
Statement of Corporate Intent 2011/12 – 2014



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Introduction

State Owned Enterprises Act 1986

This Statement of Corporate Intent (“SCI”) is submitted by the Board of Directors of Genesis Power Limited trading as Genesis Energy (“Genesis Energy”) in accordance with section 14 of the State Owned Enterprises Act 1986 (“Act”).

For the purposes of this SCI and except to the extent it is necessary to distinguish between the two, Genesis Energy together with its subsidiary companies is referred to as either Genesis Energy or the company.

Nature and Scope of Activities

Genesis Energy’s core business is located in New Zealand and involves:

- The generation of electricity;
- The retailing and trading of energy;
- The development and procurement of fuel sources.

Genesis Energy has approximately 650,000 customers across New Zealand and owns and operates a diverse generation portfolio with a total installed capacity of 2,131MW.

Generation assets include:

- 685MW of hydroelectricity capacity at the Tongariro and Waikaremoana Hydro Schemes in the North Island and the Tekapo A and B power stations in the South Island, and 8.65MW of wind capacity at the Hau Nui wind farm in the Wairarapa; and
- Huntly Power Station which incorporates four 250MW coal/gas turbines (“Huntly Units 1 to 4”), one 400MW gas-fired turbine (“Huntly Unit 5”), and a 48MW gas turbine (“Huntly Unit 6”).

The scale, locations and the fuel diversity of these assets play a major role in New Zealand’s electricity markets.

The Company’s operations are supported by 965 full-time equivalent staff members, including 440 contact centre staff¹.

Genesis Energy holds a 31 per cent equity interest in the Kupe Oil and Gas Field, located in Taranaki.

¹ As at 28 February 2011, excludes consultants, contractors and fixed term employees.

Performance Objectives and Targets

Business Performance Objectives

The principal statutory objective of Genesis Energy is to “operate as a successful business, and to this end, to be:

- As profitable and efficient as comparable businesses that are not owned by the Crown;
- A good employer; and
- An organisation that exhibits a sense of social responsibility by having regard to the interests of the community in which it operates and by endeavouring to accommodate or encourage these when able to do so”.²

This is the principal objective for Genesis Energy and forms the basis of all commercial decisions. To meet this objective and to deliver on the Company’s long term goals, Genesis Energy focuses its activities on the following business objectives:

- **Financial** To be fiscally responsible while delivering on shareholder value and performance expectations;
- **Portfolio Optimisation** To provide economic trading, production and new generation solutions that demonstrate strong sustainable performance;
- **Customers** To be recognised as the leading New Zealand energy provider with excellent customer service and innovative products that provide value, choice and control of consumption;
- **Employees** To partner with the Company’s employees for success;
- **Community and Stakeholders** To manage impacts on communities in which the Company operates and to engage meaningfully with key stakeholders including iwi in the areas in which the Company operates;
- **Environmental Impact** To manage responsibly Genesis Energy’s environmental impact while growing its business; and
- **Governance and Benchmarking** To follow best practice in corporate governance and benchmark the Company’s performance.

By implementing these business performance objectives in the provision of generation, retail and trading as well as other services, Genesis Energy will deliver on shareholder value expectations and make a positive contribution to New Zealand’s energy sector and the broader communities in which Genesis Energy operates.

² State Owned Enterprises Act 1986, section 4.

Performance Targets

Genesis Energy's performance targets for the next three financial years are as follows:

Financial Performance Targets	2011/12	2012/13	2013/14
Shareholder Returns			
Total shareholder returns ³	4.2%	4.6%	5.8%
Dividend yield	0.0%	2.5%	3.9%
Dividend payout	0%	29%	44%
Return on equity	5.0%	5.5%	6.9%
Return on equity adjusted for IFRS fair value movements and asset revaluations	5.4%	5.9%	7.5%
Profitability and Efficiency			
Return on capital employed	7.2%	7.7%	8.9%
Operating margin	17.5%	17.9%	18.8%
Generator efficiency	\$46.81	\$50.33	\$55.62
Earnings before interest and tax to average total assets	5.9%	6.3%	7.3%
Solvency			
Interest cover	4.4	4.7	5.1
Solvency	1.3	1.0	1.3
Non-Financial Performance Targets	2011/12	2012/13	2013/14
Abatement, infringement and enforcement notices under the Resource Management Act	0	0	0
Reduce carbon intensity	50% below 2005/06 levels by 2015/16	50% below 2005/06 levels by 2015/16	50% below 2005/06 levels by 2015/16
Customer satisfaction ⁴	90%	90%	90%
Power Station Availability			
Hydro	88%	92%	95%
Thermal			
Huntly Units 1 to 4	79%	71%	65%
Huntly Unit 5 ⁵	94%	87%	94%
Huntly Unit 6 ⁶	80%	80%	80%
Lost Time Injuries	0	0	0

Descriptions, calculation methods and definitions for the financial performance targets are provided in Appendix 1. A comparison with last years SCI targets is provided in Appendix 2.

³ The increase in equity has been used as a proxy for future changes in commercial value.

⁴ Based on the survey question: "Thinking about all aspects of the service provided to you, how satisfied are you with the overall performance of Genesis Energy, where 0 is extremely dissatisfied and 10 is extremely satisfied."

⁵ Huntly Unit 5 major outage scheduled mid October to mid/late November 2012.

⁶ Huntly Unit 6 operated as a peaking plant.

Capital Expenditure

Genesis Energy projects capital expenditure of approximately \$417 million over the next three financial years⁷. Capital expenditure includes both reinvestment expenditure and new generation development activities.

Financing and Capital Structure

Effective capital structure management enables Genesis Energy to deliver on its key strategies over time. This capital structure management is primarily measured through the company's gearing ratio, which assesses the level of debt to debt plus equity that Genesis Energy plans to maintain. Genesis Energy estimates that the company's gearing ratio over the next three financial years will be, as follows:

Year ending 30 June	2011/12	2012/13	2013/14
Gearing Ratio (Net Debt to Net Debt + Equity)	37.7%	35.4%	35.0%

These terms have the following definitions:

Net Debt is all short and long term borrowings less cash.

Equity is the share capital of the company together with any revaluation reserves and retained earnings of the company. Retained earnings are net after-tax profits of the company, less dividends paid, calculated in accordance with Generally Accepted Accounting Practice in New Zealand ("GAAP").

Ratio of Consolidated Shareholders' Funds to Total Assets

Genesis Energy estimates that the ratio of Consolidated Shareholders' Funds to Total Assets over the next three financial years will be, as follows:

Year ending 30 June	2011/12	2012/13	2013/14
Consolidated Shareholders' Funds: Total Assets	46.9%	47.7%	48.4%

These terms have the following definitions:

Consolidated Shareholders' Funds has the same definition as Equity.

Total Assets is the aggregate net book value of the assets of the company calculated in accordance with GAAP.

⁷ Financial years include 2011/12, 2012/13 and 2013/14.

Accounting Policies

Genesis Energy's accounting policies, as at the date of the last published financial statements, 30 June 2010, are set out in Appendix 3.

Reporting Requirements

Section 15 of the State Owned Enterprises Act 1986 requires the company to submit to shareholding Ministers no later than three months after the end of a financial year:

- An Annual Report of the operations of the company and its subsidiaries;
- Audited consolidated financial statements for that financial year; and
- The auditor's report on those financial statements.

The Annual Report is required to contain such information as is necessary to enable an informed assessment of the operations of the company and its subsidiaries, including a comparison of the performance of the company and subsidiaries with the relevant Statement of Corporate Intent. It must also state the dividend payable to the Crown.

For Half-Yearly Reports, section 16 requires that they be delivered within two months of the end of the first half of the financial year. The report must include the information that is required by the Statement of Corporate Intent.

