

Aotearoa Fisheries Limited
Response to the Independent Review of Māori
Commercial Fishing Structures

Under

The Māori Fisheries Act 2004

5 May 2015



PREFACE

The Māori Fisheries settlement was given effect through the passing of the Māori Fisheries Act 2004 (**MFA**), which created Aotearoa Fisheries Limited (**AFL**)¹. The MFA provides for a review of governance arrangements after the first 10 years of operation as prescribed in sections 114 -128. In 2014 Te Ohu Kai Moana Trustee Limited (**Te Ohu**) constituted a Committee of Representatives to appoint a reviewer and set the terms of reference. Mr Tim Castle was appointed as the independent reviewer (the **Reviewer**), and in accordance with section 125 of the MFA, Mr Castle issued his review report of Māori commercial fisheries structures "*Independent Review of Māori Commercial Fisheries Structures under the Māori Fisheries Act 2004*" (the **Review**) on 6 March 2015.

Section 126 of the MFA, requires AFL within 40 working days of the Review to prepare a plan specifying the actions it intends to take to address the findings and recommendations of the Reviewer. This report is therefore made pursuant to section 126 of the MFA.

In making this report AFL has considered the Review with due care and attention and in a purposive light. AFL has had the additional and significant benefit in that regard of also being able to study the Draft Working Paper "*Review of Māori Fisheries Entities – Existing and proposed governance arrangements*" (the **Draft Working Paper**), prepared by the Iwi Working Group (**IWG**). There is nothing in this report that is in disagreement with the responses of the IWG to the recommendations of the Reviewer as outlined in the Draft Working Paper.

Section 62(1)(g) of the MFA states that AFL has a constitutional obligation to use best endeavours to work co-operatively with Iwi on commercial matters. The Reviewer has interpreted this as meaning that AFL must not compete with Iwi in the business and activity of commercial fishing. AFL disagrees with this interpretation and legal advice received is unequivocal that this does not mean not to compete, as this would prevent AFL carrying out any operations where Iwi have a competing interest and would directly contradict AFL's statutory duty under section 61(1) of the MFA to act in a commercial manner. AFL notes that the Draft Working Paper is consistent with AFL's interpretation.

AFL intends to address all the findings and recommendations outlined in the Review, with the exception of the recommendation not to compete as discussed above. Some of the Reviewer's recommendations such as those pertaining to Rēkohu Wharekauri, and Sealord Group Limited are already in progress. AFL will work closely with Te Ohu to implement any Review recommendations that are agreed by Iwi at the special general meeting on 4 June 2015, particularly those that will require constitutional or legislative changes.

AFL will also give full consideration to ways in which it can further co-operate with Iwi on commercial matters, and will consider developing an operating model that allows Iwi to participate with AFL in the full value chain from quota through to customer.

¹ The MFA also created Te Ohu Kai Moana Trustee Limited, Te Putea Whakatupu Trust and Te Wai Māori Trust, however this Report only deals with Review findings and recommendations relevant to Aotearoa Fisheries Limited.

This report contains two Sections:

Section A: Actions Required to Implement Findings and Recommendations

This section outlines the actions that AFL intends to take to address all the findings and recommendations of the Reviewer, as required in section 126 of the MFA.

Section B: AFL's Obligation to use Best Endeavours to Co-operate with Iwi on Commercial Matters

This section outlines why AFL disagrees with the Reviewer's interpretation that AFL must not compete with Iwi, and gives examples where AFL currently co-operates with Iwi.

This report also contains two appendices:

Appendix 1: Iwi Participation in the Commercial Fishing Industry

The appendix gives an overview of the New Zealand ACE market and the source of ACE to certain fishing companies.

Appendix 2: Possible Business Model

The appendix sets out a high level overview of a possible approach to facilitating Iwi to have direct participation in the value chain through their own respective quota, while retaining the current benefit that AFL has in scale, capacity and supply chain capability.

SECTION A:

Actions Required to Implement Findings and Recommendations

Executive Summary

The Reviewer makes recommendations applicable to AFL in the areas of:

- Capital structure;
- Governance;
- AFL's requirement to use best endeavours to co-operate with Iwi on commercial matters;
- Restrictions on asset sales; and
- Rēkohu Wharekauri.

AFL's responses to the Review recommendations and findings are in alignment with the views expressed by the IWG as outlined in the Draft Working Paper.

AFL supports direct Iwi ownership of ordinary shares (i.e., voting and income shares) in AFL, and Iwi directly appointing directors to the AFL Board based on merit, as is currently the case. AFL also agrees with the comments of the IWG in the Draft Working Paper that these ownership and governance arrangements will create the right incentives for AFL to co-operate and align with Iwi as much as possible. In addition to implementing these structural changes, AFL will continue to give full consideration to the ways in which it can co-operate with Iwi on commercial matters.

Actions to address the Reviewer's recommendations in relation to capital structure and governance, and co-operation with Iwi, are substantial endeavours and, in some cases, will require wide ranging change to AFL's constitution. Some will also require amendments to the MFA. Thus, completion will take some time, significant investment, and will depend on close co-ordination between AFL, Iwi and Te Ohu.

The recommendations relating to Rēkohu Wharekauri and Sealord Group Limited are already work in progress.

The findings and recommendations relating to AFL's requirement to use best endeavours to co-operate with Iwi on commercial matters are dealt with in **Section B**.

1. Relevant Review Findings

The Reviewer's findings and recommendations cover AFL's capital structure and governance arrangements, cooperation and competition between AFL and Iwi, and AFL and Sealord Group Limited, restrictions on asset sales, and Rēkohu Wharekauri.

Table A1 provides a summary of the recommendations and the relevant paragraphs in the Review. The table also provides a reference to the recommendation number from the IWG Draft Working Paper.

Table A1: Summary of Review Recommendations

Number	Description	Review Paragraph
	<p><u>Capital Structure</u> (IWG recommendation number 2)</p>	
1	<ul style="list-style-type: none"> Allocate 100% of AFL's voting and income shares to Iwi. 	Executive Summary 36
2	<ul style="list-style-type: none"> Iwi to decide the basis for allocating shares. 	Executive Summary 38
	<p><u>Governance</u> (IWG recommendation numbers 2,3,4 and 7)</p>	
3	<ul style="list-style-type: none"> Iwi to appoint directors to the AFL Board. 	Executive Summary 47
4	<ul style="list-style-type: none"> AFL and Iwi to address the lack of fishing industry operational experience on the AFL board. 	Executive Summary 48, main report 206,207
5	<ul style="list-style-type: none"> AFL should consider the establishment of a Shareholders' Council. 	Main report 93b, 227,235
6	<ul style="list-style-type: none"> In the event that Recommendation 1 is adopted then AFL's constitution should require a two thirds majority approval of special resolutions with respect to major transactions. 	Main report 286
	<p><u>AFL Iwi and Sealord Co-operation</u> (IWG recommendation numbers 5 and 6)</p>	
7	<ul style="list-style-type: none"> AFL should not compete with Iwi in the business and activity of fishing. 	Executive Summary 35,41 main report 36
8	<ul style="list-style-type: none"> AFL and Sealord should rationalise their operations to avoid competing. 	Main report 251
	<p><u>Restrictions on Asset Sales</u> (IWG recommendation number 10)</p>	
9	<ul style="list-style-type: none"> Restrictions on the sale of AFL shares to be retained but with an easier process for willing buyer / willing seller sales within the Māori pool. 	Executive Summary 80,81 main report 120,121,268
	<p><u>Rēkohu Wharekauri/Chatham Islands</u> (IWG recommendation numbers 11 - 14)</p>	
10	<ul style="list-style-type: none"> AFL and Rēkohu Wharekauri Imi/Iwi should urgently establish a task force to resolve Māori fishing industry issues for Rēkohu Wharekauri. 	Main report 312,313

2. Action Plans

The following sections are intended to provide an indication of the scope of work required, likely time frames and cost of implementing the Review recommendations. In some cases actions are already underway which will deliver on Review recommendations, such as those relating to Rēkohu Wharekaui, and Sealord Group Limited. A number of the recommendations can be addressed through a single Action Plan. Formal project plans incorporating detailed planning and budgeting will be required before implementation of the larger Action Plans commences, and this Action Plan would need to be completed with close co-ordination between AFL, Te Ohu, and Iwi.

2.1 AFL Capital Structure, Share Transfer Process, Voting Thresholds, and Board

Changing AFL's capital structure and governance arrangements is a major project that will encompass changes to AFL's share structure including the process for allocation of shares, its constitution, the process for appointing directors, and associated changes to the MFA. The proposed changes in share structure and governance will need to be reviewed to ensure there are no tax implications, or any ramifications for AFL's contractual arrangements with third parties, including the Kura Limited joint venture with Nissui.

Given the extent of changes required to the constitution and the MFA, it would make sense to address the Review recommendations in relation to share transfer processes (Table A1 Recommendation 9), and approval thresholds for shareholder resolutions (Table A1 Recommendation 6) at the same time. The process will have direct impact on all Iwi asset holding companies and will therefore need to be completed with full consultation and in coordination with all affected parties.

Table A2 provides a very high level view of the work streams required and approximate minimum time to complete to the point of initiating the legislative process required to amend the MFA.

Table A2: Capital Structure and Governance Change main Work Streams

Action	Month					
	1	2	3	4	5	6
Project Initiation including Iwi and Te Ohu participation process						
Legal, accounting, tax due diligence						
Address external party issues including change of control impacts						
Design and agree new share structure and share allocations						
Address AFL and Iwi AHC balance sheet, P+L, tax, and treasury impacts						
Establish voting thresholds for classes of decisions						
Develop share sale and transfer process including pre-emptive rights						
Review for consistency with Iwi AHC rules and restrictions						
Develop process for appointment and removal of Directors, Chair, and Deputy Chair						
Develop necessary changes to rules on term of appointment, eligibility, alternates						
Draft amendments to constitution						
Obtain all required AFL, Te Ohu, Iwi approvals subject to MFA amendment						
Draft necessary changes to MFA & MFA amendment process						+++



+++ Significant additional time will be required to complete these parts, and the required time will largely be outside the control of Te Ohu, AFL, and Iwi.

The project will generate expenditure with external legal, tax, and accounting advisors and commitment of AFL resources to project management, communication, and engagement with Iwi and Te Ohu. An approximate estimate of cost to reach the point of drafting changes to the MFA could easily be in the range of \$1.0 million made up of \$0.3 million legal costs, \$0.2 million other external advisors, \$0.2 million AFL internal resources, and \$0.3 million spread across Iwi and Te Ohu.

It is difficult to put a full timeline on the project given the need to amend the MFA through the legislative process. An optimistic view would be 6 months to the point of having draft changes to the MFA prepared and ready for engagement with Government, and a further 12 months at least for the legislation to pass through Parliament. Logically all required changes to the MFA will be submitted to Parliament as a single set of amendments to the MFA. If this is the case, progress on all changes will be determined by the date at which the last Action Plan process is able to submit required changes to the MFA.

The Reviewer's recommendations in relation to the desirability of AFL directors having operational experience in the fishing industry (Table A1 Recommendation 4) can be addressed directly by the Iwi shareholders as and when vacancies arise on the Board, if that is their wish. We note that the current competence skills matrix that is used for the appointment of AFL directors was developed with extensive input from Iwi AHC representatives. That matrix has industry knowledge as one of its key attributes and can be further applied even before any formal changes are made.

2.2 AFL Competition with Iwi

AFL has in **Section B** addressed the Reviewer's findings with respect to competition between AFL and Iwi and AFL's performance of its obligation to use its best endeavours to cooperate with Iwi on commercial matters.

2.3 Shareholders' Council

The Reviewer has recommended the establishment of Shareholders' Council (Table A1 Recommendation 5).

AFL agrees with the IWG that a Shareholders' Council is not necessary when Iwi hold all the voting shares in AFL. If Iwi decide to proceed with the recommendation, it will be critical that the function of the Shareholders' Council is designed by Iwi to meet their expectations. The role of the Shareholders' Council must be defined so that it does not overlap, duplicate, or confuse the responsibilities and accountabilities of the Board. The Action Plan set out in Table A3 is based on the premise that the project is managed by a committee of Iwi and AFL board representatives with support and resources provided by AFL. Table A3 sets out the main work streams and timings involved in the establishment of a Shareholders' Council with full participation of Iwi in the process and decision making.

Table A3: Shareholders' Council Establishment**A**

Action	Month					
	1	2	3	4	5	6
Establish Representative Committee and project management resources						
Review the role of shareholder council's in other commercial entities, e.g. Fonterra and the Livestock Improvement Company, and similar representative bodies in Iwi organisations						
Design the role and function of an AFL Shareholders' Council						
Determine the size of the Council, eligibility rules for membership, and process for electing representatives						
Consultation and communication with all Iwi						
Draft the Council's constitution						
Draft amendments to AFL's constitution to support establishment of the Council						
Approval by Iwi						
First Council election						

The project is likely to cost in the order of \$0.25 million made up of \$0.1 million legal expenses, \$0.1 million Iwi communication and engagement costs, \$0.05 million external resources.

The establishment of a Shareholders' Council can proceed, if supported by Iwi, irrespective of decisions made in relation to AFL's capital structure and board governance arrangements. If changes to AFL capital structure and governance arrangements are made, it would be logical to plan the development of a Shareholders' Council to occur once these changes have been agreed. The Shareholders' Council establishment is unlikely to require legislative enablement and could proceed while capital structure and governance amendments to the MFA are in the legislative process.

The Reviewer comments² on the current Letter of Expectation between Te Ohu and AFL and notes that Iwi have extensive experience with this form of accountability protocol which will be *"useful tools in the development of accountability protocols between Iwi exercising full shareholder rights and responsibilities as owners of AFL"*. In the course of putting the new governance and arrangements in place, AFL would also have a new Statement of Corporate Intent for ratification by Iwi shareholders and subsequent review from time to time in the normal course of business.

2.4 AFL and Sealord Operational Rationalisation and Industry Consolidation

The Reviewer recommends (Table A1 Recommendation 8) that there should be rationalisation of AFL's and Sealord's operations *"to avoid them competing with each other as has unfortunately occurred to date"*.

The Reviewer further sees the need for rationalisation of the number participants in the fishing industry and suggests that Iwi Māori and the commercial entities they own (AFL and Sealord its joint venture) engage in this as soon as possible.

² Review paragraphs 200 to 204



AFL is working at both Board and management level to achieve greater alignment and co-operation between AFL and Sealord in shared markets and is satisfied that good progress is being made.

2.5 Rēkohu Wharekauri/Chatham Islands

The Reviewer discusses³ the issue of ownership and utilisation of Rēkohu Wharekauri quota and recommends (Table A1 Recommendation 10) that a joint AFL/Rēkohu Wharekauri Imi/Iwi task force is formed to urgently address Māori fisheries issues for Rēkohu Wharekauri.

AFL and the Rēkohu Wharekauri Imi/Iwi, Ngāti Mutunga and Moriori, have already reached agreement in principle to form a partnership to harvest, process, and market, under a Chatham Islands brand, their inshore quota utilising Rēkohu Wharekauri fishers. Profits from the partnership will be shared between AFL, the Imi/Iwi, and fishers. AFL has committed to rebuilding its plant at Waitangi as part of this arrangement. AFL and the Rēkohu Wharekauri Imi/Iwi will continue to work together to develop further opportunities for joint investment in the utilisation of Rēkohu Wharekauri resources.

2.6 Industry Representation

The Reviewer advocates that AFL take a leading advocacy role in the commercial fishing industry. AFL agrees with this comment. AFL is represented on all the main industry bodies including Seafood NZ, the Deepwater Group, Fisheries Inshore NZ, the Paua Industry Council, the Rock Lobster Industry Council, and Aquaculture NZ. AFL works in close cooperation with Te Ohu, and would continue to work with Te Ohu if the IWG's proposals are adopted by Iwi, on a wide range of fisheries management and fisheries policy issues.

3. Funding

AFL agrees with the Reviewer's finding that the cost of facilitating Iwi consideration and decision making should be met from the funds held by Te Ohu and believes that this principle should be extended to funding implementation of recommendations that are accepted by Iwi. AFL estimates that the delivery of the Action Plans outlined in Sections 2.1 and 2.3 will involve expenditure of between \$1.25 and \$2.0 million.

4. Concluding Comments

AFL supports direct Iwi ownership of ordinary shares (i.e., voting and income shares) in AFL, and Iwi directly appointing directors to the AFL Board based on merit and through the operation of an appointments committee. AFL also agrees with the comments of the IWG in the Draft Working Paper that these ownership and governance arrangements will create the right incentives for AFL to co-operate and align with Iwi as much as possible. AFL supports the development of an operating model that facilitates full Iwi participation in the value chain from quota to customer, and the joint utilisation of AFL and Iwi ACE.

³ Review paragraphs 305 -313

AFL sets out in **Appendix 2** a high level overview of a possible approach to facilitating Iwi participation in the value chain, while retaining the current benefit that AFL has in scale, capacity and supply chain capability.

A

SECTION B:

AFL's Obligation to use Best Endeavours to Co-operate with Iwi on Commercial Matters

Executive Summary

Section 61(1)(g) of the MFA states that AFL has a requirement to use its best endeavours to work co-operatively with Iwi on commercial matters. The Reviewer has interpreted this as meaning that AFL must not compete with Iwi in the business activity of fishing.

AFL does not agree with the Reviewer's interpretation of section 61(1)(g). This section does not state nor even imply the duty not to compete, and to apply it in that way would raise the real risk that AFL breaches its duty to manage its assets in a commercial manner, as outlined in section 61(1). AFL is a commercial company that must compete with other industry parties (including Iwi). A complete prohibition on competing with Iwi could undermine AFL's viability, requiring AFL to withdraw from core business activities that would jeopardise the sustainability of this 100% Iwi owned enterprise.

The independent four yearly audits of AFL carried out in accordance with section 110 of the MFA also confirm that AFL has met its statutory obligation to use best endeavours to work co-operatively with Iwi on commercial matters.

