

Reference: 20200398

3 February 2021

s9(2)(a)

Dear s9(2)(a)

Thank you for your Official Information Act request, received on 23 November 2020.
You requested:

This is a request under the Official Information Act for the following documents:

- 1 July Joint report by Inland Revenue and the Treasury BN 2020/340
T2020/2198: Aide Memoire: Update on the use of tax relief schemes;
- 2 July Aide Memoire T2020/2206 Bank of Canada comments on negative interest rates;
- 7 July Treasury Report T2020/1832: Business support – stocktake and next steps;
- 9 July Aide Memoire T2020/2354: Update on Transmission Gully PPP negotiations;
- 16 July Treasury report T2020/1699: Revised indemnity request for Provincial Growth Fund Ltd;
- 16 July Aide Memoire T2020/2430: Update on non-deposit taking lenders;
- 27 July Joint report by the Treasury and Ministry of Transport T2020/2544: Auckland light rail – next steps.

I note that on 11 December 2020 the Treasury advised you via email of the need to extend the time for deciding on your request by 20 working days.

Information being released

Please find enclosed the following documents:

Item	Date	Document Description	Decision
1.	1 July 2020	Aide Memoire T2020/2198: Update on the use of tax relief schemes	Release in part
2.	2 July 2020	Aide Memoire T2020/2206: Bank of Canada comments on negative rates	Release in part

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PO Box 3724
Wellington 6140
New Zealand
tel. +64-4-472-2733

<https://treasury.govt.nz>

3.	6 July 2020	Treasury Report T2020/1832: Business Support – Stocktake and Next Steps	Release in part
4.	16 July 2020	Treasury Report T2020/1699: Indemnity Request for Provincial Growth Fund Limited	Release in part
5.	16 July 2020	Aide Memoire: Update on non-deposit taking lenders (NDTLs)	Release in part
6.	27 July 2020	Joint report by the Treasury and Ministry of Transport T2020/2544: Auckland Light Rail - next steps	Release in part

I have decided to release the documents listed above, subject to information being withheld under one or more of the following sections of the Official Information Act, as applicable:

- names and contact details of officials, under section 9(2)(g)(ii) – to maintain the effective conduct of public affairs through protecting ministers, members of government organisations, officers and employees from improper pressure or harassment,
- advice still under consideration, section 9(2)(f)(iv) – to maintain the current constitutional conventions protecting the confidentiality of advice tendered by Ministers and officials,
- certain sensitive advice, under section 9(2)(g)(i) – to maintain the effective conduct of public affairs through the free and frank expression of opinions,
- commercially sensitive information, under section 9(2)(b)(ii) – to protect the commercial position of the person who supplied the information, or who is the subject of the information,
- legal advice, under section 9(2)(h) – to maintain legal professional privilege, and
- direct dial phone numbers of officials under section 9(2)(k) – to prevent the discloser if official information for improper gain or advantage.

Direct dial phone numbers of officials have been redacted under section 9(2)(k) in order to reduce the possibility of staff being exposed to phishing and other scams. This is because information released under the OIA may end up in the public domain, for example, on websites including Treasury's website.

Information publicly available

The following information is also covered by your request and is publicly available on the Treasury website:

Item	Date	Document Description	Website Address
7.	9 July 2020	Aide Memoire T2020/2354: Update on Transmission Gully PPP negotiations	https://www.treasury.govt.nz/ publications

Accordingly, I have refused your request for the documents listed in the above table under section 18(d) of the Official Information Act:

- the information requested is or will soon be publicly available.

Some relevant information has been removed from documents listed in the above table and should continue to be withheld under the Official Information Act, on the grounds described in the documents.

Please note that this letter (with your personal details removed) and enclosed documents may be published on the Treasury website.

This reply addresses the information you requested. You have the right to ask the Ombudsman to investigate and review my decision.

Yours sincerely

Jean McDowall
Acting Team Leader Ministerial Advisory

OIA 20200398

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Briefing note

Reference: BN2020/340, T2020/2198

Date: 1 July 2020

To: Tax Advisor, Minister of Finance – Paul Young
Revenue Advisor, Minister of Revenue – Thomas Allen
Private Secretary, Minister of Revenue – Alice Yan

cc: Naomi Ferguson, Commissioner
David Carrigan, Deputy Commissioner
Emma Grigg, Policy Director
Kerryn McIntosh-Watt, Policy Director (Acting)
Phil Whittington, Chief Economist
Joanne Petrie, Executive Support Advisor to the Commissioner
Jill Compton, PA to Deputy Commissioner
Government & Executive Services (Ministerial Services)

From: Michael Sherwood, Jessica Rowe, Stewart Donaldson

Subject: **Aide Memoire: Update on the use of tax relief schemes**

Purpose

This note provides an update on the use of various tax relief schemes available to taxpayers during the current COVID-19 situation. Taxpayers have been utilising a mix of existing mechanisms (including entering into instalment arrangements and not paying their tax debt) and new schemes (including the small business cash flow scheme, loss carry back scheme and use of money interest remission) to help manage financial difficulties arising due to COVID-19. The take-up of these various measures has been mixed.

Small Business Cash Flow (Loan) Scheme (SBCS)

The SBCS has provided significant lending to businesses that needed it ...

The SBCS was launched on 12 May and the application period ends on 24 July. On 1 July DEV will consider the recommendation to extend the scheme to 31 December 2020.

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The objective of the SBCS is to provide immediate liquidity support to small and medium businesses impacted by COVID-19 to help them pay for non-wage costs.

Feedback on the scheme indicates that the loan provides a source of immediate support for businesses and is helpful for managing cashflow issues. The absence of personal guarantees also makes the scheme a comparatively attractive source of funding.

As at 30 June 2020, 89,479 applications have been received, 85,007 have been approved and \$1.423 billion has been disbursed. Small businesses with five or fewer employees account for 80% of applications and 63% of the value of loans issued. Industries which have benefited the most, each accounting for over 10% of the volume of applications, are construction, accommodation and food services, and professional, scientific and technical services.

... but it is unclear how much will be repaid.

The appropriated capital available for lending for the Scheme is \$5.2 billion with an initial fair-value write-down of \$3.4 billion, which equates to a write-down of approximately 66%.

Uptake of the loan has been lower than the original appropriation. This is likely to reflect the inherent uncertainty of the original appropriation, and an environment where businesses are still deciding whether to take on further debt given the economic uncertainty.

Based on the \$1.423 billion lending to date, the fair-value write-down is \$0.939 billion. Inland Revenue will undertake a full valuation of the lending as at 30 June, which will replace the 66% with an updated fair value write-down.

The fair value write-down reflects a best estimate of:

- expected credit losses (i.e. how many borrowers will default, and how much is the Crown likely to recover in the event of defaults); and
- the concessionary interest rate and terms of the loan (i.e. by deploying the capital at below-market-rates, the Crown incurs an economic cost due to the time value of money).

The initial write down in the appropriation amounts reflects a total default rate assumption of roughly 56%. We think this is conservatively high, but defensible. In the Stats NZ Business Demography Statistics the average firm five year survival rate for businesses with less than 50 employees is around 60%. This means our baseline expectation is that even in comparatively in good economic conditions, around 40% of SMEs alive today would not survive to pay out the full five year term.¹

¹ The Business Demography data comes from the 2009 – 2017 period, so it probably overestimates firm survival compared to the current economic environment.

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Estimating the fair value write-down to account for these factors is challenging because it requires projecting the estimated repayments when the loan is first advanced. As borrowers do not have to start repayments until month 25 (although some borrowers will repay earlier than that) repayment profiles will need to be assumed. This differs from bank loans where monthly repayment amounts generally are set in contract and commence immediately.

More information on the fair value will be made publicly available over time

The fair value write-down of loans at 30 June 2020 will be formally valued by expert valuers in late July/early August in preparation for inclusion in the Financial Statements of the Government (FSG), which are published in the first two weeks of October. This valuation will also be audited.

The value of loans will be continually re-measured through the life of the scheme (at least annually) and the portfolio value will change as more information about borrower repayments emerges.

Instalment arrangements and tax debt***The number of taxpayers entering into instalment arrangements has increased ...***

Taxpayers that are unable to pay their taxes on time are able to talk to IR and request an instalment arrangement. Taxpayers are now able to set up instalment arrangements for some tax types entirely online, including setting up direct debit payments. If certain criteria are met, an instalment arrangement proposed by a taxpayer can be automatically approved.

Between February and May 2020, nearly 73,000 instalment arrangements have been set up for taxpayers that needed them. This is an increase in instalment arrangements of around 25,000 relative to the same period in 2019.

In addition, the amount of tax subject to new instalment arrangements during this period has more than doubled since 2019 (from just under \$500 million between February and May 2019, to over \$1 billion between February and May 2020).

Where use of money interest is being waived for these taxpayers, these tax instalment arrangements behave like an interest free loan to businesses.

... but the number of taxpayers who are not paying their taxes at all has also increased.

While taxpayers have the option to enter into instalment arrangements with Inland Revenue to pay their taxes, some choose instead to not pay their taxes at all. This becomes tax debt that IR needs to recover. Total overdue tax debt as at May 2020

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(excluding child support) is around \$6.1 billion. This is around \$1 billion higher as compared to May 2019. This increase is spread among multiple tax types, including GST, PAYE, income tax and working for families.

It is important to note that this increase in debt will not be entirely due to COVID-19. There is a natural increase in overdue tax debt over time, as well as monthly fluctuations due to a variety of factors, including when tax falls due. The increase in debt may also reflect redeployment of staff from debt collection to other functions. By comparison, total overdue tax debt in February 2020 was about \$500 million higher than it was in February 2019. This increase in debt is unlikely to be attributable to COVID-19.

It is the additional increase in relative debt in May 2020 that may provide some insight into how COVID-19 has affected the amount of tax debt. The fact that tax debt is \$1 billion higher in May 2020 when compared to 2019, but only \$500 million higher in February 2020 when compared to 2019, suggests that the increase in tax debt due to COVID-19 is potentially around \$500 million², although this estimate is also subject to some uncertainty.

Use of money interest remission***UOMI is being remitted for some taxpayers affected by COVID-19 ...***

UOMI is the interest charged on overdue tax owed to Inland Revenue. The current interest rate on overdue tax is 7%. UOMI is intended to compensate the Government for the lost time value of money from taxpayers underpaying their tax, and to provide (along with penalties) an incentive for taxpayers to not underpay their tax.

Inland Revenue has been given a temporary power to remit UOMI for tax due between February 2020 and March 2022 for taxpayer's who have had their ability to pay tax on time significantly affected by the COVID-19 outbreak.

As at 30 June 2020, a total of 33,154 customers have had remission granted, to a total value of \$2.190m. This remission is applied to customers who have been identified as impacted by COVID-19.

... with more expected to benefit when they repay their debt.

While UOMI is only being remitted for taxpayers who have repaid their core tax debt, allowances have been made for taxpayers who have had to enter into instalment arrangements to repay their tax debt over time. UOMI is currently being charged at 0% for these taxpayers provided they meet the criteria for UOMI remission, adhere to the conditions of the instalment arrangement and repay the core debt.

² \$1 billion less \$0.5 billion

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As at 27 June 2020, a total of 16,551 customers identified as impacted by COVID-19 have entered into an instalment arrangement. The total estimated value of interest suppressed (i.e. currently charged at 0% rather than 7%) is \$2.709m. This is in addition to the \$2.190m of UOMI already remitted. This amount is only indicative, as the actual amount of interest remitted will depend on the action of taxpayers.

Loss carry back scheme***Uptake of the loss carry back scheme has been limited to date ...***

You have recently been provided an update on the loss carry back scheme, including reasons given through private sector consultation for the low uptake of the scheme (BN2020/331 refers). As at 29 June, 2,031 taxpayers have taken up the loss carry back scheme receiving \$87.1 million in refunds.

We have approached a number of external stakeholders including accounting firms and the tax pooling intermediaries to canvass their views why the uptake from the scheme might be lower than initially expected. They have been unanimous in their feedback describing the scheme as a "slow burner" in that it might be slow to develop but it would develop over time. The reasons they gave for this included:

1. at present taxpayers are focused on one thing, survival, and anything to do with tax is being put on the backburner. They will eventually turn their mind to the future and what their loss position might look like once they have sorted out a plan for today;
2. because of the fluid situation under COVID-19 and not knowing ultimately how it will affect their businesses are taking a very cautious approach and until they are sure of the extent of any losses they are unlikely to gamble in case there is a sudden change in the environment; and
3. a number of taxpayers still have not completed their 2019/20 income year because of late balance dates. Those with late balance dates are the ones most likely to suffer losses in that year as they have had the most exposure to the COVID-19 lockdown and until they finalise that year they won't know the extent of losses. These should become clearer between June and September when those late balance date companies finalise their 2019/20 results and we get an indication from other taxpayers as to the effect of COVID-19 on them through the first instalment of provisional tax due on 28 August.

It is important to note that the cost of the loss carry back scheme was forecast before the SBCS was implemented. This introduction of the SBCS has likely reduced the uptake of the loss carry back scheme. The SBCS is simpler and carries less risk for businesses, as there is no requirement on businesses to estimate their earnings for future years in an uncertain economic environment. A business that overestimates their losses in the current year could end up facing a UOMI charge.

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... and the cost of the policy is expected to be lower than previously thought

We expect that the loss carry back scheme will be used more as time progresses, but only once taxpayers are certain of the amount of loss that will be incurred for their applicable income year. In addition, once the regime is more widely known and understood, taxpayers will also plan for the availability of the loss carry back in the 2020-21 income year.

