Ministry for Primary Industries
Manatū Ahu Matua

Summary of submissions

Proposed amendments to kiwifruit export regulations

November 2016

New Zealand Government

Growing and Protecting New Zealand

Zespri share ownership

1. On 26 February 2016, MPI released a discussion document *Proposed Amendments to the Kiwifruit Export Regulations 1999* and invited submissions on this. Thirty three (33) individual submissions were received. The submission provided by the Kiwifruit Industry Strategy Project (KISP) included 769 signatories, largely from kiwifruit growers.

2. The full breadth of the industry was represented in submissions. Submissions were received from kiwifruit growers, packhouse operators, collaborative marketers, owners of proprietary varieties of kiwifruit, Zespri, New Zealand Kiwifruit Growers Incorporated (NZKGI) and Kiwifruit New Zealand (KNZ).

3. The discussion document considered four options in relation to Zespri's share ownership. Option 1 proposed retaining the status quo. The remaining three options were variations on the Kiwifruit Industry Strategy Project (KISP) proposal to create alignment through regulatory amendment.

<table>
<tr><td rowspan="2">Zespri share ownership</td><td colspan="3">Option 1 (status quo) - shares fully tradable amongst growers and former growers</td></tr>
<tr><td>Option 2A (KISP)
Remove regs 22 and 23 and allow a share cap to be set by Zespri</td><td>Option 2B keep Regs 22 and 23 but specify a 4:1 share cap</td><td>Option 2C
Amend regs 22 and 23 to allow a share cap set by Zespri, subject to KNZ approval</td></tr>
</table>

4. All submissions commenting on the ownership proposals supported a greater alignment of share ownership to supply than currently exists. However, submitters were split as to the means for creating alignment.

5. Submitters' support for alignment ranged from a pure cooperative model (1:1 alignment of share ownership to supply), to the KISP proposal of 4:1 ratio with potential for further alignment in the future.

6. Submitters generally agreed with the risks of misalignment as identified in the discussion document – that Zespri's performance could be hampered if the interests of growers and shareholders were to diverge.

A minority of submitters supported the status quo and recommended that commercial mechanisms be used to create alignment

7. A minority of submitters submitted that commercial options, rather than regulatory change, should be used to improve alignment. It was submitted that a coordinated programme of share buybacks and share offers should be explored prior to intervening through regulation to permit a share cap.

8. Submitters who supported the status quo also raised concerns about the potential for unwarranted regulatory interference with personal property rights. They stated that

overshared shareholders have made commercial decisions on the expectation that they would be able to retain shares to earn dividends, until such a time as they were prepared to sell.

9. One submitter, submitted that his retirement savings consisted mostly of Zespri shares. He submitted that many dry shareholders would have made similar retirement decisions, and would be negatively affected if dividends were restricted and the share price were to fall due to the imposition share cap.

The majority of submitters supported amending or revoking regulations 22 and 23 to enable a share cap to be introduced by Zespri with shareholder approval

10. A majority of submitters supported either option 2A or 2B. Option 2A, the KISP option, would revoke regulations 22 and 23 in their entirety. Regulations 22 and 23 prescribe Zespri's corporate form and provide a range of protections for minority shareholders. Option 2B would amend regulations 22 and 23 to the minimum extent necessary to allow Zespri shareholders to vote to impose a 4:1 share cap.

11. Zespri and NZKGI were amongst those submitters who expressed a clear preference for option 2A (revoke regulations 22 and 23). Zespri submitted that regulations 22 and 23 did not provide meaningful protections for shareholders. NZKGI submitted that it was for the industry to determine Zespri's ownership structure.

12. Submitters who expressed a preference for option 2B (amending regulations 22 and 23), including a number of dry shareholders and larger corporate interests, submitted that option 2B provided the most protection for property rights, aside from the status quo. Submitters who preferred option 2B also stated that they wanted to retain government oversight of Zespri's ownership, given the regulated nature of the industry.

