

Draft: 27 June 2002

Date:

Parties

WELLINGTON REGIONAL COUNCIL
(WRC)

WRC HOLDINGS LIMITED
(WRC Holdings)

NEW ZEALAND BUS LIMITED
(Stagecoach)

HEADS OF AGREEMENT - TRANZ METRO BUSINESS PUBLIC PRIVATE PARTNERSHIP

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Date:

PARTIES

- (1) WELLINGTON REGIONAL COUNCIL, a local authority at Wellington (*WRC*)
- (2) WRC HOLDINGS LIMITED, a company having its registered office at Wellington (*WRC Ho/dings*)
- (3) NEW ZEALAND BUS LIMITED, a company having its registered office at Wellington (or its nominee) (*Stagecoach*)

BACKGROUND

- A Tranz Rail Holdings Limited (*Tranz Rail Holdings*) is the operator of the Tranz Metro passenger transport business in the Wellington region (the *Tranz Metro Business*).
- B WRC Holdings, a company wholly owned by WRC, and Stagecoach have agreed that they will establish a company, to be called Wellington Regional Rail Limited (or an unincorporated joint venture, if agreed by all of the parties), to acquire the Tranz Metro Business. This Agreement records the expectations and intent of the parties in connection with the formation of the Company and the acquisition and operation of the Tranz Metro Business. It is acknowledged that if the parties decide to establish an unincorporated joint venture to acquire the Tranz Metro Business then this agreement may require amendment.

THE PARTIES AGREE as follows:

1 DEFINITIONS AND CONSTRUCTION

1.1 Defined Terms

In this agreement, unless the context requires otherwise:

Asset Management Plan means the management plan relating to the long term management of the maintenance, enhancement and sustainability of the Company's assets in order to meet the Company's long term objectives;

Business Plan means the business plan to be approved by the Board of the Company in accordance with clause 9 of the Shareholders' Agreement, substantially in the form attached to the Shareholders' Agreement as Schedule 3;

Capital Expenditure Programme means the capital expenditure programme relating to the replacement and refurbishment of the passenger transport rolling stock used in the Tranz Metro Business, and such other capital expenditure requirements as the Participants may agree;

Company means the company to be established by WRC Holdings and Stagecoach, to be called Wellington Regional Rail Limited;

Funding Agreement means the Funding Agreement for the Provision of Suburban Rail Service for Wellington Region between WRC and the Company;

LATE means a local authority trading enterprise, as that term is defined in section 594B of the Local Government Act 1974;

Participants means each of WRC, WRC Holdings and Stagecoach;

Shareholders' Agreement means the shareholders' agreement to be entered into between WRC Holdings and Stagecoach, substantially in the form attached to this agreement as Schedule 2;

Stakeholders include central and local government bodies which have invested money and other resources in the Wellington regional passenger rail transport service from time to time and the local body ratepayers and users of the service;

Tranz Metro Business means the Tranz Metro passenger transport business in the Wellington region.

1.2 Construction

In the construction of this agreement, unless the context requires otherwise:

Business Days: anything required by this agreement to be done on a day which is not a Business Day may be done effectually on the next Business Day;

Clauses and Schedules: a reference to a clause or a schedule is to a clause or schedule of this agreement, and a reference in a schedule to a clause is a reference to a clause in that schedule;

Defined Terms: words or phrases appearing in this agreement with capitalised initial letters are defined terms and have the meanings given to them in this agreement;

Documents: a reference to any document, including this agreement, includes a reference to that document as amended or replaced from time to time;

Headings: headings appear as a matter of convenience and do not affect the construction of this agreement;

Parties: a reference to a party to this agreement or any other document includes that party's personal representatives/successors and permitted assigns;

Person: a reference to a person includes a corporation sole and also a body of persons, whether corporate or unincorporate;

Related Terms: where a word or expression is defined in this agreement' other parts of speech and grammatical forms of that word or expression have corresponding meanings;

Schedules: the schedules form part of this agreement;

Singular, Plural and Gender: the singular includes the plural and vice versa, and words importing one gender include the other genders;

Statutes and Regulations: a reference to an enactment or any regulations is a reference to that enactment or those regulations as amended, or to any enactment or regulations substituted for that enactment or those regulations;

Writing: a reference to "written" or "in writing" includes all modes of presenting or reproducing words, figures and symbols in a tangible and permanently visible form;

2 **CONDITIONS PRECEDENT**

It is acknowledged that WRC Holdings is not obliged to take any action under this agreement until the relevant New Zealand law has been amended to authorise and permit WRC Holdings to take such action. In addition, it is acknowledged that WRC Holdings is a company owned and controlled by WRC, a local authority in New Zealand, and that WRC proposes to undertake a process of public consultation among its ratepayers in the Wellington Region to gauge the level of support for its involvement in the public/private partnership to acquire the Tranz

Metro Business. WRC will only proceed with the transaction, if, in its opinion, there is a sufficient level of public support.