IR and Treasury will work to revise the forecasts for the loss carry-back measure over the next few weeks. The revised figures are likely to assume lower take-up for the 2019-20 income year, but ensure there is enough appropriated to cover those impacted by COVID-19 who intend to claim when they file their 2019-20 returns in the next 12 months. It is likely too soon to make any assessment about the uptake (and the accuracy of the forecast) for the 2020-21 year.

Michael Sherwood, Analyst, Tax Strategy, s9(2)(k)

Jessica Rowe, Manager (Acting), Tax Strategy, s9(2)(k)

Stewart Donaldson, Principal Policy Advisor, Policy and Strategy, Inland Revenue, s9(2)(k)

s9(2)(k)

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Reference: T2020/2206 MC-1-1-1-2 (RBNZ Institutional Frameworks)

Date: 2 July 2020

To: Minister of Finance (Hon Grant Robertson)

Deadline: None
(if any)

Aide Memoire: Bank of Canada comments on negative rates

Purpose

This Aide Memoire responds to your request for further details on comments made by the Governor of the Bank of Canada on negative rates. These comments were provided to you at a high level in the Weekly Fiscal Update provided on 26 June. As well as further details on the comments made by the Governor of the Bank of Canada, we have also provided some comments on negative rates in a New Zealand context and an update on the next steps for alternative monetary policy (AMP).

Comments made by the Governor of Bank of Canada

On 22 June, in his first speech as the Governor of the Bank of Canada, Tiff Macklem explained how the Bank of Canada's commitment to low, stable and predictable inflation has guided their actions during COVID-19, in an address to Canadian Clubs.

The Governor's speech outlined the impact of COVID-19 on the Canadian economy, highlighted the Bank's main objective of delivering low, stable and predictable inflation, and explained some of the monetary policy tools available or in use by the Bank at this time. The policy interest rate was not a significant topic in his speech.

On the policy interest rate specifically, the entirety of the comments made by the Governor were:

"Back in March, the Bank rapidly lowered our policy interest rate to 0.25 percent. This action was not really expected to boost spending in the early days of the pandemic. Its immediate purpose was to help support confidence and provide some interest rate relief. But as more retail businesses reopen, low interest rates will help support spending."

The policy rate is now at its effective lower bound. Some central banks have taken their policy rates below zero. We feel that bringing that rate into negative territory could lead to distortions in the behaviour of financial institutions. However, the Bank has a number of other tools we can use to help stimulate demand."

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The speech relayed the Bank's view that other policy tools, namely quantitative easing, are working effectively to deliver stimulus. The Governor's scepticism of negative policy rates is not out-of-line with previous statements from the Bank of Canada. The Reserve Bank of Australia (RBA) has also expressed scepticism over negative rates.

A lower or negative OCR in the NZ context

The Reserve Bank of New Zealand's Monetary Policy Committee (MPC) has stated that the Official Cash Rate (OCR) in New Zealand will be held at +0.25% until at least March 2021. However, they have signalled that further reducing the OCR could be a viable option in New Zealand in due course.

Based on analysis to date, the Treasury's view on further reducing the OCR is that it is likely to be an effective tool in due course (including to negative levels). There are currently temporary constraints to further reductions of the OCR in New Zealand, including the Reserve Bank's forward guidance, IT systems, and some loan and derivative contracts. However, once these are addressed, further reductions in the OCR could usefully contribute to the achievement of the Reserve Bank's economic objectives and the economic recovery. Negative interest rates would likely only apply in wholesale markets, and are unlikely to apply to retail customers for the foreseeable future.

We continue to monitor the views of other central banks. However, we are unable to fully understand the Bank of Canada's current aversion to negative rates, as they have not released their underlying analysis or research to justify the Governor's comments.

Next steps on Alternative Monetary Policy

As well as looking at the possibility of further reductions in the OCR in the New Zealand context, the Treasury and the Reserve Bank are currently analysing further AMP tools, including term lending, foreign exchange intervention, and changes to the current Large Scale Asset Purchases (LSAP) programme.

We are currently anticipating that the Reserve Bank will request an expansion to the current Large Scale Asset Purchase (LSAP) indemnity ahead of the 12 August Monetary Policy Statement to cover further LSAPs, term lending, and foreign exchange intervention. This would allow the MPC to decide whether to use any of these tools in the August, September or subsequent decisions. This follows public statements by the MPC at the last monetary policy decision that the Bank may use these tools in the coming months. If the Reserve Bank requests an expanded indemnity as signalled, we intend to provide you with advice on this in late July.

We are happy to provide further information on AMP separately to advising on the indemnity request if you wish.

Hannah Waine, Graduate Analyst, Macroeconomic and Fiscal Policy, s9(2)(k)
Renee Philip, Manager, Macroeconomic and Fiscal Policy, s9(2)(k)

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TE TAI ŌHANGA
THE TREASURY**Treasury Report: Business Support – Stocktake and Next Steps**

Date:	6 July 2020	Report No:	T2020/1832
		File Number:	SH-1-6-1-3-5-2-1-2

Action sought

	Action sought	Deadline
Hon Grant Robertson Minister of Finance	Indicate if you wish to discuss the contents of this report.	14 July 2020

Contact for telephone discussion (if required)

Name	Position	Telephone		1st Contact
Alistair Birchall	Acting Manager, Firm Support	s9(2)(k)	s9(2)(g)(ii)	
Chrisana Archer	Senior Analyst, Firm Support			✓
Alastair Cameron	Manager, COVID Policy			

Minister's Office actions (if required)

Return the signed report to Treasury.

Note any
feedback on
the quality of
the report

Enclosure: NO

IN-CONFIDENCE**Treasury Report: Business Support – Stocktake and Next Steps**

Executive Summary

This report responds to your questions regarding the alignment of schemes developed to support businesses: the “business support landscape”. The report outlines the way businesses have responded to COVID-19, the ongoing challenges we see businesses facing, and the work we are doing on possible policy responses if the economic and/or public health situation deteriorates.

Of immediate relevance, we are aligning our work on broad firm support policies with advice on wage subsidy options under different scenarios. We have also provided you with a separate report on this topic today [TR2020/2094 refers]. You have an opportunity to consider the objectives, settings and triggers for policy responses in a resurgence of the virus to ensure responses are aligned with the Government’s objectives, public health scenarios and the changed economic and fiscal environment.

In the early stages of the crisis we took a “no regrets” approach to business support

A number of schemes were developed quickly. Alignment has been sought where possible, but a greater emphasis has been placed on ensuring broad coverage.

The business support landscape includes the Wage Subsidy Scheme (WSS), Small Business Cashflow Scheme (SBCS), the Business Finance Guarantee Scheme (BFG), a number of tax measures, and various commercial and property law changes. Monetary policy has reduced interest rates to help support lower borrowing costs for businesses.

The primary policy objective for this work has been to “cushion the blow” and avoid the potential for a disorderly wave of business failures.

The primary challenge faced by business has been dealing with uncertainty regarding demand for their goods and services

In their initial response to COVID-19, businesses went “off-risk”: this means that they have limited or deferred spending and reduced their level of activity.

Businesses have predominantly relied on schemes that have provided them with cashflow or allowed them to preserve their existing cash balances. The WSS has been by far the dominant form of support, and market engagement suggests the scheme has provided an essential cushion to business.

By contrast, the “credit channels” (i.e. the provision of debt to businesses) have played a less significant role during the COVID-19 response than we might have expected. Given limited certainty around demand many businesses have not felt confident they can repay additional debt. Many businesses also entered COVID-19 with a relatively high degree of existing debt.

Current support measures are fit for purpose, but now is a good time to take stock

The management of COVID-19 domestically and the shift to lower Alert Levels has meant the economy is in stronger shape than many business anticipated in March / April. Early data shows a rebound in activity. This can be seen in the “high-frequency” indicators we are monitoring, such as traffic and freight movements and retail spending.

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This rebound remains extremely fragile. In our view, it most likely reflects pent-up spending delayed under lockdown. Even under positive health scenarios a plausible consequence is that businesses will face their most significant financial pressures and make their key decisions in the third and fourth quarters of 2020, reflecting the end of the WSS, weakened balance sheets, and low consumer demand. There are potential health and economic scenarios where these outcomes will be far worse: in particular, a second wave of transmission is likely to have an outsized impact on confidence.

As the economy opens up, some businesses may have greater demand for financing tools like the existing SBCS and BFG. These measures, which supply credit to viable firms, rather than broad-based measures like the wage-subsidy, are also consistent with our previous advice to move to a more “market-led” rebuild. Accordingly we consider these measures remain a useful and important part of the business support landscape.

We see a case for additional measures to support business confidence...

In light of the business environment, we consider it is helpful to take stock and consider what is needed for the future. Changes may be required as we move further into the “recovery” phase and potentially in to “rebuild”. We have been working with other agencies to develop our thinking.

We continue to advise you in favour of fiscal stimulus measures to improve aggregate demand to support business certainty and confidence, and will be in a position to advise you further on options to achieve this at the appropriate time.

In addition to a stimulus, we recommend:

- s9(2)(f)(iv)
-

... and will keep a watching brief on access to finance

Business balance sheets are likely to be stretched, and more debt will not be the answer. A recent “market sounding exercise”, and engagement with other agencies, highlighted a challenge for small and mid-sized business to access equity funding as they seek to rebuild and grow. This financing challenge pre-dates COVID-19.

We will continue to monitor the operation and effectiveness of existing business support measures in light of changes economic circumstances. In order to maintain a holistic, aligned view of the landscape, we are working with other agencies (in particular MBIE, RBNZ, and IR) on the question of access to finance.

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Recommended Action

We recommend that you:

- a **note** the existing landscape of business support measures are fit for purpose in the current economic environment.
- b s9(2)(f)(iv)
- c **note** that we are continuing to monitor the implementation and effectiveness of the SBCS and the BFG, and considering how that can contribute to the cross-government work programme to investigate and address gaps in capital markets.
- d **note** we are working with other agencies to develop a holistic, aligned view of the business support landscape.
- e **indicate** if you would like a discussion with officials about the business support landscape.

Yes/No.

Alastair Cameron
Manager, COVID Policy

Hon Grant Robertson
Minister of Finance

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Treasury Report: Business Support – Stocktake and Next Steps

Purpose of Report

1. This report responds to your questions regarding the alignment of schemes developed to support businesses: the “business support landscape”.
2. The report outlines the way businesses have responded to COVID-19. Given the changing economic and health environment, the report considers potential next steps.

How Have Businesses Experienced COVID-19 to Date?

Many businesses suffered operating losses during the lockdown period

3. During the lockdown, many businesses saw a severe reduction in revenue. Xero’s data indicates SME revenue was 34% lower in April 2020 than it was in April 2019.
4. When faced with these revenue reductions, and with significant uncertainty about both future demand and their ability to operate at full capacity, businesses sought to preserve cash and limit their level of risk.
5. Businesses nonetheless retain many fixed costs that do not vary with their level of activity. Most business will have experienced operating losses that they will not expect to immediately recover.

The primary objective for the Government response has been to “cushion the blow”

6. The primary policy objective for businesses has been to “cushion the blow”, and avoid a disorderly wave of business failures. There would be long-lasting impacts from a simultaneous wave of failures, resulting in a significant loss of business value and jobs [TR2020/1564 refers].
7. To support this objective a number of schemes have been developed quickly, taking a “no regrets” approach. Alignment has been sought where possible, but a greater emphasis has been placed on ensuring broad coverage.
8. Five types of schemes have been introduced:
 - **Grants.** These measures provide cash to businesses, without a need for repayment. The key grant in place has been the wage subsidy scheme (WSS) and the wage subsidy extension (WSX). Both have been open to businesses that have seen a substantial decline in revenue (30% for the WSS, and 40% for the WSX) as a result of COVID-19.
 - **Cashflow Measures.** These measures provide businesses with a “timing benefit”: they receive cash more quickly or have access to their cash for longer.
 - The tax loss carry-back scheme, allowing businesses to carry back losses in their 2020 (or 2021) income year and receive a refund of previously paid tax. This measure has a loan like quality, as firms who opt into this scheme will have increased tax payments in the future once they get back into profit.

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- Greater flexibility around tax payment and filing times, including waiving interest for late payments (known as use of money interest, or “UOMI”).
 - Excluding more taxpayers from the provisional tax system, so they don’t have to pay tax in instalments over the year, but instead pay tax in a lump sum after the income year finishes. This lets them hold onto their cash for longer.
 - **Investment Incentives.** These measures provide additional cash or a timing benefit to businesses, but also require the investment of new money, in order to stimulate activity. This includes:
 - The low value asset write-off. This allows a deduction of the full cost of assets with a value of less than \$5,000 in the year of purchase (dropping to \$1,000 next year).
 - The re-introduction of depreciation on commercial and industrial buildings. Businesses can claim depreciation deductions to reduce their tax bill.
 - Loosening the rules around carrying tax losses forward. The new rules allow businesses to retain more of their tax losses after bringing in new shareholders. This will typically support a higher price for shares, assisting the recapitalisation of some businesses.
 - **Concessional Financing.** The Small Business Cashflow Scheme (SBCS) allows businesses that meet the WSS criteria to take a 5-year, low interest loan from the IRD, with the maximum amount of the loan set by reference to the number of FTEs.
 - **Commercial Financing Schemes,** being Business Finance Guarantee Scheme (BFG). The BFG provides an 80% Crown guarantee over term loans or revolving credit facilities up to \$500,000. Lending decisions are made by banks. In addition, the Crown has agreed a \$900 million loan facility for Air New Zealand, using the principles from the economically significant business (ESB) framework. While currently undrawn, this facility has been an important backstop for the business during a period when there have been ongoing discussions regarding its strategy and capital structure.
9. In addition to those schemes:
- The private sector has provided for deferral or reductions of some costs.
 - The Government has introduced a variety of commercial and property law changes, such as the creation of a “business debt hibernation” scheme allowing businesses affected by COVID-19 disruptions to place their existing debts on hold for a period.
 - Monetary policy is also playing a role, bringing down interest rates to support low borrowing costs for business and encourage investment.