In addition to the required statutory reports, Genesis Energy will supply:

- Quarterly reports to shareholding Ministers which will include summarised financial statements together with a brief commentary on key events for the previous quarter and performance against key SCI targets, and a business outlook;
- Quarterly reports to the public which will include a brief commentary on the financial results and key events for the previous quarter, performance against key SCI targets, key business metrics and a business outlook;
- The provision of monthly and quarterly financial performance information through Crown Financial Information System ('CFIS');
- The provision of information for use in the Crown Ownership Monitoring Unit ("COMU") benchmarking and performance website publications;
- Information to the public that is required to be disclosed under the shareholders continuous disclosure regime, which came into effect on 1 January 2010; and
- The disclosure requirements for the Capital Bonds under the NZX continuous disclosure requirements.

A summary of Genesis Energy's Business Plan and a draft Statement of Corporate Intent will be supplied to shareholding Ministers for discussion prior to the start of the financial year to which they relate. Genesis Energy will also provide, in a timely manner, any other information requested by shareholding Ministers, pursuant to section 18 of the Act.

Delivering Shareholder Value

Economic Value Added Analysis

Economic Value Added (“**EVA**”) is a measure of “economic profit” that indicates how well the company expects to perform over the forecast period relative to the cost of the capital invested in the company, as measured by the Weighted Average Cost of Capital (“**nominal WACC**”).

Genesis Energy’s return on capital projections average approximately 7.9% per annum over the business planning horizon and reflect an approximation for the company’s EVA over the next three financial years. Genesis Energy’s return on capital projections show a lower performance over last year’s SCI for 2011/12 and the 2012/13 period due to the revaluation, at 30 June 2011, increasing Equity by \$316 million. The ‘Strategy and Investment Programme’ commentary outlines the business strategy in place to raise performance and increase shareholder value.

Value of the Crown’s Investment in the Company

The Board of Directors’ estimate of the current consolidated commercial value of the Crown’s investment in Genesis Power Limited (“**Genesis Energy**”) is \$2,120 million. Key points about the manner in which that value was assessed are:

- The valuation was calculated as at 30 June 2011;
- The valuation was reviewed independently by PricewaterhouseCoopers (“**PwC**”);
- The valuation takes into account the existing operations of Genesis Energy and does not value any assets under construction, business development opportunities currently under consideration or other future generation opportunities;
- A discounted cash flow (“**DCF**”) analysis was used to calculate the valuation of Genesis Energy’s consolidated business (including all subsidiaries), on an after-tax basis;
- The DCF is based on nominal (i.e., including inflation) future “free cash flows” projections until 2034. The cashflow projections incorporate:
 - Genesis Energy’s 2011/12-16 Business Plan and projections based thereon;
 - A wholesale electricity price path derived from Genesis Energy’s in-house modelling; and
 - A terminal value of \$482 million to account for the cash flows from 2035 until the end of the expected life of each asset.
- Genesis Energy’s estimate of WACC (excluding Kupe⁸) used for the valuation is consistent with the range of WACC estimated by PwC of 7.8% to 8.8%.

The valuation of \$2,120 million compares favourably by \$496 million with the commercial value reported at 30 June 2010 of \$1,624 million. The key reasons for the increase in commercial value are:

⁸Due to commercial confidentiality no comment is made around the Kupe WACC.

- An increase of \$456 million in the value of the existing generation business. Contributing to this increase is an increase to the Company's view of the long term wholesale electricity price;
- This increase is offset by a revaluation loss on acquisition of the Tekapo A and B power stations of \$103 million; and
- An increase of \$143 million in the Shareholders Investment in the business through retained cash flows which were used to partly fund the acquisition of the Tekapo A and B power station assets.

Dividend Policy

In determining dividends payable to shareholding Ministers, Genesis Energy will comply with the solvency levels specified in the Companies Act 1993 and will follow the processes and procedures generally adopted by directors of publicly listed companies.

Under ordinary business circumstances, the dividend to be declared will be determined by reference to:

- Genesis Energy's working capital requirements;
- Genesis Energy's medium-term fixed asset expenditure programme;
- Genesis Energy's investment in new business opportunities; and
- Genesis Energy's risk profile, taking into account the sustainable financial structure for the business and considering predictions of short and medium term economic and market conditions.

Subject to the above circumstances that will affect from year to year the quantum of dividend paid, the financial performance targets outlined in this SCI assume annual dividend payments being made at a payout ratio of 80% of "Free Cash Flows"⁹.

No dividend is being paid for 2011/12 financial year due to the acquisition of Tekapo A and B power stations.

Procedures for Share Subscriptions or Purchases

Subscriptions for shares in any company or interests in any other organisation will, where substantial, or which involve a significant overseas equity investment, be subject to consultation with shareholding Ministers. The procedures for the establishment of subsidiary companies and the sale of substantial assets in the company are set out in Appendix 4.

⁹ "Free Cash Flows" is the net cash inflow from operating activities less net cash outflow to investing activities less interest paid and other finance charges.

Compensation from the Crown

In general, Genesis Energy will seek full compensation from the Crown for any activities or obligations which will result in a reduction of the company's net profit or net worth, which the company is required by the Crown to undertake under the provisions of the Act, and for which a commercial return is not forthcoming.

Genesis Energy is also entitled to compensation or other adjustments in certain circumstances, under agreements relating to its formation and to the purchase of assets from the Electricity Corporation of New Zealand Limited.

In order to facilitate Genesis Energy committing to the Huntly Unit 5 project within normal commercial parameters, a risk sharing agreement was entered into with the Crown. Under the agreement, the Crown assumes certain risks with respect to the long term supply of gas.

Business Outlook

The following commentary summarises the major market forces expected to impact the company's strategy and projected performance over the three year business planning period:

Market Outlook

The persistence of challenging economic conditions in the 2011 calendar year suggests that the growth in electricity demand will remain below historic trends in the short term before resuming to higher longer term levels from 2012. Based on this expectation, Genesis Energy projects a 1.5% per annum electricity growth rate over the business planning period.

New baseload renewable and mid-merit gas-fired thermal generation has come into the market in the last year. The company projects approximately 540MW of "effective" new generation will be commissioned by competitors by 2015/16. This new and generally lower cost or "must-run" generation will continue to displace the coal/gas fired Huntly Units 1 to 4 in the merit order, and will require Huntly Units 1 to 4 to be placed on a profile which will remove one or more units from service over the next few years.

Official gas reserve figures show New Zealand's total gas demand exceeding gas supply after 2016.

Genesis Energy's financial liability under the current New Zealand Emission Trading Scheme ("ETS") legislation is expected to increase over time and remain a key issue. Commercially, the ability to recoup the cost of carbon from the retail market remains an uncertainty.

The Minister for Climate Change Issues has established a panel to review the NZ ETS by June 2011. Part of this review will address if or how transitional arrangements will apply in the NZ ETS after 2012. Genesis Energy will manage the outcomes of any review taking into account the impact on the company's assets, its trading operations and its customers. The Company's financial projections assume transitional arrangements will apply after 31 December 2012.

Following the Ministerial Review of Electricity Market Performance in 2009, a number of regulatory measures have either been implemented or are under development. These include capacity scarcity pricing to set spot market prices during outages, public conservation campaigns and other scarcity situations, a customer compensation regime and price floors to apply during public conservation campaigns and a locational price risk mechanism to help parties manage spot price risks created by transmission congestion.

Recent announcements by competitors suggest a range of price increases will occur across the market to reflect underlying cost pressures (including carbon) and the price of new generation.

Business Strategy and Investment Programme

Genesis Energy's strategy is designed to deliver long-term shareholder value. The company operates in a competitive business environment and adapts its commercial strategy accordingly.

Huntly Units 1 to 4

Genesis Energy continues to keep under active consideration and review the role of Huntly Units 1 to 4 within its generation portfolio. The degree of re-positioning required of Huntly Units 1 to 4 will be determined by the ability of the company to make a commercial return on these assets.

Genesis Energy will continue to seek commercial hedge arrangements over the next few years. However, the current scheduled entry into long-term storage for the first two units at the Huntly Power Station remains January 2013 for the first unit and December 2014 for the second unit.

Current operating resource management consents for the Huntly Power Station site expire in 2013/14. The Company intends lodging consent applications to secure the site's future as a long term generation site of national significance. This reflects its critical role in supplying firm and controllable electricity and important ancillary services such as frequency and voltage support, and its proximity to major North Island load centres.

