List of persons interviewed for the purpose of this Review

1. Hon. Jim Marurai, *Prime Minister*
2. Hon. Robert Wigmore, *Former Cabinet Minister, now Deputy Prime Minister*
3. Hon. Wilkie Rasmussen, *Former Cabinet Minister, now Minister of Finance*
4. Hon. William Heather Jnr, *Former MP, now Minister of Works*
5. Hon. Apii Piho, *Former MP, now Minister of Health*
6. Dr Terepai Maoate, *Former DPM and Minister of Finance, now Member of Parliament*
7. Ngamau Munokoa, *Former Cabinet Minister, now Member of Parliament*
8. Tangata Vavia, *Former Cabinet Minister, now Member of Parliament*
9. Kete Ioane, *Former Cabinet Minister, now Member of Parliament*
10. Grover Lee Harmon, *Secretary of Cabinet*
11. Tingika Elikana, *Solicitor General*
12. Sholan Ivaiti, *Former Financial Secretary*
13. Kevin Carr, PERC, *Acting Financial Secretary*
14. Marie Frances, *PERC Chairperson*
15. Navy Epati, *PSC Commissioner*
16. Mac Mokoroa, *Chief of Staff, Office of Prime Minister*
17. Steve Anderson, *President Chamber of Commerce/TAU Board Member*
18. Brian Mason, *Former Chairman, now Budget Review Committee Member*
19. Dallas Young, *Senior Budget & Planning Officer, MFEM*
20. Quentin Thorburn, *Economist, MFEM*
21. Brett Porter, *Toa Owner*
22. Scott Leith, *Toa Consultant*

23. Tony Manarangi, *Barrister & Solicitor/Toa*

24. Timothy Arnold, *Barrister & Solicitor/Triad*

25. Chris Vaile, *Triad Owner*

26. Helen Maunga, *Director of Labour & Consumers Services*

27. Bredina Drollet, *HOM for Ministry of Internal Affairs*

28. Tapi Taio, *Chairman of CIIC, Fuel Importer*

29. Aukino Tairea, *HOM Transport*

30. Nooroa Tou, *CEO Ports Authority*

31. Garth Henderson, *Landowner, TOA Land*

32. Tereapii Timoti, CEO *TAU*

33. Piltz Napa, *Chairman TAU Board*

34. Lloyd Miles, *Acting CEO CIIC*

35. Philip Nicholas, Landowner

36. Mike Parker, EEA Consultant – Interview by questionnaire

37. Peter Walsh, EEA Consultant – Interview by questionnaire

SUMMARY OF GOVERNMENT EXPENDITURE FROM 1 NOVEMBER 2007 TO 18 June 2010

Department	Expenses	Paid	Balance Due
1 **AUDIT OFFICE (Toa Review)**			
Charles Little Legal Fees Triad Proceedings	20,076.95	20,076.95	-
	20,076.95	20,076.95	
Audit Investigation Expenses	59,949.10	50,889.31	9,059.79
	59,949.10	50,889.31	9,059.79
Ernst & Young	6,683.00	6,683.00	-
	6,683.00	6,683.00	
2 **MFEM**			
MFEM POBOC A/C 94017	210,524.19	210,524.19	-
EDI A/C	44,831.05	44,831.05	-
Apex Agency A/C 94930 (Executive Council Order)	1,750,000.00	1,750,000.00	-
Triad Petroleum A/C 94930 (Executive Council Order)	81,101.90	81,101.90	-
	2,086,457.14	2,086,457.14	
3 **DPM SUPPORT OFFICE**			
DPM Support Office Expenses paid by MFEM	263,993.30	180,382.30	83,611.00
	263,993.30	180,382.30	83,611.00
4 **JUSTICE**	8,810.31	8,810.31	-
	8,810.31	8,810.31	-
5 **CROWN**	81,729.67	81,729.67	-
	81,729.67	81,729.67	-
6 **PARLIAMENT**	13,713.40	13,713.40	-
	13,713.40	13,713.40	-
TOTALS	**2,541,412.87**	**2,448,742.08**	**92,670.79**

Note: DPM Support Office Expenses were paid by MFEM due to change of Ministerial Portfolio

Debtors: DPM Support Office	83,611.00
Audit Office	9,059.79
Total Debtors	92,670.79

Implementing a Regulatory Contract
Mobil Oil Australia Pty Ltd, Apex Agencies Ltd trading as TOA Petroleum and the Cook Islands Government's Fuel Price Review Committee

Agreements Reached on Fuel Pricing Template

PREAMBLE
Where as Mobil Oil Australia Pty Ltd are current suppliers of fuel to the Cook Islands and Toa Petroleum Limited, a Cook Islands registered company, act as agents for Mobil Oil Australia Pty Ltd with regard to the distribution and supply of fuel to the Cook Islands and Cook Islands Government representing the regulatory authority with regard to the supply of and pricing of fuel for the Cook Islands. Mobil and Toa are in the process of entering a sale and purchase agreement for the installation currently own by Mobil at Avatiu, Rarotonga. The purpose of this document is to record the intention of the parties prior to the execution of a regulatory contract in relation to a template arrangement for the pricing of fuel.

1) **Basis for costing Fuel**
The cost of fuel ex Singapore will be calculated on the basis of the average of 50% of the daily rates for MOPS and 50% of the daily rates for Posted for the calendar month in which the LCT is loaded in Fiji. A price adjustment application must be filed for each delivery within seven days of the commencement of the following month regardless of whether it is for an increase or decrease.

2) **MR Freight**
The rate for the MR freight will be taken from the last MR loading date in Singapore immediately prior to the loading date for the LCT in Fiji and Mobil shall supply an invoice for verification purpose.

❖ **Insurance/Ocean Loss/Demurrage/MR Port Terminalling Fee**
These rates will not be directly verifiable but the Price Control Tribunal will seek confirmation from its advisor that the rates are reasonable. Should advice be received that the rates are not reasonable Mobil and the Price Tribunal agree to discuss and if necessary Mobil will provide justification for the costs.

3) **LCT Freight**
Mobil will supply evidence verifying these costs to the Price Tribunal's Advisor.

4) **LCT Insurance**
As for Insurance/Ocean Loss/Demurrage/Terminalling Fee above

5) **Wharfage**
Wharfage will be verified by the Price Tribunal based on locally obtained information.

6) **Distribution Costs**

❖ **Actual v Budget**
Distribution costs will be calculated on a six month MAT (moving annual total) of Actuals. The review will take place in August and February for the years ending June and December respectively.

ATM

- **Regional Costs**
  There will be no regional costs following the sale of the Terminal and operations to TOA

- **Review individual costs**
  Mobil/TOA will maintain an adequate financial reporting system and a representative of the Pricing Tribunal and the Ministry of Finance and Economic Management will review the expenses with Mobil/TOA when reviewing the six monthly MAT.

  The commencement distribution costs, as they will apply after the proposed sale, will be reviewed by the representatives of the Pricing Tribunal and Ministry of Finance and Economic Management before the end of June 2006.

- **Costs relating to non regulated operations**

  - **Contracts**
    The non price regulated contracts, after the proposed sale will be included in the total volume that is used to calculate the price order with the exception of Outer Island Energy until such time as Government has completed its review of the policy for the supply of fuel to the Outer Islands. For the avoidance of doubt, Non Price Regulated Contracts shall include the supply of aviation fuel.

  - **Other petroleum fuels**
    After the proposed sale, TOA undertake to ensure that other petroleum fuels bear a fair share of the distribution costs and will show this in their accounts as a deduction from the distribution costs to be included in the pricing template. This calculation will be reviewed as part of the normal six monthly MAT review.

7) **ROI**
In view of the impending sale the ROI will remain unchanged at 25% before tax until after the sale to TOA is completed when it will change to 20% before tax.

8) **Inventory**
The ROI on inventory will remain at 50 days but will be subject to review during the annual review process.

- **Stock piling**
  Government accepts that the high diesel volumes late last year were due to an error and will not reoccur. However Government retains the right to review the situation should it consider the over stocking has reoccurred but before taking any action undertakes to discuss the situation with TOA.

9) **Debtors**
The ROI on debtors will remain at 42 days however subsequent to the proposed sale, shall be reduced to 14 days.

10) **Assets basis of value**
Agreed that historical cost will remain until the proposed sale to TOA is completed, then the basis of valuation will be the purchase price paid by TOA to Mobil of NZ$3.1m plus the historical cost of NZ$.4m being the cost of assets currently held by TOA. This later figure will be subject to confirmation from a review of the records of TOA before the 30 June 2006.

11) **Government preferential rates**
Government preferential prices will be calculated separately using the template rather than making the appropriate levy adjustment to the final price calculated for the regulated volume.

ATM

12) **Basis of volumes**
The non price regulated contracts will in future be included in the total volume that is used to calculate the price order with the exception of Outer Island Energy until such time as Government has completed its review of the policy for the supply of fuel to the Outer Islands. For the avoidance of doubt, Non Price Regulated Contracts shall include the supply of aviation fuel.

Distribution volumes will be calculated on a six month MAT (moving annual total) of Actuals in . The review will take place in August and February for the years ending June and December respectively.

13) **Compensation for lost business**
This issue relates to the situation where the dominant supplier loses volume to a competitor and as a result of the same costs being spread over a lower volume the market price increases. It was agreed that this is a complex issue that could only be addressed by a review of the overall fuel policy for the Cook Islands and should be left to the Review Committee that is to be established by Government to consider.

14) **Regulatory Contract**
As the draft proposed regulatory contract has not been received from the Cook Islands Government advisor it was agreed that this document shall be the basis for the execution of a formal regulatory contract.

15) **Annual Statements and Review**
As TOA's financial year ends on the 30th June it was agreed that a formal annual review would take place each year during August when both the six monthly actual volume and cost review would take place as well as a review of the performance relating to the other elements of the Template.

16) **Rationalisation of LCTs.**
Mobil agree to consider the request to review the LCT policy so that there is a rationalisation of the use of LCTs to avoid the present need for two partly filled tankers to the Cook Islands rather than one.

It was acknowledged that any change to the present policy would have implications for other suppliers and countries and any change must be carefully coordinated.

17) **Premium paid by Toa to Mobil of US$6.40 per barrel.**

There is an arrangement in place between Mobil and Toa that Toa will pay a premium to Mobil of US$6.40 per barrel on the continued supply of fuel after the Mobil/Toa sale. This premium which at current rates equates to about 6.49cents per litre is regarded as security for the continued supply and the continued application of the basis of this template. It also acknowledges Mobil's role which previously was dealt with within their ROI, is now excluded from the calculations. The premium acknowledges that TOA has no expertise in going direct to the market and accordingly represents also a procurement cost, which previously Mobil absorbed and recouped in their ROI. The committee has been advised by both Mobil and Toa that despite the payment of the US$6.40 per barrel premium there are savings to be made under local ownership and these should be reflected in future regulated prices. For the purposes of the template this premium shall be included in the LCT costs and shown as LCT Freight cost and Premium.

