

# REPORT ON OPERATIONAL AND FINANCIAL PERFORMANCE

FOR THE NINE MONTHS ENDED  
31 MARCH 2011

TRANSPower



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Transpower is the State Owned Enterprise that plans, builds, maintains and operates New Zealand's high voltage electricity transmission network – the National Grid – which links generators to distribution companies and major industrial users.

**THIS IS THE FIRST  
QUARTERLY REPORT  
PRODUCED BY TRANSPOWER.  
THE REPORT SUMMARISES  
THE UNAUDITED FINANCIAL  
RESULTS OF TRANSPOWER  
FOR THE NINE MONTHS  
ENDED 31 MARCH 2011,  
TOGETHER WITH THE RESULTS  
FOR THE COMPARATIVE  
PRIOR-YEAR PERIOD.**

The report also sets out year-to-date progress against Transpower's Statement of Corporate Intent (SCI) performance targets.

The report is based on the unaudited financial results. The procedures undertaken to prepare this report are not as comprehensive as those undertaken for interim (six-monthly) and annual financial statements. There are also a reduced number of disclosures compared with the interim and annual financial statements.

In future years, similar reports will be published for the three months ending 30 September as well as the nine months ending 31 March. This will provide quarterly financial and operational information between the publication of the interim (six-monthly) and annual reports. Future quarterly reports will be published within one month of the end of the reporting period.

We welcome your feedback on this report. Please send feedback to [communications@transpower.co.nz](mailto:communications@transpower.co.nz).

## Update on Transpower's operations for the nine months ended 31 March 2011

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### Financial Performance

Net profit after tax for the nine months ended 31 March 2011, before net changes in financial instruments, was \$119 million, compared with \$128 million for the previous corresponding period.

The lower profit is due primarily to a net gain from significant one-off events in 2009/10, being a gain from recognition of cross border lease income of \$28 million, less a \$19 million impairment expense due to the write-down in value of freehold properties on the route of the North Island Grid Upgrade Project (NIGUP). The impairment position will next be reviewed at 30 June 2011 and any resulting impairment recorded in the full-year financial results.

Transmission revenue increased by 2 per cent to \$498 million.

Expenses increased by 2 per cent to \$202 million.

Net finance costs increased by 20 per cent to \$62 million. This reflected the increase in debt to fund our substantial capital programme.

Total capital expenditure, excluding freehold property purchases, was \$399 million, an increase of \$68 million over the previous period. The increase arose from expenditure on the NIGUP and the HVDC upgrade project (Pole 3).

### Operational Update

The North Island Grid Upgrade Project is progressing satisfactorily. Over 100 of the 426 towers have been erected; work on the Whakamaru, Brownhill and Pakuranga substations is underway; and installation of the underground cable from Brownhill to Pakuranga has started. All but two easements have now been secured.

The HVDC Upgrade (Pole 3) is well advanced but at some risk of delay. Subsequent to the end of the reporting period, we were informed by Siemens AG, the turnkey contractor for the project, of a delay in the supply and testing of the Pole 3 control system in Germany. We are in discussions with Siemens to determine the extent of the impact on the final commissioning date of Pole 3. Commissioning had been planned for the last quarter of fiscal year 2012. It is now likely to occur in the second quarter of 2012/13.

On the third major project, the North Auckland and Northland (NAaN) project, cable contracts have been placed and substation design and other preparatory work continues to plan.

In addition to the three major projects, we are engaged in significant other project work across the network. Of particular note, the Notice of Requirements and consents public hearing for the planned new Wairakei to Whakamaru C line was held in early March. A final decision, confirming the designations and resource consents, was notified by Taupo District Council on 15 April. The statutory appeal period closed on Friday 13 May.

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In February 2011, we submitted the forecast operating and capital expenditure requirements for the period 2012/13 to 2014/15 to the Commerce Commission for approval. Also in February, we applied to the High Court seeking merits and judicial review of the Commerce Commission's final decision on the form of revenue regulation to apply to Transpower from 1 April 2011.

We also launched Transmission Tomorrow, a look forward at how Transpower will develop and operate the National Grid over the next 20 years and beyond.

In March 2011, random drug and alcohol testing was implemented at all field work sites and for all staff working in safety-sensitive divisions.

**Statement of Corporate Intent Measures** (refer to table on page 11)

We are on target to achieve the majority of our SCI performance measures, although safety and network reliability targets have been missed or are at risk.

#### **Financial Measures**

Year-to-date financial performance is ahead of plan. This is reflected in favourable financial measures including operating profit margin, return on capital employed, return on equity and interest cover.

