

The Treasury

Ruataniwha Dam Information Release

Release Document

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Treasury Report: Crown Irrigation Investments Ltd: 2013 Draft Statement of Intent and Business Plan

Date:	23 September 2013	Report No:	T2013/2176
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Action Sought

	Action Sought	Deadline
Minister of Finance (Hon Bill English)	Agree to the recommendations	Friday, 27 September 2013
Associate Minister of Finance (Hon Steven Joyce)	For your information	None
Associate Minister of Finance (Hon Dr Jonathan Coleman)	For your information	None
Minister for Primary Industries (Hon Nathan Guy)	Agree to the recommendations and sign the attached letter to the Chair of Crown Irrigation Investments	Friday, 27 September 2013

Contact for Telephone Discussion (if required)

Name	Position	Telephone	1st Contact
Aaron Gill	Senior Advisor, Monitoring - Commercial	[1]	N/A (mob) ✓
James Cunningham	Manager, Monitoring - Commercial	[1]	[1]

Minister for Primary Industries' Office's Actions

Send the attached letter to Crown Irrigation Investments Ltd's Chair and a copy to the acting Chief Executive

Enclosure: Yes [\(Crown Irrigation 2013/14 draft SOI 19 August \(2\):2719288\)](#)

Treasury Report: Crown Irrigation Investments Ltd: 2013 Draft Statement of Intent and Business Plan

Executive Summary

Crown Irrigation Investments Ltd (Crown Irrigation) has delivered its draft 2013 Statement of Intent (SOI) and Business Plan.

The purpose of Crown Irrigation as outlined in its constitution is to implement government policy by co-investing in off-farm irrigation schemes which are expected to be commercially viable in the long term; and seek to exit those investments once they become commercially viable. COMU considers that Crown Irrigation's scope, objectives and outcomes in its SOI and Business Plan reflect this.

Crown Irrigation has divided its initial work plan into two key phases: establishing the company and beginning to engage with prospective irrigation scheme sponsors.

Crown Irrigation has not included any investments in irrigation schemes in this SOI as it does not yet have sufficient information from prospective schemes. [2],[3],[4]
[2],[3],[4]

Crown Irrigation will not be a large organisation. It will manage the 'lumpy' workload associated with assessing, making and exiting investments by relying on specialist advisors and contractors. It will maintain a core team of permanent staff who are able to manage investments and support functions. During this three-year plan staff numbers are expected to reach a maximum of 8.5 full time equivalents (FTEs).

This plan includes operating expenditure of roughly \$2.7 million each year before transaction-related costs (estimated at \$1.6 million per year). We do not consider this to be unreasonable, when compared to other organisations of similar size and nature that we monitor. [6]

[7]

Crown Irrigation was incorporated with unpaid share capital of 80 million \$1 shares. The Minister for Primary Industries and the Minister of Finance each own 50% of these shares. The Crown must make a payment for any capital called by the company within 20 working days.

On incorporation, Crown Irrigation made a call on \$2.1 million of the uncalled share capital to fund its first six months of operations. It plans to make calls for operating expenditure, in line with its SOI, every six months. Calls to fund investments in schemes will be made as required.

Recommended Action

We recommend that you:

- a **note** that Crown Irrigation has delivered its draft 2013/14 Statement of Intent (SOI) for shareholding Ministers' comments
- b **note** that the Board is currently recruiting a permanent CEO and that the appointee will be responsible for appointing permanent staff members
- c **note** that Crown Irrigation's SOI includes base operating expenditure of approximately \$2.7 million per year and transactional costs of \$1.6 million per year
- d [6]
- e **note** that Crown Irrigation's SOI does not include any investments in irrigation schemes in its first three years. [2],[3],[4]
- f [2],[3],[4]
- g **agree** that the Minister for Primary Industries should sign the attached letter to the Chair of Crown Irrigation, on behalf of the shareholding Ministers, asking the company to submit 50 copies of its SOI for tabling in the House of Representatives.

Agree/disagree.
Minister of Finance

Agree/disagree.
Minister for Primary Industries

James Cunningham
Manager, Monitoring - Commercial

Hon Bill English
Minister of Finance

Hon Nathan Guy
Minister for Primary Industries

Treasury Report: Crown Irrigation Investments Ltd: 2013 Draft Statement of Intent and Business Plan

Purpose of Report

1. This report provides a summary of the key issues and content of Crown Irrigation Investments Ltd's (Crown Irrigation's) draft 2013 Statement of Intent (SOI) and Business Plan and recommends that the SOI, in its final form, be tabled in the House of Representatives.