18) **TAU**
This document has not addressed any of the issues of the supply of fuel to TAU. These shall have to be the subject of further discussion between TOA and the Cook Islands Government.

ATM

CONCLUSION

The above agreement assumes that the proposed sale of Mobil's operations to Toa will proceed within 6 weeks. In the event that the sale is deferred or abandoned then there are issues that are contained in this document that will have to be renegotiated.

The parties to this document acknowledge the agreements reached through this document and confirm the intention that this document should form the basis of the Regulatory Contract subject to the parties obtaining the appropriate approvals.

Dated at Rarotonga this 14th day of June 2006

....

Mobil Oil Australia Pty Ltd
Andrew McNaught

....

Apex Agencies Ltd trading as TOA Petroleum
Brett Porter

....

Chairman of Fuel Price Review Committee
Cook Islands Government
Kevin Carr

GOVERNMENT OF THE COOK ISLANDS
OFFICE OF THE CABINET SERVICES
GOVERNMENT BUILDING
RAROTONGA, COOK ISLANDS

Telephone:682) 25494
Facsimile:682) 23792

<u>MEMORANDUM</u>

DATE: 10 June 2008

TO: Chief of Staff, Office of the Prime Minister
Acting Solicitor General, Crown Law Office
Financial Secretary, Ministry of Finance and Economic Management

SUBJECT: FUEL REVIEW PRICING COMMITTEE RECOMMENDATIONS

At a Cabinet meeting held on Tuesday, 10 June 2008, Cabinet gave consideration to matters relevant to your Department/Ministry in reference to the above-mentioned subject.

CM (08) 316

Paper dated 9 June 2008

Submitted by the Deputy Prime Minister and Minister of Finance, Hon. Sir. Terepai Maoate, KBE

Approved that the short term recommendations made by the Fuel Pricing Review Committee (FPRC) be implemented; the short term recommendations are as follows:

1. LCT costs; require TOA (ExxonMobil), Air BP and BP (TAU) to review the use of a common LCT to improve tanker utilisation and thereby reduce costs.

2. Fuel Pricing Review Committee to negotiate with TOA to change the current pricing template to be more reasonable to the consumer given the already high costs of fuel on-shore.

3. Introduce National Fuel Supply specifications for Motor Spirit and Diesel.

4. Product (FOB) costs to be verified by reference to daily MOPS quotes which make up the monthly averages.

5. Shipping costs for the MRT deliveries Singapore to Fiji to be verified by seeking copies of the invoices for MRT freight cost for deliveries to Fiji.

6. Implement consistent processes to review on-shore costs for individual companies.

7. Establish clear set of procedures to be developed and issued to on-shore operators to enable annual reviews to be completed.

8. Assess all terminal operations plans and processes to minimise environmental contamination due to leakage and operational spills.

9. Assess all terminals for compliance to relevant engineering and operational standards.

10. Conduct as a minimum, statistical analysis of through puts with pressure testing at locations if leakage is evident.

11. Review current Mark Up allowed by reviewing service station profitability at the high medium and low end of the volume throughputs and propose a change from % based margin to a cents per litre margin.

Approved that the FPRC consult with stakeholders in order to implement the short term recommendations above.

Noted the four (4) options for long term solutions to minimize the increasing costs of fuel. The 4 options are as follows:

1. National Fuel Tender: Government fuel purchasing programme with appropriate asset and operating compliance programmes.

2. National Fuel Tender and On-shore Operator Rationalisation.

3. National Fuel Tender and On-shore Buyout of Existing Operators Assets plus Tender for Single On-shore Operator.

4. National Fuel Tender and Plan to Implement New Terminal Facilities to Replace All Existing Terminals. Tender for On-shore Operator.

Noted once consultations with stakeholders above are done the FPRC will report back to Cabinet on which option is favoured and why.

Approved that the FPRC can start planning to implement the selected option.

Grover Lee Harmon
SECRETARY TO CABINET

GOVERNMENT OF THE COOK ISLANDS
OFFICE OF THE CABINET SERVICES
GOVERNMENT BUILDING
RAROTONGA, COOK ISLANDS

Telephone:682) 25494
Facsimile:682) 23792

MEMORANDUM

DATE: 17 September 2008

TO: Chief Executive Officer, Cook Islands Investment Corporation
Chief of Staff, Office of the Prime Minister
Solicitor General, Crown Law Office
Financial Secretary, Ministry of Finance and Economic Management

SUBJECT: GOVERNMENT PURCHASE OF BP SOUTH WEST PACIFIC (SWP) AVIATION ASSETS ON RAROTONGA

At a Cabinet meeting held on Tuesday, 16 September 2008, Cabinet gave consideration to matters relevant to your Department/Ministry in reference to the above-mentioned subject.

CM (08) 540

Paper dated 15 September 2008

Submitted by the Deputy Prime Minister and Minister of Finance, the Hon. Sir Terepai Maoate, K.B.E (MD)

Approved

1. that the Financial Secretary through his Fuel Consultants (EEA Pty Ltd) can enter into any arrangement on behalf of the Cook Islands Government specifically to acquire the aviation assets currently owned by BP South West Pacific on Rarotonga

2. if applicable that legislation amendments be made to enforce the sale of these aviation assets to the Cook Islands Government by Crown Law Office

3. that the Financial Secretary through his Fuel Consultants (EEA Pty Ltd) appoint an operator for the fuel tank farm once acquisition is successful for a minimum of 12 months

Grover Lee Harmon
SECRETARY TO CABINET

GOVERNMENT OF THE COOK ISLANDS
OFFICE OF THE CABINET SERVICES
GOVERNMENT BUILDING
RAROTONGA, COOK ISLANDS

Telephone:682) 25494
Facsimile:682) 23792

MEMORANDUM

DATE: 7th October 2008

TO: Chief Executive Officer, Cook Islands Investment Corporation
Chief of Staff, Office of the Prime Minister
Solicitor General, Crown Law Office
Financial Secretary, Ministry of Finance and Economic Management

SUBJECT: GOVERNMENT PURCHASE OF ASSETS OWNED BY TOA PETROLEUM ON RAROTONGA

At a Cabinet meeting held on Tuesday, 7th October 2008, Cabinet gave consideration to matters relevant to your Department/Ministry in reference to the above-mentioned subject.

CM (08) 585

Paper dated 7 October 2008

Submitted by the Deputy Prime Minister, the Hon. Sir. Terepai Maoate, KBE

Approved

1. the Financial Secretary through his appointed Fuel Consultants (EEA Pty Ltd) can enter into an arrangement on behalf of the Cook Islands Government specifically to acquire the fuel facility assets owned by TOA Petroleum on Rarotonga.

2. that the Financial Secretary through his appointed Fuel Consultants (EEA Pty Ltd) appoint an operator for the fuel facility assets once acquisition is successful for a minimum of 12 months.

Grover Lee Harmon
SECRETARY TO CABINET

MINISTRY OF FINANCE AND ECONOMIC MANAGEMENT
GOVERNMENT OF THE COOK ISLANDS

PO Box 99, Rarotonga, Cook Islands
Telephone + 682 22878 ♦ Facsimile + 682 23877
EMAIL cifinsec@mfem.gov.ck ♦ http://www.mfem.gov.ck

3rd November 2008

Dallas Young
Treasury Management Division
RAROTONGA

MFEM Supplementary Budget

Kia Orana

Please find listed below initiatives which were not included in the previous 2008/09 Appropriations for which funding is being requested:

1. Government equity injection into BCI [redacted] A fund to be set up by BCI on behalf of Government to provide concessional financing to existing small businesses only that are experiencing difficulties. They will still go through BCI due diligence and MFEM in conjunction with BTIB to develop a policy for this fund which will be administered through BCI. Financing to be set at an interest rate of 4% for a maximum period of 5 years.

2. [redacted] to acquire TOA Petroleum business. This is the maximum amount. Actual amount likely to be less than this. This is extremely confidential for now. Need to generalise this so not obvious in the budget. We are in final negotiations with TOA.

3. Increase the Economic Development POBOC [redacted] wait

4. Potential commencement of Welfare payments in December as opposed to January 2009. Cost for December likely to be about [redacted] If need be this will come out from our reserves in the bank.

FILE COPY

scan

5. [redacted]rom reserves set to construct the Mangaia Harbour.

6. A potential cash bonus injection of at mos[redacted]s a one-off payment. The Threshold increase from $10k - $12k as per Quentin likely to cost the Government $2.6m. MFEM Treasury to brainstorm and come up with options for this to be put in place e.g $200 child bonus in December, or $500 payment to employees earning less than $50k commencing Dec or Jan. This to counter the introduction of 4% COLA as well as possibly increasing the tax free threshold from $10k to $12k.

Justification

Points 1, 4, 5, and 6 to assist with economic incentives for the private sector:

- Targeted to those current businesses experiencing difficulties with their business given the global recession and increasing price of commodities and energy).

- Assist existing businesses with cash-flow issues

- Generate economic activity by putting funds into people's pockets as well as businesses in time of recession.

Points 2:

- This will enable Government to move towards its strategy to nationalise fuel and allow fuel to be acquired and shipped by one supplier. It is envisaged in the long run that the cost of fuel to the Cook Islands will reduce

Point 3:

- This is mainly to fund petroleum consultants who we have employed to negotiate on Government's behalf to achieve our strategy to nationalise fuel in the Cook Islands.

1

Sholan Ivaiti
Financial Secretary

Cc: Sir Terepai Maoate – Deputy Prime Minister and Minister of Finance.
Priscilla Maruariki – Treasury Operations Manager

MINISTRY OF FINANCE AND ECONOMIC MANAGEMENT
GOVERNMENT OF THE COOK ISLANDS

PO Box 99, Rarotonga, Cook Islands
Telephone + 682 22878 ♦ Facsimile + 682 23877
EMAIL cifinsec@mfem.gov.ck ♦ http://www.mfem.gov.ck

4th December 2008

To: Tingika Elikana – Solicitor General

From: Sholan Ivaiti – Financial Secretary

Kia Orana

Heads of Agreement with TOA

I am requesting confirmation from you that the attached document titled; "GOC TOA Heads of Agreement" from a legal point of view is appropriate for me to enter into. By appropriate I mean that there is nothing in this agreement that will significantly disadvantage Government or hold Government liable to a significant financial risk.

Meitaki Maata

Sholan Ivaiti
Financial Secretary

Can you confirm this by signing the below:
I.....TINGIKA.....ELIKANA...as the Solicitor General for the Cook Islands Government have reviewed the "GOC TOA Heads of Agreement" and confirm that this document is legally in order to sign.