Delivering Customers Choices and Control

Genesis Energy intends on changing the customer experience to its customers. This will encompass new retail value propositions to end-use customers through leveraging recent investments made in upgrading back office systems and rolling out advanced meter technology. In 2011, the Company began introducing new products and services that will give customers more choices and control over their energy consumption and cost and that will facilitate increased demand-side participation.

To support these developments, the Company will continue to improve its delivery platforms, communication channels and customer service.

Genesis Energy will continue to reprofile its current Retail load to more closely match its economic generation, and to rebalance North Island and South Island Retail loads as a result of the Tekapo A and B power station acquisition and the virtual asset swaps contracts entered into with Meridian Energy.

Portfolio Management and Generation Growth

On 1 June 2011, Genesis Energy acquired the Tekapo A and B power stations from Meridian Energy. These assets have been integrated into the Company's generation portfolio. Along with the addition of the virtual asset swaps, the acquisition of the Tekapo A and B power stations allows Genesis Energy to take a more significant position as a South Island retailer.

Genesis Energy continues to develop a pipeline of future economic generation opportunities that better position the Company for growth. Genesis Energy remains open to opportunities for partnerships in these developments. The Company is advancing a range of wind farm options including two potentially significant wind farm sites (Castle Hill and Hau Nui Stage 3) in the Wairarapa region. Genesis Energy continues to progress work on other wind, hydro, geothermal and thermal prospects.

Genesis Energy has a target to consent and construct 300MW of renewable energy projects by 2015. The company will invest only in economically viable projects.

Fuel Management

Genesis Energy fuel portfolio enables the company to provide energy, both as a primary fuel (gas and LPG) and as electricity, to its customers. The Company continues to manage its fuel requirements on a commercial basis for coal and gas.

Kupe Investment

The Kupe Oil and Gas field has now been in commercial production for a year and has been a key contributor to the Company's revenue and cash flows over the last 12 months. Genesis Energy holds a 31% interest in the Kupe Oil and Gas field. The Company has contracted 100% of the gas supply.

Community and Iwi

Genesis Energy will continue to partner with, and support, the communities in which it operates. This will include localized community sponsorships and initiatives. The Company also has a range of broad based community initiatives which include the Genesis Oncology Trust, Schoolgen and Curtain Bank.

Genesis Energy is committed to working with iwi and looks forward to building on established relationships and working on new opportunities as they arise.

Financial Performance and Risks

Genesis Energy faces significant challenges from changes in market conditions, and these are reflected in the financial projections contained in this SCI for the next three years. Genesis Energy's commercial strategy manages these issues, and repositions the business to deliver sustainable shareholder value.

However, projections inevitably involve risks and uncertainties, which increase as the horizon extends. Relevant risks include economic, regulatory, political and operational uncertainties, many of which are outside the control of Genesis Energy and cannot be accurately predicted. Actual results may therefore differ from the projections presented in this SCI. Key risks include the pass through of the price of carbon, the level of generation and demand, and the future price of oil.

Genesis Energy's enterprise-wide risk management framework helps to manage the business risks that are specific to the company and which may pose a threat to future operations and profitability.

Other Matters

No other matters have been agreed by shareholding Ministers and the Board of Directors for inclusion in this SCI pursuant to section 14(2)(j) of the Act.

Rt Hon Dame Jenny Shipley, DNZM
Chairman of the Board of Directors
On behalf of the Board of Genesis Energy
30 June 2011

Appendix 1: Performance Targets – Descriptions, Calculation Methods and Definitions ¹⁰

Measure	Description	Calculation
Shareholder Returns		
Total shareholder return	Performance from an investor perspective – dividends and investment growth.	$(\text{Commercial value}_{\text{end}} / \text{less Commercial value}_{\text{beg}} \text{ plus dividends paid less equity injected}) / \text{Commercial value}_{\text{beg}}$
Dividend yield	The cash return to the shareholder.	Dividends paid / Average commercial value.
Dividend payout	Proportion of a SOEs net operating cash flows less allowance for capital maintenance paid out as a dividend to the shareholder.	Dividends paid / Net cash flow from operating activities less depreciation expense.
Return on equity	How much profit a company generates with the funds the shareholder has invested in the company.	Net profit after tax / Average equity.
Return on equity adjusted for IFRS fair value movements and asset revaluations	Return on equity after removing the impact of IFRS fair value movements and asset revaluations.	Net profit after tax adjusted for IFRS fair value movements (net of tax) / Average of share capital plus retained earnings.

¹⁰ Source: Crown Ownership Monitoring Unit ('COMU'), 31 May 2010

Measure	Description	Calculation
Profitability and Efficiency		
Return on capital employed	The efficiency and profitability of a company's capital from both debt and equity sources.	EBIT adjusted for IFRS fair value movements /Average capital employed.
Operating margin	The profitability of the company per dollar of revenue.	EBITDAF/Revenue.
Generator efficiency	The efficiency and profitability of the company's electricity generation.	EBITDAF/MWh.
Solvency		
Interest cover	The number of times that earnings can cover interest.	EBITDAF/Interest paid.
Solvency	Ability of the company to pay its debts as they fall due.	Current assets/Current liabilities.

Term	Definition
Capital employed	Interest-bearing debt plus share capital plus retained earnings.
Capital expenditure	Payments for the purchase of property, plant and equipment items taken from the cash flow statement.
Commercial value	This is the board's estimate of the current commercial value of the Crown's investment in the Group as per the company's Statement of Corporate Intent.
Depreciation expense	Depreciation expense per the profit and loss account.
Dividends paid	Dividends paid to the shareholder during the financial year per the cash flow statement.
EBIT	Earnings before interest and taxation.
EBITDA	Earnings before interest and taxation, depreciation and amortisation.
EBITDAF	Earnings before interest and taxation, depreciation and amortisation and fair value adjustments.
Equity	Total shareholders' equity taken from the balance sheet.
Fair value adjustments	Includes unrealised fair value gains/losses on derivatives or all fair value gains/losses on derivatives where the entity does not separately identify unrealised items. Also includes changes in the fair value of biological assets and investment properties.
Interest paid	Interest paid for the financial year on interest-bearing debt per the company's cash flow statement.
Net cash flow from operating activities	Taken directly from the cash flow statement – this is cash flows from operating activities less cash flows to operating activities. Ensure that interest paid is included in operating activities.

Term	Definition
Net debt	Interest-bearing debt such as loans, bonds and commercial paper plus interest-bearing finance leases less cash.
Retained earnings	Profits retained in the business (i.e. after dividends to the shareholder).
Revaluation reserve	When an asset is revalued to fair market value for accounting purposes the increase in the value of the asset is reflected in a revaluation reserve within equity.
Revenue	Revenue from the operations of the business. Interest revenue should be excluded.
Share capital	The amount of capital originally invested by the shareholder and any subsequent equity injections.
Tax on fair value adjustments	This is the tax effect relating to changes in fair values.

Appendix 2: Performance Targets – Comparison with 2010/11-2013 Statement of Corporate Intent

The following table shows revised 2011/12-2014 SCI performance targets which vary to those in last year's 2010/11-2013 SCI:

Financial Performance Targets: Period	2011/12		2012/13	
	This Year	Last Year	This Year	Last Year
Shareholder Returns				
Total shareholder return	4.2%	4.7%	4.6%	5.3%
Dividend yield	0.0%	6.1%	2.5%	7.2%
Dividend payout	0%	87%	29%	105%
Return on equity	5.0%	4.9%	5.5%	6.1%
Return on equity adjusted for IFRS fair value movements and asset revaluations	5.4%	4.6%	5.9%	5.5%
Profitability and Efficiency				
Return on capital employed	7.2%	7.1%	7.7%	8.0%
Operating margin	17.5%	12.9%	17.9%	12.4%
Generator efficiency	\$46.81	\$38.97	\$50.33	\$39.48
Earnings before interest and tax to average total assets	5.9%	5.6%	6.3%	6.5
Solvency				
Interest cover	4.4	6.5	4.7	7.0

The following factors contributed to the change in these specific financial performance targets:

Total shareholder returns drop approximately 0.6% due to the revaluation at 30 June 2011. The revaluation reduces total shareholder returns by 1%¹¹ because it increases equity. If the revaluation is excluded, total shareholder returns are higher than in last year's SCI due to reducing gas discounts and better performance in the wholesale electricity market. The revaluation at 30 June 2011 increases the projected total shareholder returns to 30.5% in 2010/11 from last year's 2.4% due to the revaluation increase being included in total shareholder returns.