Background

2. In December 2012 Cabinet agreed to invest up to \$400 million into irrigation infrastructure. Cabinet noted that "Unlocking reliable water, through well designed water storage and off-farm irrigation infrastructure, will support ongoing economic growth in the context of a reformed water management system which is based on setting and managing within limits for water quality and quantity" [EGI Min (12) 29/5 refers].
3. Due to the complexity of the decisions required and the size and commercial nature of the investments Cabinet agreed to establish a Crown-owned company to manage the Crown's investment in irrigation. Accordingly, Crown Irrigation was incorporated on 1 July 2013 under the Companies Act 1993 and is a Crown-entity company listed on Schedule 2 of the Crown Entities Act 2004 (the Act). Crown Irrigation has an independent Board appointed by the Minister for Primary Industries on advice provided by COMU's Appointments and Governance team.
4. In accordance with section 140(1) of the Act, as a newly established entity, Crown Irrigation must prepare its initial SOI as soon as practicable after its establishment date. In line with the shareholding Ministers' expectations set out in the 2013/14 Letter of Expectations, Crown Irrigation submitted its draft SOI for comment prior to 31 July 2013.
5. For the 2013/14 financial year the Government appropriated \$80 million for Crown Irrigation to use for both investing in irrigation schemes and for its operating costs.

Scope of Business

6. The purpose of Crown Irrigation as outlined in its Constitution is to implement government policy by co-investing in off-farm irrigation schemes which are expected to be commercially viable in the long term; and to seek to exit those investments once they become commercially viable. In doing so it will:
 - Seek to avoid investing in irrigation schemes where its investment will replace or crowd out alternative investment which is available to a scheme
 - Manage its investments using best practice management approaches, and
 - Not seek a controlling interest in those schemes.COMU considers that Crown Irrigation's scope, objectives and outcomes in its SOI and Business Plan reflect this.
7. Crown Irrigation has divided its initial work plan into two key phases: establishing the company and beginning to engage with prospective irrigation scheme sponsors.

Key Risks

Timeliness of Schemes Reaching the 'Investment Ready' Stage

8. Crown Irrigation will only make investments in irrigation schemes where the schemes are found to be 'investment ready'. The summary investment strategy in Appendix One sets out what is required to be 'investment ready'.
9. It is not Crown Irrigation's role to assist schemes to become 'investment ready'. Therefore there is a risk that Crown Irrigation will not achieve its objectives if schemes do not achieve this and it does not proceed with investments. However, the Irrigation Acceleration Fund (IAF)¹ has received Government funding for this purpose.

Funding

10. In the 2013/14 budget the Government appropriated \$80 million through vote Primary Industries for Crown Irrigation to invest in irrigation schemes and for its operating expenditure. The Government has commented that it is willing to invest up to \$400 million for this purpose; however it is unknown when additional amounts will be appropriated because those are decisions for future budgets.
11. [6]
12. [5]

Success of Irrigation Schemes

13. There are a number of risks to the Crown's investment in relation to the success of irrigation schemes which Crown Irrigation invests in. These risks include build risk of the scheme, management of the scheme and uptake by farmers.
14. Crown Irrigation will obtain engineering advice on prospective schemes and will monitor progress of the build. The 'investment ready' requirements in Appendix One include that the scheme needs to be affordable to farmers, and this should ensure farmer uptake is achieved.

Performance

Forecast Investments

15. Crown Irrigation has not included any investments in irrigation schemes in its SOI. There are two reasons for this; the first is that its investment pipeline is still being developed. Until expressions of interest are received from scheme sponsors and Crown Irrigation has had time to consider these, the level of potential investments in the next three years is unknown.

¹ The IAF is a programme run by MPI with the main purpose of supporting regional-scale, rural, water infrastructure proposals. The 2011 Budget allocated the IAF \$35 million over five years to support the development of irrigation infrastructure proposals to the 'investment-ready' prospectus stage.

16. The second reason is that, as it only expects to make a small number of investments in any one financial year, including in the SOI the expected value of investments which have not yet been negotiated could impact on the commercial negotiations.
17. [2],[3],[4]

18. [2],[3],[4]

Forecast Operational Expenditure

19. Crown Irrigation has not forecast any revenue over the three years covered by this plan. We understand that once funding is finalised, schemes are likely to take a number of years to build the planned irrigation infrastructure. Therefore, we would not expect Crown Irrigation to be budgeting any revenue in its early years.
20. Crown Irrigation will not be a large organisation. It will manage the 'lumpy' workload associated with assessing, making and exiting investments by relying on specialist advisors and contractors. It will maintain a core team of permanent staff who are able to manage investments and support functions. During this three-year plan staff numbers are expected to reach a maximum of 8.5 full time equivalents (FTEs).

Table 2. Forecast Operational Expenditure

\$ millions	2013/14	2015/16	2016/17	Total
Staff Costs	1.6	1.7	1.8	5.1
Transaction Costs	1.6	1.6	1.6	4.8
Board Costs	0.4	0.3	0.3	1.0
Other	0.7	0.6	0.7	2.0
Total	4.3	4.2	4.4	12.9

Source: Crown Irrigation's 3-year Business Plan 1 July 2013 – 30 June 2016

21. This plan includes operating expenditure of roughly \$2.7 million each year before transaction related costs. We do not consider this to be unreasonable, when compared to other organisations of similar size and nature that we monitor. ^[6]
[6]