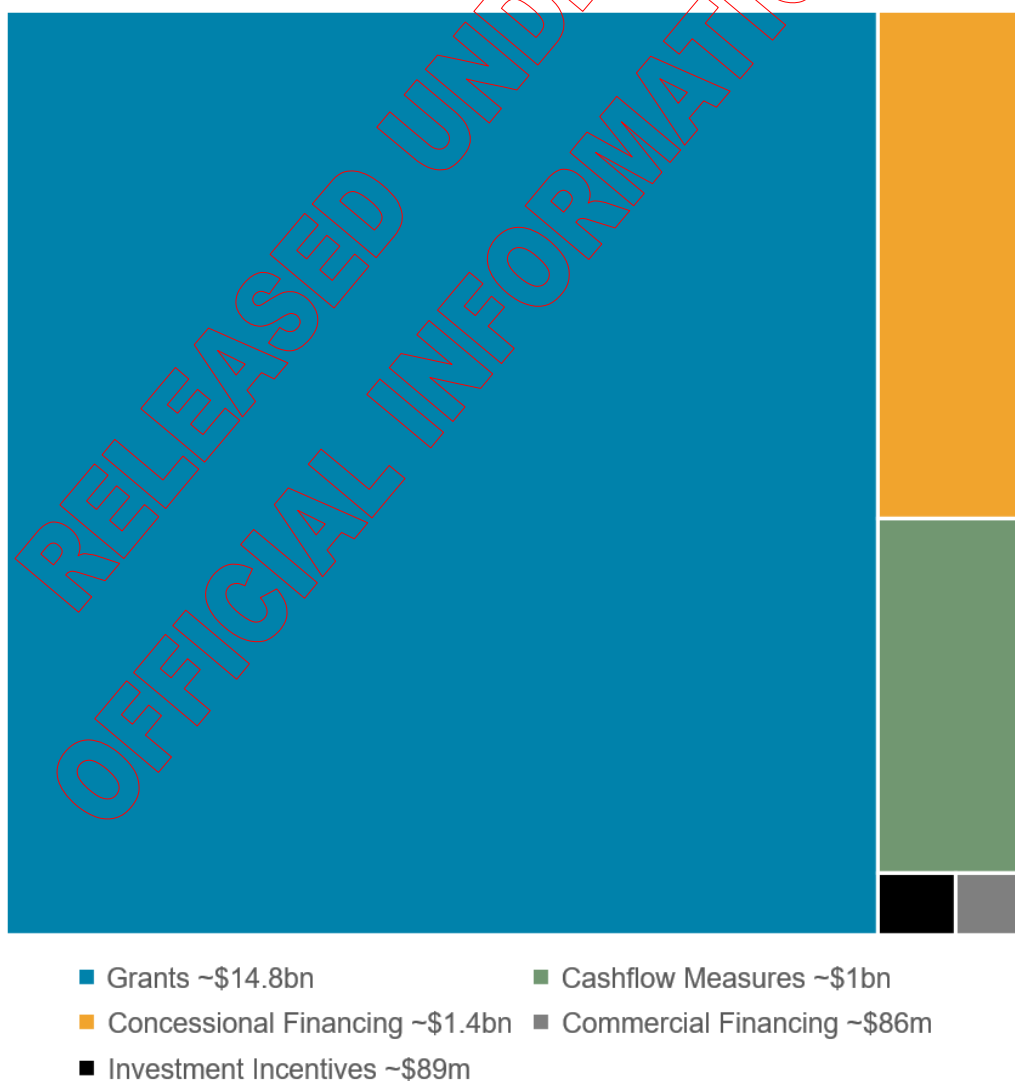
Uptake has been most substantial for support measures that provide businesses with cashflow or preserve their existing cash balances

10. In an environment of significant uncertainty, businesses have relied primarily on “grants” and “cashflow measures”.

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11. The wage subsidy has provided the dominant form of support. The WSS paid out \$10.9 billion in subsidies covering around 1.7 million jobs, and the WSX is paying out around \$3.9 billion. Market engagement suggests the scheme has provided an essential cushion to business: an MSD's survey of WSS recipients found 78% of businesses believed it had a positive impact on staff retention. The WSS has been particularly valuable to businesses in sectors where labour costs per worker are relatively low, such as hospitality.
12. The WSS and WSX have helped businesses meet some of their labour costs. The use of a "high-trust" approach and an upfront payment structure have also supported liquidity, as businesses were able to receive the cash very quickly. The MSD Survey found 63% of businesses reported a strong positive impact on cashflow, and 31% a small positive impact.
13. The chart below shows the distribution of support. The chart provides a relatively imprecise estimate for some of the smaller schemes, but overall it highlights that support from grants (i.e. WSS and WSX) has significantly exceeded all other schemes.

Chart 1: Estimated Cash Inflows from Q2/Q3 2020 Business Support Initiatives



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14. Businesses have also pulled the other levers they have available to preserve both their cashflow and existing cash balances. These levers include:
- *Significant deferral or renegotiation of expenses:* Banks and non-bank lenders have provided loan repayment deferrals (or similar options such as shifting to interest only). To date \$13.5bn (10 percent) of business lending has had some or all loan payments deferred.¹ Many businesses have been able to arrange for rent deferrals or temporary rent reductions. In some cases businesses have unilaterally chosen not to pay certain expenses, and payment times have increased.
 - *Reducing costs:* many businesses have negotiated lower staff costs (for example moving to 80%). Businesses are also deferring discretionary expenditure and investment.
 - *Utilising tax measures as a substitute for finance:* we estimate that tax debt may have increased by approximately \$1.0 billion since COVID-19. This is a mixture of approximately \$500 million in instalment arrangements (with UOMI remitted), and \$500 million that has not been negotiated with the IRD.
15. We think that most of this money has already been received and possibly also spent by businesses. Deferral arrangements and cashflow measures are temporary and will typically result in businesses facing increased costs on their expiry (for example higher debt servicing costs or tax bills in the future). To the extent there is a “fiscal cliff” with current support, we are close to or already past it.

The “credit channels” have been less important

16. An initial focus of the COVID-19 response was on finding ways to support the “credit channels”: the provision of debt to businesses.
17. The credit channels have played a less significant role during the COVID-19 response than we might have expected. Given the high level of uncertainty about both the health situation and the economic environment, many businesses appear uncomfortable taking on more debt, or were already fully leveraged prior to the crisis. This has been the case even with the SBCS, which is concessional, and does not involve credit assessment. We have not seen an observable increase in new lending activity, and market intelligence suggests this primarily reflects low demand.
18. The shift to a “risk off” approach is reflected in emerging data. Net debt balances have reduced in many sectors and businesses have not rushed to draw down on existing debt facilities.

The impact of COVID was not evenly distributed

19. The impact of COVID-19 has not been felt evenly across different business sectors. The level of impact has been and will be dependent on the:
- *Extent of the COVID-19 impact:* COVID-19 has had a heightened impact on businesses that directly or indirectly rely on international customers, cross-border-supply chains, or that cannot operate near full capacity under social distancing restrictions. This includes tourism, international education, hospitality, and arts and entertainment. In contrast, businesses such as supermarkets and telecommunications companies may have seen an increase in revenue.

¹ For SMEs, reduced or deferred mortgage payments may also have an impact on their ability to fund their business. As at early June around ~\$40bn of consumer lending has been reduced or deferred by banks.

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- *Structural challenges / disruption:* COVID-19 has accelerated the structural shifts being experienced in sectors such as media, and retail. Sectors with highly leveraged balance sheets or high fixed costs prior to COVID-19 also have limited resilience to a reduction in revenue.
- *Engagement with the capital markets:* businesses that are engaged with the capital markets (for example businesses listed on the NZX) have been able to access capital to address potential operating losses from COVID-19 and to help manage the risks they face due to uncertainty. \$2.75bn in new equity capital has been raised on the NZX to date. New equity also unlocks additional debt; many equity raises have also seen business extending or increasing their access to debt facilities.

What Might the Future Hold?***The full impact of COVID-19 will take time to fully play out...***

20. Under Alert Level 1, the economy is now operating at around 90-95% of capacity [TR 2020/973 refers]. Early data shows a sizable rebound in activity. This can be seen in the “high-frequency” indicators we are monitoring, such as traffic and freight movements and retail spending.
21. There is a risk that any rebound in demand is temporary, and simply reflects pent-up spending delayed under lockdown. A plausible consequence is that many businesses are responding by deferring decisions, and business activity will reduce later in 2020:
 - The end of the WSS and the WSX reduces the support available to most businesses [TR2020/2094 refers]. The end of these schemes will start to reveal the degree to which job losses have been delayed but not avoided. Businesses will also progressively lose the cashflow benefits
 - Businesses will be focusing on “right-sizing” their operations. These decisions will be informed by their experience of operating at Alert Level 1: July and August will be particularly influential. It is likely we will see an increase in unemployment, and consumers becoming more cautious about their spending.
 - The immediate impact of COVID-19 (and in some cases the continuing impact) means that for many businesses, balance sheets will have been weakened and there is likely to be less inclination to invest and take risk [T2020/1908 refers]. This will have occurred both through operating losses, as well as falling asset values (in particular intangibles, goodwill, and the ability to collect receipts from customers). A key challenge we anticipate will be the ability of small and mid-sized business to access the funding they need to rebuild and grow. More debt will not provide the answer. This challenge predates COVID-19: New Zealand’s capital markets are relatively thin, with a narrow range of funding options.

...and will be heavily shaped by the health and global outlook

22. There are potential health and economic scenarios where these outcomes will be far worse: in particular, a second wave of transmission is likely to have an outsized impact on confidence.
23. While the domestic environment is more positive than it was several months ago, the external outlook also appears more challenging. Based on a recent OECD forecast New Zealand’s trading partners will see a 4.5% contraction in 2020. Anecdotal feedback suggests that businesses are continuing to see challenges in managing their global supply chains.

IN-CONFIDENCE**Taking Stock**

Now is a good time to take stock of the situation

24. Changes to the BFG and SBCS are now in train. We understand that when considering these changes you asked about the landscape of business support.
25. As previously indicated, the focus of support should shift from preserving existing businesses and jobs to an approach that allows for more of a “market-led” recovery, particularly now that restrictions on businesses have been removed.
26. Achieving this outcomes face operational challenges that need to be considered. Attempts to “target” support to viable businesses will often run into one of two issues:
 - The process of “targeting” is complex and takes time. Support may end up being poorly directed or arrive too late.
 - Targeting will typically require working with delivery agents, for example either inside (e.g. IRD) or outside the Crown (e.g. banks). These agents will face incentives and potential capacity constraints that may not support good outcomes. For example, distributing support through bank channels will often see the application of commercial lending standards that do not align with the Crown’s policy objectives.

Broader economic initiatives remain an important component of supporting firms

27. We continue to advise in favour of fiscal stimulus measures to improve aggregate demand would support business certainty and confidence, and will be in a position to advise you further on options to achieve this at the appropriate time [TR2020/1908 refers].
28. While they do not all result in a direct cash benefit to firms, broader measures to support or stimulate the economy will also ultimately benefit businesses by increasing incomes, consumer confidence, spending, and positioning the economy to recover from the economic shock of COVID-19. This includes various measures already announced, including support for re-training and re-employment, shovel-ready infrastructure projects, and support for the tourism sector. Further allocations from the CRRF will also have the potential to support businesses in this way.

We have also identified a number of potential options that are worth further investigation

29. s9(2)(f)(iv)

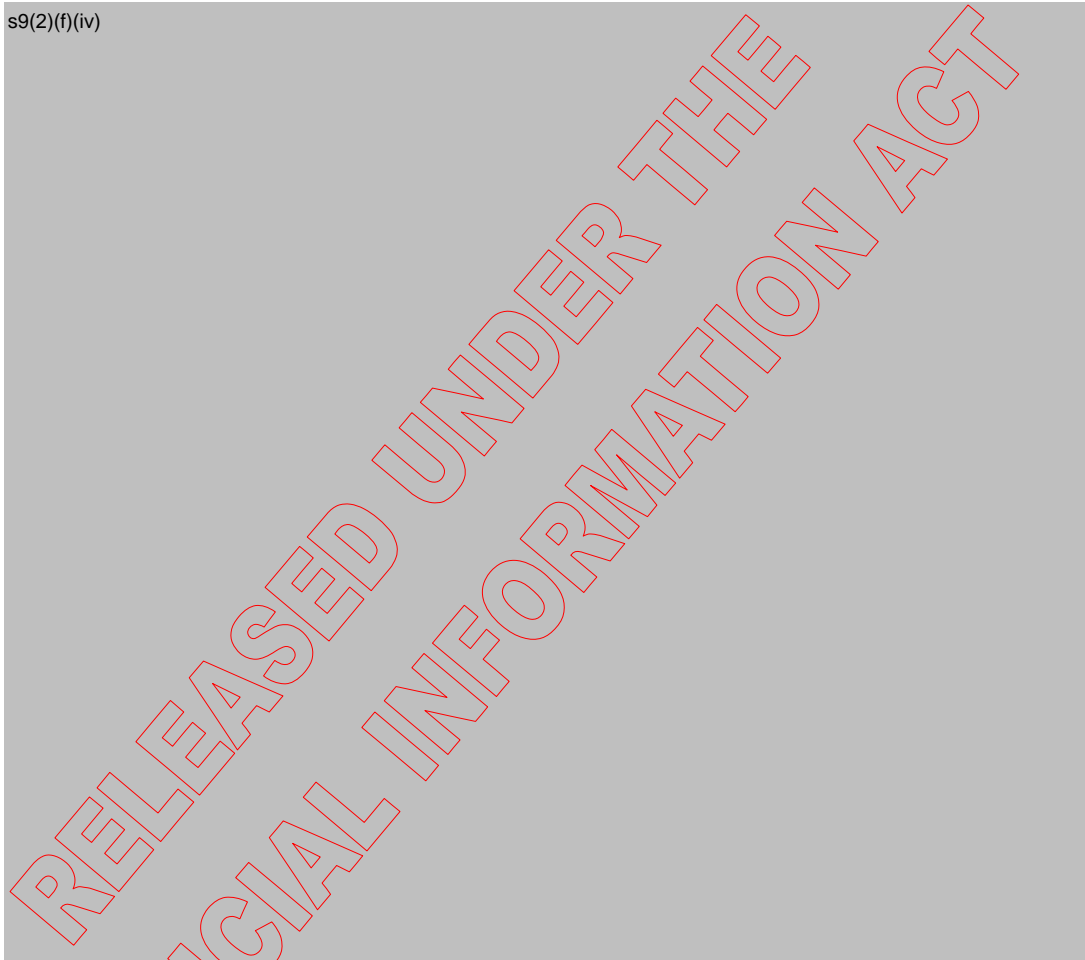
30. We will also monitor access to finance among SMEs, particularly in relation to existing measures. This financing challenge pre-dates COVID-19.

