

# **The Treasury**

## **Solid Energy Information Release**

**March 2013**

### **Release Document**

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- [1] 9(2)(a) - to protect the privacy of natural persons, including deceased people
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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:** Solid Energy NZ Ltd (Solid Energy): Preparation for the 2011 Annual General Meeting (AGM)

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|--------------|-----------------|-------------------|------------|
| <b>Date:</b> | 14 October 2011 | <b>Report No:</b> | T2011/2224 |
|--------------|-----------------|-------------------|------------|

**Action Sought**

|  | <b>Action Sought</b>        | <b>Deadline</b>         |
|--|-----------------------------|-------------------------|
| Minister of Finance<br>(Hon Bill English)                | <b>Note</b> recommendations | Monday, 17 October 2011 |
| Minister for State Owned Enterprises<br>(Hon Tony Ryall) | <b>Note</b> recommendations | Monday, 17 October 2011 |
| Associate Minister of Finance<br>(Hon Steven Joyce)      | For your information        | None                    |

**Contact for Telephone Discussion** (if required)

| <b>Name</b>      | <b>Position</b>            | <b>Telephone</b> | <b>1st Contact</b> |
|------------------|----------------------------|------------------|--------------------|
| [4]              | Analyst, Sector Monitoring | [1]              | ✓                  |
| James Cunningham | Manager, Sector Monitoring | [1]              |                    |

**Minister of Finance's Office Actions** (if required)

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|-------|
| None. |
|-------|

**Minister for State Owned Enterprises' Office Actions** (if required)

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| None. |
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**Enclosure:** Yes

## **Treasury Report: Solid Energy NZ Ltd (Solid Energy): Preparation for the 2011 Annual General Meeting (AGM)**

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### **Purpose of Report**

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1. This report provides background material for the Solid Energy AGM which will be held in Christchurch at 12.30pm on Tuesday 18 October 2011. We are specifically reporting in advance of this AGM because it is more likely to be contentious. This is because of ongoing debate we are having with Solid Energy about its commercial valuation disclosure and because of the Mixed Ownership Model (MoM) Scoping Study results.

### **Background**

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2. The purpose of the AGM is for shareholding Ministers to have a free and frank discussion about company performance and to communicate shareholder expectations directly to the board.
3. Solid Energy's Annual Public meeting will be held on the same day as the AGM, 3.30pm at the Middleton Grange School auditorium. We understand that neither shareholding Minister is available to attend the AGM or Public Meeting. Proxy forms appointing a COMU representative ([4] and failing that, John Crawford) have already been prepared.

### **Attendees**

4. Solid Energy will be represented at the AGM by its Board and members of the senior management team. Officials from COMU, including members of the Commercial Transactions Group (CTG) (who have been involved with the Solid Energy MoM Scoping Study) will attend. No media or members of the public will be in attendance.

### **Meeting Agenda and Questions for the Chair**

5. Solid Energy has provided an agenda which is attached in Annex 1. The items on the agenda are typical for an AGM. Agenda item 'D' (Shareholder Questions), provides a forum for discussing the company's performance. Paragraph 17 details those issues which COMU proposes to comment on to the Solid Energy Board at the AGM, on behalf of shareholding Ministers.

### **Solid Energy's 2010/11 Financial Year Performance**

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6. Solid Energy produced a net profit after tax (NPAT) of \$87.2 million for the 2010/11 year. This result is \$21.1 million higher than plan and \$19.4 million higher than the 2009/10 year NPAT of \$67.8 million. Both Operating Margin<sup>1</sup> and EBITDA (earnings before interest, taxation, depreciation and amortisation) for the year were above budget.

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<sup>1</sup> The Operating Margin measures the profitability of the company per dollar of revenue and is calculated as EBITDAF (earnings before interest, taxation, depreciation, amortisation and financial instruments) divided by revenue, expressed as a percentage.