Tingika Elikana
Solicitor General

HEADS OF AGREEMENT

BETWEEN

GOVERNMENT OF THE COOK ISLANDS

AND

APEX AGENCIES LTD TRADING AS TOA

1 . 9

AGREEMENT dated this ....4TH.......day of ...December.........2008

BETWEEN

THE GOVERNMENT OF THE COOK ISLANDS acting by and through the Secretary of Finance Sholan Ivaiti of the one part hereinafter referred to as "the Government"

AND

APEX AGENCIES LTD a company registered in Rarotonga Cook Islands trading as TOA of the other part hereinafter referred to as the "TOA"

WHEREAS

a. TOA is the owner of certain Fuel Facility Assets in Rarotonga located at their Avarua Bulk Fuel Terminal including other assets associated with this Facility including delivery and aviation dispensing equipment, office equipment and vehicles and TOA share of external pipelines ("the Assets").

b. The Parties have agreed that TOA will sell and the Government will buy the Assets on terms and conditions more fully set out in this Heads of Agreement.

c. The Parties have agreed to enter a Sale and Purchase Agreement to affect this sale and Purchase of the Assets.

d. The Parties have agreed to enter into a Distribution and Management Agreement for a period of 18 months on completion of the Sale and Purchase appointing TOA as the Distributor under terms and conditions agreed between the Parties.

e. The Parties have agreed that before executing the Sales and Purchase and Distribution Management Agreement that certain due diligence processes are required to be completed.

f. The Parties have agreed that on the satisfactory completion of the due diligence processes they will complete all necessary documentation to affect the Sale and

1200

Purchase Agreement and to document the terms and condition of the Distribution and Management Contract.

g. The Parties have agreed that included in the terms and conditions of the Distribution and Management Agreement will be a revised Cook Island Fuel Pricing Template which will record changes to the methodology used for setting Fuel Pricing in the Cooks Islands. It is the intention of the parties that the revised Cook Island Pricing Template (Schedule 1) will provide for a fixed Management Fee and that the recovery of all other operating or maintenance costs will be on the basis of neither rewarding nor disadvantaging TOA during the course of the Distribution Agreement

h. The Parties acknowledge that TOA is a party to a Bulk Fuel Supply Agreement with Mobil Oil Australia Pty Ltd ("Mobil") for the supply of Petroleum Products dated 4th July 2006 and that this Agreement will continue in TOA's name until its expiry on or before 31st October 2010.

i. The Parties acknowledge that TOA is not a party to an Aviation Technical Services Agreement.

NOW THEREFORE the Parties agree as follows

1. Sale and Purchase

Subject to the terms of this Agreement, TOA agrees;

a. To sell to the Government TOA's Fuel Facility Assets (the Assets) for the sum of NZ$ 5,160,000 and to enter into a Sale and Purchase Agreement with the Government to complete the Sale.

b. To provide the Government with a full list of these Assets confirming they are free of all legal encumbrances, in the case of any assets subject to any encumbrances to undertake to remove such encumbrances before execution.

c. To perform all tasks required to transfer any leases, licences or rights to occupy or use any land associated with the Assets currently in TOA's name that Government requires to be transferred.

2. Distribution and Management Agreement

On execution of the Sale and Purchase Agreement the Government will enter into a Distribution and Management Agreement with TOA appointing them as the Agent to operate and manage the Assets on the following terms;

a. Payment of an annual Management Fee of NZ$ 225,000 per annum paid monthly in arrears as further provided for in the revised Cook Island Fuel Pricing Template. (Schedule 1)
b. Payment of agreed Distribution and Operating costs, as further provided for in the Cook Island Fuel Pricing Template.(Schedule 1)
c. Payment of an agreed return on investment percentage (ROI %) on working capital funds applied for the purchase of Stock and the net impact of funding fuel creditors and debtors, as further provided for in the Cook Island Fuel Pricing Template.(Schedule 1)
d. Payment of agreed annual planned maintenance costs, as further provided for in the Cook Island Fuel Pricing Template.(Schedule 1)
e. The term of the Distribution and Management Agreement will be 18 months from the date upon which the Sale and Purchase Agreement is completed and payment of the sale amount has been made to TOA.
f. The Distribution and Management Agreement will include the revised Cook Island Pricing Template (as set out in Schedule 1) which will be used to set Maximum Wholesale Prices for nominated Petroleum Products and to remunerate TOA their Management Fee, Operating and Maintenance Costs and ROI or such other costs as Government may allow.
g. The Distribution and Management Agreement will include the operating tasks and parameters that TOA as Distributor will be required to comply with including the Health, Safety, Security and Environmental (HSSE) management requirements to operate the Fuel Facility Assets.

3. Due Diligence Process; Asset Integrity

The Government intends to appoint an inspector and or consultants to undertake an inspection of the Assets to determine their fitness for purpose and current state of maintenance and integrity. TOA undertakes to provide all information and their full support to enable this inspection to be completed. The Government will provide a copy of the inspector report to TOA.

4. <u>Due Diligence Process; Environmental Integrity</u>

The Government intends to appoint an inspector and or consultants to undertake an inspection of any sites on which the Assets have been utilised to determine if there has been any spillage of fuels or contamination of the ground. TOA agrees to provide the Government with a copy of the Mobil report prepared as part of TOA acquisition of these Assets in 2006 from Mobil and copies of all incident reporting or other records completed since 2006.

5. <u>Arrangements regarding the Provision of New or Replacement Assets</u>

Government proposes to work with the Distributor to establish if new or replacement Assets are required to enhance the operational integrity and efficiency of the existing Fuel Facility Assets. Any capital investment will be made by the Government.

6. <u>Assignment</u>

Neither Party will during the term of this Heads of Agreement, assign its rights in relation to this Agreement or any other Agreement relating to the Supply of Fuel or Services to a third party without the consent of the Government being obtained in writing.

7. <u>Confidentiality</u>

The Parties agree that the contents of this Heads of Agreement and any other Agreements entered into will remain confidential between the Parties.

8. <u>Communications</u>

The Parties agree that all communications to non related persons or corporations including the media (newspapers, TV, Radio) relating to this Heads of Agreement or any other Agreement relating to the Assets or Fuel Supply be copied to the nominated persons in Clause 11 Notices and their agreement obtained or otherwise before such communication is passed to the non related entity.

9. Transitional arrangements

The Parties agree to meet prior to the commencement of the Distribution and Management Agreement to ensure all matters required to be attended to progress the change to the Distribution and Management Agreement have been addressed.

10. Additional Undertakings

In the event that the Government acquires the BP Aviation Assets at Rarotonga Airport, Government undertakes to enter into a Distribution and Management Aviation Agreement with TOA on the following terms;

a. Aviation Operating Standards and Procedures will be agreed based on an independently sourced Aviation Technical Service Agreement
b. Operating, maintenance and working capital costs will be set in accordance with the same principles as set out in Clause 2 above.
c. In the event that the Parties have completed the Sale and Purchase Agreement contemplated by this Head Of Agreement then the Management Fee for the Distribution and Management Aviation Agreement will be set at $100,000 per annum and will be paid in addition to the Management Fee set out in Clause 2a. above.
d. In the event that the Parties have not completed the Sale and Purchase Agreement contemplated by this Head Of Agreement then the Management Fee for the Distribution and Management Aviation Agreement will be set at $150,000 per annum until such time as the Sale and Purchase Agreement above is completed at which time the Management Fee Aviation and the Management Fee as set out in Clause 2 a above will be adjusted to a combined figure of $325,000 per annum.
e. The Term of the Distribution and Management Aviation Agreement will be a maximum of 18 months or the expiry of the Distribution and Management Agreement whichever occurs first.

11. Notices

Notice given by the Government or TOA will be given in writing and will be delivered or sent by facsimile or post to the following;

To Government

Financial Secretary

Rarotonga

Fax: 23877

Attention Mr. S. Ivaiti

To TOA

Executive

Rarotonga

Fax: 28001

Attention Mr. B. Porter.

12. Costs

Each Party will bear its own costs in regard to the preparation and execution of the Agreement contemplated by and including this Heads of Agreement.

13. Jurisdiction

This Agreement is subject to the laws and jurisdiction of the Cook Islands.

14. VAT and Other Taxes.

Where applicable all fees and charges are plus to VAT or other Government Imposts.

IN WITNESS WHEREOF this Agreement has been executed this .....4TH..........day of ...December...........2008

SIGNED by the FINANCIAL SECRETARY
SHOLAN IVAITI) 04/12/08
on behalf of the Government of Cook Islands)
in the presence of:

M.D. PARKER

SIGNED by the Bill Porter)
on behalf of Apex Agencies Ltd (Trading as TOA))
in the presence of:

Scott Leith.

Director

Auckland.

Schedule 1:

Computation and Administration of the Cooks Islands Pricing Template

Overview of Monthly Price Determinations

Maximum Wholesale Selling Prices (MWSP) for all products are set on a cargo by cargo basis using the pricing components set out below and as set out on the attached (Refer Sch 2 Cooks Islands Pricing Template CIPT)

Product Supply costs

Product Supply costs will be set in accordance with the Mobil / TOA Supply Contract dated 4 July 2006, unless otherwise varied. The Cook Islands Pricing Template indicates the components of the Product Supply costs.

Government taxes and charges

The Agent is responsible to pay all Government-imposed taxes and charges. All Taxes and Charges will be passed through in the MWSP from the date at which any changes in relevant rates become effective. The CIPT indicates the current rates and unit charges which apply for each of the following:

Excise - Principal Petroleum Tax levied by Government: Paid on 20th day of the Month following the month of the cargo discharge

Gross Importer VAT -Value-added Tax rate, which is applied uniformly to all imports; Paid on 20th Month following the month of the cargo discharge

Government/SOE charges.

- Wharfage and Port Charges – Cook Island Port Authority charges for infrastructure and services provided in the port: Paid on receipt of invoices from Authority or as provided.
- Rarotonga Airport Fee- a charge levied by the Airports Authority relating to refuelling of aircraft paid quarterly in arrears

- Government Terminal Fee-a fee levied by Government to recover the cost of the Government's investment in terminal facilities and related infrastructure, Working Capital in relation to the investment, and a Terminal Fee: Paid on Monthly Sales Volumes on the 20 Day of the following month.

- Capital Projects Fee- a charge levied by the Government to recover the costs of any capital expenditure that is required to ensure integrity, safety and efficiency of Terminal operations paid on the 20th Day of the following month

- Other is a provision to recover items not otherwise defined paid on the 20th Day of the following month.

The Agent will be responsible to remit these charges (or any changes to these charges) to the appropriate authority as advised by the due date.

Agent Cost Recoveries

The following Operating Costs and Charges are based on the agreed forward budgets provided by the Distributor. The MWSP will reflect these costs and charges as finally accepted by Government.

- **Local Coastal Tanker Loss.** A cost associated with loss of product in transit and discharging which as per current Supply Contract with Mobil..

- **Annual Terminal Maintenance Charge** A Terminal Maintenance Charge will be allowed in the Pricing Template based on forward estimates agreed between the Government and the Distributor. This Charge is to cover maintenance of the Government Fuel Facilities

- **Annual Management Charge** The Annual Management Charge is to cover the Distributor's management fee only. The volume denominator to be used to compute the Annual Fixed Terminal Charge as a unit rate per litre will be set using the sales volumes for the most recent rolling twelve months period.