Non-Financial Performance

22. Crown Irrigation's Board is in the process of recruiting a Chief and Executive and this position is expected to commence at the end of the 2013 calendar year. Currently all staff are temporary with permanent appointments to be a responsibility of the Chief Executive.
23. Crown Irrigation has the following one-year non-financial targets:
- To be fully independent from MPI with processes and systems established that mean it is fully operational
 - To be able to engage with prospective scheme sponsors without unduly holding up the development of irrigation schemes and be ready and able to complete negotiations and invest in schemes, consistent with the investment objective, and
 - Have an improved view of the pipeline of prospective schemes.
24. Crown Irrigation has the following three-year non-financial targets:

Leadership in the Irrigation Sector

- Engaging with all known prospective irrigation scheme sponsors and wider stakeholders
- Advising prospective irrigation schemes of requirements and expectations for Crown Irrigation investment

Investment Process

- Engage with all schemes that submit a Registration of Interest to Crown Irrigation, and
- Progress negotiations, and make investments, to the extent consistent with Crown Irrigation's investment objective and process and where schemes meet Crown Irrigation's investment criteria.

Capital Expenditure, Dividend Policy and Capital Structure

Capital Expenditure

25. Crown Irrigation will not incur any significant capital expenditure. As an investment company capital expenditure will be limited to office furniture and IT equipment.

Dividend Policy

26. [2],[3],[4]

27. There are no returns of capital expected in the period of this initial three-year plan.

Capital Structure

28. As a Crown-entity company, in accordance with section 162 of the Act, Crown Irrigation is restricted from raising debt without the joint approval from the entity's responsible Minister and the Minister of Finance. [2],[3],[4]
[2],[3],[4]

29. Crown Irrigation was incorporated with unpaid share capital of 80 million \$1 shares. The Minister for Primary Industries and the Minister of Finance each own 50% of these shares. The Crown must make a payment for any capital called by the company within 20 working days.
30. On incorporation, Crown Irrigation made a call on \$2.1 million of the uncalled share capital to fund its first six months of operations. It plans to make calls for operating expenditure, in line with its SOI, every six months. Calls to fund investments in schemes will be made as required.

Table 3. Forecast Capital Requirements

\$ millions	2013/14	2015/16	2016/17	Total
SOI (assuming no investments made)	4.9	4.2	4.3	13.4
[2],[3],[4]				

Source: Crown Irrigation's 2013 SOI and 3-year Business Plan 1 July 2013 – 30 June 2016

31. [2],[3],[4],[6]

Consultation

32. COMU has consulted with Ministry for Primary Industries on the content of this report and it agrees with the recommendations.

Appendix One – Summary Investment Strategy

Guidance has been developed to assist in identifying what schemes Crown Irrigation should invest in, how it will invest and on what terms. In particular, Crown Irrigation will invest:

1. In off-farm water storage and irrigation infrastructure that contributes regional economic benefits.
2. In schemes that are 'Investment Ready'. To be 'Investment Ready', schemes must:
 - a. Be technically feasible.
 - b. Have the required resource consents in place.
 - c. Be affordable to farm businesses.
 - d. Have sound governance and management structures and business planning processes.
 - e. Be commercially viable in the long term.
3. In schemes that are an appropriate size for the area to be irrigated over the longer term.
4. Such that it:
 - a. Is a minority investor (having less than 50% of the voting rights).
 - b. Minimises its investment in any given scheme.
 - c. Does not act as a scheme sponsor.
5. On the basis of a clear exit strategy:
 - a. The exit mechanism should be established as a condition of Crown Irrigation investment.
 - b. Crown Irrigation should be the first to exit when schemes become commercially viable.
 - c. Returns to schemes above a commercial rate should be used to accelerate Crown Irrigation exit.
6. On the basis of a rate of return that is greater than zero in nominal terms, less than a commercial rate (if necessary) but minimises the discount relative to the commercial rate.
7. If scheme risks are appropriately allocated between customers, suppliers, investors and lenders and the risks to Crown Irrigation are optimised.

Ms Alison Paterson
Chair
Crown Irrigation Investments Ltd
PO Box 5177
WELLINGTON 6145

Dear Ms Paterson

2013 STATEMENT OF INTENT AND BUSINESS PLAN

Thank you for providing shareholding Ministers with Crown Irrigation Investments Limited's (Crown Irrigation's) draft 2013 Statement of Intent (SOI) and Business Plan. We appreciate all of the time and effort which has gone into producing these documents.

Crown Irrigation has a busy three years ahead, establishing itself as an independent entity and engaging with prospective irrigation schemes. In common with all entities owned by the Crown, we expect the company to carefully manage its costs. ^[5]

[6]

Although Crown Irrigation will not invest in irrigation schemes until they have reached the 'investment-ready' stage we encourage you to engage with all known prospective schemes as early as possible and where appropriate to proceed to finalising investments.

We look forward to hearing of your progress through your monthly updates and wish you every success in the year ahead.

Please now have 50 copies of the final SOI forwarded to my office, for tabling in the House of Representatives. Please also pass on our thanks to the rest of your Board and the establishment staff of Crown Irrigation for their continuing efforts.

Yours sincerely

Hon Nathan Guy
Minister for Primary Industries
on behalf of shareholding Ministers

cc Mr Damian Diack, Interim Chief Executive Officer, Crown Irrigation Investments Ltd,
PO Box 5177, Wellington 6145