7. However, 2010/11 was a year of mixed fortunes for Solid Energy. Higher than forecast export coal prices improving the export coal margins. However, a significant impact of the Christchurch earthquakes was a reduction in the coal volume exported due to damage to the Lyttelton Port infrastructure (to both the wharf and the coal loader), leading to the cancellation of three planned shipments. Total coal sales of 4.1 million tonnes was 0.6 million tonnes below budget, but still ahead of last year.
8. Solid Energy's coal and logistics revenues accounted for 96% of total revenue. The remaining revenue came from 'renewables', being Switch, Biodiesel and Nature's Flame. Only Biodiesel was above its revenue target, and for all the non-coal businesses their total expenses exceeded revenue by \$14.8 million.
9. Given the renewable businesses' lack of profitability, and under performance on sales targets<sup>2</sup> the Net Present Value (NPV) of these projects is likely to be significantly lower than originally planned. This is of particular concern given the investment by Solid Energy to date (in excess of \$100 million). This also raises concerns about Solid Energy's ability to successfully develop businesses outside of its conventional coal business.

### **2010/11 Dividend**

10. Solid Energy has already paid total dividends of \$50 million for the year, which is \$30 million above the level forecast in its 2011 Statement of Corporate Intent (SCI). However, the dividend is consistent with its dividend policy which effectively sets a minimum dividend, published in the SCI, with further distributions being paid when actual NPAT is higher than budget. Solid Energy is yet to determine whether it will pay any further dividend in respect of the 2010/11 year.

### **Transparency of Performance**

11. The Solid Energy annual report does not provide separate financial details of the performance of its differing areas of operation (such as Switch, Biodiesel and Nature's Flame). It is therefore not possible to determine from the annual report which areas of the business are profitable and which are not. The lack of clarity is inconsistent with shareholding Ministers' expectations for greater disclosure and an increased amount of performance information being made publicly available. We intend to question the Board as to how, or if, it intends to increase the transparency of disclosure about its non-coal businesses.

### **Solid Energy's 2012 Draft SCI**

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12. Under section 14(4) of the State-Owned Enterprises Act 1986 (the SOE Act) shareholding Ministers agreed to extend the date for receipt of the draft SCI to 30 September 2011 so that the Board could fully consider outstanding issues. Specifically, as recently reported, COMU does not consider that the current SCI is suitable for tabling, given concerns we have with the commercial valuation disclosure (T2011/2143 refers).
13. Although COMU has highlighted to Solid Energy shareholding Ministers' expectations with respect to the commercial valuation disclosure, the Board has chosen not to comply with the requested disclosure. To date the Board has simply provided the commercial valuation, without detailing assumptions or providing any commentary on how the valuation has changed since the last year's SCI and nor has the valuation been peer-reviewed. Therefore a reader of the Solid Energy SCI could not meaningfully understand how the valuation is derived.

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<sup>2</sup> Solid Energy has in its SCI, year-on-year, reduced its forecast sales of each product (Wood Pellets, Biodiesel, Coal Seam Gas, Underground Coal Gasification, and Briquettes).

14. Not only does the Solid Energy disclosure not provide the transparency which shareholding Ministers have requested, it is also questionable if the disclosure fully meets the requirement under the SOE Act (Part 3 - Accountability Section 3) of including "...a statement of the manner in which that value was assessed".
15. In T2011/2143 we advised the Minister for State Owned Enterprises to write, on behalf of shareholding Ministers, to the Solid Energy Board requesting it reconsider its position on the commercial valuation disclosure and to resubmit an SCI with a more extensive explanation of the valuation. It is likely that the Board may seek to discuss the commercial valuation disclosure at the AGM.

### Mixed Ownership Model (MoM) Solid Energy Scoping Study Results

16. UBS has prepared its draft scoping study report on Solid Energy. UBS presented the report to the management of Solid Energy on 13 October 2011. Members of CTG will be present at the Solid Energy Board meeting to discuss the report.

### Comments and Questions for the Solid Energy Board

17. At the AGM, on behalf of shareholding Ministers, COMU proposes to comment that:
  - despite the disruptions of the Christchurch earthquakes this has been a good year for the coal business. In particular, higher volumes of coal sales were achieved at prices higher than forecast. Shareholders appreciate the efforts of staff and management over this year in achieving these results in the face of adversity caused by the Canterbury earthquakes.
  - although it was a good year for the coal business we note that all other areas of the business continue to be unprofitable. In addition, production in those other areas of the business was below budget (including Coal, Wood Pellets, Biodiesel, Gas, and Briquettes). How does the Board see the prospects for the renewable businesses and when does the Board see these businesses becoming profitable?
  - Solid Energy is becoming an increasingly diverse business and one of Ministers' expectations for SOEs has been to increase the transparency of SOEs through greater public disclosure. In this context, what consideration has been given to providing greater transparency in public reporting? For instance has Solid Energy considered including divisional accounts within its annual report?, and
  - what does the Board see, excluding the MoM considerations, as the priorities for the management team for the 2011/12 year?