3 PUBLIC/PRIVATE PARTNERSHIP COMPANY

3.1 Subject to the prior satisfaction (or waiver) of the conditions precedent in clause 2:

3.7.7 Incorporation of Company or Establishment of JV

WRC Holdings and Stagecoach will either arrange for the incorporation of a limited liability company under the Companies Act 1993, to be called Wellington Regional Rail Limited, or arrange for the establishment of a partnership or an unincorporated joint venture. The Company will be a LATE. The constitution of the Company will be substantially in the form attached hereto as Schedule 1, and will incorporate any amendments or additions to that form which may be necessary to reflect the resolutions of the issues listed in clause 6.1 below which are reached by the Participants.

3.1.2 Shareholders' Agreement

. WRC Holdings and Stagecoach will enter into a Shareholders' Agreement governing their rights and obligations in respect of the Company and the Tranz Metro Business. The Shareholders' Agreement will be substantially in the form attached as Schedule 2, and will incorporate any amendments or additions to that form which may be necessary to reflect the resolutions of the issues listed in *clause* 6.7 below which are reached by the Participants.

3.1.3 Capital Expenditure Programme

The Participants will prepare a draft Capital Expenditure Programme for the Company which is intended to be adopted by the Company in accordance with clause 9.1 of the Shareholders Agreement.

3.7.4 Asset Management Plan

The Participants will prepare a draft Asset Management Plan for the Company which is intended to be adopted by the Company in accordance with clause 9.3 of the Shareholders Agreement.

3.2 Business Plan

In accordance with clause 9.2 of the Shareholders' Agreement, the Participants agree that the Company will annually approve and adopt a Budget and a Business Plan for the Company, addressing the matters set out in Schedule 5 to the Shareholders' Agreement.

3.3 Statement of Corporate Intent

In accordance with clause 9.4 of the Shareholders' Agreement, the Board will annually approve a Statement of Corporate Intent for the company, addressing the matters set out in Schedule 4 to the Shareholders' Agreement.

3.4 Reporting Requirements

The Company, as a LATE, will have to comply with sections 594S to 594ZD of the Local Government Act 1974. The Company's obligations under those provisions are set out in more detail in clause 9 of the Shareholders' Agreement, and include the obligation to prepare and make publicly available an annual statement of corporate intent containing specified information, a bi-annual report of its operations and annual audited consolidated financial statements.

3.5 Ownership and Control

3.51 The provisions of the Shareholders' Agreement will govern the ownership and control of the Company.

3.5.2 Subject to clause 3.5.3, the Participants intend that the Company will be owned and controlled equally between themselves, in particular:

3.5.2.1 each of the Participants will subscribe for 50% of the initial ordinary share capital of the Company, as described in clause 5.4 of the Shareholders' Agreement; and

3.5.2.2 the Board of the Company shall comprise six Directors. Each of the Participants will be entitled from time to time to appoint up to three of the Directors and to remove any Director so appointed. The right to appoint the chairperson of the Board will alternate annually between WRC Holdings and Stagecoach.

3.5.3 WRC will subscribe for one C Share in the Company, in accordance with clause 5.4 of the Shareholders' Agreement, which will have the rights specified in the Eighth Schedule to the Constitution. Pursuant to clause 35 of the Constitution, the C Share will confer on WRC the right, in specified circumstances, to appoint one Director and to remove any Director so appointed. For the avoidance of doubt, it is acknowledged and agreed that the C Share is not intended to change the scope of the provisions in clauses 7.4 and 7.5 of the Shareholders' Agreement which require unanimous agreement of matters before those matters are pursued or undertaken by the Company.

3.6 Right to Select Future Public/Private Partners

The Board of the Company must unanimously approve any additional Participants who may become shareholders in the Company in addition to

Stagecoach. The pre-emptive rights provisions in the First Schedule to the Constitution and the Second Schedule to the Shareholders' Agreement govern the introduction of any additional Participants in replacement for Stagecoach.

