



## COVERSHEET

<b>Minister</b>	Hon Stuart Nash	<b>Portfolio</b>	Economic Regional Development
<b>Title of Cabinet paper</b>	Provincial Growth Fund: Transitioning Provincial Growth Fund Limited to an active company.	<b>Date to be published</b>	30 September 2021

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### Information redacted

**YES / NO** (please select)

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## **IN CONFIDENCE**

Office of the Minister of Finance  
Office of the Minister for Regional Economic Development

Chair  
Cabinet Economic Development Committee

## **Provincial Growth Fund: Transitioning Provincial Growth Fund Limited to an active company**

### **Proposal**

- 1 This paper seeks approval to transition the Provincial Growth Fund Limited (PGFL) from a passive holding company to an active company.

### **Executive Summary**

- 2 Cabinet agreed to establish PGFL as a Schedule 4A asset holding company that holds loan and equity investments made through the Provincial Growth Fund (PGF). PGFL has outsourced the management and administration functions associated with these investments through a management agreement with the Provincial Development Unit (PDU). PGFL is now an established and fully functional company that holds investments.
- 3 PGFL was initially established as a passive holding company with a limited oversight role. This was based on the uncertainty at the time around the volume and type of investments that PGFL would hold. A transition from a passive holding company to an active company was always envisaged and built into PGFL's design and structure. Given the scale, volume and complexity of PGFL's portfolio, we consider it timely to transition PGFL from a passive holding company to an active company. This will support the PGF response to COVID-19, in line with the Government's broader economic response, by actively managing the delivery of regional investments which will ensure that people are working and businesses continue generating economic activity.
- 4 PGFL will now be holding a greater range of investments, in terms of type, volume and complexity, than was originally expected. By the end of June 2020, it is expected that the company will be holding up to \$400 million worth of investments so it is timely to make this shift. The magnitude of PGFL's portfolio will mean it is one of the larger companies held in the Crown's portfolio.
- 5 Managing and administering a number of PGFL's investments will require a more active management approach and additional technical oversight and expertise. As a passive holding company, PGFL faces challenges of being able to directly undertake project development roles and provide guidance and advice about its investments. We consider that having a more active company would be a better vehicle to ensure that investments held by PGFL

are best managed and delivers on both the Government's economic and wellbeing objectives and the PGF's objectives. This is even more important now in a COVID-19 recovery phase.

- 6 Officials from the Provincial Development Unit (PDU) are currently working on the details of the design and operational changes required to allow PGFL to transition to an active company, and we have asked officials to report back to the Minister of Finance and the Minister for Regional Economic Development, as Shareholding Ministers of PGFL, on possible design options. We recommend that final design decisions be delegated to the Minister of Finance and Minister of Regional Economic Development.
- 7 Officials will provide advice on to what extent PGFL becomes active, considering a variety of factors including impacts on Ministerial decision making. Initial advice indicates it should be feasible to strike a balance which maintains current decision making structures on new investments, limiting changes to PGFL's existing design and structure, while permitting PGFL to undertake certain activities.
- 8 The transition to an active company will also allow active subsidiary companies to be established under PGFL. The current mandate of PGFL restricts the powers of any subsidiary to also play a limited role as the powers of a Crown Entity company subsidiary cannot be greater than its parent. Being able to establish active subsidiaries will support the ability to develop the in-depth expertise needed to fully capitalise on opportunities presented by strategically important sectors. Work is underway to establish two active subsidiary companies under PGFL one for aquaculture related investments and **Commercial Information**  
[REDACTED]
- 9 Following final decisions on design, amendments will need to be made to the PGFL Constitution and other related documents to reflect Ministerial decisions. Given the complexities involved, transitioning PGFL to an active company will take up to three months. There will need to be consideration around appointments to the PGFL Board due to the scale of the change to the mandate of PGFL and whether a larger board of directors is more appropriate. We recommend that the current PGFL Board of Directors continue in their roles for the time being as the transition occurs.

## **Background**

- 10 The PGF aims to lift productivity and increase economic development opportunities in the provinces through investment in skills, sectors and infrastructure, generating jobs and better outcomes for New Zealanders.
- 11 The PGF has a number of options for how to fund or contribute to projects. These range from grants and loans through to underwriting or part ownership in a project, including equity shares. In some instances, funding arrangements involve a mix of investment mechanisms, adding complexity to how funding allocations are administered.

