

Kath McIndoe

From: Chris Mackenzie [Chris.Mackenzie@parliament.govt.nz]
Sent: Thursday, 3 April 2008 2:27 p.m.
To: brian.roche@nz.pwc.com
Cc: Pat.Bowler@russellmcveagh.com; William Peet
Subject: Re: Fw: Requested mark up

Attachments: 1 April 2008 The Rail Business.doc



1 April 2008 The
Rail Business...

This document proves that we made the right decision yesterday, based on Pat's advice.

I will leave it to you Pat with William to come back with a set of words (I am not usurping your role Brian) which take us back to where we were yesterday but a couple of comments.

First, they are not to change the Crown's Strategy, if necessary we should reproduce the para 13 verbatim in italics and indicate this is Cabinets words which lead to the mandate that we are operating under;

Secondly, the changes in ii should be on page 2 under the heading "In customer relation terms, this means:" and we need to ensure that we agree that all scenarios are covered;

Thirdly, on page 3 I do not agree with the first and last right of refusal;

Fourthly, are we happy with the dates on page 3?

Lastly, there is no way that we will agree with the land paras.

I think that we make our changes, get it back to Toll and then if necessary go to Auckland tomorrow afternoon to discuss.

Also see that John has been copied into this, that is one closer to Paul.

Regards

Chris

(Chris Mackenzie
Senior Advisor
Deputy Prime Minister's Office
(04) 471 9935 or (021) 799 499)

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brian.roche@nz.pw
c.com

03/04/2008 12:41
pm

To
<Pat.Bowler@russellmcveagh.com>,
<Chris.Mackenzie@parliament.govt.nz
>

cc

Subject

Fw: Requested mark up

See below - just arrived. Please look at it and then we can arrange to discuss.

Regards
Brian
pp Kate

----- Forwarded by Kate J Riley/NZ/FAS/PwC on 03/04/2008 12:38 -----

David Jackson
<djackson@tollnz.
co.nz>

03/04/2008 11:54

Brian Roche/NZ/FAS/PwC@AsiaPac

To

cc

Greg Steele <gsteele@tollnz.co.nz>, Grant
Devonport <gdevonport@tollnz.co.nz>, John Ludeke
(TOLL AU) <john_ludeke@toll.com.au>

Subject

FW: Requested mark up

Brian,

Thank you for the meeting yesterday and the confirmation of the interim TAC arrangements.

Attached is our mark-up of the document as requested. As discussed yesterday, the issue around FCL services is fundamental to the retained business and we have attempted to arrive at a position that is consistent with the assumption around the value of the TTL business, enhance the industry in general and also deliver the governments objectives.

It is important to recap how an indicative value of \$80 million was arrived at for TTL. On 23rd January we responded to William Peet, as to how the TTL business looks today and how it would look after transfer of both IMEX and CT terminals back into Rail. The assumed EBIT of the TTL business moved from around \$13.4m to \$9.3m. William Peet responded on 15th February that "...a business like TTL to sell for an EBIT multiple of 8- 12...on the information you have given us, the enterprise value of TTL could be around \$80m".

It is our view that given both the strategic importance of the FCL business, and the impact to the earnings profile of TTL going forward, this could reduce the value of TTL by as much as \$30 million. The contra is this value would then increase the future earnings of the Rail business, and we should expect to be paid for that increased

value.

In closing, it is our intention now to enter into meaningful discussions around price. We have spent an enormous amount of time and effort in establishing the framework and general terms of an agreement which as it stands today remains precariously placed given the significant distance the parties remain apart. It seems pointless and we are not prepared to waste anymore time on the general terms unless there is a clear indication the we both get to a commercial outcome that we can each live with.

Regards,

David.

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The Rail Business

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- The rail business is a provider of freight services to major industrial and transport companies in New Zealand and operates in a competitive market. The Crown acknowledges that customers will ultimately decide what service they want, therefore the key determinant of its behaviour should be "what's the best solution for the customer":

Deleted: Toll's Position¶
 ¶
 <#>RailCo will provide rail transport services to freight forwarders and other non-rail transport and logistics providers. RailCo will not have relationships with the end customers (other than described in following bullet point). Such relationships will be controlled by freight forwarders.¶
 ¶
 RailCo will deal directly with end customers only where the customer's products are delivered/available direct to or from a rail terminal.

- i. RailCo will offer long term contracts to customers in an effort to guarantee baseload traffics (and revenue) to support the high fixed costs of maintaining the infrastructure and providing broad access for industry to the networks.

Deleted: ¶
Crown's Strategy¶

- ii. The rail customer base will continue to be centred on large customers requiring one or a combination of the following services:

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IMEX (Import / Export) Services:

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Providing unit train services for import and export rail linehaul services from terminal to terminal, customer direct to or from port, or port to port including refrigerated temperature controlled product, inclusive of third party staging points (ie box companies).

