

Hon Bill English
ORIGINAL



Treasury Report: South Canterbury Finance Limited (SCF) - Liquidity Support

Date:	3 August 2010	Report No:	T2010/1436
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Action Sought

	Action Sought	Deadline
Minister of Finance (Hon Bill English)	<p>Note the attached letter from SCF seeking liquidity support.</p> <p>Agree that the request for support be declined at this time.</p> <p>Note that officials undertake further work on the possible provision Crown guarantee backing of liquidity support for SCF by way of Deed of Nomination in order to retain it as an option, should a compelling case for reconsidering liquidity support arise in the future</p> <p>Note that officials will not agree any future requests for liquidity support without reference to your office</p>	4 August 2010 to enable a prompt response

Contact for Telephone Discussion (if required)

Name	Position	Telephone	1st Contact
John Park	Manager	[Withheld under s9(2)(a)]	✓
Stephen Revill	Senior Solicitor		

Minister of Finance's Office Actions (if required)

Forward to the Prime Minister for his information.

Enclosure: Yes, attached
Letter from Bell Gully ^[s9(2)(a)] - Application for Nominated Beneficiary - 30 July 2010
(Treasury:1877818v1) Add to worklist

- 4 AUG 2010

3 August 2010


Treasury Report: South Canterbury Finance Limited - Liquidity Support

1. The Deposit Guarantee Team has received a letter from South Canterbury Finance Limited's (SCF) solicitors seeking backing through the Crown guarantee for a proposal from a "high net worth individual" to provide short term liquidity support for SCF (letter attached).
2. The proposal is designed to provide SCF with greater certainty in relation their liquidity position while SCF progresses other options to restructure and avoid failure. Treasury is in discussion with SCF in relation to those options but negotiations between SCF and potential investors have not yet reached a stage where a firm proposal is available for the Crown to evaluate.
3. The letter proposes that support be given by extending the benefit of the Crown guarantee to cover an investment of \$50,000,000 from an unnamed investor. The guarantee would be extended to the investor by way of a Deed of Nomination, since the amount to be invested is well in excess of the guarantee's normal liability cap of \$1 million.
4. SCF and its advisors noted in discussions last week that cash reserves have been relatively stable over recent weeks and forecast liquidity requirements are expected to be manageable over the next month at least.
5. Treasury does not consider that the provision of support is appropriate at this time. The Crown has consistently signalled it is reluctant to provide liquidity support in the past and Treasury is concerned that approval would undermine that position and may prejudice the Crown's position in relation to the restructuring proposals under development by SCF, including reducing the incentives on the company to ensure timely resolution.
6. Treasury is therefore proposing to respond to SCF stating that the Crown is unwilling to provide the Deed of Nomination required for the transaction to proceed at this time.
7. Treasury agrees with the views expressed in the letter that the proposed transaction would not increase the Crown's liability under the guarantee scheme. Treasury also agrees that the proposed approach involving a Deed of Nomination would be viable and could be delivered quickly and without the need for complex documentation as would be the case with a loan by the Crown.
8. Separately, Treasury will undertake further work on the Deed of Nomination option to allow it to be deployed at short notice should a compelling case for reconsidering liquidity support arise in the future. Any discussions with SCF in that regard would make it clear that they are without prejudice to the Crown's position and do not constitute any commitment by the Crown in relation to the current or any future requests for liquidity support. That work could include reviewing the relevant documentation and arrangements, being made aware of the identity of the proposed investor (and the source of funding) and developing the necessary form of nomination.
9. In the event that any further requests for liquidity support are received from SCF, no decision will be made without reference to your office, even if Treasury were satisfied that it would be an appropriate course of action for the Crown.

Recommended Action

We recommend that you:

- a **Note** the attached letter from South Canterbury Finance Limited seeking liquidity support.
- b **Agree** that the request for support be declined at this time.
Agree/disagree.
- c **Note** that Treasury undertake further work on the possible provision Crown guarantee backing of liquidity support for SCF by way of Deed of Nomination in order to retain it as an option, should a compelling case for reconsidering liquidity support arise in the future.
- d **Note** that officials will not agree to any future requests for liquidity support without reference to your office.