AFL's view, which is consistent with the unequivocal legal advice received is that:

- AFL's primary statutory duty is to manage its assets in a commercial manner in the best interests of AFL;
- AFL is obliged to consider all reasonable opportunities to work with Iwi for mutual benefit in fishing and fisheries-related activities. AFL should actively explore opportunities for mutual co-operation;
- When AFL works co-operatively with an Iwi on a commercial matter, AFL is neither obliged nor permitted to prefer the interests of that Iwi over the interests of AFL (and the body of Iwi that ultimately own AFL); and
- The legislative history of the MFA contemplates that AFL and Iwi-owned fishing companies will compete with one another. AFL is not obliged to withdraw from any commercial opportunity in order to avoid competing with Iwi.

For the reasons set out in this report, AFL does not intend to take any action to address the Reviewer's finding and subsequent recommendation that AFL has a statutory duty not to compete with Iwi in the business and activity of commercial fishing.

It is relevant to note however that since inception in 2004, AFL has entered into a wide range of commercial arrangements with individual Iwi, and with Iwi collectives that are consistent with its constitutional obligations to use best endeavours to work co-operatively with Iwi on commercial matters, and its statutory duty to act in a commercial manner. Examples of these arrangements are set out in part 3 of this section.

AFL will continue to give full consideration to the ways in which it can co-operate with Iwi on commercial matters, and to developing an operating model that allows Iwi to participate with AFL in the full value chain from quota to customer.

B

1. Māori Fisheries Act Anticipated Competition

The architects of the MFA were clearly cognisant of the likelihood of competition when drafting the legislation. The primary purpose of AFL as defined in section 61 of the MFA is to “*manage its assets in a commercial manner*”. Commercial management implies that AFL will fully participate in the fishing industry for the purpose of generating sustainable profits, an outcome anticipated in section 76 of the MFA which requires that AFL pay dividends of at least 40% of its net profit after tax.

Competition is an inherent facet of participation in the fishing (or any other) industry. As the Iwi Asset Holding Companies required to be established by Iwi to receive settlement quota would also be participants in the fishing industry and under a similar imperative to generate dividends (refer Schedule 7 Kaupapa 7 of the MFA) the potential for indirect competition between Iwi and AFL was clear at the time the MFA was drafted.

The legislator’s response was to include in section 62(1)(g) of the MFA a requirement that AFL’s constitution include an obligation to “*use best endeavours to work co-operatively with Iwi on commercial matters*”. This obligation recognises that delivering on the purpose of the MFA to “*provide for the development of the collective and individual interests of Iwi in fisheries, fishing, and fisheries related activity in a manner that is ultimately for the benefit of all Māori*” would be enhanced by setting a high expectation that AFL would co-operate with Iwi.

It would have been reasonable for the drafters of the legislation to have made an explicit direction in section 62(1)(g) of the MFA that AFL not compete with Iwi if they had thought this to be necessary or compatible with the purposes of the MFA. The fact that they choose not to go down this route, but rather opted to require that AFL’s constitution include an obligation to use best endeavours to co-operate commercially with Iwi, recognised the unavailability of indirect, and potentially even direct, competition between AFL and Iwi in the market for consumer seafood products and direct competition between Iwi in the ACE market.

2. Competition is inherent in the Settlement Structure

In commercial terms, the implementation of the MFA resulted in the progressive establishment of 57 Iwi fishing industry businesses, holding largely subscale parcels of settlement quota, and the formation of AFL as a holding company for Iwi investment in Sealord and a number of independently managed subsidiary companies.

The immediate priority for the managers of Iwi asset holding companies was to generate cash returns from quota and for the managers of AFL to turn operating losses to profits. The resulting competition between Iwi, and indirectly between Iwi and AFL as a consequence of Iwi ACE supply to AFL’s competitors, was a natural outcome of Iwi and AFL becoming active players in the fishing industry. AFL sets out in **Appendix 1** an overview of the arrangements which lead to this competition.

3. AFL Cooperation with Iwi

AFL believes that the 2012 independent statutory audit report prepared in accordance with section 110 of the MFA properly identified the key features of AFL's obligation to work co-operatively with Iwi when it referred to:

- AFL endeavouring to *“enter into commercial arrangements with the owners of Iwi fishing assets in ways that use the combined strength of distinct Māori fishing interests to optimise the commercial outcomes for AFL”*;
- *“The combination of Iwi owned quota and AFL’s expertise in growing harvesting, processing, and marketing seafood ... when used together” providing “the development of commercial relationships over the medium to long term and [providing] benefits to all parties”*; and
- *“The development and maintenance of strong commercial relationships with Iwi”*.

AFL has entered into a wide range of commercial arrangements with individual Iwi and with Iwi collectives. When making these arrangements, AFL has been mindful of its obligation under section 61 of the MFA to manage its assets in a commercial manner, and of its constitutional obligation to ensure that a commercial arrangement with an Iwi or group of Iwi is not detrimental to its remaining Iwi shareholders. The range of commercial arrangements that AFL has entered into with Iwi include:

- Sales of assets including property and quota to individual Iwi;
- Purchase of quota subject to options in favour of individual Iwi;
- Short and long term ACE lease agreements;
- Ihu To Mai agreements;
- Joint venture partnerships;
- Processing agreements;
- Marketing agreements;
- Pataka kai arrangements; and
- Funding and resource support for Iwi initiatives.

The nature of the arrangements reflect different Iwi objectives, appetite for risk, and desire for exposure to the full value chain.

Table B1 on the following page provides a summary of the main forms of commercial arrangements currently in place between Iwi and AFL.

Table B1: Types of Commercial Arrangements with Iwi

Type of Agreement	Exposure to Value Chain	Risk Management
ACE Supply, market pricing, annual or multi-year	ACE only, returns reflect market dynamics for each stock in the ACE parcel. Returns not directly linked to AFL's value chain performance.	Return fixed for a defined period, similar in risk profile to a fixed interest bank deposit, subject to AFL credit risk.
Ihu To Mai	Iwi participant receives a fully comingled volume based proportionate share of the operating cash flow generated by Sealord from harvesting, processing, and marketing the ACE in conjunction with the rest of its ACE portfolio. Returns are directly linked to Sealord value chain performance.	Returns are fully variable with opportunity gains or losses with respect to market ACE returns to the extent that Sealord over or under performs relative to its competitors. The Ihu To Mai agreements give Iwi opt out rights at the start of each year if forecast returns are unacceptable.
Partnerships	Iwi participants and AFL enter into a partnership arrangement to harvest, process, and market a combined ACE portfolio. Returns are derived directly by the partnership operation. AFL may be contracted as the partnership manager and may provide some or all of the harvesting, processing, and marketing services required by the partnership. In the case of the Inshore Fisheries partnership between the ICP and AFL harvesting and processing services are provided by both AFL and Ngāti Porou.	The partnership is governed by a Board appointed by Iwi and AFL. Returns are subject to decisions made by the Board relating to partnership operations and the performance of the manager. The participating Iwi and AFL share fully in the cash flow generated by the partnership and are exposed to the same level of risk.
Processing and marketing	AFL provides contract processing and / or marketing services to the participating Iwi on fee for service basis.	Returns are fully variable and specific to the participating Iwi. Both AFL and the participating Iwi benefit from processing scale and market presence. Market decisions including pricing and timing of sales are made jointly. Revenues are specific to the participating Iwi's product. Contract rates for processing are transparent.

AFL and Sealord have commercial arrangements with over half of AFL's shareholding Iwi. Iwi engagement with AFL spans direct agreements, working through the ICP, or multiple arrangements in some cases. Table B2 provides a summary of current commercial arrangements between Iwi and AFL/Sealord.

Increasing Iwi appetite for full involvement in fishing industry returns and risks is evident in the oversubscribed offer of Anton's quota with five of the eight subscribing Iwi opting to take up an Ihu To Mai arrangement rather than a fixed return ACE lease. AFL and Rēkohu Wharekauri Imi/Iwi, Ngāti Mutunga and Moriori, have recently agreed in principle to the formation of a partnership arrangement covering harvesting, processing, and marketing of inshore wet fish, under a unique Chatham Islands brand. Partnership returns will be shared between AFL, the Iwi, and Rēkohu Wharekauri fishers. The move to greater industry value chain involvement is consistent with the development of the Port Nicholson Fisheries Partnership, the ICP's relationship with Sanford Ltd, and Ngāi Tahu's continued success as a lobster exporter.

Table B2: AFL arrangements with Iwi

Type of arrangement	Number of arrangements with individual Iwi		Comment
	AFL	Sealord	
Annual ACE	1	1	On quota held by Te Ohu pending allocation
Formal Multi-year ACE	4		Terms tailored to suite each Iwi
Informal ACE supply	3		Longstanding informal arrangements spanning multiple years
Ihu To Mai		5	Covering full deep water ACE packages of participating Iwi. A number of Iwi have pooled ACE to participate
Ihu To Mai	5		Arising from Anton's quota purchase. ACE passed to Sealord
Fixed return	3		Arising from Anton's quota purchase. ACE passed to Sealord
JV Partnerships	2		Inshore Fisheries JV with ICP (12 Iwi), and Rēkohu Wharekauri Wet Fish JV with Rēkohu Wharekauri Imi/ Iwi (agreed in principle)
Processing	2		Ngāti Porou and Ngāi Tahu
Marketing	1		Ngāi Tahu

4. Iwi Views Expressed in Submissions

Seventeen written submissions were received by the Reviewer from Iwi. A number of submissions were made on behalf of collectives of Iwi so that the actual number of Iwi whose views are covered in written submissions is higher than the number of submissions received. The Review⁴ provides tabular and graphical analysis of the submissions received. The analysis indicates that 12 of the 17 written submissions from Iwi supported the view that *"AFL (including Sealord) commercial alignment with Iwi requires improvement"*.

It is clear from the written submissions of Iwi and the Reviewer's comments from his hui with Iwi representatives, that Iwi are looking for AFL to play a more active role in the development of a Māori fishing industry, by creating opportunities for all Iwi to participate with AFL in the full value chain from quota to customer. AFL is eager to take up this challenge.

5. The Way Forward

Value chain participation in high volume low value products, in essence the core of the NZ fishing industry, excluding lobster and pāua, requires scale and access to capital to support investment in vessels, plant, product and market development, and brand. Individual Iwi settlement quota packages do not, in most cases, have sufficient scale in market preferred species to support direct participation in the value chain beyond quota and ACE.

⁴ Review Pages 31-33

AFL fully supports the view that it and Iwi can evolve into a true Māori fishing industry in which all Iwi are able to participate in the full value chain from quota to customer. AFL has demonstrated its resilience and operational capability by maintaining its operating earnings in the face of a very adverse foreign exchange environment, static or reducing allowable catches, and a global financial crisis that has created challenging international markets for AFL's high margin products. AFL has invested in new processing facilities in Whitianga, Auckland, and Palmerston North, has committed to rebuilding its Rēkohu Wharekauri plant, and has launched the progressive renewal of its inshore fleet in conjunction with its fishers.

B

APPENDIX 1

Iwi Participation in the Commercial Fishing Industry⁵

Since 2004 individual Iwi have developed a wide range of commercial relationships with other Iwi, AFL, Sealord, and other players in the industry including:

- long term ACE supply arrangements with harvesters;
- long term brokering arrangements with ACE resellers;
- joint venture pooling of ACE with other Iwi to achieve commercial scale;
- joint venture participation in harvesting, processing, and marketing;
- direct investment in harvesting, processing, and marketing; and
- equity investment in partner companies.

Iwi are, either individually or through collective arrangements such as the Iwi Collective Partnership (ICP), ACE supply partners to all the major players in the fishing industry. Iwi are active participants in the industry in their own right. In many instances ACE buyers source ACE from more than one Iwi, or from brokers who are on selling Iwi sourced ACE. The companies that Iwi supply ACE to are, in some cases, competitors.

