

The Treasury

Project Korimako - Release of advice

December 2022

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- [37] 9(2)(i) - to enable the Crown to carry out commercial activities without disadvantage or prejudice
- [38] 9(2)(j) - to enable the Crown to negotiate without disadvantage or prejudice
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Treasury Report: Project Korimako - Engagements and Next Steps

Date:	30 September 2021	Report No:	T2021/1832
		File Number:	SE-2-12-4-2-3

Action sought

	Action sought	Deadline
Minister of Finance (Hon Grant Robertson)	Indicate if you would like to discuss this report with officials Agree to officials conducting further discussions with NZSF to refine its ownership proposal	13 October 2021
Associate Minister of Finance (Hon Dr Megan Woods)	Note the contents of this report	None
Associate Minister of Finance (Hon David Parker)	Note the contents of this report	None

Contact for telephone discussion (if required)

Name	Position	Telephone	1st Contact	
David Stanley	Principal Advisor, Commercial Performance	[39]	[35]	✓
Shelley Hollingsworth	Manager, Commercial Performance			

Minister's Office actions

Return the signed report to Treasury.

Note any feedback on the quality of the report

Enclosure: No

Treasury Report: Project Korimako - Engagements and Next Steps

Executive Summary

At the Minister of Finance's direction following our 3 June 2021 advice, we have now held discussions with the Crown Financial Institution (CFI) shareholders of Kiwi Group Holdings (KGH), namely the New Zealand Superannuation Fund (NZSF) and the Accident Compensation Corporation (ACC), [33], [37], [38]

regarding KGH ownership [T2021/1036 refers].¹ This report provides you with the insights we gained from our engagements and proposes a way forward to revising the ownership arrangements for KGH in a manner that achieves the Government's objectives.

Feedback from CFI Shareholders

[25], [26]

NZSF considers that there is 'unlocked potential' in Kiwibank (the major operating subsidiary of KGH) but that it needs a period of focussed shareholder control to be successful.

[25] and [33]

[25]

[33], [37], [38]

¹ Conversations with each party are undertaken in confidence and their content is unknown by other parties.
[25]

[33], [37], [38]

A Proposed Way Forward

Based on the views of the parties we engaged with and the Government's previously stated objectives for Kiwibank, there is a potential deal that would meet the objectives of everyone involved. We consider there to be merit in an ownership arrangement where NZSF has majority control of KGH with the Crown [33], [37], [38]

The benefits of this ownership structure would be that it would:

- provide the supportive, aligned, and capable ownership and governance needed to support Kiwibank during its transformation period, [25]
- allow ACC and NZ Post to exit,
- [33], [37], [38]
- [25], [37]

Based on our recent discussions with NZSF we do not consider that the Crown having a direct shareholding in KGH during Kiwibank's transition phase will further its objectives beyond those it can achieve through other means, however, the inclusion of a direct Crown stake, [33], [37], [38] will be further explored with NZSF and contemplated within this structure. Regardless, any new ownership arrangement would also include mechanisms to meet your requirement for KGH to remain New Zealand owned. This was enabled through the previous documentation via a lock-up period and first rights of refusal for the Crown to purchase shares before they were offered to any third parties. Similar arrangements could be adopted in the future and would not need to be dependent on the Crown having a direct holding

We would like to check that you are comfortable with officials working with KGH shareholders to further develop a KGH ownership proposal as described above

We propose that officials conduct further discussions with NZSF to indicate the high-level requirements that amended ownership arrangements for KGH would need to meet to satisfy the Government's objectives and requesting that NZSF submits an amended proposal that meets those requirements. [33], [37], [38]

Crown requirements such as maintaining New Zealand ownership.

Following the discussions with NZSF, we would expect NZSF to provide an amended proposal that responded to the Government's requirements, likely including alternative options for you to consider. Specifically, it may include options for NZSF to own a majority stake greater or less than 75% and the different terms under which each shareholding level would be satisfactory to it. On receipt of such a proposal we would report to you on the relative merits of the options for you to identify a preferred approach which could then lead to formal negotiations with the current shareholders of KGH.

Recommended Action

We recommend that you:

- a **indicate** if you would like to meet with officials to discuss this report

Yes/no.

Minister of Finance

- b **agree** to officials undertaking further discussions with NZSF with a view to NZSF submitting a revised ownership proposal that is consistent with the Government's views on any new ownership arrangements as follows:

- i The Government sees merit in NZSF's proposal to be an active majority shareholder in KGH, [33] and wishes to have the proposal further refined.

