
From: John Wilson
Sent: Thursday, 30 August 2007 1:27 p.m.
To: ^Parliament: Nic Blakeley
Cc: ^MOF: Chris MacKenzie; Robert Barton; Stephanie Ward
Subject: Rail paper for Monday
Attachments: 1002665_1.DOC

Nic

Attached as discussed is the rail cabinet paper for Monday.

My understanding is that Dr Cullen wants to take some copies with him to Cabinet on Monday, distribute them for discussion with his colleagues, and then collect them and bring them back from Cabinet.

The papers are Commercial-sensitive as they have implications for 2 listed companies.

Happy to discuss.

John Wilson

MEMORANDUM FOR CABINET

RAIL: TOLL NEW ZEALAND

Proposal

This paper proposes that Cabinet give me authority to start a process with Toll Holdings about a Crown purchase of Toll New Zealand.

Background

Toll New Zealand is the former Tranz Rail (minus the rail tracks). It operates all freight and long-distance passenger trains in New Zealand, the Wellington metro trains, the Interislander ferry service and Tranzlink trucks. Toll Holdings, its dominant shareholder, bought its shareholding as a result of its 2003 takeover of Tranz Rail. In a linked transaction, at that time, the Crown took over the rail network for a nominal \$1, and agreed to pay \$200 million towards refurbishing the track, while Toll agreed to invest \$100 million in the operating business.

The agreement with Toll provided that, once the Crown's \$200 million was used up, Toll would pay the full operating and capital costs of the track. In the event Toll has been no more successful at recovering the full costs of the rail system from its customers than was Tranz Rail. There have consequently been a series of disputes with Toll about access charges. At present Toll is paying \$54 million a year in access charges, which covers less than half of the long-term costs of the track. Beyond that Toll has been arguing that it needs some additional financial support from the Crown before it can commit to purchasing new locomotives and rolling stock. Officials have been exploring with Toll a number of options in that area.

Comment

I have come to the view that, rather than continue this stream of disputes with Toll, a better approach would be to buy Toll NZ (the New Zealand based rail, ferry and truck from Toll Holdings). In doing so I have the following objectives:

- To buy Toll NZ in its entirety rather than just some assets Toll Holdings may wish to sell to us.

- To complete the transaction for a reasonable price.
- To have the substance of the transaction, and any substantive disputes with Toll about it, resolved before the end of calendar 2007.

My intention is that the Toll NZ operation should be merged into ONTRACK. In the immediate term no legislation would be needed to implement that.

I will report back to Cabinet on 8 October on the following issues:

- A more detailed strategy for how to achieve the outcomes set out above.
- Likely financial implications and timing.
- A clear approach to implementing this transaction. While normally Treasury would implement a major Crown commercial transaction, this can be seen as an acquisition by an SOE, which would suggest that ONTRACK should take the lead on this transaction.
- A communications strategy

To implement this project, the Crown will need financial advisers. I will give any financial approvals necessary in the meantime for the appointment of financial advisers.

It is important that at this stage this issue be kept highly confidential. Toll NZ is still listed on the NZ Stock Exchange, although Toll Holdings is in the process of buying it out. Toll Holdings is listed in Australia. This proposal is therefore highly market sensitive.

Recommendations

I recommend that Cabinet

Agree that I start a process leading to the Crown purchasing Toll NZ

Note that my objectives in this process are

- To buy Toll NZ in its entirety
- To complete the transaction for a reasonable price.
- To have the substance of the transaction resolved before the end of calendar 2007.

Agree that I should give any financial approvals necessary for the appointment of financial advisers to the Crown

Note that I will report back to Cabinet on 8 October with more detailed proposals on:

- A more detailed strategy for purchase
- Financial implications and timing.
- Accountabilities for implementing this transaction.
- Communications

Hon Dr Michael Cullen
Minister of Finance

Date: