

Treasury Report: Rail Project Leadership

Date:	5 September 2007	Treasury Priority:	High
Security Classification:		Report No:	T2007/1712

Action Sought

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Minister of Finance (Hon Dr Michael Cullen)	Agree that accountability for the purchase of Toll NZ be given to ONTRACK	ASAP

Contact for Telephone Discussion (if required)

Name	Position	Telephone	1st Contact
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Enclosure: No

Treasury Report: Rail Project Leadership and Accountability

1. Following on from Ministers' decision on 3 September to start a process leading to Crown purchase of Toll NZ, it is necessary to decide which agency should take the lead in implementing this transaction.
2. There are essentially 2 options for leading the project: ONTRACK or Treasury.
3. While normally the Treasury leads major Crown asset purchases or sales, ONTRACK is an SOE. If as we understand, Ministers are clear that if purchased Toll NZ should be merged into ONTRACK, then the purchase of Toll NZ could be treated simply as a purchase by an SOE of a new business.
4. There are thus two broad options:
 - The Treasury leads the project, and calls on ONTRACK to provide technical rail expertise. In this case the purchase would be funded by an appropriation to Vote: Finance, and then the asset would be passed to ONTRACK at the completion of the transaction. The price and conditions at which the rail operating business passed from the Crown to ONTRACK would be subject to agreement with the ONTRACK board, and might not necessarily be the same as those at which it passed from Toll Holdings to the Crown. Any additional costs to the Treasury from the transaction, over and above what it can reasonably be expected to absorb, would be funded by direct appropriation to the Treasury.
 - ONTRACK leads the project, and Treasury provides some support for ONTRACK in terms of issues such as preparing Cabinet papers. In this case the acquisition, including any transaction costs that ONTRACK cannot be reasonably expected to absorb, would be funded by a capital advance to ONTRACK. Treasury would report independently of ONTRACK on the scale of any capital advance needed.
5. The following are the issues that arise in determining who should lead such a project.
 - a. The process of purchasing Toll NZ will require a substantive commitment of resourcing from whichever organisation leads it, plus outside financial and legal advisors. This would put resourcing pressure on either organisation.
 - b. A joint approach, with shared accountability, will not work well. This is a difficult project, with limited certainty of success. It therefore needs clear accountability from one government agency to Ministers for achieving this.
 - c. ONTRACK has presented a strategy to Ministers, involving presenting a "take-it-or-leave-it" offer to Toll Holdings, based around the scale of their investment in Toll NZ to date. While this strategy is designed to achieve Crown ownership of Toll NZ quickly, and at a reasonable cost, Treasury is not confident that this is the best strategy. If Treasury were in charge of the project, our approach would be to use financial advisors to come to a better understanding of Toll Holding's view of sale; to develop a (likely more realistic) Crown view of both reasonable price, timing and the necessary asset mix, and of bottom lines for price and mix of assets, and to open discussions with Toll Holdings without signalling how determined Ministers are to acquire the asset. In our view the Treasury approach is more likely (but by no means certain) to succeed, but is likely to take more time. If Ministers prefer the ONTRACK approach, clearly it would be better to have ONTRACK implement it.

- d. On balance, Treasury's view is that it is perfectly appropriate for ONTRACK to manage this transaction as an expansion of the scope of business of an SOE. Any other approach will lead to some potential difficulties in transferring the asset from the Crown to ONTRACK. If Ministers are attracted to the strategy ONTRACK has presented to date, it would make particular sense for ONTRACK to implement the transaction. Treasury's role would be to assist ONTRACK in advising Cabinet and to advise you on ONTRACK's capital requirements for the transaction.
6. Given the commercial sensitivity with this project, we have restricted the distribution of this report to your office. You may wish however to share this report with your Associate Ministers.

Recommended Action

We recommend that you **agree** that accountability for the purchase of Toll NZ be given to ONTRACK.

Mike James

Deputy Secretary – Economic Performance Group
for Secretary to the Treasury

Hon Dr Michael Cullen

Minister of Finance