12.08	Treasury Report T2008/2368: Improving the performance of State Owned Enterprises	Some information withheld under s 9(2)(a) and (g)(i)
2.	27.1.09	CCMAU Report: Kiwibank: Meeting with Minister for SOEs on 28 January 2009	Some information withheld under s 9(2)(a) and (b)(ii)
3.	Feb 2009	Presentation to Ministers: Enhancing SOE Performance	Some information withheld under s 9(2)(b)(ii) and (g)(i)
4.	13.2.09	CCMAU Report: New Zealand Post Ltd: Aide Memoire re Potential Debt Listing on New Zealand Debt Exchange	Some information withheld under s 9(2)(a) and (ba)(i)

I have decided to release the documents listed above, subject to information being withheld under one or more of the following sections of the Official Information Act, as applicable:

- section 9(2)(a) - to protect the privacy of natural persons, including deceased people;

- section 9(2)(b)(ii) - to protect the commercial position of the person who supplied the information, or who is the subject of the information;

- section 9(2)(ba) - to protect information that is subject to an obligation of confidence, or that was or could be provided under legal compulsion, and where releasing the information would either prejudice the supply of similar information in the future - and it is in the public interest that such information should continue to be supplied - or would damage the public interest in some other way; and

- section 9(2)(g)(i) - to maintain the effective conduct of public affairs through the free and frank expressions of opinion.

Information to be withheld

There are an additional eight documents covered by your request that I have decided to withhold in full under sections 9(2)(b)(ii) and (g)(i) of the Official Information Act 1982, as cited above, or sections 9(2)(f)(iv):

- advice still under consideration, section 9(2)(f)(iv) - to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials.

In making my decision, I have considered the public interest considerations in section 9(1) of the Official Information Act.

This fully covers the information you requested.

You have the right to ask the Ombudsman to investigate and review my decision.

In relation to the information withheld, I would like to clarify that the Government has commissioned no work on the sale or partial sale of Crown assets monitored by COMU and that we have provided no advice. For the most part, the withheld documents respond to specific issues connected with individual Crown agencies, raised by the agencies themselves or third parties. Two further withheld documents have only small parts that are relevant as part of higher-level pieces about the possible future of the Crown's balance sheet. Finally, there are two internal papers commissioned by Treasury's Executive Leadership Team, still in draft form, which cover SOE ownership, including issues of concern to the public connected with privatisation. This was the work John Whitehead referred to on TVNZ's Q+A programme on 30 May 2010.

Yours sincerely

Nic Blakely

pp JAMES CUNNINGHAM

Nic Blakeley
Manager, Sector Balance & Performance
for Secretary to the Treasury

COMMERCIAL-IN-CONFIDENCE

RECEIVED
2 3 DEC 2008
MINISTERIALS

Hon Bill English
ORIGINAL

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THE TREASURY
Kaitohutohu Kaupapa Rawa

Treasury Report: Improving the performance of State-Owned Enterprises

Date:	19 December 2008	Report No:	T2008/2368

Action Sought

	Action Sought	Deadline
Minister of Finance (Hon Bill English)	Note contents	None
Minister for State-Owned Enterprises (Hon Simon Power)	Note contents	None

Contact for Telephone Discussion (if required)

Name	Position	Telephone	1st Contact
Chris White	Manager, Climate Change, Energy and Commercial Operations	[Withheld under s 9(2)(a)]	✓
Juston Anderson	Senior Analyst, Climate Change, Energy and Commercial Operations		

Minister of Finance's Office Actions (if required)

None.

Enclosure: No

2 2 DEC 2008

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MINISTERIALS

19 December 2008 SE-1-2

Treasury Report: Improving the performance of State-Owned Enterprises

Executive Summary

Earlier this week the Minister for SOEs signed outlook letters to SOEs. These letters gave SOEs a strong message on the need to improve their performance and productivity.

We have a number of suggestions for improving SOE performance which we would like to discuss with Ministers, before the SOE business planning round begins in early 2009.

In our view, while the SOE model is sound, the operation of the model, and the performance of SOEs, has eroded over time. We think the model needs to be reinvigorated.

While recognising Government policy, and the broad political support for retaining state control and ownership of current commercial assets, we think better performance will be achieved by moving towards greater private sector involvement in SOEs. There are a range of options for achieving this while retaining 100% government ownership.

As well as greater private sector involvement in SOEs, we think there is a need for other steps to improve SOE performance:

- Improve the quality of, and possibly the process for, appointments to SOE boards;
- Put pressure on SOEs to increase their gearing (which as a side-effect will result in greater dividends being paid to the Crown). The way that Ministers think about SOE gearing and special dividends may link to the wider Crown balance sheet management issues that Ministers are interested in;
- Encourage SOEs to be more transparent with the public about their performance; and
- Improve the monitoring of SOEs.

The body of this report provides further details of our proposals.

Recommended Action

We recommend that you **note** the contents of this report and discuss it with officials.

