TRANSPOWER

Adapting to a new energy future

ANNUAL REPORT 2017_18

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TRANSPOWER

Corporate Governance Statement

for the year ended 30 June 2018

Transpower is committed to exceptional corporate governance policies and practices.

Diversity of thought, skill and experience across our Board and executive leadership team is fundamental to our long-term success, protecting the interests of our investors and creating value.

We regularly review our corporate governance systems and are always looking for opportunities to improve.

Introduction

Transpower has dual roles as system operator and grid operator, which are supported by key business functions. The grid operator component of the business is responsible for designing, building, operating and maintaining the national grid. The system operator component of the business is responsible for managing the electricity market in real-time. These core services are supported by corporate functions such as people services, corporate services and corporate governance, and are enabled by our information services and technology (IST), customers, stakeholders and environment and transformation functions.

Transpower is a limited liability company and a State-Owned Enterprise (SOE) with its shares held on behalf of the Crown by the Minister of Finance and the Minister for State-Owned Enterprises. Transpower has debt listed with the NZX and therefore is required to comply with debt listing obligations.

Transpower's Board of Directors is responsible for Transpower's long-term success and supervision of our management and business affairs. The Board and management are committed to creating and maintaining a high standard of corporate governance. This corporate governance statement demonstrates this commitment. Additional information on other activities of the Board this year and plans for next year can be found in the Online Annual Review.

The NZX Corporate Governance Code

In this corporate governance statement, Transpower has elected to report against the NZX Corporate Governance Code (the NZX Code). The NZX Code describes principles of corporate governance and the recommended action to demonstrate best practice.

There are certain parts of the NZX Code that do not apply to Transpower, such as those clauses related to director appointments, takeovers, directors' remuneration and shareholder rights. As an SOE, these governance arrangements are the responsibility of the Crown. These are identified in the statement.

Transpower considers that, during the reporting period, the company materially complied with the NZX Code.

Principle 1:

Code of ethical behaviour

"Directors should set high standards of ethical behaviour, model this behaviour and hold management accountable for delivering these standards throughout the organisation."

Recommendation 1.1 Code of conduct for Transpower's people and directors

"The board should document minimum standards of ethical behaviour to which the issuer's directors and employees are expected to adhere (a code of ethics)."

Transpower has a Code of Ethics and Conduct Policy that directors, employees, contractors and consultants are expected to comply with. The policy is designed to promote and maintain high standards of ethical behaviour and provides advice on how to deal with ethical problems that may be encountered in our operations.

Transpower's Code of Ethics and Conduct Policy sets out explicit expectations:

- acting honestly and with high standards of personal and professional integrity
- appropriately managing conflicts of interest
- proper use of Transpower's property or information
- not participating in any illegal or unethical activity, including safeguards against insider trading in the entity's securities (refer also to the Insider Trading Policy and Guidelines)
- fair dealing with shareholders, customers and other stakeholders
- standards around giving and receiving gifts, koha, facilitation payments and bribes (refer also to the Discretionary Expenditure, Gifts and Travel Policy)
- compliance with relevant laws and regulations
- reporting of unethical decision-making and/or behaviour (refer also to the Compliance Policy)
- conduct expected of management and the Board in responding to and supporting instances of whistleblowing (refer also to the Compliance Policy).

New employees are required to acknowledge that they have read, understood and will comply with the requirements of Transpower's Code of Ethics and Conduct Policy. The induction process includes the completion of the 'Doing the right thing at Transpower' online e-learning module, which ensures people who join Transpower are familiar with the organisation and what is expected of them while they are part of Transpower's team. This includes familiarisation with the Code of Ethics and Conduct Policy.

The Board reviews the Code of Ethics and Conduct Policy every five years and is regularly updated by the General Manager People and General Counsel and Company Secretary on any non-compliance with the policy.

Recommendation 1.2 Financial dealing policy

"An issuer should have a financial product dealing policy which applies to employees and directors."

Transpower's Insider Trading Policy and Guidelines set out the requirements for all directors, officers, staff and contractors of Transpower and its subsidiaries who wish to deal in Transpower's debt securities. The Board reviews the Insider Trading Policy and Guidelines every five years, and it was reviewed and approved by the Board in June 2018.

Principle 2:

Board composition and performance

"To ensure an effective board, there should be a balance of independence, skills, knowledge, experience and perspectives."

Recommendation 2.1 Board charter

"The board of an issuer should operate under a written charter which sets out the roles and responsibilities of the board. The board charter should clearly distinguish and disclose the respective roles and responsibilities of the board and management."

The role and responsibilities of the Board are set out in Transpower's Board Charter. The Board reviews the Board Charter every three years to ensure its relevance.

The Board has a minimum of eight scheduled meetings each year and meets whenever necessary to discuss urgent business. The Chair, Chief Executive, and General Counsel and Company Secretary establish meeting agendas to ensure key issues are covered throughout the year. The directors generally receive materials for Board meetings seven days in advance.

The Board appoints the Chief Executive and delegates responsibility for Transpower's day-to-day management to the Chief Executive, who in turn may delegate authority to executive managers.

Transpower's Delegated Authority Policy describes the limits of delegated authority and prescribes the matters in respect of which the Board reserves its decision-making authority.

Recommendation 2.2 Nominating and appointing directors to the Board

"Every issuer should have a procedure for the nomination and appointment of directors to the board."

The shareholding Ministers and ultimately the Cabinet appoints our directors on advice from The Treasury. Directors are independent and non-executive and are generally appointed for terms of up to three years, although they may be reappointed. Our shareholding Ministers, in conjunction with the Board, seek to ensure there is a balance and diversity of skills, knowledge, experience and perspectives among directors.

Recommendation 2.3 Written agreements with each director

"An issuer should enter into written agreements with each newly appointed director establishing the terms of their appointment."

Transpower's directors hold office sanctioned by our shareholding Ministers and accept appointment on terms and conditions set out upon their appointment.

Recommendation 2.4 Information on directors

"Every issuer should disclose information about each director in its annual report or on its website, including a profile of experience, length of service, independence and ownership interests."

The members of the Board of directors and their attendance at meetings during the 2017/18 financial year are listed below.

DIRECTOR	DATE COMMENCED IN OFFICE	MEETINGS HELD	MEETINGS ATTENDED
Tony Ryall (Chair)	1 May 2016	9	9
Don Huse (Deputy Chair – retired 30 April 2018)	1 May 2011	7	7
Jan Evans-Freeman	1 November 2012	9	9
Tim Lusk (retired 20 September 2018)	1 May 2015	9	8
Pip Dunphy (Deputy Chair from 1 May 2018)	1 May 2015	9	8
Bill Osborne	1 May 2016	9	9
Dean Carroll	1 November 2016	9	9
Sheridan Broadbent (appointed 1 May 2018)	1 May 2018	2	2

Tim Lusk retired from the Board on 20 September 2018 after four years. Don Huse, Deputy Chair, retired from the Board on 30 April 2018 after seven years. Pip Dunphy was appointed as Deputy Chair of the Board on 1 May 2018. Sheridan Broadbent was appointed to the Board on 1 May 2018.

Profiles of each director's experience can be found on Transpower's website and in the Online Annual Review. All directors are independent.

No directors hold shares in Transpower, have loans from Transpower or have made any request to use company information received in their capacity as directors that would not otherwise have been available to them.

Transpower's Directors' Interests Policy governs how Transpower resolves and manages the way directors' individual interests are disclosed.

The following directors have made general disclosures of interest with certain external organisations based on them being a Chair, director, Board member, trustee, council member, member, employee or consultant of those organisations or holding bonds or shares of those organisations. The disclosures of interest cover the period up to the date the financial statements were signed, on 23 August 2018.

DIRECTOR	POSITION	ORGANISATION
Tony Ryall	Chair	Nib NZ Limited
	Chair	Nib NZ Holdings Limited
	Director	NMH Holdings Limited
	Trustee	Massey University Foundation
	Consultant**	Simpson Grierson
	Chief Executive*	BestStart Educare
Don Huse**	Chair	OTTP New Zealand Forest Investments Limited
	Director	Precinct Properties New Zealand Limited
Jan Evans-Freeman	Pro Vice-chancellor	College of Engineering, University of Canterbury
	Director	Wireless Research Institute
	Director	Electric Power Engineering Centre
	Director	University of Canterbury Quake Centre
	Director*	QuakeCore
	Member	Engineering NZ Governing Board
Tim Lusk	Director	Environmental Protection Authority
	Director**	Enable Networks Limited
	Director**	Enable Services Limited
	Independent Director**	Wairarapa Rural Fire Board
	Director*	Wairarapa Water Limited
Pip Dunphy	Chair	First Gas Holdings TopCo Limited and subsidiary companies
	Chair	Gas Services NZ Limited and subsidiary companies
	Deputy Chair	Abano Healthcare Limited
	Director**	ACE Insurance Limited/Chubb Insurance New Zealand Limited
	Director	Fonterra Shareholders' Fund
	Director**	New Zealand Superannuation Fund
	Director**	Tamaki Research Limited
	Consultant**	Lattice Energy
Bill Osborne	Director	Rangitira Services Limited
	Vice President*	New Zealand Rugby Union Incorporated
	Director	Ports of Auckland
	Chairman*	PlantTech Research Institute Limited
	Chairman*	Page Macrae Engineering
Dean Carroll	Nil	
Sheridan Broadbent*	Shareholder	Figured Limited
	Shareholder	Invivo Wines Limited
	Chair	Ampli Limited
	Director	Business Leaders' Health and Safety Forum
	Director	Breach Consulting Limited
	Director	Kordia Group Limited
	Director	Spruce Goose Aerospace Limited

* Appointed during the year

** Resigned during the year

The Transpower Group has directors' and officers' liability insurance policies. Indemnity is also provided by Transpower's constitution and separate deeds of indemnity between Transpower and individual directors. These ensure that, generally, directors will incur no monetary loss as a result of actions undertaken by them as directors. Certain actions are specifically excluded, for example, the incurring of penalties and fines that may be imposed in respect of breaches of the law.

Directors' skills matrix

The Board has developed a skills matrix to identify the key skills necessary for governance at Transpower. The Board then carried out a self-assessment against these key skills. Based on this assessment, each area of the skills matrix was well represented on the Board, with at least two or more directors having each identified skill below.

Executive leadership	Health and safety
Governance	Energy/infrastructure
Finance	Capital markets
Risk	Legal/regulation
Technology/innovation	Customer/service

Information on directors of subsidiary companies as at 30 June 2018

TB and T Limited

Christopher Sutherland

David Knight

Risk Reinsurance Limited

David Knight (Chair)

John Clarke

Alex Ball

Halfway Bush Finance Limited

Christopher Sutherland

David Knight

emsTradepoint Limited

John Clarke (Chair)

Alex Ball

David Knight

The directors of the subsidiary companies are all Transpower employees. Employees do not receive any additional remuneration for their role as a director.

Directors declare any interests they have after they are appointed to the Board, and the interests are updated at every meeting. The Chair and General Counsel and Company Secretary together decide whether the interests present any conflicts and manage those accordingly, including not allowing directors to vote or be present during discussions where there may be a conflict.

Recommendation 2.5 Diversity policy

"An issuer should have a written diversity policy which includes requirements for the board or a relevant committee of the board to set measurable objectives for achieving diversity (which, at a minimum, should address gender diversity) and to assess annually both the objectives and the entity's progress in achieving them. The issuer should disclose the policy or a summary of it."

As part of Transpower's behavioural transformation, the focus is on creating and maintaining a vibrant, diverse, positive work environment where all Transpower's people feel included, welcomed and valued. Transpower wants to better reflect the communities it serves and believes that a diverse workforce and inclusive culture will result in improved business performance.

Transpower has a formal Diversity and Inclusion Policy. The policy defines Transpower's commitment to building a culture that promotes diversity and inclusiveness, pay parity and attracting, recruiting, developing, promoting and retaining a diverse group of talented individuals. The policy prescribes the responsibilities of the Board, the executive team and other employee groups and outlines Transpower's approach to the measurement and reporting of gender and ethnic diversity and inclusiveness of culture.

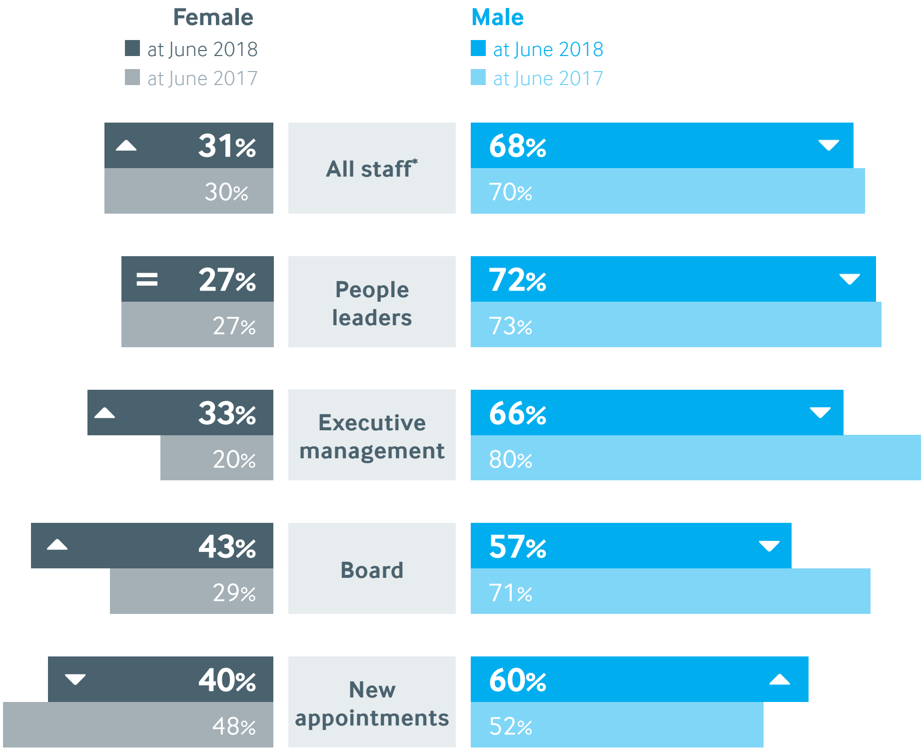
The policy identifies five diversity and inclusion initiatives that Transpower is focused on:

- making diversity and inclusion a core part of Transpower's corporate policy and reporting framework
- attracting and retaining more women with the objective of achieving a 40/40/20 gender target in teams over time (40% men, 40% women and 20% unallocated)
- attracting and retaining more Māori
- eliminating the gender pay gap in Transpower
- making diversity and inclusion a core part of Transpower's employee value proposition.

In 2017 Transpower introduced a diversity online e-learning module to develop staff awareness and capability in this area and encourage a more inclusive workplace.

A Māori responsiveness strategy was endorsed in June 2017, which sets out how Transpower will embrace Te Ao Māori to improve cultural competence, build relationships with iwi and attract and retain people with a Māori world view.

Our people



* 1% of staff chose not to state their gender

MEASURE	DESCRIPTION	AS AT JUNE 2018		AS AT JUNE 2017	
Age profile	Median age	46 years		45 years	
Gender by role	Role groupings by gender	Female %	Male %	Female %	Male %
	– All	31	68	30	70
	– People leaders	27	72	27	73
	– Executive management	33	66	20	80
	– Board	43	57	29	71
Ethnicity	Ethnicity*	%			
	– European (incl NZder)	94			
	– Māori	5			
	– Middle Eastern/Latin American/African	6			
	– Asian	17			
	– Pasifika	2			
	– Other ethnicity	2			
	– Not stated	58			
* Percentages add up to more than 100% as people can choose up to three ethnicities					
Part-time working arrangements	Percentage of staff working part-time hours	5.6		5.0	
New employees	The previous year's intake by age and gender	Median age: 39 years Gender: Female 40% Male 60%		Median age: 36 years Gender: Female 50% Male 50%	
	Ethnicity				
	– European (incl NZder)	74%			
	– Māori	3%			
	– Middle Eastern/Latin American/African	6%			
	– Asian	24%			
	– Pasifika	0%			
	– Other ethnicity	3%			
	– Not stated	27%			

MEASURE	DESCRIPTION	AS AT MARCH 2018	AS AT MARCH 2017
Internal hire rate	The previous year's appointments identifying internal versus external hires	31% of all appointments have been internal 50% of all roles in level 1-3 roles were filled by internal candidates (level 1-3 means the Chief Executive, executive management and those non-administrative roles reporting to the executive management)	34% of all appointments have been internal
Employee satisfaction	Response to the diversity statement "I feel Transpower values diversity (e.g. age, gender, ethnicity, language, education qualifications, ideas and perspectives)"	82%	74%

The Chief Executive of Transpower, Alison Andrew, is part of the Champions for Change initiative in New Zealand.

Recommendation 2.6 Director training

"Directors should undertake appropriate training to remain current on how to best perform their duties as directors of an issuer."

The Board introduces new directors to management and the business through customised induction programmes. These programmes usually include one-on-one meetings with the Chief Executive and the executive team and site visits to key locations. New directors also receive a pack containing key information about our business.

At least once a year, the Board holds strategic and professional development workshops. These provide opportunities for management to update the Board on key issues. Outside of these workshops, directors are regularly updated on relevant industry and company issues. There is an ongoing programme of presentations to the Board by all parts of the business. Transpower's directors ensure that they are independently familiar with the company's operations through continuous education to appropriately and effectively perform their duties. This includes participating in an ongoing site visits programme, and international visits to meet with peers in the energy sector.

Recommendation 2.7 Performance

"The board should have a procedure to regularly assess director, board and committee performance."

Transpower's Board is accountable to shareholding Ministers for company performance. The Treasury monitors and advises shareholding Ministers on the Board's performance. Each director's performance is evaluated by the Chair, and the Board also evaluates its overall performance annually through external evaluations.

Recommendation 2.8 Chair and CEO

"The Chair and the CEO should be different people."

In accordance with The Treasury's Owner's Expectations Manual, Transpower's Board Charter states that the Chair is separate from the Chief Executive. Tony Ryall is the Chair of the Board of Transpower, and Alison Andrew is Transpower's Chief Executive.

Principle 3:

Board committees

"The board should use committees where this will enhance its effectiveness in key areas, while still retaining board responsibility."

Transpower has three regular Board committees:

- Risk Committee
- Audit and Finance Committee
- People and Performance Committee.

Each Board committee has terms of reference that outline the role, rights, responsibilities and membership requirements for that committee.

Other committees may be established from time-to-time to consider matters of special importance or to exercise the Board's delegated authority. The Board is responsible for appointing committee members according to the skills, experience and other qualities they bring to the committee. Directors have ongoing Continuing Professional Development (CPD) objectives through their professional director organisations.

A minimum of two directors are required to sit on each committee, although typically three or more do so. The General Counsel and Company Secretary attends all meetings as Secretary at the invitation of the Board. Each committee is chaired by a director who is not the Board Chair. The agenda, papers and minutes of each committee meeting are provided to all directors. The Board is also given a verbal or written report by the committee Chair on the outcomes of each meeting.

The committees attend meetings each year scheduled to coincide with the timing of that committee's responsibilities. Each committee reviews its activities annually to ensure it is adequately covering its roles and responsibilities. The external evaluation of the Board also evaluates how each Board committee is functioning.

Recommendation 3.1 Audit committee

"An issuer's audit committee should operate under a written charter. Membership on the audit committee should be majority independent and comprise solely of non-executive directors of the issuer. The Chair of the audit committee should not also be the Chair of the board."

Transpower's Audit and Finance Committee is responsible for monitoring the financial performance and reporting of Transpower and its subsidiaries. It also reviews the appointment of external auditors (subject to the authority of the Auditor-General) and manages the external audit process, including reviewing and monitoring external audit and management reports.

Meetings of the Audit and Finance Committee

MEMBERS	MEETINGS HELD	MEETINGS ATTENDED
Don Huse (Chair – retired 30 April 2018)	3	3
Pip Dunphy (Chair from 1 May 2018)	4	4
Bill Osborne	4	4
Tony Ryall	4	4
Sheridan Broadbent (member from 24 May 2018)	0	0

The external auditor is subject to the independence rules of the Auditor-General. These rules require the audit partner to be rotated after a maximum of six years. Transpower discloses fees paid to external auditors in its annual report and differentiates between audit fees and fees for individually identified non-audit work.

Many of Transpower's directors who are members of the Audit and Finance Committee have previous financial experience. The Auditor-General has appointed Grant Taylor of Ernst & Young to carry out the audit on his behalf.

The Audit and Finance Committee also manages the internal audit process for financial matters, including reviewing, monitoring and approving internal audit reviews, annual audit plans and internal audit and management reports.

Recommendation 3.2 Employee attendance at audit committee meetings

"Employees should only attend audit committee meetings at the invitation of the audit committee."

The Audit and Finance Committee terms of reference set out that the Chief Executive and Chief Financial Officer are included as attendees at committee meetings at the request of the Chair of the committee, and all other attendees are only at the invitation or request of the Chair or Chief Executive.

Recommendation 3.3 Remuneration Committee

"An issuer should have a remuneration committee which operates under a written charter (unless this is carried out by the whole board). At least a majority of the remuneration committee should be independent directors. Management should only attend remuneration committee meetings at the invitation of the remuneration committee."

Transpower's People and Performance Committee performs the functions of a remuneration committee. This committee oversees Transpower's culture and performance and approves recruitment, remuneration, retention and termination decisions and policies and procedures regarding executive management. It reviews and recommends to the Board the Chief Executive's remuneration, terms, annual key performance indicators and performance recommendations.

Meetings of the People and Performance Committee

MEMBERS	MEETINGS HELD	MEETINGS ATTENDED
Jan Evans-Freeman (Chair)	5	5
Tim Lusk	5	4
Bill Osborne	5	5
Tony Ryall	5	5

The People and Performance Committee terms of reference set out that the General Manager People is included as an attendee at committee meetings and all other attendees are only at the invitation or request of the Chair of the committee or Chief Executive.

Recommendation 3.4 Nomination committee

"An issuer should establish a nomination committee to recommend director appointments to the board (unless this is carried out by the whole board), which should operate under a written charter. At least a majority of the nomination committee should be independent directors."

The shareholding Ministers and ultimately the Cabinet appoints Transpower's directors on advice from The Treasury.

Recommendation 3.5 Other committees

"An issuer should consider whether it is appropriate to have any other board committees as standing board committees. All committees should operate under written charters. An issuer should identify the members of each of its committees, and periodically report member attendance."

Transpower's Risk Committee has responsibility for reviewing health and safety matters on the Board's behalf and is responsible for ensuring that management has established a risk management framework that includes policy, procedures and assessment methodologies that enable Transpower to effectively manage and monitor organisational risks.

The Risk Committee also recommends the appointment of internal auditors and manages the internal audit process, including reviewing, monitoring and approving internal audit reviews, annual audit plans and internal audit and management reports. The Risk Committee will direct internal audit functions or material to either the Audit and Finance Committee or the People and Performance Committee where the subject matter is within the expertise of the respective committee. The primary objective of these internal audits is to assist the Board and the executive team in exercising good governance by providing independent assurance.

Meetings of the Risk Committee

MEMBERS	MEETINGS HELD	MEETINGS ATTENDED
Pip Dunphy (Chair until 24 May 2018)	3	3
Tim Lusk	4	4
Jan Evans-Freeman	4	4
Dean Carroll (Chair from 24 May 2018)	4	4
Sheridan Broadbent (member from 24 May 2018)	1	1

Principle 4:

Reporting and disclosure

"The board should demand integrity in financial and non-financial reporting, and in the timeliness and balance of corporate disclosures."

Recommendation 4.1 Continuous disclosure

"An issuer's board should have a written continuous disclosure policy."

Transpower has debt listed on the NZX Debt Market quoted under the ticker codes TRP010, TRP020, TRP030, TRP040 and TRP050 (together, bonds). As a listed issuer, Transpower is subject to certain requirements and obligations under the NZSX/NZDX Listing Rules, including a continuous disclosure obligation.

The Board has appointed the General Counsel and Company Secretary as the disclosure officer and, with the officer, examines continuous disclosure at the end of every meeting, including whether anything discussed at the meeting warrants disclosure, and reviews any disclosures made the previous month. The executive team also evaluates disclosure at its two-weekly meetings.

Within the last 12 months, Transpower has relied upon a waiver from rule 5.2.3, which requires at least 25% of the tranche of bonds quoted on the NZX Debt Market to be held by at least 100 bondholders who are members of the public. Accordingly, the bonds may not be widely held and there may be reduced liquidity in the bonds. In addition to disclosing the waiver and its implications and conditions in the interim and annual reports, Transpower is required to notify NZX Regulation if there is any material reduction in the total number of members of the public holding bonds and/or the percentage of total bonds held by members of the public holding at least a minimum holding.

Other disclosures

Debt listings and waivers

Transpower is required to disclose the waiver and its implications in any other offer document relating to the TRP050 bonds made during the period of the waiver. Transpower was also required to disclose the waiver, its implications and the liquidity as a risk in the pricing supplement for the TRP050 bonds.

Based on the register of bondholders, Transpower has at least the following number of bondholders as at 31 August 2018:

BONDHOLDER NUMBERS	TRP010		TRP020		TRP030		TRP040		TRP050	
	No. of bond-holders	No. of bonds (000)	No. of bond-holders	No. of bonds (000)	No. of bond-holders	No. of bonds (000)	No. of bond-holders	No. of bonds (000)	No. of bond-holders	No. of bonds (000)
1,001–5,000	22	110	4	20	7	35	5	25	1	5
5,001–10,000	66	617	26	255	33	310	21	194	16	149
10,001–100,000	266	9,548	77	3,021	104	3,521	41	1,477	48	1,711
>100,001	53	314,725	43	196,704	31	146,134	19	98,304	21	123,135
TOTAL	**407**	**325,000**	**150**	**200,000**	**175**	**150,000**	**86**	**100,000**	**86**	**125,000**

The Insider Trading Policy and Guidelines Policy has clear rules for when directors, officers and staff are dealing in listed Transpower debt securities.

Recommendation 4.2 Make key documents available

"An issuer should make its code of ethics, board and committee charters and the policies recommended in the NZX Code, together with any other key governance documents, available on its website."

Transpower's Code of Ethics and Conduct Policy, Board Charter and Terms of Reference for board committees recommended in the NZX Code, together with other governance documents, are available on Transpower's website.

Recommendation 4.3 Financial reporting

"Financial reporting should be balanced, clear and objective. An issuer should provide non-financial disclosure at least annually, including considering material exposure to environmental, economic and social sustainability risks and other key risks. It should explain how it plans to manage those risks and how operational or non-financial targets are measured."

Transpower's Audit and Finance Committee is responsible for monitoring the financial performance and reporting of the Transpower Group and its operating subsidiaries, emsTradepoint Limited and Risk Reinsurance Limited.

Transpower measures performance against a range of safety, operational, financial and non-financial performance targets. The 2017/18 targets are as per the 2017/18 Statement of Corporate Intent.

Each year, Transpower also agrees a set of system operation service targets with the Electricity Authority. There is a financial incentive to meet or outperform these targets.

Financial reporting

Transpower's executive team implements and maintains best practice and fit-for-purpose financial reporting principles, policies and internal controls designed to comply with accounting standards and applicable laws and regulations.

Transpower develops targets for and reports against five key financial metrics. These are focused on sustaining Transpower's credit rating, balance sheet strength and returns.

Non-financial reporting

Transpower reports on a number of non-financial performance measures to ensure transparency across the organisation.

Non-financial performance measures relate to the health of Transpower's long-life assets – availability of the transmission grid and the length of outages on the transmission grid – as well as measures relating to safety and the environment.

Principle 5:

Remuneration

"The remuneration of directors and executives should be transparent, fair and reasonable."

Recommendation 5.1 Director remuneration

"An issuer should recommend director remuneration to shareholders for approval in a transparent manner. Actual director remuneration should be clearly disclosed in the issuer's annual report."

Remuneration and benefits payable to directors for services as a director are determined in conjunction with the shareholding Ministers. Remuneration paid to Transpower's directors during the 2017/18 financial year is detailed in the following table.

DIRECTOR	DATE COMMENCED IN OFFICE	DATE CEASED IN OFFICE	2018 $000	2017 $000
Tony Ryall (Chair from 1 November 2016)	1 May 2016		126	104
Don Huse (Deputy Chair – retired 30 April 2018)	1 May 2011	30 April 2018	65	75
Jan Evans-Freeman	1 November 2012		65	62
Tim Lusk (retired 20 September 2018)	1 May 2015	20 September 2018	64	59
Pip Dunphy (Deputy Chair from 1 May 2018)	1 May 2015		67	62
Bill Osborne	1 May 2016		64	59
Dean Carroll	1 November 2016		64	40
Sheridan Broadbent (appointed 1 May 2018)	1 May 2018		11	–
Mark Verbiest (Chair until 31 October 2016)	1 August 2010	31 October 2016	–	50
TOTAL			**526**	**511**

During the year, no director of Transpower or the Transpower Group has received or become entitled to receive any benefit other than that disclosed above.

Recommendation 5.2 Remuneration policy for directors and officers

"An issuer should have a remuneration policy for remuneration of directors and officers, which outlines the relative weightings of remuneration components and relevant performance criteria."

Transpower's Directors' Fees and Expenses Policy sets out the directors' fees policy and how expenses incurred by directors are managed.

Transpower's framework and remuneration policy for officers is managed by the People and Performance Committee in line with the committee's terms of reference. Members of the executive team can earn incentive payments, subject to company and individual targets being met and at the absolute discretion of the Board. Any changes to executive management salaries are subject to approval by the Board following review by the People and Performance Committee. Executives have performance objectives with line of sight to the company and Chief Executive objectives. Their salaries are informed by performance ratings, and incentives can be 20–25% of their salary. In relation to their 2016/17 objectives, executive management received an average of 94% of their available incentives.

Remuneration of Transpower employees including executives

The remuneration model is designed to provide line of sight between the company objectives and individual objectives. It aims to attract, maintain and motivate employees.

All employees have fixed remuneration, adjusted each year at a level agreed by the Board on recommendation from the People and Performance Committee. Any increase is informed by data from independent remuneration specialists. Employee fixed remuneration is based on a matrix of their performance and how their salary compares to the market of a comparable position.