The projections assume that no dividends will be paid in respect of 2010/11 and 2011/12 to help fund the acquisition of Tekapo A and B power stations and to strengthen the Company's Balance Sheet. An interim dividend is projected to be paid in 2012/13 giving a dividend yield of 2.5% and a dividend payout of 28%. These are lower than last year's SCI targets of 7.2% and 105% because the projections assume that the final dividend in respect of 2011/12 will not be paid.

Return on equity is impacted by higher profits in the current projections which are offset by an increase in equity due to the revaluation. The return on equity adjusted for the revaluation is higher than in last year's SCI.

Profitability and Efficiency measures have generally improved on last year due to the higher profitability projections.

Interest cover reduces from 6.5 in last year's SCI to 4.4 due to the acquisition of the Tekapo A and B power stations which was financed by borrowings and retained earnings.

¹¹ The 1% change is calculated with the \$103 million writedown of Tekapo A and B power stations in both the pre and post revaluation projections.

Non-Financial Performance Targets: Period	2011/12		2012/13	
	This Year	Last Year	This Year	Last Year
Customer Satisfaction	90%	85%	90%	85%
Power Station Availability				
Hydro	88%	90%	92%	98%
Huntly Units 1 to 4	79%	83%	71%	70%
Huntly Unit 5	94%	92%	87%	89%

The following factors contributed to the change in these specific non-financial performance targets:

The performance measure 'Number of significant RMA non-compliances' used last year has been replaced by two new environmental performance measures:

- 'Abatement, infringement and enforcement notices under the Resource Management Act' – zero; and
- 'Reduce carbon intensity' by 50% below 2005/06 levels by 2015/16.

Customer Satisfaction targets reflect a new methodology and a higher target setting.

Hydro availability performance targets reflect the planned major project works in 2011/12 which includes Piripaua station stator rewinds, Rangipo Unit G6 rotor pole palm repairs, Tokaanu transformer replacements, Tekapo A and B inspection outages and Tokaanu station tunnel inspections. In 2012/13, major project works include Tekapo canal repairs, Piripaua transformer replacements and Tuai Unit G3 stator rewind.

The availability target for Huntly Units 1 to 4 for 2011/12 decreases from 83% to 79% reflecting the addition of two months (total of five months, December 2011 to April 2012) to the outage survey programme required for generator refurbishment work on Huntly Unit 4 and other minor asset management changes¹².

¹² Availability for Huntly 1 to 4 is calculated as a percentage of all four units (i.e. 1000MW).

Appendix 3: Statement of Accounting Policies

General information

The financial statements have been prepared for Genesis Power Limited (the Company) and its subsidiaries (together the Group). The Company was incorporated and became a state-owned enterprise on 16 December 1998 pursuant to the State-Owned Enterprises Act 1986. The Company is a profit oriented entity and is wholly owned by Her Majesty the Queen in Right of New Zealand ("the Crown"). The Group's core business is located in New Zealand and involves the generation of electricity, the retailing and trading of energy, and the development and procurement of fuel sources.

The Company is a limited liability company incorporated and domiciled in New Zealand. The address of its registered office is 602 Great South Road, Auckland.

Summary of accounting policies

The financial statements include separate financial statements for Genesis Power Limited as an individual entity and the consolidated entity consisting of Genesis Power Limited and its subsidiaries.

Basis of preparation

The financial statements are prepared in accordance with New Zealand generally accepted accounting practice (NZ GAAP). They comply with New Zealand equivalents to International Financial Reporting Standards (NZ IFRS), and other applicable New Zealand Financial Reporting Standards, as appropriate for profit orientated entities. These financial statements are presented in New Zealand dollars rounded to the nearest thousand.

Compliance with IFRS

The separate and consolidated financial statements of Genesis Power Limited also comply with International Financial Reporting Standards (IFRS).

Entities reporting

The financial statements of the 'Company' are for Genesis Power Limited as a separate legal entity.

The consolidated financial statements of the 'Group' are for the economic entity comprising Genesis Power Limited and its subsidiaries.

Statutory base

Genesis Power Limited is a company registered under the Companies Act 1993.

The financial statements are prepared in accordance with the requirements of the Financial Reporting Act 1993 and the Companies Act 1993.

Historical cost convention

The financial statements are prepared on the basis of historical cost, except for the revaluation of available-for-sale financial assets, financial assets and liabilities (including derivative instruments) at fair value through profit or loss, and certain classes of property, plant and equipment.

Critical accounting estimates and judgements

The preparation of financial statements in conformity with NZ IFRS requires the use of certain critical accounting estimates. It also requires management to exercise their judgement in the process of applying the Groups' accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements, are disclosed in the notes or the relevant accounting policy.

The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both current and future periods.

Goods and Services Tax

The statement of comprehensive income and the cash flow statement are prepared so that all components are stated exclusive of GST. All items in the balance sheet are stated net of GST, with the exception of receivables and payables, which include GST.

Principles of consolidation

Subsidiaries

The Group financial statements incorporate the financial statements of the Company and entities controlled by the Company (its subsidiaries). Control is achieved where the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

The results of subsidiaries acquired or disposed of during the year are included in the profit or loss from the effective date of acquisition or up to the effective date of disposal, as appropriate.

Where necessary, adjustments are made to the financials statements of subsidiaries to bring their accounting policies into line with those used by other members of the Group.

All intra-group transactions, balances, income and expenses are eliminated in full on consolidation.

Investments in subsidiaries' are recorded at cost in the parent company's financial statements.

Business Combinations

Acquisitions of subsidiaries and businesses are accounted for using the acquisition method.

The cost of the acquisition is measured at the aggregate of the fair values, at the date of exchange, of assets given, liabilities incurred or assumed, and equity instruments issued by the Group in exchange for control of the acquiree. Acquisition-related costs are recognised in profit or loss as incurred.

Where applicable, the cost of acquisition includes any asset or liability resulting from a contingent consideration arrangement, measured at its acquisition-date fair value. Subsequent changes in such fair values are adjusted against the cost of acquisition where they qualify as measurement period adjustments (see below). All other subsequent changes in the fair value of contingent consideration classified as an asset or liability are accounted for in accordance with relevant NZ IFRS. Changes in the fair value of contingent consideration classified as equity are not recognised.

Goodwill arising on acquisition is recognised as an asset and initially measured at cost, being the excess of the cost of the business combination over the Group's interest in the net fair value of identified assets, liabilities and contingent liabilities recognised. If, after reassessment, the Group's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities exceeds the cost of the business combination, the excess is recognised immediately in profit or loss.

The Group's goodwill accounting policy is set out below.

Joint ventures

Jointly controlled assets and entities are joint arrangements with other parties in which the Group jointly controls or owns one or more assets or entities and is consequently entitled to a share of the future economic benefits through its share of the jointly controlled asset or entity.

The Group's share of the assets, liabilities, revenues and expenses of jointly controlled assets or entities is incorporated into the Group financial statements on a proportionate line-by-line basis.

Associates

Associates are all entities over which the Group has significant influence but not control, generally evidenced by a holding between 20% and 50% of the voting rights. Investments in associates are accounted for in the parent entity financial statements using the cost method and in the consolidated financial statements using the equity method of accounting, after initially being recognised at cost. The Group's investment in associates includes goodwill (net of any accumulated impairment loss) identified on acquisition.

The Group's share of its associates' post-acquisition profits or losses is recognised in the profit or loss, and its share of post-acquisition movements in reserves is recognised in other comprehensive income. The cumulative post-acquisition movements are adjusted against the carrying amount of the investment. Dividends receivable from associates are recognised in the parent entity's profit or loss while in the consolidated financial statements they reduce the carrying amount of the investment.