Chris White
Manager, Climate Change, Energy and Commercial Operations
for Secretary to the Treasury

Hon Bill English
Minister of Finance

Hon Simon Power
Minister for State Owned Enterprises

Treasury Report: Improving the performance of State-Owned Enterprises

Greater private sector involvement in SOEs will improve performance

1. SOEs are exposed to most of the commercial disciplines faced by private sector companies, and as a result, the performance of SOEs has been significantly better than the performance of government trading organisations prior to the SOE Act.

2. However because their shares are not publicly tradable:

    - SOE management do not face the threat of takeover if the SOE is underperforming; and
    - SOE performance is not subject to the same level of scrutiny by the public and by market participants.

3. Given the broad political support for the government retaining control and ownership of the current SOEs, SOEs will not face the threat of takeover.

4. However, there are options to improve the scrutiny of SOEs by the public, while retaining Government control and ownership. In our view greater private sector involvement with and scrutiny of SOEs would be the most effective way of improving SOE performance.

5. This is backed up by comments from two [Withheld under s 9(2)(g)(i)] Both said that they found feedback and scrutiny on their public companies from informed commentators was highly valuable, and that they did not get the same level and quality of feedback from officials on their SOEs.

6. There are a number of options for encouraging greater private sector involvement in SOEs.

7. One option is to encourage SOEs to issue bonds to the public. At present SOEs raise their debt from institutions. Genesis has recently issued bonds to the public, and we understand Meridian is planning to do the same in 2009. We think this should be encouraged.

8. However, the gains from issuing public bonds would be relatively modest. Holders of SOE debt do not share in any gains in SOE performance, and only share in the downside if the SOE were to fail and could not repay the bonds. Therefore they have limited incentives to scrutinise SOEs.

9. Other options would not be consistent with the Government's policy to retain 100% ownership of SOEs. SOEs could be allowed to partially list their subsidiaries on the stock exchange. A number of SOE have already entered into joint venture subsidiary arrangements with private sector partners (NZ Post's courier business and Solid Energy's Spring Creek mine are the two main examples). It is a relatively small step in substance to move from the Government owning less than 100% of an SOE subsidiary, to non-Government owned shares in a subsidiary being publicly tradable. Again, we think the gains from this would be relatively modest, given that the vast majority of SOE value is in the SOEs themselves, rather than their subsidiaries.

10. A further step would be to partially list some SOEs on the stock exchange – in the same way as Air New Zealand is partially listed. This in our view would deliver the greatest performance gains (short of fully privatising some SOEs, for which there is no public or political support). The gains would come from: better monitoring and feedback to the SOE from the private sector investors and their agents, and from the SOE's share price; more public transparency from the SOE; and greater constraints on non-commercial influence in the SOE from the government.

11. Only large SOEs would be suitable for partial listing – small and medium sized SOEs would not attract serious private sector monitoring. However the bulk of the Crown's equity is concentrated in the largest SOEs.

12. Again, we note that this is not consistent with Government policy, and we do not intend undertaking any work on partial listing of SOEs.

Appointments to SOE Boards are critical

13. Appointments to SOE Boards are the single most important lever that Ministers have for influencing SOE performance. The Minister for SOEs is responsible for SOE Board appointments.

14. Our view, supported by a number of external commentators, is that the quality and performance of people appointed to SOE Boards could be improved. Obviously this means changes to the individuals appointed to SOE Boards (Treasury has no involvement in this), but it could also mean changes to the process for appointing SOE Boards.

15. We suggest two potential options for changes to the process:

- Ministers appoint only the Chair of the SOE, who is then responsible for selecting the other board members, subject to Ministerial and Cabinet signoff (the Air NZ model); or
- Ministers appoint Board members nominated by an independent committee (the Guardians of NZ Super model).

16. We prefer the Air NZ model. However this approach places much more weight on the selection of an appropriate Chair for each SOE, and strengthens the power of the Chair relative to other Board members.

17. We also think that the size of SOE boards should be reduced over time from the current 7-9 directors to 5-7 directors.

Increasing SOE gearing will encourage better performance

18. There are strong arguments for the Government to put pressure on SOEs to increase their gearing - i.e. encouraging SOEs to borrow more from the private sector and pay special dividends to the Crown.

19. Higher debt levels put increased pressure on SOEs to perform, by committing a fixed part of their future cashflow to debt servicing, meaning they must focus more on core business profitability, and on selecting new investment projects carefully.

20. Low debt levels may encourage complacent behaviour by SOEs, for example misjudging business risks because their strong balance sheet allows Boards to think they can ride out any problems, or a greater willingness to expand into new and risky areas of business.

21. Higher debt levels do put SOEs under greater financial stress and increase the chance that they will require additional capital from the government. High debt levels may also constrain SOEs from making value-adding investments without seeking additional equity from the Government. SOEs have been very reluctant to ask Ministers for equity even in a time of strong Crown financial performance and encouraging signals from Ministers.