3.7 Leaving the Company

- 3.7.1 When either of the Participants wishes to sell, transfer or otherwise assign its interest in the Company, that Participant must comply with the pre-emptive provisions in the First Schedule to the Constitution and the Second Schedule to the Shareholders' Agreement.
- 3.7.2 The Participants agree that on or about the fifth anniversary of the acquisition of the Tranz Metro Business by the Company, the Participants intend to enter into negotiations as to the possible sale by WRC Holdings of some or all of its shares in the Company to Stagecoach (or to some other person nominated by Stagecoach), and the terms and conditions of such sale, in accordance with clauses 15 and 16 of the Shareholders' Agreement. If WRC Holdings sells all of its shares in the Company to Stagecoach, then WRC will forthwith redeem the C Share.

4 OBJECTIVES OF THE COMPANY

The Participants agree that the primary objectives of the Company will be to:

- 4.1 operate as an efficient and effective rail passenger transport operator;
- 4.2 provide high quality, safe, reliable, sustainable passenger rail transport services to the Wellington region;
- 4.3 operate as a responsible business and effectively manage risk;
- 4.4 protect the investment of and provide a reasonable commercial return to its shareholders;
- 4.5 deliver value for public funds and take account of the interests of the Stakeholders;
- 4.6 be publicly accountable through transparency of information while not compromising commercial sensitivity.

5 EXPECTATIONS OF THE PARTICIPANTS

5.1 Rate of Return on Investment

Stagecoach acknowledges that participation in the Company and the subsequent acquisition of the Tranz Metro Business is a low risk investment. Stagecoach acknowledges that the investment will generate a commensurate return on equity.

5.2 Dividend Policy

The Participants acknowledge and agree that the Company will adopt a dividend policy which reflects their intention to obtain a commercial return on their investment in the Company.

5.3 Re-investment of Surplus Funds

Stagecoach acknowledges that due to the nature of the Tranz Metro Business it will be necessary to re-invest a reasonable proportion of any surplus funds generated by the Company in the Tranz Metro Business and assets, in order to enable the Company to execute its Business Plan and comply with the conditions of the Funding Agreement.

5.4 Future Capital Contributions

The Participants acknowledge that future capital contributions are likely to be necessary in order to ensure the long term sustainability of the business and assets. Such contributions will be shared equally by the Participants.

5.5 Ownership of Rail Infrastructure

The Participants acknowledge that if in acquiring the Tranz Metro Business from Tranz Rail Holdings, the Company acquires (or has the right to acquire) the rail infrastructure network or the right to use the rail infrastructure network on which the Tranz Metro Business is operated, the Company will dispose of its interest in or right to use the rail infrastructure network to WRC (or a company owned and controlled by WRC) for a consideration to be agreed (but which, in any event, is no more or less than the value of the rail infrastructure network in the context of the total consideration paid by the Company to Tranz Rail Holdings for the Tranz Metro Business) and otherwise on terms and conditions which ensure that the Company will continue to have access to and the right to use the rail infrastructure network on terms and conditions reasonably acceptable to the Company and the Participants.

5.6 Scope of Activities

The Company's capacity and powers will be limited in terms of clause 5 of the Company's constitution to those activities which are specified in the Eighth

Schedule to the constitution and which are necessary to further, or are incidental to the furtherance of, the objectives of the Company.

5.7 Long-term Relationship

The Participants intend, pursuant to this Agreement and the further documents and arrangements contemplated by it, to enter into a long-term relationship in order to pursue the objectives and desired outcomes of the Company and each of the Participants.

5.8 Nature of Relationship

The Participants, in their dealings with each other shall, at all times, act in good faith, ethically and fairly towards each other.

6 ISSUES TO BE AGREED

6.1 Outstanding issues

The Participants acknowledge that they will not have access to the accounts and other information relating to the operations of the Tranz Metro Business until some time after the date of this Agreement. As a result, the following issues remain to be resolved between the Participants including, but not limited to:

- 6.1.1 the value of the Tranz Metro Business;
- 6.1.2 the draft Capital Expenditure Programme;
- 6.1.3 the draft Asset Management Plan;
- 6.1.4 the appropriate debt/equity ratio for the Company, including the number of shares in the Company and the price at which those shares will be acquired by each of the Participants;
- 6.1.5 the draft initial Statement of Corporate Intent for the Company;
- 6.1.6 the draft Business Plan and Budget for the first year of operations of the Company;
- 6.1.7 the content of the draft Constitution including, among other things, resolution of the issues identified in Appendix 1 of this agreement; and
- 6.1.8 the content of the draft Shareholders' Agreement including, among other things, resolution of the issues identified in Appendix 2 of this agreement.