When the Group's share of losses in an associate equals or exceeds its interest in the associate, including any other unsecured receivables, the Group does not recognise further losses, unless it has incurred further obligations or made payments on behalf of the associate.

Unrealised gains on transactions between the Group and its associates are eliminated to the extent of the Group's interest in the associates. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of associates have been changed where necessary to ensure consistency with the policies adopted by the Group.

Foreign currency translation

Functional and presentation currency

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which it operates ('the functional currency'). The consolidated financial statements are presented in New Zealand dollars, rounded to the nearest thousand, which is Genesis Power Limited's functional and presentation currency.

Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of transactions or from their translation at balance sheet date using balance date exchange rates, are recognised in the profit or loss, except for differences arising on the retranslation of non monetary items. Gains and losses from the retranslation of non monetary items are recognised directly in other comprehensive income.

Translation differences on non monetary items, such as equities held at fair value through profit or loss, are reported as part of the fair value gain or loss. Translation differences on non monetary items, such as equities classified as available-for-sale financial assets, are included in the fair value reserve in the statement of comprehensive income.

Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable net of returns, trade allowances and duties and taxes paid. Revenue recognised for the profit or loss includes amounts received and receivable for electricity, gas, oil, LPG and energy related services, supplied to customers in the ordinary course of business. Management has exercised judgement in determining estimated retail sales for unread electricity and gas meters at balance date.

Revenue is recognised as follows:

Sales of goods

Revenue from the supply of goods is recognised when the significant risks and rewards of ownership have been transferred to the buyer.

Sales of services

Revenue from the supply of services is recognised at balance date on a straight line basis over the specified period for the services unless an alternative method better represents the stage of completion of the transaction.

Interest income

Interest income is recognised on an accrual basis using the effective interest method. The effective interest rate exactly discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount. The method applies this rate to the principal outstanding to determine interest income each period.

Rental income

Rental income is recognised in profit or loss on a straight line basis over the term of the lease. Lease incentives granted are recognised evenly over the term of the lease as a reduction in total rental income.

Dividend income

Dividend income is recognised when the right to receive payment is established.

Income Tax

The income tax expense or income for the period is the tax payable or receivable on the current period's taxable income or expense based on the New Zealand tax rate. This is adjusted by changes in deferred tax assets and liabilities attributable to temporary differences between the tax bases of assets and liabilities and their carrying amounts in the financial statements, and unused tax losses.

Deferred tax is recognised for temporary differences and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

Deferred tax liabilities are recognised for taxable temporary differences arising on investments in subsidiaries and associates, and interests in joint ventures, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset realised, based on those tax rates that are enacted or substantively enacted. The relevant tax rates are applied to the cumulative amounts of deductible and taxable temporary differences to measure the deferred tax asset or liability. Deferred tax is charged or credited to profit or loss, except when it relates to items charged or credited directly to other comprehensive income, in which case the deferred tax is also dealt with in other comprehensive income.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they related to income taxes levied by the same taxation authority and the Group intends to settle its current tax assets and liabilities on a net basis.

Leases

The Group is the lessee

Leases of property, plant and equipment where the Group has substantially all the risks and rewards of ownership, are classified as finance leases. Finance leases are capitalised at the lease's inception at the lower of the fair value of the leased property and the present value of the minimum lease payments. The corresponding rental obligations, net of finance charges, are included in other long term payables. Each lease payment is allocated between the liability and finance charges so as to achieve a constant periodic rate of interest on the finance balance outstanding. The property, plant

and equipment acquired under finance leases are depreciated over the shorter of the asset's useful life and the lease term.

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to profit or loss on a straight-line basis over the period of the lease.

The Group is the lessor

When assets are leased out under a finance lease, the present value of the minimum lease payments is recognised as a receivable. Finance lease receipts are allocated between interest revenue and reduction of the lease receivable over the term of the lease in order to reflect a constant periodic rate of return on the net investment outstanding in respect of the lease.

Assets leased to third parties under operating leases are included in property, plant and equipment in the balance sheet. They are depreciated over their expected useful lives on a basis consistent with similar owned property, plant and equipment. Rental income is recognised on a straight-line basis over the lease term.

Impairment of assets

Assets that have an indefinite useful life are not subject to amortisation and are tested annually for impairment. Assets that are subject to amortisation are reviewed for impairment annually, or whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. If an asset's carrying value exceeds its recoverable amount the difference is recognised as an impairment loss.

The recoverable amount is the higher of an asset's fair value less costs to sell, and the asset's value in use. In assessing value in use, the estimated future cash flows are discounted to their present value at a rate that reflects current market assessments of the time value of money. This discount rate is adjusted for the risks specific to the asset where the estimated cash flows have not been adjusted.

For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash generating units). Non financial assets other than goodwill that have been impaired are reviewed for possible reversal of the impairment at each reporting date.

Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but only to the extent the carrying amount of the asset at the date the impairment is reversed does not exceed what the amortised cost would have been had the impairment not been recognised. A reversal of an impairment loss is recognised in profit or loss immediately, unless the relevant asset is carried at fair value, in which case the reversal of the impairment loss is treated as a revaluation increase. Impairment of goodwill is not reversed.

Cash and cash equivalents

Cash and cash equivalents includes cash on hand, deposits held on call with financial institutions, other short-term, highly liquid investments with original maturities of three months or less that are readily convertible to known amounts of cash, and which are not subject to significant risk of changes in value, and bank overdrafts. Bank overdrafts are shown within borrowings in current liabilities on the statement of financial position.

Trade receivables

Trade receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest rate method, less impairment loss.

Appropriate allowances for estimated unrecoverable amounts are recognised in profit or loss when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of receivables.

Inventories

Fuel stocks

Coal and other fuel stocks used in electricity production are stated at the lower of cost and net realisable value. Cost is based on the weighted average basis and includes expenditure incurred in bringing the fuel stocks to their present location and condition, including shipping and handling.

Consumables and spare parts

Consumables and spare parts are stated at the lower of cost and net realisable value. Costs are assigned to individual items of inventory on the weighted average basis.

Petroleum production stock

Petroleum production stocks are stated at the lower of production cost and net realisable value. Cost of production includes attributable mining and manufacturing overheads.

Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs necessary to make the sale.

Non current assets (or disposal groups) held-for-sale

Non current assets (or disposal groups) are classified as held-for-sale and stated at the lower of their carrying amount and fair value less costs to sell, if their carrying amount will be recovered principally through a sale transaction rather than through continuing use; that is, if the assets are available for immediate sale and the sale is highly probable.

An impairment loss is recognised for any initial or subsequent write down of an asset (or disposal group) to fair value less costs to sell. A gain is recognised for any subsequent increases in fair value less costs to sell of an asset (or disposal group), but not in excess of any cumulative impairment loss previously recognised. A gain or loss not previously recognised by the date of the sale of the non current asset (or disposal group) is recognised at the date of de-recognition.

Non current assets (including those that are part of a disposal group) are not depreciated or amortised while they are classified as held-for-sale. Interest and other expenses attributable to the liabilities of a disposal group classified as held-for-sale continue to be recognised.

Non current assets classified as held-for-sale and the assets of a disposal group classified as held-for-sale are presented separately from the other assets in the balance sheet. The liabilities of a disposal group classified as held-for-sale are presented separately from other liabilities in the balance sheet.

Investments and other financial assets

Investments

Purchases and sales of investments are recognised on the trade date, being the date on which the Group commits to purchase or sell the asset. Investments are initially recognised at fair value net of transaction costs. Financial assets classified as fair value through profit or loss are initially measured at fair value.

Subsequent to initial recognition, investments in subsidiaries are measured at cost less impairment in the Company financial statements. Subsequent to initial recognition, investments in associates are accounted for under the equity method in the consolidated financial statements and the cost method in the Company financial statements.

Other financial assets

The Group classifies its other financial assets in the following categories: financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments, and available-for-sale financial assets. The classification depends on the nature of the financial assets and the purpose for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition and re-evaluates this designation at each reporting date.