IN-CONFIDENCE**Building Confidence and Certainty**

Proactive communication can help businesses to better manage risks

31. The shift to a market-led recovery is most relevant in relatively positive health scenarios. We must also think about the fiscal response if downside scenarios materialise. You have an opportunity to consider the objectives, settings and triggers for policy responses if a resurgence of the virus occurs.

32. s9(2)(f)(iv)

***Greater visibility on the economic strategy can support incentives to invest***

33. The economic strategy should incentivise a shift to a COVID resilient economy, set up to resist another shock and recover rapidly.

s9(2)(f)(iv)

34. Technological developments and the need to respond to climate change were causing disruptive changes to the global economy prior to COVID-19. COVID-19 has accelerated some of this transition. Key trends include the rapid rise of digital operating models, a mobile workforce, the shared economy, automation, and changes to supply chains and the movement of goods.
35. Responding to some of the more complex, structural issues such as climate change, housing and inequality will continue to take time and will generate transition costs [TR 2020/1987 refers].

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36. In the short-term, there are likely to be opportunities to signal elements of that transition (including funding commitments), in order to provide businesses with the confidence that investments they make will align with the future economy.

Rebuilding Balance Sheets

The credit channels remain relevant

37. The funding options for businesses are heavily influenced by the health and risk appetite of the banking system. During the course of 2020 we may see a rise in non-performing loans as unemployment increases and house prices fall.
38. There is a risk that over time this could lead to a contraction in lending which would exacerbate the economic recession. It is likely to take several months for the extent and impact of non-performing loans to become clearer. The Reserve Bank is conducting a survey of credit conditions, and more granular data will be available in July 2020.
39. In this environment schemes to support the credit channels and provide liquidity remain relevant, despite limited uptake of some schemes to date. Businesses are likely to be more willing to take on debt if a higher degree of certainty returns, and the “working capital cycle” begins again (this is the period from purchase of new stock until a business receives cash from the sale of goods and services).

Access to equity or equity-like funding will become more important as businesses seek to rebuild their balance sheets or access capital for growth

40. In order to operate on a sustainable basis, businesses require a funding mix that involves an appropriate balance of “equity” and debt.
41. Equity can be accumulated through retaining earnings (i.e. profits) or through contributions from shareholders. Businesses have limited ability to rely on debt if they have reduced equity and/or the business is not profitable.
42. As noted earlier in this report, many businesses will have seen their equity reduced or eliminated. For businesses that are highly profitable and which can recover from the COVID-19 crisis quickly, it may be possible that they can operate with a weak balance sheet for a period, and restore their position through rapid recovery and accumulation of earnings.
43. For many businesses this will not be the case, and the solution will be additional equity. This was a key theme of a “market sounding” recently completed by the Treasury [TR2020/1865 refers].²
44. For ESBIs, access to equity capital currently remains very good. Share prices have also proved resilient even as many listed businesses have either withdrawn or reduced their earnings forecasts.
45. By contrast, many smaller or mid-sized businesses appear to be facing difficulty obtaining equity or “equity-like” funding (i.e. funding or support that does not have to be repaid within a contracted period). The SME-financing challenge existed prior to COVID-19. Public and private equity markets are small; credit provision is concentrated in the residential property sector, which is large relative to New Zealand’s economy.

² The report recommended against the creation of a hybrid debt or loan guarantee scheme given those schemes were not seen to address the challenge around access to equity being faced by business.

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46. If otherwise well-run and viable businesses are unable to access equity, there is a risk that they become “zombie businesses” that cannot invest and contribute to the rebuild.

We will continue to monitor broader market conditions and the performance of existing schemes

47. We will continue to work with MBIE, the IRD, and the RBNZ over the coming weeks and months to understand market dynamics.
48. We are also considering how ongoing monitoring of the effectiveness of the SBCS and the BFG can contribute to the cross-government work programme to investigate and address gaps in capital markets and proposes a joint report back to you on these issues by the end of 2020 [refer DEV-20-SUB-0119].

Next Steps

49. We will report back to you as appropriate, and note that if market conditions were to significantly worsen, advice may need to be provided quickly.

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Treasury Report: Indemnity Request for Provincial Growth Fund Limited

Date:	16 July 2020	Report No:	T2020/1699
		File Number:	SH-11-1-2

Action sought

	Action sought	Deadline
Hon Grant Robertson Minister of Finance	<p>EITHER:</p> <p>Agree to grant MBIE's proposed indemnity and altered Constitution for Provincial Growth Fund Limited (PGFL).</p> <p>OR:</p> <p>Direct officials to prepare documents for an altered Constitution and indemnity for PGFL based on your preferred narrower scope.</p>	None

Contact for telephone discussion (if required)

Name	Position	Telephone	1st Contact
Callum Lo	Graduate Analyst, Transitions, Regions, and Economic Development	s9(2)(k)	N/A (mob) ✓
Jean Le Roux	Manager, Transitions, Regions, and Economic Development	s9(2)(k)	N/A (mob)

Minister's Office actions

Return the signed report to Treasury.

If the Minister agrees to give the indemnity requested by MBIE:

- Return** the signed, witnessed and dated *Deed of Indemnity* to Treasury.
- Arrange** for the attached Statement of Indemnity to be tabled in the House of Representatives as soon as practicable.

Refer a copy of this report to the Minister for Regional Economic Development.

Note any feedback on the quality of the report

Enclosure: Yes (attached)

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Treasury Report: Indemnity Request for Provincial Growth Fund Limited

Executive Summary

Provincial Growth Fund Limited (PGFL)'s current arrangements prevent it from holding non-PGF investments. As per PGFL's Constitution and Investment Management Agreement, it may only hold PGF investments. The indemnity you granted in December 2019 also only covers PGF investments.

Joint Ministers have since agreed to establish the \$300 million Regional Investment Opportunities Tagged Contingency (RIOTC). In addition, the Treasury understands Ministers are currently discussing proposals that PGFL hold investments from the Infrastructure Reference Group Tagged Contingency (IRGTC) and several COVID-19 response programmes.

For PGFL to hold these investments, a wider Constitution would be required. MBIE propose widening the scope of PGFL's Constitution to cover a broader range and type of investments, including those held in subsidiaries. As a shareholding Minister, you may change PGFL's Constitution jointly with the Minister for Regional Economic Development. MBIE and PGFL will alter the Investment Management Agreement between them to align with these decisions.

To prevent PGFL holding investments not covered by its indemnity, a wider indemnity would also be required. It is open to you under the Public Finance Act 1989 (PFA) to decide whether it appears necessary or expedient in the public interest to grant an indemnity on behalf of the Crown to PGFL.

Given the uncertainty and risk from the proposed indemnity, this report sets out three broad options for the scope of PGFL's Constitution and indemnity:

1. **RIOTC investments only**
Widen PGFL's scope and indemnity to include RIOTC investments only (this scope could still include subsidiaries).
2. **RIOTC and IRGTC investments only**
Widen PGFL's scope and indemnity to include RIOTC and IRGTC investments (this scope could still include subsidiaries).
3. **MBIE proposal**
Widen PGFL's scope and indemnity, as requested by MBIE, to include a broader range and type of investments, and to include investments held in subsidiaries. This scope would not be limited to any particular initiatives, and would instead serve as a "catch-all" for regional economic development funding from various initiatives.

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Recommended Action

We recommend that you:

- a. **Note** that MBIE has requested a revised Constitution and new indemnity for PGFL.
- b. **Note** that MBIE must provide a Special Resolution for you to sign to amend PGFL's Constitution.
- c. **Note** MBIE and PGFL will alter the Investment Management Agreement between them to align with these decisions.
- d. **Note** that under section 65ZD of the PFA, you may, on behalf of the Crown, give an indemnity if it appears to you to be necessary or expedient in the public interest to do so, on any terms and conditions as you see fit.
- e. **Note** that as the contingent liability of the indemnity is over \$10.0 million, section 65ZD(3) of the PFA requires you to present as soon as practicable a statement to the House of Representatives that the indemnity has been granted.
- f. **Note** that given the uncertainty and risk from MBIE's proposed indemnity, we have provided three options, detailed further in Annex C, for alternative scopes.

EITHER:

- g. **Direct** officials to provide documents to extend PGFL's scope to RIOTC investments only (this scope still includes wider asset classes and subsidiaries).

Agree / Disagree

OR:

- h. **Direct** officials to provide documents to extend PGFL's scope to RIOTC and IRGTC investments only (this scope still includes wider asset classes and subsidiaries).

Agree / Disagree

OR (Treasury recommendation):

- i. **Agree** that it is necessary or expedient in the public interest to grant MBIE's proposed indemnity to PGFL under section 65ZD of the PFA. This will also require you to:
 - i. **Sign, date and have witnessed** the attached Deed of Indemnity to grant the new indemnity proposed by MBIE.
 - ii. **Agree** to the proposed Constitution for PGFL as per rec e in MBIE briefing 3340-19-20.
 - iii. **Sign** and approve the Subscription Agreement for PGFL to hold further RIOTC funded investments as per rec i in MBIE briefing 3340-19-20.
 - iv. **Sign and date** the attached Statement of Indemnity and present it to the House of Representatives as soon as practicable after giving the indemnity, as the contingent liability of the indemnity exceeds \$10 million.

Agree / Disagree

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- j. **Agree** to write down any factors not outlined in our report that you decide to take into account as a record of your decision.

Agree / Disagree

- k. s9(2)(f)(iv)

Agree / Disagree

- l. **Refer** a copy of this report to the Minister for Regional Economic Development.

Referred / Not referred

Jean Le Roux
Manager, Transitions, Regions, and Economic Development

Hon Grant Robertson
Minister of Finance

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Treasury Report: Indemnity Request for Provincial Growth Fund Limited

Background

1. Provincial Growth Fund Limited (PGFL) is a Schedule 4A company set up to hold loan and equity investments made through the Provincial Growth Fund (PGF). It does not have any active role in managing investments. The Provincial Development Unit (PDU) within MBIE manages investments on behalf of the company. PGFL must accept novation (transfer) of all investment agreements, despite having no ability to influence, assess or approve the investments prior to novation.
2. In 2019, PGFL's directors advised MBIE that they would not act without an indemnity; you later granted this indemnity in December [TR 2019/2540 refers].
3. In January 2020, Regional Economic Development (RED) Ministers agreed to establish the \$300 million Regional Investment Opportunities Tagged Contingency (RIOTC) [BR 2030 19-20 refers]. RIOTC funds infrastructure projects that do not meet all of the PGF's criteria.
4. Shareholding Ministers also agreed to amend PGFL's constitution to include RIOTC investments and update Cabinet on the changes to the scope of PGFL. PGFL's current constitution only allows it to hold debt and equity investments from the PGF.
5. MBIE advise that it is possible that PGFL will also hold investments arising from the Infrastructure Reference Group Tagged Contingency (IRGTC).
6. MBIE now seeks agreement from you and the Minister for Regional Economic Development, as shareholding Ministers, to the proposed changes to PGFL's constitution [BR 3340-19-20 refers].
7. PGFL's indemnity from the Crown does not currently cover any losses arising from MBIE's management of these new investments. MBIE advises that a new indemnity is therefore required.
8. s9(2)(f)(iv)

IN-CONFIDENCE**Proposed Changes to Constitution**

9. MBIE proposes that the Constitution be widened to cover:
 - i. **Non-PGF investments.** PGFL could hold investments from the PGF “and other regional economic development funding”. The Investment Management Agreement would require PGFL to accept novation of investment agreements from as yet to be determined sources, including from outside the Crown.
 - ii. **PGFL subsidiaries.** Currently investments are held directly by PGFL. The Constitution would explicitly enable PGFL to establish subsidiary companies (which can be up to 49.9% non-Crown owned) for the purpose of receiving, holding, managing or administering investments.
 - iii. **All asset types.** Currently the Constitution and Investment Management Agreement enable MBIE to novate loan and equity investments to PGFL. The proposed amendments to the Constitution and Investment Management Agreement enable investments in assets (both tangible and intangible), to be novated to PGFL or any subsidiary of PGFL. This could include assets transferred to PGFL or its subsidiaries by parties outside the Crown.
10. MBIE has proposed these changes for flexibility and future-proofing, so new investments can be swiftly novated to PGFL without the need to seek future amendments.
11. Under the proposals, PGFL would still play no role in selecting or managing investments.
12. s9(2)(f)(iv)

Proposed indemnity

13. Clause 2.1 of the proposed new deed of indemnity indemnifies PGFL *‘from and against any and all losses, liabilities and damages which the Company or any Subsidiary suffers or incurs and any costs, charges and expenses which the Company or the Subsidiary properly and reasonably suffers or incurs arising out of or in connection with the performance, or non-performance, of MBIE’s powers, duties and functions under the Investment Management Agreement’*.
14. Clause 2.4 of the proposed new deed of indemnity provides that the indemnity does *‘not extend to any losses, liabilities, damages, costs, charges, expenses or any other liabilities which result (directly or indirectly) from fraud, bad faith, wilful breach of this deed or any applicable law, recklessness, or negligence on the part of the Company or any Subsidiary’*.
15. There is no cap on the proposed indemnity.

