



RESERVES POLICY

PROPOSED AUGUST 2020 FOR ANNUAL MEETING CONSULTATION

1. LEGISLATION

1.1 The Meat Board Act 2004 (the Act) provides that the New Zealand Meat Board (the Board) must:

- (a) at all times have a reserves policy;
- (b) consult farmers before setting or changing the reserves policy;
- (c) consult farmers before allocating funds for industry-good projects;
- (d) make the policy available to farmers on request;
- (e) comply with its reserves policy.

1.2 The Board is also required to maintain a prudent level of net assets to avoid jeopardising quota markets and the integrity of the quota management system (section 12(1) of the Act). To the extent that the net assets are not fees paid by quota applicants, they are defined as reserves.

2. BACKGROUND

2.1. This Reserves Policy provides that the Board's reserves will serve three purposes:

- a) to satisfy section 12(1) of the Act (The Board must maintain a prudent level of net assets to avoid jeopardising quota markets and the integrity of quota management systems);
- b) to provide a contingency fund to assist the meat industry's response to any major industry crisis (as provided for in section 8(1)(c)(i) of the Act);
- c) to provide funding for industry-good projects (as provided for in section 8(1)(c)(iii) of the Act).

2.2. The NZMB reserves, their balances and purpose as at 30 September 2020 can be summarised as shown below.

Reserves Held	Purpose
Contingency Fund \$56.1 million	Available for industry crisis funding in export markets, inflation adjusted quarterly
Quota Jeopardy Reserve \$2.54 million	Available for quota management contingencies, inflation adjusted quarterly
General Reserves \$17.4 million	Remaining NZMB Reserves, inflation adjusted quarterly

- 2.3. In order to satisfy purposes a) and b) above, in 2018 net assets of \$2.5 million and \$55 million respectively were retained. This was to ensure that there are sufficient funds to cover the costs of possible quota jeopardy or integrity of quota management system events and have available an adequate contingency fund. The contingency fund (including quota jeopardy) had been capped at \$57.5 million since 2008 without any adjustment for inflation.
- 2.4. In 2017-18 the Board revised its investment policy and a Statement of Investment Policies and Objectives (SIPO) was approved in April 2018. Jarden was appointed Investment Manager in November 2018. The investment policy required investment of the Board's reserves in a balanced portfolio of growth and fixed interest asset classes (held both domestically and offshore) into a managed fund. Investment income will be generated from interest and dividend income in cash and long-term growth from unrealised or realised gains from the value of the investments. The Board has the intention to grow reserves in the medium and longer term.
- 2.5. The Board will inflation adjust Contingency Fund, the Quota Jeopardy Reserve on a quarterly basis from the Investment Fluctuation Reserve.
- 2.6. At 30 September 2020 the balance of the Quota Jeopardy Reserve was \$2.54 million. The Board reviews this reserve every three years. Any reassessment will be based on the Board's view on the likelihood of the need to amend quota administration systems and the extent to which the Board's risks in relation to quota can continue to be mitigated by other means (including insurance).
- 2.7. If there are insufficient quota management reserves to fund these activities in any one year, then the NZMB is required to fund from its general reserves.
- 2.8. At 30 September 2020, the balance of the Contingency Fund was \$56.1 million. The Board remains of the view that, given the likely costs of responding to a major crisis in export markets, where management or recovery might be

assisted by a range of measures such as additional research, auditing and promotion, this amount remains appropriate to be retained. This is reviewed every five years.

3. RESERVES POLICY

- 3.1 It is intended that the Board's quota management systems will be fully funded by applicants for, and users of, quota within the financial year in which the cost arises.
- 3.2 Where, despite the Board's reasonable endeavours, a deficit arises between the quota management fees collected and the actual costs of the system/s in a financial year, that deficit may be met from either income earned on the reserves during the financial year or from general reserves.
- 3.3 If reserves or income from reserves are called upon to meet a deficit in relation to the Board's quota management systems, the Board may, where appropriate and permissible, recover the amount used by way of an increase in fees paid by applicants for quota in subsequent financial years. Any increased fees must be applied to the specific quota(s) whose administration generated the deficit.