- **Annual Operating Charge.** The Annual Terminal Charge covers the Government / Agent agreed budgets for operating the Government's Fuel

Facilities at Rarotonga and for the distribution of petroleum fuels to service stations and to customer's bulk tanks excluding Aviation related dispensing costs.

Outer Islands

Costs associated with transporting fuels to the Outer Islands are to be advised separately.

Agent Exposure

- **Stock Value Gains/Losses.** Under the Supply Agreement with Mobil the Agent purchases fuel based on the pricing components set out in that Agreement. As the MWSP changes on a cargo by cargo basis the Agent has in the past born the cost / benefit of changes in the price on any stock on hand it is holding. Government will now account for the impact of these price timing gains and losses within the Cook Island Pricing Template. The Agent will be required to advise Government the volume of stock they are holding (at Ambient Temperature) for all products on the date cargoes arrive in Rarotonga and an estimate of stock on hand 15 days later (excluding the cargo) ie the date the MWSP is changed. Any stock gain or loss incurred will be fully accounted for by adjusting the setting of the MWSP (Refer Sch 2).
- **Foreign Exchange Rate Correction.** Under the Supply Agreement with Mobil, the Agent prepays for Cargoes of fuel in US dollars 7 days before the Local Coastal Tanker is loaded in Fiji. The Exchange rate used in the MWSP is the average of NZ$ to US$ selling rate for the month of Local Coastal Tanker Loading. The impact of this prepayment and recovery via the MWSP template creates the risk of losses or gains due to exchange variations between date of prepayment and the MWSP. This loss or gain is adjusted on the MWSP to ensure the Agent is neither advantaged nor disadvantaged.
- **Temperature Correction.** Under the Supply Agreement with Mobil, the Agent purchases fuel on a temperature corrected basis at 15C. Under the terms of the Distribution and Management Agreement with Government they sell product at ambient temperature to end customers. The impact of this sale and purchase process is that a volume gain is recovered by the Distributor. The MWSP accounts

for this volume gain by applying standard industry coefficients to the Agent Landed Cost

- **Other.** Government recognises that special circumstances may arise which require the Agent to amend their cost base above or to cover once off events unforseen at the commencement of the contract. Subject to acceptance by Government, a Temporary adjustment will be applied to the MWSP to recover these costs. Costs associated with special circumstances should not be included in any other of the Agents costs.

Working capital financing costs

The MWSP includes a component to allow the Agent to recover the net working capital financing costs of fuel stock, including the impact of paying Government taxes, charges and providing credit to customers. The Working Capital Unit Cost is calculated based on the current month unit cost of stocks, debtors and Government taxes and charges by applying the Government Agreed interest rate.

Government Assets Capital Costs

The Government and the Agent will set annual capital budget for the Fuel Facility assets, all costs of this nature are to the Government's account. In the event that a capital item expended by Governments results in a change to the Distributor's Terminal or Aviation operating costs, then the benefit / cost of this change will be bought to account by a increase or decrease in the Annual Terminal Charge.

SCHEDULE 2

Petroleum Products Pricing Template TOA.

GOVERNMENT OF THE COOK ISLANDS
OFFICE OF THE CABINET SERVICES
GOVERNMENT BUILDING
RAROTONGA, COOK ISLANDS

Telephone:682) 25494
Facsimile:682) 23792

MEMORANDUM

DATE: 3 February 2009

TO: Chief of Staff, Office of the Prime Minister
Solicitor General, Crown Law Office
Financial Secretary, Ministry of Finance and Economic Management

SUBJECT: (INFORMATION PAPER)-ACQUISITION OF TOA PETROLEUM

At a Cabinet meeting held on Tuesday, 3 February 2009, Cabinet gave consideration to matters relevant to your Department/Ministry in reference to the above-mentioned subject.

CM (09) 72

Paper dated 3 February 2009

Submitted by the Deputy Prime Minister and Minister of Finance, the Hon. Sir. Terepai Maoate, KBE

Deferred the paper for next week's Cabinet meeting

Grover Lee Harmon
SECRETARY TO CABINET

MINISTRY OF FINANCE AND ECONOMIC MANAGEMENT
GOVERNMENT OF THE COOK ISLANDS

APPROVED TRAINING ORGANISATION
INSTITUTE OF CHARTERED ACCOUNTANTS AUTHORISED BY NEW ZEALAND

PO Box 99, Rarotonga, Cook Islands
Telephone + 682 22878 ♦ Facsimile + 682 23877
EMAIL cifinsec@mfem.gov.ck ♦ http://www.mfem.gov.ck

2nd February 2009

CABINET PAPER: ACQUISITION OF TOA PETROLEUM

Executive Summary

This paper has been prepared as an information paper for Cabinet regarding the possible acquisition of TOA Petroleum in order to implement the strategy to make fuel cheaper in the Cook Islands for the consumer.

In hindsight the strategy that has been put in place to ensure a fairer price for fuel in the Cook Islands is as follows:

1. Acquire the assets ONLY of TOA Petroleum. Giving the Government access to over **6 million litres of fuel volume**. Note this site has just less than 4 years left on its lease.

2. Then to acquire the BP Juhi fuel facility that has recently been purchased by Fiji Holdings. This will give Government access to **8 million litres of fuel.** This has about 2 years to go on its lease. Government owns the land that this facility is located on.

3. Wait for the current Te Aponga contract (have not seen any to confirm this from Te Aponga Uira) to expire with TRIAD in May 2010. Have access to 7 **million litres** of fuel. In addition the 6 cents a litre charged by TRIAD to store this fuel which the consumer pays is removed.

4. In 2010 consolidate these **21 million litres of fuel** and go out to a national tender for one supplier. The bulk tender will give Government greater purchasing power and a better position to negotiate better prices which will ensure cheaper fuel price for consumers.

1. Acquisition of TOA

After some months of negotiations with TOA the following purchase price was agreed for its ASSETS only at its Panama fuel facility:

Value of assets (tanks, vehicles, pipeline, etc)	$3,000,000
Goodwill (based on future profit projections)	$2,160,000
TOTAL	$5,160,000

Why this $5,160,000?

In 2008 TOA sold 6.5 million litres of fuel (Petrol, Diesel, and Aviation Jet A1 fuel). Government records confirmed that about 3.7 million litres of diesel was purchased in 2008. However we note that subsequent to May 2008 these volumes dropped because of the loss of the contract to supply Te Aponga. Using the last 6 months results for diesel, TOA was bringing an average of 71,000 litres per month. If this was extrapolated over 12 months this would equate to 856,000 litres per annum.

Unleaded petrol volume purchased in 2008 was about 2.3 million litres per annum or about 193,000 litres per month.

TOA also sells about 1.7 million litres per annum of Jet A1 fuel to Air Rarotonga.

To illustrate why we believe that the $5,160,000 price tag was a reasonable deal is reflected in the table where I have made the following assumptions:

- Discounted (taken off) volumes by a further 15%.
- Assumed margins were 20 cents per litre (from price orders received the actual margin is higher).

Please refer to the table below which summarises the above:

FUEL TYPE	LITRES (A)	15% discount in LITRES (B)	(A) - (B)	MARGIN (20 cents per litre)
Diesel	856,000	128,400	727,600	$145,520
Unleaded petrol	2,300,000	345,000	1,955,000	$391,000
Aviation fuel	1,700,000	255,000	1,445,000	$289,000
TOTAL	4,856,000	728,400	4,127,600	**$825,520**

If you multiply the $825,520 x 4 yrs (time on lease) = **3,302,080 (Margin)**

In 2006 the Mobil assets purchased by TOA was $3,491,000. If you were to depreciate these assets by average of 15% using the straight-line method. As at 1st February 2009 the book value of these assets on average would be (I acknowledge that each asset will have different depreciable rates, 15% used as average depreciation to illustrate what the approximate value is of these assets):

Value of assets at 1/07/06	$3,491,000 (A)
Depreciation per annum (15%)	$523,650
2.5 yrs of depreciation	$1,309,125 (B)
(A) – (B)	**$2,181,875**

Total Value = $3,302,080 + $2,181,875
= **$5,483,955**

Government offer = $5,160,000
TOA Asset Value = $5,483,955
Savings = **$323,955**

As the illustration above indicates the deal agreed to was a reasonable one because:

1. The consumer will not have to pay the current financing charges that TOA pays which it passes onto them (13%).

2. Government having access to cheaper financing will only recover the finance charges plus a 1% margin to be used for its own initiatives. The consumer receives savings versus the current position.

3. It removes the fact that whatever TOA constructs from now until mid 2010 the public will not have to pay a 20% Return on Investment (ROI) to TOA.

4. Government has the opportunity now to acquire the ASSETS only of TOA at a much cheaper amount which gives it the opportunity to provide savings to the consumer now. Our estimates are 7 cents per litre.

How Was Government going to Fund this $5,160,000?

Before the passing of the second supplementary budget in November 2008 if Government wanted to pursue the acquisition of key strategic assets (TOA) funding was required. 2 options were able to do this. The first was to use reserves, and the second was to raise a loan. Several donors like ADB and the People's Republic of China were asked if they funded acquisitions of this nature. The responses were not favourable. The local banks were also asked if Government were to borrow from them what rates or proposals could Government expect to get. Interest rates were about the 10% mark. This was not a favourable option.

If Government wanted to pursue this acquisition then the cheapest option at the time was to use Government's reserves. Hence the request to Parliament in November 2008 to use reserve funds to achieve this acquisition of a strategic asset which will see the implementation of our strategy to ensure that the consumer pays a fair price for fuel in 2010.

During this time we were still negotiating this acquisition with TOA, we needed to have a cap so $5.5m was set to achieve this as negotiations were still throwing between $5m and $5.3m.

In December 2008 the Financial Secretary having seen interest rates drop around the world because of the global financial crisis wrote to the 2 banks (Westpac and ANZ) and requested a proposal from each which would preclude government from having to use its reserves ($5.5m) to fund the acquisition.

Westpac and ANZ offered several options, but the most attractive were the variable rates. Westpac offered 8.25%. ANZ offered in the end a variable rate of 7.1%.

Assuming a term of 15 years would mean the following annual payments:

1. Westpac and ANZ in October/November 2008

Term	15 years
Variable rate	**10.25%**
Principle	5,500,000
Annual payments	$719,368

2. Westpac:

Term	15 years
Variable rate	**8.25%**
Principle	5,500,000
Annual payments	$640,293

3. ANZ:

Term	15 years
Variable rate	7.1%
Principle	5,500,000
Annual payments	$596,922

Please note the table 2 and 3 above have variable rates these could go down or up.

However it does illustrate that we are in a more favourable position today to borrow.

The ANZ proposal also gave the government the opportunity to leave its reserves in the bank and still earn interest on these funds.

This opportunity was not available last year.

