

## Treasury Report: South Canterbury Finance: Managed Receivership Strategy

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| <b>Date:</b> | 2 September 2010 | <b>Report No:</b> | T2010/1641 |
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### Action Sought

|   | Action Sought   | Deadline                             |
|---|---|--------------------------------------|
| Minister of Finance<br>(Hon Bill English) | <p><b>Note</b> the overall strategy for an SCF managed Receivership.</p> <p><b>Note</b> the Treasury will provide further advice on the structure for Crown engagement once the preferred approach is finalised.</p> <p><b>Note</b> the Treasury will provide further advice on a transparent process for managing and considering any offers from potential purchasers of all or part of SCF's assets once it has been agreed.</p> <p><b>Note</b> that communications on this issue are proposed to be at high level and involving less intensive Ministerial engagement.</p> <p><b>Indicate</b> whether there are any other issues raised by this report that you wish to cover.</p> <p><b>Refer</b> this report to the Prime Minister for his information.</p> | <b>9 am, Friday 3 September 2010</b> |

### Contact for Telephone Discussion (if required)

| Name          | Position                                    | Telephone | 1st Contact |
|---------------|---|-----------|-------------|
| John Park     | Manager, Guarantee Schemes                  |           | ✓           |
| Joanna Gordon | Manager, Financial Markets and Institutions |           |             |

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

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| Refer this report to the Prime Minister. |
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**Enclosure: No**

## **Treasury Report: South Canterbury Finance: Managed Receivership Strategy**

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### **Summary**

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#### **SCF - not a standard receivership**

The South Canterbury Finance (SCF) receivership is clearly not a standard receivership. Treasury has been considering the way in which this process would be managed. While there will be considerable detail to be worked through during this process, there are a number of issues that will be guiding our approach to the content of the receivership as well as how we manage the relationship between the Crown and the Receivers (Kerry Downey and William Black, McGrathNichol).

We will be meeting with the Receivers tomorrow morning to discuss the high level strategy outlined in this report in relation to the handling of the SCF receivership, items that we consider need more urgent attention (staff and systems) and communications around the approach and specific items (that is, messages to SCF staff who will be critical to keeping the business operating and clients who have obligations under loan and other contracts).

We consider that the Crowns' approach to strategic management of the receivership should not assume a resolution in the short term and that any actions must therefore be consistent with a receivership spanning up to 4 years.

#### **High Level Strategy**

Our approach to the high level strategy has been one that ensures that there is an orderly, well managed approach to this slightly unordinary receivership and that this process gives confidence that the Crown maximises value from this and can be confident in the way in which this value has been obtained.

#### ***Structure for Crown engagement***

The Receiver has been appointed by the Trustee (Trustees Executors) under the SCF Trust Deed. Formally, the Receiver answers to the Trustee, who answers to the Crown. It is preferable for the Crown (via the Treasury) to have the ability to formally engage with, and direct the Receiver if necessary. This will ensure the Receiver focuses on the return to the Crown, the Crowns' other priorities and operating in accordance with good practice in managing and disposing of these assets (e.g. making sure processes are transparent). We consider that this can be achieved through amending the SCF Trust Deed and will report further on this shortly.

In our report to you yesterday, we indicated that an Advisory Committee is being established (TR2010/1625 refers). This committee was being formally set up as part of the process to clear prior charges, but will take a lesser role if the Trust Deed is changed to enable the Crown to direct the Receiver.

## ***Components related to SCF operating in receivership***

The high level strategy comprises main “content” components. Communications is further component and is the means for information to be exchanged:

- Between the Crown and the Receivers;
- To directly affected parties (staff, clients, bidders); and
- Generally (around the high level approach to this receivership).

The key content components, which are interlinked, are described below.

### *“Business as usual”*

Business as usual includes:

- A commercial approach to maintaining value in the good parts of the SCF business. That is, the management of the well-performing loans and earnings from SCF’s investments; and
- New lending as loans mature/roll-over;
- Optimising value on the bad loans part of the business (which may involve enforcement and could result in receiverships).

SCF has already structured the business along these lines. We are, therefore, expecting that the business will be kept in the three parts it has already been divided into, with SCF staff and systems largely managing these parts of the business. Whether these three points are separated into three separate entities is the sort of issue that would need to be worked through with the Receiver.

We see the business structure being maintained, at least in the short term, as follows:

- Good loans where there is a good business here but SCF was not able to provide the capital to support it. We expect there will be new lending but whether this part of the business should, for example, be grown is an issue that will need to be worked through;
- Investments that are earning returns for SCF (i.e. Scales, Helicopters and Dairy Holdings);
- Impaired business *[Withheld under s.9(2)(b)(i) & s.9(2)(d)]*

Similar issues of detail will need to be worked through in relation to each of these parts. This structure would not preclude potential bids for all of SCF as a going concern nor does it hinder separation.