#### **Operational Measures**

Our targets for network reliability – as measured by the number of loss of supply events – are at risk. The measures have been impacted by two loss of supply events as a result of the Christchurch earthquakes (although our assets coped extremely well with those significant events) and several outages on a small Bay of Plenty line for which a major maintenance and upgrade project is now underway. HVAC availability is slightly below target due to the large number of planned outages on the network necessary to accommodate the extensive project works and maintenance activity.

#### **Non-Financial Measures**

By 31 March, 21 medical treatment injuries had been recorded in 2010/11 against an SCI target of 20 for the full year. This target was set to be lower than last year's outcome, despite the significantly greater hours being worked in the current year. The continued recurrence of largely avoidable injuries to our contractors and staff reinforces our commitment to improve the safety on all our operations. We have embarked on a concerted campaign across our business and in close conjunction with our field contractors, to change attitudes and behaviours to reduce the risk and incidence of harm.

Other non-financial measures are all on track.

## Consolidated Statement of Comprehensive Income

For the nine months ended 31 March 2011

		UNAUDITED	UNAUDITED	AUDITED
	NOTES	9 MONTHS 31 MAR 2011	9 MONTHS 31 MAR 2010	YEAR 30 JUN 2010
		\$M	\$M	\$M
<b>Operating revenue</b>				
Transmission revenue	2	497.9	489.8	653.4
Other revenue	2	43.1	63.9	77.0
Finance revenue	4	3.0	1.9	4.1
		544.0	555.6	734.5
<b>Expenditure</b>				
Transmission expenditure	3	97.6	101.3	133.9
Employee benefits	3	42.3	38.4	52.2
Other operating expenditure	3	61.8	58.6	83.9
		201.7	198.3	270.0
<b>Earnings before interest expense, impairment, tax, depreciation, amortisation and changes in the fair value of financial instruments</b>		342.3	357.3	464.5
Depreciation		101.3	95.5	127.9
Amortisation		10.4	6.5	12.0
Impairment on property, plant and equipment		-	12.6	24.5
Impairment on held for sale property		-	4.6	5.2
Finance costs	4	65.0	53.5	75.6
<b>Earnings before changes in the fair value of financial instruments and tax</b>		165.6	184.6	219.3
Gain (loss) in the fair value of financial instruments		(18.6)	(65.9)	(110.6)
<b>Earnings before tax</b>		147.0	118.7	108.7
Income tax expense (credit)		41.0	36.2	43.7
Net profit (loss)		106.0	82.5	65.0
<i>Total net profit (loss) for the period is attributable to:</i>				
Non controlling interest (NCI)		2.0	3.8	1.2
Owners of the parent		104.0	78.7	63.8
		106.0	82.5	65.0
<b>Other comprehensive income for the period net of tax</b>		-	-	-
<b>Total comprehensive income for the period</b>		106.0	82.5	65.0
<i>Total comprehensive income for the period is attributable to:</i>				
Non controlling interest (NCI)		2.0	3.8	1.2
Owners of the parent		104.0	78.7	63.8
		106.0	82.5	65.0
<i>Reconciliation of net profit (loss) specifying the net impact of fair value movements</i>				
Earnings before changes in the fair value of financial instruments and tax		165.6	184.6	219.3
Income tax expense (credit) excluding changes in the fair value of financial instruments		46.4	56.2	76.9
<b>Earnings before net changes in fair value of financial instruments</b>		119.2	128.4	142.4
Gain (loss) in the fair value of financial instruments		(18.6)	(65.9)	(110.6)
Income tax expense (credit) on changes in the fair value of financial instruments		(5.4)	(20.0)	(33.2)
Net profit (loss)		106.0	82.5	65.0

These statements are to be read in conjunction with the accompanying notes.