Officials’ assessment

16. Section 65ZD of the PFA provides that you may give an indemnity on behalf of the Crown if it appears to you that it is “*necessary or expedient in the public interest*” to do so, and to give such an indemnity on any terms and conditions that you think.
17. It is a matter for you to decide whether you are satisfied that it is necessary or expedient in the public interest to give the indemnity and any terms and conditions that you think fit. The PFA does not contain any express mandatory criteria that you must

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consider when making the decision. There is also no case law on how the test in section 65ZD of the PFA is to be applied.

18. The following paragraphs set out factors that officials consider are relevant to that assessment. You may decide to ignore these factors, or take into account other factors you consider relevant, and you may give such weight to the factors referred to below as you deem fit. You should make an independent decision and are not bound to accept the assessment below. However, your decision must be based on reasonable grounds.
19. If you take into account other factors not outlined in our report, we recommend that you write these down as a record of your decision.
20. We consider, however, that there is a degree of uncertainty and risk in the current indemnity as proposed. As such, this report also sets out a number of options, in Annex C, with alternative scopes.

Public interest

21. The PFA does not define 'the public interest'. However, it is generally accepted that the public interest is broadly equivalent to the concept of the public good and can cover a wide range of values and principles relating to the public good, or what is in the best interests of society. In the context of the PFA, the public interest should be viewed in a New Zealand context, that is, in the interest of the New Zealand public.
22. Our advice was that the public interest in the original indemnity was indirect [TR 2019/2540 refers]. There was a public interest in having the investments managed beyond the life of PGF by a separate legal entity. The indemnity enabled PGFL to operate as intended. There was also a public interest in having directors with necessary skills and experience to oversee the management of PGFL investments. We considered it unlikely that appropriately skilled directors would accept their appointment to PGFL without an indemnity.
23. Our view is that there would be the same indirect public interest from the wider indemnity proposed by MBIE.

Necessary or expedient

24. "Necessary" or "expedient" is not defined in the PFA, so the ordinary meaning of those words will apply. The Treasury considers that "necessary" is a higher threshold than "expedient". "Necessary" suggests that the activity could not go ahead without the indemnity, or there is no reasonable alternative to making the indemnity.
25. In determining whether giving an indemnity is 'necessary or expedient in the public interest' it is necessary to assess the risks of the indemnity, and benefits. A table of risks and benefits is set out in Annex B.

Is the public interest test met?

26. We consider that it is open to you to determine whether it is necessary or expedient in the public interest to grant an indemnity to PGFL.
27. Treasury considers that there is an indirect public interest in granting this indemnity and that the public interest test is met for all three of the options provided in Annex C.
28. While the new indemnity will cover riskier investments, these investments would sit with the Crown anyway should these investments not be transferred to PGFL.
29. However, it is ultimately for you to decide whether it is necessary or expedient in the public interest to provide this indemnity.
30. Annex B provides in-depth analysis of the risks and benefits of granting an indemnity to PGFL. This analysis applies to all three options presented in Annex C.

IN-CONFIDENCE***Recommended Terms and Conditions***

31. Regardless of which option you select, or if you select an option we have not suggested, we recommend that any indemnity that you grant be reviewed once decisions are made as to whether PGFL will become an active company.

Other Relevant Information

32. This indemnity request has been prepared in consultation with MBIE. MBIE's legal team is comfortable with the proposed indemnity wording.
33. We note that this report has been independently reviewed by a commercial barrister who was also formerly the Treasury Chief Legal Advisor.

Next Steps

34. If you wish to proceed with option 1 or 2, we will ask MBIE to prepare an alternative deed of indemnity for you to sign, once we receive your view on the preferred scope of the indemnity.
35. If you agree that it appears to you to be necessary or expedient in the public interest to give the indemnity on the terms proposed by MBIE (option 3) then you will need to sign, date and have witnessed the deed of indemnity.
36. As with the last indemnity, we are currently unable to estimate the potential claims under the new indemnity, but it is highly likely that these could exceed \$10 million. If you decide to grant the indemnity, we recommend that you present the Statement to the House of Representatives as required by section 65ZD(3) of the PFA (see Annex A).

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*Annex A: Statement of Indemnity for presentation to the House***STATEMENT OF INDEMNITY GIVEN UNDER SECTION 65ZD OF THE PUBLIC FINANCE ACT 1989**

On _____, I, Grant Robertson, Minister of Finance, on behalf of the Crown, gave an indemnity to Provincial Growth Fund Limited in relation to the investment management agreement between to Provincial Growth Fund Limited and the Ministry of Business, Innovation & Employment.

Dated at _____ this _____ day of _____ 2020

Grant Robertson
Minister of Finance

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*Annex B: Risks and Benefits***Risks**

Risk	Explanation
Loss to a third party	If MBIE's management of the investments created loss for a third party, PGFL as the legal owner of the assets, could potentially be liable to that third party (for example a party to the Investment Management Agreement, or the owner of property damaged by a physical asset owned by PGFL but managed by MBIE).
Broader classes of assets	<p>Currently the types of investments that can be novated to PGFL are loan or equity investments. It is proposed that other assets (both tangible and intangible (such as contract rights, or intellectual property)) will also be able to be novated to PGFL or its subsidiaries.</p> <p>The risks of managing loan and equity investments are different from managing assets. In our view, the management of assets has a much broader range of risks than management of loan or equity investments, and assets are more likely to require more active management (for example maintenance or insurance). In addition, the nature of any potential legal liability and therefore potential quantum of loss differs depending on the type of investment. For example, potential legal liability relating to a loan, will be different compared to potential legal liability for a physical asset.</p>
Investments with as-yet unknown investment criteria	Currently PGFL receives novation of PGF investments. Investments made from the PGF and the RIOTC have known investment criteria, therefore the risk profile of these investments is known to a certain extent. The proposed new indemnity would extend to investments from funds with as yet unknown funding criteria. This means the risk profile of such investments cannot be assessed at this time, nor the extent to which any such risks are mitigated by the Investment Management Agreement. Therefore the question of whether this increases the likelihood that the indemnity will be called cannot be determined.
Investments owned by parties other than the Crown	In addition, the investments (including assets) proposed to be transferred to PGFL are no longer proposed to be restricted to investments owned by the Crown and could include investments owned by third parties. The risk profile of such investments is unknown and because MBIE has had no involvement with the investments, it cannot give covenants or warranties to PGFL as to whether (for example) security documents relating to the investment have been properly signed and authorised.
Subsidiaries under PGFL	<p>To date PGFL has not established any subsidiaries. But we understand that it is proposed that PGFL may establish subsidiaries in the future to hold specific types of investments, s9(2)(f)(iv)</p> <p>s9(2)(f)(iv) We are unable to assess their constitutions, purpose or powers, or the degree to which PGFL may own or control the subsidiaries, as the subsidiaries have not been established. Therefore, we are unable to assess fully how any such subsidiaries may increase the risk of the indemnity being called.</p>
PGFL's ability to monitor and control subsidiaries	<p>MBIE has advised that the effect of section 97 of the Crown Entities Act is that the subsidiaries would not be able to do anything that the PGFL cannot do.</p> <p>We note that section 97 of the Crown Entities Act provides that the parent</p>

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	<p>Crown entity, must ensure, to the extent that it is reasonably able to do so, that any of its subsidiaries does not do anything that the parent itself does not have the power to do. The extent to which the parent Crown entity can ensure this will depend on the constitution of the subsidiary and the rights it has under that, and also the extent to which the company is owned or controlled by the parent Crown entity. The changes to the Constitution do not propose to limit the types of subsidiaries that PGFL could establish. It is clear from the legislative history to section 97 that it has been recognised that where a subsidiary is not wholly owned or controlled by a Crown entity there may be circumstances where section 97 of the Crown Entities Act may not be able to be applied.</p>
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Benefits

Benefit	Explanation
Removal of risky assets from Crown balance sheets	<p>In considering the risks of widening PGFL's indemnity, it is important to note the relevant comparison is between these investments sitting with PGFL, and the alternative (the indemnity being denied and the investments remaining with the Crown). RIOTC investments and relevant IRGTC investments will likely be managed by the PDU under either scenario, and will likely remain on MBIE's balance sheet if they cannot be novated to PGFL. Other investments may sit elsewhere within the state sector.</p> <p>Thus a key benefit of granting the indemnity is the removal of these risky assets from Crown balance sheets.</p>
Retention of suitable directors for PGFL	<p>MBIE advise that it is unlikely that the directors of PGFL will be willing to accept novation of the broader range and type of investments without a revised indemnity to cover those new investments. Directors have no power to select the investments, and day-to-day management of the investments is carried out by MBIE. However, the directors are responsible for their director duties under the Companies Act 1993 and for having oversight of how MBIE manages and administers the investments on PGFL's behalf.</p> <p>As above, we consider that there is benefit in having the investments managed beyond the life of the PGF by a separate legal entity and enabling PGFL to operate as intended. In this instance, the indemnity will allow PGFL to hold wider regional investments for purposes determined by Cabinet. There is also benefit in having directors with the necessary skill and expertise having oversight of how the investments held by PGFL are managed. It is unlikely skilled directors would accept appointment without an indemnity.</p>

Balancing of risks and benefits

1. MBIE's management of the investments could potentially cause loss to PGFL, the legal owner of the investments. In addition, if MBIE's management of the investments created loss for a third party, PGFL as the legal owner of the assets, could potentially be liable to that third party. However, these risks will likely still sit with the Crown if investments are not novated to PGFL.
2. However, certain factors will cause risks to differ, based on where the investments sit. The Crown has the benefit of certain statutory immunities, producing a better position in relation to any legal liability if it owns the investments, compared to if they are owned by PGFL or its subsidiaries (each an entity outside the legal Crown). However, whether

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and the extent to which immunities are available would require a case by case assessment.

3. The reputational risk to the Crown may also be greater if PGFL's directors call an indemnity than if losses occur on MBIE's balance sheet.
4. If the investments sit with PGFL and are managed by PDU, they are governed by PGFL's Investment Management Agreement. This does not place any specific obligations on MBIE in relation to risks that might arise from owning assets. For example, an obligation to ensure any physical assets are appropriately maintained or insured.

Form of the Indemnity

5. Any changes to the classes and types of investments that PGFL will hold, and whether these will be held by subsidiaries of PGFL, require changes to PGFL's Constitution. As discussed above, because of the limited role of the directors of PGFL, these changes must also be reflected in the scope of the indemnity. Therefore, if you agree to grant an indemnity with a revised scope, changes that are consistent with that scope will need to be made to PGFL's Constitution.
6. We are not aware of any Cabinet or Ministerial decisions having been taken yet about PGFL holding non-PGF funded investments, other than the agreement by shareholding Ministers to make amendments to the PGFL constitution to allow investments made from RIOTC funds to also be held by PGFL.

7. s9(2)(f)(iv)

8.

9.

10.

11. In Annex C we detail the options regarding the scope of the indemnity.

No viable alternatives to an indemnity

12. Treasury considers that there are no alternatives to providing an indemnity to PGFL, if the current model is to continue to operate. MBIE also considers that the scope of any

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indemnity needs to be consistent with the scope of the investments to be novated to PGFL.

13. In principle we agree that the scope of any indemnity needs to match the scope of any investments to be novated to PGFL. If you were to grant an indemnity in relation to certain types of investments (rather than the broader range of investments proposed by MBIE), this would restrict the types of investments that could be novated to PGFL.