The Financial Secretary also received a contact from our consultants within OPEC to make an application for a concessional loan to the OPEC Fund as the Samoan Government did when it implemented this strategy. Interest rates are about 1-2% over 20-30 years. The Financial Secretary is putting a proposal together to source this cheaper financing which will mean if approved more savings to the consumer.

If the go ahead is not given this will not be pursued.

Landowners

Throughout this process the Financial Secretary has been negotiating with the family representative on this matter. A proposal was made to the family:

- Goodwill = $500,000 ($250,000 to be paid in yr 1 and $250,000 in yr 2)
- 0.5 cents a litre which equates to about $32,500 p.a based on 6.5 million litres
- This will increase when the Te Aponga Uira Volume is accessed by Government therefore landowners have potential in 2010 to get (7,000,000 + 6,500,000) 13,500,000 x 0.005 = $67,500 per annum

These costs will be recovered through the new pricing template that has been developed.

TOA Acquisition 2009 to 2010 Savings

Back in November 2008 our estimates indicated that between now and mid 2010 cost savings of between NZ$ 0.8m and NZ$ 1.3 million per annum, including GOC recovery for asset depreciation, can be generated by:

- Reduction of TOA's on shore operating costs

- Reduction in Capital ROI through the removal of the current TOA ROI of 20% and the substitution of the GOC ROI of 8%

- Reduction in Local Coastal Tanker (LCT) freight, this will only is achieved if Exxon Mobil and BP SWP are prepared to cooperate in relation to maximising loads on LCTs.

These savings equate to:

If minimum achieved:

NZ $800,000 over 6,500,000	12 cents per litre

If maximum achieved:

NZ $1,300,000 over 6,500,000	20 cents per litre

However when we finalised the new pricing template at the end of January 2008 when all costs were inputted assuming Government had in fact taken ownership of the assets savings to consumers was about 7 cents a litre or $455,000.

The difference is that we are now aware of all the costs that will be involved in acquiring TOA's assets and operating this on behalf of Government.

Government if it does not want to proceed with this will forego the opportunity to implement its overall strategy at the price we have negotiated which from an overall point of view in implementing our strategy is reasonable.

NPV Analysis of this acquisition

Government Return on Investment Rate of Return and Capital Recovery / Depreciation Allowance

8% Investment Rate of Return has been used in the analysis.

Capital Recovery / Depreciation Allowance is based on a 15 year payback period if a longer period is applied then further savings can be identified.

Discounted Cash Flow

The discounted cash flows of the investment post 2010 (depreciation has been removed as a non cash item) results in a Nett Present Value (NPV) of $1.8m on the Capital Acquisition costs of $5.2m with a payback period of 2.83 years, based on 15% return before tax.

15% has been used as the discount factor as it believed to represent what a Commercial Entity in the Cooks would borrow money at. Clearly a reduction in this results in improved NPV and pay back period.

NPV					
Rate	15%	2009	2010	2011	2012
	Investment	$5,160,000			
	Net savings	$1,734,295	$1,734,295	$3,386,438	$3,386,438
	Nett Present Value	$1,822,304			
	PayPack Years	2.83			

What this table illustrates is that if we had to borrow at 15% to acquire TOA the results are still positive in that we will get savings of about $1.7m per annum. Meaning we can repay our investment in over just 2 years then in 2011 can give even more savings to the consumer once consolidation of other volumes is achieved.

We also have a positive Nett Present Value (NPV) of $1,822,304 indicating a sound investment even if rates were at 15%.

Using Governments rate of 8% (7.1% + 0.9% buffer)

NPV					
Rate	8%	2009	2010	2011	2012
	Investment	-$5,160,000			
	Net savings	$1,734,295	$1,734,295	$3,386,438	$3,386,438
	Nett Present Value	$3,110,104			
	Pay Pack Years	1.66			

With Government's financing potential from ANZ the pay back period is only 1.66 years. And the NPV = $3,110,104.

An excellent and sound investment for Government to proceed with this project.

2. <u>Acquisition of BP JUHI</u>

To date we have had continual negotiations with BP Juhi to acquire its assets. There is about 2 years left on this lease. The urgency to acquire the aviation assets of this facility is not as important as that of the TOA assets given the short term of lease to expire at the beginning of 2011.

However back in November/December 2008 BP SWP sold its operations to Fiji Holdings Ltd. They are still going through a transitional phase.

If we are not pursing the acquisition of TOA it is pointless to proceed with the acquisition of aviation assets also in Panama.

However if Government wishes to pursue this second step this would have given Government access to in excess of 8,000,000 litres of aviation fuel and in a better bargaining position to negotiate cheaper fuel for consumers through maximising transporting efficiencies.

We have had some resistance from BP regarding Government's wish to acquire these assets. Hence we advised BP that we would consider price ordering Jet A1 fuel. There is no risk to the airlines as this will require Air BP to justify their costing to the airlines. Government will review and ensure that these costs are reasonable.

3. Te Aponga Uira (TAU) Volume

In May 2010 when the contract to supply fuel by BP (we have not to this date confirmed whether such a contract exists) ends and the storage of its fuel by TRIAD at a cost of 6 cents per litre (0.06 x 7,000,000 = $420,000 per annum) also ends.

Our proposition for Government was to direct TAU not to renew this contract as Government would like to pool this volume (7,000,000 litres of diesel per annum) together with other volumes of TOA and BP.

Total volume of fuel = 6,500,000 + 8,000,000 + 7,000,000 = 21,500,000.

This will then increase the Government's negotiating and purchase power to negotiate better rates.

4. What are the estimated savings?

2010 and onwards
From mid 2010 cost savings increase to NZ$ 3.39m per annum
This is achieved through;

- Reduction in Supplier Margins through the implementation of a competitive National Bulk Fuel Tender for all Petroleum products (this will include current TOA, TAU and BP Jet volumes)
- Reduction in LCT freight cost under the National Bulk Fuel Tender
- Reduction in the cost of servicing the TAU volume as this will now be marginally costed

- The continuing cost savings achieved from the pre 2010 period above

Current Operators TOA and BP will be required to purchase their fuel requirement under the National Fuel Tender either ex the LCT or ex the TOA terminal.

The NZ$3.39m savings are inclusive of;

- A Capital Recovery or Depreciation Allowance over 15 years to recover the TOA acquisition cost
- A provision for Fuel Facility Management costs to ensure operator compliance to pricing and operating standards. GOC has the option of structuring the ongoing management in any way that it sees fit, though for the analysis it is important to reflect a cost.

The Cost Savings are summarised as follows

Area	Savings NZ Dollars Millions
TOA	$1,577,690
TOA/ Outer Islands	$156,610
BP/TAU/TRIAD	$1,491,220
Air BP	$160,920
Total Savings	$3,386,440

- The savings from TOA will give 7 cents per litre
- The savings from BP JUHI will give 2 cents per litre
- The savings from TAU/TRIAD 6.75 cents per litre

Estimated savings 15.75 cents per litre

This does not include potential to negotiate other savings from the increased purchasing power and opportunity to bulk purchase.

If other suppliers and operators like TRIAD decides to also bring their volume and include it as part of Government's tender of fuel supply this will also provide added savings.

Government may want to consider if it does move ahead with its strategy to also acquire TRIAD assets to access their volume. More work though is required in this area.

5. Retailer Margins

As part of our strategy it is advisable that we change how margins are determined for retailers.

At the moment this is determined by % basis. 14.5% to be exact

If the price of fuel increase retailers earn more however if this trend reverses as it has retailers earn less. This hurts the smaller retailer even more because the margins they got when price was high is not there anymore. So they have fewer saving to spend on purchasing more stock. The following table illustrates this:

	Price without Margin	Price with Margin (14.5%).	Margin in cents per litre
High Petrol price (cents per litre)	2.20	2.52	32
Low Petrol price (cents per litre)	1.80	2.06	26

High Petrol Price

	Volume of Retailer sold monthly	Margin (cents per litre)	Margin made
Small retailer	2,000	0.32	$640
Large retailer	10,000	0.32	$3,200

Low Petrol Price

	Volume of Retailer sold monthly	Margin (cents per litre)	Margin made
Small retailer	2,000	0.26	$520
Large retailer	10,000	0.26	$2,600

Our recommendation is that the % margin be changed to a cent per litre margin so that regardless whether the price for fuel increases or decreases retailers will get their cents per litre margin. For them to make more margins they have to increase the volume they sell.

Under this scenario of cents per litre margin the small retailers are protected.

2. True costs are charged to the consumer and businesses through a new pricing template that can be easily audited	2. Consumers have to pay the ROI made by operators which is at least 20%
3. Safety and environmental standards are maintained	3. Consumers have to pay the freight costs for each separate operator. Consumers will not enjoy the savings had we adopted the consolidation of volume
4. Any increases globally on price of fuel the impact under Government's strategy will minimise these to consumers and businesses alike.	4. The price of fuel rises significantly in the short to medium term, consumer pay higher prices. This could impact 2010 elections
	5. Deal with the added costs of 5 suppliers for a limited volume.
	6. Mobil Exxon may charge an added amount equivalent to USD$6 per barrel to the consumer because agreed volumes with TOA have not been achieved because of the loss to the TAU volume as per supplier agreement. This is retrospective from June 2008.
	7. The costs to this later will be much more costly for Government to achieve. In 2004 Government had the opportunity to buy MOBIL assets for about $3.4million much less that what we have negotiated today.

7. Recommendation

It is clear from the work done and numbers crunched the position recommended for Government to pursue in order to ensure that the Cook Islands (Consumers/businesses) pay a fair price for fuel is to implement the proposed strategy to acquire key assets and consolidate volumes to enhance purchasing power and ability to negotiate a more favourable deal. Achieved by tendering the supply of fuel for 3 yrs – 5 yrs through consolidation of volume. And also tendering the management and operation of these assets to the Private sector (ideally having one operator). Government stays out of business.

My advice is to pursue with this to ensure that our people pay a fair price for fuel. Whereas currently they are not. Otherwise may god help us when the price of fuel increases in the future.

KPMG

Office Address
Parakura House
Rarotonga
Cook Islands

Mail Address
PO Box 691
Rarotonga
Cook Islands

Telephone: (682) 20486
Fax: (682) 21486
email: office@kpmg.co.ck

The Directors
Triad Pacific Petroleum Limited
PO Box 264
RAROTONGA

11 May 2009

Attention: **Mr Chris Vaile**

Dear Chris,

Re: **Cabinet Paper dated 2 February 2009 : Acquisition of Toa Petroleum**

You have requested us to review and comment on the above mentioned Cabinet Paper, specifically in relation to the method of valuation and application of same and the amount of goodwill for the proposed purchase from Toa Petroleum ("TOA"). We also comment on the profitability (or otherwise) and the cash flow of the proposal, and add some areas of concerns we have identified. Page references are to the bold numbering at the bottom right of each page (we have received pages 370 – 381 from you).