22. The credit crisis also tempers our advice around increasing SOE gearing. The expected recession will impact on the finances of SOEs, reducing their ability to take on debt (although it may also lead to them reducing or delaying planned capital expenditure). However since most large SOEs are utilities their finances are likely to be less affected by an economic downturn. So far we have had no indication that as a result of the credit crisis the large SOEs are having difficulty raising debt, or will have to pay significantly higher interest rates on their debt.

23. All of this means there is a need to strike an appropriate balance in SOE capital structures between the incentives to perform and the risks of too much debt.

24. Shareholding Ministers and SOEs are likely to have different perspectives on the appropriate balance. SOEs will favour lower than optimal gearing levels, as that reduces the personal risk to directors resulting from company failure, increases the SOEs operational flexibility, and reduces the likelihood of having to ask shareholders for additional capital.

25. Without sustained and effective pressure from Ministers, SOEs will tend to err on the side of having too little debt on their balance sheets.

26. Increasing SOE gearing will have fiscal benefits to the Crown. It provides additional cash for the core Crown to use as it wishes, either on capital spending or to reduce gross core Crown debt. This is at the cost of that cash not being available to SOEs to use as they wish.

27. The fiscal gains to the core Crown from increased gearing could be significant, although they would be one-off gains rather than ongoing improvements, and might be partially offset by the need to provide some equity to more highly geared SOEs in the future if they wished to undertake significant capital spending.

28. In our view increasing SOE gearing should be undertaken as part of a strategy to deliver a sustained increase in SOE performance. The short-term fiscal benefits should be seen as a side-effect, not the driver of the gearing policy.

29. Past efforts to influence SOEs to increase their gearing through Ministerial persuasion have had limited success. We suggest that if persuasion continues to be ineffective, Ministers should consider directing an SOE or SOEs to pay a special dividend.

30. Ministers have never directed an SOE over dividends in the past. Such a direction could undermine the Board's accountability for running an SOE, and so Treasury has been reluctant to recommend this in the past. As part of wider discussions on SOE policy we informally consulted two senior SOE Chairs on whether such a direction would be appropriate, and received mixed feedback. One Chair said that capital structure was quite rightly a matter for owners to decide and therefore he had no concerns with Ministers directing an SOE on this issue; the other said that he would see it as undermining the Board – in his view a good Board would have the shareholder's interests at heart and so should not need to be directed.

Improved monitoring of SOEs is required

31. There are two aspects to monitoring of SOEs:

- Monitoring by officials, on behalf of Ministers; and
- Public monitoring based on disclosure by the companies.

Monitoring by officials

32. Monitoring by officials is an input into shareholding Ministers relationship with SOEs, and the views expressed by Ministers to the companies. This monitoring is generally not made public as it relies on commercially sensitive information supplied by SOEs.

33. Improving monitoring by officials requires better analysis, particularly more benchmarking of SOEs against comparable companies, and more comprehensive financial performance analysis in the business planning round, in the quarterly SOE performance reporting to Ministers, and in commenting on SOE annual reports.

34. Monitoring is of no use unless it changes SOE behaviour. Therefore improved monitoring needs to result in clear performance targets and expectations set for the SOEs by Ministers. Ministers also need to be willing to take action if these targets and expectations are not met by the SOEs.

35. There is an opportunity for greater private sector involvement in monitoring of SOEs, building on private sector experience in monitoring listed companies. Our engaging private sector equity analysts to carry out SOE valuations is an example of what can be done here, although the value of this is dependent on the information the SOEs make available to the public.

36. There is also a question of to what extent the views of Ministers and the analysis by officials can be made public, without compromising the SOE's commercial position.

Monitoring by the public

37. Public monitoring of SOEs is currently very limited and is generally below what would be expected for publicly listed companies. SOE annual reports and SCIs currently provide insufficient information to enable an informed assessment of SOE financial performance. We are concerned that this lack of public disclosure does not sufficiently expose SOEs to public scrutiny, analysis and informed comment.

38. SOEs need to be encouraged to improve the quality of their public disclosures. This will be difficult, as, unlike listed companies, SOEs have incentives to keep information about their performance confidential, particularly unflattering information. In our view an SOE's willingness to make information public, and to subject itself to outside scrutiny and criticism, is a strong indicator of whether or not it is performing well.

39. SOEs should publicly provide greater analysis of their financial performance, particularly an assessment of their performance against their previous targets (e.g. in the SCI) and benchmarking against their competitors and comparable companies. SOEs also need to provide more credible estimates of their commercial value on an annual basis, so that changes in this value over time can be used to assess their performance.

40. To promote public participation and review of SOE performance, the level of disclosure should be comparable to large publicly listed companies. SOEs also need to make greater use of less formal disclosure routes such as annual meetings, investor presentations and public announcements of any material variances in expected profitability.

41. Insufficient public disclosure by the SOEs could be balanced by greater public dissemination of information and analysis by officials (subject to the commercial sensitivity test).

Which SOEs?