- ii [33], [37], [38]

- iii The Government considers it important that any new ownership arrangement for KGH provides the Crown with mechanisms that can ensure that KGH remains New Zealand owned.

Agree/disagree.

Minister of Finance

Shelley Hollingsworth
Manager, Commercial Performance

Hon Grant Robertson
Minister of Finance

Hon Dr Megan Woods
Associate Minister of Finance

Hon David Parker
Associate Minister of Finance

Treasury Report: Project Korimako - Engagements and Next Steps

Purpose of Report

1. This report provides you with the key insights we gained from our engagements with the two Crown Financial Institution (CFI) shareholders of Kiwi Group Holdings (KGH), [33], [37], [38]

Based on these insights, this report assesses the shareholding arrangements most likely to be aligned with the Government's objectives for KGH and the transformation strategy being implemented by KGH's major operating subsidiary Kiwibank.

2. This report also proposes some principles under which, if you agree, Treasury officials would hold further discussions with the New Zealand Superannuation Fund (NZSF) and request that it submit a refined proposal that meets the Government's objectives.

Engagements Since Previous Advice

[33], [37], [38]

3. You agreed that we should engage [33], [37], [38] regarding ownership interests in KGH [T2021/1036 *refers*]. The discussions [33], [37], [38] were not formal negotiations, and all the conversations were on a confidential basis and we made this clear to those we engaged with.

4. [33]

5. Our engagement with ACC was focused on understanding its position, as it was the only shareholder that had not yet clearly stated its intentions regarding whether it would seek to further invest in or retain its existing 22% interest in KGH, or to exit following the five year lock-up period (which ends on 31 October 2021).

6. [33], [37], [38]

- 7.

13. [37]

[25], [37]

[33], [37], [38]

16. [33], [37], [38]

17.

[33], [37], [38]

18. [33], [37], [38]

19. [33], [37], [38]

[33], [37], [38]

20. [33], [37], [38]

21.

22.

[33], [37], [38]

23. [33], [37], [38]

24.

⁴ Environmental, social and governance (ESG) criteria are a set of standards relating to a firm's approach to how the business is overseen and operated, its approach to social matters (including a stakeholders' interests approach) and its effect on the environment. Investors are increasingly applying ESG criteria as non-financial factors to be considered in their investment decision-making processes.

25. [33], [37], [38]

26.

[33], [37], [38]

27. [33], [37], [38]

[33], [37], [38]

28. [33], [37], [38]

Proposed Ownership Arrangements for Further Development

29. We have considered the views of the parties we engaged with, the current commercial position of KGH and Kiwibank, its principle operating business, how this could be improved, and the relative strengths and weaknesses of NZSF or the Crown as the majority shareholder in KGH. Based on these considerations, there is an ownership arrangement option emerging that best enables the stated objectives of the Government and the imperatives of KGH.

30. The three main components of this are:

- ***NZSF having a controlling interest for an initial period*** – this recognises the need for focused and capable ownership that has the level of control to drive the stabilisation and transformation of Kiwibank.

- [33], [37], [38]

- ***The Crown may still seek a direct holding in this structure*** - we do not consider that the Crown having a direct shareholding in KGH during Kiwibank's transition phase will further its objectives beyond those it can achieve through other means, however, the inclusion of a direct Crown stake, [33], [37], [38] will be further explored with NZSF and contemplated within this structure.

[33], [37], [38]

31. Exact preferred shareholding levels can be refined as the overall arrangement is further developed. We know that NZSF will prefer an at least 75% shareholding [25], [37]

32. [33], [37], [38]

33. We discuss the merits of these potential ownership arrangements and their consistency with the Government's objectives for KGH below.

The proposed ownership arrangements are consistent with your objectives for KGH as NZSF is best placed to be the majority shareholder driving Kiwibank's impact on the financial services market

34. You have stated the Government's objectives for KGH as being:

- to remain New Zealand owned (at least partially through the Crown),
- to operate in a commercially sustainable manner,
- through Kiwibank, to be a disrupter bank, particularly in SME markets,
- for Kiwibank to improve accessibility to banking services for New Zealanders, and
- [25]

35. Most of these objectives could be achieved under arrangements involving either full (or majority) Crown ownership, or full (or majority) NZSF ownership. However, for Kiwibank to be both commercially successful and a disruptor bank, it needs to undergo significant change over the next few years [34], [37]

[25]

to become a significant well-capitalised disrupter bank:

