Office of Hon Bill English

Deputy Prime Minister
Minister of Finance
MP for Clutha-Southland

05 September 2012

Tena koe

MIXED OWNERSHIP MODEL COMPANIES: CONSULTATION ON "SHARES PLUS" PROPOSAL

1. As you will be aware, on Monday 3 September 2012 the Government announced that it will proceed with an initial public offering (IPO) of up to 49 per cent of Mighty River Power in the period March to June 2013. That will be followed by IPOs of up to 49 per cent of Meridian Energy and Genesis Energy.

2. The Government also announced that over the next five weeks it would be undertaking a targeted consultation with directly affected Māori interests about the "shares plus" concept discussed in the Waitangi Tribunal's interim report on claims to freshwater and geothermal resources delivered on 24 August 2012.[1]

3. The purpose of this letter is to seek your input into that consultation exercise, and provide some information as the starting point for that consultation.

The "shares plus" concept

4. One of the issues considered in the Tribunal's report was whether the Government's intention to sell up to 49% of the "mixed ownership model" (MOM) companies would affect the Crown's ability to recognise Māori rights and interests in freshwater and geothermal resources, and provide redress for past Treaty breaches.

5. The Crown has consistently expressed the view that the partial sale of these companies does not impact on the Crown's ability to recognise Māori rights and interests in water. The Tribunal largely agreed, finding that the Crown would not be prevented by the sales from providing appropriate rights recognition, and that

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[1] Waitangi Tribunal *Interim Report on the National Freshwater and Geothermal Resources Claim* (Wai 2358). The Report is available at http://www.waitangi-tribunal.govt.nz/doclibrary/public/reports/generic/Wai2358/Wai2358W.pdf.

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there would be many options for rights recognition and redress after the sale of shares in MOM companies.[2]

6. However there was one respect in which the Tribunal considered that a partial sale of shares could affect the Crown's ability to provide appropriate rights recognition and redress. In its interim report the Tribunal said:[3]

> *But there is one area in which the Crown will not be able to provide appropriate rights recognition or redress after the partial privatisation, and that is in the area that we have termed "shares plus" : the provision of shares or special classes of shares which, in conjunction with amended company constitutions and shareholders' agreements, could provide Māori with a meaningful form of commercial rights recognition. As we have found, "shares plus" are not 'fungible' and company law would in practical terms prevent the Crown from providing this form of rights recognition after the introduction of private shareholdings, certainly after the sale of more than 25 per cent of shares and arguably before that too. The detailed analysis of company law and of the parties' evidence and submissions that supports this finding is set out above in sections 3.7.3 and 3.8.2.*
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> *We conclude therefore that the sale of up to 49 per cent of shares in power-generating SOE companies will affect the Crown's ability to recognise Māori rights and remedy their breach, where such breach is proven.*

7. This "shares plus" concept is the issue on which we are now seeking your views.

The Government's preliminary view on "shares plus"

8. Although the Tribunal's interim report put considerable emphasis on the potential significance of "shares plus" as a form of rights recognition and redress, the report did not discuss the detail of what outcomes might be achieved using the "shares plus" mechanism, or consider whether the same outcomes could be achieved in other ways.

9. The Government has carefully considered what rights recognition and redress outcomes "shares plus" might deliver, and whether this mechanism has the significance suggested in the Tribunal's interim report. The Government's current view, as a result of this analysis, is that the "shares plus" idea should not be progressed. There are five main reasons for this view.

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[2] Wai 2358 at 196-197.

[3] Wai 2358 at 197.

10. One is that we do not believe it is in the national interest for any group among the 49 per cent minority shareholders in these companies to be given special rights.

11. Second, almost every form of rights recognition and redress for Māori that could be delivered by "shares plus" can also be achieved in other ways.

12. Third, the remaining elements of "shares plus" in relation to decision rights over management or strategic decisions would not work in practice as an effective form of rights recognition or redress.

13. Fourth, if the "shares plus" concept was put in place, it would be likely to make the company less attractive to investors, which in turn could be reflected in a lower sale price and therefore be to the detriment of all taxpayers.

14. Fifth, following consultation with iwi, a careful and deliberate decision was made to ensure that the Crown's obligations under the Treaty continue to rest with the Crown, not with the companies. They are not themselves appropriate vehicles for achieving redress.

15. For these reasons the Government does not believe "shares plus" is necessary or desirable. Further, we do not believe that to continue with the share offer without "shares plus" would be a Treaty breach.

