

Submission to the Commerce Commission
on
The proposed merger of Foodstuffs North Island and Foodstuffs South Island

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Background

The proposed merger between Foodstuffs North Island (NI) and Foodstuffs South Island (SI) raises some very legitimate concerns about competition in the sector which has been raised by other submitters to the proposal.

My concerns revolve around the future stability, ownership and control of the merged entity, and these are related to the potential instabilities within the larger of the two merging entities – Foodstuffs North Island.

Facts:

The following facts are reported by the entities themselves to the Companies Register via submissions or documents, and are thus not readily disputable by these companies.

- 1) Foodstuffs SI is a cooperative company, and its shares are relatively evenly distributed among a large body of shareholders, the largest reported holding being c. 4%.
- 2) Foodstuffs NI is a private limited company with two forms of common share ('A', voting & 'B', non-voting). 92% of these common shares are held by another private limited company (Strategic Interchange Ltd.). The remainder (<10%) of the 'A' & 'B' shares are distributed among the store owners in much the same way as is observed in Foodstuffs SI.
- 3) Foodstuffs NI also has a third class of shares 'C' shares. The voting rights of these shares are outlined in the most recently submitted constitution of Foodstuffs NI. 'C' shares have no voting rights unless a 'triggering event' occurs. These triggering events are listed and described in the constitution and involve events related to attempts to change ownership or take over the company.
- 4) If a triggering event does occur then these 'C' shares have either considerable or overwhelming power at any meeting that they may be deployed at. In the case of special meetings 'C' shares have votes equal to one third of 'A' share votes cast plus ten (considerable), and in a regular meeting the voting power of the 'C' shares is all 'A' share votes cast plus ten (overwhelming).
- 5) There are only fifty 'C' shares on issue. All of these 'C' shares are held in another plc, 'Tetrad Ltd.'
- 6) Both Strategic Interchange and Tetrad appear to non-trading 'shell' entities. Both have a board of four members, and these two boards are the same for both companies. These four directors are also listed as owners of 100% of the shares in these two companies.

7) The four gentlemen are listed below. None are currently Foodstuffs 'store owners':

Peter James Anderson	(Ex Foodstuffs NI store owner)
Murray Peter Jordan	(Ex CEO Foodstuffs NI)
John Francis Street	(Ex Foodstuffs NI store owner)
Martin James Wiseman	(Lawyer, partner DLI Piper)

It should be stated directly that this submission in no way questions the integrity or the motives of these four gentlemen. It addresses the circumstances and the organisational structure within which they are operating.

8) Foodstuffs NI is NOT listed as the ultimate holding company of either Strategic Interchange Ltd. or Tetrad Ltd. No ultimate holding company is identified in either case.

9) The constitutions of Tetrad Ltd. and Strategic Interchange Ltd. do not seem to depart in any major way from the 'bog standard' constitution of a shell private limited company (plc), and this appears to apply to the rights/obligations of the directors and shareholders.

10) There is no evidence in the filed documents to suggest that Foodstuffs NI Ltd. have any direct call, ownership or control over the directors of Tetrad Ltd. and Strategic Interchange Ltd. and the assets that they own.

11) The four gentlemen above who are identified as director/owners of Tetrad Ltd. and Strategic Interchange Ltd. are also listed as the four 'Protection and Perpetuation Trustees' in literature supplied by Foodstuffs NI Ltd. to the Companies Register, Commerce Commission and the general public.

12) It is NOT known if being a Foodstuffs NI 'protection and perpetuation trustee' also makes you, as of right/appointment, an owner director of Strategic Interchange Ltd. and Tetrad Ltd., but it is not an unreasonable deduction to make on the basis reported historical arrivals/departures from these roles.

13) It would appear that the trust deeds of the Protection and Perpetuation Trust and any connected documentation are not required to be filed in any accessible register. There may also be other relevant trusts.

14) Consequently, these documents do not appear to be publicly available, and they do not appear to have been made available or published by the Commerce Commission as part of this merger application.

15) The constitution of Foodstuffs NI (filed 2013) has a set of 'Paramount Principles'. These are shown in the screenshot below. These paramount principles govern the organisation. They are not widely disseminated, and they are not entirely aligned with the aims, objectives and nature of the organisation as it is represented on their website. This particularly applies to Principle Three and its requirement to support hereditary succession to co-op assets within families. This 'paramount principle' is somewhat at odds with the 'jolly-apple-cheeked-grocer-boy-made-good-from-the-packing-room-floor' image which is commonly represented.

1.0 COOPERATIVE PRINCIPLES

Paramount Principle

- 1.1 (a) It is declared as a matter of paramount principle and policy that:
- (i) The Company is the cornerstone and organisational heart of the mutual cooperative organisation of independent grocers (comprising Shareholders of the Company) owning and operating their own businesses which has been built around the Company and is known collectively as "Foodstuffs" or "Foodstuffs Members";
 - (ii) The Company is guardian of the cooperative principles on which such organisation is based and has the responsibility to preserve, protect, perpetuate and promote the organisation and to work for the mutual benefit of all members of the organisation;
 - (iii) Family Succession: The Company recognises family values; the Company encourages family progression to ownership of a Grocery Business and to the role of a Qualifying Individual or Operating Principal in respect of a Foodstuffs Member.
- (b) This Constitution shall be given a full, fair and liberal interpretation and issues arising in relation to it shall be determined in such manner as shall be consistent with and shall best give effect to the above principle and policy, facilitate the carrying out of such responsibility and ensure the continuing operation and advancement of such cooperative organisation.