- 12 On 10 April 2019, Cabinet agreed to establish PGFL as a Schedule 4A company under the Public Finance Act 1989 [DEV-19-MIN-0084]. PGFL is established as an asset holding company that holds loan and equity investments made through the PGF. The Minister of Finance and the Minister for Regional Economic Development are the Shareholding Ministers.
- 13 Establishing PGFL as a Schedule 4A company was considered the most appropriate form of Crown entity to provide the necessary structure and flexibility to best manage loan and equity investments. PGFL holding these investments ensures that there is an entity in place with appropriate oversight and expertise that will be responsible for such investments beyond the life of the PGF and ensuring the Crown benefits from its investment.
- 14 Currently, the purpose of PGFL is to:
  - 14.1 act solely as the nominated legal entity for taking assignment of PGF debt and equity investments;
  - 14.2 act at all times in accordance with its constitution and its management agreement with the Ministry of Business, Innovation and Employment (MBIE) in relation to any matter relating to those investments; and,
  - 14.3 subject to compliance with the Companies Act 1993, distribute the receipts or proceeds of any PGF investments to shareholding Ministers, as agents of the Crown, unless otherwise agreed between PGFL, MBIE and Shareholding Ministers.
- 15 PGFL has no operational role in the day-to-day management and administration of PGF investments. PGFL has outsourced these functions to the Provincial Development Unit (PDU) within the Ministry of Business, Innovation and Employment (MBIE) through a management agreement, authorising it to act on behalf of the Company. Decision making responsibilities on PGF investments will remain unchanged.
- 16 PGFL is now an established and fully functional company, with the Board meeting monthly to discuss operational matters. The past 12 months have focused on the establishment and set-up of PGFL to enable the novation (or transfer) of investments and investment agreements to the Company to hold. Below are the key milestones that have been achieved in the past 12 months:
  - Mr Rodger Finlay (as Chair of the Board), Mr Neville Harris QSO and Mr Graeme Mitchell were appointed as directors of the PGFL Board each for a three year term on 1 August 2019 [CAB-19-MIN-0320.01].
  - We as Shareholding Ministers approved the company constitution for PGFL and PGFL was incorporated on 3 September 2019 and registered with the Companies Office with the Minister of Finance and the Minister for Regional Economic Development each holding 50% of the shares in PGFL.



- PGFL was added to Schedule 4A of the PFA and Schedule 35 of the Income Tax Act 2007, establishing PGFL as a Schedule 4A company with an income tax exemption [LEG-19-MIN-0149].
  - The Minister of Finance granted an indemnity to PGFL under the PFA.
  - PGFL's Statement of Intent and Statement of Performance Expectations were tabled in Parliament.
  - PGFL and MBIE entered into a management agreement which confirms the roles and responsibilities of both parties in terms of managing PGF investments.
  - We as Shareholding Ministers approved PGFL entering into funding arrangements with the Crown via a subscription agreement and agreed to the call payment of \$186,000,000 for PGFL to be able to make payments to PGF recipients.
  - The Associate Minister of Justice granted an exemption to PGFL from the requirements of the Anti-Money Laundering and Countering Financing of Terrorism Act 2009.
  - Relevant operational systems and processes have been established and set up.
  - The first contracted investment agreements were novated to PGFL.
- 17 Following the establishment of the \$300 million Regional Investment Opportunities Tagged Contingency from the Government's \$12 billion Capital Investment Package, we agreed that technical amendments be made to the constitution to allow for PGFL to hold asset investments and investments funded from non-PGF funds.
- 18 The PDU officials are implementing these changes as well as making subsequent changes to related PGFL documentation to reflect the change to the constitution.

**Given the scale, volume and complexity of PGFL's portfolio, it is timely to transition PGFL to an active company**

- 19 We consider it is now timely to transition PGFL from a passive holding company to an active company. This will support the PGF response to COVID-19, in line with the Government's broader economic response, by actively managing the delivery of regional investments which will ensure that people are working and businesses continue generating economic activity.
- 20 PGFL was initially established as a passive holding company with a limited oversight role. This was based on the uncertainty, at the time of establishment, around the volume and type of investments that PGFL would be expected to hold. The design of the company deliberately contemplated an eventual shift from passive to active at the appropriate time, and establishing PGFL as a Schedule 4A company provides that flexibility.
- 21 When Cabinet agreed to establish the company, it directed the PDU to report back to DEV within 12 months with an assessment of whether the current arrangement continues to be fit for purpose – it has now been 12 months. To

ensure the structure of the entity is fit for purpose, an assessment should be made on the nature, size, and complexity of PGFL's investment portfolio and as well as the pipeline of possible investments that PGFL hold.