41. The level and degree of performance disclosure should be proportionate to the scale of the SOE. Therefore improving the level of public disclosure about financial performance should be targeted at the larger SOEs: Genesis, Meridian, Mighty River Power, NZ Post, Landcorp and Solid Energy. Together, these six SOEs make up around 87% of the total SOE portfolio by value[1] (excluding NZRC, which is technically an SOE but is not fully commercial).

42. The other large SOE is Transpower, which is a regulated monopoly subject to oversight by the Electricity Commission. Transpower is between 5 and 10% of the SOE portfolio, depending on whether revenue, assets or equity is the measure.

[1] These six SOEs made up 87.3% of total SOE revenue, 87.7% of SOE assets and 86.7% of SOE equity for the year ended 30 June 2008.

ccmau
CROWN COMPANY MONITORING ADVISORY UNIT
TE MATA AROTURUKI RAWA A TE KARAUNA
Protecting and enhancing shareholder value

Kiwibank: Meeting with Minister for SOEs on 28 January 2009

Date	27 January 2009	**Priority**	Urgent
Security level	Commercial: In Confidence	**Reference**	NZP-032/A71808

Minister	**Action sought**	**Deadline**
Minister of Finance	Approve recommendations.	28 January 2009
Minister for State Owned Enterprises	Approve recommendations.	28 January 2009
Associate Minister of Finance (Hon Steven Joyce)	Approve recommendations.	28 January 2009

Report summary

- The Minister for SOEs is meeting with the chief executive of Kiwibank, Sam Knowles, on 28 January 2009 as a follow up to the meeting the Minister for SOEs had on 14 January 2009 with the Chair and chief executive of New Zealand Post Ltd (NZ Post). - Jim Bolger is also attending
- The Minister for SOEs has asked Kiwibank to brief him on two issues: [Not Relevant] and the details of the proposal by NZ Post to raise $150-200 million via a bond issue.
- Given that the funding options outlined in the 14 January meeting are primarily intended to fund growth opportunities for Kiwibank and, at the same time, preserve NZ Post's current Standard and Poor's (S&P) rating, NZ Post has been asked [Withheld under s 9(2)(b)(ii)] This is unlikely to be prepared in time for the 28 January meeting, but Sam Knowles will probably provide an update on developments, [Not Relevant]

Contacts

James Cunningham	Manager - Communications, Services & Infrastructure - CCMAU	[Withheld under s 9(2)(a)]	**First contact**
Paul Goodhead	Senior Advisor - Communications, Services & Infrastructure - CCMAU		

Ministers' comments

Please return this document to CCMAU

Kiwibank: Meeting with Minister for SOEs on 28 January 2009

Purpose

1. This briefing provides background information for the Minister of SOEs' meeting with Sam Knowles, chief executive of Kiwibank, on 28 January 2009.

Introduction

2. At the meeting with the Minister for SOEs on 14 January, NZ Post indicated (amongst other topics) that it:

[Not Relevant]

b signalled an intention to request $100 million injection of equity from the Crown to supplement a market debt-raising of $150-200 million, in order to replace some current debt, fund the NZ Post Group's growth, and at the same time preserve the current S&P rating of AA- (stable).

[Not Relevant]

4. Sam Knowles was not present at the meeting on 14 January and the meeting with him on 28 January was organised to cover the debt-raising plan [Not Relevant] in more depth.

[Not Relevant]

[Not Relevant]

[Not Relevant]

NZ Post's funding plans

11. NZ Post has indicated that the total required funding for its expansion plans would be in the order of around $300million. However, because of the need to preserve its S&P rating, this funding cannot be achieved through conventional debt-raising in the marketplace.

12. NZ Post has considered various alternative funding options and its preferred funding route is a combination of a capital injection from the Crown (~$100million) and a listed Hybrid Bond (~$200million).

13. The Hybrid Bond proposed is a long dated, subordinated and low covenant corporate bond with no voting or convertibility (into equity) rights for the holders. The bond allows the issuer to suspend interest payments for up to 5 years (these then accumulate and must be paid in full at that time). [Not Relevant]

[Not Relevant] The other main feature is that there is a step up in the interest rate payable after five years to incentivise the issuer to either re-market or redeem the notes – this means that economically the bond can be priced as a medium-term rather than a long-term instrument.

14. In effect the above features of the Hybrid Bond allow S&P to recognise 50% of the proceeds as equity capital, which is positive for NZ Post's overall credit rating. However, to ensure it is seen as permanent equity (by S&P and the senior bond holders), any redemption or re-marketing by NZ Post must ensure a similar equity content is maintained. That is, it needs to either redeem the notes through the issuance of new equity capital or re-market a similar Hybrid instrument. There is therefore, a risk that the Crown may need to provide some further capital at the 5 year step up point, but only if there is no market for a new Hybrid Bond, the Crown wants to retain 100% ownership, and NZ Post cannot continue with the existing bonds (at the stepped up interest rate). We understand that there are also a number of other options available to NZ Post that would reduce the possibility of a future equity injection being needed at the step up point.