### *Maintaining SCF Staff and Systems*

Closely linked to the above, in order to maintain value in the business, we consider it is important that SCF staff be assured that they will be retained to run the business and utilizing SCF systems. The business itself is largely well operated and, on the basis of the advice we have on it, there is no reason not to allow staff and systems to continue with appropriate oversight.

This is an issue that will need to be discussed with the Receivers urgently. Any communications arising from this discussion would be expected to come from the Receivers as there is a good chance that key people may leave.

As we have been obtaining advice and have been monitoring SCF for some while, it is likely that we are in a good position relative to the receivers who would, in the first instance, need to adopt an approach whereby they need to undertake their own investigations to be satisfied on this and may also tend toward cutting back in these areas as a first step in a more standard approach.

### *SCF clients*

It is important that SCF clients are aware of a business as usual, commercial approach to these relationships would be maintained. Obligations to pay need to be met and it will be necessary to follow-upon non-payment.

As depositors have effectively been paid out, there will be less pressure on realizing assets but non-payment (or failure to meet contracted obligations) will still need to be handled in a commercial way.

### *Commercial approach to the receivership*

As above, our approach would involve SCF continuing to run as a business. This would continue to be the case unless there was a reason for it to change (e.g. sale of the business as a whole or in part).

### **Other issues**

The Crown received a formal offer to purchase the assets of SCF out of receivership on the basis of a going concern. The offer was formally addressed to the Receivers however it was recognised that Crown agreement (as the sole effective creditor) would be necessary if the bid were to proceed. Based on our assessment of this bid, as we advised you earlier today, is that Treasury would recommend that the Crown decline to accept the bid.

Other bids can be expected to come in on an ad hoc basis for all or part of the business (via the Receivers). We would want the process for managing and considering any offers to be transparent and to ensure the Crown retains all its options, especially in regard to when or if a decision was made.

At this point, the details of how bids and a bid process may be managed have not been concluded as there are still many details to be worked through. Treasury will update you the process once the detail is clear.

### **Risks**

We have identified some risks that need management now (in relation to maintaining SCF staff and systems) and those arising from bids. We can also anticipate that there may be issues that arise as the receivership runs through. For example, there is an outside risk that the Crown is required to provide funding to support the continuation of the good business. Any such support would need to be made on the basis of a business case presented.

### **Communications**

At this point, there are some important high level messages around the management of the receivership that will help to facilitate this process getting underway and to ensure a level of general confidence that the Crown's engagement with the SCF receivership. After this, most of the communications around the receivership would be handled as part of the receivership (with Crown input through the Advisory Committee).

We are talking with the Receiver in the next 48 hours about the strategy outlined in this report and about how we manage the relationship between the Crown and the receivers and communications going forward. We expect this to be at a high level in the first instance, with the detailed planning to happen as a rapid next step.

We think messages along the following lines would be helpful to be made early next week:

- While the Crown has a significant interest in the receivership of SCF, it is in receivership and as such, the Receivers are managing and running the process;
- The Crown has a significant interest in the conduct of the receivership. It recognises that there are good parts to the SCF business and it is important that the people and systems supporting these parts of the business continue to operate as they normally would where that is reasonable (discussions in relation to the “business as usual” approach will take place with the Receivers over coming days); and
- Anyone with a genuine interest in purchasing some or all of SCF’s assets should contact the Receivers.

## Recommended Action

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We recommend that you:

- a. note** that in order to manage the Crown’s interest in South Canterbury Finance’s receivership, the high level approach, which will need to be fleshed out in more detail, is as follows:
  - “business as usual”
  - maintaining SCF staff and systems unless or until there is a need for this to change
  - clients
  - a commercial approach;
- b. note** the Treasury will provide further advice on the structure for Crown engagement, including the ability to direct the receiver, once the preferred approach is finalised;
- c. note** a transparent process for managing and considering any offers from potential purchasers of all or part of SCF’s assets will be put in place and Treasury will provide further advice once that has been agreed;
- d. note** that there are some important high level messages that the Minister of Finance and Prime Minister can make to assist with this strategy and then allow the receivership to operate under the proposed high level strategy outlined;
- e. indicate** whether there are any other issues raised by this report that you wish to cover;

Discuss/no further issues at this stage.

f. **refer** this report to the Prime Minister for his information.

Yes/no.

John Park  
Manager, Guarantee Scheme  
**for Secretary to the Treasury**

Hon Bill English  
**Minister of Finance**