(i) Financial assets at fair value through profit or loss

This category has two sub-categories: financial assets held-for-trading, and those designated at fair value through profit or loss on initial recognition. A financial asset is classified in this category if acquired principally for the purpose of selling in the short term or if so designated by management. A financial asset is designated as held-for-trading if the possibility exists that it will be sold in the short term and the asset is subject to frequent changes in fair value. Derivatives are also categorised as held-for-trading unless they are designated as hedges. Assets in this category are classified as current assets if they are either held-for-trading or are expected to be realised within 12 months of the balance sheet date.

(ii) Loans and receivables

Loans and receivables are non derivative financial assets with fixed or determinable payments that are not quoted in an active market and are measured at an amortised cost. They arise when the Group provides money, goods or services directly to a debtor with no intention of selling the receivable. They are included in current assets, except for those with maturities greater than 12 months after the balance sheet date which are classified as non-current assets. Loans and receivables are included in receivables in the balance sheet.

(iii) Held-to-maturity investments

Held-to-maturity investments are non derivative financial assets with fixed or determinable payments and fixed maturities that the Group's management has the positive intention and ability to hold to maturity.

(iv) Available-for-sale financial assets

Available-for-sale financial assets, comprising principally marketable equity securities, are non derivative financial assets that are either designated in this category or not classified in any of the other categories. They are included in non current assets unless management intends to dispose of the investment within 12 months of the balance sheet date.

Other financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or have been transferred and the Group has transferred substantially all the risks and rewards of ownership.

Available-for-sale financial assets and financial assets at fair value through profit and loss are subsequently carried at fair value. Loans and receivables and held-to-maturity investments are carried

at amortised cost using the effective interest rate method less impairment. Realised and unrealised gains and losses arising from changes in the fair value of the 'financial assets at fair value through profit or loss' category are included in the profit or loss in the period in which they arise. Unrealised gains and losses arising from changes in the fair value of financial assets classified as available-for-sale are recognised in other comprehensive income and accumulated as a separate component of equity. When securities classified as available-for-sale are sold, the accumulated fair value adjustments are reclassified from equity to profit and loss as gains and losses from investment securities.

If the market for a financial asset is not active (and for unlisted securities), the Group establishes fair value by using valuation techniques. These include reference to the fair values of recent arm's length transactions, involving the same instruments or other instruments that are substantially the same, estimated discounted cash flow analyses, and option pricing models refined to reflect the issuer's specific circumstances.

Financial assets, other than those at fair value through profit or loss, are assessed for indicators of impairment at each balance date. Financial assets are impaired where there is objective evidence that as a result of events occurring after initial recognition the estimated future cash flows of the asset have been impacted. In the case of equity securities classified as available-for-sale, a significant or prolonged decline in the fair value of a security below its cost is considered in determining whether the security is impaired. If any such evidence exists for available-for-sale financial assets, the cumulative loss measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit and loss, is removed from equity and recognised in the statement of comprehensive income. In respect of available-for-sale equity instruments, any subsequent increase in fair value after an impairment loss is recognised directly in other comprehensive income.

The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of trade receivables where the carrying amount is reduced through the use of an allowance account. When a trade receivable is uncollectible, it is charged to profit or loss. Changes in the carrying amount of the allowance account are usually recognised in profit or loss.

With the exception of available-for-sale equity instruments, if, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed through the profit or loss to the extent the carrying amount of the asset at the date the impairment is reversed does not exceed what the amortised cost would have been had the impairment not been recognised.

Derivatives

Derivatives are initially recognised at fair value on the date a derivative contract is entered into and are subsequently remeasured to their fair value. The method of recognising the resulting gain or loss depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged. The Group designates certain derivatives as either; (1) hedges of the fair value of recognised assets or liabilities or a firm commitment (fair value hedge); or (2) hedges of highly probable forecast transactions (cash flow hedges).

The Group has entered into transactions using financial instruments within predetermined policies and limits in order to reduce risks from carrying out its ongoing business. These instruments include forward exchange contracts, interest rate swaps. The Group enters into these contracts to hedge its foreign currency and interest rate exposure. The Group has also entered into forward and option contracts to manage its exposure to price fluctuations in the wholesale electricity market, and for sales of oil products.

The Group documents at the inception of the transaction the relationship between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions. The Group also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions have been and will continue to be highly effective in offsetting changes in fair values or cash flows of hedged items.

The fair values of various financial instruments used for hedging purposes and movements in the hedging reserve in shareholders' equity are shown in the Notes to the Financial Statements.

Fair value hedge

Changes in the fair value of derivatives that are designated and qualify as fair value hedges are recorded in the profit or loss, together with any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk.

Cash flow hedge

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges is recognised in other comprehensive income and accumulated as a separate component of equity in the hedging reserve. The gain or loss relating to the ineffective portion is recognised immediately in profit or loss.

Amounts accumulated in equity are recycled in profit or loss in the periods when the hedged item will affect profit or loss (for instance when the forecast sale that is hedged takes place). However, when the forecast transaction that is hedged results in the recognition of a non financial asset (for example, inventory) or a non financial liability, the gains and losses previously deferred in equity are transferred from equity and included in the measurement of the initial cost or carrying amount of the asset or liability.

When a hedging instrument expires or is sold or terminated, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity and is recognised when the forecast transaction is ultimately recognised in profit or loss. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately transferred to profit or loss.

The fair value of hedging derivatives is classified as non-current assets or non-current liabilities if the remaining maturity of the hedging relationship is more than 12 months and as a current asset or current liability if the remaining maturity of the hedging relationship is less than 12 months.

Derivatives that do not qualify for hedge accounting

Certain derivative instruments do not qualify for hedge accounting. Changes in the fair value of any derivative instrument that does not qualify for hedge accounting are recognised immediately in profit or loss.

Embedded derivatives

Derivatives embedded in other financial instruments or other non financial host contracts are treated as separate derivatives when their risks and characteristics are not closely related to those of the host contract, and the host contract is not carried at fair value with unrealised gains or losses reported in profit or loss.

Fair value estimation

The fair value of financial assets and financial liabilities must be estimated for recognition and measurement or for disclosure purposes.

The fair value of financial instruments traded in active markets (such as publicly traded derivatives, and trading and available-for-sale securities) is based on quoted market prices at the balance sheet date. The quoted market price used for financial assets held by the Group is the current bid price; the quoted market price for financial liabilities is the current ask price.

The fair value of financial instruments that are not traded in an active market (for example, over the counter derivatives) is determined using valuation techniques.

The Group uses a variety of methods and makes assumptions that are based on market conditions existing at each balance date. Quoted market prices or dealer quotes for similar instruments are used for long term debt instruments held. Other techniques, such as estimated discounted cash flow analysis, are used to determine fair value for the remaining financial instruments. The fair value of interest rate swaps is calculated as the present value of the estimated future cash flows. The fair value of forward exchange contracts is determined using forward exchange market rates at the balance sheet date. The fair value of electricity derivatives are calculated as the present value of the estimated future cash flows taking into account a market price path where available or an internally generated electricity price path.

The nominal value less estimate credit adjustments of trade receivables and payables are assumed to approximate their fair values.

Deferred 'day 1' gains/losses

Where the Group estimates fair values of derivative financial instruments using internally generated future price paths, as is the case with electricity derivatives, the instrument is fair valued at inception and the difference arising between the estimated fair value and its cost (nil) is a valuation adjustment. Other than for some energy option contracts, the valuation adjustment is eliminated by adjusting the future price path used to determine the fair value of electricity derivative by a constant dollar amount

to return the initial fair value to nil. For the energy option contracts the valuation adjustment is effectively amortised based on expected call volumes over the term of the contract.

Property, plant and equipment

Generation assets

Generation assets are stated in the balance sheet at cost, or in the case of previously revalued items, at fair value at the date of revaluation, less any subsequent accumulated depreciation and impairment losses. Revaluations are performed with sufficient regularity, not to exceed five years, to ensure the carrying amount does not differ materially from that which would be determined using fair values at the balance sheet date.