15. NZ Post's advisor, ABN AMRO, believes there would be considerably higher interest in the offering (and therefore pricing advantages for NZ Post) if it is listed on the New Zealand Debt Exchange (NZDE). Because this allows easier trading of the note, the attractiveness for investors is heightened by listing. The company has given officials examples of similar offerings by other companies showing that listing is the norm for these types of instruments.

16. Officials see merits in the listing option, not just because of the marketing advantages for NZ Post, but also because the extra market scrutiny will add another element of accountability and transparency to complement the monitoring already carried out by officials.

17. However, listing would require NZ Post to comply with the NZDE listing rules, and aspects of these rules clash with requirements NZ Post needs to meet under the State Owned Enterprises Act 1986 (SOE Act). NZDE's dates for publishing half-year and annual reports are about one month earlier than the dates for delivery to Ministers and tabling in the House of Representatives. Furthermore, NZDE's continuous disclosure rules require 'material information' to be communicated to the exchange before any other party (including shareholding ministers).

18. Officials and NZ Post have explored these issues and our initial view is that the potential hurdles are manageable. NZDE has the ability to give exemptions/waivers, and has indicated a willingness to consider NZ Post's situation. Indeed, the NZDE may be very willing to be flexible, given its keenness to see more SOE issues listed on its exchange. NZ Post has also analysed 'material' events in the recent past to see which, if any, would have been required by the continuous reporting requirement to be reported to the

market before Ministers[2]. In all cases where we would require it, NZ Post would be able to discuss the matters with Ministers and officials up to the point where events became 'sufficiently certain' – this would allow 'no surprises' discussions, consultation, and feedback, as per the current practice. Discussions would need to remain confidential (as they are now), unless NZ Post made public announcements (which it tends to do on all matters that are not commercially sensitive).

19. However, Parliamentary processes such as the Finance and Expenditure Select Committee's (FEC's) Review may need to be carefully managed. For instance, when Air New Zealand (which is subject to NZ Stock Exchange rules) is called to the FEC, specific instructions are sent to Committee Members about what can and cannot be asked and answered without breaching Air New Zealand's listing obligations.

20. Our conclusion is that reporting requirements should not stand in the way of listing, if listing has significant commercial advantages for NZ Post. We would expect NZ Post to negotiate exemptions/waivers with NZDE, particularly around reporting dates for half-year and annual reporting, and it would be willing to do this.

21. NZ Post has also indicated that it is maintaining ongoing discussions with S&P throughout this planning stage. [Withheld under s 9(2)(b)(ii)]

22. Finally, there is a chance that issuance of the Hybrid Bond could be portrayed as the Crown transferring part of its equity interest to private sector bond holders. However, we note that:

a The Crown retains 100% ownership of the shares in NZ Post

b The holders of the notes have no control, voting or convertibility rights.

Nevertheless, the public communication of this issue would need to be managed carefully by NZ Post, and potentially, Ministers.

Summary

23. [Withheld under s 9(2)(b)(ii)]

[2] These events include presentation of draft business plans to officials, quarterly reporting, negotiation and set up of Australian joint venture (Express Couriers Australia (Proprietary) Ltd), Kiwibank's profit announcement, fair value adjustments to accounts, sale of Auckland Mail Centre site, pricing changes, Commerce Commission investigations, sudden falls in postal volumes etc.

24. In principle, officials support NZ Post's plan to use a Hybrid debt instrument and to list that instrument, if its final analysis concludes that these are the best options.

Consultation

25. The Treasury has been consulted and agrees with the content of this report.

Recommendations

26. We recommend that you:

[Not Relevant]

c **note** that officials support, in principle, NZ Post's use of a Hybrid Bond for debt-raising and also the listing of that instrument on the New Zealand Debt Exchange, provided that all issues can be resolved satisfactorily and there is no diminution in shareholding Ministers' right and powers under relevant legislation

d **agree** that, should the Hybrid Bond issue proceed (and, as this raises some policy issues), then the Prime Minister and Cabinet colleagues should be briefed on these issues

(agree / disagree)	(agree / disagree)	(agree / disagree)
Minister of Finance	**Minister for State Owned Enterprises**	**Associate Minister of Finance (Hon Steven Joyce)**

e **note** that, if required, CCMAU could draft an aide memoire on the Hybrid Bond issue for the Minister for SOEs in advance of the regular Senior Ministers' meeting. Alternatively, we could draft a Cabinet Paper if this was thought necessary.