Intermodal Services:

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Providing single unit terminal to terminal linehaul including refrigerated services.

Kombi Services:

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Providing wholesale linehaul servies to freight forwarders from terminal / private siding to terminal / private siding including refrigerated services.

Bulk Services:

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Providing rail linehaul services from customer to customer or customer to port. Services include coal, bulk milk, logs, woodchips and fertilizer.

The rail business has no intention of entering the trucking/ logistics/freight forwarding business.

- iii. Rail will service those customers who require rail as a core component of their freight distribution needs. Where other transport service components are required to meet the customer's requirements RailCo will work cooperatively with other service providers (including TTL) to develop a solution that meets the customer's needs, with the parties acknowledging

the importance of each other's contribution in retaining rail volume in a competitive market.

Deleted: RailCo has no present intention of owning trucks. Any services to / from the railhead will be competitively contracted by the rail business or handled by the customer directly (at the customer's option).

- Commercial principles and transparency must apply.
- The rail business will not enter into any restraints of trade or arrangements that limit its future commercial freedom.
- While a transition period in the separation of TTL from the rail business is inevitable, there must be no ongoing non-commercial preference to TTL relative to other freight forwarders / logistics operators. Pricing, service and terms should, however, recognise the relativity of scale of TTL's operations and use of rail services. TTL would expect a "world's best pricing" provision in line with normal commercial practice and in recognition of its status as a major rail customer.
- The parties must co-operate to ensure that existing customer contracts with the Toll group of companies are executed as profitably as possible.
- The future rail and ferry business will be operated on a commercial basis and in a manner supportive of the Government's transport and infrastructure policy direction.

Deleted: commercially

In customer relation terms, this means:

- Rail will work cooperatively with other service providers to develop a solution that meets the customers needs, with the parties acknowledging the importance of each other's contribution in retaining rail volume in a competitive market.
- Rail will deal directly with customers where the customers products are delivered/available direct to or from a rail terminal.
- Rail does not envisage direct relationships with customers regarding LCL transport solutions.

Deleted: may deal directly with customers that have transport requirements for FCL, where it is advantageous for Rail to have a direct relationship with the customer. This may require Rail to contract with a service provider to move the FCL to/from the customer's premises from/to the rail terminal.

We have not yet reviewed this list and do not yet agree on the split.

Some customers will require services which would be provided by both RailCo and TTL. Given RailCo's stated intention of not entering logistics and freight forwarding markets, it is likely that some customers may, if they elect to do so, have accounts with both RailCo and TTL from inception.

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RailCo Customers	TTL Customers

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Other smaller customers not referred to in the table will be allocated by name, following due diligence confirming the services provided to them.

- For Services provided by RailCo between completion and 30 June 2009 (or later, if a bona fide longer term fixed price contract had been signed prior to 31 March 2008, confirmed in due diligence), RailCo will not itself:

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- Provide (either directly or through contract) substitute services to any of the customers which have been allocated to TTL;
- Pursue any customers at all seeking to contract directly to provide consolidation / deconsolidation, trucking not involving warehousing, or warehousing services.

- For services provided by TTL between completion and 30 June 2009 or later if a bona fide longer term fixed price contract had been signed prior to 31 March 2008, confirmed in due diligence) TTL will not itself:

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- Provide (either directly or through contract) substitute services to any customers which have been allocated to RailCo;
- Pursue any customers at all seeking to contract to provide road services in substitution for rail services.

- RailCo expects to co-operate with all services providers who wish to offer bundled services to end customers. However, until 30 June 2009, RailCo will give TTL the first opportunity to do so, without inhibiting RailCo's ability to deal with other services providers. In particular, TTL will have a right of first and last refusal in relation to any proposal delivered directly to RailCo (other than opportunities presented by another freight forwarder or operator).

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- RailCo's intermodal and wagon rates to TTL (by services type and volume) will be agreed with TTL as part of the sale contracts, following due diligence disclosure compared to other forwarders relative to volume, service and terms.

- The areas and rentals to apply for six years for each terminal to be offered to TTL will be agreed as part of the sale contracts, following due diligence disclosure. Rent reviews will be in line with CPI within a cap and collar. There

- should be three 6 year rights of renewal. TTL will have a development right exercisable within the first 4 years of the term, under which TTL will have a right to extend onto land identified as development land. TTL will submit copies of proposed plans when exercising any "development right" option.
- Upon exercising such a right the parties will enter into a new lease for the development site with such lease to have a term of not less than 25 years.

- Service levels, including equipment supply (actual vs ordered/agreed), on time arrival by corridor, and bookings vs travel by corridor) will be included within TTL's rail service agreement.

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