6.2 Reasonable endeavours

Each of the Participants will use all reasonable endeavours to agree, in good faith, each of the above issues by 31 March 2003 (or such later date as the Participants may agree).

6.3 Amendment to Shareholders' Agreement and Constitution

The Participants acknowledge that the terms of the Shareholders' Agreement and of the Constitution, in the form attached as Schedules to this Agreement, will be varied as is necessary to reflect the resolutions of the issues listed in clause 6.7 above which are reached by the Participants.

7 TERMINATION OF THIS AGREEMENT

7.1 Termination by Notice in Writing

In the event that the Participants are unable to reach agreement on any of the issues listed in clause 6.7 in accordance with *clause* 6.2 above, either Participant may terminate this Agreement by delivering written notice to that effect to the other Participant.

7.2 Extension of Time for Negotiation

If the Participants have made significant progress towards agreement on the majority of the issues in clause 6.7 above and neither Participant wishes to terminate this Agreement, the Participants may agree in writing to extend the time for negotiating agreement on the outstanding issues to a specified date.

7.3 Binding Nature of Agreement

Except in relation to clauses 8.1, 8.3, 8.5 and 8.6, which shall be binding on the Participants in accordance with their respective terms, the Participants do not intend to be bound by the terms of this agreement. This agreement is intended to be superseded by, and shall be of no further effect once the Participants have entered into, the Shareholders Agreement.

8 MISCELLANEOUS CLAUSES

8.1 Confidentiality

The Participants agree that all information that each of them may acquire from the other Participants or from Tranz Rail Holdings Limited or from their affiliates, agents or advisors in the context of the establishment of the Company and the acquisition and operation of the Tranz Metro Business shall be treated in strictest confidence, will not be used for any other purpose other than the purpose for which the Participant acquired the information and will not be disclosed to any other person (other than the Participant's employees or professional advisors), without the prior written consent of the other Participants.

8.2 Further Assurances

Each of the parties agrees to execute and deliver any documents and to do all things as may reasonably be required to give full effect to this agreement and the further documents contemplated by this agreement according to their true intent.

8.3 Costs

The Participants agree that they will each be responsible for their own costs and expenses (including third party costs and expenses of advisors engaged by each of them) in relation to this agreement and the matters contemplated by this agreement. However, where such costs are incurred by one Participant on behalf of all of the Participants in connection with the matters contemplated by this agreement and all Participants have agreed in writing, in advance of the costs and expenses being incurred, that those costs and expenses will be shared, then those costs will be shared equally between WRC and WRC Holdings, as to half and Stagecoach, as to the other half.

8.4 Time of the Essence

Time shall be of the essence as regards the performance by each of the parties of their respective obligations under this agreement.

8.5 Governing Law

This agreement shall be governed by and construed in accordance with New Zealand law.

8.6 Submission to New Zealand Jurisdiction

Each party irrevocably and unconditionally submits to the exclusive jurisdiction of the courts of New Zealand for the purpose of hearing and determining any disputes or proceedings arising out of or in connection with this agreement.

EXECUTION

Signed for and on behalf of
NEW ZEALAND BUS LIMITED by:

Director/Authorised Person

Director/Authorised Person

Signed for and on behalf of
WELLINGTON REGIONAL COUNCIL
by:

Authorised Person

In the presence of:

Name:

Occupation:

Address:

Signed for and on behalf of
WRC HOLDINGS LIMITED by:

Director/Authorised Person

Director/Authorised Person

**FIRST SCHEDULE:
FORM OF CONSTITUTION OF THE COMPANY**

**SECOND SCHEDULE:
FORM OF SHAREHOLDERS' AGREEMENT**

APPENDIX 1

Stagecoach Legal Comments on draft Constitution

This document comprises what is expected in the governing document of Wellington Rail. It is noted that the Constitution is subordinate to the Shareholders Agreement in the event of any conflict. The C Share provision, whilst unusual, is acceptable in principle, but it should not be used to force future capital expenditure which is not part of the agreed plans.

The document will be amended to reflect final agreements and acquisition terms but requires no critique at this time as for the most part, it is acceptable.

Stagecoach Commercial Comments on draft Constitution

No material comments other than conforming with other comments in paragraph 17 of Stagecoach's Proposal.

