

# Marlborough Lines Limited Ownership Review



14 October 2008



Mr Ken Forrest  
Managing Director  
Marlborough Lines Limited  
P.O. Box 144  
Blenheim 7240

14 October 2008

Dear Mr Forrest,

**Ownership Review of Marlborough Lines Limited**

We are pleased to provide herewith our report on the performance of Marlborough Lines Limited (“MLL”) and a review of share ownership options to contribute to the five yearly review of ownership as required by the Trust Deed of the Marlborough Electric Power Trust. This report is provided in accordance with our engagement letter dated 17 September 2008 and is subject to the restrictions in Appendix 1.

This report includes an assessment of MLL’s performance, and ownership options. It does not include the conclusions of the Directors of MLL as to the most appropriate form of ownership in according with clauses 4.1.d-e of the Trust Deed.

If you require any clarification or further information, please do not hesitate to contact either of the undersigned.

Yours sincerely  
**PricewaterhouseCoopers**



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# Section 1

## Introduction

# 1. Introduction

Marlborough Electric Power Trust (“MEPT” or “the Trust”) is required every five years to request a report from the Directors of Marlborough Lines Limited (“MLL” or “the Company”), the company that it holds in trust on behalf of its beneficiaries. The report must comply with the requirements of Section 4 of the MEPT Trust Deed as summarised opposite.

PricewaterhouseCoopers (“PwC”) has been engaged to provide professional advice in respect of clauses 4.1.a, 4.1.b and 4.1.c for input into the Directors’ report.

In conducting this review, PwC has relied on financial information supplied by MLL, published information disclosure documents for other electricity distribution companies, PwC databases, interviews with the Chairman of the MEPT Trust and interviews with the Chairman and other board members of MLL.

This report has been structured into three parts as follows:

- Analysis of ownership options available to MEPT and its beneficiaries, including the current Trust ownership structure;
- Analysis of the performance of the Company over the last six years;
- Performance review of MLL’s electricity distribution business in comparison with other companies engaged in electricity distribution.

This report is subject to the Restrictions in Appendix 1. Appendices 2 and 3 include supporting information for the performance assessment of MLL. Appendix 4 contains a glossary of terms used throughout the report.

## Scope of the Ownership Review

Under Clause 4 of the Trust Deed, the Ownership Review Report must contain the following:

- 4.1.a an analysis of the performance of the Company to the date of the report together with a summary of the advantages and disadvantages of Trust ownership;
- 4.1.b an analysis of the various ownership options considered including, without limitation, a Share distribution to Consumers, a sale of Shares to the public, a sale of Shares to institutional investors and retention by the Trust;
- 4.1.c a comparison of the performance by the Company with the performance of other electricity network companies operating on a similar basis;
- 4.1.d the conclusions of the directors as to the most appropriate form of ownership together with an indication whether the conclusions are unanimous and if the decision is not unanimous, a summary of the conclusions of the dissenting directors shall be included;
- 4.1.e the matters contained in Clause 4.7 if a distribution of Shares is recommended; and
- 4.1.f a summary of the professional advice (if any) obtained in respect of the preparation of the report.

# Section 2

## Executive Summary

## 2. Executive Summary

### Review of Ownership Options

Since the 2002 Ownership Review MLL has faced significant changes within the industry in which it operates. While the Company has not acquired new network assets over this period, it has invested a substantial amount into both its Marlborough distribution network and its interest in the OtagoNet Joint Venture (“OJV”). Due to this investment, the Company is now a larger entity, and continues to focus on commercial returns and long term financial sustainability. Performance excellence also remains as a key objective. Other key changes have been the introduction of the Commerce Commission’s targeted control regulatory regime over Electricity Distribution Businesses (“EDBs”) and, with the Company’s interests in the OJV and Nelson Electricity Limited (“NEL”) networks, the impact this regime has over consumers who are not beneficiaries of the Trust.

In undertaking our analysis of the ownership options available to MLL, including the assessment of the advantages and disadvantages of Trust ownership, we have considered the implications of these changes.

We have also considered the obligations of the Trustees - as embodied in MEPT’s Trust Deed, and the Statement of Corporate Intent (“SCI”) the key strategic document for the Company which is jointly endorsed by both the Board and the Trust.

There are a number of different ownership options available, and for the purposes of this report we have examined the following alternatives which fall across the spectrum of 100% Trust ownership to 100% divestment:

- 100% Trust ownership;
- Joint Ventures;
- Merger by Way of Equity Exchange;

- Distribution of 24.9% or 49.9% of Shares to Beneficiaries;
- Sale of 24.9% or 49.9% of Shares to Consumers, the Public, Industry or Institutional Investors;
- Distribution of 100% of Shares to Beneficiaries; and
- Sale of 100% of Shares to Consumers, the Public, Industry or Institutional Investors.

In assessing the ownership options for MLL we have used the following criteria which are consistent with the SCI and the Trust Deed:

- **Capability for Growth** – encompassing the ability to enhance and maximise shareholder value over the long term including acquiring other businesses, developing new businesses, expanding new businesses or merging with compatible businesses; and, within the existing business, providing for potential future development.
- **Performance Excellence** – encompassing excellence in safety, cost efficiency, network reliability, resource utilisation, productivity, environmental sustainability, price stability, customer servicing, employee satisfaction and being a responsible member of the community.
- **Commerciality** – operating the business in a successful manner, including generating similar unit revenue to comparable EDBs, operating efficiently, achieving commercial rates of return and undertaking prudent investments consistent with regulatory and commercial requirements.

We have also added the following criteria to our assessments:

- **Governance and Control** – incorporating the effectiveness of governance processes, flexibility in governance and the level of control over business activities inherent in each option.
- **Administrative Complexity** – including the costs and complexities of each option.

## 2. Executive Summary

### Conclusions on Trust Ownership

The key advantages of retaining 100% MEPT ownership are the ability for the Trust to influence the financial and non financial performance of MLL, the simplicity of the structure and the ability to act in the role of custodian for existing and future generations of Marlborough consumers. There appears to be a real benefit to Trust ownership in achieving these objectives. It is also the most simple option to implement, because it requires no change from the Status Quo.

The existing Trust structure has served MLL well to date. At some point in the future this structure may impose limitations on MLL's ability to meet its growth, excellence and commercial objectives. A further review of its ownership structure would be appropriate at that time. As MLL faces increasing demand on capital to invest in its own ageing network infrastructure, funds for distribution to the beneficiaries of the Trust (by way of both discounts to Marlborough consumers and distributions directly to MEPT) will have to compete with funds for investment in new activities to achieve growth.

The 100% Trust ownership option potentially constrains MLL's ability to meet its growth objectives and to maintain shareholder value in the medium term. Limited access to external influences and expertise are a key factor, as well as limited access to capital. The effectiveness of the 100% MEPT ownership model is also dependent on the election cycle and the calibre and interests of local Trustee candidates. Solutions to this could include strengthening the Trust model by reviewing the appointment of the Chair and providing guidelines for the skills required of trustee candidates.

There is ongoing impetus to consolidate EDBs within the industry and MLL management recognise that unless the MLL business continues to grow the Company is at risk of being acquired should an acquirer present a substantial cash offer to MLL's owners, being the Trust directly and the consumers of the Marlborough region indirectly.

The existing benefits of Trust ownership can be retained to a greater or lesser extent by a number of the alternative ownership options considered (and other versions of these) and the external funding options available. The joint venture option is a model that MLL has already implemented in its acquisition of the OtagoNet EDB. This has allowed the Company to retain the benefits of trust ownership over its core assets, while accessing external resources to support growth into new geographic areas or industrial segments.

One issue that the Company does need to consider in some detail is its ability to respond quickly to opportunities as they arise. This may take the form of identification of potential sources of debt funding, potential joint venture or equity partners or plans for partial distribution or sale of either some of MLL's investments or the business as a whole. Part of this process would involve a discussion with the Trust as to their preferred options for alternative ownership models.

## 2. Executive Summary

When and if MLL takes the first step away from a 100% Trust model is, in our view, dependent on the size and nature of the growth opportunities that arise, the readiness of MLL to respond to these, the availability of debt funding and the availability of suitable investors or partners. At this time there does not appear to be an opportunity which is sufficiently advanced to justify MLL making a decision to move from the Status Quo although we note that at present MLL could significantly benefit from an increased scale of operations.

### Analysis of Other Ownership Options

**Joint Ventures** – This option is able to be implemented alongside continued MEPT ownership of core (network) assets and provides a vehicle for value growth and access to external expertise to improve performance. MLL has already successfully instigated an EDB ownership joint venture arrangement with Electricity Invercargill Limited (“EIL”) and The Power Company (“TPC”) in respect of the OtagoNet EDB.

**Merger by Way of Equity Exchange** – The role of the MEPT can be preserved in relation to MLL’s existing assets. In addition, a merger provides opportunities for economies of scale and sharing of best practice to improve MLL’s performance and increase value.

**Distribution of 24.9% or 49.9% of Shares to Beneficiaries** – While MEPT retains control under this scenario, MLL’s obligations to all shareholders would mean the influence of the Trust is more limited. This share give-away option provides no immediate access to capital or external expertise.

**Sale of 24.9% or 49.9% of Shares to Consumers, the Public, Industry or Institutional Investors** – Similar to a partial share distribution, but this option provides access to capital. Shares may be listed.

**Distribution of 100% of Shares to Beneficiaries** – MEPT loses influence over MLL’s assets and is dissolved. Existing beneficiaries are gifted shares or cash for their own use. MLL potentially gains access to capital markets. Returns to shareholders may become the primary measure of performance.

**Sale of 100% of Shares to Consumers, the Public, Industry or Institutional Investors** – MEPT loses influence over MLL’s assets, but potentially gains a fund to manage on behalf of its beneficiaries, or alternatively existing consumers gain shares or cash for their own use. Shares may be listed. MLL gains access to capital markets and is able to pursue growth opportunities. As above, returns to shareholders may become the primary measure of performance.

### MLL’s Performance

Over the past five years, MLL has shown strong revenue and earnings growth, coupled with a significant increase in its asset base. Increasing requirements for investment on the Marlborough network and external regulatory scrutiny have been challenges MLL has had to meet over this period, as well managing its interests in OJV and NEL and expanding its contracting businesses.

## 2. Executive Summary

Despite these limitations, MLL has been able to grow revenues from \$30.9 million (before discounts) in 2004 to \$44.4 million in 2008 with its operating surplus (EBITDA) growing from \$11.7 million to \$20.9 million over the same period.

The experience of the management team means that the Company has implemented a number of significant improvements including bedding in and generating a return from its investments in OJV and NEL, growing its line contracting business, and has undertaken a number of environmental initiatives.

MLL's commitment to excellence including its focus on quality systems and processes, customer service and ongoing communication with all stakeholders is starting to set it apart from many of its peers.

The Company has recently won a number of awards for the presentation of its annual report and consistently achieves high satisfaction levels in customer surveys.

### Performance Against SCI Targets

There have been challenges to meeting SCI targets over the 2003 – 2008 period. Even though significant expenditure has been made on improving supply quality, the Company has faced obstacles in providing a high quality of supply, particularly as a result of planned outages resulting from network improvements and expansion. In addition, increasing maintenance, input and regulatory costs have contributed to the Company exceeding its cost per customer targets. In spite of these higher costs, MLL has achieved, or been very close to achieving its earnings targets each year, and has exceeded its equity ratio targets.

### Performance Compared with Other EDBs

We have compared MLL's lines business performance with that of a group of like lines businesses, that is those that have load and customer density characteristics that most closely match those of MLL. For this purpose we have used the lines business regulatory disclosure information for the 2006 and 2007 years for MLL and the following EDBs:

- Buller Electricity;
- Centralines;
- Eastland Network;
- MainPower;
- Network Waitaki;
- OtagoNet Joint Venture;
- The Lines Company;
- The Power Company;
- Top Energy; and
- Westpower.

These EDBs service provincial centres with large rural hinterlands, many of which include reticulation located in remote and difficult access terrain.

It should be noted that care must be taken when comparing EDBs as all line networks have different attributes which influence the various metrics examined. Topography, climate, growth rates, historical design practices, network configuration and customer density are all factors that affect these measures and as such this analysis only provides a high level indication of performance.

## 2. Executive Summary

Our key observations were:

- In 2006 and 2007 MLL's interruption duration ("SAIDI") and in 2006 MLL's interruption frequency ("SAIFI") marginally exceeded the medians of the comparable group (with MLL ranked 7<sup>th</sup> out of 11 in each). In 2007, MLL ranked 4<sup>th</sup> in respect of SAIFI. We note that in both years the network was subject to a high level of planned outages in order to carry out the installation of new connections, capacity upgrades and the replacement of old network assets.
- In 2006, MLL's average unit revenues were near the top of the comparable group, attaining a ranking of 2. MLL agreed with the Commerce Commission not to raise prices in the 2007 financial year and its peer ranking has consequently fallen slightly. We note that this measure of revenue includes capital contributions, which are significant in the Marlborough network.
- MLL's performance in the two key measures that consumers are primarily concerned with, system reliability and price, is broadly in line with its peer group once planned system outages and capital contributions are taken into account.
- Our analysis of unit operating costs shows that MLL has higher operating costs than its peers. Managing a large investment programme, coupled with a significant amount regulatory scrutiny has created cost pressures for MLL when compared to its peers.

- The financial return measures rank MLL in the lower half of its peer group. After adjusting for the different distribution policies of other EDBs, MLL's ranking remains in the lower half of its peer group demonstrating that MLL's high relative revenues are more than offset by its high relative expenses.

### Conclusion on Performance

In relation to comparable EDBs, MLL displays comparable if somewhat lower levels of system reliability than its peer group. Both revenues and operating expenses are high and are somewhat offsetting, resulting in a slightly lower level of profitability than is experienced, on average, by MLL's peers. Overall, the performance of MLL is well within the expected range of its peer group.

# Section 3

## Ownership Structure

## 3. Ownership Structure

### Review of Ownership Options

The last ownership review was undertaken in 2002. MLL is, to some extent, a different entity in 2008 than it was in 2002. The industry in which it operates is also somewhat different. Key changes which are relevant to the current ownership review are:

- MLL has 'bedded in' the acquisition of a 51% interest in the OtagoNet network in mid 2002, an EDB servicing the eastern, non-metropolitan portion of Otago, through a joint venture with EIL and TPC. In conjunction with this acquisition, MLL also acquired a 51% interest in Otago Power Service Limited ("OPSL"), a network contracting company based in Balclutha. With this acquisition, MLL has a 51% interest in supplying an additional 14,700 customers (compared to 23,500 in its Marlborough network) via 4,100 circuit kilometres of distribution lines.
- From an opening value of approximately \$100 million ODV, MLL has made a substantial investment of \$44.3 million in distribution network property and equipment over the 2004 to 2008 period.
- The Commerce Commission has introduced a regulatory regime to actively monitor the price, profit and quality performance of EDBs.

Section 4 of this report summarises MLL's achievements since 2003 and its performance over that period including comparison with other electricity distribution companies.

Our brief in respect of the review of ownership options was to consider:

- An analysis of the performance of the Company to the date of the report together with a discussion of the advantages and disadvantages of Trust ownership; and
- An analysis of the various ownership options considered including without limitation, a share distribution to consumers, a sale of shares to the public, a sale of shares to institutional investors and retention by the Trust.

We have also considered the following documents:

- MEPT's Trust Deed which requires the Trustees to encourage and facilitate the Company in meeting its objectives of being a successful business and operating on a commercial basis, and to distribute to consumers the benefits of their ownership of the Company by means that are efficient and appropriate.
- The SCI which is the key strategic document for the Company, updated annually with objectives for the following 12 month period. The SCI is reviewed and endorsed by the Trust. The 2007/08 SCI includes the objectives summarised on the following page.

## 3. Ownership Structure

### 2007/08 SCI Objectives

- The Company intends to ensure that all services provided are responsive to customer requirements, are subject to regular monitoring and review and are provided with the highest standards of customer service.
- The commercial objectives of the Company include:
  - achieving a satisfactory commercial return on equity over the medium term;
  - achieving revenues and efficiency levels that compare well with other similar EDBs;
  - achieving quality outcomes consistent with commercial and regulatory requirements;
  - adopting a transparent pricing strategy to customers and electricity retailers;
  - achieving the efficient utilisation of all Company resources;
  - undertaking capital investment where that investment achieves a WACC return, and meets MLL's non-financial investment criteria ( including safety and legislative requirements) ;
  - making provision for future development;
  - maximising the long term value of shareholder funds; and
  - acceptance of any control mechanisms instituted by the Commerce Commission.
- In addition, other key aims include:
  - maintaining ISO management system accreditations;
  - remaining committed to providing a safe and rewarding workplace environment for employees;
  - being a good corporate citizen and a responsible member of the community;
  - promoting energy efficiency;
  - being a diligent respecter of the environment;
  - providing distribution services to all customers in a fair and equitable manner; and
  - maximising the benefits available to shareholders.

## 3. Ownership Structure

### Ownership Options

There are a number of different ownership options available across a spectrum bounded by continued 100% Trust ownership at one end and full divestment to consumers, institutional investors, industry investors or the public at the other end. Across the spectrum there are many permutations representing partial divestment or dilution of the existing 100% Trust ownership. For the purposes of this report we have examined the advantages and disadvantages of the following options which are representative of options which fall across the range<sup>2</sup>:

- 100% consumer Trust ownership
- Joint Ventures
- Merger by Way of Equity Exchange
- Distribution of 24.9% or 49.9% of Shares to Beneficiaries
- Sale of 24.9% or 49.9% of Shares to Consumers, the Public, Industry or Institutional Investors
- Distribution of 100% of Shares to Beneficiaries
- Sale of 100% of Shares to Consumers, the Public, Industry or Institutional Investors.

In evaluating each of these options we have considered the following factors:

- capacity for growth;
- performance excellence;
- commerciality;
- governance and control; and
- administrative complexity.

We have not considered regulatory or tax implications, however we recommend that advice is sought in each of these areas should a change from the Status Quo be considered further.

On the following pages we summarise the advantages and disadvantages of each of the options listed opposite. In the final part of this section of the report we review this analysis in the context of MLL's own objectives and plans.

<sup>2</sup> A co-operative option is similar to the existing Trust structure with some minor variations. For this reason we have not examined this option further.

## 3. Ownership Structure

### Trust Ownership

Trust ownership is very common among New Zealand EDBs, with 21 of 29 companies having some trust ownership and 18 having full trust ownership like MLL. The MEPT holds the shares of MLL on behalf of current and future consumers, and the consumers of the day are the beneficiaries of the Trust. Any major variation to the ownership provisions of the Trust Deed would require specialist legal advice, following which consumer consultation and an application to the High Court may well be required.

The advantages and disadvantages of Trust ownership can be summarised as follows:

#### Advantages

- A 'natural state' with no implementation costs.
- Trust can influence financial and non-financial objectives through the SCI and the appointment of Directors.
- Direct financial benefits flow to consumers.
- Consumers maintain control by election of trustees.
- Environmental considerations are able to be supported.
- Able to manage the investment in long-term assets for the benefit of both current and future generations.
- Ownership and management remains localised, enabling a strategic focus on regional benefits.
- Allows the Company to focus on operating performance and growth strategies rather than primarily shareholder returns.
- Ownership by a single entity simplifies reporting and governance procedures, minimising compliance costs.
- Avoids the problem of finding 'a better investment' to apply the proceeds of sale.
- Retains the option to merge to enhance company value and shareholder returns.
- Under the Commerce Amendment Act 2008, certain Trusts become exempt from price-quality regulation from 1 April 2009.

#### Disadvantages

- May impede optimal commercial outcomes for the Company such as mergers.
- Trust's regional objectives may be inconsistent with the Company's obligation to operate commercially.
- Trust may find it challenging to maintain a desired level of dividends. Difficulty raising new equity means the Trust must sacrifice dividends and immediate benefits for beneficiaries in order for the Company to pursue growth opportunities. Some opportunities will not be possible to pursue due to size.
- Company may find it difficult to implement 'best in class' service and keep up with innovation without access to external influences.
- Election cycle may generate risk of instability in Trust operations.
- May be unable to attract Trustees with necessary skills to fulfil obligations.
- A poor relationship between the Trust and the Board may impede the exploitation of opportunities.

## 3. Ownership Structure

### Joint Ventures

In order to achieve growth objectives Joint Ventures are a means of entering into new business relationships with other parties for some of the business activities of an entity, while retaining some of the existing ownership structure. MLL has experience in the creation and operation of joint venture arrangements through its interest in the OJV.

#### Advantages

- Achieves growth objectives.
- Ownership and management of core business may remain localised, enabling a strategic focus on regional benefits.
- Trusts may be able to continue to direct non-commercial objectives for some parts of the business (as appropriate).
- May enhance access to capital.
- Typically provides access to expertise to support horizontal or vertical growth opportunities.
- Shares the risks inherent in new business opportunities.
- Avoids incurring divestment costs.
- Retains the option to merge to enhance company value and shareholder returns.
- Can be relatively low cost and quick to implement.
- Develops a model and relationships that may be used for other growth opportunities.

#### Disadvantages

- Benefits of the Joint Venture are limited to the scope of the activities they are associated with.
- Potential loss of control over Joint Venture activities.
- Other disadvantages of Trust ownership remain for core business such as potential conflict between local and commercial objectives, difficulty in raising capital, stability of Trust.
- There are one off costs associated with establishing a Joint Venture.
- Selection of the Joint Venture partners is crucial and the nature of the relationship may change over time.
- Networks with Joint Venture owners are not exempt from price-quality regulation.

## 3. Ownership Structure

### Merger by Way of Equity Exchange

Mergers with like businesses, such as other EDBs, are most readily executed by way of equity exchange, thus in effect diluting the existing trust ownership, but achieving an interest in a larger entity and potentially realising operational synergies and scale benefits.

#### Advantages

- Opportunity for both participants to capture and share synergy gains.
- Provides opportunity to enhance value through merger benefits.
- Does not require capital outlay to implement.
- Values can be equalised through capital repatriation.
- Local ownership retained, albeit shared.
- Facilitates growth objectives.
- Local objectives can be accommodated, e.g. different price and service objectives.
- Linkages between the Trust and Company are preserved.
- In most instances, the process can be implemented relatively quickly with minimal cost.
- Mergers with other trust owners who have exempt regulatory status is likely to preserve this if certain conditions are met.

#### Disadvantages

- Relative value setting can be contentious.
- Governance and reporting structures tend to be complicated as the needs of both shareholders must be met.
- Management restructuring may meet resistance. Job losses inevitably occur and head office may shift outside the region.
- May result in loss of effective control without a control premium.
- Most effective with a similar entity, therefore opportunities are limited.
- Dilution of focus on local issues.
- Trust regional objectives may be inconsistent with the Company's obligations to act commercially.
- Trust remains exposed to election cycle and Trustee candidate risk.

## 3. Ownership Structure

### Distribution of 24.9% or 49.9% of Shares to Beneficiaries

Distribution of 24.9% allows the Trust to retain control over the Company's constitution, and distribution of 49.9% allows the Trust to retain outright control. In practice a distribution (share give-away) would result in some beneficiaries selling their shares to external investors.

#### Advantages

- Shares retained by the Trust could be used as currency in future transactions.
- Potentially exposes the Company to external monitoring and disciplines.
- Results in a one off injection of wealth into the local community.

#### Disadvantages

- Local ownership could be diluted.
- Provides no direct access to additional capital or skills for growth.
- Implementing change could be more difficult given a broad shareholder base and difficulty in achieving consensus.
- Company would be more exposed as a takeover target.
- Potential increased compliance (disclosure, reporting) costs and complexity under public ownership.
- Trust reduces its ability to assist its beneficiaries through influencing Company policy as the Company must consider its obligations to all shareholders.
- Fragmented ownership may hinder future M&A activity for the Company due to an inability to achieve consensus.
- Ownership would be difficult to recover if the Trust changes its mind.
- Distribution to existing beneficiaries raises intergenerational equity issues.
- Process takes time and can be costly.
- Regulatory exempt status would be lost.
- Future Consumers are disadvantaged.

## 3. Ownership Structure

### Sale of 24.9% or 49.9% of Shares to Consumers, the Public, Industry or Institutional Investors

Sale of 24.9% allows the Trust to retain control over the Company's constitution, and sale of 49.9% allows the Trust to retain outright control. Shares may be listed.

#### Advantages

- Under partial public ownership the Company would be able to access equity capital more readily, enhancing its growth prospects.
- Shares retained by the Trust could be used as currency in future transactions.
- Company decision making would be more democratic and less driven by local concerns.
- Scope for employee incentive or share option schemes to be introduced based on share price performance.
- Exposes the Company to external or market disciplines and monitoring.
- Trust could retain a shareholding of significant influence and control and still diversify its investment with the sale proceeds.
- The Trust could invest in debt or convertible securities that produce a more reliable income stream for its beneficiaries, while at the same time preserving the investment value in real terms through investment.
- The Trust could invest in a more diversified portfolio of assets, consistent with prudent investment guidelines.
- Company may become more efficient (e.g., through growth or takeover) enabling lower pricing for consumers and/or higher returns for owners.

#### Disadvantages

- Local ownership would be diluted and the Company's focus on regional benefits would diminish.
- Sale price would not be optimal as no control premium would be achieved.
- Implementing change could be more difficult given a broad shareholder base and difficulty in achieving consensus.
- Company would be more exposed as a takeover target.
- Increased compliance (disclosure, reporting) costs and complexity under public ownership.
- Trust reduces its ability to assist its beneficiaries through influencing Company policy as the Company must consider its obligations to all shareholders.
- Fragmented ownership may hinder future M&A activity for the Company due to an inability to achieve consensus.
- Ownership would be difficult to recover if the Trust changes its mind.
- Process takes time and can be costly.
- Regulatory exemptions would be lost.
- Future Consumers are disadvantaged.

## 3. Ownership Structure

### Distribution of 100% of Shares to Beneficiaries

The full distribution (give-away) option would mean that the Trust would cease to exist. Historical practice has been for a significant proportion of beneficiaries to sell their shares to external investors.

#### Advantages

- Beneficiaries who retain their shares gain a hedge against a more profit-focused network owner.
- Potentially exposes the Company to external or market disciplines and monitoring.
- Potentially results in partial public ownership which would enable the Company to access equity capital more readily, enhancing its growth prospects.
- Results in a one off injection of wealth into the local economy.

#### Disadvantages

- Local ownership would be diluted and the Company's focus on regional benefits would diminish.
- Provides no direct access to additional capital or skills for growth.
- Distribution process may be complex and time consuming depending on number and quality of parties involved.
- Implementing change could be more difficult given a broad shareholder base and difficulty in achieving consensus.
- Increased compliance (disclosure, reporting) costs and complexity under public ownership.
- Trust loses its ability to assist its beneficiaries through influencing Company policy and/or lower quality of service. Customers are thus exposed to higher pricing or lower quality if regulation is relaxed.
- Fragmented ownership may hinder future M&A activity for the Company due to an inability to achieve consensus.
- Ownership would be impossible to recover if the Trust changes its mind.
- Distribution to existing beneficiaries raises intergenerational equity issues.
- Regulatory exemptions would be lost.
- Future Consumers are disadvantaged.

## 3. Ownership Structure

### Sale of 100% of Shares to Consumers, the Public, Industry or Institutional Investors

The full sale option would require the Trust to determine whether or not it retained the proceeds of sale to manage on behalf of its existing and future beneficiaries.

#### Advantages

- Under public ownership the Company would be able to access equity capital more readily, enhancing its growth prospects.
- Company decision making would be less influenced by local concerns.
- Selling to another EDB should enable the Trust to achieve a high sale price, due to the value of synergies between the two entities, reflected in a control premium. This is best achieved under a contestable tender process conducted with trade buyers.
- Trade buyers are able to offer variable consideration (e.g. cash, shares, interest bearing securities) that may fulfil the Trust's future investment requirements.
- Beneficiaries could purchase shares as 'insurance' against a more profit-focused network owner.
- Scope for employee incentive or share option schemes to be introduced based on share price performance.
- Exposes the Company to external or market disciplines and monitoring.
- The Trust could invest in debt securities that produce a more reliable income stream for its beneficiaries, while at the same time preserving the investment value in real terms through investment.
- The Trust could invest in a more diversified portfolio of assets, consistent with prudent investment guidelines.
- Company may become more efficient (e.g., through growth) enabling lower pricing for consumers and/or higher returns for owners.

#### Disadvantages

- Local ownership would be diluted and the Company's focus on regional benefits would diminish.
- Sale process may be complex and time consuming depending on number and quality of parties involved.
- Implementing change could be more difficult given a broad shareholder base and difficulty in achieving consensus.
- Increased compliance (disclosure, reporting) costs and complexity under public ownership.
- Trust reduces its ability to assist its beneficiaries through influencing Company policy and/or lower quality of service. Customers are thus exposed to higher pricing or lower quality if regulation is relaxed.
- Fragmented ownership may hinder future M&A activity for the Company due to an inability to achieve consensus.
- Ownership would be difficult to recover if the Trust changes its mind.
- The uncertainty surrounding the 2010 regulatory reset may impact on value. This may mean that buyers discount value.
- Regulatory exemptions would be lost.

## 3. Ownership Structure

### Potential Ownership Options for MLL

As demonstrated in this report, MLL has made a number of achievements since the last ownership review in 2003. From our discussions with MLL's management, Directors and the Chairman of MEPT we believed that these achievements have been assisted by the current ownership structure, in particular the ease of decision making and the willingness of the Trust to support the objectives of the Company over this period. In particular we note that the SCI process ensures that the Company and the Trustees engage annually on the future objectives of the Company and that these objectives cover a broad range of performance measures, both financial and non financial.

In assessing the potential ownership options for MLL we have therefore considered the objectives outlined in the 2007/08 SCI as we believe this best represents the common objectives of the Company and its owners and provides direction as to the future challenges MLL is likely to face.

As outlined earlier, key themes embodied in the SCI for the 2008 period may be summarised as follows:

- Enhancing shareholder value by expansion both within and outside of core business activities;
- Excellence in performance including safety, cost efficiency, network reliability, productivity, environmental sustainability customer servicing and employee satisfaction;
- Achieving commercial rates of return; and
- Prudent investment in lines business assets.

The SCI also presents the Company's intention to continue operating in the following core business areas:

- Network Operation;
- Contracting;
- Property Investment; and
- EDB / Contracting related investments.

The SCI also details MLL openness to the possibilities of a merger of part or all of its business operations with other compatible companies.

MLL's current scope of operations is dominated by its electricity distribution activities, both directly and as investments, with smaller operations in network maintenance and installation.

Although the existing Trust ownership has assisted MLL over the past five years, it is not certain that the status quo will provide the most beneficial ownership structure to assist MLL to achieve its objectives looking forward. Therefore in order to expand on the generic assessment of the alternative options presented earlier, we have assessed each of these options for MLL in the context of both the factors presented earlier and the SCI objectives.

We have grouped these factors into the five key criteria shown on the following page.

## 3. Ownership Structure

### Assessment Criteria

- **Capability for Growth** – encompassing the ability to enhance and maximise shareholder value over the long term including acquiring other businesses, developing new businesses, expanding new businesses or merging with compatible businesses; and, within the existing business, providing for potential future development.
- **Performance Excellence** – encompassing excellence in safety, cost efficiency, network reliability, resource utilisation, productivity, environmental sustainability, price stability, customer servicing, employee satisfaction and being a responsible member of the community.
- **Commerciality** – operating the business in a successful manner, including generating similar unit revenue to comparable EDBs, operating efficiently, achieving commercial rates of return and undertaking prudent investments consistent with regulatory and commercial requirements.
- **Governance and Control** – incorporating the effectiveness of governance processes, flexibility in governance and the level of control over business activities inherent in each option.
- **Administrative Complexity** – including the costs and complexities of each option.

The table overleaf summarises our current assessment of the ownership options identified earlier against these criteria for MLL.

As stated previously, it is important to note that there are many permutations of these ownership options and we have chosen to focus on these seven alternatives which fall across the spectrum.

## 3. Ownership Structure

### Assessment of Ownership Options for MLL

Criteria	100% Trust	Joint Ventures	Merger through Equity	24.9% or 49.9% Distribution	24.9% or 49.9% Sale	100% Distribution	100% Sale
<b>Capability for Growth</b>	Low to Medium, capacity currently limited to small incremental opportunities, limited capacity to acquire new skills	Medium, good vehicle for expansion into non-core opportunities, acquires skills of JV Partners	Medium, good vehicle for expansion into like businesses, creates value through synergies, scale and ability to acquire skills	Low to Medium, may ultimately result in some ability to raise capital and acquire skills if beneficiaries sell their shares	Medium to High, raises capital, some ability to acquire skills through industry investors, broad growth options available	Medium to High, may ultimately result in some ability to raise capital and acquire skills if beneficiaries sell their shares	High, raises capital, some ability to acquire skills through industry investors, broad growth options available
<b>Performance Excellence</b>	Medium, able to focus on core business but limited access to external influences may constrain achievements	Medium to High, focus on core business maintained, but injection of expertise in some areas, economies of scope available	Medium to High, focus on core business enhanced with exposure to external practices, economies of scale available	Medium, focus on core business maintained. May be conflict between objectives of Trust and other shareholders	Medium, focus on core business maintained. May be conflict between objectives of Trust and other shareholders over priorities	Low to Medium, conflict between returns to shareholders and performance excellence potentially difficult to manage	Low to Medium, conflict between returns to shareholders and performance excellence potentially difficult to manage
<b>Commerciality</b>	Low to Medium, core business performance remains constrained, regulatory influence weakened, subject to Trust endorsement of financial objectives	Low to Medium, provides access to non regulated returns, core business performance remains constrained, subject to influence of Trust over commercial objectives	Low to Medium, provides access to performance improvements necessary to increase returns, subject to Trust(s) endorsement of financial objectives	Low to Medium, depends on degree of influence of other shareholders and Trust. Provides no funds for investment in growth opportunities	Low to Medium, depends on degree of influence of other shareholders and Trust, provides funds to invest in a broad range of opportunities to enhance returns	Medium, depends on influence of shareholder groups. Provides no funds to invest in growth	Medium to High, depends on influence of shareholder groups, provides funds to invest in a broad range of opportunities to enhance returns
<b>Governance and Control</b>	Simple, but subject to the influence of minority interests, the ability to attract skilled Trustees and the election cycle	Average, depends on relationship with JV partner, risks of Trust ownership remain	Average, depends on relationship and influence of merger partner, risks of Trust ownership remain	Average - Complex, potentially encompasses the challenges of all options	Average - Complex, potentially encompasses the challenges of all options	Average, external/public scrutiny and disclosure to be managed	Average, external/public scrutiny and disclosure to be managed
<b>Administrative Complexity</b>	Medium, and ongoing	Medium to High, and ongoing	Medium to High, and ongoing	High initially and ongoing	High initially and ongoing	High initially, then Medium	High initially, then Medium

## 3. Ownership Structure

### Assessment of Ownership Options for MLL

The following table provides a simple summary of the options. More complex analysis is possible by assigning weightings to the assessment criteria. We suggest the Directors may wish to consider weighting these criteria in accordance with their current strategy in their deliberations of the alternatives presented.

Criteria	100% Trust	Joint Venture	Merger through Equity Exchange	24.9% or 49.9% Dist.	24.9% or 49.9% Sale	100% Dist.	100% Sale
Capability for Growth	Low - Medium	Medium	Medium	Low - Medium	Medium - High	Medium - High	High
Performance Excellence	Medium	Medium - High	Medium - High	Medium	Medium	Low - Medium	Low - Medium
Commerciality	Low - Medium	Low - Medium	Low - Medium	Low - Medium	Low - Medium	Medium	Medium - High
Governance and Control	Simple	Average	Average	Average - Complex	Average - Complex	Average	Average
Administrative Complexity	Medium	Medium - High	Medium - High	High	High	High initially, then Medium	High initially, then Medium

### Summary of the Advantages and Disadvantages of each Option for MLL

**100% Trust Ownership** - The key advantages for retaining 100% MEPT ownership are the ability for the Trust to balance financial and non financial performance (through the SCI and appointment of Directors), the simplicity of the structure and the role of custodian for existing and future generations of Marlborough consumers. It is also the most simple option to implement, because it requires no change from the Status Quo. This option potentially constrains MLL's ability to meet its growth objectives and to maintain shareholder value in the medium term. Limited exposure to external influences and access to expertise are key factors, as well as limited access to capital. The effectiveness of the 100% MEPT model is also dependent on the election cycle and calibre and interests of local Trustee candidates. Solutions to this could include strengthening the Trust model by some or all of the following:

- Increasing the number of trustees;
- Reviewing the appointment of the Chair (say) annually; and
- Providing guidelines for the skills required of trustee candidates.

## 3. Ownership Structure

**Joint Ventures** – This option is able to be implemented alongside continued MEPT ownership of core (network) assets and provides a vehicle for value growth and access to external expertise to improve performance. The advantages of MEPT ownership over core assets are able to be retained. Its successful implementation depends on the identification of suitable opportunities and JV partners. The challenges of Trust ownership remain, albeit diluted to some extent. MLL has already successfully instigated a joint venture arrangement for the acquisition of the OtagoNet EDB.

**Merger by Way of Equity Exchange** – This is most likely to be implemented with like or related businesses such as another network owner or provider of services to network businesses. The role of the MEPT can be preserved in relation to existing assets, but the merger provides opportunities for economies of scale and sharing of best practice to improve MLL's performance and increase value. The successful implementation depends on identification of suitable opportunities and effective negotiation with the other party or parties. The challenges of Trust ownership are retained.

**Distribution of 24.9% or 49.9% of Shares to Beneficiaries** – While MEPT retains control under this scenario, MLL's obligations to all shareholders would mean in effect the scope of influence of the Trust over core assets is more limited than under the previous models. This give-away option provides no immediate access to capital or external expertise. External reporting, disclosure and administrative requirements would be added to the existing costs of the Trust model.

**Sale of 24.9% or 49.9% of Shares to Consumers, the Public, Industry or Institutional Investors** – While the MEPT retains control under this scenario, MLL's obligations to all shareholders would mean the influence of the Trust over core assets is also limited. This option provides access to capital but limited access to external expertise for performance improvement. Shares may be listed. As above, external reporting, disclosure and administrative requirements would be added to the existing costs of the Trust model. The challenges of Trust ownership are retained, albeit somewhat diluted.

**Distribution of 100% of Shares to Beneficiaries** – MEPT loses influence over MLL's assets and is dissolved. Existing beneficiaries are gifted shares or cash for their own use. MLL potentially gains access to capital markets and the Company is subject to a high degree of external scrutiny that must be managed. Returns to existing shareholders may become the primary measure of performance, at the expense of service quality for existing and future consumers or other existing objectives such as environmental considerations or community sponsorship.

**Sale of 100% of Shares to Consumers, the Public, Industry or Institutional Investors** – MEPT loses influence over MLL's assets, but potentially gains a fund to manage on behalf of its beneficiaries, or alternatively existing consumers gain shares or cash for their own use. MLL gains access to capital and is able to pursue growth opportunities. Shares may be listed. The Company is subject to a high degree of external scrutiny that must be managed. As above, returns to existing shareholders may become the primary measure of performance, at the expense of service quality for existing and future consumers.

## 3. Ownership Structure

### Options for Funding Growth

One of the key issues MLL must address as part of this Ownership Review is the best means of funding its growth strategy. In this respect we make the following observations:

- There are essentially three sources of funds available - senior debt, subordinated debt and equity.
- Senior debt is generally the preferred source up to a ceiling which is defined by either banking covenants, the preference of the Company to retain some headroom or credit ratings (either actual or shadow). For network companies, investment grade ratings of BBB/BBB+ are typical.
- Subordinated debt is generally the next preference and may be sourced from bank or retail sources. It is also possible to structure hybrid equity instruments (which may be excluded from bank covenants). The ceilings for this source are generally based on debt servicing covenants.
- Equity injection is typically the source of last resort as it results in dilution of current shareholders' interests.

*Progression through each of these steps has been demonstrated by Vector as it sought to fund its purchase of UnitedNetworks followed by Natural Gas Corporation. It was only when it reached its ceiling for senior debt that it introduced other sources of debt, and finally elected to sell down 24.9% of its equity.*

### Conclusion on Ownership Options for MLL

There appears to be a real benefit to Trust ownership in the balancing of financial and non financial performance and the retention of local influence over local assets for the benefit of both current and future generations of consumers. It is also the most simple option to implement because it requires no change from the status quo.

The existing Trust structure has served MLL well to date as evidenced by the investments made in OJV, NEL and OPSL. This should continue to be the case, however at some point in the future this structure may impose limitations on MLL's ability to meet its growth, excellence and commercial objectives. A further review of its ownership structure would be appropriate at that time. The 100% Trust option potentially limits MLL's ability to fund investments in new activities whether they are expansion of existing activities or entry into new activities. This in turn may limit MLL's ability to achieve its target returns and improve shareholder value. As MLL faces increasing demand on capital to invest in its own ageing network infrastructure, funds for distribution to the beneficiaries of the Trust will have to compete with funds for investment in new activities to meet the Company's growth objectives.

The existing benefits of Trust ownership can be retained to a greater or lesser extent by a number of the alternative ownership options considered (and other versions of these) and the external funding options available. The Commerce Commission now monitors EDB price, profit and quality performance on behalf of consumers, which previously was essentially the preserve of the consumer trusts. The 100% trust option provides for an exemption from this oversight, but as a fall back option it remains.

## 3. Ownership Structure

We acknowledge that in the case of MLL, the realm of the Trust excludes consumers located on the NEL and OJV networks, however the obligations of the Company to treat all customers fairly, combined with the Trust oversight in effect means that all consumers benefit to some extent from this interest, subject to the interests of the other shareholders in these investments. A divestment or sale of 100% of the shares in the Trust forgoes these benefits.

When and if MLL takes the first step away from a 100% Trust model is, in our view, dependent on the size and nature of the growth opportunities that arise, the readiness of MLL to respond to these opportunities, the availability of debt funding and the availability of suitable investors or partners. At this time there does not appear to be an opportunity which is sufficiently advanced to justify MLL making a decision to move from the status quo, although we note that continuing acquisitions and consolidation within the sector may provide opportunities in the future.

One issue that the Company does need to consider in some detail is its ability to respond quickly to opportunities as they arise. This may take the form of identification of potential sources of debt funding, potential joint venture or equity partners, a plan for partial share distribution or sale and discussion with the Trust as to their preferred options for alternative ownership models.

The type of scenarios MLL may wish to consider include those which are consistent with the overall strategy of the company, its expertise and those which meet commercial objectives. Possible scenarios include:

- Identification of potential joint venture partners for vertical expansion opportunities such as generation, embedded generation and contracting.

*Examples of vertical integrations include Vector's part ownership of Treescape, a vegetation control company, the Eastland Trust's acquisition of the local seaport in addition to its electricity network interests and Electra's purchase of DataCol, an electricity, gas and water meter reading business.*

- Additional agreements with other council or Trust owned lines businesses for potential mergers or acquisitions of networks.

*Examples of network acquisitions include MLL and Network Tasman's joint purchase of NEL and MLL, and TPC and EIL's purchase of Otago Power in a joint venture.*

- Development of a network management company with or without other partners to explore opportunities for facility management of other infrastructural businesses.

*Examples include PowerNet, which is owned by TPC and EIL, which manages both these networks, plus the OtagoNet JV network and more recently the Stewart Island electricity supply, and Unison, which manages the Centralines network.*

# Section 4

## MLL's Performance

## 4. MLL's Performance

### Operational Highlights

Since 2003 MLL has continued to transform itself into a regional network company with interests in Marlborough, Nelson and Otago. The acquisition of the OtagoNet EDB by way of joint venture with EIL and TPC in 2002 built upon MLL's acquisition of 50% of NEL in 1996. These transactions increased MLL's total supply catchment from 11,300 km<sup>2</sup> to over 23,000 km<sup>2</sup>, and increased its share of customer connections from 25,325 in 2002 to over 47,200<sup>1</sup>.

Much of MLL's network was installed during the 1950s, '60s and '70s and significant portions of the network will need to be replaced over the next 20 years. In addition to ageing assets, economic growth in MLL's catchment has been strong in the recent past, especially in respect to the viticulture industry, and is expected to continue to grow significantly in the future. This growth has already required significant expenditure on new reticulation and a strengthening of the capacity of existing feeder infrastructure. Collectively, this demand growth combined with ageing infrastructure is predicted to result in capital expenditures of approximately \$10 million per annum for at least the next ten years, a significant increase when compared to the \$4.7 million spent in the 2004 financial year.

The implementation of the targeted control regime by the Commerce Commission has seen limitations placed on the prices that EDBs can charge to consumers. Price increases by MLL in 2004, 2005, 2006 and 2008 breached these thresholds and resulted in ongoing discussions with the Commerce Commission over how a return on investment from MLL's significant network expansion can be generated under the current regime. MLL and the Commerce Commission agreed to a price freeze in 2007 to allow time for suitable pricing regime to be agreed, but when this could not be achieved MLL

<sup>1</sup> Calculation based upon MLL accounting for 51% of OJV's and 50% of NEL's customers as their own.

resumed price increases in order to generate an adequate return on its network assets. A secondary effect of the regime and the ensuing price breaches has been a notable increase in the costs of regulatory compliance.

Despite these limitations, MLL has been able to grow total revenues from \$22 million (pre discounts) in 2003 to \$44 million in 2008 with its operating surplus (EBITDA) growing from \$3.5 million to \$14.5 million over the same period. MLL enjoyed a fixed asset revaluation gain of \$90 million in 2004, and a further gain of \$31 million in 2007. As part of the growth of MLL's investments, OJV's assets were revalued by \$17 million in 2007, and NEL's assets were revalued in 2005 and 2008, leading to valuation gains of \$9 million and \$5 million respectively.

MLL Parent	2003	2004	2005	2006	2007	2008
Total System Length (kms)	3,173	3,141	3,169	3,213	3,261	3,464
Network Area (km <sup>2</sup> )	11,300	11,300	11,300	11,300	11,300	11,300
Customers	21,417	22,251	22,590	22,932	23,118	23,584
Staff	93	86	96	117	137	123
Operating Revenues (pre discounts) (\$m)	19.6	22.8	24.7	30.8	31.5	38.8
Operating Surplus (EBITDA) (\$m)	3.5	7.7	8.2	12.6	11.1	14.5
Capex (\$m)	3.3	6.4	4.8	10.6	11.3	13.3
System Fixed Asset Value (DRC \$m)*	16	108	109	117	153	n/a
Total Assets (\$m)	92	188	194	200	238	251
Transformer Capacity (MVA)	232	245	256	265	271	288
Maximum Demand (MW)	55	55	58	58	68	70
Energy into Network (GWh)	324	326	343	350	357	373

Source: MLL Annual Reports 2003-2008

\*DRC values for system fixed assets are sourced from Gazetted Information Disclosures 2003-2007.

## 4. MLL's Performance

### Operational Highlights

In addition to the expansion of the network, MLL has embarked on a number of improvements to its network to increase the security of supply to its customers. Initiatives implemented by MLL include installing bird spikes and longer-length possum guards on poles, and continuing to install distribution capacity ahead of growing customer requirements. We also note that MLL's concerns relating to restricted transmission capacity have been somewhat alleviated by Transpower completing a third high-voltage circuit into the region. At this time MLL is not pursuing a substantial programme of undergrounding due to an inability to generate a sufficient return on those assets under the present regulatory regime.

MLL has taken a proactive stance in respect to the environment, achieving an ISO 14001 environmental accreditation and the Company is the only EDB in New Zealand that has assessed its carbon footprint (excluding network losses). In this process, the Company discovered that its assessed footprint is offset by the carbon capture delivered by MLL's native forest holdings. The Company has also completely sound-proofed the 33/11kV zone substations in Blenheim and Picton for the benefit of neighbouring residents.

MLL has also strived to improve its internal standards, implementing ISO accredited systems for management and health and safety. MLL and its staff have also received several awards including Best 2007 Annual Report in New Zealand for companies in the small to medium category, a Silver Award in the Australasian Annual Report Awards, Young ITC talent of the year (Amanda White) and OPSL has received the ESITO Excellence Award.

MLL is also a keen supporter of the Marlborough community, sponsoring a range of youth, education and community events. In particular, the Company continues to support the Omaka Aviation Heritage Centre, the Classic Fighters Airshow and the Marlborough Lines Stadium, in addition to several other events and awards.

As for other EDBs, MLL has noted the difficulties in recruiting suitably experienced construction and maintenance staff from New Zealand's increasingly limited talent pool. This is an important consideration for MLL as it progresses its programs of network renewal and expansion. To assist in addressing this issue, Marlborough Lines Contracting has implemented its own in-house training programme and promotes staff interchanges between itself and OPSL. The contracting division also promotes a quality and safe workplace environment, and has achieved three ISO quality systems accreditations and an 'Achiever Status' award from Occupational Health and Safety for health and safety initiatives.

## 4. MLL's Performance

### Performance against SCI Targets

Each year the Trustees of MEPT and the Directors of MLL agree on the SCI for the Company for the coming year. The SCI sets out certain financial and quality of supply targets which the Trustees can use as a benchmark for the Company's performance in order to ensure that the best interests of the Trust's beneficiaries and MLL's customers in general are being served.

The table opposite sets out MLL's performance against SCI targets for the period 2003 to 2008. A full analysis of performance against these targets can be found in Appendix 2.

MLL has shown a mixed performance with respect to earnings targets, but we note that in years when targets have not been achieved, the shortfall has generally been small. From 2003 onwards, the Company has achieved all operating turnover targets with the exception of 2007 (the year of the price freeze). Net operating surplus after tax targets have all been met except in 2005 and 2007. Since 2003 shareholders equity targets have all been achieved with the exception of 2007.

Operation and maintenance cost targets have not been met in four of the six periods examined. Costs have been impacted by increasing material and labour costs and the substantial level of maintenance that MLL is incurring to improve the reliability of its network. Capital expenditure targets with the exception of 2004 have been met.

Targets for dividends received from NEL and dividends paid to MEPT have been met in most years. Targets for discounts paid to MLL's customers have been met in three of the six financial periods, although we note that in two of the three years the shortfall in discounts paid compared to the target was immaterial.

### MLL SCI Performance - Achievement of Targets

	2003	2004	2005	2006	2007	2008
<b>Financial Measures</b>						
Operating turnover	√	√	√	√	x	√
Operating surplus after tax	√	√	x	√	x	√
EBIT/average net funds employed	√	x	x	√	x	√
NPAT/shareholders funds	√	x	x	√	x	√
Adjusted NPAT/shareholders funds*	x	x	√	√	x	√
Shareholders equity	√	√	√	√	x	√
Net asset backing per share	√	√	√	√	√	√
Shareholder funds/ total assets	x	√	x	√	√	√
Return on equity after tax from NEL						x
Return on equity after tax from Otago region investment						x
<b>Expenditure</b>						
Network business maintenance and operations expenditure per customer	√	x	x	x	√	x
Capital expenditure	√	x	√	√	√	√
<b>Dividends/Discounts</b>						
Dividends received from NEL			√	√	√	x
Discounts paid to Marlborough Lines customers	x	√	√	x	√	x
Dividends paid to MEPT	√	x	√	√	√	√
<b>Network Performance</b>						
Energy supplied to the Marlborough Network	√	x	√	x	x	√
SAIDI Planned	√	√	x	x	x	√
SAIDI Unplanned	√	x	x	x	x	x
Total SAIDI	x	x	x	x	x	x
SAIFI Planned	√	√	x	√	x	
SAIFI Unplanned	√	√	√	x	x	
CAIDI Planned	x	√	x	x	x	
CAIDI Unplanned	x	x	x	√	√	
Faults per 100 km line	√	√	√	x	x	

Source: MLL Annual Reports 2003-2008

\* After adding back discounts and using DRC to establish the value of net assets.

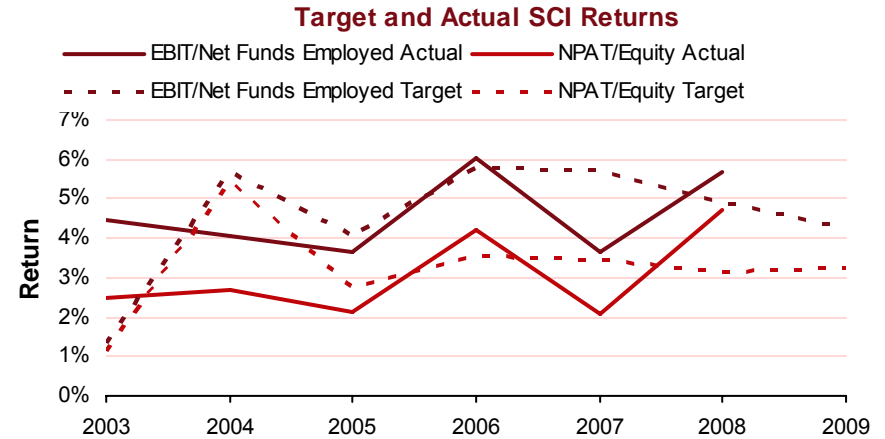
## 4. MLL's Performance

### Performance against SCI Targets

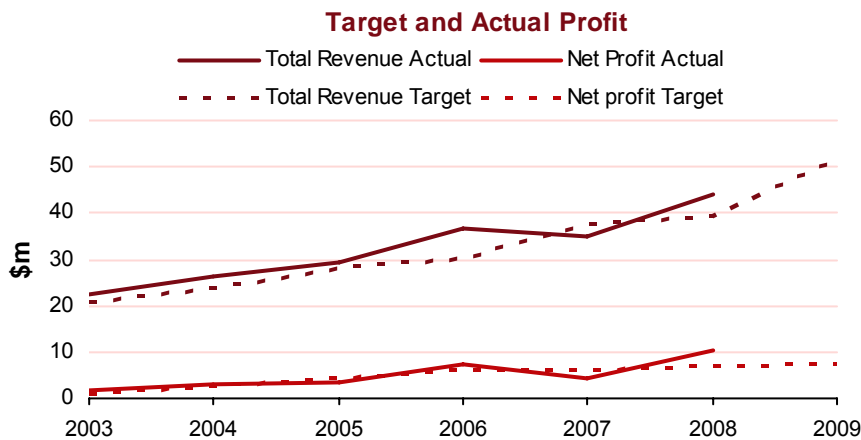
MLL has demonstrated mixed performance with respect to quality of supply as the duration and frequency of both planned and unplanned outages have not met SCI targets. Total SAIDI has failed to meet the SCI targets for all six years. The SAIDI results are mainly attributable to high levels of planned outages resulting from network development and expansion demands which have occurred over the period examined.

### 2009 Targets

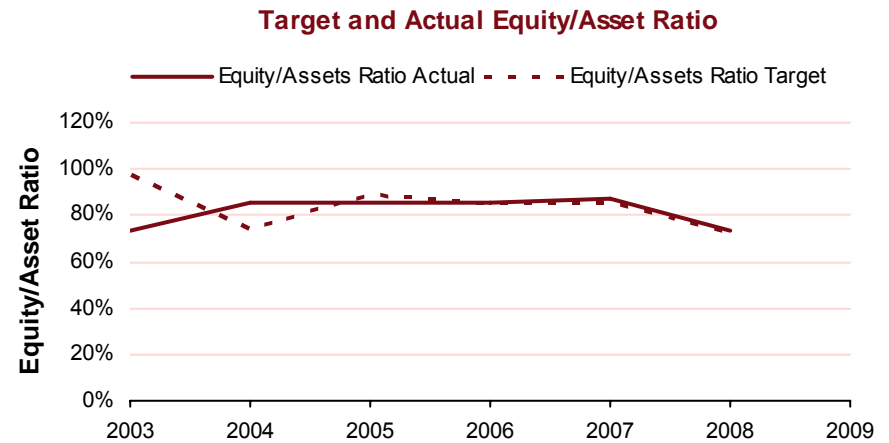
The most recent SCI also outlines budgeted and projected targets for 2009, which are set out, together with historical targets and actual performance, on the charts below, opposite and in Appendix 2.



Source: MLL Annual Reports 2003 – 2008, 2008 SCI



Source: MLL Annual Reports 2003 – 2008, 2008 SCI



Source: MLL Annual Reports 2003 – 2008, 2008 SCI

## 4. MLL's Performance

### Financial Performance

MLL has applied the NZ IFRS standards to the preparation of its financial statements for the year ended 31 March 2008. Comparative information for the 2007 year is also provided under NZ IFRS. Therefore, a direct comparison of financial performance over the period 2003 to 2008 cannot be made. We set out the historical financial performance of the Company under both reporting standards in the tables on the following page. The restated 2007 financial statements show that the results prepared under NZ IFRS do not result in significant differences to those prepared under NZ GAAP.

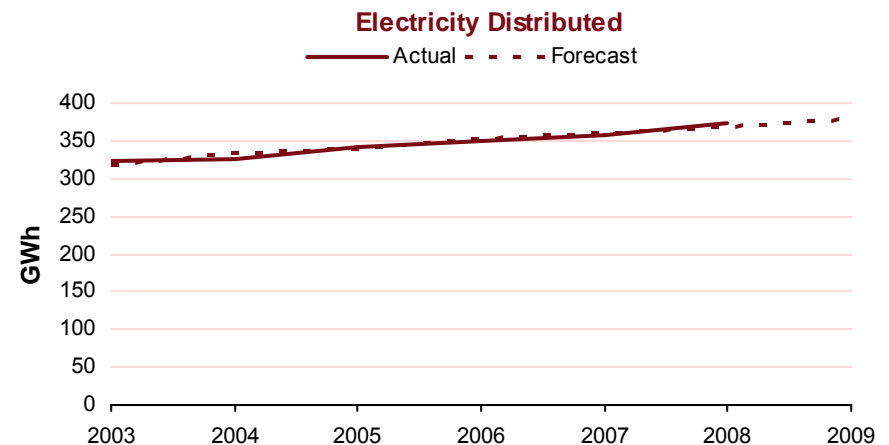
Overall MLL has performed very well over the six years to 2008. MLL's operating revenue has increased by 98%, or 12% per annum, over the period 2003 to 2008. This strong growth is driven by two factors: volume growth and price increases. The primary reason for the volume growth (illustrated opposite) is the region's ongoing economic expansion during the period, particularly in relation to the growth of the viticulture, aquaculture and forestry sectors. Tourism is also contributing to increasing energy demands.

Growth in revenue has also been enhanced by line charge increases in April 2003 (5.7%), June 2004 (12%), May 2005 (8.4%), and April 2007 (12.0%). These increases have primarily been introduced to achieve a more commercial return on investment. Operating revenues are expected to further increase in 2009 due to line charges increasing by 17.6% on 1 April 2008.

This revenue increase has been partly offset by higher expenses. Higher operating expenses reflect increased input costs for wages and salaries and the cost of imported distribution equipment components (cooper, aluminium etc). MLL has also incurred higher regulatory expenses due to the Commerce Commission's investigations following price increases. MLL has reported that compliance costs are up to \$15 per customer per annum.

As illustrated overleaf, increased net profit has been a result of revenue growing at a faster rate than expenses. The reported net profit has increased by 36% per annum on average over the 2003 to 2008 period, although this trend was interrupted in 2007 with the price freeze.

The sole beneficiaries of MEPT are electricity customers connected to the Marlborough network. All surpluses of the Company are either provided to customers by way of discount, provided to the Trust as a dividend or are reinvested. MLL's total distributions to customers make up a significant proportion of its net surplus before tax, with an aggregate of \$30.9 million paid out between 2003 and 2008.



Source: MLL Annual Reports 2003 – 2008

## 4. MLL's Performance

### Financial Performance

<b>MLL Parent</b> <b>Year ended 31 March</b>	<b>2003</b> <b>(\$000)</b>	<b>2004</b> <b>(\$000)</b>	<b>2005</b> <b>(\$000)</b>	<b>2006</b> <b>(\$000)</b>	<b>2007</b> <b>(\$000)</b>
<b>Operating Revenue</b>	<b>19,583</b>	<b>22,757</b>	<b>24,710</b>	<b>30,780</b>	<b>31,501</b>
Change		16%	9%	25%	2%
Dividend Income	850	950	1,100	1,900	1,060
Share of Associates Net Surplus	(20)	(121)	(324)	(1,024)	(367)
Discounts	(4,001)	(4,000)	(4,100)	(4,170)	(4,341)
Operating Expenses	(12,892)	(11,882)	(13,146)	(14,893)	(16,790)
<b>EBITDA</b>	<b>3,520</b>	<b>7,704</b>	<b>8,240</b>	<b>12,593</b>	<b>11,063</b>
Change		19%	7%	53%	-12%
Depreciation	(1,982)	(4,533)	(4,971)	(5,497)	(5,939)
Amortisation	(109)	(109)	(109)	(109)	(109)
<b>EBIT</b>	<b>1,429</b>	<b>3,062</b>	<b>3,160</b>	<b>6,987</b>	<b>5,015</b>
Change		114%	3%	121%	-28%
Interest Income	2,039	2,632	3,454	3,846	2,594
Interest Expense	(1,143)	(1,203)	(1,238)	(1,314)	(1,287)
<b>Operating Earnings Before Tax</b>	<b>2,325</b>	<b>4,491</b>	<b>5,376</b>	<b>9,519</b>	<b>6,322</b>
Change		93%	20%	77%	-34%
Income Tax	(680)	(1,426)	(1,841)	(2,293)	(2,067)
<b>Net Profit After Tax</b>	<b>1,645</b>	<b>3,065</b>	<b>3,535</b>	<b>7,226</b>	<b>4,255</b>
Change		86%	15%	104%	-41%
Discounts	4,001	4,000	4,100	4,170	4,341
Dividends paid to MEPT	265	150	150	150	250
<b>Total Distributions</b>	<b>4,266</b>	<b>4,150</b>	<b>4,250</b>	<b>4,320</b>	<b>4,591</b>
As a percentage of Operating Earnings before Tax	183%	92%	79%	45%	73%

Source: 2003-2007 Annual Reports prepared in accordance with NZ GAAP

<b>MLL Parent</b> <b>Year ended 31 March</b>	<b>2007</b> <b>(\$000)</b>	<b>2008</b> <b>(\$000)</b>
<b>Operating Revenue</b>	<b>31,501</b>	<b>38,832</b>
Change		23%
Dividend Income	1,060	900
Other income	(70)	53
Discounts	(4,341)	(4,461)
Operating Expenses	(16,912)	(20,828)
<b>EBITDA</b>	<b>11,238</b>	<b>14,496</b>
Change		29%
Depreciation	(5,556)	(6,171)
Amortisation	(368)	(275)
<b>EBIT</b>	<b>5,314</b>	<b>8,050</b>
Change		51%
Interest Income	2,594	4,365
Interest Expense	(1,287)	(1,623)
<b>Operating Earnings Before Tax</b>	<b>6,621</b>	<b>10,793</b>
Change		63%
Income Tax	(2,042)	(325)
<b>Net Profit After Tax</b>	<b>4,579</b>	<b>10,468</b>
Change		129%
Discounts	4,341	4,461
Dividends paid to MEPT	250	250
<b>Total Distributions</b>	<b>4,591</b>	<b>4,711</b>
As a percentage of Operating Earnings before Tax	69%	44%

Source: 2008 Annual Report prepared in accordance with NZ IFRS

## 4. MLL's Performance

### Financial Position

MLL's Statement of Financial Position set out on the following page illustrates the significant increase in the size of the Company since 2003. Total assets have increased by 175% over the period reflecting the 2004 and 2007 revaluations of MLL's local electricity reticulation network. The 2004 revaluation reflects a change in accounting policy from historical cost to a fair value revaluation, based on a depreciated replacement cost ("DRC") approach. A further DRC revaluation was undertaken in 2007 to ensure the carrying value remained consistent with fair value.

A reduction in term loans in 2004 together with the increase in shareholders funds arising from the network revaluation resulted in the debt to debt-plus-equity ratio declining from 26% in 2003 to 11% in 2004. The debt to debt-plus-equity ratio has remained at around 11% over the 2004 to 2008 period. MLL therefore has significant capacity to raise capital via debt sources.

## 4. MLL's Performance

### Financial Position

MLL Parent Year ended 31 March	2003 (\$'000)	2004 (\$'000)	2005 (\$'000)	2006 (\$'000)	2007 (\$'000)
<b>Current Assets</b>					
Cash and Bank Balances	55	424	(733)	90	(235)
Short Term Deposits	-	-	500	200	-
Accounts Receivable	2,198	2,314	3,115	3,966	3,331
Taxation Receivable (payable)	(711)	(1,330)	125	(1,478)	(1,314)
Inventories and Work in Progress	2,006	1,825	2,773	3,156	2,948
<b>Total Current Assets</b>	<b>3,548</b>	<b>3,233</b>	<b>5,780</b>	<b>5,934</b>	<b>4,730</b>
<b>Non-Current Assets</b>					
Investments	66,174	66,616	69,507	68,482	68,369
Plant, Property and Equipment	20,134	116,858	118,502	125,904	165,328
Goodwill	1,438	1,329	-	-	-
Future Income Tax Benefits	213	-	-	-	-
<b>Total Non-Current Assets</b>	<b>87,959</b>	<b>184,803</b>	<b>188,009</b>	<b>194,386</b>	<b>233,697</b>
<b>Total Assets</b>	<b>91,507</b>	<b>188,036</b>	<b>193,789</b>	<b>200,320</b>	<b>238,427</b>
Change		105%	3%	3%	19%
<b>Current Liabilities</b>					
Creditors and Accruals	1,303	2,568	2,491	3,083	3,450
<b>Total Current Liabilities</b>	<b>1,303</b>	<b>2,568</b>	<b>2,491</b>	<b>3,083</b>	<b>3,450</b>
<b>Non-Current Liabilities</b>					
Employee Entitlement	401	332	386	460	495
Deferred Tax	-	4,954	5,459	6,028	6,939
Term Loans	23,000	20,000	20,000	18,800	20,500
<b>Total Non-Current Liabilities</b>	<b>23,401</b>	<b>25,286</b>	<b>25,845</b>	<b>25,288</b>	<b>27,934</b>
<b>Total Liabilities</b>	<b>24,704</b>	<b>27,854</b>	<b>28,336</b>	<b>28,371</b>	<b>31,384</b>
Change		13%	2%	0%	11%
<b>Equity</b>	66,803	160,182	165,453	171,949	207,043
Change		140%	3%	4%	20%
<b>Total Liabilities &amp; Equity</b>	<b>91,507</b>	<b>188,036</b>	<b>193,789</b>	<b>200,320</b>	<b>238,427</b>

Source: MLL Annual Reports 2003-2007 prepared in accordance with NZ GAAP

MLL Parent Year ended 31 March	2007 (\$'000)	2008 (\$'000)
<b>Current Assets</b>		
Cash and Bank Balances	-	22
Other Current Financial Assets	97	53
Accounts Receivable	3,480	3,923
Taxation Receivable (Payable)	(1,315)	(2,167)
Inventories and Work in Progress	2,948	3,841
<b>Total Current Assets</b>	<b>5,210</b>	<b>5,672</b>
<b>Non-Current Assets</b>		
Investments	56,922	56,672
Plant, Property and Equipment	162,501	174,557
Investment Property	2,100	2,100
Intangible Assets	742	814
<b>Total Non-Current Assets</b>	<b>233,935</b>	<b>245,813</b>
<b>Total Assets</b>	<b>239,145</b>	<b>251,485</b>
Change		5%
<b>Current Liabilities</b>		
Cash and Cash Equivalents	235	-
Trade and Other Payables	2,932	3,986
Employee Entitlements	518	682
Other Current Liabilities	167	-
<b>Total Current Liabilities</b>	<b>3,852</b>	<b>4,668</b>
<b>Non-Current Liabilities</b>		
Employee Entitlement	495	473
Deferred Tax	40,733	38,649
Term Loans	20,500	23,350
<b>Total Non-Current Liabilities</b>	<b>61,728</b>	<b>62,472</b>
<b>Total Liabilities</b>	<b>65,580</b>	<b>67,140</b>
Change		2%
<b>Equity</b>	173,565	184,345
Change		6%
<b>Total Liabilities &amp; Equity</b>	<b>239,145</b>	<b>251,485</b>

Source: MLL Annual Report 2008 prepared in accordance with NZ IFRS

## 4. MLL's Performance

### Performance of Investments

MLL's investments (NEL, OJV and OPSL) have made positive contributions to MLL's financial results over the 2003-2008 period. These investments have demonstrated increased profitability and have benefited MLL through increasing dividends and continued growth. The 2007 and 2008 financial results for NEL, OJV and OPSL are set out in the table opposite.

Key financial and operational measures for NEL, OJV and OPSL are set out on the following page. MLL's investments in NEL and OPSL produced total tax paid dividends of \$7.8 million over the 2003 to 2008 period. The Company's investment in OJV contributed cash earnings of \$15.2 million over the same period and produced significant tax benefits which reduced MLL's payable taxation. OPSL generated the highest average return on investment (15.4% over 2003-2008). NEL and OJV produced an average 9.5% and 4.3% return on investment respectively over 2003-2008.

Like MLL, NEL and OJV's networks have experienced noticeable growth over the past six years. The asset values have increased by 72% and 18% for NEL and OJV respectively from 2003 to 2007. Maximum demand for NEL has also increased by 15% over the same period.

Financial Summary for MLL's Associate Entities for the Year ended 31 March	2007	2008	2007	2008	2007	2008
	(\$000)	(\$000)	(\$000)	(\$000)	(\$000)	(\$000)
	NEL		OJV		OPSL	
<b>MLL's Share</b>	50%		51%		51%	
<b>Revenue</b>						
Operating Revenue	7,402	7,480	19,720	24,247	8,155	9,210
Other	258	281	583	-	-	-
<b>Expenditure</b>						
Operation and Maintenance	(3,822)	(3,751)	(9,985)	(8,803)	-	-
Cost of sales	-	-	-	-	(5,677)	(6,847)
Administration	(86)	(90)	(106)	(116)	(29)	(29)
<b>EBITDA</b>	<b>3,752</b>	<b>3,919</b>	<b>10,212</b>	<b>15,328</b>	<b>2,449</b>	<b>2,334</b>
Depreciation	(991)	(1,169)	(4,534)	(4,662)	(510)	(721)
<b>EBIT</b>	<b>2,761</b>	<b>2,750</b>	<b>5,678</b>	<b>10,666</b>	<b>1,939</b>	<b>1,613</b>
Interest Income	41	29	25	29	-	-
Interest Expense	(256)	(293)	(24)	(2)	(90)	(120)
<b>Operating Earnings Before Tax</b>	<b>2,546</b>	<b>2,487</b>	<b>5,679</b>	<b>10,693</b>	<b>1,849</b>	<b>1,493</b>
Income Tax	(942)	(962)	-	-	(614)	(509)
<b>Net Profit After Tax</b>	<b>1,604</b>	<b>1,525</b>	<b>5,679</b>	<b>10,693</b>	<b>1,235</b>	<b>983</b>
Current Assets	825	812	2,493	2,528	1,966	1,833
Non Current Assets	24,258	28,462	122,229	125,685	2,808	3,496
<b>Total Assets</b>	<b>25,083</b>	<b>29,274</b>	<b>124,722</b>	<b>128,213</b>	<b>4,774</b>	<b>5,329</b>
Current Liability	724	517	1,449	1,790	915	1,088
Non Current Liability	3,470	3,600	-	-	1,200	1,200
Equity	20,889	25,157	123,273	126,423	2,659	3,041
<b>Total Equity and Liabilities</b>	<b>25,083</b>	<b>29,274</b>	<b>124,722</b>	<b>128,213</b>	<b>4,774</b>	<b>5,329</b>

Source: MLL Annual Report 2008 prepared in accordance with NZ IFRS, reflecting 100% of each entity.

## 4. MLL's Performance

### Performance of Investments

Returns from Investments for the Year ended 31 March	2003 (\$000)	2004 (\$000)	2005 (\$000)	2006 (\$000)	2007 (\$000)	2008 (\$000)
<b>Distributions to MLL</b>						
From NEL	850	950	1,100	1,900	1,060	900
Change		2%	16%	73%	-44%	-15%
From OJV*	1,479	2,305	2,193	2,703	2,270	4,233
Change		56%	-5%	23%	-16%	87%
From OPSL		204	153	153	204	306
Change						
<b>Total</b>	<b>2,329</b>	<b>3,459</b>	<b>3,446</b>	<b>4,756</b>	<b>3,534</b>	<b>5,439</b>
		49%	0%	38%	-26%	54%
<b>Interest In Associate Entities**</b>						
NEL	11,408	11,338	12,058	12,327	11,631	11,670
		-1%	6%	2%	-6%	0%
OJV	56,215	56,442	56,668	56,668	56,795	63,866
		0%	0%	0%	0%	12%
OPSL	952	955	971	1,162	1,669	2,107
		0%	2%	20%	44%	26%
<b>Return on Investment***</b>						
NEL	7%	8%	9%	15%	9%	8%
OJV	3%	4%	4%	5%	4%	7%
OPSL	-	21%	16%	13%	12%	15%

Source: MLL Annual Reports 2003-2008

\* Includes MLL's 5% interest in OJV's distributions to JV parties. Excludes tax benefit derived by MLL from OJV.

\*\* Average book value of investment.

\*\*\* Dividend yield for NEL and OPSL, return on book value of investment for OJV.

Performance of Investments for the Year ended 31 March	2003	2004	2005	2006	2007	2008
<b>NEL</b>						
Network Asset Value (DRC \$m)	13.3	13.5	22.2	23.3	22.9	26.7
System Length (kms)	242	240	242	244	245	246
Customer Numbers	8,614	8,735	8,876	8,915	8,900	8,894
Electricity Distributed (GWh)	151	146	154	153	157	159
Maximum Demand (MW)	30	30	30	31	32	34
<b>OJV</b>						
Network Asset Value (DRC \$m)	91.1	91.0	89.3	90.0	107.6	110.2
System Length (kms)	4,210	4,355	4,370	4,344	4,380	4,147
Customer Numbers	14,502	14,542	14,585	14,497	14,692	14,747
Electricity Distributed (GWh)	368	367	380	372	376	390
Maximum Demand (MW)	53	55	55	54	54	54

Source: PricewaterhouseCoopers ELB Compendium 2003-2007, MLL Annual Report 2008

## 4. MLL's Performance

### Operations

As illustrated in the table opposite, MLL has experienced continued growth across its network over the past six years. System length has increased by 9%, the number of customer connections (ICPs) has increased by 10%, transformer capacity has increased by 24% and maximum demand has increased by 27%. Significantly, the total volume of electricity has increased by 15%.

<b>MLL Parent Operational Performance</b>	<b>2003</b>	<b>2004</b>	<b>2005</b>	<b>2006</b>	<b>2007</b>	<b>2008</b>
System Length (kms)	3,173	3,141	3,169	3,213	3,261	3,464
Total Customers (ICPs)	21,417	22,251	22,590	22,932	23,118	23,584
Transformer Capacity (MVA)	232	245	256	265	271	288
Maximum Demand (MW)	55	55	58	58	68	70
Electricity Distributed (GWh)	324	326	343	350	357	373

Source: MLL Annual Reports 2003-2008

### Tariffs

Average unit revenues excluding capital contributions, measured on a per kWh and per ICP basis, have shown a significant increase over the period as a result of tariff adjustments in 2004, 2005, 2006 and 2008, and steady growth in the volume of electricity distributed. The price increases reflect MLL's target of moving towards achieving a more commercial return on investment.

<b>MLL Parent Line Charge Revenue*</b>	<b>2003</b>	<b>2004</b>	<b>2005</b>	<b>2006</b>	<b>2007</b>	<b>2008</b>
Revenue \$/ICP	726	733	833	936	949	1,077
Revenue cents/kWh	5.1	5.3	5.9	6.5	6.6	6.8

Source: PricewaterhouseCoopers ELB Compendium 2002-2007, MLL annual report 2008

\* Before discount

### Costs

Costs, both direct and indirect as measured on a per km, a per ICP and a per kWh basis, have shown substantial increases since 2003. This is attributed to the increase in underlying input costs for materials and labour, rising staff numbers, an increase in regulatory compliance costs and increased spending on improving network reliability in remote areas. It is expected that as the network continues to age, costs will continue to increase until the benefits of the planned network renewal program begin to impact on repair and maintenance costs.

<b>MLL Parent Costs</b>	<b>2003</b>	<b>2004</b>	<b>2005</b>	<b>2006</b>	<b>2007</b>
Direct & Indirect Line Costs \$/km	1,012	1,834	2,107	2,256	2,465
Direct & Indirect Line Costs \$/ICP	201	259	296	316	348
Direct & Indirect Line Costs cents/kWh	1.1	1.9	2.1	2.2	2.4

Source: PricewaterhouseCoopers ELB Compendium 2003-2007

## 4. MLL's Performance

### Network Return Metrics

As illustrated in the table opposite, MLL's network has generated improving returns since 2003. The large ROI achieved in 2004 was the result of gains from the 2004 ODV revaluation of network assets. Whilst returns could have been further improved, they were achieved against a background of regulatory constraints and price increases which exceeded the pricing guidelines of the Commerce Commission. The increasing ODV value since 2004 also has an offsetting impact on the regulatory returns.

### Capital Expenditure

Capital expenditure has increased by 297% from 2003 to 2008. 45% of capital expenditure has been in relation to overhead and underground reticulation and 29% to substation installation and renewal. The increased loads arising from the wine industry, the strong regional economy and population growth experienced during the period has resulted in demand for new electricity reticulation, transformers and increased zone substation capacity. Capital expenditure is expected to continue to increase to ensure that capacity is available to meet future demand. Another driver of increased capital expenditure is network reliability. MLL continues to experience relatively high levels of unplanned interruptions as many areas in the Marlborough region are subject to severe storms. Network reinforcement expenditure, along with targeted maintenance, such as tree trimming, are aimed at reducing interruptions in the medium term.

<b>MLL Parent Performance ratios</b>	<b>2003 %</b>	<b>2004 %</b>	<b>2005 %</b>	<b>2006 %</b>	<b>2007 %</b>
Return on Funds (ROF)	0.40	1.96	2.43	5.90	4.19
Return on Equity (ROE)	-0.08	1.10	1.61	4.94	3.09
Return on Investment (ROI)	5.14	28.23	1.31	4.60	2.78

Source: PricewaterhouseCoopers ELB Compendium 2003-2007

<b>MLL Parent Capital Expenditure</b>	<b>2003 (\$000)</b>	<b>2004 (\$000)</b>	<b>2005 (\$000)</b>	<b>2006 (\$000)</b>	<b>2007 (\$000)</b>	<b>2008 (\$000)</b>
Overhead and Underground Reticulation	1,248	4,528	2,335	4,245	4,729	5,122
Main Substations	1,129	526	360	4,806	3,849	3,704
Other	971	1,346	2,104	1,533	2,745	4,474
<b>Total</b>	<b>3,348</b>	<b>6,401</b>	<b>4,799</b>	<b>10,583</b>	<b>11,323</b>	<b>13,300</b>

Source: Annual Reports 2003-2008

## 4. MLL's Performance

### Service Quality

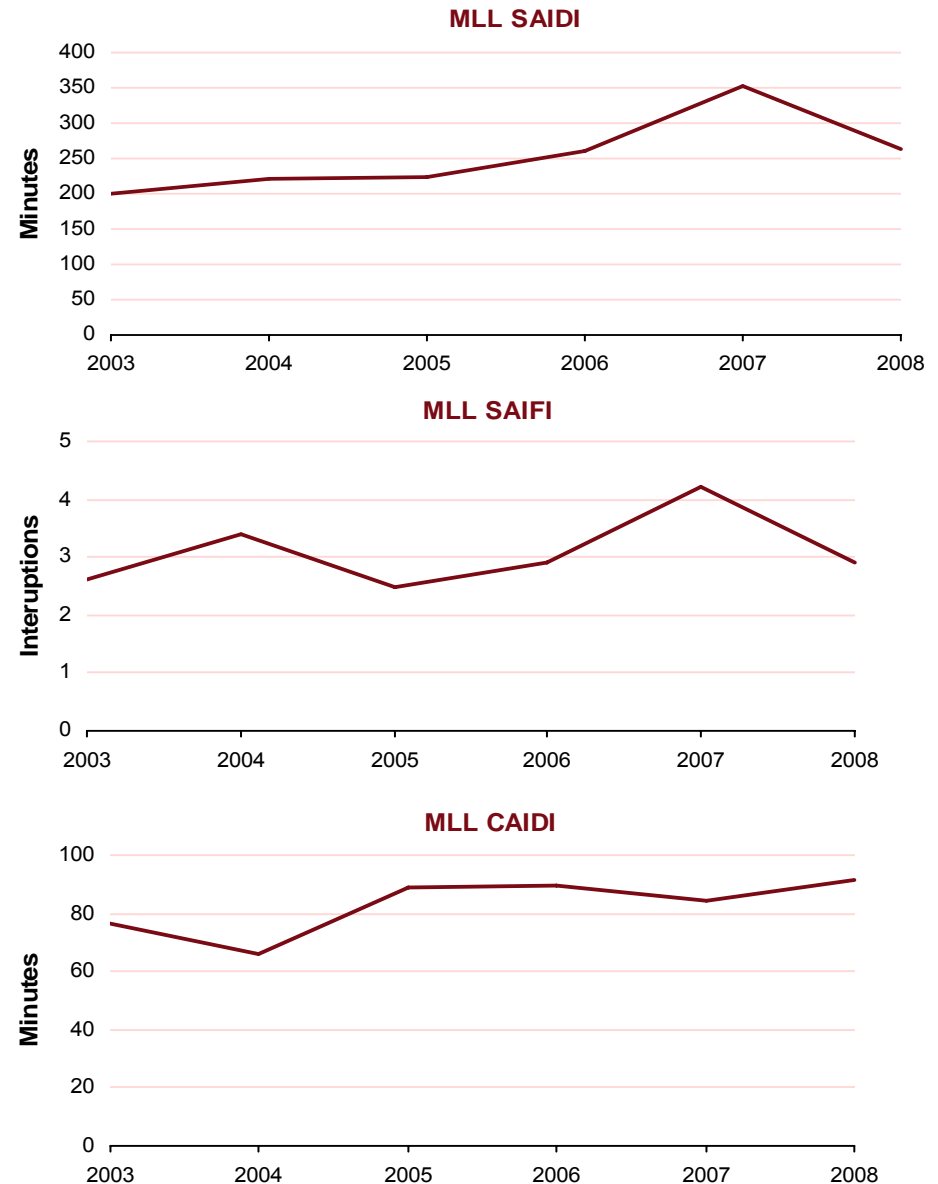
The provision of a high quality service by MLL is not only of interest to the Trust, which is charged with monitoring MLL's performance on behalf of its beneficiaries, but also to the Commerce Commission, which is concerned with the interests of consumers in general. In addition to the three standard industry measures of supply quality (SAIDI, SAIFI and CAIDI), MLL's Asset Management Plan and SCI outline other less-readily measurable service targets. These include:

- a reliable, efficient network;
- satisfied customers and stakeholders;
- a safe and healthy workplace;
- care of the environment;
- motivated and committed employees; and
- the timely provision of financial information to shareholders.

In addition, MLL has in place targets relating to improvements in reliability for its worst feeders, voltage quality and the servicing of all stakeholders. All of these targets are monitored and assessed to ensure MLL provides a high quality service throughout its network.

The table opposite displays MLL's system reliability performance over the past six years.

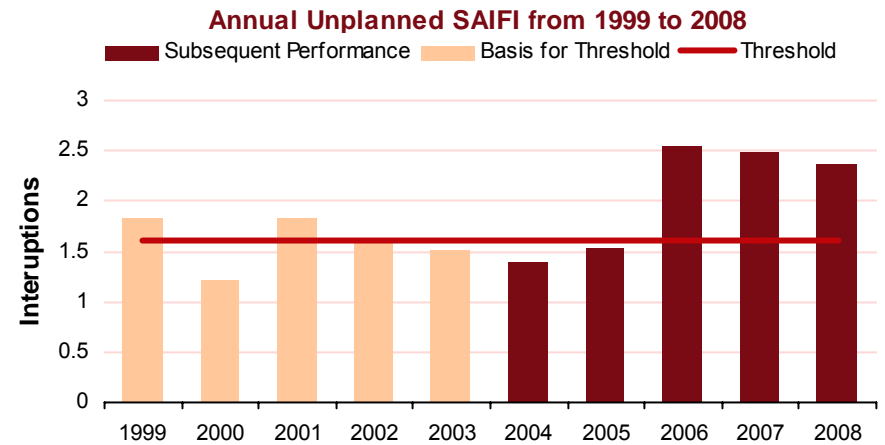
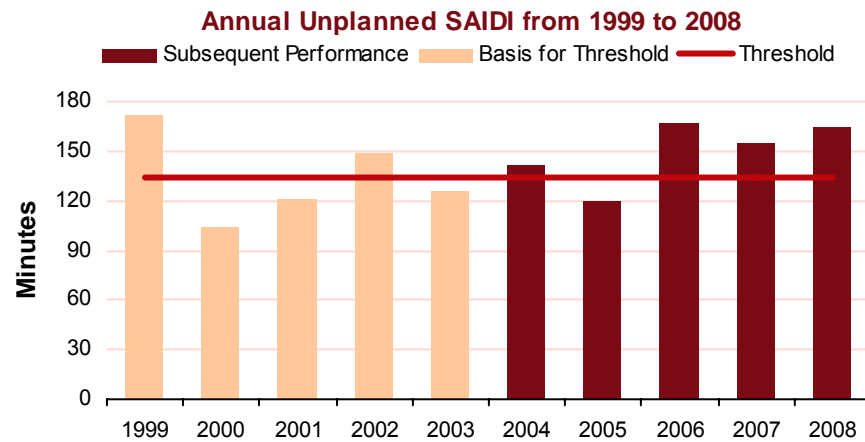
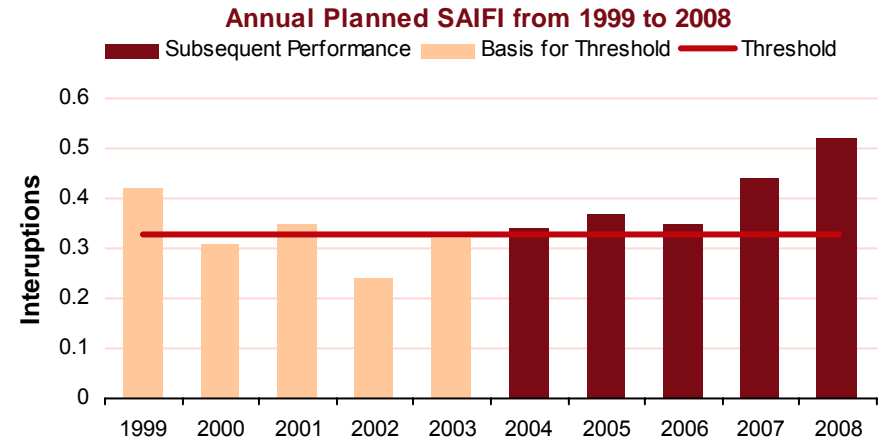
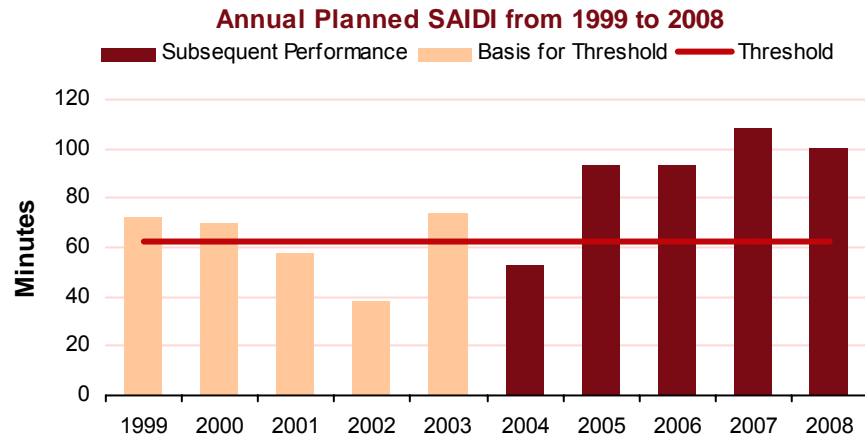
The charts set out overleaf display the performance of the Marlborough network in relation to the quality thresholds set by the Commerce Commission.



Source: MLL Annual Reports 2003 – 2008

## 4. MLL's Performance

### Service Quality



Source: PricewaterhouseCoopers ELB Compendium 1999-2007, MLL Annual Report 2008

## 4. MLL's Performance

### Service Quality

#### SAIDI

MLL has shown a deterioration in SAIDI (a measure of the annual duration of supply interruptions) over the 2003-2008 period. MLL has failed to achieve both its SCI and threshold SAIDI targets from 2006 to 2008. This has mainly been the result of planned outages associated with the significant capital expenditure programme undertaken by MLL over the period. The significant increase in planned outages reflects an increased number of new connections, capacity upgrades and asset replacements carried out during this period. In addition, 25% of the total SAIDI in 2007 was a result of Transpower outages. The rural and remote nature of some of the Company's lines has a significant impact on the Company's reliability. MLL has noted that if the rural figures were removed from the total SAIDI figures, SAIDI would reduce by 30% to 70% over the 2003-2008 period.

The breaches of the SAIDI thresholds are mainly attributed to the planned shutdowns. When compared to the historical five year average (from 1999-2003), planned shutdowns have increased by 59% between the 1999-2003 and 2005-2008 periods. Planned SAIFI also shows a similar pattern over 2003-2008.

Unplanned outages have also increased significantly with a 20% increase compared to the historical five year average for each year from 2005-2008. The increase in the faults was mainly due to adverse weather, incidents involving other parties working near lines or external forces, all of which were beyond the direct control of MLL.

#### SAIFI

SAIFI (the measure of the annual frequency of supply interruptions) has shown large variations over the last six years. This variation relates to both planned and unplanned outages in both urban and rural areas.

#### CAIDI

MLL's SAIDI and SAIFI results have resulted in mixed CAIDI results. CAIDI is the average annual duration of an interruption that a customer experiences.

## 4. MLL's Performance

### Service Quality

#### Customer Communication

Since 2004, MLL has been required to:

- Properly advise consumers about the price-quality trade offs available to them in relation to the goods and services provided by the lines business; and
- Consult with consumers about the quality of the goods and services that they require, with reference to the prices of those goods and services.

MLL has complied with these requirements since they were introduced in 2004.

Overall, across all of MLL customer groups there is a very high level of satisfaction with the quality and reliability of the electricity supply service which MLL is currently delivering. Generally, MLL consumers are aware of the price – quality trade offs that are available to them and they are not willing to pay more for a more reliable electricity supply or accept a lower level of supply reliability.

MLL has also provided free energy efficiency and electrical advisory services to customers to ensure everyone connected to the network is fully informed through the Company's website, media releases and a quarterly newsletter. A recent independent survey in 2007 shows that 90.5% of the total sample of commercial and residential customers are either satisfied or very satisfied with the Company's overall performance.

## 4. MLL's Performance

### Lines Business Industry Performance Benchmarking

Whilst the standard measures used previously allow for a substantial analysis of MLL's performance, the consideration of these measures in isolation from other EDBs ignores the influences that affect the performance of the electricity distribution sector as a whole. By comparing MLL's lines business performance with its peers, impacts on performance relating to industry-wide issues such as increasing costs, regulation and other external influences outside of MLL's control can be contrasted and the relative underlying performance of the network illustrated.

The most recent comparative industry-wide information available is from the 31 March 2007 EDB disclosures. This data and its 2006 equivalent are used for the purposes of this analysis and is summarised within the charts in this section.

It should be noted that care must be taken when comparing EDBs as all line networks have different attributes which influence the various metrics examined. Topography, climate, growth rates, historical design practices, network configuration and customer density are all factors that affect these measures and as such this analysis only provides a high level indication of performance.

## 4. MLL's Performance

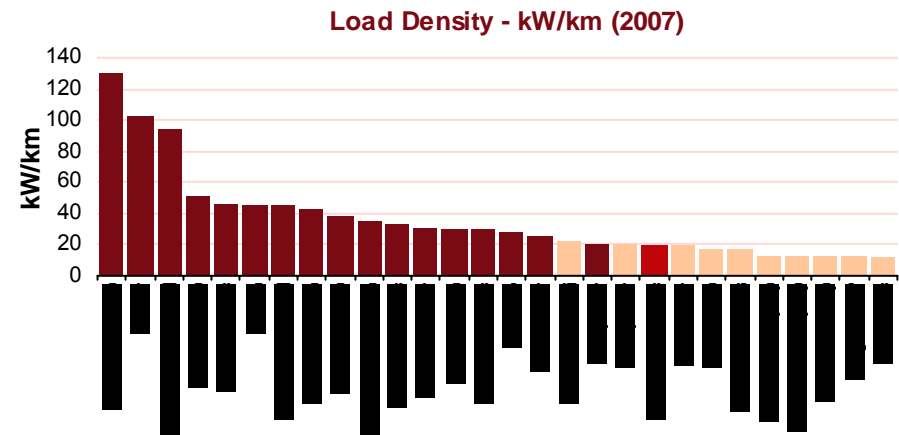
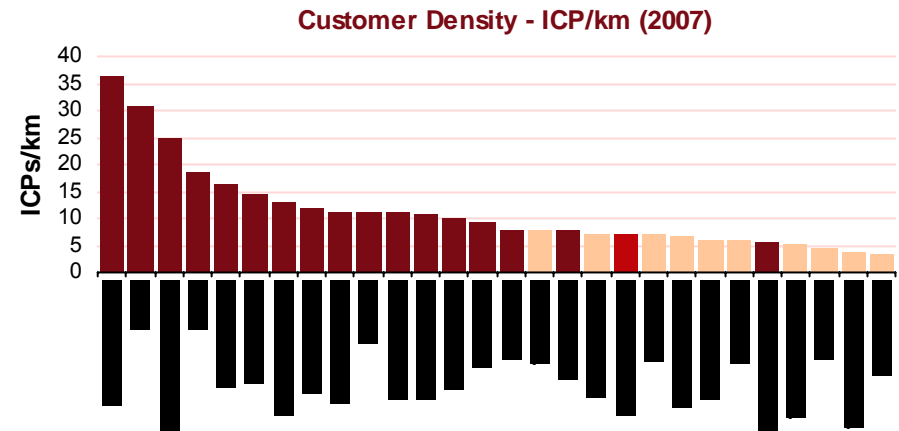
### Line Business Industry Performance Benchmarking

The group of EDBs used in this comparison were selected on the basis of both load and customer density. The following 10 EDBs, which are ranked the lowest in relation to customer density and load density (ie. a range of 3 to 8 ICPs per circuit kilometre and a range of 11 to 21 kW per circuit kilometre) are used in the comparative analysis.

- Buller Electricity
- Centralines
- Eastland Network
- MainPower
- Network Waitaki
- OtagoNet Joint Venture
- The Lines Company
- The Power Company
- Top Energy
- Westpower

These 10 low density EDBs are rural networks, servicing provincial centres and large rural areas without large dominant load customers. Although Alpine Energy, Electricity Ashburton and Scanpower fall within the selected range, we have excluded them from the peer group because their networks are fundamentally different to the rest of the group. Alpine Energy's load is dominated by large customers. Electricity Ashburton is dominated by high demand irrigation load. Scanpower has a very simple network with no sub transmission network and its highest voltage is 11kV.

Peer group rankings for the following analysis can be found in Appendix 3.



Source: PricewaterhouseCoopers ELB Compendium 2007

## 4. MLL's Performance

### Line Business Industry Performance Benchmarking

#### System Reliability

The key service performance indicator for a distribution network is the level of reliability, measured by interruption duration (SAIDI) and interruption frequency (SAIFI). Any consideration of reliability should ideally be undertaken over the medium to long term, as investment or under investment in reliability improvements take time to appear in reliability statistics.

In 2006 and 2007 MLL's SAIDI exceeded the medians of the peer group. SAIFI in both years was close to the medians of the peer group. As is shown in the tables opposite, both planned and unplanned outages contribute to these rankings, but MLL experiences significantly more planned outages than the group.

Further comparative analysis can be found in Appendix 3.

	Total System Interruption Duration				Total System Interruption Frequency			
	2006		2007		2006		2007	
	SAIDI	Rank	SAIDI	Rank	SAIFI	Rank	SAIFI	Rank
MLL	260	7	264	7	2.8	7	2.9	4
Group Median	175	-	237	-	2.7	-	3.1	-

*Rank 1= lowest interruptions, 11= highest interruptions*

	Planned and Unplanned System Interruption Duration							
	2006 SAIDI				2007 SAIDI			
	Planned	Rank	Unplanned	Rank	Planned	Rank	Unplanned	Rank
MLL	94	8	167	8	109	8	155	5
Group Median	45	-	116	-	42	-	181	-

*Rank 1= lowest interruptions, 11= highest interruptions*

	Planned and Unplanned System Interruption Frequency							
	2006 SAIFI				2007 SAIFI			
	Planned	Rank	Unplanned	Rank	Planned	Rank	Unplanned	Rank
MLL	0.4	8	2.6	7	0.4	9	2.5	5
Group Median	0.2	-	2.2	-	0.2	-	2.7	-

*Rank 1= lowest interruptions, 11= highest interruptions*

Source: PricewaterhouseCoopers ELB Compendium 2006-2007

## 4. MLL's Performance

### Line Business Industry Performance Benchmarking

#### Revenue

The ability of an EDB to produce revenue via its distribution business is a key driver in being able to generate the economic profit that allows for network renewal, debt servicing, expansion and distributions to be made to owners. Revenues generated for distribution services have been estimated by subtracting transmission charges, discounts, interest revenue and gains from the sale of assets from line charges, access charges and other income.

Revenues are presented as average revenue per unit of electricity delivered and average revenue per unit of installed capacity. These best reflect the demands consumers place on the electricity distribution function, although it is recognised that reliability is an important customer requirement as well.

MLL's average distribution revenue per unit delivered for both 2006 and 2007 were near the top of its peer group. This is largely attributable to MLL's significant line charge increases in 2006 and in prior years. Average unit revenue dropped slightly from 2006 to 2007. This reflected MLL's agreement with the Commerce Commission to forgo price increases in 2007. The faster growth in transformer capacity in 2007 (i.e. 6% compared to the average of peer group of 2%) has resulted in revenue per installed capacity which falls slightly below the group median in 2007.

	Distribution Revenue per Unit				Distribution Revenue per				Direct and Indirect Costs per			
	2006		2007		2006		2007		2006		2007	
	c/kWh	Rank	c/kWh	Rank	\$/kVA	Rank	\$/kVA	Rank	\$/ICP	Rank	\$/ICP	Rank
MLL	6.8	2	6.7	3	88.6	4	82.4	7	316	9	348	9
Group Median	5.5	-	5.7	-	85.3	-	84.4	-	212	-	255	-

Rank 1= highest revenue, 11= lowest revenue

Source: PricewaterhouseCoopers ELB Compendium 2006-2007

We note that the growth experienced within the Marlborough network over the last five years has led to significant revenue being generated from capital contributions. As can be seen from the information set out in the table below, this has ranged between 0.7 cents/kWh in 2004 to 1.9 cents/kWh in 2008, a significant contributor to MLL's high revenue ranking. Unfortunately due to the inconsistent capital contribution practices of other EDBs within the peer group a comparison of the impact of capital contributions on revenue cannot be made.

MLL's performance in the two key measures that consumers are primarily concerned with, system reliability and price, is broadly in line with its peer group, with slightly poorer quality performance and slightly higher unit revenues than the group average.

MLL Parent	2003	2004	2005	2006	2007	2008
Year ended 31 March						
Capital Contributions (\$000)	280	2,140	2,411	3,925	3,121	6,924
Change		664%	13%	63%	-20%	122%
Capital Contributions cents/kWh	0.086	0.657	0.703	1.121	0.873	1.857
Change		660%	7%	59%	-22%	113%

Source: MLL Annual Reports 2003-2008

## 4. MLL's Performance

### Line Business Industry Performance Benchmarking

#### Operating Expenditure

There is no single indicator which provides a definitive comparison of costs across networks, even once networks of similar load and connection densities are grouped together. The three key outputs for distribution networks are capacity (measured in installed capacity or kVA), connectivity (measured in circuit kilometres) and connections (measured in numbers of ICPs). By considering the overall picture provided by these three indicators, we can make a high level assessment of the performance of a network when compared to its peers.

	Distribution Revenue per Unit Delivered		Distribution Revenue per Installed Capacity				Direct and Indirect Costs per Connection					
	2006	2007	2006	2007	2006	2007	2006	2007	2006	2007		
	c/kWh	Rank	c/kWh	Rank	\$/kVA	Rank	\$/kVA	Rank	\$/ICP	Rank	\$/ICP	Rank
MLL	6.8	2	6.7	3	88.6	4	82.4	7	316	9	348	9
Group Median	5.5	-	5.7	-	85.3	-	84.4	-	212	-	255	-

Rank 1= highest revenue, 11= lowest revenue

Source: PricewaterhouseCoopers ELB Compendium 2006-2007

Overall, MLL's unit operating costs were consistently higher than the group median for both years. Costs per circuit kilometre were near the top of its peer group, being the second highest in 2006 and the third highest in 2007. When costs are expressed on a per capacity and per connection basis the results show similar patterns.

MLL's high operating expenditure are driven by growing staff numbers, rising labour and material costs, and significantly increased regulatory compliance costs. The extensive nature of MLL's rugged and rural networks imposes unique demands in terms of maintaining high levels

of network reliability. These are reflected in the relatively high cost levels across the peer group.