Summary

We summarise the matters which we have considered as follows:

1. The method of valuation detailed in the Cabinet Paper is fundamentally incorrect and accordingly the assets are grossly overvalued.
2. There is no basis established in the Cabinet Paper for the purported value of $2,160,000 for goodwill.
3. From figures provided in the Cabinet Paper we conclude that the operation of the TOA assets by Government will result in a significant accounting loss for a number of years.
4. Furthermore, again based on the Cabinet Paper figures, there will be a cash flow deficit for a number of years.
5. A number of other matters in the Cabinet Paper need further detail or clarification, are difficult to follow and are possibly incorrect.

We comment in detail on each of the above matters as follows:

1. Valuation

We have been requested to comment on the methodology of valuation and the application of those methods. We have not been requested to undertake a valuation. If one was to undertake a valuation the following items of information would normally be required:

- historical financial statements for up to five years:
- the most recent operating results [and cash flows]:
- the most recent statement of financial position, including commitments and contingencies;
- the company's constitution;
- the company's business plan;
- other future orientated financial information such as budgets, forecasts and projections:
- list of key staff;
- other information unique to the business or industry.

We do not have such information and we thus base our comments solely on the information in the Cabinet Paper.

There are four generally accepted methods of valuing a business. These are briefly described as follows: -

a. The dividend method – this is appropriate where there is no control of the company and typically used for valuations of shares of public listed companies.

b. Capitalisation of earnings method – this is often the most appropriate method of valuation for privately owned and profitable businesses. This method assumes a sustainable level of future earnings and applies an appropriate multiple to these earnings.

c. Discounted cash flows method – (similar to capitalisation of earnings method), forecasted cash flows are discounted back to the valuation date, generating a net present value for the cash flow stream of the business.

d. Net asset value method – this is appropriate where there is control of the company and the value lies in the underlying assets and not the ongoing operations of the business. It assumes the assets are easily valued and readily saleable. If appropriate, a premium to reflect the value of intangible assets not recorded on the balance sheet can be included.

The Capitalisation of Earnings method reviews the recent annual profitability of a business, estimates the future maintainable earnings (excluding interest and tax), and divides this by the purchaser's required return percentage to give the Capitalisation of Earnings value. As can be seen at the bottom of Pg 371 the figure used of $825,520 is the annual projected gross sales margin of the operation. The correct figure to be used is maintainable earnings, which takes into account all operating and overhead expenses (except interest). No consideration has been given in the Cabinet Paper for operating and overhead costs such as insurance, salaries and wages, repairs and maintenance, management costs, land owners rental, depreciation expense and amortization of goodwill. Obviously in all businesses Net Earnings is significantly less than the Gross Profit (gross margin). This method requires a review of actual costs and profits, rather than be based on theoretical gross margins.

The net assets method of valuation should use an independent and recent valuation of assets. It will be noted at the top of page 372 that the Cabinet Paper accepts the depreciated value of TOA. No comment is made as to whether any valuation has been carried out to assess the quality of these assets and therefore their value. It appears the original purchase price when TOA purchased from Mobil, less depreciation, is accepted as a correct value. There is no evidence given to support this. Furthermore the short term remaining on the lease raises questions as to the appropriateness of this method (this is discussed in detail later).

While the application of both methods used in the Cabinet Paper are subject to doubt, of **greater concern is that the Cabinet Paper combines the two methods and arrives at a valuation of $5,483,955. Based on the two (questionable applications) of the Cabinet Paper methods this overstates the value of the business by over two million dollars.** The price of $5,483,955 is some two million greater than the (erroneous) gross margin method, and some three million greater than the current vendor's book value.

The purported savings of $323,955 shown on page 372 are non existent.

Furthermore, we note that in 2004 Government had the opportunity to buy the Mobil assets for $3,400,000 (Pg 380), and TOA did purchase the assets for $3,491,000 (according to pg 372) in 2006. The lease has half the years remaining now than in 2004 and assets values will have decreased. Ignoring all valuation methods, what reason is there that has increased the value to $5,483,955?.

2. Goodwill

The concept of goodwill is often misunderstood in relation to business valuation, and is very subjective. In the Cook Islands it is often further confused with Goodwill paid on the purchase of a lease.

Business goodwill can arise from a number of factors. These include an existing operation, a niche market, strong customer and supplier networks, key staff, monopoly or dominant market positionand legal protection or legal constraints on competition. Such factors contribute to the business earning greater profits than competitors or than industry norms.

Typically in a business valuation the Goodwill will be the difference between the value of a business based on a capitalization of profits method and the value based on a net tangible assets valuation. This recognizes that the complete business operation has more value than the value of the individual assets that make up the business.

Goodwill needs to be substantiated by a careful analysis of the vendor's recent Financial Statements and a clear understanding as to why "superior" profits are generated.

Assuming the book value of the assets is realistic at $2,181,875, and that the Gross Margin is correct at $825,520, with further operating and overhead costs to be recognized which will decrease the net profit (detailed later), we question if there is any goodwill attributable to the vendor's business.

We note towards the top of Pg 371 beside the word "Goodwill" there is the narration "based on future profit projections" then the figure $2,160,000. This is the only reference to goodwill, and we are unaware how this figure is arrived at. **Based on the detail in the Cabinet Paper, and without proof of existing vendor profits, we do not believe that there is vendor goodwill of $2,160,000.**

Auditing standards require a robust analysis of any Goodwill carried on companies' balance sheets, and if there exists any impairment to the stated value, such impairment must be written down.

3. Profitability

According to the Cabinet Paper the proposed Gross Margin of the operation will be $825,520 (pg 371). We note this is based on a discount of 15% of volume ie 728,400 litres. For the benefit of the Cabinet Paper's proposal we will add back the 20 cents margin to our calculation ($145,680). A number of expenses need to be deducted from the Gross Margin to arrive at the profitability of this operation. These are as follows:

a. Interest expense – the minimum interest rate shown on pg 373 is 7.1%. That page notes that this is based on a variable rate and could go up or down. The term is for 15 years so the rate could vary significantly over the term of the loan. The principal repayments are shown as $596,922. Assuming a monthly repayment of $49,744 we calculate the interest expense portion of this to be $383,648 for the first year and $368,003 for the second year.

b. Depreciation expense – while it is acknowledged that different assets depreciate at different rates, pg 372 suggests an average rate of 15%. We comment further on the appropriateness of this rate later in this report. Assume a new lease is negotiated and apply a depreciation rate of 15% to the proposed asset value of $3,000,000, then the annual depreciation expense will be $450,000.

c. Landowners' expenses – while the paper acknowledges that negotiations to extend the lease are continuing, and therefore both the goodwill for the lease and annual rental payments are unknown, we have used the figures shown on pg 374. If a payment of $500,000 was made for goodwill, and amortized over 60 years, the annual expense will be $8,333. In addition the annual land rent is estimated to be $32,500. The total annual expense is $40,833.

d. Amortization of goodwill – at pg 371 the paper proposes the purchase price to include the sum of $2,160,000 as goodwill. As noted, auditing standards require a robust analysis of any Goodwill carried on companies' balance sheets, and if there exists any impairment to the stated value, such impairment must be written down. It could well be that the full amount of Goodwill should be written down in the first year, however for the purposes of this calculation we have given the benefit of the doubt to the Cabinet Paper and suggest a 5 year write off period is appropriate. This results in an annual amortization charge of $432,000.

e. As noted earlier, no mention is made in the Cabinet Paper of operating expenses such as insurance, salaries and wages, repairs and maintenance, land owners rental, depreciation expense and amortization of goodwill. While government has publicly stated they will pay an operation/management fee to a third party, there will continue to be additional expenses such as insurance and repairs and maintenance. We are not privy to any expense calculations but have taken the liberty of suggesting such costs will be in excess of $300,000.

f. Summary of profitability

Gross operating margin			$825,520
plus - margin on 728,400 litres			145,680
			$971,200
less	Interest expense	$383,648	
	Depreciation	$450,000	
	Land rent and lease amortisation	$40,833	
	Amortization of goodwill	$432,000	
	Operating costs	$300,000	
			$1,606,481
	Net loss for first year		**$(635,281)**

There will be little change to this result in years two to five unless the volume increases or the margin per litre is increased. The expenses will be similar, with the slight decrease in interest expense being offset by the cost of funding the cash deficit in years one and two.

4. Cashflow

To adjust the above profit to a cash position for the year, non cash expenses need to be added back, and capital payments deducted. We calculate this as follows:

Profit / (loss) as above		$(635,281)
Add back non cash items		
Depreciation	$450,000	
Land lease amortization	$ 8,833	
Amortization of goodwill	$432,000	
		$890,333
Less other cash payments		
Payment for lease	$250,000	
Principle repayments to bank	$596,922	
Add back portion of interest	$(383,648)	
		$(463,274)
Net Cash position at end of first year		**$(208,222)**

This ignores any capital expenditure or further fixed asset purchases. These would result in further outflows of cash.

According to our calculations, the net cash position at the end of year one will be negative $208,222. Year two will be similar as the second $250,000 for the lease will be paid in that year. Further funding will be required to service this deficit, in turn reducing profitability further.

5. Other Matters

a. Landowners & Lease term – at Pg 370 it is noted that there are "just less than 4 years left on the lease." Pg 374 states "throughout this process the Financial Secretary has been negotiating with the family representative on this matter." It appears from this wording that there is no verbal (let alone written) agreement in relation to the extension of the lease.

Any business operation needs to be based on certainty of land tenure, not just in the Cook Islands but in any country. This is particularly important in the Cook Islands under our lease of land system, where there is no compensation for either land improvements or permanent structures on the land. While we assume the lease will be renewed, there is no certainty of the costs associated thereto. Such costs will need to be included in any valuation of the business, and any projected profit and payback calculations.

In the absence of any evidence to the contrary, Government would be well advised to treat the potential ownership of the TOA assets as expiring in four years.

Furthermore, without certainty of tenure and the associated costs thereto, the basis of an ongoing business, any business valuations, cash flows and projections becomes very subjective.

b. Depreciation – Pg 372 uses an average of 15% on a straight line method. This implies a remaining useful life of the assets of just under seven years. We are mindful that a significant number of the major assets at the TOA fuel depot are a number of years old. Our island environment is harsh on metal assets and specialised equipment, through both the proximity to the sea and the humid conditions. We question if an independent detailed inspection has been undertaken and therefore what reliance has the Government on the remaining lifespan of the assets. We also note that many new assets do not have a useful life of seven years, such as computers, air conditioners and other electronic equipment.

Normally all assets associated with the lease would be depreciated over remaining term of the lease, in this case four years.

c. Return on investment (Pg 375-376) – We have not had the time nor seen the background detail to the numbers provided to analyse these calculations fully. We make the following observations in relation to these calculations:

1. At a proposed purchase price of $5,160,000, a gross margin of $825,520, and with other expenses to be included, it is difficult to understand a claimed return on investment of two years.

2. The total Gross Margin of $3,302,080 over four years (as noted the profit will be less) represents 64% of the proposed purchase price of $5,160,000.

