The Treasury

Mixed Ownership Model for Crown Commercial Entities:
Treasury Advice Information Release

4 September 2012

Release Document

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[1] 9(2)(a) - to protect the privacy of natural persons, including deceased people

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

[3] 9(2)(f)(iv) - to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials

[4] 9(2)(g)(i) - to maintain the effective conduct of public affairs through the free and frank expression of opinions

[5] 9(2)(h) - to maintain professional legal privilege

[6] 9(2)(i) - to enable the Crown to carry out commercial activities without disadvantage or prejudice, or

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In preparing this Information Release, the Treasury has considered the public interest considerations in section 9(1) of the Official Information Act.
**Treasury Report:** Comparison of powers of shareholding Ministers in the SOE and mixed ownership model regimes

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<thead>
<tr>
<th>Date:</th>
<th>8 March 2012</th>
<th>Report No:</th>
<th>T2012/386</th>
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### Action Sought

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<tr>
<th>Minister of Finance (Hon Bill English)</th>
<th>Action Sought</th>
<th>Deadline</th>
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<tr>
<td>For information</td>
<td>None</td>
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<tr>
<th>Minister for State Owned Enterprises (Hon Tony Ryall)</th>
<th>Action Sought</th>
<th>Deadline</th>
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<tr>
<td>For information</td>
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### Contact for Telephone Discussion (if required)

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<thead>
<tr>
<th>Name</th>
<th>Position</th>
<th>Telephone</th>
<th>1st Contact</th>
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<tbody>
<tr>
<td>John Beaglehole</td>
<td>Commercial Transactions Group</td>
<td>[1]</td>
<td>✓</td>
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<tr>
<td>Chris White</td>
<td>Commercial Transactions Manager</td>
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### Minister of Finance’s Office Actions (if required)

None.

Enclosure: Yes
Treasury Report: Comparison of powers of shareholding Ministers in the SOE and mixed ownership model regimes

We enclose for your information a schedule comparing the powers of shareholding Ministers under the State Owned Enterprises Act 1986 with those contained in the Mixed Ownership Model regime. This is a preliminary piece of work, and we will develop it further, to provide advice on how the Crown should act as a shareholder in the mixed ownership model companies. We are also preparing a further report on the ability of Ministers as shareholders to control sales of sensitive assets; we envisage having that to you shortly.

Recommended Action

We recommend that you note the attached schedule.

Agree/disagree.

Chris White
Manager, Commercial Transactions

Hon Bill English
Minister of Finance
<table>
<thead>
<tr>
<th>SOE Act and experience</th>
<th>MOM Bill</th>
<th>Commentary</th>
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<tr>
<td>s.4 sets out that the principal objective of every State enterprise shall be to operate as a successful business and, to this end, to be (a) as profitable and efficient as comparable businesses that are not owned by the Crown; and (b) a good employer; and (c) an organisation that exhibits a sense of social responsibility by having regard to the interests of the community in which it operates and by endeavouring to accommodate or encourage these when able to do so.</td>
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<td>Contains no such provision; neither does the Companies Act. (a) is implicit in being a listed company.</td>
<td>In sum: corporate social responsibility (CSR) provisions are not part of the Companies Act framework, and a survey of listed companies’ constitutions did not provide examples of CSR requirements included in their constitutions. Even so, a number of NZ corporations have corporate social responsibility programmes (Contact Energy’s sponsorship of Triathlon New Zealand, Telecom New Zealand’s Telecom Foundation, and Fonterra’s ‘Milk for Kiwis’ programme). Not including a CSR provision in the Act or the constitutions will not prevent the MOMs from developing or continuing their existing work. Corporate social responsibility is typically defined as the voluntary integration of social and environmental concerns into a business’ operations, and interactions with stakeholders. Organisations choose to pursue CSR because it can be good for business through building stakeholder trust in an organisation’s ability to balance vested interests and the public good, sometimes termed an organisation’s ‘licence to operate’. We would argue that all businesses are incentivised to do this as a matter of course.</td>
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<td>There have been several legal cases considering the meaning of this section of the Act. We have drawn the following conclusions from these:</td>
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<td>• What can amount to operating “as a successful business” has to be determined in the context of the three requirements of s 4(1), and there is nothing to suggest that they should not be treated as being of the same weight;</td>
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<td>• When considering whether an SOE is an organisation that exhibits a sense of social responsibility, courts will most likely assess this over a period of time and not in relation to a particular act or transaction in the course of the SOE’s business;</td>
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<td>• Courts will be reluctant to second guess subjective decisions of SOEs which involve a “balancing act” between the requirements of s 4(1).</td>
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| s.7 provides for the Crown and an SOE to enter into an agreement for the non-commercial provision of goods or services by an SOE, with the Crown paying all or part of the associated costs. The Act is ambiguous on the extent to which the Crown can compel the SOE to absorb some of the costs of the provision. |
| The Bill contains no similar provision. | No power is required as the Government can contract with the companies on an arm’s-length, commercial basis, with the Crown paying the full costs. As far as we are aware, this provision has only been used once, for Kiriiri’s public policy rail initiatives (for which there is an appropriation of $3.720M). We are not aware of any occasion where the SOE has absorbed part of the costs of the service. Making the MOM companies absorb some of the costs of non-commercial goods or services, as is theoretically possible under section 7, is not appropriate given they will have minority shareholders. |