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Annex C: Options on the scope of the new indemnity

Options	Advantages	Disadvantages
1. Grant an indemnity that extends to RIOTC investments	Consistent with the decision of shareholding Ministers to change the PGFL constitution to allow RIOTC investments to also be held by PGFL.	<p>RIOTC investments include physical assets, which are riskier than debt or equity investments.</p> <p>If Cabinet, or relevant Ministers, decide additional classes or types of investments to be held by PGFL shareholding, then additional changes to PGFL's Constitution and a new indemnity will be required.</p>
2. Grant an indemnity that extends to RIOTC investments and IRGTC investments	<p>Consistent with the decision of shareholding Ministers to change the PGFL constitution to allow RIOTC investments to be held by PGFL.</p> <p>Provides flexibility to transfer IRGTC investments should Cabinet or relevant Ministers decide it was appropriate for PGFL to hold these.</p>	<p>RIOTC investments include physical assets, which are riskier than debt or equity investments.</p> <p>We do not have sufficient information to assess all the risks of granting the indemnity if PGFL were to hold IRGTC investments.</p> <p>The changes pre-empt any decisions of Cabinet or relevant Ministers on who will hold any IRGTC investments.</p> <p>If Cabinet, or relevant Ministers decide additional classes or types of investments to be held by PGFL, then additional changes to PGFL's Constitution and a new indemnity will be required.</p> <p>The changes to include IRGTC investments would occur before Cabinet decisions were made on whether PGFL would transition to an active company.</p>
3. Grant an indemnity with the scope requested by MBIE	<p>Consistent with the decision of shareholding Ministers to change the PGFL constitution to allow RIOTC investments to be held by PGFL.</p> <p>Provides flexibility to transfer any other investments should Cabinet or relevant Ministers decide it was appropriate for PGFL or its subsidiaries to hold these.</p>	<p>RIOTC investments include physical assets, which are riskier than debt or equity investments.</p> <p>We do not have sufficient information to assess the risk of granting the indemnity if PGFL were to hold other non-PGF investments, or if PGFL subsidiaries were to be established.</p> <p>The changes pre-empt any decisions of Cabinet or relevant Ministers on who will hold any non-PGF investments.</p> <p>s9(2)(f)(iv)</p>



Deed of Indemnity

Provincial Growth Fund Limited (the Company)
The Sovereign in Right of New Zealand acting by and
through the Minister of Finance (the Crown)

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DEED OF INDEMNITY

Date:

PARTIES

Provincial Growth Fund Limited (the Company)

The Sovereign in Right of New Zealand acting by and through the Minister of Finance (the Crown)

(each, a Party and together, the Parties)

BACKGROUND

- A The New Zealand Government has allocated three billion dollars over a three year term to invest in regional economic development through the Provincial Growth Fund (*PGF*) which aims to lift productivity potential in New Zealand's provinces. The PGF is administered by the Provincial Development Unit (*PDU*) which was established in 2018 within the Ministry of Business, Innovation and Employment (*MBIE*). Other regional economic development funding may be administered by, or with the assistance of, the PDU from time to time.
- B In the course of administering the PGF and other regional economic development funding, MBIE may identify certain Investment Agreements that are to be transferred to the Company.
- C The Company, a Schedule 4A company under the Public Finance Act 1989, was established to act as the nominated legal entity for taking novation of rights and obligations under an Investment Agreement and its Related Agreements in relation to the relevant Investment.
- D On or about the date of this deed, MBIE and the Company entered into an investment management agreement (the *Investment Management Agreement*) whereby the parties agreed the manner in which rights and obligations under an Investment Agreement will be novated to the Company, and the manner in which MBIE will manage and administer the Novated Investments and Novated Investment Agreements on behalf of the Company.
- E Accordingly, the Crown has agreed (among other things) to indemnify the Company from and against any and all losses, liabilities and damages which the Company or any Subsidiary suffers or incurs and any costs, charges and expenses which the Company or any Subsidiary properly and reasonably suffers or incurs arising out of or in connection with the performance, or non-performance, of MBIE's powers, duties and functions under the Investment Management Agreement in accordance with the terms of this deed. This indemnity is given pursuant to section 65ZD of the Public Finance Act 1989.

COVENANTS**1 DEFINITIONS AND INTERPRETATION****1.1 Definitions**

In this deed, unless the context requires otherwise:

Board means the board of directors of the Company;

Business Day means a day (other than a Saturday or Sunday) on which registered banks (as defined in the Reserve Bank of New Zealand Act 1989) are open for general banking business in Wellington, New Zealand;

Company means Provincial Growth Fund Limited, company number 7707517, having its registered office at 15 Stout Street, Wellington Central, Wellington, 6011, New Zealand;

Indemnified Amounts means any all losses, liabilities, damages, costs, charges and expenses indemnified pursuant to clause 2.1;

Investments has the meaning given to that term in the Investment Management Agreement;

Investment Agreements has the meaning given to that term in the Investment Management Agreement;

Investment Management Agreement has the meaning given to that term in Recital D;

MBIE has the meaning given to that term in Recital A;

Novated Investments has the meaning given to that term in the Investment Management Agreement;

Novated Investment Agreements has the meaning given to that term in the Investment Management Agreement;

PDU has the meaning given to that term in Recital A;

PGF has the meaning given to that term in Recital A;

Recipient has the meaning given to that term in the Investment Management Agreement;

Related Agreements has the meaning given to that term in the Investment Management Agreement;

Relevant Action means any action or claim which is brought, or threatened in writing to be brought, against the Company or any Subsidiary, in respect of which indemnity may be sought by the Company from the Crown pursuant to clause 2.1; and

Subsidiary means a subsidiary of the Company within the meaning given to that term "subsidiary" in section 5 of the Act and has been established in accordance with the Company's constitution.

1.2 Interpretation

In the interpretation of this deed, unless the context otherwise requires:

Clauses and Schedules: a reference to a clause or a schedule is to a clause or schedule of this deed, and a reference in a schedule to a clause is a reference to a clause in that schedule;

Currency: a reference to any monetary amount is to New Zealand currency;

Defined Terms: words or phrases appearing in this deed with capitalised initial letters are defined terms and have the meanings given to them in this deed;

Documents: a reference to any document, including this deed, includes a reference to that document as amended or replaced from time to time;

Headings: headings appear as a matter of convenience and do not affect the construction of this deed;

No Contra Proferentem Construction: the rule of construction known as the contra proferentem rule does not apply to this deed;

Related Terms: where a word or expression is defined in this deed, other parts of speech and grammatical forms of that word or expression have corresponding meanings;

Singular, Plural and Gender: the singular includes the plural and vice versa, and words importing one gender include the other genders;

Statutes and Regulations: a reference to an enactment or any regulations is a reference to that enactment or those regulations as amended, or to any enactment or regulations substituted for that enactment or those regulations; and

Writing: a reference to "written" or "in writing" includes all modes of presenting or reproducing words, figures and symbols in a tangible and permanently visible form.

2 **INDEMNITY**

2.1 **Crown Indemnity**

To the fullest extent permitted by law and subject to the terms of this deed, the Crown irrevocably indemnifies (and agrees to keep indemnified) the Company from and against any and all losses, liabilities and damages which the Company or any Subsidiary suffers or incurs and any costs, charges and expenses which the Company or the Subsidiary properly and reasonably suffers or incurs arising out of or in connection with the performance, or non-performance, of MBIE's powers, duties and functions under the Investment Management Agreement.

2.2 **Notification of Claims**

- (a) The Company shall, as soon as practicable (or, in the case of a Relevant Action which is threatened in writing to be brought, as soon as practicable after the Company becomes aware of the same), notify the Crown in writing of such Relevant Action (giving reasonable details thereof).
- (b) In the case of any Relevant Action which has been commenced, the Crown must assume the defence thereof.

2.3 **Conduct of Defence by the Crown**

- (a) The Company shall provide, and shall procure that any Subsidiary provides, to the Crown all such information and assistance as the Crown reasonably requests, subject to the reimbursement of all fees, costs and expenses properly and reasonably incurred in providing such information and assistance, to allow the Crown to conduct the defence of the Relevant Action.

- (b) The Crown shall to the extent reasonable and practicable in all the circumstances, keep the Company informed of a Relevant Action as and when reasonably requested by the Company in respect of that Relevant Action (or any proposed settlement or compromise thereof).

2.4 **Limitation of Indemnity**

The indemnity contained in this clause 2 shall not extend to any losses, liabilities, damages, costs, charges, expenses or any other liabilities which result (directly or indirectly) from fraud, bad faith, wilful breach of this deed or any applicable law, recklessness, or negligence on the part of the Company or any Subsidiary.

3 **PAYMENT**

3.1 **The Crown's Payment Obligations**

Subject to clause 2.4, the Crown shall promptly pay the Company upon demand in respect of its indemnity for any Indemnified Amount (*Indemnity Payment*).

3.2 **Reimbursement**

If the Company receives an Indemnity Payment, and the Company or any Subsidiary subsequently recovers any amount from any third party for or in respect of any Relevant Action to which the Indemnity Payment relates (*Recovered Amount*), the Company must promptly:

- (a) notify the Crown of the Recovered Amount; and
- (b) pay the Crown an amount equal to the lesser of:
 - (i) the Recovered Amount less any reasonable costs and expenses incurred by the Company in making that recovery; or
 - (ii) the Indemnity Payment.

3.3 **Legal Privilege**

- (a) In relation to any notification or assistance to be provided in terms of this deed and in all other communications between the Company, any Subsidiary, the Crown and their respective legal advisors in relation to any legal proceeding or claim, confidentiality shall be maintained, disclosure is to be made on the basis of common interest, and legal privilege will continue to be asserted and not waived unless the Parties otherwise agree, in writing.
- (b) The Parties will take all reasonable steps to maintain legal privilege in their communications regarding any legal proceeding or claim.

4 **NO COUNTER-INDEMNITY**

Regardless of any rights of the Crown at law, the Crown acknowledges and agrees that the Company is not liable to repay, reimburse or counter-indemnify the Crown for any payment the Crown may make under this deed except to the extent provided for in clause 3.1 or otherwise in this deed.

5 **ASSIGNMENT**

The Company may not assign, transfer or otherwise deal with its rights, interests or obligations under this deed without the prior written consent of the Crown.

6 **CONFIDENTIALITY**

6.1 **Confidentiality**

Subject to clause 6.2, the Parties must keep confidential the terms of this deed.

6.2 **Permitted Disclosure**

- (a) Nothing in clause 6.1 will limit:
- (i) any disclosures required to be made by a Party by law (including in accordance with paragraph (c) below) or required by any regulatory authority or in accordance with the requirements of any New Zealand Government or Parliamentary convention ; or
 - (ii) disclosures to professional advisers; or
 - (iii) disclosures in the context of any proceedings in respect of this deed or in defence of legal proceedings brought by or against any person; or
 - (iv) a public statement by a Party about this deed, provided that, in each case, each Party will first provide each other Party with a reasonable opportunity to review and comment on the proposed public statement; or
 - (v) any disclosure agreed to in writing by the Parties.
- (b) Prior to any disclosure under paragraphs (a)(i) and (a)(iii) above, or (c) below, the Party intending to disclose any part of the terms and/or the existence of this deed must first notify the other party in writing of the intended disclosure and exercise its reasonable efforts to obtain assurances that the terms disclosed and/or the existence of this deed will be treated confidentially.
- (c) Each Party acknowledges that the other is or may be subject to the Official Information Act 1982 (the *OIA*) and that each party is obliged to disclose the terms and the existence of this deed under the *OIA* if so requested unless there is good reason pursuant to the terms of the *OIA* to withhold that information. Each party will use reasonable endeavours to advise the other party of any request received by it under the *OIA* that relates to the terms and the existence of this deed.

7 NOTICES AND COMMUNICATIONS

7.1 Notice Details

The details of the Parties are as follows:

Name Provincial Growth Fund Limited
 Address 15 Stout Street, PO Box 1473, Wellington 6140
 Email PGFL-secretary@pgflimited.co.nz
 Phone 0508 743 473
 Attention Robert Pigou

Name The Sovereign in right of New Zealand acting by and through the Minister of Finance
 Address Level 3 (Reception), 1 The Terrace, Wellington 6011
 Phone 04 472 2733
 Attention The Treasury Solicitor

7.2 Form of Notice

Each notice, demand, consent, approval or other communication (*Notice*) under this deed:

- (a) must be in writing and signed by an authorised representative of the Party; and
- (b) must be hand delivered or sent by prepaid post or e-mail (if applicable) to the recipient's address for notices specified in clause 7.1 of this deed (as varied by any Notice given by the recipient to the party).

7.3 Effective on Receipt

A Notice given in accordance with clause 7.2 takes effect when received (or at a later time specified in it), and is taken to be received:

- (a) if hand delivered, on delivery; or
- (b) if sent by prepaid post, on the fifth Business Day after the date of posting; or
- (c) if sent by e-mail, on the date and time at which it enters the addressee's information system as shown in a confirmation delivery report from the sender's information system which indicates the e-mail was sent to the e-mail address of the addressee notified for the purposes of this clause,

but if the delivery, receipt or transmission is not on a Business Day or is after 5:00 p.m. (addressee's time) on a Business Day, the Notice is taken to be received at 9:00 a.m. (addressee's time) on the next Business Day.

1 DISPUTES

The Parties agree that in the event of a dispute concerning the terms of this deed (a *Dispute*):

- (a) the Parties will make an effort to resolve the Dispute in at least one meeting of the authorised representatives of each of the Crown and the Company within 10 Business Days of the Dispute being raised in writing by either Party; and
- (b) if the Dispute is not resolved within the time period set out in paragraph (a) above, or in the event a meeting of authorised representatives does not take place within that time period, the Dispute will be referred for resolution to the Minister of Finance (or an authorised representative) and the chair of the Company's board and those parties will make an effort to resolve the Dispute in at least one meeting within 20 Business Days of it being referred to them; and
- (c) if the Dispute is not resolved within the time period set out in subclause (b) above, or in the event that a meeting of the Minister of Finance (or an authorised representative) and the chair of the Company's board is not held within that time period (for whatever reason), the Dispute will be referred to and finally resolved by arbitration in accordance with the Arbitration Act 1996, excluding all of the Second Schedule to that Act other than clause 3 of that Schedule, in accordance with the following terms:
 - (i) if the Parties cannot agree on an arbitrator within 10 Business Days of one party notifying the other of its intention to exercise its right to refer the Dispute to arbitration pursuant to this subclause (c), then an arbitrator will be appointed by the President of the New Zealand Law Society for the time being; and
 - (ii) the number of arbitrators will be one and the place of arbitration will be Wellington, New Zealand.

2 GENERAL

2.1 Amendment

No amendment to this deed will be effective unless it is in writing and executed by all the Parties.

2.2 Counterparts

This deed may be executed in any number of counterparts. Once the Parties have executed the counterparts, and each Party has received a copy of each signed counterpart which that party did not execute, each counterpart will be deemed to be as valid and binding on the party executing it as if it had been executed by all the Parties.

2.3 Entire Agreement

This deed is the entire agreement between the Parties on its subject matter. This deed replaces all earlier agreements, whether oral or written, between the Parties relating to its subject matter.

2.4 Further Assurances

Each Party must do any thing, including execute and deliver any documents, as may reasonably be required by any other Party to obtain the full benefit of this deed according to its true intent. This obligation survives the termination of this deed.