John Park
Manager, Guarantee Scheme
for Secretary to the Treasury



Hon Bill English
Minister of Finance

BELL GULLY

By email

Mr John Park
The Treasury
1 The Terrace
Wellington

FROM **Hugh Kettle**
DDI 64 4 915 6929
MOBILE 64 21 390 478
EMAIL hugh.kettle@bellgully.com
MATTER NO. 01-342-7952
DATE 30 July 2010

Dear John

South Canterbury Finance Limited - Retail Deposit Guarantee - application for Nominated Beneficiary

We act for South Canterbury Finance Limited (the **Company**), which has asked us to write to you on its behalf.

As you are aware the Company has been progressing discussions with a number of third party investors. A range of possible transactions have been and are being considered. Without repeating all the background, with which you are familiar, the Company is seeking to address two separate issues by way of these potential transactions:

- first, its long term capital structure, with a view to achieving long term stability with a balance sheet and asset mixture suitable that meets both its board's objectives and the prudential requirements for non-bank deposit takers; and
- secondly, shorter-term liquidity needs.

The Company has commenced discussions with a high net worth individual willing to assist with the second objective above by providing a liquidity buffer to the Company. This individual (the **Investor**) is a New Zealand citizen and resident. He is not an associated person of the Company or connected with the Company in any way. The Company will provide more details on the Investor once it has had the opportunity to discuss its proposal, set out below, with you.

The Proposal

The Investor has indicated that he has up to \$50,000,000 available to be invested in the Company, subject to due diligence and documentation. The Company has considered a number of structures and the proposal it would like you to consider is as follows:

1. The Investor deposits \$50,000,000 (or such other sum as is agreed) with the Company. An alternative is that some or all of the \$50,000,000 remain undrawn until needed.
2. The Investor will be issued debenture stock or a similar debt instrument evidencing his investment. He will be paid interest on the principal advanced or, if an undrawn structure is put in place, a line fee on the undrawn balance from time to time.
3. The \$50,000,000 (or so much as is drawn down) be held within a segregated trust account, which could either be set up by the Company or through a solicitors' trust account.

4. The balance of the trust account from time to time will only be available for the repayment of maturing debenture stock (or repayment of the Investor) and not for re-lending or the general operations of the Company.
5. At the time the deposit is made or the liquidity facility entered into, the Crown enters into a Nomination (as defined in both the revised and extended Crown Deeds of Guarantee) under which the Investor is a Nominated Beneficiary, under both those deeds of guarantee, for the full amount of his deposit or facility.
6. The deposit would be due to be repaid to the Investor over the six month period through to approximately 31 March 2011 (to be determined with and advised by the Investor).

The key aspect of this structure is that it would be designed so the Crown's exposure under the Deeds of Guarantee would not be increased. The 'new' \$50,000,000 could only be used for repayment of up to \$50,000,000 of existing debenture stock, in a scenario where payment could not otherwise be made from the Company's reserves. On this basis the structure would be financially neutral from the Crown's perspective.

In the Company's view this structure has benefits to both the Company and the Crown. It would obviously improve the Company's liquidity position and provide it with enhanced certainty.

From the Crown's perspective, the liquidity line would also provide certainty that a buffer exists, reducing the need for the Company to make funding requests directly to the Crown, or simply running out of cash, although it is recognised that this is still a potential risk even if this request is approved. As noted above this would be structured so it does not increase the Crown's exposure. In a worst case scenario, it means the Crown would be dealing with a payout to a single investor of \$50,000,000, rather than dealing with hundreds of investors, totalling \$50,000,000 in aggregate, who would have already been repaid from the liquidity line.

The Company would of course be happy to discuss the details of this with you further. It would expect the structure to be completely transparent from the Crown's perspective - including such controls as the Crown required relating to the use and structure of the trust account, and such reporting as the Crown required.

Could you please respond to us on this as soon as possible – the Company has undertaken to respond to the Investor as quickly as it can to let him know whether it will be able to transact as set out above.

Yours sincerely



Hugh Kettle
Partner