



Minute of Decision

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KiwiRail Group Turnaround Plan

Portfolios: Finance / State Owned Enterprises / Transport

On 19 April 2010, Cabinet:

Freight network

- 1 **noted** that the KiwiRail Group (KRG) business consists of a commercial rail freight business and the non-commercial metro rail business in Auckland and Wellington;
- 2 **noted** that KRG has submitted a 10-year Turnaround Plan to shareholding Ministers and the Minister of Transport;
- 3 **noted** that the objective of the Turnaround Plan is for KRG to become, within ten years, a sustainable rail freight business that is able to fund its ongoing operating and capital expenditures solely from customer revenue;
- 4 **noted** that the Turnaround Plan envisages total capital expenditure over ten years of approximately \$4.6 billion, of which the Crown is being asked to contribute some \$1.1 billion, largely in the first five years, to complement funding generated from customer revenue;
- 5 **noted** that the Turnaround Plan contemplates the closure and mothballing of minor lines, and that these decisions would be the subject of separate processes;
- 6 **noted** that on 10 February 2010, shareholding Ministers directed officials to:
 - 6.1 undertake a due diligence investigation into the suitability of the engineering, capital, and revenue assumptions embedded within the Turnaround Plan;
 - 6.2 consult significant existing or potential rail freight customers to understand their service expectations and likely response to an improved rail service performance;
 - 6.3 advise on the public policy case reasons for investing in rail;

- 7 **noted** that the findings of the due diligence, consultation, and public policy analysis concluded that:
- 7.1 the status quo rail freight business is not sustainable, and making no change would result in KRG's slow decline and eventual exit as a nationwide freight sector participant;
 - 7.2 the presence of an appropriately configured national rail network (Auckland to Christchurch) offers an option value by preserving a freight transport solution that otherwise might be lost or diminished;
 - 7.3 key customers indicated that improvements in reliability, timeliness performance, and in the quality and availability of rolling stock, would motivate them to put more freight onto rail;
- 8 **noted** that there remain areas where further work is required, including:
- 8.1 a prioritised and costed investment programme, focused on delivering quick results for improving customer services and greater revenue generation;
 - 8.2 identification and mitigation of capacity and capability risks associated with delivering this programme;
 - 8.3 ongoing culture change, including an efficiency programme to secure cost reductions and/or other productivity improvements;
 - 8.4 *information deleted in order to enable the Crown to negotiate without disadvantage or prejudice*
 - 8.5 engagement with stakeholders focused on revenue generation and their ongoing commitment to rail;
- 9 **noted** that the successful implementation of the Turnaround Plan and preservation of a national rail network will require considerable support from stakeholders (unions, management and customers), and that this will stretch KRG's management's capacity and capability to deliver;

Way forward and implications for Budget 2010

- 10 **noted** that the KRG Board and management are seeking the Crown's commitment to the objectives of the Turnaround Plan, and an indication of Ministers' willingness to commit the capital necessary to achieve those objectives over the next five years;
- 11 **noted** that, notwithstanding the considerable risks, shareholding Ministers are satisfied from the due diligence results and from officials' advice that there is a sufficient basis for the government to provide new capital to support the objectives of KRG's Turnaround Plan, but that this support is conditional on the KRG board and management satisfying Ministers that the risks identified in the due diligence process are being addressed;
- 12 **noted** that the Budget 2010 package:
- 12.1 includes a \$250 million capital expenditure (CAPEX) appropriation as a tangible commitment of government support for the objectives of the Turnaround Plan;

- 12.2 notes that the government Turnaround Plan supports a strategy to return KiwiRail to commercial viability that forecasts a Crown contribution of \$750 million CAPEX over the next three years;
- 13 **noted** that in October 2009, Cabinet set aside \$55 million of the between-Budget contingency for KRG to assist them in the event of a cashflow shortfall [CAB Min (09) 37/11], none of which has been drawn down yet;
- 14 **noted** that, for Budget purposes, the unspent contingency (\$55 million) was transferred into the Budget 2010 allocation;
- 15 **noted** that KRG has indicated that it will require \$20 million for cashflow purposes in 2009/10;
- 16 **noted** that the split of funding provided in Budget 2010 is \$20 million for 2009/10 cashflow purposes, with \$230 million to be provided in 2010/11 for the purposes of the KRG Turnaround Plan;
- 17 **noted** that the drawdown of capital injections into KRG is contingent on joint Ministerial approval and Cabinet consideration of specific business cases;
- 18 **noted** that the KRG Board will be required to provide a detailed three-year investment CAPEX profile;
- 19 **noted** that implementation will require enhanced performance reporting to provide Ministers with the assurance that KRG is achieving the desired outcomes from the Crown's investment;
- 20 **noted** that the Minister of Transport and Shareholding Ministers will report to the Cabinet Economic Growth and Infrastructure Committee on a quarterly basis on progress with the KRG Turnaround Plan.

Secretary of the Cabinet

Reference: CAB (10) 185