The NZ fish harvesting, processing, and marketing industry is simply too disaggregated for Iwi to find a single buyer for the entire ACE generated by their settlement quota portfolio's. Competition between Iwi in the ACE market and indirectly in the harvesting, processing, and marketing segments of the industry is a natural result of Iwi being participants in the industry. AFL's largest 5 shareholders provide a snapshot of the range of commercial arrangements that have evolved to address this situation:

- Ngāpuhi Asset Holding Company Ltd (Ngāpuhi) are joint venture partners with DSM Ltd (Peter Dawson) in Northland Deepwater JV Ltd, a deep water trawling business;
- Ngāti Porou Seafoods Ltd (Ngāti Porou) through the ICP are in joint venture with AFL with respect to their inshore quota, Sanford Limited (Sanford) with respect to their deepwater quota, and are investors in lobster exporter Port Nicholson Fisheries Limited Partnership with Ngāti Mutunga o Wharekauri Asset Holding Company Ltd and Parininihi ki Waitotara Inc. Ngāti Porou operate a fish processing factory and retail outlet in Gisborne and have invested in non-settlement quota;
- Kahungunu Asset Holding Company Limited (Kahungunu) have a long standing inshore quota ACE supply arrangement with Hawkes Bay Seafoods, supply their deepwater ACE to Sealord under an Ihu To Mai profit sharing arrangement, and are equity holders in and suppliers to lobster exporter Fiordland Lobster;
- Waikato-Tainui Fisheries Limited (Tainui) have a long term ACE supply arrangement with AFL for their inshore quota and supply their deepwater ACE to Sealord under an Ihu To Mai profit sharing arrangement;
- Ngāi Tahu Seafoods Limited are a successful lobster exporter in their own right, have inshore ACE supply arrangements with a number of affiliated fishers, supply their deepwater and a

⁵ The data in this section was derived by AFL analysis of Fish Serve quota and ACE data.

component of their inshore ACE to Talley’s Group Limited (Talley’s), and have a processing and marketing agreement with AFL covering their abalone production.

Iwi are the major suppliers in a competitive ACE market, supplying all the major harvesting and processing businesses. Figures 1 and 2 show Talley’s and Sanford ACE suppliers (excluding internal transfers).

Figure 1: Talley’s ACE Suppliers

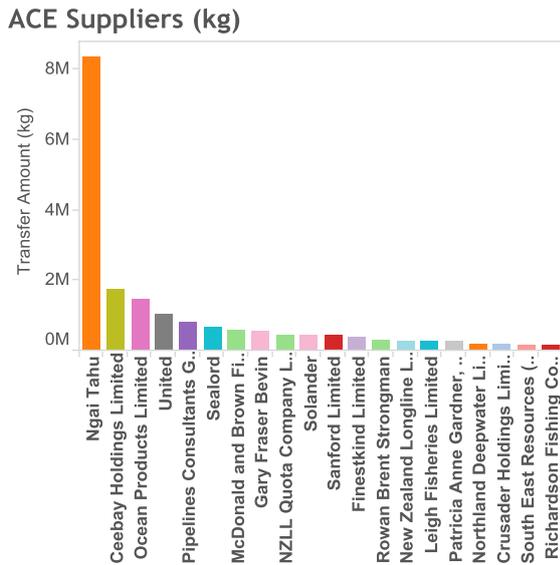
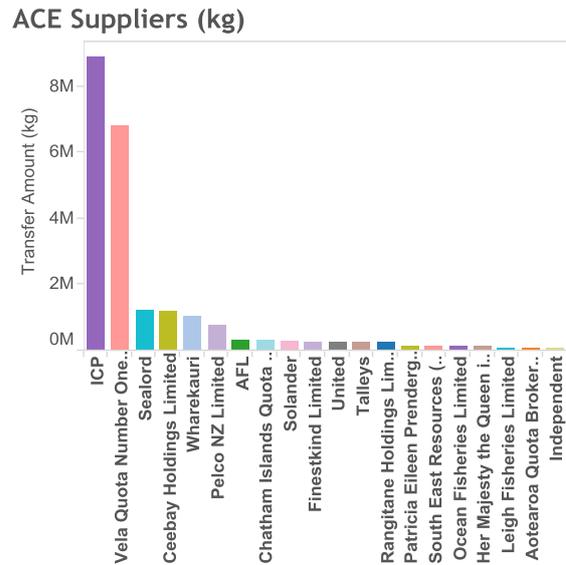


Figure 2: Sanford ACE Suppliers



Ngāi Tahu and the ICP are the largest suppliers of ACE to Talley’s and Sanford respectively who are the second and third largest buyers in the ACE market. The arrangements make commercial sense for both Ngāi Tahu and the ICP but involves competition between these Iwi and other Iwi seeking to lease ACE to Talley’s and Sanford, and indirect competition between Ngāi Tahu and the ICP members given that Talley’s and Sanford are major competitors.

Figure 3: Hawkes Bay Seafoods ACE Suppliers

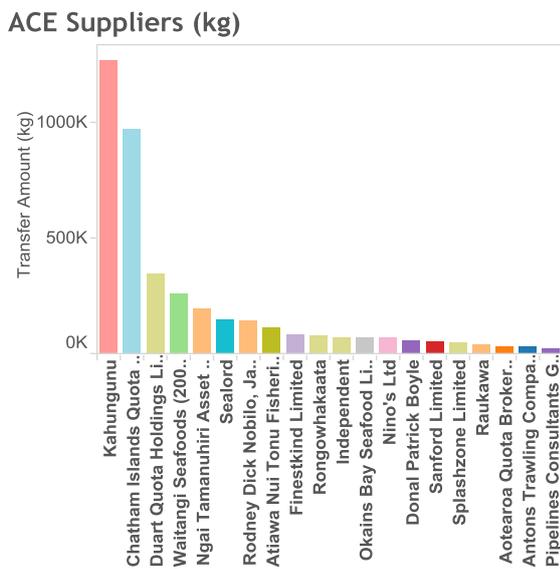
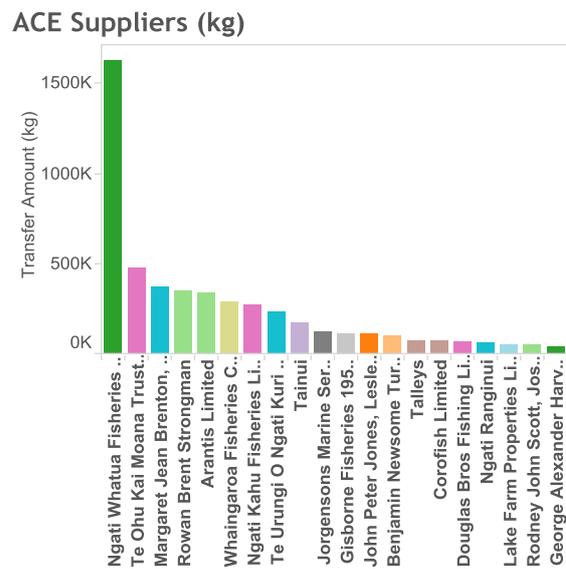


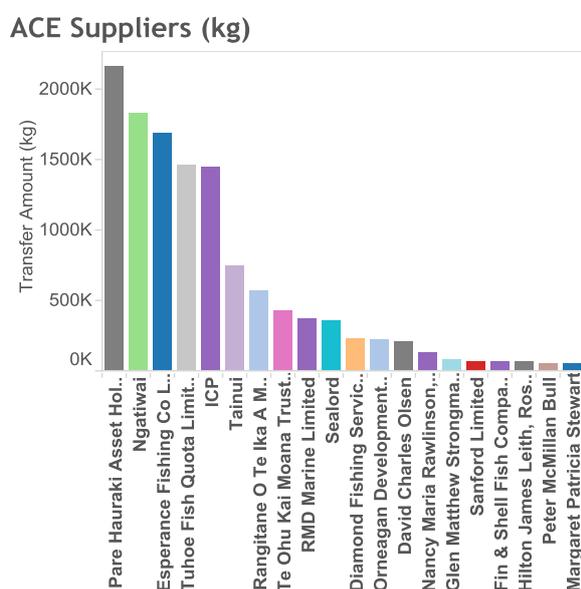
Figure 4: Leigh Fisheries Ace Suppliers



AFL and Sealord compete in the market for consumer seafood products with buyers of ACE supplied by Iwi. Iwi are the largest suppliers of ACE to Talley’s, Sanford, Leigh, and Hawkes Bay Seafoods, AFL’s major competitors in the wholesale market for fresh wet fish in New Zealand and Australia. Figures 1 and 2 show the importance of Iwi ACE to Sanford and Talley. Figures 3 and 4 show the importance of ACE supply from Kahungunu to Hawkes Bay Seafoods and from Ngāti Whātua Fisheries Limited to Leigh Fisheries.

AFL competes indirectly with Ngāi Tahu, the ICP, Kahungunu, and Ngāti Whātua by competing with their major ACE customers in the market for the supply of wet fish products. The only way in which AFL can avoid competing would be to exit the fresh fish market which would be highly detrimental to AFL’s current Iwi ACE suppliers, and its ability to pay dividends to its shareholders. AFL buys ACE from a large number of Iwi ACE suppliers as outlined in figure 5.

Figure 5: AFL ACE Suppliers



Iwi supplying AFL’s (or Sealord’s) competitors are therefore indirectly competing with those Iwi who supply ACE to AFL to the extent that competition reduces profits available for distribution under joint venture and profit share arrangements. Furthermore those Iwi are competing with all Iwi to the extent that AFL’s dividends are constrained by the effects of that competition.

These examples illustrate the extent (and complexity) of Iwi involvement as ACE suppliers in the fishing industry and the potential for competition between Iwi and Iwi and AFL/Sealord. Competition is not necessarily detrimental. The commercial relationships that have evolved following the allocation of quota reflect rational decision making based on the commercial merits of each arrangement.

AFL and Iwi rarely compete directly as they are simply not active in the same markets. AFL leases ACE from Iwi in a competitive market but is not an ACE supplier in that market (other than to its fishers). AFL competes in the market for consumer seafood products with some enterprises that lease Iwi ACE and is therefore in indirect competition with their Iwi ACE suppliers. There is no evidence that indirect competition of this type is detrimental to Iwi or AFL.

Iwi are active participants in the ACE market and are becoming increasingly involved in the market for consumer products through partnership and profit sharing arrangements. The challenge laid down for Iwi and AFL by the Review is to achieve full Iwi participation in the value chain through Iwi

owned and managed businesses, to create a true Māori Fishing Industry. AFL is ideally placed to work with Iwi to make this a reality.

APPENDIX 2

Possible Business Model

1. Summary

AFL is well placed to be the vehicle for all Iwi to benefit from full exposure to the risks and rewards of participating in the fishing industry.

The Review commented⁶ that AFL and Iwi should consider moving to specialisation in value chain management and quota ownership as recommended in the McClurg report to Te Putea Whakaputu.

AFL supports the consideration of a business model that enables Iwi to directly participate in the value chain from quota to customer, and at the same time provide greater transparency between the returns being derived from quota ownership and investment in harvesting, processing, and marketing.

One possible business model that enables and facilitates Iwi participation in the value chain, while retaining the current benefit that AFL has in scale, capacity and supply chain capability is the use of limited partnerships (LPs) between AFL and Iwi, which utilise AFL's operating divisions to access the full value chain.

In summary this business model would:

- facilitate direct Iwi participation in the full value chain from quota to customer;
- provide transparency of returns to quota ownership and investment in harvesting, processing, and marketing;
- provide a straightforward process for Iwi to commit (and withdraw) ACE to the AFL full value chain;
- reduce the need for individual partnerships between AFL and Iwi;
- return free cash flow directly to Iwi for all committed ACE;
- put Iwi in charge of how their ACE is used and how AFL invests their money; and
- provide a straightforward process for AFL and Iwi joint investment in growing the Māori Fishing Industry.