3. It appears the return on investment calculation considers the savings of the total Government fuel operation but only considers the cost of the TOA purchase (and without including the lease costs).

4. It is incorrect to include savings or profits from the proposed consolidated Government fuel operation in the return of investment calculation of one part of that operation, in this case the cost of the TOA assets. The individual costs of each component should be compared to the individual envisaged savings, or the total consolidated Government operation costs need to be compared to the total envisaged savings.

5. We are unsure if the cost of capital and the resulting operating loss is included in these calculations.

d. At Pg 372 (point 1– mid page) it states "The consumer will not have to pay the current finance charges that TOA pays which it passes onto them (13%)." Then point 2 states "Government having access to cheaper financing will only recover the finance charges plus a 1% margin… the consumer receives savings versus the current position." While we agree the savings between rates of 13% and 8.1% (7.1% plus 1%) look significant, we note the assets of TOA were purchased at $3,491,000 while the proposed Government purchase will be at $5,160,000. Applying the interest rates of 13% and 8.1% to the respective purchase prices, we calculate a saving of only $35,870. As the 7.1% offered by the bank is a variable rate, an increase to 7.8% will negate any perceived savings.

Disclaimer

Our engagement is with Triad Pacific Petroleum Limited and we accept no responsibility to any other party.

The information set out within our report has been based on the twelve pages of the Cabinet Paper dated 2nd February 2009 titled "Acquisition of Toa Petroleum". We have prepared our report on the basis of that information and nothing in this report should be taken to imply that KPMG has verified any information supplied to us, or has in any way carried out an audit of the information for the purpose of this report. Accordingly we do not accept responsibility for the accuracy or completeness of such information.

This report is prepared solely for the use of Triad Pacific Petroleum Limited. KPMG expressly disclaims any and all liability for any loss or damage of whatever kind to any person acting on information contained in this report, other than Triad Pacific Petroleum Limited.

We have only reviewed the Cabinet Paper as requested by you in arriving at our comments above. We have not reviewed any supporting documentation that may verify or explain the figures used in the Cabinet Paper. If such documents exist they may explain or clarify some of the assertions in the Cabinet Paper.

We have limited our comments to the proposed government acquisition of the assets of TOA. We do not express any view on the potential savings or otherwise that could result from a government owned fuel distribution monopoly, and express no view as to the merits, or otherwise, of such a concept.

We trust the above is of assistance to you however if you wish to discuss any of the above matters please contact the writer.

Yours faithfully
KPMG

MIKE CARR
RESIDENT DIRECTOR

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Ernst & Young Transaction Advisory Services Limited
100 Willis Street
Wellington 6011, New Zealand
PO Box 490, Wellington 6140

Tel: +64 4 499 4888
Fax: +64 4 495 7400
www.ey.com/nz

29 May 2009

Direct line: +64 4 470 0505

Email: duncan.wylie@nz.ey.com

Paul Allsworth
Audit Director
Audit (PERCA) Office
Cook Islands Government
PO Box 659
Avarua
RAROTONGA

Dear Paul

In accordance with our engagement letter dated 25 May 2009, I have reviewed the financial and valuation aspects of the two documents you sent me being:

- Cabinet paper 2 Feb 2009 re TOA
- KPMG letter of 11 May 2009 commenting on the above.

A number of issues present themselves in the Cabinet paper and seem to warrant further investigation. As you are aware, I am not familiar with the entities or the circumstances generally and hence my comments are based purely of a reading of the documents, from the perspective of their internal consistency and general methodology. The Cabinet paper in particular is very difficult to follow and potentially assumes a fair degree of local knowledge. Further, many issues are presented as findings and not supported by workings, and hence would require more extensive analysis before I could comment on them with any authority.

As far as I can understand it, the proposition is to buy the assets of petroleum import / storage / distribution businesses on the basis that the avoided costs thereafter (that is, avoidance, or the capturing, of the margins charged by the current operators) is NPV positive. The key inputs to any such examination are the cash outlaid and the cash inflows (or costs avoided) that are then forecast to ensue. With respect to the cash outlaid (the purchase price of the assets), we are not told how this number has been computed, but we are given a cross check which purports to justify the amount. In short, this cross check seems to be the aggregate of (a) the net book value of the subject assets and (b) four years of the estimated margins avoided (or captured) for the remaining life of the lease under which the assets are currently operated[1].

This rationale seems particularly problematic on face. Firstly, and most simply, this assumes the book values are correct – something that is assumed in the papers. I cannot comment on this although KPMG in their paper do make the point that this should be tested, to some degree at least. One would need to understand whether the assets are in a state of repair implied by those values and or would require capital expenditure to maintain them in an appropriate condition. Typically one would also have regard to depreciated replacement costs (which, if lower, would put the book values in question) and to any questions of economic obsolescence (are the assets capable of generating net earnings with a value equal

[1] We are not in a position to comment on whether the estimated remaining economic life of the assets is the four years referred to in the paper. References elsewhere in the paper to offers of longer term, 15 year financing may point to a longer remaining life. Even if that were the case however, it may also be that the all or some of the benefit of the assets beyond the lease term revert to the lessor with or without a purchase now, in which case they would likely not be relevant in determining the value to the lessor in the early termination/buy back seemingly in contemplation. Gaining an understanding of this would be crucial, whereas the Cabinet paper is effectively silent.

This page and the following 2 pages comprise the Annexure A
referred to in the Affidavit of Paul Allsworth
sworn at AVARUA this 2ND day of JUNE 2009
before me:

A Solicitor of the High Court of the Cook Islands to or in excess of those book values?). These are matters that one might expect to see verified in a due diligence exercise before making a binding commitment to purchase.

Secondly (and leaving aside the correctness or otherwise of accounting book values), the capital value of a collection of assets should equate to the present value of the future cash flows that the assets are expected to generate. They are each the flip side of a coin - another way of thinking about the same thing. Absent the future (net) benefits, the capital value is usually low or nil (or even negative[2]). It is incorrect to aggregate those two concepts of value, which is what has been done in the Cabinet paper. Instead, value will generally be represented by the greater of the two, but not the sum. In this respect at least, the Cabinet paper seems flawed on its face and merits further and deeper examination before reliance were to be placed on it.

As mentioned above, any value analysis must start with both the cash outlaid and the cash to be received / costs to be avoided over time. With respect to second leg of that analysis, the Cabinet paper provides estimates of the "gross margins" to be captured or avoided as a result of the purchase. The use of that terminology (and the absence of signs to the contrary) suggests that the writer may not yet have factored in the costs associated with annual operation. I do not know whether there are such costs, nor how much they would be, however it is hard to conceive of running such a business without operating costs. In addition to those operating costs, most businesses will require some allowance for amortisation of assets. This may be represented as depreciation in an accounting profit and loss statement, or maintenance capital expenditure in a cash flow sense. Neither seems to be allowed for here. If we assume, for example, that maintenance capital expenditure equals depreciation (consistent with a simplifying assumption that accounting earnings roughly equate to cash), and if we make a working assumption[3] that net margins are, say, half the gross margin, then the annual cash flows from the asset would be half that assumed in the Cabinet paper. Again, this is predicated solely on the use of the term gross margin in the paper, from which, conventionally, we would expect operating costs to be deducted. It is crucial to understand this position more accurately than is possible from the paper and it would be unwise to place reliance on the paper without verifying the existence and magnitude of the operating costs, including depreciation / capital expenditure.

In the event that such costs do exist and are not factored into the Cabinet paper analysis, the direct implications of that scenario would likely include:

- The capital value of the asset may be greatly less than the amount being proposed to be paid, and
- The amounts available to remunerate all sources of capital (which are assumed in the cabinet paper to be 100% debt funded) are lower than that assumed.

It is asserted that the gross margins (being stated as circa $825,000 p.a., or some 16% p.a. of the proposed purchase price) are sufficient to service principal and interest on a 15 year bank loan for 100% of the purchase price. We are told that the cost of debt may be in the region of 7-8% p.a., with that rate being variable over time. The issues discussed above regarding the potential costs to operate the assets are of course highly relevant to the capacity to service debt. If one continued with the illustrative example whereby half that gross margin was consumed by costs, the necessary implication would be that the

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[2] This might be the case if, for example, there are make good or remedial costs attaching to them for, say, environmental liability reasons. When dealing with assets of this nature, this is another matter one would expect to see addressed in a due diligence process prior to purchase.
[3] Again, we have no basis for this assumption, based only on a review of the papers. However, it is unlikely that the business / assets can operate without costs and an assumption of a 50% gross margin has been chosen purely to illustrate a point.

resultant surplus would seem barely sufficient to repay even interest alone on the full purchase price[4]. Conventional analysis would suggest that equity funding would be more expensive still (as would a more typical blend of the two). Indeed, later in the Cabinet paper a rate of 15% is used to estimate a commercial / non-governmental borrowing rate. The result of that, all else equal, would seem to point to the need for detailed analysis of the risk for the project to be NPV negative, or value destroying.

I note that it is also proposed in the Cabinet paper to change the operating structure of the business by fixing retailer margins. It is not clear what effect, if any, this will have on the assets proposed to be purchased (that is, whether such change impacts the upstream storage assets). However:

- If it does impact them, this would seem to increase the relative risk of that business, all else equal, by fixing a cost which is currently variable, thereby transferring that risk from the retailer to the storage company to some degree, or
- If it does not, that change would seem to be an option available to Government whether or not it bought the assets and therefore is not a factor to take account of in the project analysis.

The Cabinet paper goes on to discuss other potential initiatives for what appear to be follow on, or "bolt on" investments which, by implication, would in turn create more savings. The paper is not clear how these arise and the DCF results presented appear confusing do not lend themselves to checking or analysis on their face by the reader.

In short, a first reading of the Cabinet paper seems to raise a range of issues which would need further explanation but which, at face value, seem internally inconsistent and would benefit from careful analysis. Further, I would normally expect a proposed acquisition such as this to be supported by a greater level of due diligence and valuation analysis than that which the Cabinet paper offers the reader. The nature and potential materiality of the issues raised above (material uncertainties or, indeed, no information about such matters as condition of assets, remaining economic life, costs to operate, ability to service debt and the like) would suggest that the reader ought not place reliance on the analysis without further research and analysis being undertaken. Indeed, at first blush there are reasons to suspect that the values of the assets may be overstated. In the event that they are not, the information necessary to reach any such conclusion to the contrary is not obviously presented.

Yours sincerely
Ernst & Young Transaction Advisory Services Limited

Duncan Wylie
Director

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[4] And this would of course assume that the remaining economic life was at least 15 years, rather than the mere 4 years discussed in the paper. Once again, this is a key point that would need to be clarified.

(5)

Recd 6.3.10 ex. P.A.

This document is legally privileged and confidential to the Parties. It contains commercially sensitive information.