- 3.4 If the contingency fund is ever to be called upon, the mechanism for replenishment may be via an adjustment to the levies (within the range set in the relevant levy order/s) collected by Beef + Lamb New Zealand (B+LNZ) in subsequent years. The replenishment of the contingency fund is solely a B+LNZ decision.
- 3.5 The Board's policy regarding use of reserves as a contingency fund is attached as appendix 1 (and forms part of this reserves policy).
- 3.6 The balance of funds retained after setting aside the Contingency Fund and Quota Jeopardy Reserve are held as General Reserves and totalled \$15.7 million as at 30 September 2019) excluding the Investment Fluctuation Reserve (refer 3.8).
- 3.7 Grant funding for Industry Good projects is available from cashflow generated from interest and dividends from the investment portfolio (which includes the Quota Jeopardy and Contingency Funds and General Reserves) after reserve management costs.
- 3.8 Investment income arising from unrealised and realised gains or losses from the investment portfolio is reported in the Investment Fluctuation Reserve (which had a surplus of \$2.276 million surplus at 30 September 2019).
- 3.9 Where the Investment Fluctuation Reserve is in surplus and after providing for the maintenance of real value of reserves, the Board may elect to set aside funds into an Investment Reserve Buffer Account. The Investment Reserve Buffer account may be available at the Board's discretion, for industry good funding in any year when interest and dividend returns are not sufficient to fund reserves management expenditure and committed grants. The Board has an objective to build an Investment Reserve Buffer of three years of industry good funding being \$5.7 million.
- 3.10 If reserve management activities (excluding the movement in the Investment Fluctuation Reserve) incurs a deficit for any year the Board may elect to fund from the Reserve Buffer Account. No industry good funding can be made available in future years until any prior year reserve management deficits have been recovered.
- 3.11 If the reserves are utilised for the permitted purposes the Board will consider whether the reserves need to be rebuilt to the same level (or a greater or lesser level), and how this might occur.

4. INDUSTRY-GOOD PROJECTS

4.1 Reserves that are surplus to the requirements of purposes a) and b) above (including income not required to maintain the real value the contingency fund) will be available for purpose 3); the funding of industry-good projects (“Projects”). These Projects will be carried out by B+LNZ, and applications for grant funding from B+LNZ will be considered against this policy, and the provisions of the Meat Board Act 2004.

4.2 The guidelines for considering Projects for reserve funding are as follows:

Project Criteria

Projects will:

- be expected to have the potential to lead to a significant shift in the overall positioning/profitability of the sheepmeat and beef industry (the Industry); and
- because of their nature and/or scale fall outside the activities that can be funded, or fully funded, by B+LNZ’s levies; and
- be for the collective good of the Industry.

These projects can include projects partly funded by levies, where reserves are used to supplement that funding.

4.3 Standard Evaluation Criteria

- 4.3.1 All Projects will have to be required to have applied an intervention logic methodology which is a representation of clear and well-thought-out understanding how the planned project actions are expected to lead to desired outcomes. Only projects with an expected positive benefit to the Industry as a whole, that warrants the level of investment will be considered.
- 4.3.2 Where benefits to the industry are likely to be taken, at the initial stages, by participants outside the farm gate, such participants will be required to make cash or in-kind contributions.
- 4.3.3 A similar project must not be being undertaken concurrently by B+LNZ or by other participants in the industry.
- 4.3.4 Projects should only be considered to the extent that they are “industry-good”, in that they would be unlikely to occur without NZMB grant funding.
- 4.3.5 While Projects should be industry wide in ultimate impact, this does not preclude funding of partnerships with individual industry participants.
- 4.3.6 NZMB grant funding can be provided for over multiple years however must be subject an annual funding application.

5. Standard process of review of Projects

Grant funding for all Projects will be based on annual milestones. Where milestones are not met, the Board may cease funding of that Project.

6. Benefit to Livestock farmers

The Board's reserves stem from income received on behalf of beef and sheepmeat producers, the primary benefit from a project should be to beef and sheepmeat producers.

7. Exceptional circumstances

If in the Board's opinion, exceptional circumstances exist in relation to an application for funding of a project that is outside of the criteria set out above, approval may be given provided the project is consistent with the object of the Board, the potential return on the investment justifies the investment and that the rationale for such an approach is minuted by the Board.