2.5 No Waiver

A waiver of any provision of this deed will not be effective unless given in writing, and then it will be effective only to the extent that it is expressly stated to be given. A failure, delay or indulgence by any Party in exercising any power or right will not operate as a waiver of that power or right. A single exercise or partial exercise of any power or right will not preclude further exercises of that power or right or the exercise of any other power or right

2.6 Costs

Except as otherwise provided in this deed, each Party will pay its own costs in relation to this deed.

2.7 Governing Law

This deed and the rights of the Parties are governed by and construed in accordance with the laws of New Zealand. Each of the Parties irrevocably agrees that the Courts of New Zealand have non-exclusive jurisdiction to hear any suit, action or proceedings, and to settle any disputes which may arise out of or in connection with this deed and for such purposes irrevocably submits to the jurisdiction of such Courts.

EXECUTION

Signed for and on behalf of **the Sovereign in Right of New Zealand** acting by and through the **Minister of Finance** by:

Signature

Name:

Position:

Date:

in the presence of:

Name:

Occupation:

Address:

Signed for and on behalf of **Provincial Growth Fund Limited** by:

Director/Authorised Person

Director/Authorised Person

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Reference: T2020/2430 SH-11-4-3-13-2-5 (Aide Memoires)

Date: 16 July 2020

To: Minister of Finance (Hon Grant Robertson)

Deadline: None

Aide Memoire: Update on non-deposit taking lenders (NDTLs)

s9(2)(b)(ii)

You previously received advice on consumer credit support and several requests for assistance from NDTLs (*T2020-1063 refers*), and asked officials to undertake continued monitoring of the sector.

We are engaging regularly with the Financial Services Federation (FSF)

We are having fortnightly calls with the FSF, which is a key industry group for NDTLs (representing a number of non-bank lenders and large car finance companies), and receive fortnightly updates on hardship requests.

Hardship requests peaked over lockdown but have since dropped off

Hardship requests (for loan deferrals or reduced payments) from consumers and businesses increased significantly over the Level 4 lockdown period, peaking in the fortnight between 27 March and 9 April. Since then, the number of requests have largely tapered off and have been at normal levels over recent weeks. **Tables 1 and 2** demonstrate this trend based on data from FSF members between 14 March and 19 June. According to the survey, on the consumer lending side, 15% of mortgage customers and 7% of vehicle loan customers made hardship requests. On the business lending side, 19% of those with unsecured loans and nearly all with operating leases made hardship requests to NDTLs. Most customers who have made hardship requests have been granted loan variations by their lenders.

The FSF has not yet seen significant funding pressures amongst its members, but this may change as payment arrears increase. A few NDTLs have shown tentative signs of pressure. More widespread pressure could lead to funding difficulties for NDTLs who are funded by securitisations (bond trusts which are made up of pools of similar loans, and invested in by third-parties).

s9(2)(b)(ii)

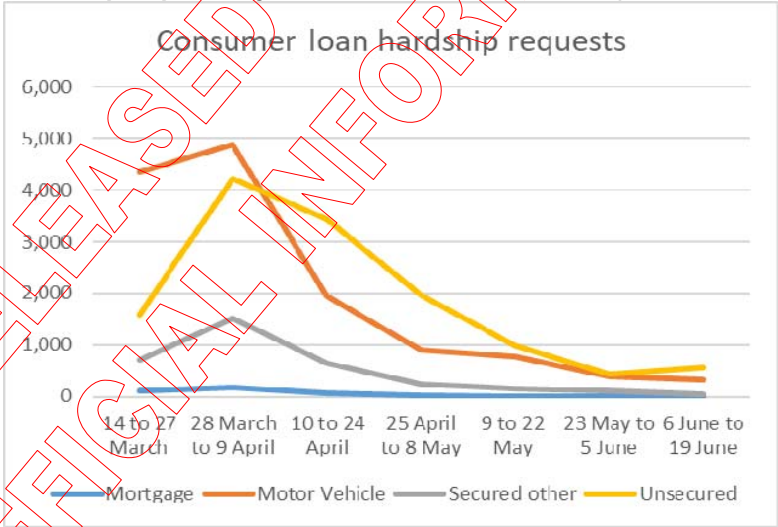
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The FSF expects that hardship requests and payment arrears will increase once further rounds of government support (such as the wage subsidy scheme and small business cashflow loan scheme) are used up. The FSF has noted that most of its members have not applied for the wage subsidy scheme despite offering hardship assistance to customers, because lenders still had their loan books and were unable to demonstrate their revenue had dropped significantly over the period of eligibility. NDTLs are currently engaging with customers who have low prospects of repayment to discuss their future options (for example, some vehicles have been voluntarily surrendered by customers who are no longer able to make loan repayments). NDTLs are also concerned about the customers they have yet to hear from, and are beginning to reach out to these customers as well.

We will continue to engage with the FSF and monitor the NDTL sector

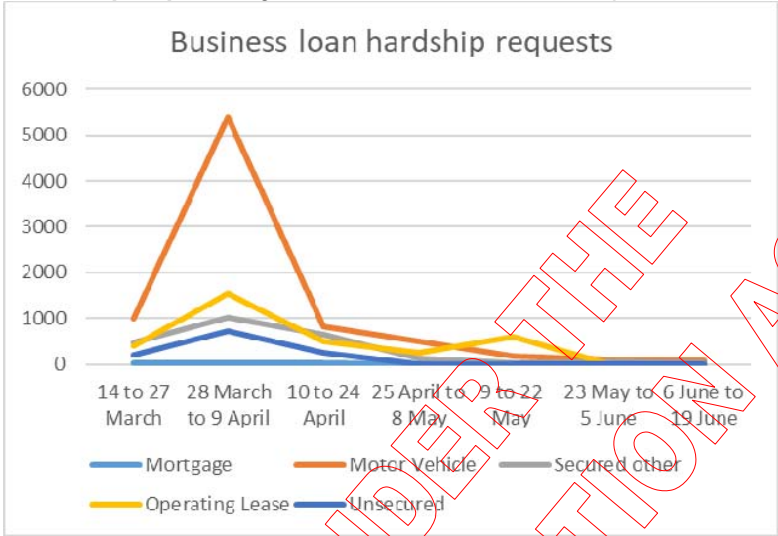
We will report back to you if there are any significant developments or signs of distress in the sector. s9(2)(f)(iv)

Table 1: Hardship requests by NDTL consumer customers (14 March to 19 June)



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Table 2: Hardship requests by NDTL business customers (14 March to 19 June)



Leona Feng, Senior Analyst, Financial Markets, s9(2)(k)
Robbie Taylor, Manager, Financial Markets, s9(2)(k)

Ministry of Transport
TE MANATO WAKA



Auckland Light Rail - next steps

Reason for this briefing	Cabinet has recently agreed to end the Auckland Light Rail proposals process and to refer the project to the Ministry of Transport and Treasury for further work. This briefing provides you with advice on how the Ministry of Transport and the Treasury intend to move forward.
Action required	Minister Twyford: discuss with Ministry officials. Ministers Robertson and Twyford: agree with recommendations, including for the transfer of funding to enable the Ministry and the Treasury to progress the work programme including the intellectual property discussions.
Deadline	5 August 2020
Reason for deadline	To allow the Ministry and the Treasury to mobilise the necessary advisors in a timely way, this will support the work to initiate intellectual property discussions.

Contact for telephone discussion (if required)

Name	Position	Telephone	First contact
Siobhan Routledge	Director, System Strategy and Investment	s9(2)(g)(ii)	
Steph Ward	Programme Director, Auckland Light Rail		
Bryn Gandy	Deputy Chief Executive, System Strategy and Investment		
Erana Sitterle	Senior Analyst, National Infrastructure Unit, The Treasury		
David Taylor	Manager, National Infrastructure Unit, The Treasury	s9(2)(k)	

MINISTER'S COMMENTS:

Date:		Briefing number:	OC200555
Attention:	Hon Phil Twyford Minister of Transport Hon Grant Robertson Minister of Finance	Security level:	COMMERCIAL IN CONFIDENCE

Minister of Transport's office actions☐ *Noted*☐ *Seen*☐ *Approved*☐ *Needs change*☐ *Referred to*☐ *Withdrawn*☐ *Not seen by Minister*☐ *Overtaken by events*

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Purpose of briefing

1. This briefing outlines how the Ministry of Transport and the Treasury intend to take forward the next phase of the city centre to Mangere (CC2M) Auckland light rail project (the project) in order to provide advice to the incoming government. This includes:
 - 1.1. Working collaboratively with a number of agencies to prepare advice to the incoming government regarding the public service delivery of the project, following the Cabinet direction [CAB-20-MIN-0300 refers]
 - 1.2. Reviewing, valuing and acquiring intellectual property held by the two Respondents, so that it can be used to inform the project's next phase.
2. The briefing seeks agreement from joint Ministers to re-purpose funding from the Ministry of Transport's baseline for this purpose. The work programme is challenging and will require continued access to specialist advisors, both to deliver the advice needed and to ensure that a project could be scaled up quickly if an incoming government wants to proceed.

Background

3. On 22 June 2020, Cabinet "agreed to formally terminate the Proposals Process and revert to public service delivery; and noted that as a consequence, neither proposal will be progressed". The Ministry and the Treasury were directed to report to Ministers on optimal arrangements for public service delivery following the general election. Cabinet directed that this work should be carried out in close consultation with Auckland Transport Alignment Project (ATAP) partners and the Ministry of Housing and Urban Development (MHUD).
4. Given that closing-out the proposals process may take several months (with the Respondents controlling much of the timing) there will be an overlap between this process and our future work programme. The overlap between the processes has some implications for how we can proceed. The decision to terminate the proposals process means that:

4.1.

4.2.

4.3.

4.4.

5. Cabinet also agreed to establish a tagged contingency to enable the Ministry to acquire intellectual property from the Respondents. This provides the Ministry with sufficient assurance that it can commence discussions with NZ Infra, with joint Ministers' (Minister of Finance and Minister of Transport) approval required to complete any deal. Any intellectual property that the Government wishes to obtain from Waka Kotahi is unlikely to require funding, given its Crown Entity status. However, there will need to be a formal process for reviewing and obtaining intellectual property from Waka Kotahi, consistent with the Crown's ongoing obligations to treat both Respondents in good faith.

6. We will review and assess the intellectual property contained within the proposals so that, where appropriate, it can be used for the next phase of the project. The project delivery entity will have to develop and own an alignment and technical solution, and the intellectual property acquired could potentially support this stream of work and get it underway quickly.
7. You will receive further advice on the acquisition process in a separate paper.

We will prepare advice for an incoming government regarding how it could move forward with the project

8. The work programme agreed between the Ministry and the Treasury supports the development of advice to an incoming Government regarding the delivery of light rapid transit in Auckland.
9. The advice will enable decisions to be made by an incoming government on the next steps that could be taken with the project. For example, this may be to initiate the establishment of a delivery entity, or to direct further work if the government needs further advice on how elements of the project would be delivered, or to not proceed. We will deliver that advice in October 2020, subject to the formation of the incoming government.
10. The advice will include the following areas of work:
 - 10.1. A stocktake of analysis and information on the strategic case, outcomes and project scope. This part of the work programme will collate any intellectual property acquired from the Respondents and work completed prior to the proposals process, and will be an essential set of information for the delivery entity, so that it can use the best of what has been produced over the last 5 or so years
 - 10.2. The arrangements for the delivery of the project, including the nature of any decisions needed to enable the establishment of a delivery entity (or entities) and the roles of the key agencies
 - 10.3. Options for funding and financing the project
 - 10.4. Key policy issues and implications
 - 10.5. A future work programme, containing a clear timeframe for the feasible delivery of the project, and the nature of any decisions needed to meet that timeframe.
11. While we will provide advice based on the optimal arrangements for the project (a "first best" public delivery option), an incoming government may have differing objectives from the current government, and we will provide advice on the options available.
12. The development of this advice will be led by officials from the Ministry and the Treasury and we will work collaboratively with ATAP partners, MHUD and Kainga Ora to inform our advice. The advice will demonstrate how the perspectives of partner agencies have been reflected, and where there are any differences of view.
13. It will be important that these agency perspectives are fully understood by the incoming Government, particularly as Auckland Council and Auckland Transport face new challenges arising from COVID-19 revenue reductions.
14. The core aspects of our work programme are discussed in more detail below.

Considerations relating to the strategic case, outcomes and project scope

15. A set of outcomes for the City Centre to Mangere (CC2M) project were developed jointly by central and local government agencies in 2019. These were designed to be enduring, and are 'design and solution' agnostic. These are:
 - 15.1. **Access and integration:** improved access to opportunities through enhancing Auckland's Rapid Transit Network and integration with Auckland's current and future transport network
 - 15.2. **Urban development:** enabling quality integrated urban communities, especially around Mangere, Onehunga and Mt Roskill
 - 15.3. **Environment:** optimised environmental quality and embedded sustainable practices
 - 15.4. **Experience:** a high quality service that is attractive to users, with high levels of patronage.
16. We do not propose to revisit the project's outcomes, and we understand that Auckland Transport and Auckland Council remain comfortable with these, and with highest weightings applying to access and integration and urban development. Within this context, however, future decisions relating to the project will need to have regard to how technical scope and parameters affects the delivery of these outcomes.
17. We are not proposing to revisit the strategic case for rapid transit and light rail as outlined in ATAP 2018. ATAP was based on extensive research and consultation, and Auckland Council and Auckland Transport continue to emphasise that a rapid transit solution is required to address growing bus congestion in the CC2M area (particularly Mount Roskill to the city).
18. However, should the ATAP refresh (that is currently underway) yield new insights or signal any shift in prioritisation, we will ensure we reflect this in our work.
19. We will provide an incoming government an overview of how some key design characteristics would impact on the delivery of the project outcomes. This work will draw together the considerable work that has been completed by experts over a number of years, and the collective knowledge of local and central government agencies. This will enable the incoming government to better understand the trade-offs involved between the broad approaches that are available.
20. The delivery entity will need a clear understanding of central and local government requirements so that it can make operational decisions and trade-offs. We will work with agencies and with technical advisors so that what is provided to Ministers is at the right level. In effect the intent will be to provide an opportunity for Ministers to establish some high level requirements, while also balancing the need to give the delivery entity the flexibility it needs to develop and own the project and manage a stakeholder engagement process with community, business and mana whenua / Iwi.

