

# **The Treasury**

## **Mixed Ownership Model for Crown Commercial Entities: Shares Plus Proposal Information Release**

**21 December 2012**

### **Release Document**

**[www.treasury.govt.nz/publications/reviews-consultation/sharesplus](http://www.treasury.govt.nz/publications/reviews-consultation/sharesplus)**

Key to sections of the Official Information Act 1982 under which information has been withheld.

Certain information in this document has been withheld under one or more of the following sections of the Official Information Act, as applicable:

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

9(2)(b)(i) - to protect trade secrets

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

9(2)(f)(ii) - to maintain the current constitutional conventions protecting collective and individual ministerial responsibility

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

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

9(2)(h) - to maintain professional legal privilege

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

Not relevant.

Where information has been withheld a reference to the applicable section of the Official Information Act has been made, as listed above.

In preparing this Information Release, the Treasury has considered the public interest considerations in section 9(1) of the Official Information Act.

## Appendix Two – Analysis of “Shares-Plus”

Rights	Test 1 - Substitutability	Test 2 – Feasibility pre-listing			Test 3 – Feasibility post-listing	
Nature of the enhanced right	Relevance as form of Treaty redress – can the right be provided in another way?	Can the right be granted under company or other law or regulations?	Can the right be implemented in a practical terms?	What is the impact on the government’s policy objectives (fiscal, efficiency, market development)	Can the right be granted under company or other law or regulations?	Can the right be implemented in a practical terms?
<p>Preferential financial return:</p> <ul style="list-style-type: none"> <li>• Higher levels of dividend.</li> <li>• Greater certainty of payment.</li> <li>• Preferred ranking for dividend rights.</li> <li>• Enhanced capital distribution rights on liquidation.</li> <li>• Preferred capital distribution rights on liquidation.</li> </ul>	<p><b>Yes</b></p> <ul style="list-style-type: none"> <li>• These rights are of financial value only. They can be readily substituted.</li> <li>• The level of return can be increased by increasing Māori’s shareholding (up to 10%).</li> <li>• The Crown can fund any return over and above “normal” with a derivative instrument.</li> <li>• Special shares to enhance financial returns suffer from the lack of a direct link to the resources claimed (as compared, for example, to a royalty).</li> </ul>	<p><b>Yes, subject to 10% cap (absent a law change)</b></p> <ul style="list-style-type: none"> <li>• Separate classes of shares with preferential returns are possible under company law and NZX listing rules.</li> <li>• Under the new Part 5A of the PFA, the Crown is required to hold at least 51% of all classes of securities. No other investor may have a relevant interest in &gt;10% of each class.</li> <li>• If Māori hold ≤10%, the Crown will have to hold the balance, i.e. ≥90%.</li> <li>• If Māori wish to hold more than 10%, no party could hold a relevant interest &gt;10% meaning shareholding blocks would have to be held by unrelated parties and no agreements could exist between those parties regarding the exercise of voting rights attached to their respective shares.</li> <li>• A law change could address these constraints.</li> </ul>	<p><b>Potentially</b></p> <ul style="list-style-type: none"> <li>• Special shares would need to be issued ahead of listing.</li> <li>• The special shares would not be tradable given they relate to an underlying right held only by particular shareholders. Or, if they were tradable, the enhanced rights would need to fall away when they are sold. Sale would require the approval of the Crown if that sale would have the effect of diluting the Crown below 51% ownership, as the Crown would then be required to purchase shares to stay above 51%. Insider trading rules may, however, impact on the Crown’s ability to purchase shares.</li> </ul>	<p><b>Some, or significant compromise</b></p> <ul style="list-style-type: none"> <li>• Preferential shares for one class of shareholders would reduce the value of the ordinary minority shares being sold at IPO. By how much depends on the nature of the preferential return required (may be manageable, but will be a focus for investors).</li> <li>• Special shares could not be issued ahead of listing on the government’s timetable to float MRP in 2012 (not manageable).</li> <li>• Depending on the level of preferential returns, the company might need to ration capital, which would impact company performance, growth prospects, dividend policy, capital structure and potentially electricity market performance: these implications will all go to the value achieved by the Crown.</li> <li>• Special shares may also hinder the company’s ability to raise additional capital in the future.</li> </ul>	<p><b>Not practically achievable</b></p> <ul style="list-style-type: none"> <li>• Absent an NZX waiver, the issue of special shares would need approval of shareholders by ordinary resolution. Potentially, the Crown may not be able to vote.</li> <li>• The constitution could be amended post-listing to provide for the issue of special shares but the Crown, as the holder of only 51% of the company, could not ensure that the resolution was passed (requires 75%) and under the Listing Rules. NZX may, in any event, require non-Crown shareholders to approve the issue of special shares.</li> </ul>	<p><b>Unlikely</b></p> <ul style="list-style-type: none"> <li>• May be very hard for directors to determine the consideration to be provided for the shares and certify that the issue of the special shares is fair and reasonable to the company and all existing shareholders.</li> </ul>