James Cunningham
Manager - Communications, Services & Infrastructure
CCMAU

Bill Eng

Hon Bill English	Hon Simon Power	Hon Steven Joyce
Minister of Finance	**Minister for State Owned Enterprises**	**Associate Minister of Finance**

Recommendations

26. We recommend that you:

[Not Relevant]

c **note** that officials support, in principle, NZ Post's use of a Hybrid Bond for debt-raising and also the listing of that instrument on the New Zealand Debt Exchange, provided that all issues can be resolved satisfactorily and there is no diminution in shareholding Ministers' right and powers under relevant legislation

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(agree / disagree)	(agree / disagree)	(agree / disagree)
Minister of Finance	**Minister for State Owned Enterprises**	**Associate Minister of Finance (Hon Steven Joyce)**

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James Cunningham
Manager - Communications, Services & Infrastructure
CCMAU

Hon Bill English	Hon Simon Power	Hon Steven Joyce
Minister of Finance	**Minister for State Owned Enterprises**	**Associate Minister of Finance**

Enhancing SOE performance

Presentation to Ministers
By CCMAU
February 2009

Agenda

- Objectives
- Drivers of improved performance
- Other related matters
- Discussion
- Authority to proceed

Objectives

- Drive improved performance in the SOE portfolio of companies through:
  - Stronger boards
  - Clear and transparent shareholder expectations
  - Consistent and robust performance reviews
  - Robust feedback and clear consequences
- Other related considerations:
  - Commerce Committee recommendations
  - Leveraging of company balance sheets
  - Reduce regulatory barriers and simplify processes
  - Focus at the portfolio level

Stronger boards – *already underway*

- Replace inappropriate/non-performing board appointees
- Appoint according to process
- Ensure all directors have relevant skills and experience, especially appointees to major boards
- Strengthen identification and development of future chairs
- Minister to meet with key boards (eg at business planning time)

Clear and transparent shareholder expectations

- Ministers to set consistent performance targets (eg for increases in equity/value; returns exceeding cost of equity, etc)
- Agree broad classification of companies as * , growth, infrastructure etc and focus companies on that end
- Review business plans/funding requests with this focus in mind
- Stronger use of outlook letters, more informative SCI/business plan discussions
- Require reporting on material subsidiaries
- Promote greater gearing (increased pressure to perform) – one off special dividend

* [Withheld under s 9(2)(g)(i)]

Consistent and robust performance reviews

- Greater public engagement and involvement
- CCMAU publish performance data and critique on website
- CCMAU publish 'league tables' of performance data across the portfolio
- Promote listing of bond issues by the companies
- Continue valuation work on major SOEs
- Commission more analytical work (EVAs, benchmarking)
- Encourage boards to evaluate return on investment of recent major projects notified to or funded by the Crown
- Encourage public AGMs and investor presentations by larger SOEs
- Expand analysis and feedback by officials

Robust feedback and clear consequences

- Ministers/CCMAU give more detailed/frank feedback to companies
- Encourage public comment and feedback
- Minister to attend occasional board meeting, for key SOEs
- More direct engagement with key companies early in the business cycle
- Periodically, look at whole-of-portfolio and cross-portfolio issues/projects
- Concentrate attention more on high importance companies
- Influence boards to put more pressure on managements re gearing and value-enhancing developments

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Commerce Committee Recommendations – *already underway*

Recommendation 1: the CCMAU be required to report annually on the performance of the state enterprise portfolio by aggregating the data it already collects regarding the individual state enterprises.

Recommendation 2: That the CCMAU be asked to consider and report to the Government on the publication of an annual market-based assessment of the recent performance of the state-owned enterprise portfolio, along with a current forward-looking valuation of the portfolio.

Recommendation 3: That Statistics New Zealand be asked to report to the Government on the possibility of including an analysis of the state-owned enterprise portfolio in its annual publication of productivity statistics in the market sector.

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Leveraging of company balance sheets

- On paper, the following companies would appear to have significant capacity for increasing gearing:
    - **Gentailers, TVNZ (not an SOE), Solid Energy, NZ Post, CIAL**
- In principle, companies could make special dividend payments totalling $100+ million without inordinate stress to their balance sheets
- Therefore, we should explore the feasibility of increasing gearing/dividend from selected companies
- The potential benefit of this:

Financial	*Non-financial*
Dividends available for other Crown uses	**Focus the companies on activities that will generate returns**
Balance sheet used for funding for projects	**Ensures discipline around new capital project selection**

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Reduce regulatory barriers and simplify processes

- **Some key barriers:**
    - Land disposal processes
    - Official Information Act
    - Resource Management Act
    - Commerce Act
- **Set up cross-agency workgroups to explore streamlining opportunities**

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Focus at portfolio level

- Categorise companies (growth, *, infrastructure etc)
- Focus some companies back to core business
- Focus more attention on key companies
- Create medium-term Crown plans for problem companies
- Transfer as appropriate
- Set up projects re overlaps/duplication
- Report portfolio performance

* [Withheld under s 9(2)(g)(i)]

Companies crucial to building infrastructure:

- Kordia
- KiwiRail
- Meridian
- Genesis
- MRP
- Transpower

Potential * companies for the Crown:

- NZ Post
- Landcorp
- TVNZ
- MRP
- Meridian
- Genesis
- Solid Energy

* [Withheld under s 9(2)(g)(i)]

Companies that could create long-term value for the Crown, if we invest in them:

- NZ Post/Kiwibank
- Solid Energy
- Kordia
- Meridian
- MRP
- Genesis
- AsureQuality

Companies that could create long-term value elsewhere in the economy:

- CRIs
- NZVIF
- Kiwibank
- KiwiRail
- Kordia
- MRP
- Meridian
- Genesis
- Transpower
- Animal Control Products