## Consolidated Balance Sheet

As at 31 March 2011

	UNAUDITED	UNAUDITED	AUDITED
	31 MAR 2011	31 MAR 2010	30 JUN 2010
	\$M	\$M	\$M
<b>ASSETS EMPLOYED</b>			
<b>Current assets</b>			
Cash and cash equivalents	0.8	28.2	22.9
Trade and other receivables	56.4	67.0	66.1
Current tax asset	-	-	1.5
Investments	64.8	97.7	63.2
Derivatives in gain	27.0	20.8	-
Other financial assets	28.0	25.8	32.4
Non current assets held for sale	48.3	28.1	33.8
Inventories	12.9	12.1	10.7
	238.2	279.7	230.6
<b>Non current assets</b>			
Trade and other receivables	13.7	7.3	9.5
Derivatives in gain	170.7	160.9	107.1
Other financial assets	103.1	93.8	108.3
Capital work in progress	597.1	518.6	475.3
Property, plant and equipment	2,588.4	2,403.7	2,481.9
Intangibles	197.7	40.5	152.8
	3,670.7	3,224.8	3,334.9
<b>TOTAL ASSETS EMPLOYED</b>	<b>3,908.9</b>	<b>3,504.5</b>	<b>3,565.5</b>
<b>FUNDS EMPLOYED</b>			
<b>Current liabilities</b>			
Trade and other payables	67.6	54.5	92.6
Current tax liability	16.9	15.1	-
Current debt	177.0	319.4	154.0
Derivatives in loss	122.1	98.6	77.2
Deferred income	34.7	33.4	34.4
Provisions	11.1	6.1	11.3
	429.4	527.1	369.5
<b>Non current liabilities</b>			
Trade and other payables	2.3	2.6	2.5
Finance lease liabilities	1.0	1.3	1.2
Derivatives in loss	156.9	70.3	59.6
Non current debt	1,598.5	1,285.3	1,511.8
Deferred tax	152.1	132.3	155.9
Provisions	7.8	13.1	10.2
	1,918.6	1,504.9	1,741.0
<b>Total liabilities</b>	<b>2,348.0</b>	<b>2,032.0</b>	<b>2,110.5</b>
<b>Equity</b>			
Capital	1,200.0	1,200.0	1,200.0
Available for sale financial assets reserve	(0.9)	(0.9)	(0.9)
Accumulated surplus (deficit)	368.6	279.5	264.6
Non controlling interest	(6.8)	(6.1)	(8.7)
<b>Total equity</b>	<b>1,560.9</b>	<b>1,472.5</b>	<b>1,455.0</b>
<b>TOTAL FUNDS EMPLOYED</b>	<b>3,908.9</b>	<b>3,504.5</b>	<b>3,565.5</b>

These statements are to be read in conjunction with the accompanying notes.

## Consolidated Cash Flow Statement

For the nine months ended 31 March 2011

	UNAUDITED	UNAUDITED	AUDITED
	9 MONTHS 31 MAR 2011	9 MONTHS 31 MAR 2010	YEAR 30 JUN 2010
	\$M	\$M	\$M
<b>CASH FLOW FROM OPERATIONS</b>			
<b>Cash was provided from:</b>			
Receipts from customers	551.5	513.4	718.3
Interest received	3.0	1.9	4.1
<b>Cash was applied to:</b>			
Payments to suppliers and employees	(232.1)	(229.8)	(259.4)
Tax payments	(23.5)	(31.2)	(35.6)
Interest paid	(90.5)	(75.6)	(114.6)
<b>Net cash inflows from operations</b>	<b>208.4</b>	<b>178.7</b>	<b>312.8</b>
<b>CASH FLOW FROM INVESTMENTS</b>			
<b>Cash was provided from:</b>			
Sale of property, plant and equipment	12.0	0.6	8.1
Short-term investments	301.5	330.7	500.2
<b>Cash was applied to:</b>			
Purchase of property, plant and equipment	(393.1)	(353.4)	(554.8)
Short-term investments	(303.1)	(344.6)	(479.5)
<b>Net cash outflows to investments</b>	<b>(382.7)</b>	<b>(366.7)</b>	<b>(526.0)</b>
<b>CASH FLOW FROM FINANCING</b>			
<b>Cash was provided from:</b>			
Increase in loans	762.1	1,011.8	1,022.1
<b>Cash was applied to:</b>			
Increase in long-term investments	-	-	-
Dividends paid	-	-	-
Repayment of loans	(609.9)	(836.3)	(826.7)
<b>Net cash inflows from financing</b>	<b>152.2</b>	<b>175.5</b>	<b>195.4</b>
Net increase (decrease) in cash held	(22.1)	(12.5)	(17.8)
Opening balance brought forward	22.9	40.7	40.7
<b>Closing net cash carried forward</b>	<b>0.8</b>	<b>28.2</b>	<b>22.9</b>
<b>Closing net cash carried forward comprises:</b>			
Cash and bank	0.8	28.2	22.9

These statements are to be read in conjunction with the accompanying notes.

# Notes to the Financial Statements

For the nine months ended 31 March 2011

## 1. STATEMENT OF ACCOUNTING POLICIES

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### **Reporting Entity and Statutory Base**

Transpower New Zealand Limited is a State-Owned Enterprise registered in New Zealand under the Companies Act 1993. The financial statements are in New Zealand dollars and are of Transpower New Zealand Limited (Transpower or Parent) and its subsidiaries (together, the Group).