Rights	Test 1 - Substitutability	Test 2 – Feasibility pre-listing			Test 3 – Feasibility post-listing	
Nature of the enhanced right	Relevance as form of Treaty redress – can the right be provided in another way?	Can the right be granted under company or other law or regulations?	Can the right be implemented in a practical terms?	What is the impact on the government's policy objectives (fiscal, efficiency, market development)	Can the right be granted under company or other law or regulations?	Can the right be implemented in a practical terms?
<p>Enhanced voting rights – over issues normally controlled by shareholders:</p> <ul style="list-style-type: none"> <li>• Appointment of directors.</li> <li>• Major transactions.</li> <li>• Some share issues/repurchases.</li> <li>• Changes to the constitution.</li> <li>• Related party transactions.</li> </ul>	<p><b>Yes</b></p> <ul style="list-style-type: none"> <li>• The level of voting rights can be increased by increasing Māori's shareholding (up to 10%, absent a law change).</li> <li>• Within some limits, the Crown can enter into an agreement with Māori on how it will exercise its 51% voting rights on certain matters, e.g. to procure the appointment of a director nominated by Māori interests.</li> <li>• The link provided to the resource via MRP as only one user of the resource would be very indirect. It would not provide a distinctive Maori voice on management matters. This could be better achieved in other ways, e.g. enhanced regulatory involvement.</li> </ul>	<p><b>Yes, subject to 10% cap (absent a law change), and within limits</b></p> <ul style="list-style-type: none"> <li>• Separate classes of shares with enhanced voting rights are possible.</li> <li>• The same issues arise under the 51% floor and 10% cap as for preferential financial returns.</li> <li>• Benefit may be limited as, for example, any director appointed to represent Māori would need to act in the best interests of the company – not of their appointer, or of designated interests or to protect relevant resources. In addition, the director may be unable to share company confidential information with wider stakeholder group, so unable to consult with represented interests on many strategic matters relating to use of resources.</li> <li>• Alternatively, Māori could be granted the right under the constitution to appoint a set number of directors to the board, provided their appointees are acceptable to the Crown and the board (acting reasonably).</li> </ul>	<p><b>Potentially</b></p> <ul style="list-style-type: none"> <li>• Special shares would need to be issued ahead of listing.</li> <li>• There are examples in the region of corporations collapsing separate classes of shares for reasons including valuation, investor confidence and access to capital.</li> <li>• The cost of separate classes of shares can be significant if not managed effectively.</li> <li>• The special shares would not be tradable given they relate to an underlying right held only by particular shareholders. Or, if they were tradable, the enhanced rights would need to fall away when they are sold. Sale would require the approval of the Crown if that sale would have the effect of diluting the Crown below a 51% ownership, as the Crown would then be required to purchase shares to stay above 51%. Insider trading rules may, however, impact the ability of the Crown to purchase shares.</li> </ul>	<p><b>Some, significant, or fatal compromise</b></p> <ul style="list-style-type: none"> <li>• There is evidence that representative boards perform less well than independent boards.</li> <li>• Any indication that the Crown intended to take a non-commercial approach to the ongoing management of its shareholding would impact adversely on company value and the consequent fiscal and macroeconomic benefits from reducing Crown debt using sale proceeds.</li> <li>• Providing open ended or poorly defined commitments to take instruction on how to vote the Crown's 51% shareholding would not be feasible as it would have significant negative equity markets consequences. Incoming minority shareholders at IPO would interpret this as diminishing their voting rights and would be concerned as to the quality of potential board appointments to drive value.</li> </ul>	<p><b>Not practically achievable</b></p> <ul style="list-style-type: none"> <li>• Absent an NZX waiver, the issue of special shares would need approval of shareholders by ordinary resolution. Potentially, the Crown may not be able to vote on such resolution.</li> <li>• Technically, the constitution could be amended post-listing to provide for the issue of special shares but the Crown, as the holder of only 51% of the company, could not ensure that such a resolution was passed (requires 75%) and under the Listing Rules NZX may, in any event, require non-Crown shareholders to approve the issue of special shares.</li> </ul>	<p><b>Unlikely</b></p> <ul style="list-style-type: none"> <li>• May be very hard for directors to determine the consideration to be provided for the shares and certify that the issue of the special shares is fair and reasonable to the company and all existing shareholders.</li> </ul>