8. Consultation

8.1 The Meat Board Act 2004 prevents the Board from funding Projects unless it has first consulted livestock farmers. While the Board may choose to consult independently, B+LNZ will provide the Board with the opportunity to consult livestock farmers in B+LNZ's annual consultation.

8.2 The Board will ensure that farmers can participate in consultation, including by providing appropriate notice of the means of consultation and information regarding the proposed projects for funding.

8.3 The Board will need to seek assurance from B+LNZ that, for any grant funding application made that is of sufficient value to trigger "*Significant Transaction*" or "*Major Transaction*" provisions of the B+LNZ Ltd Constitution and the Companies Act 1993, the required approvals have been obtained by B+LNZ.

9. Review

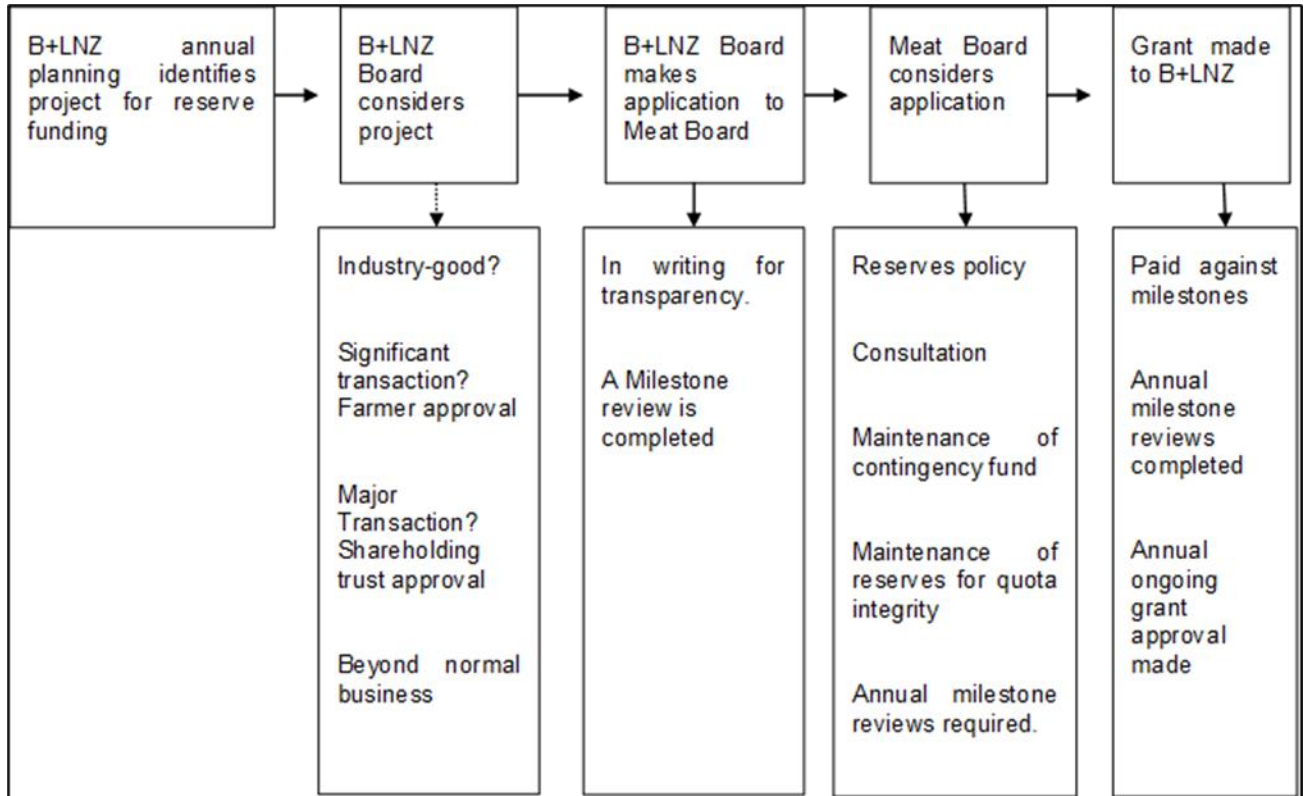
Review periods are scheduled as follows:

- This Reserves Policy will be reviewed three-yearly or earlier at the Board's discretion.
- The reserve policy for quota jeopardy will be reviewed three-yearly, the next being due in 2023
- The Contingency Fund Policy will be reviewed five-yearly the next review being due in 2024

Livestock farmers will be consulted before any changes are approved.