Companies with the greatest potential to increase public good if we invest in them:

- MetService
- Transpower

* companies:

- KiwiRail
- Kordia
- LML
- CIAL
- PFL
- Public Trust
- REANNZ

*[Withheld under s 9(2)(g)(i)]

Companies that are most likely to ask for cash from the Crown over the next 2-3 years:

[Withheld under s 9(2)(b)(ii) and (g)(i)]

What are the lever points that CCMAU can use to maximise performance/value:

- SCI/Business planning discussions
- Outlook letters
- Relationship management
- Analysis of investment proposals by companies
- Referral power (access to the Minister)
- Special projects

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New Zealand Post Ltd: Aide Memoire re Potential Debt Listing on New Zealand Debt Exchange

To	Minister for State Owned Enterprises	**Priority**	Semi-urgent
Date	13 February 2009	**Deadline**	20 February 2009

Purpose

The attached aide memoire contains background information to enable you to brief your Ministerial colleagues on the plan by New Zealand Post Ltd (NZ Post) to list its upcoming debt issue on the New Zealand Debt Exchange (NZDX). This would be the first such listing by a State-owned enterprise (SOE).

Commentary

NZ Post plans to raise $150-200 million of debt in April 2009 in order to replace current debt and fund some of the company's planned growth. NZ Post is planning to use a 'hybrid bond' for the debt-raising. A brief description is included in the aide memoire.

The hybrid bond has the advantage that, although it is a debt instrument, it has features that mean that Standard and Poor's (S&P) will recognise 50% of its value to qualify as equity for credit rating purposes. This will help NZ Post to retain its current AA- rating, which is particularly important for its Kiwibank subsidiary.

Because the hybrid instrument is not a common vehicle for debt-raising, NZ Post's advisor, ABN AMRO, has suggested that the issue should be listed on NZDX. This would allow access to a bigger pool of potential investors, with the easier ability to trade a listed product, thus lowering the risk and increasing the attractiveness for those investors. These factors would increase the prospects of a successful issue at a good price for NZ Post.

In principle, listing is supported by CCMAU and The Treasury. In addition to the marketing advantages for NZ Post, we believe that the extra market scrutiny will add another element of accountability and transparency to complement the monitoring already carried out by officials.

Listing would require NZ Post to comply with NZDX listing rules, and aspects of these rules create some tension with the requirements NZ Post needs to meet under the State-Owned Enterprises Act 1986 (SOE Act) and the 'no surprises' policy. However, officials and NZ Post have explored these issues and we believe the hurdles are manageable. The aide memoire outlines the potential hurdles, and the possible remedies.

NZ Post recognises that this would be the first instance of an SOE listing a debt instrument on NZDX. Consequently, although this is an operational matter and therefore a decision for its Board, NZ Post has sought feedback from shareholding ministers on its proposal. It is looking to promote the debt-raising issue in early March

2009 so that it will be ready to replace $75 million of current debt that is due to be retired in April 2009.

You have indicated that you would like to consult with your Ministerial colleagues concerning NZ Post's plan to list its debt-raising. The attached aide memoire is intended to assist you in doing that.

James Cunningham	Hon Simon Power
Manager - Communications, Services & Infrastructure	**Minister for State Owned Enterprises**
CCMAU [Withheld under s 9(2)(a)]	

Aide memoire concerning NZ Post's possible listing of its debt issue on New Zealand Debt Exchange (NZDX)

NZ Post's intention and reasoning

1. NZ Post is looking to list its upcoming debt raising ($150-200 million) on NZDX. This would be the first such listing by an SOE.

2. The prospectus would be published in March 2009 and the funds raised would be used to retire $75 million of existing debt (due to mature in April 2009) and to fund NZ Post's growth plans. We expect to receive a detailed business case on these plans shortly.

3. The issue will be for $150 million with the option of taking on an extra $50 million in over-subscriptions.

4. NZ Post has selected a 'hybrid bond' for the debt-raising. The advantage of this form is that Standard and Poor's (S&P) will recognise 50% of the issue's value as qualifying as equity for rating purposes. This will help NZ Post to retain its AA- rating as company growth continues, with less reliance on the Crown to inject capital to preserve key ratios. Nevertheless, the instrument is a debt instrument, and note-holders will have no equity rights.

5. NZDX listing has significant marketing advantages for NZ Post (a more liquid asset for investors and a wider investor pool should result in strong subscription at an attractive price for NZ Post).

6. There are no legislative impediments to an SOE listing debt securities on the NZDX, but there are three important considerations that Ministers need to be aware of:

   a. The disclosure requirements under listing rules

   b. The replacement capital covenant feature of NZ Post's hybrid bond proposal

   c. A clause in the proposed bond terms that could, under certain circumstances, affect dividends paid to the Crown.

7. CCMAU and Treasury officials do not believe that any of the potential hurdles are insurmountable, and we support listing.