Any increase arising on the revaluation of generation assets is recognised in other comprehensive income and accumulated as a separate component of equity in the asset revaluation reserve, except to the extent that it reverses a revaluation decrease for the same asset previously recognised in profit or loss, in which case the increase is credited to the statement of comprehensive income to the extent of the decrease previously charged. A decrease in carrying amount arising on the revaluation of such generation assets is charged to profit or loss to the extent that it exceeds the balance, if any, held in the assets revaluation reserve relating to a previous revaluation of that asset.

Depreciation on revalued generation assets is charged to profit or loss. On the subsequent sale or retirement of a revalued asset, the attributable revaluation surplus remaining in the assets revaluation reserve is transferred directly to retained earnings.

Property and plant constructed for production or administrative purposes, is carried at cost, or in the case of previously revalued items, at fair value at the date of revaluation, less any subsequent accumulated impairment losses. The cost of assets constructed by the Group, including capital work in progress, is the cost of all materials used in construction, direct labour costs of construction, resource management consent costs, and an appropriate proportion of applicable variable and fixed overheads. Where applicable, cost also includes the estimated cost of dismantling and removing the asset and restoring the site on which it is located.

Other property, plant and equipment

All remaining property, plant and equipment, except for land and capital work in progress (which is not depreciated), are stated at cost less accumulated depreciation, and any accumulated impairment losses.

Depreciation

With the exception of land and property and plant under construction, depreciation is charged on a straight line basis at rates calculated to allocate the costs or valuation of an item of property, plant and equipment, less any estimated residual value, over its estimated useful life.

The estimated useful lives of different classes of property plant and equipment are as follows:

	Estimated Useful Life
Generation assets	10 to 50 years
Buildings and improvements	10 to 50 years
Other plant and equipment	3 to 15 years
Leased plant and equipment	20 to 25 years
Freehold land is not depreciated.	

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

An asset's carrying amount is written down immediately to its recoverable amount if the carrying amount is greater than its estimated recoverable amount.

Gains and losses on disposals or retirement of an item of property, plant and equipment as the difference between the sales proceeds and the carrying amount of the asset and is recognised in profit or loss. When revalued assets are disposed, it is Group policy to transfer the attributable surplus remaining in the asset revaluation reserve in respect of those assets to retained earnings.

Oil and gas exploration and development assets

Exploration and evaluation expenditure

Exploration and evaluation expenditure is accounted for in accordance with the area of interest method. An area of interest is defined as being a permit area, where the Group has a current right of tenure. The application of the area of interest method is based on a partial capitalisation model aligned to the 'successive efforts' approach. All exploration and evaluation costs, including directly attributable overheads, general permit activity, geological and geophysical costs are expensed as incurred except the costs of drilling exploration wells and the costs of acquiring new interests. The costs of drilling exploration wells are initially capitalised pending the determination of the success of the well. Costs are expensed where the well does not result in a successful discovery. Costs incurred before the Group has obtained the legal rights to explore an area are recognised in profit or loss.

Exploration and evaluation expenditure is partially or fully capitalised where either (i) the expenditure is expected to be recouped through successful development and exploitation of the area of interest (or alternatively, by its sale) or (ii) exploration and evaluation activities in the area of interest have not at the reporting date reached a stage which permits a reasonable assessment of the existence or otherwise or economically recoverable reserves, and active and significant operations in, or in relation to, the area of interest are continuing, or where both conditions are met.

Upon approval for the commercial development of a project, the accumulated expenditure is transferred to oil and gas development assets.

Oil and gas development assets

The costs of oil and gas assets in the development phase are separately accounted for and include costs transferred from exploration and evaluation, and all development drilling and other subsurface expenditure.

Oil and gas development assets are assessed annually for indicators of impairment. Any impairment is recognised in profit or loss. No amortisation is provided, in respect of oil and gas development assets, until they are reclassified as oil and gas producing assets. When production commences, the accumulated expenditure is transferred to oil and gas producing assets.

Mining licences

The costs of acquiring mining licences are capitalised as intangible assets. The licence costs of unsuccessful efforts are deemed impaired and charged the profit or loss when the decision to abandon an area of interest or licence is made. No amortisation is provided in respect of the licence costs of successful efforts, until the licence area is reclassified as oil and gas producing assets.

Licence costs of successful efforts are reclassified to oil and gas producing assets when the wells contained within the licence area enter commercial production.

Oil and gas producing and other oil and gas assets

The costs of oil and gas assets in production are separately accounted for and include costs transferred from exploration and evaluation expenditure, transferred development expenditure and the ongoing costs of continuing to develop reserves for production. These costs are subject to depreciation, depletion and amortisation in accordance with the policy outlined below.

Land and buildings and surface plant and equipment associated with oil and gas producing assets are recorded in the other land and buildings and other plant and equipment categories respectively.

With the exception of oil and gas producing assets (including land), depreciation is charged to profit or loss on a straight-line basis over the estimated useful lives of each part of an item of property, plant and equipment. The carrying values of oil and gas producing assets are amortised on a units of production basis using the proved (P90) reserves to which they relate.

The units of production basis is an accounting method where the provision for depreciation, depletion and amortisation is computed at a fixed rate per unit of product, based on an estimate of the total number of units the oil and gas property will produce during its service life.

Proven reserves (P90) are the estimated quantities of oil and gas which geological and engineering data demonstrate with reasonable certainty to be recoverable in future years from known reservoirs, under existing economic and operating conditions. Proven and probable reserves (P50) are defined as those which have a 50% chance or better of being technically and economically producible.

The estimated useful lives of other oil and gas assets are as follows:

	Estimated Useful Life
Buildings	50 years
Storage facilities	25 years
Sales pipeline	25 years
Motor vehicles	5 years
Freehold land is not depreciated.	

Intangible assets

Intangible assets include goodwill, research and development, computer software, naming rights and emissions units. Assets with indefinite useful lives are not amortised, but are tested at least annually for impairment and whenever there is an indication that the asset may be impaired. Where there is an active market for an intangible asset, the asset is recorded at a revalued amount, being fair value less any subsequent accumulated amortisation and subsequent accumulated impairment losses. Revaluations are completed for each intangible asset, not for a class of asset. Realised gains and losses arising from disposal of intangible assets are recognised in profit or loss in the period in which the transaction occurs. Unrealised gains and losses arising from changes in the value of intangible assets are recognised as at balance date. To the extent that a gain reverses a loss previously charged to profit or loss, the gain is credited to profit or loss. Otherwise, gains are credited to an asset revaluation reserve for that asset. To the extent that there is a balance in the asset revaluation reserve for the intangible asset a revaluation loss is debited to the reserve. Otherwise, losses are reported in profit or loss.

Goodwill

Goodwill arising on the acquisition of a subsidiary or a jointly controlled entity represents the excess of the cost of acquisition over the group's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities of the subsidiary or jointly controlled entity recognised at the date of acquisition. Goodwill is initially recognised as an asset at cost and is subsequently measured at cost less any accumulated impairment losses. Goodwill is not amortised, but is reviewed for impairment at least annually.

For the purpose of impairment testing, goodwill is allocated to each of the Group's cash generating units expected to benefit from the synergies of the combination. Cash generating units to which goodwill has been allocated are tested for impairment annually, or more frequently when there is an indication that the unit may be impaired. The recoverable amount is the higher of fair value less cost to sell and value in use. If the recoverable amount of the cash generating unit is less than the carrying amount of the unit, the impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to the unit and then to the other assets of the unit pro-rata on the basis of the carrying amount of each asset in the unit. Any impairment loss is recognised immediately in profit or loss and is not reversed in a subsequent period.

On disposal of a subsidiary or jointly controlled entity, the attributable amount of goodwill is included in the determination of the profit or loss on disposal. The Group's policy for goodwill arising on the

acquisition of an associate is described at (b) and impairment testing of the carrying amount of an associate is described at (g) above.

Research and development

Expenditure on research activities, undertaken with the prospect of obtaining new scientific or technical knowledge and understanding, is recognised in profit or loss as an expense when it is incurred. Expenditure incurred on research of an internally generated intangible asset is expensed when it is incurred. Where the research phase cannot be distinguished from the development phase, the expenditure is expensed when it is incurred.