- 22 Previous advice from TSY and PDU officials was that an investment portfolio of at least \$150 million was an appropriate "tipping point" to consider a transition to an active company with an active company likely to be preferred as the investment portfolio grew beyond \$200 million.
- 23 By the end of June 2020, it is expected that the company will be holding up to \$400 million worth of investments so it is timely to make this shift. The magnitude of PGFL's portfolio will mean it is one of the larger companies (as measured by total assets) held in the Crown's portfolio.
- 24 Additionally PGFL will now be holding a greater range of investments, in terms of type, volume and complexity, than was originally expected. Currently, PGFL investments range from under \$500,000 to tens of millions. These investments vary from suspensory loans to support water storage development projects in the Hawkes Bay to a subordinated convertible loan to support the development a mussel processing factory and farming operations in Ōpōtiki. Loans that PGFL hold differ on lending terms such interest rates, repayment schedules and general security arrangements.
- 25 PGFL will soon hold its first equity investment in the form of shares either converting from existing convertible loan agreements or the subscription for new shares. A number of approved equity proposals still under negotiation and will be transferred to PGFL in due course.
- 26 PGFL's equity portfolio is likely to include differing classes of shares in both growing and mature companies and full ownership of regional infrastructure assets or part ownership alongside both private interests and local authorities. Recent decisions that PGFL will hold projects funded from the Regional Investment Opportunities Tagged Contingency are an example of investments made in infrastructure assets that the Crown will own. This includes the Ōpōtiki Harbour Development and the West Coast Ports projects – the first physical assets that the company will hold.
- 27 Managing and administering these infrastructure projects will require a more active management approach and additional technical oversight and expertise. The challenges of PGFL being able to undertake project development roles as a passive holding company is very restrictive, resulting in unnecessary and time consuming work around solutions needing to be put in place.
- 28 We consider that having a more active company would be a better vehicle to ensure that investments held by PGFL are best managed and delivers on both the Government's economic and wellbeing objectives and the PGF's objectives ensuring that projects can be delivered in an effective and timely manner, and that the assets developed are carefully managed on behalf of the Crown. This is even more important now in a COVID-19 recovery phase.

### **Initial design work is already underway**

- 29 We recommend that Cabinet agree that PGFL be transitioned from a passive holding company to an active company.
- 30 PDU officials are currently working on the details of the design and operational changes required to allow PGFL to transition to an active company, and we have asked officials to report back to me and the Minister of Finance, as Shareholding Ministers of PGFL, on those details for consideration and decision making. These details will include possible design options and associated implications of each option.
- 31 Officials will provide advice on to what extent PGFL becomes active, considering factors such as roles and responsibilities of both PGFL and PDU, governance, form, function, capacity and capability. A pure active company would typically be structured as an independent commercially focused entity playing a more operational role resourced with staff and personnel. However, a pure active structure would have implications on Ministerial decision making as well as higher resource requirements. A balance can be struck in the legal design of the company that will allow for the benefits of it providing a more “hands on” approach to managing investments and any risk and liability and supporting the delivery of its projects while maximising value and efficiency.
- 32 Implications for Ministerial decision making will be a key consideration relating to each option. Initial advice indicates it should be feasible to strike a balance which maintains current decision making structures on new investments, limiting changes to PGFL’s existing design and structure, while permitting PGFL to undertake certain activities. Other options could include transferring decision making powers to PGFL to make decisions on what it chooses to invest in. This approach is typical of a pure active holding company but may have broader implications on the PGF decision making framework. Alternatively, a staged approach could be used that scales up PGFL’s powers and activities over time.
- 33 We recommend that final design decisions be delegated to the Minister of Finance and the Minister for Regional Economic Development as Shareholding Ministers of PGFL.

### **Active subsidiary companies are able to be established under PGFL**

- 34 The transition to an active company will allow active subsidiary companies to be established under PGFL. The current mandate of PGFL restricts the powers of any subsidiary to also play a limited role as the powers of a Crown Entity company subsidiary cannot be greater than its parent. Being able to establish active subsidiaries will support the ability to develop the in-depth expertise needed to fully capitalise on opportunities presented by strategically important sectors.
- 35 Active subsidiaries will provide the ability to facilitate and coordinate investments from a national perspective in pursuit of our strategic objective of generating a more productive, sustainable and inclusive economy. For

example, PGFL currently holds a number of strategic aquaculture assets, and there is an opportunity to use a strategic investment entity to accelerate the aquaculture sector's growth in line with both New Zealand's aquaculture strategy and other Industry Transformation Plans.

- 36 We consider an active subsidiary focused on strategic aquaculture investments can play a critical role in fostering an industry-wide transformation towards high value sustainable economic development that has the potential to significantly benefit Māori communities as well as New Zealand as a whole. Facilitating investment from a national perspective will allow us to coordinate dependent investments and overcome barriers to accelerated growth.
- 37 For example, on-water development of open ocean technologies - that would deploy advanced technologies while helping to mitigate some key environmental concerns relating to inshore aquaculture – has been delayed due to a lack of timely investment in core infrastructure (e.g. ports and wharves) and earlier value chain projects (e.g. hatcheries).
- 38 Based on this opportunity PDU and MPI officials are currently working on a proposal to establish an aquaculture-focused investment entity. It is appropriate that this entity sit under PGFL because it already holds a number of assets, that could be easily transferred to an active aquaculture entity, and which would provide foundation investments upon which an investment strategy could be built. Expertise gained by officials who have worked on these investments would also be able to be utilised by the entity.
- 39 The Ministers for Regional Economic Development and Fisheries will be bringing a proposal to establish an active aquaculture investment entity to Cabinet in the coming weeks.