2. Possible Business Model

A relatively straightforward business model may be developed by AFL to deliver the benefits noted above utilising a LP structure⁷ to aggregate AFL and Iwi ACE and to contract AFL's operating divisions to provide harvesting, processing, and marketing services. Returns generated by the proposed LPs would be passed back to Iwi and AFL in proportion to ACE contributed. Iwi will receive returns in the form of dividends from AFL and LP payments to the extent they contribute ACE. The business model will have the features illustrated in figure 1 and described over:

⁶ Main report paragraphs 72, 73, 74, 94b, 94c, 212 and 222

⁷ Refer page 129 of the Review for a description of Limited Partnerships

- Iwi will hold 100% of the shares in the AFL with full rights to appoint and remove directors;
- AFL will establish a new subsidiary AFL OpCo Ltd;
- AFL's staff and harvesting, processing, and marketing assets will be transferred to AFL OpCo which will retain AFL's current divisional structure and existing relationships with suppliers and customers;
- AFL will establish three LPs covering wet fish, lobster, and paua;
- AFL will supply its ACE to the relevant LP;
- all Iwi will have the automatic right to be limited partners in each LP and may choose to supply ACE to the LP;
- the LPs will contract AFL OpCo's divisions to harvest, process, and market each LP's ACE for a fee. The fee will recover AFL OpCo's costs inclusive of a capital charge on assets employed;
- returns from the sale of products less AFL OpCo's contract fee will be passed back to the limited partners (including AFL) in each LP in proportion to ACE contributed; and
- Iwi will receive returns as shareholders in AFL and as limited partners in each LP to the extent that they contribute ACE to the LP.

This possible business model puts Iwi in charge of the utilisation of their quota as owners and governors of AFL and allows Iwi to make full use of their investment in harvesting, processing, and marketing assets and capability through AFL by committing ACE through the LP structure.

2.1 Governance

Assuming the Review recommendations regarding AFL's share structure are accepted, AFL will be 100% Iwi owned with all Iwi becoming ordinary shareholders. Individual Iwi will have the rights that normally attach to ordinary shares including the right to vote on the appointment and removal of directors and to vote on major transactions. Iwi will have control of AFL.

2.2 Quota Ownership

The structure is based on continued ownership of quota by AFL and commitment of the derived ACE to the proposed LP arrangements. Retaining quota within AFL greatly simplifies management of AFL's current debt and retains capacity to raise debt for new investment.

2.3 ACE Limited Partnerships

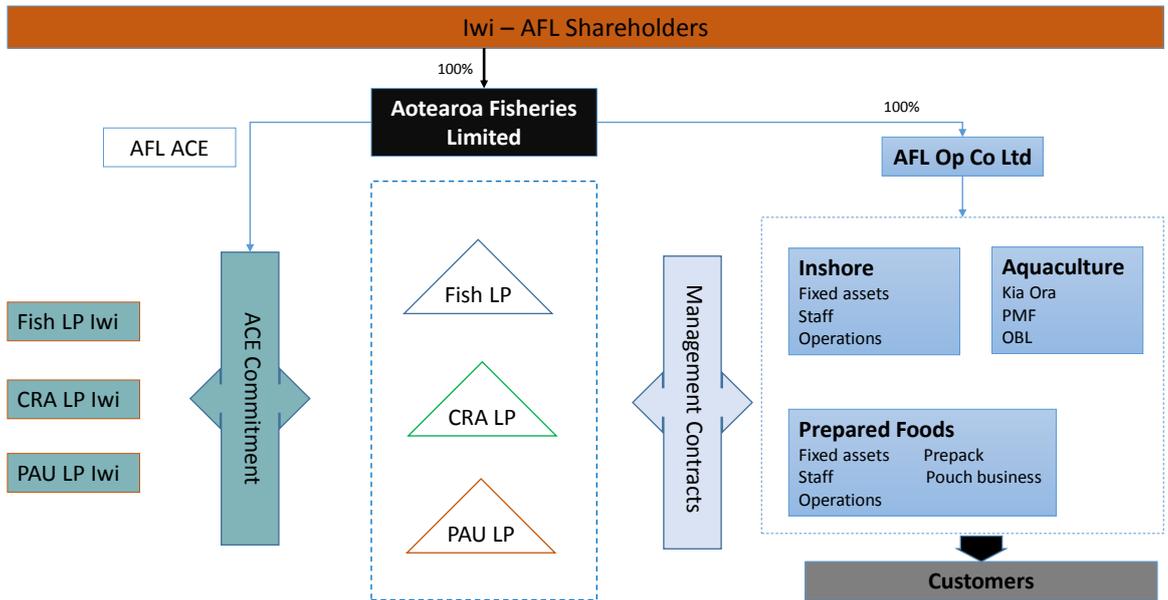
The ACE LPs are the vehicle through which Iwi can access the scale offered by their common investment in AFL. AFL's ACE will be 100% committed to each LP for an initial term matched to the economic life of AFL's processing and marketing assets.

Iwi may contribute ACE to each LP in return for a share of the residual cash flow generated by the LP in proportion to the value of ACE contributed.

2.4 Non Quota Based Businesses

AFL's Aquaculture, pouch meal, and ration pack businesses will transfer to AFL OpCo as part of the current divisional structure. AFL's 50% shareholding in Kura Limited and the Pupuri Taonga Trust will continue to be held as direct subsidiaries of AFL.

Figure 1: Possible Business Model



SCHEDULE

Glossary of Acronyms and Terms

ACE	Annual Catch Entitlement as specified under the Quota Management System.
AFL	Aotearoa Fisheries Limited.
AFL OpCo	The subsidiary of the Parent Company proposed in Appendix 2 to hold AFL's harvesting, processing, and marketing and other non quota assets.
Draft Working Paper	<i>"Review of Māori Fisheries Entities – Existing and proposed governance arrangements"</i> released by the IWG.
ICP	Iwi Collective Partnership.
IWG	Iwi Working Group.
LP	A Limited Partnership under the Limited Partnership Act 2008.
MFA	Māori Fisheries Act 2004.
Review	<i>"Independent Review of Māori Commercial Fisheries Structures under the Māori Fisheries Act 2004"</i> released on 6 March 2015.
Reviewer	Tim Castle, the independent reviewer appointed under section 125 of the MFA.
Te Ohu	Te Ohu Kai Moana Trustee Limited.