Delivery entity considerations

21. Cabinet has directed that the project be delivered by a public sector entity. We will take a 'form follows function' approach to arriving at advice on entity structure and role. The questions in respect of entity form are connected to the scope and parameters of the project, the rights and powers needed by the entity, the management of risk, and how the project will be funded and financed.

22. Key issues that this part of the work programme will need to consider will include:
- 22.1. The nature of the risks in the design, delivery and operation of the project, and who is best placed to manage each risk (i.e. the allocation of risk between Crown agencies, local government agencies and the private sector). This will be a key driver in the consideration of different entity forms. Given the complexity of the project and its significant funding requirements, we anticipate that there will need to be robust governance and assurance to manage Crown risk, including a detailed approach to change management and contingency management.
 - 22.2. How incentives can be aligned between the Crown and the entity or entities responsible for project delivery. Typical Crown entity arrangements may not offer the high level of alignment of outcomes (which goes well beyond a 'design and construct' approach) that may be needed for delivery of a project like this, where a high level of integration between transport and other outcomes is sought, and delivery is complex and will inevitably require compromise along the way.
 - 22.3. The nature of relationships needed with key partner agencies, including Auckland Transport, Auckland Council, Waka Kotahi and Kainga Ora, and how to best achieve these through mechanisms such as major project governance structures.
 - 22.4. s9(2)(b)(ii)
23. The capability and capacity demands of a project of this scale and complexity are almost unprecedented in New Zealand, and no current entity has the necessary capabilities to deliver the project. All options will be considered, including building expertise within an existing entity or establishing a new one.

Funding and financing considerations

24. The Proposals process demonstrated that the project could be delivered in accordance with ATAP expectations. ATAP signals that the project should be suitable to leverage alternative funding and financing, through the provision of seed funding.
- s9(2)(b)(ii)
25. However, with COVID-19, the Crown's financial position has changed, with greater levels of debt being raised to support economic recovery and with some ongoing challenges for the National Land Transport Fund.
26. The work programme will need to consider the range of options for funding and financing in this context, and consider factors including:
- 26.1. Potential sources of funding for the project, drawing on past work on the opportunity for urban development to reduce the draw on Crown funding
 - 26.2. The nature of long term Crown borrowing that would be needed for the project

- 26.3. How funding and financing arrangements might accommodate other potential options such as private equity
- 26.4. Updated advice on the National Land Transport Fund, including revenue and expenditure scenarios
- 26.5. The extent to which this project may support a greater confidence in the infrastructure market and as an anchor project for Auckland (while recognising that construction would feasibly take another 2 to 3 years to commence)
- 26.6. The international market for financing, and the likelihood that this project could attract international financing over the next 2 to 3 years (recognising the ongoing and uncertain effects of COVID-19).

There are a number of wider policy matters that will need to be progressed

- 27. The Proposals process has revealed that current policy settings are not fit for purpose for large, nationally significant brown-fields infrastructure projects such as light rapid transit. The work programme to address these issues is extensive. The next three months provides an opportunity to get define the policy work programme and to get aspects of it underway, working with ATAP partners and MHUD. By providing advice on the policy work programme, the incoming government will also be well positioned to confirm its priorities for the policy work and to set clear direction to policy agencies – this will support accelerated delivery of the policy work, as required.
- 28. A project of this nature involves coordinated works across a number of sectors, subject to a range of regulatory and legislative regimes. The work programme will help highlight these key constraints, and inform the advice to Ministers about the steps necessary to overcome these.
- 29. Policy responses will most likely be needed to respond to the following key constraints facing large-scale infrastructure projects in New Zealand:
 - 29.1. The limited ability of central and local government agencies to take a coordinated approach to compulsory acquisition of land and to delegate these powers in appropriate circumstances
 - 29.2. The suitability of current policy and legislative settings relating to the compulsory acquisition of land to be used for urban development in association with the primary infrastructure
 - 29.3. The availability of appropriate land value capture mechanisms, including limited familiarity in New Zealand of using these tools
 - 29.4. The potential limited flexibility of existing legislative settings to enable a coordinated and certain process for accessing, moving and managing utilities during construction.
- 30. s9(2)(f)(iv)

s9(2)(f)(iv)

31. In addition to the fit for purpose issues highlighted above, a key issue for the work programme will be to assist Ministers to work through choices relating to the emphasis on, and relationship between, transport outcomes and urban development outcomes.
32. The work programme will identify best practice approaches to Transit Oriented Developments, and will particularly consider how effective partnerships could be established between the public sector delivery entity, Kainga Ora, Auckland Council and others such as Panuku. A further focus area for the policy programme will be to consider how to ensure that the roles of Auckland Transport under any public sector delivery arrangement are clear and workable. It will be important that Auckland Transport, as the network integrator, has clear roles and responsibilities vis a vis the public sector delivery entity, and that it is confident that it can build appropriate relationships with that entity.
33. Current legislative settings will need to be considered through this part of the work programme, including the Land Transport Management Act which sets out Auckland Transport's role to plan and contract for public transport in Auckland.

The acquisition and purchase of intellectual property

34. The Respondents have developed extensively researched routes and designs for the CC2M project, including proposals for service delivery. In doing so, they have received advice from internationally experienced light metro designers and experts, and have drawn off expertise and analysis conducted by New Zealand based agencies including Auckland Transport.
35. The work programme proposes to:
 - 35.1. Engage with Respondents on their intellectual property. This includes reviewing, assessing and valuing their intellectual property, including the extent to which it is likely to be valuable to the future public sector delivery entity
 - 35.2. Work with Auckland Transport, MHUD and Kainga Ora to ensure that any intellectual property acquired is likely to be relevant and usable for the project
 - 35.3. Following discussions with the Respondents, officials will brief Ministers on the findings of the intellectual property assessment, with a view to obtaining agreement to proceed with a purchase of intellectual property from NZ Infra. Waka Kotahi's intellectual property is Crown-owned and should not be subject to any cost to the Crown.
36. This part of the work programme will rely on continued use of the technical, legal and commercial expertise that has been engaged in the first part of the process. This is necessary to assess the content of the proposals and value the intellectual property, and to execute negotiations. We expect that NZ Infra would approach the negotiations from a strongly commercial perspective. As noted above, discussions with Waka Kotahi will need to be approached in a formal way to manage the Crown's ongoing good faith obligations.

¹ The Transport and Works Act 1992 (UK) provides for the making of an order to authorise a new railway or tramway scheme in England and Wales. This order allows for the transfer of relevant powers to the promoter of the infrastructure scheme for that particular scheme (such as compulsory acquisition of land or the power to close streets) through the amendment, repeal or revocation of some statutory provisions of local application.

How we propose to work with other agencies

37. We will shortly initiate discussions with ATAP agencies, MHUD and Kainga Ora to identify how they would like to engage in the next phase of the project. There has been considerable work by these agencies on Auckland light rail over recent years and our preference is to use this process to bring together all the analysis into one place. We will be inviting all relevant agencies to be involved in a series of workshops to generate and test content for the advice that the Treasury and the Ministry is preparing.
38. While the advice to the incoming government will be the responsibility of the Ministry and the Treasury to deliver, we would like it to present a collective view of the relevant agencies, or at least be clear on where there are differing views and why.
39. We envisage that the existing ATAP governance mechanisms can be applied to the project, with Auckland Light Rapid Transit becoming one of ATAP's regular agenda items. This will ensure that there is Chief Executive engagement, supported by working group arrangements that will be agreed between agencies.
40. While we have not yet engaged with agencies on the scope of the work programme, we have starting testing their ability to provide team members over the next ten weeks and we have had a positive reception. We have not yet had requests for funding from the agencies to support their involvement.

Resourcing for the next phase

41. The Ministry and the Treasury will need to access technical, legal and commercial advice. It is also a priority to retain the project knowledge that sits with key advisors who have been exposed to the ideas in both proposals, to provide a way forward for the delivery entity that is free from obligations to the proposals process; and to have the ability to scale up quickly if a new government wishes to proceed with the project.
42. The Ministry is in discussions with Waka Kotahi on the prospect of using the remaining funding that Waka Kotahi has agreed to provide to support the Ministry's close-out work on the proposals process, including the opportunity to apply this remainder towards the IP discussions. However, additional funding will be needed for external support for the forward work programme. In particular, external support is needed in respect of:
 - 42.1. Technical and engineering support to inform the collation of analysis on project outcomes and scope, and delivery approach
 - 42.2. Legal support to complement the analysis above. In addition, this support would also be focused on assisting the Ministry and the Treasury with legal issues around delivery approach and entity form. In scope this would be similar to the legal work that helped establish the corporate structure for City Rail Link Limited
 - 42.3. Commercial support to complement the analysis above and also to assist the Ministry and the Treasury on funding and financing matters
 - 42.4. Resource to support other government and potentially local government agencies to undertake policy work on an 'as needed' basis
 - 42.5. Senior support from industry experts to provide oversight and challenge to the advice before it is presented to the incoming government.

43. In order to maintain continuity and to get the work underway as quickly as possible, the Ministry and the Treasury intend, where possible, to retain the services of contractors and firms that assisted the Ministry throughout the proposals process. The Ministry anticipates that approximately \$1 million of funding will be required to progress the work programme through to the advice provided to the incoming government and into the next phase, should the incoming government decide to proceed.
44. The Ministry's baseline funding is under significant pressure and a significant portion of the funding is for specific initiatives and is treated as ring-fenced (e.g. search and rescue activities, New Zealand Upgrade Programme and the Provincial Growth Fund). There is very little discretionary funding available to fund the proposed work programme and it would not be feasible for the Ministry to reprioritise its entire work programme given the majority of these are transport priorities for the Government.

We recommend repurposing funding allocated to the Green Transport Card

45. The Ministry has \$4.64 million in its 2019/20 baseline allocated to the establishment of the Green Transport Card. Given the likelihood that the Green Transport Card will not proceed within this Parliamentary term, the Minister of Transport has previously agreed with the Ministry's recommendation to repurpose this funding to support the exclusive negotiation phase of the Auckland Light Rail project [OC200292 refers]. In June 2020, the Ministers of Transport and Finance agreed to an in-principle expense transfer for \$4.640 million from 2019/20 to 2020/21 for establishing a Green Transport Card within the Ministry's Policy Advice appropriation [OC200442 refers].
46. Given Cabinet's decision to terminate the proposals process, this funding is no longer needed for the exclusive negotiation process. We recommend that \$1 million of the \$4.64 million Green Transport Card funding is repurposed to support the proposed work programme for the Auckland Light Rail project.
47. If no additional funding is secured, the work programme detailed above is unlikely able to be delivered within the proposed scope and timeframes, and is likely to result in heavily scaled back advice being provided to the incoming government on approaches to delivering the project.
48. We are seeking early confirmation of \$1.000 million of this in-principle expense transfer. In-principle expense transfers are usually confirmed through the October 2020 Baseline Update once 2019/20 year-end results are confirmed. The Ministry is confident that none of the Green Transport Card funding was spent in 2019/20 so the \$1.000 million being sought for early confirmation is available.

Recommendations

49. The recommendations are that you:

(a) **Note** the proposed work programme and discuss with officials.

Yes/No

(b) **Note** that the Minister of Transport and Minister of Finance have previously approved an in-principle expense transfer of up to \$4.640 million from 2019/20 to 2020/21 for establishing a Green Transport Card.

- (c) **Agree** to an early confirmation of \$1.000 million of the in-principle expense transfer for establishing a Green TransportCard.

Yes/No

- (d) **Approve** the following changes to appropriations to provide for the decision in recommendation (c) above, with no impact on the operating balance across the forecast period:

	\$m - increase/(decrease)				
Vote Transport Minister of Transport	2020/21	2021/22	2022/23	2023/24	2024/25 and Out years
Multi-Category Expenses and Capital Expenditure: Policy Advice and Related Outputs MCA					
Departmental Output Expenses : Policy Advice	1.000	-	-	-	-

Yes/No

- (e) **Note** that the Ministry of Transport expects \$1 000 million of funding is required to implement the next stage of the Auckland Light Rail project.
- (f) **Agree** to reallocate \$1.000 million from the Green Transport Card funding to support the Auckland Light Rail project.

Yes/No

- (g) **Approve** the following fiscally neutral adjustment to provide for recommendation (f), with no impact on the operating balance and net core Crown debt:

	\$m - increase/(decrease)				
Vote Transport Minister of Transport	2020/21	2021/22	2022/23	2023/24	2024/25 and Out years
Multi-Category Expenses and Capital Expenditure: Policy Advice and Related Outputs MCA					
Departmental Output Expenses: Policy Advice	(1.000)	-	-	-	-
Departmental Output Expense: Transport - Policy advice, ministerial servicing, governance, and other functions	1.000	-	-	-	-

Yes/No

- (h) **Agree** that the proposed change to appropriations for 2020/21 above be included in the 2020/21 Supplementary Estimates and that, in the interim, the increase be met from Imprest Supply.

Yes/No


Bryn Gandy
Deputy Chief Executive, System Strategy
and Investment


David Taylor
Manager, National Infrastructure Unit, The
Treasury

MINISTER OF TRANSPORT'S SIGNATURE:

DATE:

MINISTER OF FINANCE'S SIGNATURE:

DATE: