

The Treasury

Project Korimako - Release of advice

December 2022

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- [35] 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
- [36] 9(2)(h) - to maintain legal professional privilege
- [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
- [39] 9(2)(k) - to prevent the disclosure of official information for improper gain or improper advantage

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Treasury Report: Project Korimako - Final Project Documentation

Date:	11 August 2022	Report No:	T2022/1663
		File Number:	SE-1-3-22-2

Action sought

	Action sought	Deadline
Minister of Finance (Hon Grant Robertson) Associate Minister of Finance (Hon David Parker)	<p>Agree to enter into the Korimako Sale and Purchase Agreement (SPA) on the terms outlined in this report</p> <p>Agree (Minister of Finance only) to give a guarantee/indemnity to the vendors under which the Crown would be jointly and severally liable for the obligations of Kiwi Group Capital Limited (KGC) under the SPA</p> <p>Note that final execution versions of the SPA and supporting documents will be provided for signature on 18 August 2022</p>	17 August 2022

Contact for telephone discussion (if required)

Name	Position	Telephone	1st Contact
Dominic Milichich	Principal Advisor, Project Korimako	N/A [35]	
David Stanley	Principal Advisor, Commercial and Institutional Performance	[39]	✓

Minister's Office actions (if required)

Return the signed report to Treasury.

Note any feedback on the quality of the report

Enclosure:

- Appendix A: Key terms of SPA
- Appendix B: Scope of due diligence
- Appendix C: Due diligence findings
- Appendix D: Warranties
- Appendix E: Project Korimako valuation considerations

Treasury Report: Project Korimako - Final Project Documentation

Executive Summary

This report seeks your agreement to enter into the Korimako Sale and Purchase Agreement (SPA) for the purchase of all of the shares in Kiwi Group Holdings Limited (KGH) on the terms outlined in this report.

To support your decision-making, this report provides information covering the material features of the SPA, the guarantee/indemnity to the KGH vendors implicit in the SPA (as the Crown would be jointly and severally liable for the SPA obligations of Kiwi Group Capital Limited (KGC)), the scope and results of the due diligence process undertaken with the assistance of external advisers, the approach on SPA warranties, the basis for the Crown's offer price and a scenario analysis for Kiwibank which has been undertaken by EY to better inform the Crown about the predominant asset within KGH.

Treasury recommends that you agree to enter into the SPA for the Crown to purchase 100% of KGH. We consider this to be a satisfactory commercial arrangement to meet the Government's policy goals with respect to KGH and Kiwibank. Specifically, we note that:

- a transaction agreement was achieved through a robust commercial negotiation process over several months with each existing KGH shareholder (on a bilateral basis until preparation of a final joint SPA) in which the Crown and KGH shareholders utilised external advisors
- b the price of the purchase is at a level that was originally proposed to KGH shareholders by the Crown after valuation perspectives were provided by, and we consulted with, our commercial advisors. [25], [33], [37]
- c the SPA provides the Crown with an appropriate level of risk mitigation given the transaction is occurring within the wider Crown and the passive involvement of the KGH shareholders in the underlying operational businesses
- d the Crown guarantee/indemnity provided through becoming jointly and severally liable for KGC's SPA obligations is expedient in the public interest as there are no viable alternatives and it poses no increased risk for the Crown, and
- e the risks identified by the due diligence process are consistent with ownership of an entity of this nature and/or were already known and incorporated into the pricing of the Crown's offer for KGH.

Final executable versions of the Korimako transaction documents will be provided for you to sign on 18 August 2022.

Recommended Action

We recommend that you:

- a **agree** to enter into the Korimako Sale and Purchase Agreement on the terms outlined in this report

Agree/disagree
Minister of Finance

Agree/disagree
Associate Minister of Finance

- b **agree** (Minister of Finance only) that it appears to you to be expedient in the public interest to enter into liability obligations in favour of the vendors on the terms set out in the SPA, and agree to enter into these liability obligations under section 65ZD of the Public Finance Act 1989

Agree/disagree.
Minister of Finance

- c **note** that final execution versions of the SPA and supporting documents will be provided for signature on 18 August 2022.

David Stanley
Principal Advisor, Commercial and Institutional Performance

Hon Grant Robertson
Minister of Finance

Hon David Parker
Associate Minister of Finance

Treasury Report: Project Korimako - Final Project Documentation

Purpose of report

1. This report seeks your agreement to enter into the Korimako Sale and Purchase Agreement (SPA) for the purchase of all of the shares in Kiwi Group Holdings Limited (KGH) on the terms outlined in this report.
2. To support your decision-making, this report will provide information covering:
 - the material features of the SPA
 - the guarantee/indemnity to the KGH vendors implicit in the SPA (as the Crown would be jointly and severally liable for the SPA obligations of Kiwi Group Capital Limited (KGC))¹
 - the scope and results of the due diligence process undertaken with the assistance of external advisers
 - the approach on SPA warranties, and
 - the basis for the Crown's offer price (and a scenario analysis for Kiwibank Limited (Kiwibank) which has been undertaken by EY to better inform the Crown about the predominant asset within KGH).

The Sale and Purchase Agreement

3. The SPA is the contract between the Crown (acting by and through the Minister of Finance and Minister for State Owned Enterprises) and the vendors specifying all aspects of the transaction. Agreement has been reached with all three KGH shareholders for the Crown to purchase their KGH shareholdings.
4. The key terms of the SPA are summarised in Appendix A. Particularly material features of the SPA are that:
 - a the Crown purchases 100% of KGH shares [25], [33], [38]
 - b the purchase price will be adjusted up by the amount which the final net sale proceeds of Kiwi Wealth Management Limited (Kiwi Wealth) [25], [33], [37], [38] ²
 - c the Crown may transfer its rights under the SPA to a Crown Entity (intended to be KGC) but remains jointly and severally liable for its performance under the SPA (giving rise to the guarantee/indemnity discussed at paragraphs 5 to 13 below)
 - d the vendors provide to the Crown general warranties in respect of the areas of focus identified by the Project Korimako team through the confirmatory due diligence exercise. However, except where the warranties relate to matters within the full knowledge or control of a Vendor, the warranties are framed by reference to the Vendor's knowledge. The approach to warranties is discussed further at Appendix D.

¹ We note that the guarantee/indemnity implicit in the SPA referred to above, [25]

² We note that the Kiwi Wealth sale is subject to the meeting of certain conditions including Overseas Investment Office approval. [25]

SPA joint and several liability provisions being a guarantee / indemnity

5. The SPA allows the Crown to transfer the Crown's rights and obligations under the SPA to KGC (or another Minister or Crown party). This can take place:
 - a prior to completion of the KGH share transfer, by way of the Crown transferring its rights and obligations to KGC as nominated purchaser under clause 2 (Nomination); or
 - b after completion of the KGH share transfer, by way of the Crown transferring its rights and obligations to KGC under clause 16.5 (Assignment).
6. Under both clauses, following the transfer the Crown will be jointly and severally liable with KGC (or other applicable party) for the performance of the liabilities, obligations, and undertakings of the Crown and KGC under the SPA (the Liability Obligations).
7. This report seeks the Minister of Finance's agreement to enter into the Liability Obligations, as we consider that they may constitute a guarantee and/or an indemnity in favour of the vendors.
8. Section 65ZD of the Public Finance Act 1989 (the Act) empowers the Minister of Finance, as the Minister responsible for the administration of the Act, to give a guarantee or indemnity to a person, organisation or government if it appears to him to be 'necessary or expedient in the public interest' to do so, and to give such a guarantee or indemnity on any terms and conditions that he thinks fit.
9. In brief, the Treasury considers that in the circumstances giving the requested Liability Obligations on the terms set out in the SPA satisfies the "public interest test" in section 65ZD of the PFA.
10. Entry into the Liability Obligations will allow the Crown to enter into the SPA as purchaser in the first instance and retain the power to nominate KGC as alternative purchaser in accordance with the Crown's preferred ownership structure. It is expedient on the basis that the vendors would not reasonably accept KGC (which would then be a newly incorporated company with no assets other than its initial capital injection from the Crown) as a sufficiently creditworthy purchaser of their KGH shares. The Liability Obligations do not give rise to any new or additional risk for the wider Crown; they provide only that the Crown is jointly and severally liable for KGC's obligations under the SPA. In addition, the Liability Obligations are highly unlikely to be called upon, given that KGC is to be capitalised with sufficient funds to complete the purchase of the KGH shares.
11. In light of the above, officials consider that:
 - a there is a public interest in entering into the Liability Obligations in favour of the vendors on the terms set out in the SPA
 - b the benefits of the Liability Obligations appear to outweigh the risks, and
 - c there are no viable alternatives to the Liability Obligations when it comes to enabling KGC to take a transfer of the Crown's rights and obligations under the SPA.
12. Accordingly, officials are of the view that the Liability Obligations are expedient in the public interest.
13. [34] the Treasury does not consider that the contingent liability exceeds \$10 million and so a statement to the House of Representatives under section 65ZD(3) of the PFA is not required.

Due diligence

14. Due diligence has now been completed. Financial and legal due diligence was provided by EY and Minter Ellison Rudd Watts (Minters) respectively, and Marsh undertook an insurance review. The due diligence process was designed to provide the Crown with a broad confirmatory review of the KGH group's business and operations, while managing the costs and disruption the process imposed on the KGH group, taking the timeframe into account and recognising that all parties involved in the transaction are part of the wider Crown. The scope of due diligence is outlined further at Appendix B.
15. The due diligence reports did not reveal any issues that Treasury considers to be sufficiently significant to affect proceeding with Project Korimako, [25], [33], [37]

Risks around completion of the Kiwi Wealth sale by KGH (Project Weka)

16. KGH is currently in the final stages of divesting Kiwi Wealth with a SPA expected to be signed in mid-August 2022. KGH advises that it will send Ministers a "no surprises" note immediately after the SPA is signed. Project Weka was well advanced when Korimako began, and the high confidence of all parties that Kiwi Wealth would be successfully sold has meant that it has not featured in the Korimako process [33], [37]
17. We note that the agreement will be subject to several conditions, including obtaining approval from the Overseas Investment Office (OIO). The preferred bidder is Fisher Funds Management, a group majority owned by Toi Foundation (formerly named the TSB Community Trust) and 34% by TA Associates, an investment group based overseas. There is a risk that OIO approval is not forthcoming, but we note that there are a number of overseas-owned long-term savings service providers operating in New Zealand, whereas this purchaser is majority New Zealand-owned and already manages some of the country's largest managed funds.
18. We note that in the unlikely event that the Kiwi Wealth process does not complete there is a residual risk that the Crown will retain ownership of the business as part of KGH. We did not consider it prudent to expend public money on due diligence on such a low risk event, and we considered that the intensely contested nature of the Kiwi Wealth process would provide appropriate demonstration of value and risk should the Crown end up as owner. [25]

[33], [37]

19. [25], [33], [37]

Valuation considerations relating to the Project Korimako transaction

20. The Crown set its initial proposal valuation based on an enterprise value for KGH of \$2,120 million after valuation perspectives were provided by, and we consulted with, our commercial advisor Goldman Sachs. [25], [33], [38]
21. [25], [33], [38]
22. The Treasury instructed EY to provide a valuation scenarios analysis as part of an addendum to the red flags due diligence report. The scenarios assess the potential impact on the value of Kiwibank from changes to various value driver assumptions for Kiwibank – many of which had been identified through EY’s due diligence process and/or by the Treasury.
23. [25], [33], [37]

Treasury’s view

24. Treasury recommends that you agree to enter into the SPA for the Crown to purchase 100% of KGH. We consider this to be a satisfactory commercial arrangement to meet the Government’s policy goals with respect to KGH and Kiwibank. Specifically, we note that:
- a the price of the purchase is at a level that was originally proposed to KGH shareholders by the Crown after valuation perspectives were provided by, and we consulted with, our commercial advisor. [25], [33], [37]
 - b the SPA provides the Crown with an appropriate level of risk mitigation given the transaction is occurring within the wider Crown and the passive involvement of the KGH shareholders in the underlying operational businesses
 - c the Crown guarantee/indemnity provided through becoming jointly and severally liable for KGC’s SPA obligations is expedient in the public interest as there are no viable alternatives and it poses no increased risk for the Crown, and
 - d the risks identified by the due diligence process are consistent with ownership of an entity of this nature and/or were already known and incorporated into the pricing of the Crown’s offer for KGH.

Next Steps

SPA execution

25. At the time of writing this report we are finalising the SPA and do not expect anything untoward or new to come from this or the vendor verification process and will confirm whether that is the case when we send through the final version for signature.
26. Assuming you agree to enter into the SPA, officials will prepare executable copies of the SPA and other related documents and provide them to you for signing.
27. The key dates over the next two weeks are listed below.