Transpower's employee remuneration tables for remuneration greater than $100,000

Aside from the Chief Executive, Transpower employees who received total remuneration of greater than $100,000 were in the following bands:

	2017/18	2016/17
800–809	1*	
610–619	1	
590–599		1
530–539		1
520–529	1	
510–519	1	1
500–509		1
450–459	2	1
440–449	1	1
430–439		1
420–429	1	
400–409		2*
390–399	1*	
380–389		1
370–379	1*	1
360–369	1*	
350–359		1*
320–329	2	2
310–319	2*	
300–309	1	2
290–299	1	1
280–289		1
270–279	3	4
260–269	4	7
250–259	5	3
240–249	9	5
230–239	12	12
220–229	7	7
210–219	11*	9
200–209	4	8
190–199	11	13
180–189	24	19
170–179	15	10*
160–169	26*	30*
150–159	55	35
140–149	65*	68*
130–139	76	70*
120–129	74	63
110–119	66	74*
100–109	63*	62*
	547	**517**

The bands above include all remuneration paid to or on behalf of employees, including base salary, performance payment, KiwiSaver, medical insurance, death and disability insurance, income protection insurance and severance or redundancy payments.

* The asterisk indicates those remuneration bands that include at least one former employee who received a severance or redundancy payment, without which they would not have been in that band.

Recommendation 5.3 CEO remuneration

"An issuer should disclose the remuneration arrangements in place for the CEO in its annual report. This should include disclosure of the base salary, short-term incentives and long-term incentives and the performance criteria used to determine performance based payments."

The Chief Executive can earn incentive payments, subject to company and individual targets being met and at the discretion of the Board. Any changes to Chief Executive salary is subject to approval by the Board following a review by the People and Performance Committee.

The Chief Executive objectives for 2017/18 related to the following:

MEASURES
Zero fatalities or permanent injuries
Total recordable injury frequency rate (TRIFR) ≤6
Achieve staff engagement target
Achieve target for restoration
Achieve EBITDA plan
Delivery ≥95% of base capex build
Achieve HVDC and HVAC availability targets
Achieve positive incentive outcome for system operator
Achieve grid interruptions target
Deliver Auckland development to agreed milestones
Deliver RCP3 plan to agreed milestones
Deliver Transmission Tomorrow focus areas to agreed milestones

The details of the Chief Executive remuneration are set out below. Figures include KiwiSaver. Incentives are based on company and individual objectives. The incentive and amount of the incentive relate to that salaried year.

YEAR	FIXED REMUNERATION PAID AND PAYABLE $000	% OF INCENTIVE MET RELATING TO THAT YEAR*	AMOUNT OF INCENTIVE $000	CARPARK $000	TOTAL REMUNERATION RELATING TO THAT YEAR $000
2017/18	998				
2016/17	969	94	271[1]	5	1,245
2015/16	940	97	271[2]	5	1,216

* The 2017/18 year incentive payment % has not yet been calculated.

1 This payment was made in September 2017 but related to the performance in the 2016/17 financial year.

2 This payment was made in September 2016 but related to the performance in the 2015/16 financial year.

Principle 6:

Risk management

"Directors should have a sound understanding of the material risks faced by the issuer and how to manage them. The Board should regularly verify that the issuer has appropriate processes that identify and manage potential and material risks."

Recommendation 6.1 Risk management framework

"An issuer should have a risk management framework for its business and the issuer's board should receive and review regular reports. A framework should also be put in place to manage any existing risks and to report the material risks facing the business and how these are being managed."

Transpower recognises that risk management is an integral element of good management practice and governance. The Board requires rigorous processes for risk management, supported by internal controls, to ensure that Transpower meets strategic objectives and the organisation is protected from adverse events.

Transpower's risk management covers the enterprise's entire perspective, including strategic, operational, commercial and financial aspects. The risk management policy is consistent with the internationally recognised standard AS/NZS ISO 31000:2009 and reflects the same risk management principles. Transpower's risk management methodologies include bowtie risk analysis and semi-quantitative risk assessment. These methodologies enable Transpower to have a more comprehensive understanding of the risks faced and the control environment used to manage those risks.

Transpower's Risk Committee has responsibility for ensuring that management has established a risk management framework that includes policy, procedures and assessment methodologies that enable us to effectively manage and monitor organisational risks.

Management report on the status of key risks and the control environment to the Risk Committee on a quarterly basis.

The following is a summary of our strategic priorities and the key risks that relate to them:

ICON	STRATEGIC PRIORITY
	Sustain our social licence to operate
	Reduce costs and evolve our services to remain competitive
	Develop our organisational effectiveness
	Improve our asset management
	Match our infrastructure build to need over time
	Play an active role in shaping the industry's future

KEY RISKS	EXPLANATION AND MITIGATION	STRATEGIC PRIORITIES
Risk of a serious workplace injury or death at a Transpower site or involving Transpower assets	Our work relates to development, operation and maintenance of assets where there is a risk of serious personal injury. We have sound, documented work processes and we use risk bowties along with other forms of risk analysis in the planning and execution of projects and maintenance work. We collaborate closely with our service providers in the choice of techniques and solutions we apply. Transpower is a member of StayLive, an industry group that works together to share knowledge and drive improvements in safety. In June 2018, StayLive won the ACC best leadership of an industry sector or region award at the New Zealand Workplace Health and Safety Awards.	

KEY RISKS	EXPLANATION AND MITIGATION	STRATEGIC PRIORITIES
Risk of harming the environment	Our environmental management and sustainability strategy seeks to minimise legal and reputational risks as well as risks to the physical environment and communities affected by our infrastructure. Transpower is committed to managing climate change risks (including minimising release of SF^6 gas) and ensuring resilience of the national grid to extreme weather events. Examples of environmental risks include managing potentially hazardous substances, contaminated land, noise effects, earthworks, land disturbance and our historic/cultural heritage. Transpower's Sustainability Strategy covers all aspects of our activities and services throughout the asset life cycle. It sets a clear vision for environmental management within Transpower, driving the business to be environmentally and socially responsible by adopting environmentally sustainable practices.	
Risk of power supply interruptions	A core part of our role is to plan, build, operate and maintain the national grid, with the objective of 'keeping the energy flowing' for New Zealand electricity consumers. In the unlikely event that the lights do go off, we need to ensure there is sufficient resilience in the grid to reconnect people to their power supply as soon as possible. Those events could be related to asset failure, operations error or external circumstances, such as severe adverse weather or a national catastrophe. An important risk-reduction measure is our investment in the replacement and refurbishment of assets as their health and condition deteriorates. Ongoing measures include reliability-informed maintenance reviews, emergency preparedness and a collaborative approach to contingency planning with our customers.	
Risks in system operations	Another core part of our role is that of system operator, in which we manage and coordinate electricity generation and operation of the electricity market minute by minute, 24/7, 365 days per year to provide an efficient and reliable power system. There is a constant risk that an event on the power system could impact our ability to ensure delivery of electricity around the country or maintain operation of the market. Key risk controls include having the people, systems and processes with which we plan for and manage any event in real-time, and having the flexibility to respond and adapt to whatever event arises.	

KEY RISKS	EXPLANATION AND MITIGATION	STRATEGIC PRIORITIES
Risk of a cybersecurity breach	We use a number of information, communications and technology systems that are critical for the supply of power and for system operations. To protect our systems and information against this sophisticated and ever-changing threat, continuous and systematic work aligned to international best-practice standards is ongoing to ensure information security. To achieve this, we are working closely with other stakeholders in the sector and with national authorities.	
Risk of not being able to find the skilled resources we need to effectively deliver our services	Engineers (electrical, civil and mechanical) and IT professionals with transmission and/or power systems experience have always been a skills shortage in New Zealand. The skills shortage will increase as our population ages and as market demand for skilled people to build and connect generation increases globally, as electric vehicles grow their share for transport and as renewable energy increasingly substitutes for fossil fuels. As markets for skilled people are internationally connected, New Zealand will continue to recruit from a global talent pool, subject to New Zealand Immigration settings for acquiring skilled migrants. Equally, New Zealand may become a source of workforce supply for other countries, thus further reducing the skilled workforce required nationally to operate and maintain the grid. In response, we have developed a people strategy and we are focused on building a diverse and inclusive workforce, having a strong employment brand and employee value proposition that will enable us to attract and retain talent. We continue to build awareness of the sector and attractiveness of science, technology, engineering and maths (STEM) jobs at a national level (see our Online Annual Review). Transpower is engaging with stakeholders in the energy sector to increase domestic training of electricity workers.	
Risk of not being able to adequately respond to exponential growth of emerging technologies such as batteries or in transport	Potential changes in electricity consumption, generation and customer response technologies bring with them greater uncertainty about future grid usage. Our challenge is to sustain a cost-effective transmission service that continues to provide an appropriate level of reliability while adapting to changing demands. We foster dialogue and develop forecasts to help us understand trends that will impact the grid and invest in asset management improvements and innovation so we can anticipate and respond to changes.	

KEY RISKS	EXPLANATION AND MITIGATION	STRATEGIC PRIORITIES
Reputational risk	Transpower provides a lifeline utility service for New Zealand and grid reliability is highly valued by our customers and electricity consumers. Our biggest reputational risk is associated with our ability to deliver on our mission 24/7, through all seasons and unaffected by weather conditions and other events. Furthermore, through our investments and operations, we have a physical presence throughout the country. This means that we need to continuously seek acceptance for our plans and ongoing activities. To establish and maintain good relations with the outside world, we proactively reach out to communities and stakeholders in specific cases. We have also increased our efforts to foster a dialogue with stakeholders on the future of our sector. A recent example of this is Te Mauri Hiko – Energy Futures, launched in June 2018.	
Financial risk	Transpower's activities expose it to a variety of financial risks. We have a strong framework for financial risk management and treasury policies that include guidelines and limits related to liquidity risk, interest rate risk, currency risk, credit risk, commodity risk and insurance risk. Further details for each of these categories is provided in the notes to the financial section of this report. A specific financial risk relates to the fact that Transpower, as a natural monopoly, is regulated by the Commerce Commission. The Commerce Commission determines what rate of return applies to our assets, as well as the incentives for meeting and exceeding operating expenditure, capital expenditure and meeting certain deliverables and outage targets.	

Recommendation 6.2 Health and safety risks

"An issuer should disclose how it manages its health and safety risks and should report on their health and safety risks, performance and management."

Transpower strives to provide a working environment in which there are no fatalities or injuries causing permanent disability. The company also seeks to reduce the rate at which activities cause injury through continuously focusing on safety and making improvements to processes. The Board focuses on reducing the target for injuries in each year. The target for fatalities is always zero.

The Board closely monitors health and safety, and it is a standing agenda item at the commencement of every meeting. The Risk Committee also undertakes deep dives into matters of interest relevant to health and safety at the Board's direction. Reporting to the Board and the business on relevant metrics is crucial in understanding health and safety risks and trends. As well as the Total Recordable Injury Frequency Rate (TRIFR), Transpower also uses a severity index to measure and track the severity of health and safety incidents, including near misses, to provide us with more information about our more serious incidents.

The staff who work for Transpower's service provider organisations – Broadspectrum, Electrix, ElectroNet and Northpower – are the most exposed to health and safety risks inherent in carrying out high voltage work, often at height in remote parts of New Zealand. Transpower works with these organisations on health and safety issues, and a health and safety leadership team, comprising the Transpower Chief Executive and Chief Executive Officers of the four service providers, meets three times a year to ensure a national focus for an ongoing safe healthy working environment. The objective of these meetings is to implement major change programmes to improve safety performance, with a strong focus on behavioural safety management.

Principle 7:

Auditors

"The board should ensure the quality and independence of the external audit process."

Recommendation 7.1 Establish a framework

"The board should establish a framework for the issuer's relationship with its external auditors."

Transpower's Audit and Finance Committee reviews the appointment of external auditors (subject to the authority of the Auditor-General) and manages the external audit process, including reviewing and monitoring external audit and management reports. There is regular dialogue between the Board and Board committees with both the internal and external auditors.

The external auditor is subject to the independence rules of the Auditor-General. These rules require the audit partner to be rotated after a maximum of six years. Transpower discloses fees paid to external auditors in the annual report and differentiates between audit fees and fees for individually identified non-audit work.

Recommendation 7.2 External auditor attendance at annual meeting

"The external auditor should attend the issuer's Annual Meeting to answer questions from shareholders in relation to the audit."

Transpower meets with shareholding Ministers or their representatives annually to examine the company's performance and review the strategic direction. Shareholding Ministers or their representatives can place items on the agenda for the annual meeting (including any governance or strategy items) and request other meetings throughout the year, if required. Transpower's Board, Chief Executive, General Counsel and Company Secretary and other executives by invitation, attend the annual shareholders' meeting and are available to answer any questions the shareholding Ministers have.

Transpower also attends the Transport and Infrastructure Select Committee (previously Finance and Expenditure Committee) annually to discuss the company's performance during the year. The Transport and Infrastructure Select Committee also meets separately with Transpower's external auditors.

Recommendation 7.3 Internal audit

"Internal audit functions should be disclosed."

The Risk Committee recommends the appointment of internal auditors and also manages the internal audit process for non-financial audits, including reviewing, monitoring and approving internal audit reviews, annual audit plans and internal audit and management reports. The Risk Committee will direct internal audit functions or material to either the Audit and Finance Committee or the People and Performance Committee where the subject matter is within the expertise of the respective committee. The primary objective of these internal audits is to assist the Board and the executive team in exercising good governance by providing independent assurance.

Transpower delivers its internal audit function utilising external resources (predominantly Deloitte) to carry out a range of compliance and improvement audits. The internal audit reports are provided to the Risk Committee or the Audit and Finance Committee. All Board members have access to these reports. The internal audit partner attends the Risk Committee on request.

Principle 8:

Shareholder rights and relations

"The board should respect the rights of shareholders and foster constructive relationships with shareholders that encourage them to engage with the issuer."

Recommendation 8.1 Website

"An issuer should have a website where investors and interested stakeholders can access financial and operational information and key corporate governance information about the issuer."

Financial disclosures and information for investors can be found in the investor section of Transpower's website.

Recommendation 8.2 Investor communications

"An issuer should allow investors the ability to easily communicate with the issuer, including providing the option to receive communications from the issuer electronically."

Transpower communicates with investors via multiple channels throughout the year: continuous market disclosure, half-year and full-year reporting of financial and non-financial performance and half-year and full-year investor briefings. In addition, we hold an annual public meeting, providing stakeholders with an opportunity to learn more about Transpower's business performance, future growth and corporate social responsibility focus. We also hold a number of stakeholder events throughout the year. The Board has hosted and attended a number of these events, and directors have also undertaken a number of customer visits to better understand customer needs.

In addition to shareholding Ministers, Transpower's stakeholders include other Ministers of the Crown and their ministries, The Treasury, customers, regulators, iwi, industry and business groups, contractors and suppliers, and the wider public. Transpower invests considerable effort in maintaining productive relationships with stakeholders. This includes providing timely and appropriate information and opportunities for feedback.

Transpower's Board has a clear policy for engagement and regular communication with significant stakeholders, in particular, customers and regulators. The Board regularly assesses its stakeholder engagement and ensures that conduct towards stakeholders complies with ethical obligations and the law, and is within broadly accepted social, environmental and ethical norms.

Transpower has debt securities listed on the NZX. Its bond holders are set out in Principle 4. Transpower regularly updates bond holders with information relevant to their investment and takes the opportunity to meet with them and their representatives regularly.

Investors can contact the executive or the Board by entering their details on this web page.

Financial statements

for the year ended 30 June 2018

CONTENTS

Statement of comprehensive income

for the year ended 30 June 2018

		GROUP	
		2018	**2017**
	NOTES	$M	$M
Operating revenue	2	1,084.4	1,061.1
Operating expenses	3	293.9	287.8
Earnings before interest, tax, depreciation, amortisation, asset write-offs, impairment and changes in the fair value of financial instruments	1	790.5	773.3
Depreciation, amortisation and asset write-offs and impairment	5	307.3	277.4
Net interest expenses	4	195.8	204.9
Earnings before changes in the fair value of financial instruments and tax		287.4	291.0
(Gain) loss in the fair value of financial instruments	15	(46.7)	(80.0)
Earnings before tax		334.1	371.0
Income tax expense	16	94.7	105.0
Net profit and total comprehensive income		239.4	266.0
Net profit and total comprehensive income for the period is attributable to:			
Non-controlling interest	8	(3.4)	4.6
Owners of the parent		242.8	261.4
		239.4	266.0

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

Reconciliation of net profit specifying the net impact of fair value movements

Earnings before changes in the fair value of financial instruments and tax		287.4	291.0
Income tax expense excluding changes in the fair value of financial instruments		80.9	82.6
Earnings before net changes in the fair value of financial instruments	1	206.5	208.4
(Gain) loss in the fair value of financial instruments		(46.7)	(80.0)
Income tax expense (credit) on changes in the fair value of financial instruments		13.8	22.4
Net profit		239.4	266.0

Statement of financial position

as at 30 June 2018

	NOTES	GROUP 2018 $M	2017 $M
ASSETS EMPLOYED			
Cash and cash equivalents		76.0	28.3
Investments	9	149.8	97.2
Trade receivables and other assets	10	137.0	142.1
Derivatives and hedge commitment in gain	7	242.4	197.6
NZPCL investment	8	76.3	77.6
Property, plant and equipment	5	4,615.0	4,589.4
Intangibles	5	377.4	389.4
Capital work in progress	5	75.0	75.9
TOTAL ASSETS EMPLOYED		5,748.9	5,597.5
FUNDS EMPLOYED			
Liabilities			
Cash and cash equivalents		1.0	–
Trade and other payables	11	96.6	107.9
Current tax liability		27.1	19.2
Deferred income	2	97.8	84.0
Derivatives and hedge commitment in loss	7	267.4	339.7
Provisions	12	58.9	30.4
Debt	6	3,152.9	3,082.8
NZPCL debt	8	77.7	74.4
Deferred tax	16	413.8	377.8
Total liabilities		4,193.2	4,116.2
EQUITY			
Capital	13	1,200.0	1,200.0
Accumulated surplus		356.8	279.0
Non-controlling interest	8	(1.1)	2.3
Total equity		1,555.7	1,481.3
TOTAL FUNDS EMPLOYED		5,748.9	5,597.5

The Board of directors of Transpower New Zealand Limited authorised these financial statements for issue on 23 August 2018.

For, and on behalf of, the Board

HON. TONY RYALL
CHAIR

PIP DUNPHY
DEPUTY CHAIR

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

Statement of changes in equity

for the year ended 30 June 2018

		GROUP				
	NOTES	**ORDINARY SHARES** $M	**RETAINED EARNINGS** $M	**OWNERS OF THE PARENT** $M	**NON-CONTROLLING INTEREST** $M	**TOTAL** $M
2017/18						
Equity at 1 July 2017		1,200.0	279.0	1,479.0	2.3	1,481.3
Profit for the period		–	242.8	242.8	(3.4)	239.4
Other comprehensive income		–	–	–	–	–
Total comprehensive income		–	242.8	242.8	(3.4)	239.4
Transactions with owners						
Dividends paid	13	–	(165.0)	(165.0)	–	(165.0)
Total equity at 30 June 2018		1,200.0	356.8	1,556.8	(1.1)	1,555.7
2016/17						
Equity at 1 July 2016		1,200.0	181.8	1,381.8	(2.3)	1,379.5
Profit for the period		–	261.4	261.4	4.6	266.0
Other comprehensive income		–	–	–	–	–
Total comprehensive income		–	261.4	261.4	4.6	266.0
Transactions with owners						
Dividends paid	13	–	(164.2)	(164.2)	–	(164.2)
Total equity at 30 June 2017		1,200.0	279.0	1,479.0	2.3	1,481.3

Non-controlling interest – refer to note 8 for a detailed description.

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

Cash flow statement

for the year ended 30 June 2018

	GROUP	
	2018	**2017**
	$M	$M
CASH FLOW FROM OPERATIONS		
Receipts from customers	1,100.6	1,059.8
Interest received	5.0	5.5
Payments to suppliers and employees	(302.1)	(281.4)
Tax payments	(50.7)	(51.3)
Interest paid	(198.5)	(210.4)
Net cash inflows from operations	554.3	522.2
CASH FLOW FROM INVESTMENTS		
Sale of property, plant and equipment	2.3	4.7
Sale of short-term investments	126.3	104.9
Purchase of property, plant and equipment and intangibles	(293.7)	(265.6)
Purchase of short-term investments	(177.7)	(74.0)
Net cash (outflows) from investments	(342.8)	(230.0)
CASH FLOW FROM FINANCING		
Increase in loans	418.5	792.7
Dividends paid	(165.0)	(164.2)
Interest rate swap terminations	(5.4)	–
Repayment of loans	(412.9)	(972.3)
Net cash (outflows) from financing	(164.8)	(343.8)
Net increase/(decrease) in cash held	46.7	(51.6)
Opening balance brought forward	28.3	79.9
Closing net cash carried forward	75.0	28.3
Closing net cash carried forward comprises:		
Cash and on-call deposits	21.9	0.9
Short-term deposits with original maturities less than three months	53.1	27.4

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

Cash flow statement reconciliation

Reconciliation of net profit (loss) with net cash flow from operations

	GROUP	
	2018	**2017**
	$M	$M
Net profit	239.4	266.0
Add (deduct) non-cash items:		
Change in the fair value of financial instruments	(47.2)	(80.3)
Depreciation, amortisation and write-offs	307.3	277.4
Deferred tax	36.0	49.0
Capitalised interest	(6.4)	(6.0)
Movements in working capital items:		
(Increase)/decrease in trade and other receivables	7.6	(7.2)
(Increase)/decrease in prepayments	(3.9)	1.2
(Decrease)/increase in trade and other payables, interest payable and deferred income	7.0	16.4
(Decrease)/increase in taxation payable	7.9	4.6
(Decrease)/increase in provisions	6.6	1.1
Net cash flow from operations	554.3	522.2

Notes to financial statements
for the year ended 30 June 2018

1. Transpower Group information

Reporting entity and statutory base

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

The Group is the owner and operator of New Zealand's national electricity grid. The Group is a for-profit entity in accordance with XRB A1 Accounting Standards Framework.

Basis of preparation

The financial statements have been presented in accordance with the State-Owned Enterprises Act 1986 and are prepared in accordance with the Financial Markets Conduct Act 2013. The financial statements have been prepared and comply with generally accepted accounting practice (GAAP) in New Zealand and the Financial Reporting Act 2013.

The financial statements comply with New Zealand Equivalents to International Financial Reporting Standards (NZ IFRS). The financial statements comply with International Financial Reporting Standards (IFRS).

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 statement of financial position are stated exclusive of GST with the exception of receivables and payables, which include GST.

The financial statements of the Group's subsidiaries are prepared in the functional currency of that entity, being New Zealand dollars. The exception to this is New Zealand Power Cayman 2003-1 Limited which has a functional currency of US dollars and a presentational currency of New Zealand dollars.

Measurement basis

The measurement basis adopted in the preparation of these financial statements is historical cost except as modified for certain investments, held for sale assets, financial assets and financial liabilities.

Transpower discloses an alternative measure of profit which is earnings before net changes in fair values of financial instruments. Transpower discloses this information as it provides a different measure of underlying performance to the IFRS mandated profit measures, which are also disclosed. The directors consider that this additional profit measure is useful additional information for users of the financial statements. Transpower has consistently reported an alternative profit on this basis since the adoption of IFRS.

1. Transpower Group information (continued)

Significant accounting policies

a) The Group financial statements consolidate the financial statements of subsidiaries as at and for the year ended 30 June 2018. Subsidiaries are those entities controlled, directly or indirectly, by Transpower.

All significant intercompany balances and transactions are eliminated on consolidation.

The Group discloses a non-controlling interest (NCI) relating to New Zealand Power Cayman 2003-1 Limited. The NCI is measured at the NCI's share of net assets.

b) Accounting policies and information about judgements that have had a significant effect on the amounts recognised in the financial statements are disclosed in the relevant notes as follows:

i. Operating revenue and deferred income	Note 2
ii. Capital assets and commitments	Note 5
iii. Debt, financial instruments and risk management	Note 6

New standards not yet adopted

Transpower has elected not to early adopt the following standards (or revisions to standards) considered to be relevant to the financial statements but not yet effective.

NZ IFRS 9 Financial instruments, effective from 1 July 2018

NZ IFRS 9 addresses the classification and measurement of financial assets and liabilities, the impairment of financial assets and hedge accounting. The only material change that will affect Transpower on adoption is that for financial liabilities the presentation of fair value movement attributing to own credit risk will move from profit or loss to other comprehensive income. For the year to June 2018, this is a loss of $12.7 million. For hedge accounting, NZ IFRS 9 adopts a more principled approach that potentially enables Transpower to adopt hedge accounting for its net debt, cross currency interest rate swaps and interest rate swaps. Transpower does not intend to adopt hedge accounting in the next financial year for these instruments. The other changes introduced by NZ IFRS 9 are the new classification model for financial assets and the new impairment model, neither of which will have a material impact upon Transpower.

NZ IFRS 15 Revenue from contracts with customers, effective from 1 July 2018

NZ IFRS 15 applies to contracts to deliver goods and services to customers. Guiding principles in the standard affect when, how and how much revenue is recognised in an entity's financial statements in any given reporting period. The standard and its subsequent amendment will replace all existing IFRS guidance for revenue recognition. Management has performed an assessment of Transpower's revenue contracts and concluded that the new standard will not have a material impact upon the financial statements.

NZ IFRS 16 Leases, effective from 1 July 2019

On adoption of NZ IFRS 16, all leases for lessees (with certain exemptions) will come onto the balance sheet. A right of use asset will be created with a materially offsetting liability. The right of use asset will be depreciated. The liability will decrease over time with an imputed interest expense recognised. Accordingly, the profit or loss impact is a decrease in leasehold expenditure and an increase in depreciation expense and imputed interest expense. Management is in the process of examining all lease contracts. It is expected that the majority of lease commitments disclosed in note 3, discounted to present value, would be capitalised as an asset and an offsetting liability created. An estimate range is that the asset and liability created would be $100–150 million with the net profit or loss difference (between the old and new standard) in any given year being +/- $3 million.

New standards adopted during the period

There were no new or revised standards adopted during the period that had a material impact on the financial statements.

2. Operating revenue and deferred income

	GROUP	
	2018	**2017**
	$M	$M
Transmission revenue		
HVAC interconnection	687.6	689.3
HVAC connection	127.3	124.4
EV (rebate) charge – HVAC	13.6	(14.5)
HVDC	133.5	126.2
EV (rebate) charge – HVDC	16.4	25.3
Other regulated transmission	4.3	4.6
Customer investment contracts	28.0	38.9
Other transmission	18.5	7.5
	1,029.2	1,001.7
Other revenue		
System operator	40.8	45.3
Other	14.4	14.1
	55.2	59.4
Total operating revenue	1,084.4	1,061.1

Description

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).

Customer investment contracts are contracts entered into with customers to build grid connection assets. Transpower recovers the cost of these assets over the life of the asset.

System operator income relates to payments received for the provision of real time services to ensure the short-term security of the New Zealand electricity system.

Included in the above numbers is revenue subject to the telecommunications development levy of $2.5 million in the year to 30 June 2018 (June 2017: $2.4 million).

Accounting policies

Transmission revenue is recorded as it is invoiced, apart from customer investment contracts. Revenue from customer investment contracts is grossed up for an imputed interest expense and recognised over the estimated life of the related assets.

Certain transactions relating to the operation of the electricity market, specifically wholesale market-related ancillary services and losses and constraint payments, are passed through and are therefore not recorded in profit or loss. This pass-through occurs because Transpower is deemed to act only as an agent. Similarly, Transpower acts as an agent relating to its natural gas market operation.

Agreements between Transpower and third parties to underground and/or realign certain transmission line assets are recognised based on the revenue source. If the revenue is received from central or local government or their agencies, the revenue is recognised according to the government grants standard (NZ IAS 20) with revenue grossed up for an imputed interest expense and recognised over the life of the related transmission assets. If revenue is received from non-government parties, it is recognised once the related assets are commissioned. The related assets are also written off.

Related disclosures

	GROUP	
	2018	**2017**
	$M	$M
Deferred income		
Customer investment contracts	35.4	19.6
Transmission realignment	58.8	60.0
Other	3.6	4.4
Total deferred income	97.8	84.0

3. Operating expenses and lease commitments

	GROUP	
	2018	**2017**
	$M	$M
Grid maintenance		
HVAC substations maintenance	44.3	41.7
HVDC substations and cables maintenance	9.5	9.2
HVAC lines maintenance	37.6	35.4
HVDC lines maintenance	1.3	1.9
Transmission-related rates	6.8	6.8
Other	7.0	8.0
	106.5	103.0
IST maintenance and operations		
Support and maintenance	9.3	10.3
Outsourced services	14.9	14.8
Licences	8.8	8.0
IST leases	8.8	9.1
	41.8	42.2
Other operating expenses		
Investigations	17.4	15.9
Ancillary service costs	3.6	4.2
Employee benefits	107.3	100.3
Capitalised salary costs	(21.0)	(19.2)
Salary transferred to investigations	(5.9)	(4.9)
Operating lease and rental costs	4.2	3.7
Industry levies	9.4	10.8
Insurance	4.2	4.3
Other business support costs	26.4	27.5
	145.6	142.6
Total operating expenses	293.9	287.8

Description

Maintenance includes inspection, servicing and repair costs.

Other grid maintenance expenses include maintenance support, communications system and training for service providers and third parties.

Investigations includes work that the Group conducts prior to the commencement of a capital project, updates to maintenance standards and demand response costs.

Other business support costs include legal fees, office equipment, communications, vehicles, travel, consultants, contractors, donations and study grants.

Accounting policies

If there are costs associated with entering into an operating lease, these costs are treated as prepayments and are amortised to operating lease and rental costs over the life of the related operating lease.

3. Operating expenses and lease commitments (continued)

Related disclosures

Fees paid to external auditor

	GROUP	
	2018	**2017**
	$000	$000
Audit of financial statements		
Audit and reviews of financial statements[1]	448	441
Other services		
Other assurance[2]	27	8
Accounting analysis on new lease standard	29	–
Training courses	40	55
Trust deed requirements[3]	11	11
Remuneration benchmarking report	6	6
	113	80
Total fees paid to external auditor	561	521

(1) This includes an annual audit and a six monthly review.

(2) In 2017, this included a report on the wash up of the System Operator service provider agreement and in 2018 this included a review of the company valuation methodology and model.

(3) Trust deed requirements include fees payable to review directors' certificates in relation to debt held against two trust deeds.

Operating lease commitments

	GROUP	
	2018	**2017**
	$M	$M
Commitments in respect of non-cancellable operating leases payable:		
Within one year	12.3	14.5
One to two years	11.6	14.6
Two to five years	30.3	42.2
Later than five years	64.4	92.3
Total operating lease commitments	118.6	163.6

The lease commitments primarily relate to the leasing of fibre optic cables for Transpower's communications network (included in IST leases) and a lease for the Wellington office building (included in operating lease and rental costs under other operating expenses).

4. Net interest expenses

	GROUP	
	2018	**2017**
	$M	$M
Interest revenue		
Interest received	5.0	5.5
	5.0	5.5
Interest expenses		
Interest expenses and associated fees	200.3	209.9
Capitalised interest	(6.4)	(6.0)
Imputed interest	6.9	6.5
	200.8	210.4
Total net interest expenses	195.8	204.9

Description

Capitalised interest is based on Transpower's forecast weighted average cost of borrowing. For 2018, capitalised interest was 6.88% (2017: 6.92%).

Imputed interest arises on deferred income and the unwinding of the discount of future cash flows related to provisions.

5. Capital assets and commitments

This note includes property, plant and equipment, intangible assets, non-current assets held for sale, capital work in progress and capital commitments.

GROUP	HVAC TRANSMISSION LINES $M	HVDC TRANSMISSION LINES $M	HVAC SUBSTATIONS $M	HVDC SUBSTATIONS AND SUBMARINE CABLES $M
At 30 June 2018				
Cost	2,596.4	149.7	2,493.5	868.0
Accumulated depreciation/amortisation	(637.6)	(53.0)	(728.4)	(325.6)
Net book value/carrying value	1,958.8	96.7	1,765.1	542.4
30 June 2018 reconciliation				
Opening net book value/carrying value (1 July 2017)	1,937.3	98.1	1,738.5	575.6
Additions/transfers	91.1	2.7	109.3	3.3
Disposals/transfers	(2.2)	(0.1)	(6.4)	(0.1)
Impairment	(1.8)	–	(2.0)	–
Depreciation/amortisation	(65.6)	(4.0)	(74.3)	(36.4)
Closing net book value/carrying value	1,958.8	96.7	1,765.1	542.4
At 30 June 2017				
Cost	2,511.2	147.4	2,403.0	865.0
Accumulated depreciation/amortisation	(573.9)	(49.3)	(664.5)	(289.4)
Net book value/carrying value	1,937.3	98.1	1,738.5	575.6
30 June 2017 reconciliation				
Opening net book value/carrying value (1 July 2016)	1,914.5	101.0	1,731.3	611.1
Additions/transfers	95.2	1.1	87.8	1.3
Disposals/transfers	(10.1)	–	(5.1)	(0.5)
Impairment	–	–	(2.5)	–
Depreciation/amortisation	(62.3)	(4.0)	(73.0)	(36.3)
Closing net book value/carrying value	1,937.3	98.1	1,738.5	575.6

COMMUNICATIONS	ADMINISTRATION ASSETS	TOTAL PROPERTY, PLANT AND EQUIPMENT	EASEMENTS AND RIGHT TO ACCESS	SOFTWARE	TOTAL INTANGIBLE ASSETS	CAPITAL WORK IN PROGRESS
$M	$M	$M	$M	$M	$M	$M
363.7	184.8	6,656.1	308.5	327.2	635.7	75.0
(186.1)	(110.4)	(2,041.1)	(4.1)	(254.2)	(258.3)	–
177.6	74.4	4,615.0	304.4	73.0	377.4	75.0
179.2	60.7	4,589.4	299.9	89.5	389.4	75.9
29.3	24.4	260.1	5.1	19.2	24.3	281.4
(0.3)	(0.5)	(9.6)	–	(0.4)	(0.4)	(282.3)
–	–	(3.8)	–	–	–	–
(30.6)	(10.2)	(221.1)	(0.6)	(35.3)	(35.9)	–
177.6	74.4	4,615.0	304.4	73.0	377.4	75.0
349.0	184.4	6,460.0	303.5	309.5	613.0	75.9
(169.8)	(123.7)	(1,870.6)	(3.6)	(220.0)	(223.6)	–
179.2	60.7	4,589.4	299.9	89.5	389.4	75.9
174.2	67.6	4,599.7	290.6	102.3	392.9	68.0
32.1	12.9	230.4	9.9	30.4	40.3	269.7
(2.0)	(4.1)	(21.8)	–	–	–	(261.8)
–	–	(2.5)	–	–	–	–
(25.1)	(15.7)	(216.4)	(0.6)	(43.2)	(43.8)	–
179.2	60.7	4,589.4	299.9	89.5	389.4	75.9

5. Capital assets and commitments (continued)

Depreciation, amortisation, write-offs and impairment

	2018	2017
	$M	$M
Total depreciation	221.1	216.4
Total amortisation	35.9	43.8
Impairment	3.8	2.5
Write-offs	46.5	14.7
	307.3	277.4

The increase in write-offs is predominantly due to an increase in the asbestos provision during the year. The provision increased by $23.9 million of which $22.6 million related to write-offs. The remaining $1.3 million of the provision related to maintenance and is recorded in operating expenses. Refer to note 12 Provisions for further detail.

Capital work in progress can be split into the following classes:

	GROUP	
	2018	2017
	$M	$M
HVAC transmission lines	19.7	23.5
HVAC substations	43.0	35.0
Communications	2.8	1.8
Other	9.5	15.6
	75.0	75.9

Description

Administration assets include computer hardware, plant, equipment, furniture and motor vehicles.

The most significant right to access asset relates to the 2011 purchase of access rights to the Vector Tunnel in Auckland for $50 million. The Vector Tunnel right to access asset is being amortised over the contract life, which is 90 years.

Accounting policies

Transpower uses the cost model for all capital assets. Capital work in progress is recorded at cost. Cost is determined by including all costs directly associated with bringing the assets to their location and condition for use. Finance costs incurred during the period of time that is required to complete and prepare the asset for its intended use are capitalised as part of the total cost for capital work in progress.

Assets are transferred from capital work in progress at cost to property, plant and equipment or intangible assets as they become operational and available for use.

At each reporting date, Transpower reviews the carrying amounts of its tangible and intangible assets and exercises judgement to determine whether there is any indication that those assets have suffered an impairment loss. This is based on allocating the assets to cash generating units. If any such indication exists, the recoverable amount of the asset or cash generating unit is estimated in order to determine the extent of the impairment loss (if any). The recoverable amount for regulated assets is generally equal to the regulatory book value for revenue recovery purposes. In 2018, there was an impairment of $3.8 million (2017: $2.5 million). The impairment in 2018 relates to a sale of a low voltage asset (classified as held for sale).

Depreciation

Depreciation of property, plant and equipment is calculated using the straight line method to write down the cost of property, plant and equipment to its estimated residual value over its estimated useful life.

Transpower has a variety of different assets with different lives. The estimated weighted average of useful lives by asset category are as follows:

HVAC transmission lines	58 years
HVAC transmission high voltage cables	45 years
HVAC transmission lines (tower painting)	15 years
HVAC substations	43 years
HVDC substations (including submarine cables)	28 years
HVDC transmission lines	55 years
Communications assets	15 years
Administration assets	16 years

5. Capital assets and commitments (continued)

Non-current assets held for sale

Non-current assets (and disposal groups) classified as held for sale are measured at the lower of carrying amount and fair value less costs to sell.

Intangibles

The cost of acquiring a finite-life intangible asset is amortised from the date the underlying asset is held ready for use on a straight line basis over the period of its expected benefit, which is as follows:

Software	5–8 years
Right to access asset	90 years

Easements are deemed to have an indefinite useful life and are tested for impairment annually.

Certain easements have been donated by the Crown. These are recognised at cost (nil) plus any direct cost associated with putting the easement in place.

Key judgements

Transpower has exercised judgement in the following four areas:

- determining the useful life of property, plant and equipment and finite-life intangible assets. Transpower uses assistance from independent engineers. For transmission line assets, a determining factor in the life assumption is proximity to the coast
- whether or not an item is capital in nature and the appropriate component level of asset at which to depreciate
- determining the appropriate time to commission an asset and commence depreciation
- whether there are any regulated assets that ought to be impaired. See above discussion in accounting policies.

Related disclosures

Land and buildings are contained within the above classes and have a net book value of $257.5 million (2017: $250.8 million).

Held for sale non-current assets are contained within the above classes and have a net book value of $5.5 million (2017: $1.5 million).

	GROUP	
	2018	**2017**
	$M	$M
Capital commitments in respect of contracts for property, plant and equipment		
Property, plant and equipment	151.4	106.1
	151.4	106.1
Capital commitments in respect of contracts for intangible assets		
Easements and right to access assets	0.1	0.1
Software	–	–
	0.1	0.1
Total capital commitments	151.5	106.2

6. Debt, financial instruments and risk management

(a) Summary

Debt is issued by the Group in both New Zealand dollars (NZD) and foreign currencies. Derivatives are used to manage currency risk and interest rate risk by converting foreign borrowings to NZD and by converting floating interest rates to fixed interest rates. The use of derivatives means that Transpower effectively has borrowings denominated in NZD, predominantly at fixed interest rates.

Debt and associated derivatives are designated as fair value through profit or loss on the basis of preventing an accounting mismatch. The Group's debt and derivatives are managed as one integrated portfolio.

The Group also uses derivatives (foreign exchange forward contracts) in its purchase of goods and services.

The Group is subject to a number of financial risks that arise as a result of its business activities, including having a debt portfolio that is denominated in both NZD and foreign currencies, holding an investment portfolio and from purchases in certain foreign currencies.

Financial risk management is carried out by a central treasury function, which operates under policies approved by the Board of directors.

Key judgements

The fair values of debt and derivatives are determined by converting currency exposures and discounting cash flows based on the relevant yield curve. The yield curve is adjusted to reflect the credit risk of the counterparty to the transaction or the credit risk of Transpower. These valuations are considered level two in the IFRS three-level valuation hierarchy.

(b) Financial risks

i. Liquidity risk

Liquidity risk is the risk of the Group being unable to access sufficient funds to meet its financial obligations in an orderly manner. This might result from the Group not maintaining adequate funding facilities or being unable to replace existing debt maturities.

To smooth the Group's refinancing requirements in future periods, the Group's policy is that committed funding facilities maturing in any 12-month period are not to exceed NZD750 million.

Term debt

The Group has four debt facilities. The aggregate principal amount of the debt outstanding may not exceed the following:

	CURRENCY	FOREIGN CURRENCY EQUIVALENT	NZD
		$M	$M
Domestic medium-term note programme	NZD	–	No set limit
Australian medium-term note programme	AUD	750	821
European commercial paper programme (ECP)	USD	500	739
Domestic commercial paper programme (CP)	NZD	–	500

In addition to the above, the Group's liquidity policy requires the Group to have access to committed funding facilities to cover the sum of all debt that matures over the next six months plus peak cumulative anticipated operating cash flow requirements over the next six months. To meet this policy requirement Transpower has committed standby facilities split into two tranches of NZD250 million each, maturing 7 December 2018 and 6 December 2019. The facilities have been undrawn since inception.

6. Debt, financial instruments and risk management (continued)

ii. Interest rate risk

Interest rate risk is the risk of an adverse impact on the present and future finance costs of the Group arising from an increase in interest rates. Transpower uses various financial instruments to fix interest rates to mitigate interest rate risk.

The Group's policy sets minimum and maximum hedging parameters expressed as a percentage of forecast debt. Interest rate swaps and options are used to change the interest rate profile on existing and forecast debt and cross-currency interest rate swaps entered into.

iii. Currency risk

Currency risk on debt is the risk of adverse impact of exchange rate movements, which determine the NZD cost of debt (principal and interest) issued in foreign currencies.

Foreign currency borrowings are converted into a NZD-denominated exposure at the time of commitment to drawdown. Currency risk on foreign currency-denominated borrowings is managed using cross-currency interest rate swaps and basis swaps.

Cross-currency interest rate swaps eliminate foreign currency risk on the underlying debt by determining the NZD equivalent of the interest payments and final principal exchange at the time of entering into the swap.

Basis swaps are used to eliminate currency basis risk when the Group issues bonds in a foreign currency. In a basis swap, the Group receives the offshore currency floating interest rate and pays the NZD floating interest rate.

Currency risk on foreign currency-denominated purchases is the risk of adverse impact of exchange rate movements which determine the NZD cost of foreign currency-denominated purchases. It is the Group's policy to hedge committed foreign currency-denominated payments greater than NZD100,000 (NZD equivalent) by using forward foreign exchange contracts to fix or offset the NZD cost. For committed payments below NZD100,000 the Group has discretion on whether or not to hedge.

6. Debt, financial instruments and risk management (continued)

Debt and related derivatives – interest rate, currency and liquidity risk

The following table details Transpower's debt and associated derivatives. The result after derivatives is that Transpower effectively has a debt portfolio in New Zealand dollars at predominantly fixed interest rates across multiple repayment dates. The derivatives in the table below are interest rate swaps and cross-currency interest rate swaps that relate directly to the particular debt issue. The effective interest rate on debt including the effect of derivative financial instruments was 6.8% (2017: 6.8%).

GROUP 2018	DEBT CURRENCY	DEBT AND DERIVATIVE MATURITY DATE	DEBT FACE VALUE	DEBT FAIR VALUE	DERIVATIVE FAIR VALUE	TOTAL DEBT + DERIVATIVES FAIR VALUE
			$M	NZ$M	NZ$M	NZ$M
Bonds						
Bonds 2018	NZD	30-Nov-18	325.0	330.1	(3.1)	327.0
Bonds 2019	NZD	6-Sep-19	200.0	207.4	(5.4)	202.0
Bonds 2019	NZD	12-Nov-19	50.0	53.4	(3.2)	50.2
FRN CPI linked	NZD	15-May-20	100.0	99.6	1.4	101.0
Bonds 2020	NZD	10-Jun-20	150.0	162.1	(13.4)	148.7
Bonds 2022	NZD	30-Jun-22	150.0	158.8	(6.5)	152.3
Bonds 2022	NZD	16-Sep-22	100.0	104.0	(3.8)	100.2
Bonds 2023	NZD	15-Mar-23	50.0	55.0	(4.3)	50.7
Bonds 2025	NZD	6-Mar-25	125.0	125.4	(2.7)	122.7
Bonds 2028	NZD	15-Mar-28	100.0	113.2	(12.4)	100.8
European medium-term notes						
HKD EMTN	HKD	24-Mar-20	400.0	78.2	(4.6)	73.6
AUD EMTN	AUD	6-Aug-21	150.0	173.3	(6.5)	166.8
AUD EMTN	AUD	28-Aug-23	300.0	373.8	(25.8)	348.0
US private placement						
USPP 2019	USD	27-Sep-19	75.0	116.5	6.2	122.7
USPP 2021	USD	13-Oct-21	232.0	348.1	(52.2)	295.9
USPP 2022	USD	15-Dec-22	150.0	224.6	(18.9)	205.7
USPP 2023	USD	13-Oct-23	78.0	117.1	(17.6)	99.5
USPP 2026	USD	28-Jun-26	75.0	104.4	7.9	112.3
USPP 2026	USD	13-Oct-26	70.0	105.2	(17.0)	88.2
USPP 2028	USD	28-Jun-28	75.0	102.7	8.7	111.4
				3,152.9	(173.2)	2,979.7

Debt short-term		–
Current portion of long-term debt		330.1
Debt short-term		330.1
Debt long-term		2,822.8
Total debt as per statement of financial position		3,152.9
Debt face value (as per above)		
New Zealand dollar debt	1,350.0	
Foreign debt after adjusting for related cross-currency interest rate swaps	1,593.2	
	2,943.2	

The notional amount of the cross-currency interest rate swaps is NZD1,593.2 million.

6. Debt, financial instruments and risk management (continued)

Interest rate swaps (IRS) are used to fix interest payments as per the Group's treasury policy. The table below shows the notional IRS that are not directly related to underlying debt. The table includes forward starting and offsetting IRS. The IRS are net settled. The table below reflects the net cash outflows comprising both IRS assets and liabilities. IRS with unrealised gains are assets, and IRS with unrealised losses are liabilities.

	DERIVATIVE NOTIONAL VALUE	DERIVATIVE FAIR VALUE
	$M	$M
Value of interest rate swaps – liabilities	4,005.0	241.3
Value of interest rate swaps – assets	1,180.0	(43.1)
Total fair value of interest rate swaps		198.2
Total fair value of debt-related derivatives as shown above		(173.2)
Total debt derivatives fair value (refer to note 7 for further derivatives breakdown)		25.0

Effective net payable contractual cash flow maturity profile

The effective net cash flows on floating rate payments are determined by applying the applicable swap curve to determine the expected future cash flows.

	WITHIN ONE YEAR	ONE TO TWO YEARS	TWO TO THREE YEARS	THREE TO FOUR YEARS	FOUR TO FIVE YEARS	GREATER THAN FIVE YEARS	TOTAL
	$M	$M	$M	$M	$M	$M	$M
Debt	453.0	798.7	84.2	731.5	424.5	1,084.0	3,575.9
Debt-related derivatives	(35.2)	(17.0)	(8.1)	(61.3)	(19.1)	(13.2)	(153.9)
Interest rate swap (portfolio) – liabilities	100.4	89.4	13.4	13.8	12.5	24.6	254.1
Interest rate swap (portfolio) – assets	(13.1)	(9.6)	(6.1)	(6.0)	(4.8)	(7.4)	(47.0)
Trade and other payables	95.7	0.2	0.3	0.2	–	0.2	96.6
Total contractual cash flows	600.8	861.7	83.7	678.2	413.1	1,088.2	3,725.7

Reconciliation of liabilities arising from financing activities

	BALANCE 1 JULY 2017	CASH FLOWS	FAIR VALUE CHANGES	OTHER	BALANCE 30 JUNE 2018
Short-term borrowing	119.5	(119.4)	–	(0.1)	–
Long-term borrowing	2,963.3	125.0	59.1	5.5	3,152.9
Total liabilities from financing activities	3,082.8	5.6	59.1	5.4	3,152.9

Fair value changes in the table above include foreign exchange movements.

6. Debt, financial instruments and risk management (continued)

Debt and related derivatives – interest rate, currency and liquidity risk

The following table details Transpower's debt and associated derivatives. The result after derivatives is that Transpower effectively has a debt portfolio in New Zealand dollars at predominantly fixed interest rates across multiple repayment dates. The derivatives in the table below are interest rate swaps and cross-currency interest rate swaps that relate directly to the particular debt issue. The effective interest rate on debt including the effect of derivative financial instruments was 6.8% (2016: 6.9%).

GROUP 2017	DEBT CURRENCY	DEBT AND DERIVATIVE MATURITY DATE	DEBT FACE VALUE	DEBT FAIR VALUE	DERIVATIVE FAIR VALUE	TOTAL DEBT + DERIVATIVES FAIR VALUE
			$M	NZ$M	NZ$M	NZ$M
Commerial paper						
NZD Issue Aug	NZD	24-Aug-17	34.8	34.9	–	34.9
NZD Issue Sep	NZD	4-Sep-17	29.8	29.9	–	29.9
NZD Issue Sep	NZD	18-Sep-17	29.8	29.9	–	29.9
NZD Issue Sep	NZD	28-Sep-17	24.8	24.8	–	24.8
Bonds						
Bonds 2018	NZD	30-Nov-18	325.0	336.9	(8.7)	328.2
Bonds 2019	NZD	6-Sep-19	200.0	209.9	(6.7)	203.2
Bonds 2019	NZD	12-Nov-19	50.0	55.2	(4.8)	50.4
FRN CPI linked	NZD	15-May-20	100.0	98.9	2.4	101.3
Bonds 2020	NZD	10-Jun-20	150.0	166.0	(18.1)	147.9
Bonds 2022	NZD	30-Jun-22	150.0	153.2	(4.8)	148.4
Bonds 2022	NZD	16-Sep-22	100.0	102.0	(2.2)	99.8
Bonds 2023	NZD	15-Mar-23	50.0	54.5	(3.7)	50.8
Bonds 2028	NZD	15-Mar-28	100.0	109.9	(9.7)	100.2
European medium-term notes						
HKD EMTN	HKD	24-Mar-20	400.0	75.1	(1.7)	73.4
AUD EMTN	AUD	6-Aug-21	150.0	166.8	(2.3)	164.5
AUD EMTN	AUD	28-Aug-23	300.0	360.4	(14.5)	345.9
US private placement						
USPP 2019	USD	27-Sep-19	75.0	112.4	9.9	122.3
USPP 2021	USD	13-Oct-21	232.0	332.8	(36.1)	296.7
USPP 2022	USD	15-Dec-22	150.0	215.7	(13.7)	202.0
USPP 2023	USD	13-Oct-23	78.0	112.6	(13.1)	99.5
USPP 2026	USD	28-Jun-26	75.0	100.4	11.3	111.7
USPP 2026	USD	13-Oct-26	70.0	101.7	(14.3)	87.4
USPP 2028	USD	28-Jun-28	75.0	98.9	11.8	110.7
				3,082.8	(119.0)	2,963.8

Debt short-term		119.5
Current portion of long-term debt		–
Debt short-term		119.5
Debt long-term		2,963.3
Total debt as per statement of financial position		3,082.8
Debt face value (as per above)		
New Zealand dollar debt	1,344.2	
Foreign debt after adjusting for related cross-currency interest rate swaps	1,593.2	
	2,937.4	

The notional amount of the cross-currency interest rate swaps is NZD1,593.2 million.

6. Debt, financial instruments and risk management (continued)

Interest rate swaps (IRS) are used to fix interest payments as per the Group's treasury policy. The table below shows the notional IRS that are not directly related to underlying debt. The table includes forward starting and offsetting IRS. The IRS are net settled. The table below reflects the net cash outflows comprising both IRS assets and liabilities. IRS with unrealised gains are assets and IRS with unrealised losses are liabilities.

	DERIVATIVE NOTIONAL VALUE	DERIVATIVE FAIR VALUE
	$M	$M
Value of interest rate swaps – liabilities	4,205.0	303.0
Value of interest rate swaps – assets	1,280.0	(41.9)
Total fair value of interest rate swaps		261.1
Total fair value of debt-related derivatives as shown above		(119.0)
Total debt derivatives fair value (refer to note 7 for further derivatives breakdown)		142.1

Effective net payable contractual cash flow maturity profile

The effective net cash flows on floating rate payments are determined by applying the applicable swap curve to determine the expected future cash flows.

	WITHIN ONE YEAR	ONE TO TWO YEARS	TWO TO THREE YEARS	THREE TO FOUR YEARS	FOUR TO FIVE YEARS	GREATER THAN FIVE YEARS	TOTAL
	$M	$M	$M	$M	$M	$M	$M
Debt	245.4	443.5	771.5	75.6	693.4	1,298.4	3,527.9
Debt-related derivatives	(33.3)	(17.5)	20.0	9.4	(15.6)	52.8	15.8
Interest rate swap (portfolio) – liabilities	116.4	88.3	65.7	10.6	10.7	29.8	321.5
Interest rate swap (portfolio) – assets	(18.1)	(10.2)	(5.5)	(3.3)	(2.9)	(4.8)	(44.8)
Trade and other payables	106.8	0.2	0.3	0.2	–	0.4	107.9
Total contractual cash flows	417.2	504.3	852.0	92.5	685.7	1,376.6	3,928.3

Reconciliation of liabilities arising from financing activities

	BALANCE 1 JULY 2016	CASH FLOWS	FAIR VALUE CHANGES	OTHER	BALANCE 30 JUNE 2017
Short-term borrowing	–	119.4	–	0.1	119.5
Long-term borrowing	3,333.9	(298.8)	(68.5)	(3.3)	2,963.3
Total liabilities from financing activities	3,333.9	(179.4)	(68.5)	(3.2)	3,082.8

Fair value changes in the table above include foreign exchange movements.

iv. Credit risk

Credit risk is the risk of adverse impact on the Group through the failure of a counterparty bank, financial institution or customer to meet its financial obligations. Transpower's credit risk arises from financial assets. These include investments, derivatives and accounts receivable.

Treasury credit risk

The Group's policy is to establish credit limits with counterparties that are either a bank, a financial institution, a special-purpose derivative products company or a New Zealand corporate. These net credit limits are not to exceed the lesser of 20% of Group shareholders' funds or 15% of the shareholders' funds of the counterparty as shown in the most current audited annual report. In addition, if the counterparty is a New Zealand corporate, the credit limit for investments is not to exceed $40 million.

Counterparties must have a minimum long-term Standard & Poor's credit rating of A or above (or Fitch or Moody's equivalent). The exception to these minimum credit ratings is for Risk Reinsurance Limited (RRL) investments, which invests in counterparties with credit ratings to BBB. However, RRL counterparty exposures are limited to $4 million or less, by individual counterparty, and exposures are monitored on a daily basis.

6. Debt, financial instruments and risk management (continued)

For those counterparties with which the Group has a collateral support agreement (CSA), the counterparty credit limit for derivatives is defined as the maximum exposure threshold dictated by the CSA.

The maximum credit exposure in respect of non-derivative assets is best represented by their carrying value.

The credit risk arising from the use of derivative products is minimised by the netting and set-off provisions contained in the Group's International Swaps and Derivatives Association (ISDA) agreement. Under these agreements, transactions are net settled. Therefore, the maximum credit exposure is best represented by the net mark to market valuation by counterparty where the net valuation is positive as follows:

	GROUP	
	2018	**2017**
	$M	**$M**
Cross-currency interest rate swaps (CCIRS)	119.8	66.3
Interest rate swaps (IRS)	8.2	–
Foreign exchange forward contracts	1.6	–
Total	129.6	66.3

The movement in value of CCIRS is driven by a move in the New Zealand dollar lower against the CCIRS derivatives used to hedge foreign currency debt. The NZD/USD exchange rate moved from NZD1.00/USD0.73 to NZD1.00/USD0.68.

The breakdown of the CCIRS by counterparty is as follows:

	GROUP	
	2018	**2017**
	$M	**$M**
ANZ Bank New Zealand Limited	46.2	29.2
Bank of New Zealand	25.8	14.5
Citibank N.A.	12.7	3.8
Commonwealth Bank of Australia	25.6	18.8
Westpac Banking Corporation	9.5	–
	119.8	66.3

Customer credit risk

Transpower recovers the value of its transmission assets over their useful lives in accordance with Commerce Commission input methodology regulations. The effect of these regulations is that for the majority of assets a customer default would result in Transpower recovering any revenue shortfall from all other transmission customers.

Transpower's customers comprise predominantly electricity generators, distribution companies and some large industrial users. There is a high concentration of credit risk with respect to trade receivables due to the small number of significant customers from which the majority of revenue is received. It is the Group's policy to perform credit evaluations on customers requiring credit, and the Group may in some circumstances require collateral. Collateral held at 30 June 2018 was $0.2 million (June 2017: $0.2 million). The Group holds bank guarantees to protect itself in the event private developers are unable to pay any outstanding balances owing on transmission realignment projects performed on their behalf. The bank guarantee reduces as payments are made by the developers.

The entities below have receivables balances greater than 10% of the total trade receivables of $99.0 million at 30 June 2018 (June 2017: $106.5 million).

	GROUP	
	2018	**2017**
	$M	$M
Vector Limited	20.1	21.4
Meridian Energy Limited	12.0	11.8
Powerco Limited	12.8	10.9

There is a specific credit risk in relation to customer default on customer investment contracts where revenue is recovered from individual customers over time for specific assets already in use. Transpower believes the majority of this risk relates to certain large industrial users. Transpower monitors the creditworthiness of these organisations. The largest credit risk in this category relates to an organisation with future receivables out to 2046 of $8.2 million on a net present value basis.

There have been no customer defaults in 2018 (2017: nil).

6. Debt, financial instruments and risk management (continued)

v. *Sensitivity analysis*

Currency risk – debt

All foreign currency debt is converted back to NZD, eliminating foreign currency exposure. Therefore, no sensitivity analysis has been performed for foreign currency debt.

Interest rate risk

The Group has minimal interest rate exposure, given that the majority of the net debt and derivative portfolio is fixed. Therefore, no sensitivity analysis has been performed on interest rate risk.

Fair value risk

The Group's net debt is designated as fair value through profit or loss. As such, the Group is subject to fair value gains or losses. Fair value gains and losses are measured by discounting cash flows on debt and derivatives using market interest rates or yield curves. A move upwards of interest rates and yield curves results in fair value gains and a move downwards results in fair value losses.

A parallel shift in the yield curve by 1% (100 basis points) or the same movement due to a change in credit spreads would create the following fair value movements based on debt, investments and derivatives held at balance date:

GROUP	2018	2018	2017	2017
Yield curve interest rate change	+100bp	-100bp	+100bp	-100bp
	$M	$M	$M	$M
Yield curve impact on pre-tax profit/(loss)/equity	53.4	(54.6)	82.7	(85.6)

vi. *Commodity risk*

Commodity risk is the risk of an adverse impact in commodity prices such as prices for aluminium and copper. These are some of the raw materials used in the construction of the electricity transmission network. Generally, Transpower has contracts in which commodity risk is borne by the supplier.

vii. *Insurance risk*

Transpower operates a captive insurance company through its subsidiary Risk Reinsurance Limited (RRL) and also has external insurance. RRL maintains an investment portfolio to meet insurance claims.

The insurance is outlined in the table below.

Insurance policy	AMOUNT INSURED	DEDUCTIBLE	RRL RETAINED RISK	EXTERNALLY INSURED RISK	TOTAL INSURED
	$M	$M	$M	$M	$M
HVDC submarine cables	0–15	–	15.0	–	
	15–40	–	8.7	16.3	90.0
	40–90	–	–	50.0	
Other grid assets (excluding transmission lines)	0–10	0.1	9.9	–	750.0
	10–750	–	–	740.0	
Transmission lines	0–10	0.1	9.9	–	10.0

For the HVDC cables above, RRL would pay up to the first $15 million of any claim and 35% of the layer between $15–40 million, with the remaining 65% covered by external insurance providers on a pro-rata basis. The remaining layer between $40–90 million is covered entirely by external insurance providers.

viii. *Regulatory risk*

Transpower is a natural monopoly and is regulated by The Commerce Commission (CC). The CC determines what rate of return applies to Transpower's assets. It also determines the incentives that apply to Transpower, which covers operating expenditure, capital expenditure and meeting certain deliverables and outage targets.

There is a risk that Transpower's rate of return may be set at too low a level to compensate Transpower for undertaking investments in grid assets. There is also a risk Transpower does not perform against the targets set by the CC. The CC can penalise Transpower for failing to reach targets or reward Transpower for exceeding targets. The network performance incentive is +/- $10 million per annum. The operating expenditure and base capex incentive is one third of the overspend or underspend.

7. Derivatives and hedge commitment

This note shows the short-term (ST) and long-term (LT) breakdown of the derivatives and hedge commitments.

	GROUP						
	ST ASSET	LT ASSET	TOTAL ASSET	ST (LIABILITY)	LT (LIABILITY)	TOTAL (LIABILITY)	NET ASSET (LIABILITY)
	$M	$M	$M	$M	$M	$M	$M
2018							
Debt-related derivatives							
Cross-currency interest rate swaps	–	142.6	142.6	–	(22.7)	(22.7)	119.9
Interest rate swaps	36.7	61.2	97.9	(102.7)	(140.1)	(242.8)	(144.9)
Purchasing-related derivatives and hedge commitment							
Foreign exchange forward contracts	1.5	0.2	1.7	(0.1)	(0.1)	(0.2)	1.5
Commitment on fair value hedges	0.1	0.1	0.2	(1.5)	(0.2)	(1.7)	(1.5)
Total derivatives and hedge commitment	38.3	204.1	242.4	(104.3)	(163.1)	(267.4)	(25.0)
2017							
Debt-related derivatives							
Cross-currency interest rate swaps	–	95.8	95.8	–	(33.1)	(33.1)	62.7
Interest rate swaps	44.9	55.7	100.6	(120.0)	(185.4)	(305.4)	(204.8)
Purchasing-related derivatives and hedge commitment							
Foreign exchange forward contracts	–	–	–	(0.6)	(0.6)	(1.2)	(1.2)
Commitment on fair value hedges	0.6	0.6	1.2	–	–	–	1.2
Total derivatives and hedge commitment	45.5	152.1	197.6	(120.6)	(219.1)	(339.7)	(142.1)

Description

Derivatives are used to manage financial risk. The gain or loss on derivatives represents the unrealised gain or loss at balance date. The Group anticipates that the derivatives will be held until maturity and it is unlikely that settlement at the reported fair values will occur.

Accounting policies

Derivative financial instruments

The Group uses derivative financial instruments to reduce its exposures to fluctuations in foreign currency exchange rates and interest rates. All derivatives are classified as fair value through profit and loss except for those derivatives that are used to reduce foreign currency exposure on purchases. These hedges are designated as fair value hedges. For fair value hedging relationships, gains or losses on hedging instruments are included in profit or loss together with any change in the fair value of the hedged purchase commitment attributable to the foreign currency risk.

The valuation technique and key inputs used to value the derivatives are disclosed in note 6: Debt, financial instruments and risk management.

8. NZPCL debt and investment

	GROUP	
	2018	**2017**
	$M	$M
Investment		
Current	–	–
Non-current	76.3	77.6
	76.3	77.6
Debt		
Current	–	–
Non-current	77.7	74.4
	77.7	74.4
Net investment (debt)	(1.4)	3.2
Non-controlling interest net of tax	(1.1)	2.3

Description

In November 2009, the Group partially terminated the 2003 cross-border lease in respect of the majority of the HVAC transmission assets in the South Island. As a result of the partial termination, Transpower has consolidated a special-purpose vehicle, New Zealand Power Cayman 2003-1 Limited (NZPCL). NZPCL has a USD deposit with a financial institution and a USD loan from another financial institution. The cash flows from the deposit and loan offset. No consideration was transferred. The loan to NZPCL is guaranteed by Transpower.

As Transpower has no legal ownership interest in NZPCL, the net liabilities and any movements in net liabilities are recognised as a non-controlling interest. The substance of the transaction is such that Transpower rather than the non-controlling interest would be responsible for any shortfall between the value of the asset and the liability.

Accounting policies

The loan and the deposit are recognised at fair value in the Group financial statements based on discounted cash flows. These financial instruments are designated as fair value through profit or loss.

The difference between the asset and liability is due to the yield curves that have been applied to the cash flows. These valuations are considered level two in the IFRS three-level valuation hierarchy.

9. Investments

	GROUP	
	2018	2017
	$M	$M
Risk Reinsurance Limited investments		
– Deposits	40.8	28.4
– Floating rate notes	–	1.0
– Corporate bonds	46.7	67.8
	87.5	97.2
Transpower investments		
– Deposits	62.3	–
Total investments	149.8	97.2

Description

Transpower has a captive insurance company called Risk Reinsurance Limited (RRL). RRL invests premiums received from Transpower. RRL reinsures externally and maintains sufficient investments to meet expected claims. RRL does not offer insurance to any external parties.

For RRL cash and bond holdings, the counterparties have maximum limits depending on their ratings. Investments in deposits, floating rate notes and corporate bonds were made in financial instruments issued by organisations with credit ratings of BBB or above.

Accounting policies

If the market for a financial asset is not active, fair value is established by using discounted cash flow analysis based on the relevant yield curve. The yield curve is adjusted to reflect the credit risk of the counterparty to the transaction. Deposits, floating rate notes and corporate bonds are considered level two in the NZ IFRS 13 three-level valuation hierarchy.

RRL investments are classified as fair value through profit or loss. This classification is on the basis that RRL has an active investment programme (held for trading).

The investments are current assets.

10. Trade receivables and other assets

	GROUP	
	2018	**2017**
	$M	$M
Current		
Trade and other receivables	98.9	106.5
Prepayments	11.7	7.7
Inventory	2.0	3.4
	112.6	117.6
Non-current		
Prepayments	24.4	24.5
Total trade and other receivables	137.0	142.1

Ageing of trade receivables		
Current	98.9	106.5
Past 31 days	–	–
	98.9	106.5

Description

The prepayments predominantly relate to telecommunication lease connection fees.

There was no impairment of receivables during the year (2017: nil).

Accounting policies

Trade receivables are measured initially at fair value and subsequently at amortised cost. The fair value is materially similar to amortised cost. Due to the short-term nature of the receivables, no discounting is applied.

11. Trade and other payables

	GROUP	
	2018	**2017**
	$M	$M
Current		
Trade creditors and accruals	85.4	96.7
Employee entitlements	10.3	10.1
	95.7	106.8
Non-current		
Other non-current payables	0.9	1.1
Total trade and other payables	96.6	107.9

Accounting policies

Trade and other payables are measured initially at fair value and subsequently at amortised cost. The fair value is materially similar to amortised cost. Due to the short-term nature of the payables, no discounting is applied.

12. Provisions

	GROUP			
	CONTRACTOR PROVISION	DISMANTLING & ENVIRONMENTAL HAZARDS	OTHER	TOTAL
	$M	$M	$M	$M
Balance at 1 July 2017	15.0	9.3	6.1	30.4
Provisions made during the period	0.3	28.9	7.5	36.7
Provisions used during the period	(0.1)	(5.3)	(2.8)	(8.2)
Provisions reversed during the period	–	–	–	–
Balance at 30 June 2018	15.2	32.9	10.8	58.9
Current portion of provisions	15.2	4.7	3.2	23.1
Non-current portion of provisions	–	28.2	7.6	35.8
Balance at 30 June 2018	15.2	32.9	10.8	58.9

Description

Contractor provision

Transpower has determined that a future payment to a contractor should be recognised as a provision. Accordingly, the future cash flow has been present valued and recognised as a provision and also capitalised as property, plant and equipment. The present value is being amortised as the interest incurred and the provision used each year. The future payment will occur if certain assets are free from defects and have met prescribed service levels.

Dismantling and environmental hazards

Transpower recognises environmental hazard and dismantling costs where it believes a reliably measurable obligation exists. Transpower has estimated these costs based on engineering advice. Actual costs may vary from the figures indicated.

In the year to June 2018, the provision increased by $23.9 million due to asbestos-related dismantling and maintenance costs. The expense is split between write-offs $22.6 million (note 5) and maintenance expense $1.3 million (note 3). Before June 2018, an asbestos provision was recognised on approval of a business case to undertake non-capital work. The additional provision of $23.9 million has been created based on improved information, the completion of a detailed asbestos risk register of all Transpower sites and a cost history of completed asbestos jobs. The risk register was compiled based on site visits from three approved assessors. Items that had asbestos were classified between 'remove', 'encapsulate' or 'leave in situ and manage'.

The following key assumptions and estimations have been used in creating the provision:

- all items classified as remove or encapsulate have been booked to the provision
- the leave in situ and manage items have been analysed, and it was concluded that 23% of these items would be disturbed by known future work. Therefore, 23% of the costs have been booked to the provision
- if the work involves encapsulation or removal of dust, the expense has gone to maintenance. All other costs have gone to dismantling write-offs expense
- the cost for each job has been estimated based on Transpower's history of asbestos removal to date and based on engineering advice.

Accounting policies

Provisions are liabilities of uncertain timing or amount. They are measured at the amounts expected to be paid when the liabilities are settled.

13. Equity

Capital

Transpower has 1,200,000,000 issued and fully paid $1 ordinary shares. Transpower's authorised capital is $1,200,000,000 (2017: $1,200,000,000). The shares confer on the holders the right to vote at any annual general meeting of Transpower. All shares rank equally.

The Group manages capital to maintain its strong credit rating and to have sufficient capital available to meet its financing and operating requirements. Surplus equity is returned by way of dividends to shareholders.

Credit rating

Transpower's investment grade credit rating is Standard & Poor's AA- (2017: AA-) and Moody's Aa3 (2017: A1)

Net tangible assets per share

	GROUP	
	2018	**2017**
	$M	$M
Net assets (equity)	1,555.7	1,481.3
Less intangibles (note 5)	(377.4)	(389.4)
Total net tangible assets	1,178.3	1,091.9
Net tangible assets per share ($)	0.98	0.91

Dividends

Dividends declared and provided by Transpower are as follows:

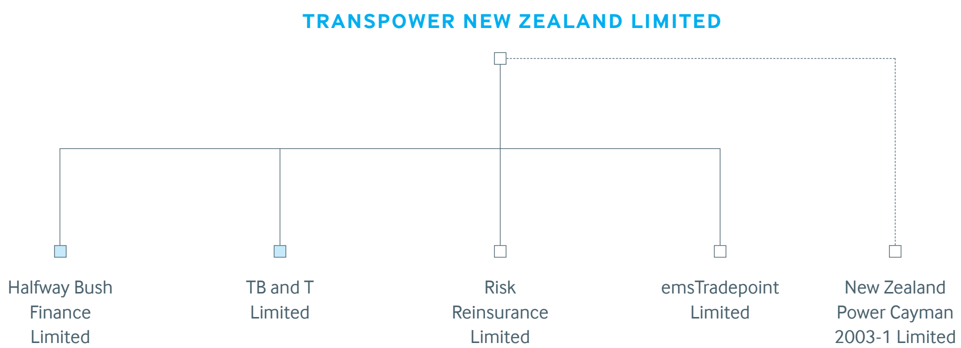
	2018 $M	**2018** CENTS PER SHARE	**2017** $M	**2017** CENTS PER SHARE
Previous year final dividend paid	99.0	8	98.2	8
Interim dividend paid	66.0	6	66.0	6
	165.0	14	164.2	14
Final dividend declared subsequent to balance date (refer note 19)	99.0	8	99.0	8

Group entities

All subsidiaries are wholly owned, are incorporated in New Zealand (except where specified otherwise) and have a balance date of 30 June 2018.

Transpower has no ownership interest in NZPCL. NZPCL is a special-purpose vehicle registered in the Cayman Islands and is consolidated for financial reporting, indicated by the dotted line in the diagram below. Refer to note 8 NZPCL debt and investment for more detail. Risk Reinsurance Limited is registered and incorporated in the Cayman Islands and was established to provide insurance for the Transpower Group.

As at balance date, the group entities are as follows:



Party to a cross-border lease over the majority of the South Island HVAC assets.

14. Segment reporting

In 2018, the Group has one reportable segment – transmission. The transmission segment activities include the transmission of electricity from the point of generation to the point of connection.

This segment has external revenue derived from New Zealand customers and its assets are based in New Zealand.

The Group has no other reportable segments. The balance of the financial information (that is not the transmission segment) is reported as 'other' in the table below.

The material portions of the other balance is made up of the following discrete activities:

- **System operator** – the provision of real-time services to ensure the short-term security of the New Zealand electricity system
- **RRL** – established in 2001 to provide insurance services to the Group.

Segment results are determined based on information provided to the Chief Operating Decision Maker. They are calculated using the avoidable cost allocation methodology (ACAM).

Major customers

External customers that contribute 10% or more of total Group revenue are:

CUSTOMER	% OF GROUP REVENUE	SEGMENT
Vector Limited	18.7 (2017: 19.5)	Transmission
Meridian Energy Limited	11.3 (2017: 11.6)	Transmission

	TRANSMISSION		OTHER		ADJUSTMENTS		TOTAL	
	2018	**2017**	**2018**	**2017**	**2018**	**2017**	**2018**	**2017**
	$M	$M	$M	$M	$M	$M	$M	$M
External revenue	1,022.6	995.3	54.9	59.3	6.9	6.5	1,084.4	1,061.1
Capex	274.0	261.3	7.4	8.6	–	–	281.4	269.9

The adjustment is:

	2018	**2017**	**EXPLANATION**
	$M	$M	
External revenue	6.9	6.5	Financial statements include imputed interest in non-operating expenses, net interest expenses (note 4) rather than revenue.

15. Change in fair value of financial instruments

	GROUP	
	2018	**2017**
	$M	$M
Accounting hedges		
Foreign exchange forward contracts – hedge accounted	(2.7)	(0.5)
Hedge commitment	2.7	0.5
	–	–
Other		
Foreign debt	70.9	(55.5)
Cross-currency interest rate swaps	(56.4)	75.6
NZD interest rate swaps	(53.3)	(76.9)
Investments	(0.7)	0.3
NZD debt	(7.2)	(23.5)
	(46.7)	(80.0)
Total fair value (gain) loss	(46.7)	(80.0)

Description

The Group experiences fair value movements through movements in underlying interest rates and exchange rates on debt and derivatives, and movements in credit spread.

The Group generally seeks to fix interest rates to provide certainty of interest rate costs. This means that, prima facie, a decrease in market interest rates will result in the Group sustaining fair value losses, and conversely, an increase in market interest rates will result in fair value gains.

