

Tammy Solomon

From: brian.roche@nz.pwc.com
Sent: Wednesday, 9 April 2008 10:23
To: David Jackson
Cc: Chris Mackenzie; murdo.beattie@cam.co.nz; Pat Bowler; William Peet (ONTRACK)
Subject: Meeting 3:00pm Today
Attachments: 67057.pdf; ATT1449566.txt

David,

As requested, here is the note from Dr Cullen. It seeks to address the points we discussed and needs to be seen in the context of our earlier papers.

As I said to you last night, our intention is to discuss this, get feedback from you as to issues/points of clarification and then to address its impact on our legal documentation. We are open to further discussion on what is highlighted.

You will note that it is classified as Commercial Secret but in the interests of moving toward some form of engagement today, I thought it would be helpful. Can you please make sure its circulation is limited to your core team.

Just to confirm, our meeting is at PwC offices (Level 16, 113-119 The Terrace) at 3:00pm. Who will be attending from your team?

Regards

Brian

This email message and attachments are confidential to our organisation and may be subject to legal privilege. If you have received this email in error, please advise the sender immediately and destroy the message and any attachments. If you are not the intended recipient you are notified that any use, distribution, amendment, copying or any action taken or omitted to be taken in reliance of this message or attachments is prohibited. An electronic communication is not received by PricewaterhouseCoopers until the contents of that communication have come to the attention of the person who is the addressee of the electronic communication. Only PricewaterhouseCoopers partners have authority to enter into legal obligations on behalf of PricewaterhouseCoopers.

TO: Chris Mackenzie
FROM: Minister of Finance
DATE: 8 April 2008



1. Negotiations with Toll

Following your briefing on the latest discussions with Toll, I understand that the negotiations are encountering some difficulties around the mechanics of the separation of the rail business (RailCo) from TTL. In particular, Toll appears concerned that the Crown as owner wishes to own trucks and enter the LCL, freight forwarding or logistics businesses.

This memorandum sets out my views on these issues. I would like you to ensure that these views are circulated to the wider Crown negotiating team so that there is no misunderstanding. You can also show this memorandum to the Toll negotiators if you think that would be helpful.

2. Government's Objectives

The Government's objective in acquiring RailCo is to enhance the efficiency and effectiveness of the rail network (including inter-island ferries) and ensure it plays its full part in the future of New Zealand's transport infrastructure.

That requires the Government to have a full set of strategic options for the future. The strategy will be developed by the RailCo Board and, after discussion with the Government, will be incorporated in the SCI. The Government's objectives, incorporated in that SCI, will be determined by its transport and economic goals, and the interests of end customers.

There is no intention for RailCo to own trucks or enter the LCL or logistics businesses, and so I would expect them to enter arrangements with transport suppliers and end customers for FCL traffic.

However, in order to preserve the value of the Crown's potential investment in RailCo, I am not prepared to make any contractual or other undertaking to any third parties (including Toll) that constrain the future strategic or business model choices available to RailCo, other than during the transitional period, as discussed below.

3. Negotiations

From my perspective therefore, the arrangements with Toll need to cover:

- The assets / customers that go with each of RailCo and TTL. As part of this separation I would have no difficulty with transitional arrangements that protect the customer allocations in the separation agreement for a year or two.
- How the parties will work together over the transitional period.



- An end date after which there are no enforceable obligations undertakings or commitments. I want this to be crystal clear because I do not want to create another NRAA type contract where both parties think one document means different things.

4. Solutions

I understand Toll could be interpreting the Crown's unwillingness to include the RailCo strategy in contract documentation as a sign that rail intends to be predatory as regards the TTL business and has an agenda to enter the trucking business.

This is not the case. If Toll need more comfort on this point I would be happy with the following solutions:

- Strengthened undertakings around the RailCo / TTL separation that make the TTL and RailCo cashflows more secure – providing always that these do not constrain RailCo's options following the transition period; or
- The Crown acquires rail and TTL and then sells TTL post-acquisition. If this approach were favoured by Toll I would envisage RailCo offering TTL for sale within twelve months with similar transitional protection afforded to the purchaser but I would not see any preference to Toll being part of any sale process.

5. Next Steps

The pricing of the rail and TTL businesses will need to reflect the terms of the separation arrangements. Therefore, before the parties can have a meaningful price discussion, the following needs to be understood and agreed:

- The proposed transaction documentation, including the separation arrangements
- Financial data that allows the parties to clearly understand the separation of cash flows between RailCo and TTL

Approved / Not Approved

Hon Dr Michael Cullen
Minister of Finance

8.../.../08