Finalisation of the SPA	5 pm, 16 August
Ministers signing the SPA and other related documents	18 August (after Kiwibank profit announcement), or 19 August
Public announcement	22 August

28. Ministers' execution of the suite of documents is scheduled for 18 August 2022. These include:
 - SPA
 - Delegation instrument to the Secretary to the Treasury in relation to making payments, and taking other ancillary actions, in relation to the SPA
 - (Minister of Finance only) Deed of Transfer, Deed of Indemnity and delegation instrument in relation to the NZ Post Deed Poll Guarantee. The Minister of Finance has already agreed to enter into these documents [T2022/1334 refers].
 - (Minister of Finance only) Crown Deed Termination Deed. This document provides that the Crown Deed (applicable in respect of the existing KGH shareholding) will terminate upon completion of the Crown's purchase of KGH.

These documents will be provided to you on 18 August and we note that the SPA will be entered into by the Crown acting through the Minister of Finance and the Minister of State Owned Enterprises (with Hon David Parker acting in that capacity).

Regulatory approvals

29. Completion of the Project Korimako transaction is subject to approval by the bank regulator, the Reserve Bank of New Zealand (RBNZ), as it involves a change in a significant interest in Kiwibank, a New Zealand registered bank.
30. Together with Kiwibank, we are in the process of preparing the Crown and KGC's application to the regulator. The approval process is expected to take up to 3 months. The regulator has indicated its comfort with the financial strength of the Crown as owner, but it will need to work through governance arrangements and satisfy itself of the bank's continued independence. We expect that successful completion of the application process is likely to require more detail on governance arrangements, particularly appointments to the board of KGC.
31. We intend to submit the Crown application as soon as practicable after the signing of the SPA and will provide the RBNZ with further information relating to governance arrangements once we have Negotiating Ministers' confirmation of a candidate list. We propose to report to you shortly with more detail on this matter.

Appendix A: Key terms of SPA

[25], [37]

[25], [37]

[25], [37]

[25], [37]

Appendix B: Scope of due diligence

1. The due diligence process undertaken by the Crown in Project Korimako was intended to be confirmatory in nature, and a means to reduce the information asymmetry the Crown has previously had vis-à-vis the vendors and KGH and its subsidiaries.
2. To enable timely completion of the due diligence process, we requested the due diligence advisors take a pragmatic approach and target critical information and material issues. In effect, we have asked the due diligence advisors to undertake a broad confirmatory review focused on accessing information that group companies have readily to hand, and only seeking new information where necessary. This has been reflected in the scope of work undertaken by EY and Minters. Following legal review, a high level “fit for purpose” review of Kiwibank’s insurances was also undertaken.
3. Treasury’s broad confirmatory due diligence approach is consistent with:
 - a. the extensive regulatory and reporting requirements to which Kiwibank is already subject as a registered bank, noting the high level of scrutiny applied by Reserve Bank of New Zealand (RBNZ), Financial Markets Authority (FMA), Office of the Auditor General (OAG), Commerce Commission, and NZX
 - b. the Crown and other involved parties’ awareness of distraction risk for the subject entities, particularly the bank while it is undertaking an intensive transformation programme
 - c. the very limited number of Kiwibank executives that have been aware of the Korimako process, as a means to reduce the risk of information leaks
 - d. timeframe, and
 - e. recognition that all the parties involved in the transaction are part of the wider Crown and the Crown will continue to have a 100% ultimate interest in the underlying businesses in which ownership is being transferred, meaning that no new financial risk is being brought into the wider Crown as part of this transaction.
4. The due diligence has primarily focused on Kiwibank, with both the New Zealand Home Loan Company Limited (NZHL) and KGH receiving due diligence attention relative to their size and value (in terms of operational activities).
5. As Kiwi Insurance Limited has already been sold, it is excluded from scope other than examining any material obligations resulting from the sale. Kiwi Wealth is also excluded from the scope of due diligence given it is intended to be sold shortly.
6. Considering the broad confirmatory approach above, we agreed the scope and ways of working with the due diligence advisors. Following the completion of KGH and Kiwibank internal due diligence mobilisation processes, the actual due diligence commenced on 16 June 2022 with opening of the Project Korimako virtual data room, which initially included Board papers and key documents. Further, management meetings between advisors and the key Kiwibank/NZHL personnel were set up and written questions and answers were submitted via the data room. The process lasted six weeks, including management interviews.

Appendix C: Due diligence findings

[25], [33], [37]

[25], [33], [37]

[25], [33], [37]

[25], [33], [37]

[25], [33], [37]

Appendix D: Warranties

[38]

[25], [33], [37]

[25], [33], [37]

[25], [33], [37]