### **Nature of Operations**

Transpower is the owner and operator of New Zealand's national electricity grid. Transpower is not a public benefit entity for the purposes of NZIAS 1 "Presentation of Financial Statements".

### **Basis of Preparation**

The financial statements included in this quarterly report have been prepared in a manner consistent with the financial statements and relevant notes included in the Transpower 2009/10 Annual Report.

The accounting policies used in preparation of these financial statements are consistent with those used in preparation of the Group financial statements for the year ended 30 June 2010.

Transpower's operations are not considered seasonal or cyclical in nature.

### **Reclassifications**

Certain reclassifications of prior period balances have been made to conform with current period classifications.

### **New Standards Not Yet Adopted**

There were no relevant standards issued in the period.

### **New Standards Adopted**

No new standards were adopted during the period.

## Notes to the Financial Statements continued

For the nine months ended 31 March 2011

<b>2 OPERATING REVENUE</b>	UNAUDITED	UNAUDITED	AUDITED
	9 MONTHS 31 MAR 2011	9 MONTHS 31 MAR 2010	YEAR 30 JUN 2010
	\$M	\$M	\$M
<b>Transmission revenue</b>			
HVAC interconnection	340.4	326.9	440.4
HVAC connection	94.2	100.8	132.2
HVDC	57.8	53.4	72.7
EV (rebate) charge – HVAC	(30.2)	(21.8)	(31.9)
EV (rebate) charge – HVDC	5.8	5.3	7.3
New investment agreements	20.0	20.1	25.0
Other	9.9	5.1	7.7
	<b>497.9</b>	<b>489.8</b>	<b>653.4</b>
<b>Other revenue</b>			
Wholesale market services	23.5	20.0	26.6
Rental income	6.0	5.4	7.5
Cross border lease income	-	27.8	27.8
Risk Reinsurance investment income	2.2	1.9	2.6
Other	11.4	8.8	12.5
	<b>43.1</b>	<b>63.9</b>	<b>77.0</b>
<b>Total operating revenue (excluding finance revenue)</b>	<b>541.0</b>	<b>553.7</b>	<b>730.4</b>

**Transmission Revenue**

Transmission revenue consists of charges for the transmission of electricity from the point of generation to the point of supply, being high voltage alternating current (HVAC) interconnection, connection and high voltage direct current (HVDC).

Transpower operates its revenue setting methodology within an Economic Value (“EV”) framework that analyses economic gains and losses between those attributable to shareholders and those attributable to customers. The balance of the accumulated gain (loss) from regulated transmission activities attributable to customers (“the EV balance”) is passed on to or claimed from customers over time as EV rebates or charges.

New investment agreements, or customer investment contracts, are contracts entered into with customers to build grid connection assets.

**Other Revenue***Wholesale market services*

Wholesale market services revenue primarily relates to revenue from System Operator services.

*Cross border lease income*

In the 2009/10 financial year, the Group partially terminated the 2003 cross border lease that related to the majority of the HVAC transmission assets in the South Island. As a result of the partial termination, the Group recognised the remainder of the income in advance relating to this lease transaction.

*Other*

Other revenue mainly consists of subsidiary income from EMS Limited and d-cyphaTrade Limited.

3. EXPENDITURE ON ACTIVITIES	UNAUDITED	UNAUDITED	AUDITED
	9 MONTHS 31 MAR 2011	9 MONTHS 31 MAR 2010	YEAR 30 JUN 2010
	\$M	\$M	\$M
<b>Transmission expenditure</b>			
Maintenance of HVAC substations	36.3	36.3	48.9
Maintenance of HVDC substations and cables	7.4	8.2	10.5
Maintenance of HVAC lines	30.7	31.4	42.9
Maintenance of HVDC lines	0.8	2.0	2.3
HVDC share of reserves	4.5	6.6	7.2
Other direct transmission expenditure	17.9	16.8	22.1
	97.6	101.3	133.9
<b>Employee benefits</b>			
Short-term benefits	40.2	36.1	49.2
Defined contribution schemes	1.9	1.7	2.2
Other	0.2	0.6	0.8
	42.3	38.4	52.2
<b>Other operating expenditure</b>			
Information technology costs	13.9	13.1	18.2
Industry levies	5.9	5.6	8.5
Other business support costs	22.6	22.4	32.1
Operating lease and rental costs	12.0	9.6	13.5
Study grants and donations	0.6	0.8	1.3
External auditor – audit fee	0.3	0.2	0.3
External auditor – other assurance	0.2	0.3	0.2
Stock and asset write-offs	3.1	3.3	5.4
Insurance	3.2	3.3	4.4
	61.8	58.6	83.9
<b>Total expenditure on activities</b>	<b>201.7</b>	<b>198.3</b>	<b>270.0</b>

Maintenance includes inspection, servicing and repair costs.