40 **Commercial Information**



**Implementing the transition to an active company**

- 41 Following final decisions on design, amendments will need to be made to the PGFL Constitution and other related documents to reflect Ministerial decisions. The PDU is engaging early with its external legal advisors to understand the scale and complexity of the changes required to the PGFL mandate and Constitution.
- 42 Given the complexities involved, transitioning PGFL to an active company will take up to three months, including the appointment of existing and/or new directors through the Cabinet Appointments and Honours Committee (APH).
- 43 There will need to be consideration around appointments to the PGFL Board due to the scale of the change to the mandate of PGFL and whether a larger board of directors is more appropriate. We intend to ensure that the current



PGFL Board is closely involved through this process to help understand those considerations early.

- 44 We recommend that the current PGFL Board of Directors continue in their roles for the time being as the transition occurs.
- 45 Once Cabinet approval is received, officials will proceed with the following steps:
- 45.1 PDU officials will report back to the Minister of Finance and the Minister for Regional Economic Development on the possible design options to make decisions on the design and operations of an active PGFL.
  - 45.2 Shareholding Ministers will amend the PGFL company constitution by special resolution which states the revised purpose of the company and reflect the design and operational changes required to make PGFL an active company.
  - 45.3 MBIE's Performance and Appointments team will form a new board for PGFL that may contain new or existing directors. In any case, appointments will be proposed to the APH committee at an appropriate time;
  - 45.4 Other PGFL related documentation will need to be amended to take account of the changes to PGFL's constitution and the company's broader mandate.
  - 45.5 Further capitalisation of PGFL may be required to be able to take on further investments.
- 46 Officials will then adjust and finalise the operational aspects required to make PGFL an active company.

### Financial Implications

- 47 A \$1.0 million appropriation is in place for both 2019/2020 and 2020/21 to cover the operational costs of PGFL in its current form. An active PGFL will mean that the company will require additional funding to meet its anticipated increase in costs to support and maintain their broader mandate. It is estimated that the operational costs for active PGFL could be between \$<sup>Commerce</sup> - <sup>Commercial Information</sup> per annum.
- 48 The final costs of running an active PGFL is dependent on the level and type of investments and activities that will come under the operation of PGFL.
- 49 We propose that this increase in operational costs be met from the PGF, reducing the funds available for other investments. However, no operational funding has been appropriated for PGFL beyond 30 June 2021, beyond the life of the PGF. New funding will need to be sought in Budget 2021 for PGFL operating costs for out years.

### Legislative Implications

- 50 There are no legislative implications associated with the proposals in this paper.

### **Regulatory Impact Statement and Climate Implications of Policy Assessment**

- 51 Regulatory Impact Analysis and Climate Implications of Policy Assessment requirements do not apply to the proposals in this paper.

### **Human Rights and Population Implications**

- 52 There are no human rights or population implications associated with this paper.

### **Consultation**

- 53 This paper has been prepared by the Provincial Development Unit of the Ministry of Business, Innovation and Employment. The following agencies have been consulted: The Treasury, State Services Commission and the Department of Prime Minister and Cabinet.

### **Communications**

- 54 There are no media releases planned.

### **Proactive Release**

- 55 In accordance with Cabinet Office guidance (CO (18) 4 – Proactive Release of Cabinet Material), PDU and Treasury officials will proactively release documents pertaining to this paper within 30 business days of decisions being made, unless there is good reason not to publish all or part of the material.

### **Recommendations**

The Minister of Finance and the Minister for Regional Economic Development recommend that the Committee:

- 1 **note** that on 10 April 2019, Cabinet agreed to establish Provincial Growth Fund Limited (PGFL) as a Schedule 4A company under the Public Finance Act 1989 [DEV-19-MIN-0084]
- 2 **note** that due to the establishment of the Regional Investment Opportunities Tagged Contingency, technical amendments are being made to PGFL's constitution to allow for the company to hold asset investments and investments funding from non-PGF funds.
- 3 **agree** that the mandate of PGFL be transitioned from a passive holding company to an active company
- 4 **agree** to delegate authority to the Minister of Finance and the Minister for Regional Economic Development to make decisions on the final design and operation of an active PGFL.

- 5 **direct** the PDU to report back to the Minister of Finance and the Minister for Regional Economic Development with a revised constitution for an active PGFL.
- 6 **agree** that the current PGFL Board of Directors continues with their role for the time being as the transition to an active company occurs

Authorised for lodgement

Hon Grant Robertson  
**Minister of Finance**

Hon Shane Jones  
**Minister for Regional Economic Development**