APPENDIX 2

Clause	Stagecoach Legal Comments on draft Shareholders' Agreement
5.2	<p>Main operating objective Should be identical to Heads of Agreement. Suggest – add as 5.2.6 - financially successful (accords with 13.15). This should be a fundamental objective.</p>
5.2.8	<p>Deliver value for public funds and protect the investment of stakeholders and shareholders (add italics). The company, through its Directors, should at all times endeavour also to protect the investment of all <i>shareholders</i>.</p>
8.1	<p>Initial funding This clause may require amendment to reflect the actual capital structure adopted for Wellington Rail.</p>
8.2	<p>Further funding As and when the company requires further funds for capital expenditure <i>in accordance with the Business Plan or the Asset Management Plan as agreed by PP (add italics)</i>. The provision of further funding should be, where possible, planned and foreseeable.</p>
9.1.2	<p>An explanation of why participation is a low risk investment needs adding. Suggest – <i>because its likely income shortfall will be made up under a Funding Agreement with the Wellington Regional Council which provides for a reasonable return to shareholders on funds invested and a reward for their introduced expertise as part of a larger subsidy grant which itself is backed by a funding commitment from Transfund.</i></p>
9.1.6	<p>There is a possible confusion between the essentiality of unanimity of Directors under 7.5 and the possibility of resolution by arbitration under clause 24 where indecision affects 'the interests of the company'. For certainty and in relation to future capital requirements, we suggest a new clause 9.1.6:</p> <p style="padding-left: 40px;">9.1.6 <i>The approval of any Business Plan, Budget or Asset Management Plan shall not be a matter that may be resolved in accordance with the provisions of clause 24, even if any non-approval is considered to be a matter affecting the interests of the company. At all times the approval required must be unanimous amongst the Directors, as provided for in</i></p>

	<i>clause 7.5.</i>
9.2	Asset Management Plan This plan should be described as a 29 year plan commencing on the first anniversary of acquisition to be consistent with clause 12 of the Funding Agreement.
10.	Dividend Policy The policy should reflect the objective of <i>providing a reasonable commercial return to shareholders as well as adequate reward for the expertise they bring to Rail Services</i> (as per 5.2 Objective and Background F of the Funding Agreement).
12.	Restraint of trade NZ Bus would need an exemption for current bus services within the Wellington Region.
15.5	One residual director would be unusual – requires discussion.
16.7.	Basis for fixing fair value of shares In addition to the criteria listed, the experts should have regard to: <ul style="list-style-type: none"> • The price paid at acquisition and subsequent capital investment. • The valuation principles and methodology applied at that time • That historical subsidy payments are a continuum. • That the business is a low risk investment. That is as to capital invested as well as income stream. • The commitments under the agreed Business and Asset Management Plans.
18. 18.1.2	Default Fails to observe or perform any of the participants <i>material</i> obligations under this agreement (add the word <i>material</i> otherwise the provision may be arbitrary or oppressive).
26.4	Suggest that consent to the charge or lien over shares <i>should not be unreasonably withheld.</i>
Second Schedule 3.5	Basis for fixing fair value of shares. Further criteria suggested in 16.7 above should be repeated.

Second Schedule 3.6.9	Where the panel of experts cannot agree on fair value, an averaging of values may be more logical than the “mid-assessment” formula suggested. The mid-assessment can fall arbitrarily anywhere between the other two extremes of value.
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Clause	Stagecoach Commercial Comments on draft Shareholders' Agreement
5.7 + 8.1	Payment of Share Capital and Funding These provisions will need to reflect the capital structure ultimately agreed.
6.2	Disposition of Rail Network Conforming change with HOA.
10	Dividend Policy This clause will need to be reviewed in the light of the overall capital structure. However Stagecoach has a clear expectation that it will receive regular dividends (or other cashflows equivalent to dividends) that represent a “reasonable return” to service its own cost of capital. This may be separate from payment for “adequate reward for the expertise which Stagecoach will be providing to the JV Company. Clearly both Stagecoach and WRC have a common goal in ensuring the capital structure is tax effective for both parties, and the capital structure should be established to reflect this.
12.1	Restraint on Trade As WRC will be aware, under this clause Stagecoach would need WRC's approval for it to continue its existing bus business. We expect that this approval would not be withheld.
15.5	Right to Appoint Director Whilst Stagecoach accepts the need for WRC to have an ongoing directorship of the Company, we would like the number of directors specified as one.