Credit spreads are an estimate of the additional premium over the relevant yield curve that would be required by market participants to compensate them for the perceived credit risk inherent in the counterparty and transaction. For derivative transactions, the impact of credit spreads is substantially lower than for debt and investment transactions due to the offsetting nature of the cash flows.

Related disclosures

The following table shows the impact of credit spread movements on fair value:

	GROUP	
	2018	**2017**
	$M	$M
Current year fair value profit/(loss) movement included above		
Fair value movement in debt due to credit spread movement	(17.7)	(67.6)
Fair value movement in asset due to credit spread movement	0.3	–
Fair value movement in derivatives due to credit spread movement	(13.2)	5.5
Statement of financial position balance – decrease in debt due to credit spread	86.8	104.5
Statement of financial position balance – (decrease) in investment due to credit spread	(2.0)	(2.3)
Statement of financial position balance – decrease in derivatives due to credit spread	19.6	32.8

16. Taxation

	GROUP	
	2018	**2017**
	$M	$M
Income tax expenses		
Current tax expense		
Current period	60.9	55.1
Adjustment for prior periods	(2.2)	0.9
	58.7	56.0
Deferred tax expense		
Origination and reversal of temporary differences	33.0	49.6
Adjustment for prior periods	3.0	(0.6)
	36.0	49.0
Total income tax expense (credit)	94.7	105.0
Reconciliation of effective tax		
Operating surplus before tax	334.1	371.0
Income tax at 28c	93.5	103.9
Tax effect of:		
Net non-deductible expenses and non-assessable items	0.4	0.8
Under/(over) provided in prior periods	0.8	0.3
Total income tax expense (credit)	94.7	105.0

Description

There are no unrecognised deferred tax balances (2017: nil).

For property, plant and equipment, deferred tax typically arises from the accounting book, including capitalised interest, differences in depreciation rates between tax and accounting and the capital contribution rules.

Accounting policies

Deferred tax arises from differences between the accounting and tax values of assets and liabilities, except where the initial recognition exemption applies (e.g. buildings).

Deferred tax is shown as a net liability for the Group. This disclosure reflects that the deferred tax balances relate to companies in the Transpower Consolidated Tax Group and are in the same jurisdiction, being New Zealand.

Imputation credits

The imputation credit balance at 30 June 2018 is $81.7 million (2017: $81.8 million). This balance includes the tax payable outstanding at 30 June 2018.

Deferred tax

	GROUP				
	BALANCE 1 JULY 2016	RECOGNISED IN PROFIT OR LOSS	BALANCE 30 JUNE 2017	RECOGNISED IN PROFIT OR LOSS	BALANCE 30 JUNE 2018
	$M	$M	$M	$M	$M
Property, plant and equipment temporary differences	433.7	28.6	462.3	28.0	490.3
Fair value of net debt and derivatives	(94.1)	21.8	(72.3)	15.5	(56.8)
Revenue deferral	(5.1)	(1.9)	(7.0)	1.4	(5.6)
Dismantling provision	(1.7)	1.6	(0.1)	(6.2)	(6.3)
Other	(4.0)	(1.1)	(5.1)	(2.7)	(7.8)
Total deferred tax	328.8	49.0	377.8	36.0	413.8

17. Related parties

Transactions with key management personnel

The Group did not conduct any business with key management personnel aside from the compensation payments below.

Key management personnel compensation

Key management personnel received the following compensation for their services to the Group:

	GROUP	
	2018	**2017**
	$M	$M
Directors' fees	0.5	0.5
Other key management personnel	5.8	5.7
Short-term employee remuneration	6.3	6.2
Defined contribution schemes	0.2	0.2

There were termination payments to key management personnel in 2018 of $0.4 million (2017: nil). There was no long-term compensation paid to key management personnel.

Government-related transactions

Transpower, being a State-Owned Enterprise, transacts with other government-related entities. The most significant transactions and balances (greater than $15 million) are as follows:

	GROUP	
	2018	**2017**
	$M	$M
Meridian Energy Limited – revenue	122.2	123.6
Electricity Authority – revenue	41.7	46.0

Meridian Energy Limited (Meridian) is a majority State-Owned company and is an electricity generator and retailer. Meridian pays Transpower primarily for the transportation of electricity across the national electricity grid.

The Electricity Authority (EA) is an independent Crown entity responsible for regulating the New Zealand electricity market. The EA pays Transpower a contracted fee for its role as system operator.

Transpower also settles its income and indirect tax obligations with Inland Revenue.

Some directors of the company may be directors or officers of other companies or organisations with which Transpower may transact.

All related party transactions are carried out at an arm's length and independent commercial basis.

18. Contingencies

(a) Guarantees

NZPCL

In November 2009, the Group partially terminated the 2003 cross-border lease in respect of the majority of the HVAC transmission assets in the South Island. As a result of the partial termination, Transpower has consolidated a special-purpose vehicle, NZPCL.

NZPCL has a USD deposit with a financial institution and a USD loan from another financial institution. The cash flows from the deposit and loan offset. No consideration was transferred. The loan to NZPCL is guaranteed by Transpower.

The substance of the transaction is such that Transpower rather than the non-controlling interest would be responsible for any shortfall between the value of the asset and the liability. The likelihood of losses in respect of these matters is considered to be remote.

Debt

Transpower has given a negative pledge covenant to certain debt holders that, while any debt issued remains outstanding, we will not, subject to certain exceptions, create or permit to exist any charge or lien over any of our assets.

18. Contingencies (continued)

(b) Economic gain (loss) account

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. Under Commerce Commission regulations, Transpower is required to pass onto or claim from customers the economic value of the net balance of any historical gains or losses incurred prior to 30 June 2012 over the regulatory periods until June 2020. Historical balances are those that pre-date the input methodologies developed by the Commission. In addition to the historical balances, further economic gains or losses arising from the beginning of Regulatory Control Period 1, which commenced on 1 July 2012, are required to be passed on or claimed from customers in the following pricing year.

The provisional balances and expected cash flows from the EV accounts for HVAC and HVDC customers at 30 June 2018 are set out below. The 30 June 2018 provisional numbers do not take into account the EV balances to be recovered (paid) in the period 1 April 2019 to 31 March 2020. These figures will not be finalised until October 2018.

	HVAC	HVDC	TOTAL
	$M	$M	$M
30 June 2018 provisional balance			
Pre input methodology EV balances to be recovered (paid) 1 July 2018 to 31 March 2020	(13.8)	27.5	13.7
Post input methodology EV balances to be recovered (paid) 1 July 2018 to 31 March 2019	(12.2)	0.7	(11.5)
Post input methodology EV balances to be recovered (paid) 1 April 2019 to 31 March 2020	(15.0)	0.4	(14.6)
Total to be recovered (paid)	(41.0)	28.6	(12.4)
30 June 2017 balance			
Pre input methodology EV balances to be recovered (paid) 1 July 2017 to 31 March 2020	(21.5)	42.9	21.4
Post input methodology EV balances to be recovered (paid) 1 April 2018 to 31 March 2019	(16.2)	0.9	(15.3)
Post input methodology EV balances to be recovered (paid) 1 April 2019 to 31 March 2020	(15.0)	0.4	(14.6)
Post input methodology EV balances to be recovered (paid) 1 July 2017 to 31 March 2018	19.6	(1.0)	18.6
Total to be recovered (paid)	(33.1)	43.2	10.1

(c) Environmental hazards

Transpower has a programme of identifying, mitigating and removing environmental hazards such as asbestos at its sites. The cost of mitigating and/or removing identified hazards will vary, depending on the particular circumstances at the site. Where a reasonable estimate of the cost of mitigating or removal of a hazard can be made, a provision has been established. During the year to June 2018, Transpower made a significant increase in its provision. The amount and basis is disclosed in note 12 Provisions.

(d) Various lawsuits, claims and investigations

Various lawsuits, claims and investigations have been brought or are pending against the Group. The directors of Transpower cannot reasonably estimate the adverse effect (if any) on the Group if any of the foregoing claims are ultimately resolved against the Group's interests.

19. Subsequent events

On 23 August 2018, the directors approved the payment of a dividend of $99.0 million. The dividend will be fully imputed and is expected to be paid on 20 September 2018.

In addition, directors approved the extension of the $250 million standby facility, due to mature 7 December 2018, by a further two years to 7 December 2020.

The directors are not aware of any other matter or circumstance since the end of the financial year that has significantly or may significantly affect the operations of Transpower or the Group.

Independent Auditor's Report

Building a better working world

Chartered Accountants

TO THE READERS OF TRANSPOWER NEW ZEALAND LIMITED'S GROUP FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2018

The Auditor-General is the auditor of Transpower New Zealand Limited group (the Group). The Auditor-General has appointed me, Grant Taylor, using the staff and resources of Ernst & Young, to carry out the audit of the consolidated financial statements of the Group on his behalf.

Opinion

We have audited the consolidated financial statements of the Group on pages 1 to 34, that comprise the consolidated statement of financial position as at 30 June 2018, and the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and the notes to the consolidated financial statements that include accounting policies and other explanatory information.

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 30 June 2018, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with New Zealand equivalents to International Financial Reporting Standards and International Financial Reporting Standards.

Basis for opinion

We conducted our audit in accordance with the Auditor-General's Auditing Standards, which incorporate the Professional and Ethical Standards and the International Standards on Auditing (New Zealand) issued by the New Zealand Auditing and Assurance Standards Board. Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report. We are independent of the Group in accordance with the Auditor-General's Auditing Standards, which incorporate Professional and Ethical Standard 1 (Revised) *Code of Ethics for Assurance Practitioners* issued by the New Zealand Auditing and Assurance Standards Board, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

In addition to the audit we have carried out assignments in the areas of other assurance services, training and remuneration benchmarking, which are compatible with those independence requirements. Other than the audit and these assignments, we have no relationship with or interests in the Group.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key Audit Matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

We have fulfilled the responsibilities described in the *Auditor's responsibilities for the audit of the financial statements* section of the audit report, including in relation to these matters. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the financial statements. The results of our audit procedures, including the procedures performed to address the matters below, provide the basis for our audit opinion on the accompanying consolidated financial statements.

How our audit addressed key audit matters

<table>
<tr><th>KEY AUDIT MATTER</th><th>HOW WE ADDRESSED THE KEY AUDIT MATTER</th></tr>
<tr><td colspan="2">Regulated assets</td></tr>
<tr><td>Transpower's regulated assets (consisting of property, plant and equipment, intangible assets and associated capital work in progress) described in Note 5 represent 88% of total assets at 30 June 2018.

Judgements required to be made by management in relation to regulated assets include:
• determining what costs ought to be capitalised;
• determining the appropriate time to commission an asset and commence depreciation;
• the period over which regulated assets should be depreciated; and
• whether there are any regulated assets that ought to be impaired.

Transpower reviews regulated assets for indicators of impairment at each reporting date.

Transpower allocates its regulated assets between cash generating units and compares the carrying amount against the regulated book value to identify possible indicators of impairment.

As described in Note 5 the recoverable amount for regulated assets is generally its regulatory book value. Regulatory book value is the amount Transpower is able to recover from customers through future revenue under the terms of the regulations per Part 4 of the Commerce Act 1986.</td><td>In obtaining sufficient reliable audit evidence we:
• Assessed the appropriateness of a sample of capitalised costs against the criteria contained in NZ IAS 16
• Reviewed a sample of assets commissioned in the period to ensure depreciation was charged from the appropriate date
• Reviewed a sample of large capital work-in-progress project balances to determine whether they ought to have been commissioned at 30 June 2018
• Understood how Transpower has re-assessed the appropriateness of the assumed asset useful lives that are the basis on which depreciation is charged
• Assessed cash generating units identified by management against the requirements of NZ IAS 36 Impairment of Assets and the allocation of regulated assets between cash generating units.
• Tested management's identification of differences between the financial statement carrying amounts and regulatory book values at 30 June 2018 and understanding the reasons for such differences.
• Independently considered the completeness of management's assessment of indicators of impairment.</td></tr>
<tr><td>Fair value of debt and derivatives</td><td></td></tr>
<tr><td>Transpower has significant debt and derivative financial instruments. The total debt and derivative portfolio at 30 June 2018 was a net liability position of $3.2b and is detailed in Note 6 of the financial statements.

Debt and derivatives are both recorded at fair value. Movements in the fair value of debt and related derivative financial instruments impact profit or loss in the same period.

The valuation of these instruments involves the application of valuation techniques which involve the exercise of judgment and the use of the assumptions and estimates as described in Note 6 to the financial statements.</td><td>In obtaining sufficient reliable audit evidence we:
• Obtained counterparty confirmations for all debt and derivatives held at 30 June 2018.
• Assessed the appropriateness of the valuation models and significant inputs.
• Compared observable inputs used against independent sources and externally available market data
• Performed our own independent valuations for a sample of instruments.
• Assessed whether the Group's disclosures in the consolidated financial statements in relation to the valuation of investments are compliant with the NZ IFRS 7 Financial Instruments: Disclosure and NZ IFRS 13 Fair Value Measurement.</td></tr>
</table>

Other Information

The directors are responsible on behalf of the Group for the other information. The other information comprises the information included on pages 1 to 22 but does not include the consolidated financial statements and our auditor's report thereon.

Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of audit opinion or assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Directors' responsibilities for the consolidated financial statements

The directors are responsible on behalf of the Group for the preparation and fair presentation of the consolidated financial statements in accordance with New Zealand equivalents to International Financial Reporting Standards and International Financial Reporting Standards, and for such internal control as the directors determine is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, the directors are responsible on behalf of the Group for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Group or to cease operations, or have no realistic alternative but to do so.

The directors' responsibilities arise from the Financial Markets Conduct Act 2013.

Auditor's responsibilities for the audit of the consolidated financial statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the Auditor-General's Auditing Standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of readers taken on the basis of these consolidated financial statements.

As part of an audit in accordance with the Auditor-General's Auditing Standards, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of the use of the going concern basis of accounting by the directors and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with the directors regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the directors with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with the directors, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Our responsibilities arise from the Public Audit Act 2001.

Grant Taylor
Ernst & Young
On behalf of the Auditor-General
Wellington, New Zealand

23 August 2018

BOARD OF DIRECTORS

CHAIR
HON TONY RYALL CNZM

DEPUTY CHAIR
PIP DUNPHY

DIRECTORS
PROFESSOR JAN EVANS-FREEMAN
TIM LUSK (retired on 20 September 2018)
BILL OSBORNE
DEAN CARROLL
SHERIDAN BROADBENT

GENERAL MANAGEMENT TEAM

CHIEF EXECUTIVE
ALISON ANDREW

CHIEF FINANCIAL OFFICER
ALEX BALL

GENERAL MANAGER OPERATIONS
JOHN CLARKE

GENERAL MANAGER GRID DEVELOPMENT
STEPHEN JAY

GENERAL MANAGER PEOPLE
BRIGHID KELLY

GENERAL COUNSEL AND COMPANY SECRETARY
DAVID KNIGHT

GENERAL MANAGER AUCKLAND DEVELOPMENT AND TRANSFORMATION
RAEWYN MOSS

GENERAL MANAGER INFORMATION SERVICES AND TECHNOLOGY
COBUS NEL

GENERAL MANAGER GRID SERVICE DELIVERY
MARK RYALL

GENERAL MANAGER CUSTOMERS AND PROJECTS
KEVIN SMALL

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