Rights	Test 1 - Substitutability	Test 2 – Feasibility pre-listing			Test 3 – Feasibility post-listing	
Nature of the enhanced right	Relevance as form of Treaty redress – can the right be provided in another way?	Can the right be granted under company or other law or regulations?	Can the right be implemented in a practical terms?	What is the impact on the government's policy objectives (fiscal, efficiency, market development)	Can the right be granted under company or other law or regulations?	Can the right be implemented in a practical terms?
<p>Voting/decision rights on strategic or management decisions (not normally controlled by shareholders):</p> <ul style="list-style-type: none"> <li>Approval or veto rights over certain decisions.</li> <li>Rights to active participation in decision making on how the companies are to be operated.</li> <li>Illustrative examples could include prohibition on sales of specific assets, management of water flows, targeting particular employment outcomes.</li> </ul>	<p><b>Yes</b></p> <ul style="list-style-type: none"> <li>Direct Māori voice/control in relation to water resources can be achieved through reform of the regulatory system and/or individual Treaty settlements. This is a significantly more direct and meaningful connection with the resource than voice/control in relation to business decisions of one user (or a handful of users) of the resource, constrained by company law obligations.</li> <li>As MRP is only one user of the resource this mechanism provides only a very indirect influence. Enhanced involvement in regulatory regimes is a superior approach to provide a distinctive Maori voice on management matters.</li> </ul>	<p><b>Partially, at best</b></p> <ul style="list-style-type: none"> <li>Special shares or company constitutions could confer special approval/veto rights on certain shareholders, for example on decisions relating to water or geothermal management or resources (similar to Kiwisha).</li> <li>Any shareholder that exercises or controls the exercise of a power that would otherwise be exercised by the board becomes a deemed director (s126(1)(b)(iii) and (2)) and would therefore be bound by the obligation to act in the best interests of the company rather than in the interest of the shareholder or specific persons. However, there is uncertainty as to whether this requirement applies to decisions about the company's share structure or to veto rights where the board has made a decision but shareholder approval is also required.</li> </ul>	<p><b>Potentially</b></p> <ul style="list-style-type: none"> <li>Companies would be designated "non-standard" and listing rule and NZX waivers would be required.</li> <li>Securing approval to commercial proposals by the holder of the rights will prove difficult in reasonable commercial timeframes if lengthy consultation processes with stakeholders are required, impacting MRP performance. In addition, there are legal constraints on the release of price-sensitive information by the company to shareholders and other persons.</li> <li>Management will not be able to operate effectively, which can undermine the quality of personnel attracted to senior positions and adversely impact on value.</li> </ul>	<p><b>Not manageable</b></p> <ul style="list-style-type: none"> <li>Even if this was possible, it could have a significant negative effect on the value of the companies and hence proceeds, and on the companies' operational and financial performance, growth prospects and the electricity market as well as adverse economic outcomes.</li> <li>It is very likely that the IPO of MRP would not be able to proceed if a specific party had the ability to influence management and potentially drive the company to uneconomic outcomes. New investors would anticipate the worst possible outcome and price accordingly, which would destroy the value the Crown could realise.</li> <li>To the extent that the companies make non-commercial decisions, this may advantage competitors including those with full private ownership.</li> </ul>	<p><b>Not practically achievable</b></p> <ul style="list-style-type: none"> <li>Absent an NZX waiver, the issue of special shares would need approval of shareholders by ordinary resolution. Potentially, the Crown may not be able to vote on such resolution.</li> <li>Technically, the constitution could be amended post-listing to provide for the issue of special shares or to confer these rights direct but the Crown, as the holder of only 51% of the company, could not ensure that such a resolution was passed (requires 75%) and under the Listing Rules NZX may, in any event, require non-Crown shareholders to approve the issue of special shares.</li> </ul>	<p><b>N/A</b></p>