10. Process

The process by which B+LNZ will apply for funding from the Board is set out in the following diagram.





POLICY FOR MANAGEMENT OF THE CONTINGENCY FUND

Reviewed and Approved December 2019

One of the purposes for which the Board may use reserves is to provide a contingency fund to assist the red meat sector's response to a major crisis. That use is governed by the following criteria.

CRITERIA FOR USE OF THE FUND:

1. Scope and coverage

- To all categories of beef and sheep meat products.
- To a crisis or crises considered likely to significantly affect the good standing of New Zealand products in all markets and/or where access to a major market or markets is significantly affected.
- Where the category of meat may be downgraded in the mind of consumers, thus reducing demand, even where the issue poses no genuine product quality or safety issue, for example atypical BSE, or where it has arisen in product from a country other than New Zealand, e.g. residues in grass fed beef from Australia.
- Only to developments affecting the good standing of New Zealand product that are regarded as impacting on a national basis (this would include fraudulent actions and other misdemeanours committed by processor/exporters if it is considered that the image of NZ industry/product is affected and the impact would be on the majority of New Zealand product from any single species or multiple species from which meat products are produced).
- Not to be made available to meet any charges imposed by New Zealand government or local authorities for activities undertaken to manage a risk or to avoid a risk situation occurring.
- Only to activities undertaken for the good of the industry, rather than a single or limited group of industry participants. For example, management of a whole of sector response to foot and mouth disease or generic promotion of the benefits of New Zealand red meat (or a type of red meat) following a residues issue.
- The fund may be utilised on activities including, but not limited to, the following:
 - Coordination of crisis activities and communications
 - Provision of specialist advice and support to levy payers and agencies leading any response to a sector crisis
 - Advocacy on behalf of the red meat sector during a crisis
 - Market research/public relations.
 - Trade and Consumer promotion including advertising.
 - Establishment and audit of quality control/food safety programmes.

- Sponsored travel to New Zealand by overseas customers/media to view mitigation systems put in place.
- Research to gain understanding of the nature of the event in order to provide factual information aimed at restoring customer confidence, or research to defend New Zealand's market access position, e.g. by opposing a safeguard action implemented by an overseas authority which results in loss, reduction or restriction of access to a market.
- Legal expenses incurred in defending the interests of the sector where seriously defamed by a third party

2. Guidelines to be taken into consideration in determining the level of funding for any event

Given the relatively limited ability to replenish the Contingency fund in between Referenda (undertaken either six-yearly or through holding a special referendum if considered justified) guidelines have been established in relation to the level of funding that the Board may draw upon for any event. These are:

- A "fundamental crisis" would rank highest and would justify drawing heavily upon the fund. A fundamental crisis would currently include FMD and BSE outbreaks (including detection of atypical BSE). These are considered the two most likely events that could result in the loss of access in major markets and affect consumer confidence for food safety reasons or impact on future demand, because of substitution with other products during the time access is banned. These events are likely to require a high level of expenditure to restore consumer confidence. The Board may declare other events as being a "fundamental crisis" from time to time. These may include loss of access to a major market or markets through, for example, an anti-dumping or safeguard action being taken against New Zealand meat imports by a foreign Government, or other regulatory action by a foreign Government which causes a major disruption in trade. Again, an effective response to the impact of these circumstances may require a high level of expenditure.
- In general, other major crises not at the level of a fundamental crisis would justify spending at a level that still leaves a reasonable balance in the fund in the event of a subsequent fundamental crisis occurring. Possible events could be:
 - the introduction of scrapie,
 - severe impacts associated with virulent *Escherichia coli*
 - a failure of essential systems such as NAIT to pass external audit
 - major residue contamination.
- Additionally, the threat of either a major or fundamental crisis occurring may, of itself, be a major crisis warranting use of the fund.
- Events that only directly impact on public/consumer confidence in the domestic New Zealand market may none-the-less constitute major crises and warrant use of the fund, particularly where it is necessary to mitigate negative international publicity, that may spill over.