The cost of an internally generated intangible asset represents expenditure incurred in the development phase of the asset only. The development phase occurs after the following can be demonstrated: technical feasibility; ability to complete the asset; intention and ability to sell or use; and development expenditure can be reliably measured.

Other development expenditure is recognised in profit or loss as an expense as incurred. Capitalised development expenditure is stated at cost less accumulated amortisation and accumulated impairment losses. Amortisation is calculated using the straight-line method to allocate the cost over the period of the expected benefit.

Computer Software

Acquired computer software licences are capitalised on the basis of the costs incurred to acquire and bring to use the specific software. These costs are amortised to profit or loss on a straight-line basis over their estimated useful lives (not exceeding four years).

Costs associated with developing or maintaining computer software programmes are recognised as an expense as incurred. Costs that are directly associated with the production of identifiable and unique software products controlled by the Group, and that will probably generate economic benefits exceeding costs beyond one year, are recognised as intangible assets. Direct costs include the software development employee costs and an appropriate portion of relevant overheads.

Computer software development costs recognised as assets are amortised to profit or loss on a straight-line basis over their estimated useful lives (not exceeding four years).

Emissions

Emissions units are purchased (or granted by the Crown) to offset the Group's emissions obligation.

Emissions units held are treated as intangible assets, and initially recorded at fair value. Fair value is cost in the case of purchased units or their initial market value in the case of government granted units. Emissions units are not revalued subsequent to initial recognition.

The difference between cost and fair value of government granted units is treated as revenue.

Emissions obligations are recognised as a current liability. An emissions liability is recognised when the Group incurs the emissions obligation. Up to the level of units held, the liability is recorded at the average cost of emissions units held on hand. When emission obligations exceed the level of units held, the net liability is measured at the market price of units, or the contract price where forward contracts exist.

Forward contracts for the purchased of emissions units are recognised when the contracts are settled and the units are received (on an accruals basis) as they are contracts for the delivery of non financial items to meet the Group's expected emissions obligations.

Financial instruments including contracts for differences and future price options in relation to emissions units are accounted for in line with the Group's accounting policy for derivatives.

Emissions units receivable from, or payable to, third parties pursuant to commercial agreements are accounted for in the period in which they are earned or the obligation has been incurred.

Trade and other payables

Trade and other accounts payable are recognised when the Group becomes obligated to make future payments resulting from the purchase of goods and services, and are subsequently carried at amortised cost.

Borrowings

Borrowings are initially recognised at fair value, net of transaction costs incurred. Borrowings are subsequently measured at amortised cost. Any difference between the proceeds (net of transaction costs) and the redemption amount is recognised in profit or loss over the period of the borrowings using the effective interest method.

Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date.

Finance costs

Finance costs include origination, commitment and transaction fees and are amortised to profit or loss as part of finance costs over the period of the borrowings using the effective interest rate method, unless such costs relate to capital work in progress.

Financing costs on capital work in progress and other qualifying assets that take a substantial period of time to construct or prepare for use or sale, are capitalised during the construction period. Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs eligible for capitalisation.

Costs cease to be capitalised when the asset is available for productive use. Depreciation of these assets on the same basis as other assets commences when the assets are ready for their intended use.

The capitalisation rate used to determine the amount of borrowing costs to be capitalised is the weighted average interest rate applicable to the Group's outstanding borrowings during the year. The weighted average interest rate is disclosed in the Notes to the Financial Statements.

All other finance costs are recognised in profit or loss in the period in which they are incurred.

Interest expense

Interest expense is accrued using the effective interest rate method. The effective interest rate discounts estimated future cash payments through the expected life of the financial liability to that liability's net carrying amount. The method applies this rate to the principal outstanding to determine interest expense each period.

Provisions

Provisions for legal claims and service warranties are recognised when: the Group has a present legal or constructive obligation as a result of past events; it is more likely than not that an outflow of resources will be required to settle the obligation; and the amount has been reliably estimated. Provisions are not recognised for future operating losses.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognised even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

Liabilities and provisions to be settled beyond 12 months are recorded at their present value. Provisions are re-assessed at each balance date. Changes in the present value of cash flow estimates are recognised in profit or loss. The provisions are reduced by expenditure incurred relating to the provision.

Provision for mitigation costs

A provision for mitigation costs is recognised when the Group has a legal or constructive obligation. The provision is based upon contractual commitments over the shorter of the contract period or the life of the resource consent.

Provision for rehabilitation and restoration

A provision for rehabilitation is recognised when the Group has a legal obligation or has publicly announced its intended rehabilitation policy for a particular site. The provision is based on an independent engineering report as to the appropriate action to rehabilitate each site. The provision is stated at the present value of the future net cash outflows expected to be incurred.

Employee benefits

Provision is made for benefits accruing to employees in respect of wages and salaries, annual leave, long service leave, and employee incentives when it is probable that settlement will be required and they are capable of being measured reliably.

Provisions made in respect of employee benefits are measured using the remuneration rate expected to apply at the time of settlement.

Contributed equity

Ordinary shares are classified as equity.

Dividends

Provision is made for the amount of any dividend declared on or before the end of the financial year but not distributed at balance date.

Resource consents

Costs incurred in obtaining resource consents are capitalised and recognised as part of the cost of property, plant and equipment. These costs are amortised over the life of the consent on a straight line basis commencing from the date that the resource consent is granted.

Financial liabilities

Financial liabilities that are classified as held-for-trading and financial liabilities designated at fair value through profit or loss are recorded at fair value with any realised and unrealised gains or losses recognised in profit or loss. A financial liability is classified in this category if acquired principally for the purpose of selling in the short term or if so designated by management to eliminate or reduce accounting mismatches. It is part of financial assets and financial liabilities managed at fair value. Gains or losses reported in profit or loss include any interest component. Transaction costs are expensed as they are incurred.

Other financial liabilities are recognised initially at fair value less transaction costs and subsequently measured at amortised cost using the effective interest rate method (refer finance costs policy).

Contingent assets and liabilities

Contingent assets and liabilities are recorded in the notes to the financial statements at the point at which the contingency is evident. Contingent liabilities are disclosed if the possibility that they will crystallise is not remote. Contingent assets are disclosed if it is probable that the benefits will be realised.

Statement of cash flows

The following are the definitions of the terms used in the statement of cash flows:

- cash is considered to be cash on hand and current accounts in banks, net of bank overdrafts;
 - investing activities are those activities relating to the acquisition, holding and disposal of property, plant and equipment and of investments;
 - financing activities are those activities that result in changes in the size and composition of the capital structure of the Group. This includes both equity and debt not falling within the definition of cash; and
 - operating activities include all transactions and other events that are not investing or financing activities.
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Appendix 4: Subsidiary and Associated Companies

The terms “share” and “subsidiary” have the same meanings as in section 2 of the Act.

1. The company will ensure at all times that:
 - (i) control of the affairs of every subsidiary of the company is exercised by a majority of directors appointed by the company; and
 - (ii) a majority of the directors of every subsidiary of the company are persons who are also directors or employees of the company, or who have been approved by the company’s Board for appointment as directors of the subsidiary.
2. The company will in relation with any single or connected series of transactions, consult with shareholding Ministers on items having a material impact on the company’s financial position not contemplated in the company’s Business Plan including:
3.
 - (i) any substantial capital investment in activities within the scope of its core business;
 - (ii) any substantial expansion of activities outside the scope of its core business into new business areas;
 - (iii) subscriptions for or sale of, shares in any company or equity interests in any other organisation which are material, involve a significant overseas equity investment, or are outside the company’s scope of business;
 - (iv) the sale or other disposal of the whole or any substantial part of the business or undertaking of the company; and
 - (v) where the company holds 20 per cent or more of the shares in any company or other body corporate (not being a subsidiary of the company), the sale or disposal of any shares in that company.

The company will also consult on specific items included in the company’s Business Plan as agreed between the company and shareholding Ministers from time to time.
