

**Report** PE04.280  
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**Committee** Policy, Finance and Strategy Committee  
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## **Draft Contract for the Provision of Urban Rail Services**

### **1. Purpose**

- To obtain approval of the draft Contract for the provision of rail services, to enable negotiations to be commenced with Toll Holdings Ltd.
- To approve the draft Contract being formally put to Transfund New Zealand (Transfund) as a draft Procurement Procedure pursuant to the *Land Transport Management Act 2003*.

### **2. Exclusion of the Public**

Grounds for exclusion of the public under section 48(1) of the *Local Government Official Information and Meetings Act 1987* are:

*That the public conduct of the whole or relevant part of the proceedings of the meeting would be likely to result in disclosure of information for which good reason for withholding would exist, i.e., to allow the carrying out of, without prejudice or disadvantage, commercial negotiations.*

### **3. Background**

Since the last formal contract with Tranz Rail Ltd for the provision of urban rail services lapsed in 1995, rail services have been procured on the basis of short-term contract rollovers.

Initially the inability of Greater Wellington to secure an ongoing commitment from Transfund to fund rail services precluded a longer term being negotiated and latterly the uncertainty over the ownership of both Tranz Metro and Tranz Rail Ltd continued this trend.

A consequence of this series of short-term “rollovers” was that the contract was effectively an operating contract, therefore, there was an unwillingness on the part of Tranz Rail Ltd to commit any funds to capital investment as part of the core contract.

The completion of the refurbishment of the Ganz Mavag electric multiple units was jointly funded by way of a special arrangement with the Council's funding contribution being on top of the ongoing operating subsidy.

This lack of capital investment has resulted in both the English Electric units, which are used predominantly on the Johnsonville line, and the carriages used on the Wairarapa services ageing to the point where they no longer meet passenger expectations as to comfort and reliability.

Also, capacity has not kept pace with growing patronage and a number of services urgently require additional units.

With the takeover of Tranz Rail Ltd by Toll Holdings Ltd, and a review of Transfund funding policies, there is now an opportunity under a sole supply framework to commence negotiations with Toll Holdings Ltd for a long-term contract for the provision of urban rail services.

#### **4. Development of a Draft Contract Document**

In order to secure funding from Transfund, it is necessary to provide both a "business case" to justify a decision to continue to purchase rail services and a "procurement procedure" covering the methodology of the purchase.

The business case has been prepared using the Council's in-house transport model and the results are reported elsewhere on this Order Paper.

Transfund suggested that the best option for a "procurement procedure" was to use the draft Contract Document and have it approved by Transfund as an approved procurement procedure. In order to achieve this, Transfund officers have taken an active part in the development of a draft Contract Document. Both parties agreed to engage ARUP, a Melbourne based transport consultancy to advise on the document. Once the draft Contract has been approved by both the Council and Transfund, any significant changes that occur during negotiations with Toll Holdings Ltd will have to be referred back to Transfund to ensure such changes do not compromise the intent to use the Contract as a "procurement procedure".

Once agreement is reached with Toll Holdings Ltd, the document will be put to both Council and Transfund's board for final approval.

#### **5. The Draft Contract**

A copy of the draft Contract is attached as attachment 1.

The Contract is required to meet Transfund's requirements of "best value for money", with serious consideration of "contracting out" where demonstrably beneficial.

In terms of Greater Wellington, we wanted to avoid the problems of past contracts, recognising that effectively there is only one potential provider of the services and, as a consequence, we have sought to develop an "open book" contract with sufficient safeguards to protect the use of public money.

In order to meet these aims, the draft Contract document to be provided to Toll Holdings Ltd includes the following key principles:

- Rail Operator to be a Separate Legal Entity.

Tranz Metro must be set up as a separate legal entity.

- Open Book Basis

Contract negotiations are to take place on the basis of “open book” disclosure by Tranz Metro.

- Conditions Precedent

Prior to the Contract being signed, the following agreements must be in place:

- An access agreement between Trackco and Toll Holdings Ltd with the Wellington passenger rights assigned to Tranz Metro.
- A 30 year Business Plan agreed by the parties.
- An Asset Management Plan agreed by the parties.

- Business Plan

All business activities will be “driven” by a Business Plan, which will be regularly updated and agreed with Greater Wellington.

- Term of Agreement

The initial term is 10 years, with an option to extend by 5 years on every fifth anniversary up to a maximum of 31 years.

- Fares and Timetables

Greater Wellington will control service levels, train consists and base fares. (Some freedom remains for Tranz Metro to set special fares for special events.)

- Quality of Services

The services must meet the standards set out in schedule 3 of the Contract.

- Infrastructure and Track Access Agreements

These are the responsibility of Toll Holdings Ltd/Tranz Metro but must be approved by Greater Wellington. Those agreements in place at the commencement of the Contract cannot be altered without Greater Wellington approval.

- Asset Management Plan

This document must be maintained for the term of the Contract and include the next 5 years’ activities in detail, with the following 25 years in

outline. It must include the maintenance procedures to be followed for each asset class and a programme for replacement when they are life expired. Compliance with the maintenance procedures in this plan is to be reported on a monthly basis.

- Stations

The minimum quality standard in schedule 3 of the Contract sets down minimum standards for stations.