Loyalty of Shareholders and Directors to Paramount Principle

- 1.2 (a) By accepting membership of the Company, a Shareholder:
- (i) Makes a commitment and undertakes a duty to uphold and promote the Paramount Principle;
 - (ii) Undertakes to deal with the Shares held by the Shareholder and

16) The constitution goes on over several pages to firmly commit store 'owners' to these paramount principles. It does appear that the four director/share owners of Tetrad and Strategic Interchange are covered by these arrangements, but some ambiguity may exist.

17) However, considerable ambiguity exists as to how the behaviour of the four director/trustees might be guided by these paramount principles when deploying their overwhelming ownership and voting power within Foodstuffs NI. Principle 1 simply describes the company as it is, not how it might be, and is thus irrelevant as a guide of trustee behaviour. Principle 3 likewise is entirely concerned with individual owner inheritance of co-operative assets in whatever form, and is thus largely irrelevant. This leaves Principle 2, and this principle is dangerously vague. Any moderately competent corporate takeover lawyer could easily justify deploying Tetrad/Strategic Interchange votes to sell out the company to a third-party purchase on the basis that such a course of action was the best way to "preserve and perpetuate the organisation" and was also "for the mutual benefit for all members of the organisation".

18) It is notable that the 'C' shares are clearly designed to prevent any takeover, but there is an assumption that they will do so by being voted against any such proposal. However, this writer can find no document that directly compels the four director shareholders of Tetrad/Strategic Interchange to vote in this manner under those circumstances. Indeed, an interpretation of the manner given under the previous point may well justify the opposite course of action. If no such safeguard exists, then these 'C' shares, far from blocking any takeover attempt, might actually serve to guarantee its success.

Commentary

- 1) The facts above reveal Foodstuffs SI to be exactly what it claims to be, a wholly store owner held co-operative.
- 2) However, Foodstuffs NI is revealed to be no such thing. It is a plc. Moreover, it is a plc with a concerningly distorted shareholding that appears to place the purported 'owners' of this company utterly at the mercy of four gentlemen who are not store owners, but who between them own and control more than 92% of one kind of voting share ('A' shares) and 100% of the other critical voting shares ('C' shares).
- 3) Not only do these arrangements place the Foodstuffs NI 'owners' entirely at the mercy of this quartet, it also places 65% of the population of the North Island in a similar position with regard to a system that supplies them with the essentials of life.
- 4) The concentration of such power into the hands of just four individuals inevitably reduces the future stability of any organisation – whoever those four people may happen to be. It is a simple matter of inertia, or rather the lack of it.
- 5) Given this ownership structure it is possible for these four gentlemen to sell their Strategic Interchange/Tetrad shares blocks to a third party. Their overwhelming voting power in both 'A' and 'C' shares makes this sale a foregone conclusion. The fact that these four gentlemen 'own' more than 90% of the shares would also allow the (overseas) purchaser of the Tetrad/Strategic Interchange share blocks to buy out the remaining 'owners' compulsorily.
- 4) There may be systems in place to prevent the scenario above occurring, but they are either dangerously ambiguous/weak (the Paramount Principles) or they are not yet in the public domain (The deeds of the Protection and Perpetuation Trust and its supporting documentation)....or they do not exist. To this list of uncertain protections may be added the doubtful protection of the Overseas Investment Office
- 5) There appears to be not much detail about how this merger is going to work on an organisational level, and it has not yet been noted to the necessary degree within this process as to just how different those two organisations are.
- 6) Given these differences, and the potential instability of the Foodstuffs NI corporate/trust structure. It would seem that it would be highly desirable for a number of reasons that the merged organisation should be based on the organisational structure of Foodstuffs SI rather than that of Foodstuffs NI.

Recommendations

These only relate to the issue of stability of the eventual organisation, not to any other drawbacks of the merger with regard to the welfare of the wider community. These are significant and have been extensively addressed by other submitters.

The Commerce Commission should:

- 1) Require that all documentation relating to the establishment and function of the Protection and Perpetuation Trust., Tetrad Ltd. and Strategic Interchange Ltd. should be surrendered, unredacted, to the Commission, and that this information should be promptly placed entirely in the public domain. While the leaders of this organisation may claim that these arrangements are entirely

their own business, the fact that they are relevant to the stability of a system that supplies the essentials of life to 65% of this nation's citizenry makes it everybody's business. The future stability of any proposed merged entity cannot be properly assessed without it.

2) Require a commentary to be supplied by Foodstuffs NI/SI as to how these arrangements will contribute to the protection and preservation of the organisation and its objectives. This commentary may or may not be credible, and most certainly should not be assumed to be so.

3) That the Commerce Commission consider these inputs, but proceed on the basis that the true co-operative structure of Foodstuffs SI is the superior model for the eventual outcome, and that the Commission only permit this merger if Tetrad Ltd. Strategic Interchange Ltd. and the Protection and Preservation Trust are all wound up and the assets that they hold are distributed pro-rata to members of the merged Foodstuffs NZ organisation under a proper co-operative company structure.

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