

The Treasury

New Zealand Aluminium Smelters (NZAS) Information Release

September 2013

Release Document

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- [1] 9(2)(a) - to protect the privacy of natural persons, including deceased people
- [2] 9(2)(b)(ii) - to protect the commercial position of the person who supplied the information, or who is the subject of the information
- [3] 9(2)(f)(iv) - to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials
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- [5] 9(2)(i) - to enable the Crown to carry out commercial activities without disadvantage or prejudice
- [6] 9(2)(j) - to enable the Crown to negotiate without disadvantage or prejudice
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- [8] 9(2)(h) – to maintain professional legal privilege

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In preparing this Information Release, the Treasury has considered the public interest considerations in section 9(1) of the Official Information Act.

Treasury Report: Update on Project 14

Date:	21 September 2012	Report No:	T2012/2375
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Action Sought

	Action Sought	Deadline
Minister of Finance (Hon Bill English)	Discuss with officials at our meeting on Monday 24 September	4pm Monday 24 September 2012
Associate Minister of Finance (Hon Steven Joyce)	Discuss with officials at our meeting on Monday 24 September	4pm Monday 24 September 2012
Minister for State Owned Enterprises (Hon Tony Ryall)	Discuss with officials at our meeting on Monday 24 September	4pm Monday 24 September 2012

Contact for Telephone Discussion (if required)

Name	Position	Telephone		1st Contact
Juston Anderson	Senior Analyst, Commercial Transactions Group	04 890 7211	[1]	✓
Andrew Blazey	Manager, Commercial Transactions Group	04 917 6985	[1]	

Actions for the Minister's Office Staff (if required)

None.

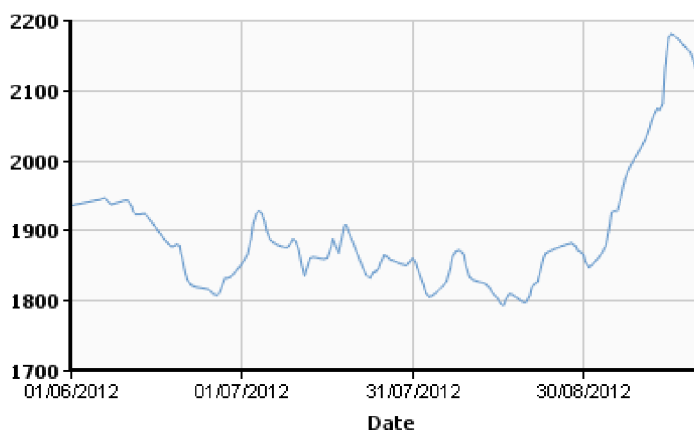
Enclosure: No

Treasury Report: Update on Project 14

1. On Monday 17 September Meridian met with Pacific Aluminium (PA) to discuss PA's request to change the electricity pricing contract it has with Meridian. As you know, PA had requested that Meridian reduce the price of electricity that PA pays under the CFD by roughly^[2,5], from 1 January 2013.
2. [2,6]
3. After Ministers declined to meet with PA, discussions between Meridian and PA resumed. Those discussions have now concluded, and PA management have returned to Brisbane to consider their position. PA's view is that it has been unable to secure a "commercial outcome" from discussions with Meridian, and therefore the future of the smelter is still uncertain. PA management have said that they will need to discuss options for the smelter with the ultimate owners of NZAS, Rio Tinto and Sumitomo.
4. PA also confirmed that it (or Rio) will continue to lobby Ministers for intervention. It is possible that to support this, PA or Rio will make public statements that closure of NZAS is an option, or is likely.
5. [4,6]

Possible smelter closure

6. [2]
7. Since PA first approached Meridian in July, aluminium prices (as reported by the London Metals Exchange) have increased by around 15% from a low of around \$US 1,800 to around \$US 2,100 per tonne (although they are now falling again) as shown in the graph below:



8. However, the \$US/NZ exchange rate has also increased over this period, offsetting some of these gains from NZAS' point of view.
9. [2]
10. [2]
11. [2,5,6]

Payments to Meridian under the contract with NZAS

12. Meridian's contract with NZAS is financial in nature, and as such it technically does not require NZAS to continue operating the smelter. The structure of the contract does give strong financial incentives for the smelter to remain open until 1 January 2016 (assuming the terms of the contract are complied with).
13. This is because NZAS is not legally entitled to give notice of its intention to terminate the contract with Meridian until 1 January 2015, and even if it does that, it must still meet its financial obligations to Meridian under the contract until at least 1 January 2016, **unless** the shareholders of NZAS are willing to allow it to renege on its obligations to Meridian (e.g. by going into liquidation).
14. As previously advised, the details of the contract between Meridian and NZAS are commercially sensitive and confidential to the parties, and as such any public comment on the terms of the contract should be avoided.

Site cleanup

15. A further issue that PA or Rio would need to consider is the smelter's obligations to remediate the site at Tiwai Point. There is only limited public information regarding these obligations. A landfill management plan submitted at the time of consent renewal states that "The landfill is included in the Closure Plan for all NZAS operations. The NZAS Closure Plan is reviewed and updated at regular intervals. The current Closure Plan provisions for the landfill are to cover, shape and revegetate the area". The Closure Plan is not a public document.
16. NZAS's financial statements include a provision for rehabilitation and closure of \$226.8 million as at 31 December 2011. Meridian has tested this figure with external parties and it is seen to be a reasonable estimate of what likely closure and remediation costs would be. However, this provision is not backed by a cash reserve and only the assets of NZAS (mostly plant) support it.
17. [2,4]
18. [2,4]

19. [2,6]

Conclusion

20. We continue to advise against Ministers becoming involved in discussions. We believe the strategy of non-involvement is working. [4]

21. Despite PA's view that it cannot reach a "commercial outcome" with Meridian (which PA defines as Meridian agreeing to PA's terms) we believe that a true commercial outcome to the discussions, where NZAS continues to operate, and both Meridian and NZAS are better off than the current contract, is possible. If Rio is acting in a commercial, rational manner then we believe such an outcome is likely (but not guaranteed) – although it may take some time and further difficult negotiations to get there.

22. If PA approaches Ministers again, and Ministers wish to meet, in our view any meeting would more appropriately be with Rio senior management, the likely ultimate decision making party, along with Sumitomo, the other shareholder. Before agreeing to a meeting we suggest Ministers could ask Rio to put in writing its intentions for NZAS.

23. [2,6]

Next steps

24. PA has advised that it will take the next one or two weeks to consider its position. This will most likely involve discussions with Rio Tinto management, as it appears PA management only have the authority to negotiate with Meridian, not the authority to make longer-term decisions about the smelter.

25. We will stay in touch with PA and advise Ministers accordingly.

Recommended Action

We recommend that you:

- a **note** the contents of this report
- b **discuss** with officials at our meeting at 4pm on Monday 24 September

Andrew Blazey
Manager, Commercial Transactions Group

Hon Bill English
Minister of Finance

Hon Steven Joyce
Associate Minister of Finance

Hon Tony Ryall
Minister for State Owned Enterprises