Zespri proposed a variation on MPI's option to amend regulations 22 and 23

13. Zespri proposed a share ownership option that would build on the MPI option to amend regulations 22 and 23 to the minimum extent necessary to impose a share cap. Zespri's version proposed to empower Zespri shareholders to set the level of the share cap at their own discretion. This would be done through a vote of shareholders at Zespri's annual general meeting. By providing the industry with control over the level of the extent of the share cap, Zespri's alternative option would achieve the primary objective of the original KISP proposal.

14. Many of the submitters who supported MPI's option to amend regulations 22 and 23 did so because it provided for continuing government oversight of the extent of any future share cap.

No support for an expanded KNZ role in overseeing Zespri ownership

15. Only one submission supported option 2C. Submitters who preferred the status quo did not believe that this option would provide sufficient oversight, due to concerns about KNZ's independence. Submitters who supported the KISP option submitted that option 2C would increase costs and bureaucracy without providing significant additional flexibility for industry.

Core business

16. The discussion document considered four options in relation to Zespri's regulated definition of core business.

Zespri core business	**Option 1 (Status quo)** – core business is the purchase and export of New Zealand-grown kiwifruit
	Option 2 (KISP) – expand the definition of Zespri's core business as requested by the industry to include: • marketing, • supply chain management, • research and development, • proprietary variety right ownership, and • 12 month supply (purchasing kiwifruit grown in the northern hemisphere to ensure a consistent year-round supply of Zespri branded kiwifruit for consumers)
	Option 3 – allow Zespri to undertake activates outside of its core business without seeking shareholder approval if KNZ assesses the activity as not posing a substantive risk to Zespri's shareholders
	Option 4 – require shareholders approve Zespri's non-core activities every six years

Submitters were split between support for options 1 and 2, with little support for either options 3 or 4

17. Submitters were split evenly between support for options 1 and 2. The majority of submitters recognised the value of Zespri undertaking the wider identified activities, including those who supported the status quo. This was particularly so with regards to branding and marketing.

18. However, many of the submitters who supported the status quo were concerned about the level of control that shareholders could retain over activities that were seen as posing a higher commercial or branding risk, such as 12 month supply, if the Regulations were amended as requested by KISP.

19. For example, submitters noted specific concerns about the brand risks that they could be exposed to by the actions of overseas growers through Zespri's 12 month supply programme. There was also concern about which source of fruit Zespri would prioritise the purchase of during those times of the year where supply from both hemispheres was a possibility – i.e. purchasing overseas-grown kiwifruit at the expense of New Zealand growers. These risks would extend to captured growers, regardless of whether or not they were shareholders.

20. Given this, some submitters preferred to retain the ability to review and influence higher-risk activities. Regulation 11(1) provides shareholders and suppliers with an opportunity to consider the relative merits of activities that are deemed to be not necessary for core business and to authorise Zespri to undertake those activities.

21. Submitters who supported option 2 focused on the certainty that a regulated amendment would provide in enabling Zespri to undertake activities that are generating significant value for New Zealand. Zespri submitted that shareholders would continue to have control over Zespri's activities through the appointment of directors.

22. There was limited support for options 3 or 4, the alternative options identified by MPI. Depending on the focus of the submitter, concerns were expressed about whether these options would either provide sufficient certainty for Zespri or effective protections for shareholders and suppliers.

Kiwifruit New Zealand board independence

23. The discussion document considered four options in relation to KNZ's board appointments. Option 1 proposed retaining the status quo, which aligned with the KISP proposal. The three variations of option 2 proposed a spectrum of independence for the board.

<table>
<tr><td rowspan="2">KNZ board composition</td><td colspan="3">Option 1 (status quo, KISP) – 3 grower elected members, 1 NZKGI appointed member, 1 independent chair elected by the KNZ board</td></tr>
<tr><td>Option 2A
7 member board – 3 independent directors and 4 industry directors</td><td>Option 2B
6 member board – 3 independent directors and 3 industry directors</td><td>Option 2C
7 member board – 4 independent directors and 3 industry directors</td></tr>
</table>

24. The majority of submitters favoured greater independence, but a range of views were expressed as to the optimal level of independence. Very few submitters supported the status quo. Zespri and KNZ supported either options 2A or 2B. Option 2C was supported by a number of submitters, who were often collaborative marketers.

25. Submitters supporting the status quo or options 2A or 2B emphasised their desire for grower control of the regulatory body. Submitters supporting option 2C emphasised the need for independence, in fact and appearance, particularly in relation to decisions on collaborative marketing.

Kiwifruit New Zealand accountability

26. The discussion document proposed two options in relation to Kiwifruit New Zealand's (KNZ's) reporting and accountability. Option 1 proposed the status quo. Option 2 proposed a suite of proposals including three-yearly statements of strategic intent, annual KNZ – MPI engagement, and six-yearly performance reviews.

Board reporting	**Option 1 (status quo)** - no reporting to government and limited government control
	Option 2 – three-yearly statements of strategic intents, annual KNZ – MPI engagement, and six-yearly performance reviews

27. The majority of submitters indicated partial support for option 2. There was concern, including by Zespri, that the statement of strategic intent could be used to set a direction for KNZ that went beyond its role as defined in the Regulations. There was concern that MPI was proposing to give KNZ a general regulatory oversight function, including over Zespri's commercial decisions. Submitters also questioned whether regulatory changes were required to implement this proposal.

28. KNZ submitted against the development of statements of strategic intent, noting that, while appropriate for a crown entity, it may undermine KNZ's independence. Instead, KNZ submitted that consideration should be given to MPI annually setting out KNZ's expected performance in fulfilling its regulated functions.

Collaborative marketing

29. The discussion document proposed two options in relation to the operation of collaborative marketing. Option 1 proposed the status-quo. Option 2 proposed a number of specific proposals to enhance the uptake of collaborative marketing, including:
    a) clarifying the possibilities for multi-year approvals;
    b) clarifying the criteria used by KNZ in deciding applications;
    c) clarifying the ability of KNZ to undertake a review of its decisions on appeal; and
    d) providing for KNZ to recommend to Zespri that it proactively maps out collaborative marketing opportunities, and to compensate collaborative marketers where an agreement is terminated where substantive ongoing business value remains.

Collaborative marketing	**Option 1** (status quo) - Zespri and KNZ aims to increase uptake of collaborative marketing
	Option 2 – provide KNZ with more tools to incentivise collaborative marketing uptake

30. The majority of submitters supported various components of option 2. There was general support for multi-year approvals, provision for an internal review of KNZ decisions on request, and Zespri proactively mapping out opportunities for collaborative marketing.

31. There was mixed support for clarifying the criteria used by KNZ in assessing applications and recognising ongoing business value when a collaborative marketing programme is terminated. Often, where components of option 2 were not supported, it was due to concern about how it would operate in practice, or uncertainty about whether regulatory reform was needed to provide for the provision.

Kiwifruit New Zelaand's funding

32. The discussion document contained two proposals with regards to KNZ's funding. Option 1 proposed the retention of the status quo. Option 2 proposed:
    a) softening the wording in the Regulation requiring KNZ to operate "as cost effectively as possible", to support a less strict interpretation by the KNZ board;
    b) providing for KNZ to recover some collaborative marketing costs from Zespri; and
    c) enhancing transparency though reporting to NZKGI.

Funding	**Option 1 (status quo)** - cost recovery
	Option 2 - more flexible cost recovery

33. Most submitters supported flexibility for cost recovery from collaborative marketing. Submitters were mixed as to whether softening the cost effective requirement was valuable. Many submitters appeared not to understand the problem as defined in the discussion document.

34. KNZ indicated that the wording of the "cost effective" provision is leading some within the sector to believe that, where there is a cheaper short-term solution, KNZ must opt for that rather than investing in long-term infrastructure, such as legal opinions and expert advice, to support ongoing robust decision-making.