| s.8 provides that before entering into any collective agreement under the Employment Relations Act 2000, every State enterprise to which this subsection applies must consult with the State Services Commissioner over the conditions of employment to be included in the collective agreement |
| The Bill contains no similar provision. | In our view this section is not appropriate for a listed company operating in a competitive environment. |

| s.11 provides that the shareholding Ministers cannot sell or otherwise dispose of shares in SOEs. |
| The Bill prevents the Crown from holding less than 51% of the voting rights in each of the companies, and will restrict non-Crown shareholders from holding more than 10% of the voting rights in each of the companies. | The Crown will not be able to hold less than 51% of the shares in each MOM company, except by an amendment to the legislation. While the Crown will own the majority of shares in each company, there is a change in control implicit in moving from 100% shareholding to being a majority shareholder. First, the Crown will no longer have complete control over the companies’ constitutions, as a special resolution (75%) is needed for changes. Second, the companies’ directors will need to bear in mind the views and interests of other shareholders, as opposed to the interests of a single shareholder. |

| s.12 provides for the issue of state enterprise equity bonds, following authorisation of the House. |
| The Bill contains no provision for equity bonds. | Equity bonds have never been issued to our knowledge. SOEs, like MOMs, are free to use a wide variety of non-voting instruments to raise capital, including instruments that have equity characteristics, and SOEs have done so. There is no clear boundary between non-voting shares at one extreme, and debt at the other. The Government’s real concern is to ensure that issue of securities with equity characteristics are not used to undermine the Crown’s 51% voting rights, which is prevented by the MOM Bill. |

| Section 13 enables Ministers to give directions in respect of the amount of dividend, and to include or omit from | There is no power of direction. Ministers have the normal shareholder | The ability to give directions to an SOE makes sense in an environment where the company is wholly owned by the Crown. Note, however, that the power to give directions is limited, and we do not believe that |
statements of corporate intent provisions of a
kind referred to in s. 14(2)(a) to (h).

s. 14(2) sets out the information that must
be included in an SOE’s statement of
corporate intent:
(a) The objectives of the group;
(b) The nature and scope of the activities to
be undertaken;
(c) The ratio of consolidated shareholders’
funds to total assets, and definitions of
those terms;
(d) The accounting policies;
(e) The performance targets and other
measures by which the performance of
the group may be judged in relation to
its objectives;
(f) A statement of the principles adopted in
determining the annual dividend
together with an estimate of the amount
or proportion of annual tax paid earnings
(from both capital and revenue sources)
that is intended to be distributed to the
Crown;
(g) The kind of information to be provided to
the shareholders by the State
enterprise during the course of those
financial years, including the information
to be included in each half-yearly report;
and
(h) The procedures to be followed before
any member of the group subscribes for
purchases, or otherwise acquires shares
in any company or other organisation.

| rights which include:                          | any direction as to dividends has ever been given. In particular, Ministers cannot give
directions in respect of individual transactions. Also, in practice directions have been
rarely given, because:
- Sell and buy shares (subject to the limits
  set out in the Bill);
- Vote on appointment of directors, major
  transactions (transactions in excess of
  half the value of the company) and other
  powers conferred on shareholders by the
  Companies Act or the companies’
  constitutions;
- Vote on changes to the constitution;
- Decide whether to take up any issue of new
  shares;
- Possibly approve the appointment of the
  chairman of the Board
  (this is yet to be
decided).

s. 18 allows shareholding Ministers to seek
effectively any information in respect of a
SOE and its subsidiaries (except for
information on individuals)
The Bill contains no similar
provision. The Companies
Act allows shareholders to
request information, but
does not have to
provide it.
The Crown can obtain further information through agreement with the MOM
companies, as it does currently for Air NZ. The Treasury can also require the MOM
companies to provide it with information necessary to prepare the Government’s
annual financial statements.

Subject to the OIA and OA.
No longer subject to the
OIA and OA.
The main purpose of the OIA and OA is to make official information more available
and hold accountable state entities that can impact on the public through their
administrative functions. In particular, it enables the public to understand why certain
decisions or policies have been made. This enables the public, either directly or
through the Ombudsman, to challenge decision-makers where appropriate. This
important because the state and most of its agencies have the characteristics of a
"monopoly", i.e. customers do not have anywhere else to go. This includes a number
of SOEs that have monopoly characteristics.

However, the MOMs operate in a competitive environment. This enables customers
or investors who have had no success in using their contractual rights, to switch to a
different provider. It also provides the MOMs with a strong incentive to be customer-
focused.

Further, we note that:
- Ministers of the Crown and officials will themselves continue to be subject to the
  OIA, and officials will continue to be subject to the OA;
- Air New Zealand is not subject to the OA or OIA;
- the companies will be subject to the Stock Exchange’s continuous disclosure
  regime.
The OIA and OA are therefore unnecessary and could place the MOMs at a
competitive disadvantage relative to other energy companies.

Other: Appointment of directors. These are
nominated and appointed in accordance
with the provisions of the Companies Act.
In other words, they are nominated by
shareholders and voted on at the annual
shareholders’ meeting.
In the case of SOEs the Government
 nominate and appoints directors.

The relevant provisions of
the Companies Act apply.
In the case of widely-held
listed companies the
practice is for the existing
Board to suggest at a
shareholders’ meeting that
somebody nominate a
particular director, who is
then voted on by
shareholders.
Boards are likely to consult with the Government and other significant shareholders
before putting forward a director for nomination and election.
Given that the Crown will be able to vote on a nominated director, there is little chance
of someone being appointed who is not acceptable to the Government.