3. Management

- In considering a major industry crisis, the Board will be guided by B+LNZ, which will initially determine if a developing crisis might warrant a response involving use of the contingency fund. In that event, B+LNZ shall immediately appraise the Board of the circumstances, its assessment of the risks, and the steps being taken to manage the situation. If B+LNZ determines that the use of the contingency fund is warranted, it will prepare recommendations outlining a plan of action to respond to the crisis by, for example, managing recovery of customer, consumer, and legislator confidence in New Zealand meat, fighting a loss of market access situation and/or developing alternate markets (Crisis Response Plan). The nature of the situation is likely to require a prompt decision on the recommendations by the Board.
- The Board may approve B+LNZ committing up to \$100,000 of Contingency fund monies for R&D and/or market research/consultancy to enable initial scoping of a crisis in order to assist in developing a Crisis Response Plan.
- If a major sector crisis requires funds to be spent, the Board will provide those funds to B+LNZ, to carry out activities in accordance with the Crisis Response Plan prepared by B+LNZ and approved by the Board.
- B+LNZ shall be required to regularly report to the Board on outcomes against the approved Crisis Response Plan. The frequency of reports will be provided for in the plan.
- B+LNZ may at any time make further recommendations to the Board to modify or amend the Crisis Response Plan.
- The Board shall determine, based on advice received from B+LNZ, when implementation of the Crisis Response Plan has been completed, and funding from the Contingency Fund is no longer required.
- B+LNZ shall be required to evaluate the effectiveness of the Crisis Response Plan and its implementation and report the outcome to the Board.
- The Board recognizes that other organisations, including Government agencies and those directly affected, may have primary responsibility in responding to a major industry crisis.
- B+LNZ has developed and maintains a generic industry crisis plan, this has been applied to a Foot and Mouth outbreak scenario for New Zealand. The last review of the industry crisis plan was completed in 2019 and this will be next reviewed in the 2023-24 financial year.

4. Management of Foreign Currency Exposure

The foreign currency exposure for the Contingency fund is incorporated in the Statement of Investment Policies and Objectives as well as in the Crisis Management Strategy and half the portfolio is held in foreign currency denominated investments.

5. Checklist for the Contingency Fund Application

1. Has there been an appropriate level of consultation undertaken with stakeholders including meat processors and exporters, Federated Farmers and government organisations such as MFAT and MPI in determining whether a crisis situation warrants use of the contingency fund, bearing in mind the provenance of the fund, the urgency of the situation, and the need to act quickly where appropriate.

2. Has a fundamental or major crisis occurred, is one developing, or threatening to develop?
 - a. Is the crisis likely to significantly affect the good standing of New Zealand product in all markets or in major markets?
 - b. Is the crisis likely to significantly affect market access?
 - c. Is the crisis likely to result in negative impacts on customer or consumer preferences for categories of NZ origin red meat?
 - d. Is the crisis likely to impact on a national basis?
 - e. Over what term is the impact likely to be felt?
 - f. What is the potential cost to the industry of the crisis?
3. Who will bear most of this cost? Were they responsible? Can or should they pay?
4. Is any remedial action undertaken likely to have significant impact on the likely financial loss?
5. Does sufficient information and skills exist within B+LNZ to scope the crisis or are additional resources needed e.g. policy, advocacy, market research, legal, analytical, promotional and PR consultancy skills?
6. Can such additional resources be funded by B+LNZ through savings in its budgeted activities that are likely to be irrelevant in the event of a crisis?
7. Is additional funding to provide for scoping the crisis required?
8. What level of funds are available at the time a crisis arises: how long is it before there will be an opportunity to seek levy payer approval to replenish the fund?
9. Where appropriate, has there been consultation with other organisations who have undertaken programmes in response to crisis situations.
10. Is it possible to leverage additional funds to assist in responding to the crisis, e.g. meat companies, government?