8. The details of the proposed hybrid bond, and the implications of listing are described below.

Description of the debt instrument

9. The planned instrument is a 30 year, low covenant, subordinated note with a coupon step-up at approximately five years:

   a. '30 year' – the long-term nature of the debt is one criterion that S&P stipulates to qualify as equity

b. 'Low covenant' – relative to normal corporate bonds, there are few default covenants or protections for bond holders

c. 'Subordinated' – repayment rights are behind other debt-holders, but ahead of common stock equity holders

d. 'Coupon step up at five years' – at five years (and theoretically at each subsequent five year anniversary), the interest rate payable by NZ Post is increased by 1% above base rate.

10. Other relevant features of the hybrid instrument include:

a. Holders have no voting or control rights

b. Holders have no equity convertibility options or rights

c. Cumulative interest payments may be withheld for a period of up to five years. However, if an interest payment is deferred, no distributions (eg dividends) can be made to the Crown unless all outstanding interest has been paid. The withholding of interest would be seen by the market as reflecting badly on NZ Post, and would only be expected if the company was in dire financial circumstances (in which case it would be unlikely to be in a position to declare dividends anyway).

d. It is expected that NZ Post, rather than incur the step-up interest rate, will choose at the step up point (in five years) to either remarket the bond (on similar or amended terms), or 'replace' the instrument with either a similar hybrid instrument or with ordinary equity (issued to current shareholders, not to debt-holders). The purpose of the requirement for issuing a similar hybrid instrument or equity is to demonstrate to the rating agency that the bond represents permanent capital.

The possible implication for the Crown at the step up time is that, should NZ Post choose not to continue with the bond at the stepped up rate and if the hybrid market softens, then the Crown could be called upon to inject further equity into NZ Post. NZ Post believes there is little likelihood of a collapse of the hybrid market, and in any case, it considers a step up of 1% to not be unduly onerous (and in recent years some international issuers have chosen to continue at the stepped up rate). Consequently, The Treasury does not believe that the small risk of a further equity injection represents a formal contingent liability for the Crown. It is clear that any equity injection would be at the absolute discretion of Ministers, and NZ Post has several options available to avoid this being necessary, if Ministers did not want to make an equity injection.

The implications of listing

11. NZ Post would need to comply with New Zealand Stock Exchange (NZX) Listing Rules, though the requirements are less onerous for listing on NZDX than for equity listings. Nevertheless this creates a tension between the

continuous disclosure requirements under the listing rules and the 'no surprises' policy. The main relevant obligations that are raised are:

a. Material information – any information that affects the price of the securities must be disclosed to the market before disclosure to any other person (including the shareholding Ministers). Because disclosure is limited to information that affects the price of the security, most of the information currently exchanged between NZ Post and officials and Ministers is unaffected (eg routine quarterly performance reporting). There may, nonetheless, be some occasions when the Minister receives information at the same time as the market does (eg an unpredicted litigation against NZ Post). It is not possible to predict in advance all the possible situations that could arise, and NZ Post would need to be careful to consider all the information it shares with Ministers in light of its obligations under the listing rules.

b. Financial information – the timetable for reporting on half-year and annual reports is one month earlier for the NZDX than the dates needed to comply with the SOE Act 1986. Some (minor) additional information is also required. NZ Post is able to meet the earlier dates.

12. There are a number of other conditions in which information can be shared with Ministers without prior release to the market. These include:

a. Where the information is not 'sufficiently certain' (eg 'no surprises' communication, draft business plans or planned acquisitions) and where it is confidential

b. Where information is confidential and commercially sensitive (eg business plans or planned acquisitions)

c. Where negotiations are confidential and incomplete (eg a planned acquisition).

13. In most situations, once events become 'certain' NZ Post tends to make public announcements in any case.

14. Waivers and exemptions can be provided [Withheld under s 9(2)(ba)(i)] We understand that NZ Post will apply for appropriate waivers.

15. One circumstance that would require specific attention is when NZ Post is called to appear before a Select Committee. In the past, when Air New Zealand (whose shares are listed on NZX) has been called to appear, The Treasury has briefed committee members beforehand to ensure that they do not cause an accidental breach of listing rules.

16. Because the hybrid bond has some equity-like characteristics, there may be a need to explain to the public that it is a debt instrument. Equity is not being sold, nor does this instrument 'pave the way' for it to be sold.

17. A final implication is that if other SOEs follow suit and list securities on the NZDX, then pressure may come on the Crown (as the holder of material information relating to those SOEs) to continuously disclose market sensitive information.

Summary

Advantages of NZDX listing	*Disadvantages of NZDX listing*
Marketing advantages for NZ Post, through access to larger investment pool and easier transaction arrangements for investors.	Some extra administrative burden for NZ Post (and possibly for officials).
Extra market scrutiny, adding to accountability and transparency and complementing the monitoring done by officials.	Care and attention needed to avoid breaches of rules, especially since this is a new experience for NZ Post, officials and Ministers.
Opportunity for the investing public to participate in one of the larger SOEs and have the ability to trade their investment.	The listing and the instrument will need to be explained to the public.