SETTLEMENT AGREEMENT

DATED: 11th December 2009

THE PARTIES:

1. **The Government of the Cook Islands**
("the Government")

2. **TRIAD PACIFIC PETROLEUM LIMITED**
("Triad")

3. **APEX AGENCIES LIMITED**
(trading as Toa Petroleum) ("TOA")

INTRODUCTION:

1. The Government and TOA entered into a Heads Of Agreement dated 4th December 2009 for the sale and purchase of TOA's fuel depot on Rarotonga.

2. Triad issued proceedings in the High Court of the Cook Islands under Plaint 2/09 to which the Government (represented by Deputy Prime Minister Sir Terepai Maoate and several government officials and agencies) were parties subsequently joined by TOA ("the Proceedings")

3. The Parties entered mediation in Rarotonga on 10 and 11 December 2009 and have agreed to settle their differences on the terms set out in this Agreement.

TERMS:

1. No later than 18 December 2009 Triad shall file in the High Court a Notice of Discontinuance of Plaint 2/09 and not take any further action or make any claims against any of the parties to the Proceedings in respect of the same subject matters.

2. The Government shall procure that there are no outstanding issues as to costs between the parties to the Proceedings to the end that no costs shall be sought by any party to the Proceedings against any other party.

3. The Parties agree to Sir Terepai Maoate issuing media releases in consultation with Triad and TOA, referring to the settlement and its benefits.

4. The Parties agree that no person representing or employed by Government, Triad or TOA shall make any disparaging statement or comment about any provision of this Agreement, the settlement of the Proceedings; or about any of the Parties in relation to the subject matter of the Proceedings.

5. The Parties agree that except as may be required by law, and subject to the provisions of clause 3, the terms of this Agreement shall be kept strictly confidential to the Parties in accordance with the terms of Mediation Agreement entered into by the representatives of the Parties 10 December 2009.

Sir Terepai Maoate on behalf of the Government of the Cook Islands	Brett Porter on behalf of Apex Agencies Limited	Chris Vaile on behalf of Triad Pacific Petroleum Limited

Recd ... ex P.A.

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DATED: 11th December 2009

THE PARTIES:

1. **The Government of the Cook Islands** ("the Government")

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INTRODUCTION:

1. The Government and TOA entered into a Heads Of Agreement dated 4th December 2009 for the sale and purchase of TOA's fuel depot on Rarotonga.

2. Triad Pacific Petroleum Limited ("Triad") issued proceedings in the High Court of the Cook Islands under Plaint 2/09 to which the Government (represented by Deputy Prime Minister Sir Terepai Maoate and several government officials and agencies) were parties subsequently joined by TOA ("the Proceedings")

3. The Parties entered mediation in Rarotonga on 10 and 11 December 2009 and have agreed to settle their differences on the terms set out in this Agreement.

TERMS: In consideration of the Agreement entered into between the Parties and Triad dated 11 December 2009 and the matters agreed herein

1. It is agreed that the Heads of Agreement shall be cancelled and to have, and have had, no effect whatsoever.

2. Neither party shall take any proceedings, nor make any claims against the other or any officers or employee thereof, in relation to the Heads of Agreement or any matter contained therein.

3. All matters arising out of or in connection with the Heads of Agreement shall be deemed to have been concluded and settled by the Agreement.

4. The Government shall pay to TOA the sum of $1,750,000 (the "Sum") in full and final settlement of any claim whatsoever that has been made, or may have been made by TOA arising out of or in connection with the Heads of Agreement, in the following manner:

   (a) the Sum shall be transferred to an account with the ANZ in the name of the Government on or before 18 December 2009;

   (b) the Government shall direct the ANZ –

      1. that the sum be held for the benefit of TOA;
      2. that the sum shall not be withdrawn from the account without the consent of TOA;
      3. on or before 31 March 2010, the Government will instruct ANZ Bank that the Sum be transferred to TOA as TOA directs.

members an opportunity to present an outline of their proposal to Cabinet.

(c) it will facilitate consideration by the Collector of Customs of proposals or representations by Triad in connection with the imposition of levies on the importation of fuel with a view to considering whether (subject with compliance with the Customs Act 1913) the bonded warehouse status of the Triad Depot should be confirmed and applied to tanktainer imports.

(d) it will facilitate the consideration by the Cook Islands Investment Corporation Board of proposals by Triad to enter arrangements for the matching of tenure of leases and/or easements relating to Triad's Panama Depot and any pipeline constructed in connection with it.

(e) in pursuing its policy objectives for fuel, the Government undertakes for the benefit of Triad that it will move forward in a timely manner to implement the Cabinet resolutions referred to in the "Kevin Carr affidavit" subject to

(i) the applicable ministry to oversee that committee and its duties to be the Ministry of Finance and Economic Management;

(ii) the terms of reference of that committee shall extend to cover issues of fuel transportation to the Cook Islands;

(iii) Triad shall, so far as practical, be consulted on the membership of the committee and its procedures with a view to securing a strong, well qualified independent chairmanship, a membership representative of all interested parties and robust, transparent (subject to commercial confidentiality issues) procedures allowing a forum for all interested parties to make representations and for considered, well-developed policy advice to be tendered to the Government in a timely manner.

4. The Parties agree that except as may be required by law, and subject to the provisions of the Agreement between the Parties and TOA dated 11 December 2009 terms of this Agreement shall be kept strictly confidential to the Parties in accordance with the terms of Mediation Agreement entered into by the representatives of the Parties 10 December 2009.

Maoate

Sir Terepai Maoate
on behalf of the
Government of the
Cook Islands

12-12-09

Chris Vaile
on behalf of Triad
Pacific Petroleum
Limited

10. The Parties agree that except as may be required by law, and subject to the provisions of the Agreement between the Parties and Triad dated 11 December 2009 the terms of this Agreement shall be kept strictly confidential to the Parties in accordance with the terms of Mediation Agreement entered into by the representatives of the Parties 10 December 2009.

Maoate

Sir Terepai Maoate
on behalf of the Government
of the Cook Islands

Brett Porter
on behalf of Apex
Agencies

ex P.A.

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SETTLEMENT AGREEMENT

DATED: 11th December 2009

THE PARTIES:

1. **The Government of the Cook Islands**
   ("the Government")

2. **TRIAD PACIFIC PETROLEUM LIMITED (trading as "Triad")**

INTRODUCTION:

1. The Government and Apex Agencies Limited ("TOA") entered into a Heads of Agreement dated 4th December 2009 for the sale and purchase of TOA's fuel depot on Rarotonga.

2. Triad issued proceedings in the High Court of the Cook Islands under Plaint 2/09 to which the Government (represented by Deputy Prime Minister Sir Terepai Maoate and several government officials and agencies) subsequently joined by TOA were parties ("the Proceedings")

3. The Parties entered mediation in Rarotonga on 10 and 11 December 2009 and have agreed to settle their differences on the terms set out in this Agreement.

TERMS:

In consideration of the Agreement entered into between the Parties and TOA dated 11 December 2009 and the matters agreed therein

1. The Government agrees that s23 Ministry of Finance and Economic Management Act 1995-1996 is important to the economic well-being of the people of the Cook Islands and agrees to use its best endeavours to ensure that its provision are complied with and will make reference (in a form considered appropriate by Government) to this in one or more of the media releases referred to in the Litigation Settlement Agreement.

2. On or before 18 December 2009, the Government shall pay to Triad the sum of \$55,000 plus VAT and the sum of \$17,190 (plus photocopying costs relating to documents in the proceedings on production of invoices for the same) inclusive of VAT by way of reimbursement for legal costs and disbursements incurred by Triad in respect of the Proceedings.

3. The Government assures Triad that:

   (a) it will not take any steps to impede or delay the approval and completion of any pipeline construction by Triad subject to compliance by Triad with applicable laws and regulations and will communicate this term of settlement to the Board of Cook Islands Investment Corporation at the earliest practical opportunity.

   (b) any proposal for the engagement of a consortium involving Triad in the project for the upgrading of roading on the island of Rarotonga shall, in a timely manner, be given full consideration by applicable agencies and officials in accordance with proper legal and commercial principles. As an initial step Government shall afford Triad and consortium members an opportunity to present an outline of their proposal to Cabinet.

(c) it will facilitate consideration by the Collector of Customs of proposals or representations by Triad in connection with the imposition of levies on the importation of fuel with a view to considering whether (subject with compliance with the Customs Act 1913) the bonded warehouse status of the Triad Depot should be confirmed and applied to tanktainer imports.

(d) it will facilitate the consideration by the Cook Islands Investment Corporation Board of proposals by Triad to enter arrangements for the matching of tenure of leases and/or easements relating to Triad's Panama Depot and any pipeline constructed in connection with it.

(e) in pursuing its policy objectives for fuel, the Government undertakes for the benefit of Triad that it will move forward in a timely manner to implement the Cabinet resolutions referred to in the "Kevin Carr affidavit" subject to

(i) the applicable ministry to oversee that committee and its duties to be the Ministry of Finance and Economic Management;

(ii) the terms of reference of that committee shall extend to cover issues of fuel transportation to the Cook Islands;

(iii) Triad shall, so far as practical, be consulted on the membership of the committee and its procedures with a view to securing a strong, well qualified independent chairmanship, a membership representative of all interested parties and robust, transparent (subject to commercial confidentiality issues) procedures allowing a forum for all interested parties to make representations and for considered, well-developed policy advice to be tendered to the Government in a timely manner.

4. The Parties agree that except as may be required by law, and subject to the provisions of the Agreement between the Parties and TOA dated 11 December 2009 terms of this Agreement shall be kept strictly confidential to the Parties in accordance with the terms of Mediation Agreement entered into by the representatives of the Parties 10 December 2009.

Maoate

Sir Terepai Maoate
on behalf of the
Government of the
Cook Islands

12-12-09

Chris Vaile
on behalf of Triad
Pacific Petroleum
Limited

Glossary

Apex Agencies Ltd - Parent company of TOA Petroleum
BP SWP - British Petroleum South West Pacific
EBITDA - Earnings Before Interest, Tax, Depreciation and Amortization
EDI – Economic Development Initiative [Fund]
EEA - Economic Energy and Analysis Ltd Pty (Fuel consultancy company)
E&Y - Ernst & Young – International Chartered Accounting Firm
FPRC - Fuel Pricing(Price) Review Committee. Committee established to review the price of fuel in the Cook Islands
GOC - Government of the Cook Islands - as referred by EEA in their reports and presentations
HOA - Heads of Agreement. Agreement entered into between TOA and Government on 4 December 2008 for the acquisition of the TOA fuel facility
JUHI – Joint User Hydraulic Installation (Aviation fuel facility on Rarotonga)
KPMG – International Chartered Accounting Firm
LCT - Local Coastal Tanker
MFEM – Ministry of Finance and Economic Management
MRT – Medium Range Tanker
NSDP – National Sustainable Development Plan 2007
PERC – Public Expenditure and Review Committee
POBOC – Payments On Behalf of Crown
ROI – Return On Investment
TAU – Te Aponga Uira (Electrical State Owned Enterprise)