- through increased lending to its core retail market [25]
 - with improved accessibility for customers through a wide array of avenues, and
 - supported by a new market-leading technology platform for improved internal processes and for customers.
36. This increased ambition, combined with the Te Ara Hou transformation and the need to meet increasingly demanding RBNZ requirements (as discussed in paragraph 10), do not imply a steady-state business that can be passively monitored in a hands-off manner. It requires a commercially strong and focused owner which understands and is prepared to take on the high (but managed) risk associated with the bank's transformation. This owner needs to actively engage with the company and make timely commercial decisions, including for the provision of regulatory, growth and risk capital. We consider NZSF is well positioned to fulfil this role as the majority shareholder. You could consider NZSF as the Crown's [33], [37], [38] steward overseeing the transformation of Kiwibank over the next few years [33], [37], [38]
37. We propose exploring with NZSF options which include a direct Crown ownership interest in KGH both in the near term or (if the Crown decides not to participate immediately) once the transformation is complete. We expect any arrangement will provide the Crown a similar right of refusal over any shares before they can be offered to third parties to that in the current Crown Deed (a right that exists whether or not the Crown owns shares in KGH). Any mechanisms by which the Crown [33], [37], [38] more shares in the future can be built into the new or updated agreements that will need to be put in place [33], [37], [38] appetite to invest in KGH may change over time as the risk-reward profile of the investment changes. Near-term decisions on investments would not preclude a future rebalancing of holdings between shareholders.
38. The alternative to NZSF having control is for the Crown to own 100% or to have majority control [33], [37], [38] This simply recognises NZSF's view that without majority control it would wish to exit its investment, ACC's intention to exit [25], and NZ Post's long-stated preference to exit.
39. [33], [34], [37], [38]
40. We see little merit in NZ Post or ACC remaining invested in KGH. They would both prefer to redirect their focus and any available capital elsewhere.

The Crown's [25] ability to maintain objectives can be enabled even with a minority shareholding

41. [33], [37], [38]

[33], [37], [38]

Under the current KGH shareholder agreement a shareholding between 20% - 39% provides the ability to appoint one director.

42. As part of establishing new KGH ownership arrangements, the Crown could also act to ensure its requirement that KGH remains New Zealand owned. This was enabled through the previous documentation via a lock-up period and first rights of refusal for the Crown to purchase shares before they were offered to any third parties. Similar arrangements could be adopted in the future and would not need to be dependent on the Crown having an initial direct holding.

[33], [37], [38]

43. [33], [37], [38]

44.

[33]

45. [33]

Next Steps

46. We propose that officials conduct further discussions with NZSF to indicate the high-level requirements that a refined proposal would need to meet to satisfy the Government's objectives and requesting that NZSF submits an amended proposal on that basis. We would indicate that the Government sees merit in NZSF's proposal to take a majority interest in KGH and wishes to have the proposal further refined. Specific features to be discussed [33], [37], [38] and Crown requirements such as maintaining New Zealand ownership. We would like you to indicate if you are comfortable with us proceeding on this basis.
47. It would be beneficial for all parties involved if the Treasury was able to communicate the Crown's position by the end of **October 2021** (the end of the lock-up period under the current KGH arrangements).

48. Following the discussions with NZSF, we would expect NZSF to provide an amended proposal that responded to the Government's requirements. The proposal would likely include options for you to consider. Specifically, it may include options for NZSF to own a majority stake greater or less than 75% and the different terms under which each shareholding level would be satisfactory to it. On receipt of such a proposal we would report to you on the costs and benefits of the options and recommend an approach. You could then instruct us to undertake formal negotiations with the current shareholders of KGH. You may also wish to take a paper to Cabinet at that point to seek Cabinet's endorsement of the proposed approach.
49. Formal negotiations would initiate several processes, including the requirement for external legal advice on the new arrangements and due diligence and transaction advice from external specialists, possibly including investment banking expertise. There would be funding implications from these processes.
50. [33], [37], [38]
51. We note that negotiations with NZ Post regarding what proportion of proceeds is retained following its disposal of KGH is a secondary question, once the preferred ownership arrangement is established. In preparation for such negotiations, we are establishing a view on NZ Post's likely optimal capital structure through financial modelling and engaging with the company regarding its long-term parcel network investment plans. While we understand from the Chair that it is likely NZ Post will seek to retain some of the proceeds from the disposal of its 53% shareholding in KGH [25], [33] we are working towards forming an independent view on NZ Post's likely capital needs ahead of any formal discussions.