16. These reasons are expanded on in the appendix to this letter.

The consultation process

17. The Government has, however, decided that the right thing to do at this point is to undertake a period of consultation with affected Māori interests on "shares plus" to discuss its preliminary view, answer questions and to listen to Māori. This consultation will consist of a written submissions process for anyone who considers themselves to be affected and, in addition, a series of hui for those with a direct interest in the water and geothermal resources used by Mighty River Power, Genesis Energy and Meridian Energy.

18. The Government will write to groups that it has identified as having a direct interest, with details of the hui, by Wednesday 12 September 2012.

19. The Crown is seeking written input from all groups by Friday 5 October 2012.

20. Please also feel free to draw this letter to the attention of those whom you are aware may be affected by these issues, so that they can participate in this process by providing written submissions.

21. Ministers will carefully consider all written and oral submissions. A final decision about "shares plus" will be made following this consultation process.

22. The topics on which written submissions are specifically sought are:

    22.1 the rights recognition and redress outcomes that "shares plus" might deliver. Are there any potential outcomes/entitlements that you consider could be achieved via "shares plus" that are not identified in the appendix to this letter?

    22.2 the capacity of the Crown to replicate by other means, after an IPO, each of the rights recognition and redress outcomes that you have identified as potential outcomes from the "shares plus" mechanism. Do you agree with the assessment in the appendix to this letter that almost all of these possible outcomes can be replicated after an IPO by other means?

    22.3 the capacity of the Crown to provide, after an IPO, more effective and more direct mechanisms for providing Māori with voice in relation to the relevant resources (e.g. through regulatory mechanisms) and/or commercial interests in the relevant resources. Do you agree with the assessment in the appendix to this letter that after an IPO the Crown will retain the capacity to provide more effective and more direct mechanisms for providing Māori with voice and/or commercial interests in the relevant resources?

    22.4 the reasons for and against proceeding with the "shares plus" concept. Are there any additional factors the Government should take into account in making a final decision on whether to implement the "shares plus" concept?

    22.5 if you consider that the Government should proceed with "shares plus":

        (a) what are the specific rights and powers in relation to the MOM companies that you consider should be delivered using this mechanism?

        (b) why do you consider that this approach is preferable to other options for providing rights recognition and redress?

23. Please note the Government may publicly release your submission, a summary of submissions and a list of the names of submitters on the Treasury's website. Your name will be made publicly available as part of your submission when it is released. Your contact details will be removed from material that is made publicly available. Please indicate if you wish that your name be removed from your submission before it is released.

24. The Treasury is subject to the Official Information Act 1982 and copies of any submissions will normally be released in response to an OIA request. Please indicate in your submission if you wish for it to remain confidential, and explain why. The Treasury will consider your confidentiality request in accordance with the grounds for withholding information in the OIA. You can view a copy of the OIA on the New Zealand Legislation website: www.legislation.govt.nz

25. Written submissions should be received no later than 5pm on Friday 5 October 2012.

26. Submissions can be sent by email to sharesplusconsultation@treasury.govt.nz or by post to:

    FreePost Authority No. 126395
    Shares Plus Consultation
    Commercial Transactions Group
    The Treasury
    PO Box 3724
    Wellington 6140

27. The Government looks forward to hearing your views on these issues.

Na matau tahi,

Hon Bill English
Minister of Finance

Hon Tony Ryall
Minister for State Owned Enterprises

Hon Christopher Finlayson
Attorney-General

APPENDIX – ANALYSIS OF "SHARES PLUS"

The Crown has identified four categories of entitlement that could in principle be attached to special shares in a MOM company or provided through the constitution of the company and/or a shareholders' agreement. These categories are analysed below.

It is important to bear in mind that the focus of this analysis is on the **capacity** of the Crown to provide particular forms of rights recognition or redress. This is quite distinct from the question of whether the Crown should provide particular forms of rights recognition or redress, or is likely to agree to do so. Put another way, the issue is whether any significant tools are being removed from the toolbox: the question of which tools might eventually be deployed is a matter for continuing discussion between the Crown and iwi, and is not within the scope of this consultation process.

Financial entitlements

The first category of entitlements that could be provided via "shares plus" is financial in nature – enhanced rights to dividends and/or distributions of capital, whether as to amount or priority, or both.

It seems clear that the Crown would retain its capacity to provide such rights following an IPO, if they are seen as an appropriate form of redress, through one or both of the following mechanisms:

- allocation of a sufficient number of ordinary shares to deliver the desired dividend/distribution rights. Ordinary shares can be provided out of any shareholding in excess of 51% retained by the Crown after an IPO, or by the Crown going into the market to buy back shares;
- a contract with the Crown to pay a specified level of return defined by reference to the MOM company's performance or declared dividends or capital distributions. All of the possible financial entitlements that could be provided via shares or the company constitution could be provided by the Crown by contract.