HVDC share of reserves – The wholesale electricity market provides reserves to cover for the loss of the largest generation unit that is dispatched in any one island (North and South) in any one trading period. If these reserve quantities are in the other island, it is expected that the HVDC link will be available to carry this quantity. The cost of these reserves is charged to the Group (as grid asset owner) as their share of the HVDC at-risk quantity.

Other direct transmission expenditure includes investigations work that the Group conducts (prior to any commencement of a capital project) and the costs associated with running the Group's communications network.

Information technology costs include such items as software licences, maintenance, application support and project investigations.

Other business support costs include such items as legal fees, office equipment, communications, vehicles, travel and consultants.

Notes to the Financial Statements continued

For the nine months ended 31 March 2011

<b>4 NET FINANCE COSTS</b>	UNAUDITED	UNAUDITED	AUDITED
	<b>9 MONTHS 31 MAR 2011</b>	<b>9 MONTHS 31 MAR 2010</b>	<b>YEAR 30 JUN 2010</b>
	\$M	\$M	\$M
<b>Finance revenue</b>			
Interest received	(3.0)	(1.9)	(4.1)
<b>Finance costs</b>			
Interest paid and associated fees	88.1	74.6	103.5
Capitalised interest	(25.5)	(22.2)	(29.7)
Cross border lease expenses	0.6	(1.5)	(1.4)
Imputed interest	1.8	2.6	3.2
	65.0	53.5	75.6
<b>Total net finance costs</b>	<b>62.0</b>	<b>51.6</b>	<b>71.5</b>

**Interest Paid and Associated Fees**

All interest paid is on financial instruments designated as fair value through profit or loss.

**Imputed Interest**

Imputed interest is on new investment agreements, cross border leases, transmission realignment and certain other prepaid transactions.

## SCI Performance Targets

OPERATIONAL PERFORMANCE TARGETS	9 MONTHS 31 MAR 2011	FULL YEAR TARGET
SYSTEM AVAILABILITY FOR HIGH VOLTAGE ALTERNATING CURRENT	98.5%	98.8%
SYSTEM AVAILABILITY FOR HIGH VOLTAGE DIRECT CURRENT – POLE 2	93.4%	92.0%
NUMBER OF LOSS OF SUPPLY EVENTS OF GREATER THAN 0.05 SYSTEM MINUTES	15	21
NUMBER OF LOSS OF SUPPLY EVENTS OF GREATER THAN 1.0 SYSTEM MINUTE	3	3

FINANCIAL PERFORMANCE TARGETS <sup>1</sup>	9 MONTHS 31 MAR 2011	FULL YEAR TARGET
OPERATING PROFIT MARGIN	63.1%	60.4%
INTEREST COVERAGE	3.5	3.4
RETURN ON CAPITAL EMPLOYED	7.7%	7.0%
RETURN ON EQUITY	10.1%	9.3%
AVERAGE TOTAL TRANSMISSION COSTS (C/KWH) <sup>2</sup>	1.68	1.65
ESTIMATED ECONOMIC VALUE ADDED (\$M)	0	(15)

NON-FINANCIAL PERFORMANCE TARGETS	9 MONTHS 31 MAR 2011	FULL YEAR TARGET
MATERIAL BREACHES OF SYSTEM OPERATOR PERFORMANCE OBLIGATIONS	0	<4
ACC WORKPLACE SAFETY AUDIT STATUS	TERTIARY	TERTIARY
NUMBER OF FATALITIES OR INJURIES CAUSING PERMANENT DISABILITIES	0	0
NUMBER OF MEDICAL TREATMENT INJURIES	21	<20

<sup>1</sup> FINANCIAL PERFORMANCE RESULTS ARE ANNUALISED FIGURES BASED ON THE PERFORMANCE IN THE PERIOD WITH THE EXCEPTION OF ESTIMATED ECONOMIC VALUE ADDED, WHICH IS THE RESULT FOR YEAR TO 31 MARCH 2011.

<sup>2</sup> THE CALCULATION IS AN ESTIMATE BASED ON ENERGY SUPPLIED IN 2009/10.