### Board Matters

18. There are eight directors on the Solid Energy Board. Two of these (Mr Alan Broome and Mrs Adrienne Cooper) have terms which expire in April 2012. Depending on the results of the MoM scoping studies, and any subsequent decisions, further consideration of the composition of the Board may be required.

## Recommended Action

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We recommend that you:

- a **note** Solid Energy has provided an agenda for its AGM on Tuesday 18 October 2011 (see Annex 1)
- b **note** that Solid Energy will also have its annual public meeting on the same day as the AGM
- c **note** paragraph 17 indicates what issues, on behalf of shareholding Ministers, COMU proposes to comment on to the Solid Energy Board, and
- d **note** that proxy forms have already been prepared, as we understand that shareholding Ministers will not be attending. These appoint a COMU representative ([4] and failing that, John Crawford) as your proxy to attend the Solid Energy AGM.

James Cunningham  
**Manager, Sector Monitoring  
for Secretary to the Treasury**

Hon Bill English  
**Minister of Finance**

Hon Tony Ryall  
**Minister for State Owned Enterprises**

## **Appendix 1: AGM Agenda supplied by Solid Energy**



**SOLID ENERGY**  
Coals of New Zealand

## **NOTICE OF ANNUAL GENERAL MEETING 2011**

Notice is given that the 2011 Annual Meeting of Shareholders of SOLID ENERGY NEW ZEALAND LIMITED will be held at Solid Energy's offices at 15 Show Place, Addington Christchurch, at 12.30 p.m. Tuesday 18 October 2011.

### **Business**

- A. Chairman's Introduction**
- B. Chief Executive Officer's Review**
- C. Financial Statements**

In relation to Solid Energy's Annual Report for the year ended 30 June 2011, to receive Solid Energy's financial statements for that period and the auditor's report on those financial statements.

- D. Shareholder Questions**

Consideration of any shareholder questions submitted prior to the Annual Meeting or raised from the floor through the Chairman.

- E. Ordinary Resolutions**

To consider and, if thought fit, to pass the following ordinary resolutions:

### **Annual Report**

The Annual Report 2011 that has been tabled is accepted by the shareholders, in particular:

- 1.1 The report of Mr JL Palmer, Chairman of Directors, as set out on pages 6-7 of the Annual Report and Dr DM Elder, Chief Executive Officer, as set out on pages 8-10 of the Annual Report;
- 1.2 The Financial Statements for the year ended 30 June 2011 (dated 22 August 2011) and Notes to those Statements as set out on pages 49-95 of the Annual Report; and
- 1.3 The report of KPMG on behalf of the Auditor-General as set out on page 96.



## **Dividend**

The shareholders note the decision of the Directors of the Company to pay a dividend of 49.3 cents per share amounting in total to \$30 million. The dividend was declared on 22 August 2011 to be paid to the shareholders on 30 September 2011.

To note the confirmed Minutes of the Annual Meeting of Shareholders of Solid Energy New Zealand Limited held 21 October 2010.

*An ordinary resolution is a resolution that is approved by a simple majority of the votes of those shareholders entitled to vote and voting on a resolution.*

## **Eligibility to Vote**

Any shareholder whose name is recorded in the Solid Energy share register at 1 October 2011 is entitled to attend the Annual Meeting and vote either in person or may appoint a proxy to attend and vote instead of the shareholder.

## **Casting Your Vote**

You may cast your vote in one of two ways:

### **1. Personal Attendance**

If you wish you can attend the Annual Meeting and vote.

### **2. Proxy**

If you do not plan to attend the meeting you can appoint a proxy to attend the meeting and vote on your behalf.

The voting/proxy form appointing a proxy must be received by Solid Energy no later than close of business on 11 October 2010 and may be posted (P.O. Box 1303 Christchurch), faxed 03 345 6069 attention: Company Secretary or emailed as a PDF document to the Company Secretary ([bill.dwyer@solidenergy.co.nz](mailto:bill.dwyer@solidenergy.co.nz)).

If you do not plan to attend the meeting you should complete the voting/proxy form and return it as soon as possible.



Bill Dwyer  
Company Secretary  
Solid Energy New Zealand Limited