So the sale of up to 49% of shares in a MOM company does not affect the Crown's capacity to provide entitlements of this kind, if at some time in the future the Government considered that this was appropriate.

Appointment of directors

The second category of entitlement that could be provided via "shares plus" is the ability to appoint one or more directors of the company.

Again, it seems clear that the Crown would retain its capacity to provide such rights after an IPO, if at some point in the future they are seen as an appropriate form of redress: the Government as owner of 51% of the shares in the company could agree to procure the appointment of one or more directors nominated by the relevant Māori interests.

So the sale of up to 49% of shares in a MOM company does not affect the Crown's capacity to provide entitlements of this kind.

Moreover company law principles would place significant limits on the extent to which the power to appoint one or more directors could operate as a meaningful form of rights recognition or redress. A director appointed by Māori interests would be required to act in the best interests of the company, not in the interests of their appointor or to protect the relevant resource. None of the exceptions to this principle in the Companies Act 1993 would appear to be applicable to such directors. (In particular, following an IPO it is highly unlikely the company would qualify as a "joint venture" for the purposes of s 131(4) of the Companies Act, as not all shareholders would be participants in a joint venture even if the Crown and Māori could be so described.)

Additional voting rights on shareholder decisions

The third category of entitlement that could in principle be provided via "shares plus" is additional voting rights on matters reserved for decision by all shareholders.

The Crown would retain its capacity to provide such rights following an IPO, if at some point in the future they are seen as an appropriate form of redress, through one or both of the following mechanisms:

- an agreed level of votes on shareholder decisions could be provided after an IPO by allocation of a sufficient number of ordinary shares to deliver the desired voting rights. As noted above, ordinary shares can be provided out of any shareholding in excess of 51% retained by the Crown after an IPO, or by the Crown going into the market to buy back shares;
- as with the power to appoint a director, the Crown would retain its capacity to provide such rights after an IPO, by entering into an agreement in relation to the manner in which the Government as owner of 51% of the shares in the company would exercise voting rights on such matters as might be agreed.

Voting/decision rights on management/strategic decisions

The fourth category of entitlement is the only one that has been identified that could not be exactly replicated following an IPO: voting/decision rights on

management/strategic decisions to be made by the MOM company, that would otherwise be made by the company's board and not by its shareholders.

The Government's current view in respect of entitlements in this category is that:

- there are more effective and more direct mechanisms for providing voice in relation to the resource (eg through regulatory mechanisms), if at some point in the future this is seen as appropriate: an IPO does not affect the Crown's capacity to promote legislation to modify the regulatory framework applicable to the relevant resources;
- there are more effective and more direct mechanisms for providing commercial interests in the resource, if at some point in the future this is seen as appropriate: an IPO does not affect the Crown's capacity to promote legislation to provide for commercial redress mechanisms;
- In exercising such rights in most if not all circumstances, holders of the special shares would be required to act in the best interests of the company, rather than for the benefit of designated interests or to protect relevant resources. Thus this mechanism would not provide a distinctive voice for Māori on management matters, as shareholders could not take a representative approach;
- there are strong commercial reasons not to provide for shareholder decision-rights of this kind, enabling a minority to make certain management decisions in relation to the company. In particular, a power of this kind conferred on any minority shareholder has the potential to affect the commercial focus and success of the company, and is therefore likely to reduce the price obtained by the Crown for the shares on an IPO to the detriment of all taxpayers, and reduce the benefit of ownership of shares in the company for shareholders.

Shareholders' agreements

The Tribunal's interim report refers, when discussing the "shares plus" concept, to shareholders' agreements that could be entered into in conjunction with the allocation of shares to Māori.

It would not be feasible to have a shareholders' agreement to which all shareholders in a MOM company are parties following an IPO: this is simply not practicable in the context of a listed company with thousands of shareholders.

A shareholders' agreement between the Crown and Māori interests entered into before an IPO could not confer on Māori shareholders any additional rights in relation to the company that would be exercisable after an IPO except to the extent that those rights were given effect through changes to the company's constitution and/or in the terms on which special classes of shares are issued.

Thus the possibility of a pre-IPO shareholders' agreement does not add to the four categories of entitlements that could be delivered via "shares plus", as outlined above.

The ability of the Crown to enter into a shareholders' agreement with Māori interests after an IPO has been identified above as one method of replicating many of the entitlements that could be provided by means of "shares plus". The availability of this mechanism for delivering entitlements is (by definition) not affected by an IPO.