- Livery

Greater Wellington retains the right to introduce a Region-wide “transport” livery at its cost.

- Payments

Payments are made up of two parts - an operating payment and an agreed payment for capital investment approved. Payments are due on the 20<sup>th</sup> day of the month following.

- Withholding Payments

Where Tranz Metro fails to meet the agreed service levels and standards, there is a schedule setting out sums which will be withheld.

- Adjustment and Review of Funding

Regular funding reviews are set down on an annual basis for the first 5 years, with an option to reduce the frequency beyond that time. Alterations of Government charges trigger an immediate review of funding to make the change neutral to Tranz Metro. Similarly, if Greater Wellington alters fares, the funding will be adjusted to make the change neutral to Tranz Metro.

- Capital Investment

The intent is that each capital investment project would be put to Greater Wellington, with options and sensitivity analysis and part of the approval process will include the method of funding.

- Economic Gain/Loss

Although funding is negotiated on an “open book” basis, the Contract includes a “safety net” for both parties should financial outcomes vary significantly from projections.

When reviewing the funding level as set out above, consideration has to be given to the economic gain or loss.

The activities of the business are considered in accordance with schedule 7 of the Contract, which will demonstrate whether there has been an economic gain or loss. If there has been a gain, 50 percent of it is payable

to Greater Wellington. If there has been a loss, 50 percent of the loss is carried forward into the next assessment period.

If Tranz Metro has not provided the services in an acceptance manner, it forgoes any benefit from this procedure.

- Reporting Requirements

There are comprehensive reporting requirements, so that officers can be confident that the business is being operated to the required standard and that maintenance procedures are being followed.

- Breach and Termination

The Contract may be terminated if:

- The Operator fails to comply with a fundamental condition of the Contract.
- The funding from Transfund ceases or is significantly reduced.
- It becomes illegal for Greater Wellington to continue to fund the services.
- A judgement order of \$1 million or more is made against the operator, insolvency, or an unapproved share sale.

- Step in Rights

If the Contract is terminated as set out above, Greater Wellington has “step in rights” which permit it to take over the assets and continue to provide the rail services while a permanent solution is found. The primary assets are set out in schedule 8 of the Contract.

- Right of Purchase

If Toll Holdings Ltd proposes to sell all or part of Tranz Metro, it must first offer the business to Greater Wellington on the same terms as offered to the potential purchaser. If Greater Wellington declines the offer to purchase, Toll Holdings Ltd may finalise a deal with the potential purchaser but before acceptance must again offer the business to Greater Wellington under the agreed terms. If Greater Wellington again declines, the sale may take place.

- Assignment

Tranz Metro may only assign its rights and obligations under this Contract with the written approval of Greater Wellington.

## 6. Legal Review

Council’s legal advisors have reviewed the draft Contract.

Although they are generally happy with the draft contract at this point in the proceedings they have raised a number of issues.

*Conditions Precedent:* It is intended that all these conditions be met before any contract is signed.

*Balance of the Document:* It is conceded that the document is somewhat biased in the favour of Council. In drafting the document we drew on our previous experience with Tranz Rail and ARUP have knowledge of the issues which arose in Melbourne when public transport was contracted out. It is accepted that there will be negotiated changes to the document as part of the agreement process.

*Asset Management Plan:* There have been a number of subsequent amendments to the document reviewed by our legal advisers which address these matters.

*Three Year Reviews:* This relates to obtaining inputs to Council's three year budget process. Normally reviews will centre on 30 June but data for the budget round is required in November.

*Capital Funding:* The document is structured to give Council the greatest flexibility in funding capital. For the reasons raised it is unlikely that we would agree to joint funding of the same asset.

*Step In Rights :* These are now common practice in Australia and are to as far as possible, ensure the service keeps running should the Operator default on the contract. We would strengthen this clause as suggested before forwarding the document to Transfund.

*Tenure :* Although nominal tenure is only 10 years the Operator would receive 5 years notice of either an extension or termination. The 10 years is in keeping with Transfund's planning horizon.

*Track Access Agreements:* Officers are attempting to obtain have the necessary agreements included in any Track Access Agreement.

*Withholding Payments :* These may be altered during the negotiation process however in principle Council should not be required to pay for a service which was not provided.

A further legal review will be commissioned prior to the final agreed Contract being brought back to the Council.

A copy of the memorandum received from Phillips Fox is appended as attachment 2.

## **7. Communications**

The key communications initiatives at this time are with Transfund in terms of finalisation of the draft Contract and with Toll Holdings Ltd in terms of negotiations once the draft Contract has been approved by the Council and Transfund.

## 8. Recommendations

*That the Committee recommend to Council that it:*

- (1) *Receive the report and note its contents.*
- (2) *Approve the draft Contract (including any amendments approved by the Committee) for the provision of rail services.*
- (3) *Agree the draft Contract be put to the Transfund board for approval in principle as an approved procurement procedure.*
- (4) *Agree that, following approval from Transfund, the draft Contract be put before Tranz Metro/Toll Holdings Ltd and negotiations commenced.*
- (5) *Note that, following the completion of negotiations with Tranz Metro/Toll Holdings Ltd, the draft Contract will be referred back to the Council and Transfund for final approval.*

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Attachments:

- 1 Draft Contract for Provision of Rail Services
- 2 Memorandum from Phillips Fox