

The Treasury

Solid Energy Information Release

March 2013

Release Document

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CROWN OWNERSHIP
MONITORING UNIT

Treasury Report: Solid Energy's Draft Statement of Corporate Intent for the Three Years Commencing 1 July 2010

Date:	3 September 2010	Report No:	T2010/1655
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Action Sought

	Action Sought	Deadline
Minister of Finance (Hon Bill English)	Agree that the Minister for SOEs should sign the attached letter to the Chair of Solid Energy	Tuesday 7 September 2010
Minister for State Owned Enterprises (Hon Simon Power)	Agree and sign the attached letter to the Chair of Solid Energy	Wednesday 8 September 2010
Associate Minister of Finance (Hon Steven Joyce)	Note contents of report	Wednesday 8 September 2010

Contact for Telephone Discussion (if required)

Name	Position	Telephone	1st Contact
Andrew Blazey	Manager, Sector Monitoring	[1]	✓
[4]	Analyst, Sector Monitoring	[1]	

Minister of Finance's Office Actions

Once report signed by the Minister of Finance, please forward to Minister for State Owned Enterprises.

Minister for SOE's Office Actions

Once agreed by the Minister of Finance and Minister for SOE's, please post signed letter.

Enclosure: Yes (attached)

Treasury Report: Solid Energy's Draft Statement of Corporate Intent for the Three Years Commencing 1 July 2010

Purpose of Report

1. The purpose of this report is to provide you with a letter of response to Solid Energy Limited (SEL) on its revised Statement of Corporate Intent (SCI).

Analysis

Background

2. On 14 July 2010, shareholding Ministers wrote to SEL advising that the draft SCI, received on 1 July 2010, did not meet their expectations as the SCI:
 - forecasts the introduction of external equity which is not consistent with the Government's current policies; and
 - suspends dividends before approval is given to invest in major capital projects.
3. On 30 August 2010, SEL provided a revised SCI which addressed concerns regarding the introduction of external equity. However, the SCI is still inconsistent with the priority the Government gives to receiving consistent and improving dividends from State Owned Enterprises.

Establishing a balance between dividends and investment

4. Rather than striking an appropriate balance between the payment of dividends and retaining cash for future investment, the SEL Board continues to place capital investment ahead of providing dividends. Dividends appear to be treated as a residual item, only to be paid after all capital requirements have been met and subject to maintaining a 35% gearing ratio (projected two years ahead).
5. To establish an appropriate balance between investment and the payment of dividends SOE dividend policies normally require that dividends are set as a percentage of net profit after tax (NPAT) or a percentage of net operating cash-flow. The SEL dividend policy does not contain any link to profits.
6. We consider that not having a linkage between profits and dividends reduces the discipline on boards to prioritise dividend payments.
7. Although SEL has requested support to suspend dividends for proposed future capital investment, if the investments are sound then these investments should increase the commercial value of SEL and therefore not necessitate the suspension of dividends.
8. In addition, as indicated by SEL to you at the meeting of 31 August 2010, the investment opportunities are independently fundable.

9. While SEL focuses on maintaining gearing of less than 35% of total shareholders equity, the level of gearing is only 5% for 2010 when calculated on SELs own commercial valuation [T2010/1239 refers]. If SEL considers that \$3.5 billion is a robust estimation of its commercial value then SEL should not have difficulty in sourcing further debt financing above the 2010 debt level of \$180 million.

Recommended Action

We recommend that you:

- a **note** that the revised SCI does not propose the payment of dividends and is therefore inconsistent with the Government's priority to receive consistent and improving dividends from State Owned Enterprises;
- b **sign** the attached letter to the Chair of SEL, John Palmer, advising that:
 - i. this Government gives priority to receiving consistent and improving dividends from State Owned Enterprises;
 - ii. an SCI that has no dividend payments does not achieve an appropriate balance between dividends and retaining cash for future investment; and
 - iii. Shareholding Ministers expect to see dividends in the forecast financial statements of the SCI.

Agree/disagree.

Minister of Finance

Agree/disagree.

Minister for State Owned Enterprises

Andrew Blazey
**Manager, Sector Monitoring
for Secretary to the Treasury**

Hon Bill English
Minister of Finance

Hon Simon Power
Minister for State Owned Enterprises

Mr John Palmer
Chair
Solid Energy New Zealand Ltd
PO Box 1303
CHRISTCHURCH 8140

Dear Mr Palmer

Statement of Corporate Intent 2010-13

Thank you for providing me with a revised SCI on 30 August 2010. I note that previous concerns regarding the introduction of external equity have been addressed. However, the revised SCI still does not meet shareholding Ministers' expectations as it does not include the payment of dividends.

This Government gives priority to receiving consistent and improving dividends from State Owned Enterprises (SOEs). Shareholding Ministers therefore expect SOE boards to strike an appropriate balance between the payment of dividends and retaining cash for future investment. An SCI that has no dividend payments does not achieve that balance and we would therefore expect the SCI to show dividends over the forecast period.

As you indicated when we met on 31 August 2010, the investment opportunities are independently fundable. If this is the case, then viable investments need not to come at the expense of dividend payments.

Further, shareholders would expect to be consulted if a proposed investment might negatively impact on a dividend payment.

I look forward to receiving an SCI aligned to shareholding Ministers' expectations, and request that 60 copies of the SCI be delivered to my office (c/o Emily Richards) by 30 September 2010, for tabling in the House of Representatives.

Yours sincerely

Hon Simon Power
Minister for State Owned Enterprises

cc: Don Elder
Chief Executive Officer
Solid Energy New Zealand Ltd