
From: John Wilson
Sent: Friday, 23 March 2007 5:04 p.m.
To: ^MOF: Chris MacKenzie
Cc: Ivan Kwok; Robert Barton
Subject: Summary of where Treasury and Ontrack got to with Toll
Attachments: 952139_1.DOC

Chris

Attached is a summary note on where Ontrack and Treasury have got to with Toll. The pieces in italics are the pieces where either discussion has been very high level, or we have not yet discussed the issue with them, so their agreement cannot be assumed.

Happy to discuss.

John Wilson

Summary of proposal as agreed between Officials and Toll for Cullen/Rowsthorn meeting.

Sections in italics are areas where it should not be assumed Toll accepts the proposition outlined.

1. Access Charges

Option 1: Set to provide Toll NZ a 12.5% rate of return (pre-tax) in each year (start around \$30m pa, rise to over \$93m at the end of 10 years).

Option 2: Set at a fixed level designed to return 12.5 % (pre-tax)

Option 3: *Set at the level established by the Independent Expert for maintenance. (\$56.1 million pa including the results of the Russian roulette process).*

Option 4A: *Start at the level determined by the independent expert, but moves to the level established by the 12.5% return when that latter level exceeds the level determined by the independent expert.*

Option 4B: *Uses the same start and end points as Option 4A, but joins them using a straight line.*

As part of this discussion two linked issues will arise:

- *To the extent that the Independent Expert outcome forms the platform for the TAC, does the “Russian roulette” part of the outcome get included or not?*
- *Toll’s request that, until these issues are resolved, the TAC be retained at \$48million, rather than increased to the outcome of the Independent Expert’s report as per ONTRACK’s request.*

2. Call option

(Discussed only at a high level with Toll)

Key issues:

Should include the operating rail business (including customer contracts)

Assets to be part of the call option should be in a subsidiary.

Basis for exercise of call option

3. Bond

To match expected payment for new rolling stock. Backed by financial institution (Awkward interface with “call option”. *Toll will probably resist having both “call option” and bond.*)

4. “Use it or Lose it” mechanism

- A mix of a use it or lose it regime that pairs a commercially marginal line with a commercially important line, along with contracts for specific payments for the most commercially unviable lines.
- Regime to be structured so that loss of exclusivity allows new operator to carry freight to destination (but not to pick up freight at intermediate points)
- Rail ferry to be part of “use-it-or-lose-it” regime. Loss of rail ferry exclusivity would require Toll to enable any new operator to have all necessary port and traffic rights.
- Toll would have the right to sub-contract without loss of exclusivity
- *Exclusivity on lines not currently served (Castlecliff, Rotorua etc) has been lost.*

- *Provision so that if Toll decides ceases operating on a line segment, that line segment is open for other operators forthwith.*

5. Right of First refusal

Remove Toll's right of first refusal for subsidies where it covers a part of the track where they have lost exclusivity.

Agree a set of principles for freight rates on new line segments, consistent with broader freight rates.

6. Long distance passenger

The revised agreement to provide for Ministers to have a choice (at their timing) between:

- Open access immediately for all services other than the TranzCoastal and the TranzAlpine. (Should also include abolition of the present 12 month stand-down period after toll ceases a service)
- A Crown agreement with Toll to operate the 3 existing services in the interim. The Crown could then choose to build new or refurbished rolling stock, and tender for a hook and pull operation, and for management of the long distance passenger system.

7. Wellington metro

Wellington metro access rights would revert to the Crown immediately, with the existing Toll Agreement with Greater Wellington Regional Council being protected through its 10 year term.

8. Land

- Toll will surrender all tracks/network sets on retained land/ marshalling yards to ONTRACK.
- Toll and the Crown will share land release proceeds 50-50.
- Toll will pay market rates for land not used for basic (as opposed to wider) rail purposes.

9. Clifford Bay

Any pre-existing agreements that could be used to assist a future development of Clifford bay would be made available to the Crown.

10. Other issues

- ONTRACK will be set a target reduction for corporate overheads
- Toll's ONTRACK directorship would terminate.
- Toll and the Crown would establish new mechanisms to provide productive collaboration