

The Treasury

South Canterbury Finance Limited Information Release

Release Document

April 2011

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- [1] 9(2)(a) - to protect the privacy of natural persons, including deceased people
- [2] 9(2)(b)(i) - to protect trade secrets
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- [5] 9(2)(d) - to avoid prejudice to the substantial economic interests of New Zealand
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- [8] 9(2)(i) - to enable the Crown to carry out commercial activities without disadvantage or prejudice.

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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.

From: [1]
Sent: Monday, 21 December 2009 2:43 p.m.
To: Brian McCulloch; John Park
Subject: Letter re SCF
Attachments: L091221 - Treasury.pdf; forbarlogo.png; FBKSSAward.png

Dear Brian & John,

Further to our meeting last week at which I passed you a letter on behalf of SCF, attached is an updated letter which corrects a couple of errors in the previous letter which became obvious after discussions between respective legal representatives. The overall intent/substance is unchanged.

We look forward to your acknowledgement in due course.

Thanks
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T: [1]

M:
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21 December 2009

The Treasury
PO Box 3724
WELLINGTON 6140

Dear Sir / Madam

South Canterbury Finance Limited - Proposed new funding arrangements with Southbury Corporation Limited

We write on behalf of South Canterbury Finance Limited (**SCF**). This letter supercedes our letter dated 14 December which, during discussions between our respective legal advisors, identified some errors in the description of the sequence by which the transactions will flow.

We refer to the New Zealand deposit guarantee scheme Crown Deed of Guarantee entered into between Her Majesty the Queen in right of New Zealand and SCF, dated 19 November 2008 (the **Deed**).

The purpose of this letter is to seek the Crown's written consent under clause 6.2(b) of the Deed to the arrangements described below.

Background

South Canterbury Finance Limited (**SCF**) had made secured advances of approximately \$82 million to Southbury Group Limited (**SGL**) (the **SCF Advance**). Earlier this year, SCF assigned \$22 million of the SCF Advance to ^[3] an entity associated with ^[1] with the result that approximately \$60 million is now owed by SGL to SCF under the SCF Advance and \$22 million is owed to CFML (the **CFML Advance**). Under the assignment arrangement, it was agreed that CFML would rank ahead of SCF's security interest over SGL's assets for \$22 million.

^[3] has also made secured advances to SGL under two facility agreements. Approximately \$40 million remains outstanding to the Bank under these agreements (the **Bank Advance**).

The intention of all parties when the documentation for the Bank Advance was entered into, and a requirement of the Bank, was that the Bank would have a first ranking security over SGL's assets in respect of its advances (in the form of a general security agreement) and that SCF would have a second ranking security interest in respect of its advances.

During the course of recent discussions with the Bank regarding the proposed recapitalisation of SGL and SCF, the Bank became aware that the security for the SCF Advance and the ^[3] Advance ranks in priority to the Bank's security for the

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Bank Advance. As indicated above, this was not the intended security position as between the Bank, SGL and SCF. A copy of the Bank's original executed documentation is attached to this letter as verification of this position.

Under the reorganisation of SGL and SCF it is proposed that:

- (a) All of the ordinary shares in SCF, and all of the ordinary shares in Helicopters NZ and 79% of the shares in Scales Corporation Limited will be transferred from SGL to Southbury Corporation Limited (**SCL**) which is currently a wholly owned subsidiary of SGL.
- (b) The Bank will lend approximately \$40 million to SCL, and [3] (or an associated entity) will lend \$22 million to SCL. Those sums will be paid by SCL to SGL as part of the purchase price for the shares referred to in (a), and SGL will simultaneously apply those sums in repaying the Bank and repaying the [3] Advance. This will have the same broad effect as if the Bank Advance and the [3] Advance have been novated to SCL, but the transaction will not be in legal form a novation.
- (c) SGL (and various entities related to Mr A J Hubbard) will guarantee the liability of SCL to the Bank. The security held by the Bank from SGL will secure that guarantee.
- (d) Accordingly the result will be that SCF will hold security from SGL securing the SCF Advance, and the Bank will hold security from SGL securing the guarantee given by SGL of the liability of SCL to the Bank.

The Bank and SCF will enter into a deed of priority whereby the Bank's security will rank first for an amount of \$40 million plus two years interest and SCF's security will rank after that. This rearrangement (the **Security Arrangement**) restores the intended position as recorded above.

SCF understands that SGL has gross assets with a value well in excess of \$122 million and that SCL will, following the restructuring of the SGL group, also have assets with a value well in excess of \$122 million. On this basis, SCF is satisfied that, while it will no longer have a first ranking security interest over SGL's assets, there will be more than sufficient assets available to enable the SCF Advance to be recovered in full should SCF need to enforce its security in respect of the SCF Advance. Accordingly, SCF will, in effect, remain fully secured for its advance notwithstanding the change in the ranking of its security. For completeness, we confirm that the Security Arrangement will be documented on normal commercial terms.

Clause 6.2(b) of the Deed

As you know, clause 6.2(b) of the Deed provides:

"During the Guarantee Period the Principal Debtor shall not (and shall ensure that its subsidiaries shall not), without the prior written consent of the Crown:... (b) enter into any transaction (or series of linked or related transactions) having a value exceeding 1% of the value of the assets of the Principal Debtor with any person who controls or is under common control with the Principal Debtor (other than a wholly-owned subsidiary of the Principal Debtor) unless:

- (i) *that transaction is on arms' length terms; and*
- (ii) *an independent expert approved by the Crown in writing first certifies to the Crown in writing that the transaction is, in the opinion of that expert, on arms' length terms."*

SCL will, at the time the Security Arrangement is entered into, be a person "who...is under common control with" SCF for the purposes of clause 6.2(b) of the Deed. The total value of SCF's assets is approximately \$2.1 billion (as stated in its audited financial statements for the period ended 30 June 2009). One percent of this figure is approximately \$21 million.

In our view, the effective "value" of the Security Arrangement for the purposes of the Deed is, arguably, \$40 million given that SCF would, in effect, be agreeing to its security for the SCF Advance being deferred by \$40 million (being the amount outstanding under the Bank Advance).

It is unclear whether entering into the Security Arrangement would constitute a "transaction" for SCF within the meaning of clause 6.2(b) of the Deed. However, given that SCF's current security position will become subordinated to the Bank's, the Security Arrangement may constitute a "transaction" within the scope of clause 6.2(b) of the Deed. Accordingly, we have decided to seek approval of the Security Arrangement under clause 6.2(b) of the Deed.

It would appear that the Bank would have the ability through legal action to obtain rectification of this error regarding their security ranking. None of the parties wish for this to occur but none wish to undertake this transaction without your acknowledgement.

Request for consent

On our reading of clause 6.2(b) of the Deed, the Crown has the ability to approve, in writing, a transaction which falls within the scope of that clause without an independent expert being appointed to certify that the transaction is on arms' length terms.

Accordingly, we request that the Crown consents, in writing, to SCF entering into the Security Arrangement pursuant to clause 6.2(b) of the Deed. We reiterate that, as set out above, the overall effect of the Security Arrangement is simply to restore the parties to their intended security positions in respect of their respective advances to SGL and that SCL will, we understand, have sufficient assets available to allow the SCF Advance to be recovered in full should SCF need to enforce its security for any reason in the future.

Please feel free to contact us if you have any questions or would like any further information.

Yours sincerely
Forsyth Barr Limited

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