#### Financial Returns

Comparing returns between peer group EDBs using standard financial return measures allows an evaluation of the respective earning performance of MLL within the peer group. As noted previously, capital contribution provide a meaningful part of MLL total network revenue, but due to the disclosure of other peer group EDBs, return ratios have only been calculated inclusive of capital contributions.

All of MLL's returns measures for 2006 exceeded the group median, partly as a result of price increases for that year. As shown in the table below, the financial return measures rank MLL at 5 for Return on Investment (4.6%) and Return on Funds (5.9%), and at 4 for Return on Equity (4.9%). The Adjusted Return on Investment (ROI) is calculated by adding back any distributions and rebates made to consumers (net of the corporate tax effect). MLL's adjusted ROI is ranked at 3 in 2006.

	ROI		ROI Adjusted		ROE		ROF									
	2006	2007	2006	2007	2006	2007	2006	2007								
	%	Rank	%	Rank	%	Rank	%	Rank								
MLL	4.6	5	2.8	7	7.1	3	5.2	7	4.9	4	3.1	8	5.9	5	4.2	7
Group Median	4.0	-	3.9	-	5.2	-	6.0	-	3.9	-	5.9	-	5.3	-	6.4	-

Rank 1= highest return, 11= lowest return

Source: PricewaterhouseCoopers ELB Compendium 2006-2007

MLL's returns for the 2007 year have reduced as a result of the 2007 price freeze and rising operating costs. Peer group EDBs show increasing returns in 2007.

## 4. MLL's Performance

### Line Business Industry Performance Benchmarking

#### Conclusion

Overall MLL has enjoyed strong revenue growth in recent years but this has been offset by relatively high costs compared to its peer group. In 2006, MLL's average unit revenues were higher than the median of the peer group following price increases and significant capital contributions in that year. Although MLL did not increase prices in 2007, its average unit revenue per kWh remains well above the group median.

In relation to comparable EDBs, MLL displays slightly poorer system reliability in 2006 and 2007, falling within the third quartile amongst its peers. MLL's average own network SAIDI (including planned and unplanned outages) over the 2003-2008 period is 232 minutes, compared with a peer group median of 215 minutes.

One explanation for these quality of supply results is the increase in planned outages or maintenance driven outages resulting from network improvement and expansion activities undertaken during the period. Unplanned outages are mainly due to adverse weather.

As emphasised earlier in this report, care must be taken when comparing EDBs as all line networks have different attributes which influence the metrics examined.

# Appendix 1

## Restrictions

## Restrictions

This report (or extracts from it) can be made available to MEPT and for public inspection in accordance with the requirements of the Marlborough Electric Power Trust Deed. Apart from this noted exception, our report is not intended for general circulation, distribution or publication nor is it to be reproduced or used for any purpose without our written permission in each specific instance. We do not assume any responsibility or liability for losses suffered by MLL, or any unauthorised user as a result of the circulation, publication, reproduction or use of this report contrary to the provisions of this restrictions section.

We have relied on financial information provided to us by MLL. We have not had the opportunity to assess the financial information in detail. We have no reason to believe that the information provided to us is inaccurate or misleading. However, we have not endeavoured to seek any independent confirmation of its reliability, accuracy or completeness. In particular, we do not imply, and it should not be construed, that we have conducted an audit or verified the information provided as the basis for our report. We accept no responsibility or liability for any losses suffered by MLL, MEPT, or by any other parties as a result of our reliance on the aforementioned financial information or material on which our views are based.

We reserve the right (but will be under no obligation) to review and amend all calculations and opinions included or referred to in this report and, if we consider it necessary, to review our report in the light of any information existing at the date of this report which subsequently becomes known to us.

# Appendix 2

## MLL's Performance against SCI Targets

## MLL's Performance against SCI Targets

MLL SCI Performance	2003			2004			2005			2006			2007			2008			2009
	Actual	Target	Achieved	Actual	Target	Achieved	Actual	Target	Achieved	Actual	Target	Achieved	Actual	Target	Achieved	Actual	Target	Achieved	Target
<b>Financial Measures</b>																			
Operating turnover (\$m)	22.5	20.8	√	26.3	23.8	√	29.3	28.0	√	36.5	30.4	√	35.2	37.6	x	44.1	39.2	√	51.7
Operating surplus after tax(\$m)	1.6	0.9	√	3.1	2.5	√	3.5	4.5	x	7.2	6.0	√	4.3	5.9	x	10.5	6.7	√	7.5
EBIT/average net funds employed	4.5%	1.3%	√	4.1%	5.7%	x	3.6%	4.1%	x	6.0%	5.8%	√	3.6%	5.7%	x	5.7%	4.9%	√	4.3%
NPAT/shareholders funds	2.5%	1.1%	√	2.7%	5.4%	x	2.1%	2.8%	x	4.2%	3.6%	√	2.1%	3.4%	x	4.7%	3.1%	√	3.3%
Adjusted NPAT/shareholders funds*	3.5%	4.9%	x	3.6%	5.9%	x	4.0%	1.9%	√	5.8%	4.3%	√	3.6%	5.3%	x	7.5%	4.5%	√	
Shareholders equity (\$m)	66.8	65.5	√	160.2	70.6	√	165.5	164.5	√	171.9	171.3	√	176.0	177.7	x	223.0	213.5	√	231.4
Net asset backing per share(\$)	2.4	2.3	√	5.7	2.5	√	5.9	5.9	√	6.1	6.1	√	7.4	6.4	√	8.0	7.6	√	8.3
Shareholder funds/ total assets	73.0%	97.3%	x	85.4%	74.1%	√	85.5%	88.9%	x	85.8%	85.5%	√	86.8%	85.8%	√	73.3%	72.6%	√	
Return on equity after tax from NEL																7.7%	10.0%	x	
Return on equity after tax from OJV																8.5%	10.0%	x	
<b>Expenditure</b>																			
Netw ork business maintenance and operations expenditure per customer (\$)	124.8	160.8	√	167.1	157.5	x	172.1	145.7	x	205.7	158.7	x	220.4	225.2	√	238.5	238.0	x	262.6
Capital expenditure (\$m)	4.3	6.4	√	6.4	4.9	x	4.8	5.5	√	10.6	11.4	√	11.3	12.1	√	13.3	14.3	√	14.4
<b>Dividends/Discounts</b>																			
Dividends received from NEL (\$m)	0.9	0.0		1.0	0.0		1.1	1.1	√	1.9	1.9	√	1.1	1.0	√	0.9	1.0	x	0.9
Discounts paid to Marlborough Lines customers (\$m)	4.0	5.0	x	4.0	4.0	√	4.1	4.1	√	4.2	4.2	x	4.3	4.3	√	4.5	4.5	x	5.8
Dividends paid to MEPT (\$m)	0.3	0.2	√	0.2	0.2	x	0.2	0.2	√	0.3	0.2	√	0.3	0.2	√	0.3	0.3	√	
<b>Network Performance</b>																			
Energy supplied to the Marlborough Netw ork (GWh)	324.0	318.0	√	326.0	334.0	x	343.0	340.0	√	350.0	353.0	x	357.0	359.0	x	373.0	368.0	√	380.0
<b>SAIDI</b>																			
SAIDI Planned	74.1	81.0	√	52.5	57.3	√	93.4	59.1	x	93.6	64.4	x	108.7	66.6	x	100.2	107.5	√	
SAIDI Unplanned	125.7	126.3	√	141.2	117.3	x	119.8	115.5	x	166.5	113.2	x	155.2	117.0	x	163.0	153.5	x	
Total SAIDI	200.0	168.0	x	222.0	156.0	x	225.0	156.0	x	260.0	156.0	x	353.0	156.0	x	264.0	156.0	x	210.0
<b>SAIFI</b>																			
SAIFI Planned	0.3	0.452	√	0.3	0.3	√	0.4	0.3	x	0.3	0.3	√	0.4	0.3	x		0.4		
SAIFI Unplanned	1.5	2.535	√	1.4	1.6	√	1.5	1.5	√	2.5	1.5	x	2.5	1.6	x		2.5		
<b>CAIDI</b>																			
CAIDI Planned	232.6	179.4	x	156	174.4	√	254.3	170.9	x	268.7	187.3	x	245.5	196.7	x		245.5		
CAIDI Unplanned	83.1	49.84	x	101.3	73.1	x	78.8	77	x	65.4	74.9	√	62.3	73.3	√		62.3		
Faults per 100 km line	6.1	11.0	√	8.8	10.0	√	9.3	10.0	√	11.6	10.0	x	14	10.0	x	13.8	10.0	x	10.0

Source: 2003-2008 Annual Reports

\* After adding back discounts and using DRC to establish the value of net assets.

# Appendix 3

## Comparative Performance

## Comparative Performance

### Peer Group Density Characteristics

Customer Density 2007		Load Density 2007			
Rank	(ICP/km)	Rank	(kW/km)		
1	OtagoNet Joint Venture	3.4	1	Centralines	11.1
2	The Power Company	3.8	2	OtagoNet Joint Venture	12.4
3	Centralines	4.6	3	Buller Electricity	13.0
4	The Lines Company	5.3	4	The Power Company	13.3
5	Westpower	5.8	5	The Lines Company	13.3
6	Network Waitaki	6.0	6	Eastland Network	16.2
7	Eastland Network	6.8	7	Top Energy	16.9
8	MainPower New Zealand	7.1	8	MainPower New Zealand	18.9
9	Marlborough Lines	7.1	9	Marlborough Lines	19.4
10	Buller Electricity	7.2	10	Westpower	20.2
11	Top Energy	7.7	11	Network Waitaki	21.2
Industry Average		11.3	Industry Average		35.8
Industry Median		8.4	Industry Median		28.5
<b>Group (excluding MLL)</b>			<b>Group (excluding MLL)</b>		
	First Quartile	4.7		First Quartile	13.1
	Median	5.9		Median	14.8
	Third Quartile	7.0		Third Quartile	18.4

Note: All data presented in Appendix 3 is sourced from the 2006 and 2007 Gazetted Information Disclosures.

## Comparative Performance

### Peer Group System Reliability

2006 SAIDI Network Planned and Unplanned		2007 SAIDI Network Planned and Unplanned		2006 SAIFI Network Planned and Unplanned		2007 SAIFI Network Planned and Unplanned				
Rank		Rank		Rank		Rank				
1	Network Waitaki	97		1	Buller Electricity	1.2		1	Buller Electricity	1.3
2	MainPower New Zealand	103		2	Westpower	1.7		2	Network Waitaki	1.5
3	Centralines	141		3	The Power Company	1.8		3	MainPower New Zealand	1.8
4	Westpower	146		4	Centralines	1.8		4	Marlborough Lines	2.9
5	The Power Company	158		5	MainPower New Zealand	2.1		5	Westpower	3.0
6	Buller Electricity	192		6	Eastland Network	2.6		6	The Power Company	3.0
7	Marlborough Lines	260		7	Marlborough Lines	2.8		7	Centralines	3.2
8	The Lines Company	278		8	Network Waitaki	3.0		8	The Lines Company	3.3
9	OtagoNet Joint Venture	307		9	The Lines Company	3.8		9	OtagoNet Joint Venture	3.5
10	Eastland Network	349		10	Top Energy	4.17		10	Eastland Network	3.9
11	Top Energy	522		11	OtagoNet Joint Venture	4.70		11	Top Energy	5.5
	Industry Average	153			Industry Average	2.72			Industry Average	2.3
	Industry Median	128			Industry Median	1.64			Industry Median	2.0
<b>Group (excluding MLL)</b>				<b>Group (excluding MLL)</b>				<b>Group (excluding MLL)</b>		
	First Quartile	142			First Quartile	1.80			First Quartile	2.1
	Median	175			Median	2.37			Median	3.1
	Third Quartile	300			Third Quartile	3.41			Third Quartile	3.5

## Comparative Performance

### Peer Group System Reliability

Rank	Planned SAIDI 2006	Rank	Unplanned SAIDI 2006	Rank	Planned SAIDI 2007	Rank	Unplanned SAIDI 2007
1	The Power Company 15	1	Network Waitaki 47	1	Top Energy 18	1	Buller Electricity 53
2	Top Energy 22	2	Westpower 69	2	Eastland Network 19	2	Westpower 110
3	Eastland Network 28	3	MainPower New Zealand 70	3	MainPower New Zealand 32	3	The Power Company 135
4	MainPower New Zealand 33	4	Buller Electricity 84	4	Centralines 39	4	Centralines 148
5	Centralines 41	5	Centralines 100	5	Network Waitaki 41	5	Marlborough Lines 155
6	Network Waitaki 50	6	OtagoNet Joint Venture 133	6	The Power Company 42	6	OtagoNet Joint Venture 177
7	Westpower 76	7	The Power Company 144	7	Westpower 56	7	MainPower New Zealand 185
8	Marlborough Lines 94	8	Marlborough Lines 167	8	Marlborough Lines 109	8	The Lines Company 233
9	The Lines Company 98	9	The Lines Company 180	9	Buller Electricity 109	9	Eastland Network 238
10	Buller Electricity 108	10	Eastland Network 322	10	The Lines Company 110	10	Network Waitaki 291
11	OtagoNet Joint Venture 174	11	Top Energy 500	11	OtagoNet Joint Venture 293	11	Top Energy 399
	Industry Average 37		Industry Average 115		Industry Average 50		Industry Average 222
	Industry Median 26		Industry Median 89		Industry Median 32		Industry Median 134
<b>Group (excluding MLL)</b>		<b>Group (excluding MLL)</b>		<b>Group (excluding MLL)</b>		<b>Group (excluding MLL)</b>	
	First Quartile 29		First Quartile 73		First Quartile 33		First Quartile 138
	Median 45		Median 116		Median 42		Median 181
	Third Quartile 92		Third Quartile 171		Third Quartile 96		Third Quartile 236

## Comparative Performance

### Peer Group System Reliability

Rank	Planned SAIFI 2006	Rank	Unplanned SAIFI 2006	Rank	Planned SAIFI 2007	Rank	Unplanned SAIFI 2007
1	The Power Company 0.1	1	Network Waitaki 0.9	1	Top Energy 0.1	1	Buller Electricity 0.9
2	Top Energy 0.1	2	Buller Electricity 1.2	2	Centralines 0.1	2	Network Waitaki 1.3
3	Centralines 0.1	3	Westpower 1.5	3	Eastland Network 0.2	3	MainPower New Zealand 1.5
4	Eastland Network 0.2	4	MainPower New Zealand 1.5	4	Network Waitaki 0.2	4	OtagoNet Joint Venture 2.2
5	MainPower New Zealand 0.2	5	OtagoNet Joint Venture 2.0	5	MainPower New Zealand 0.2	5	Marlborough Lines 2.5
6	Westpower 0.3	6	Eastland Network 2.5	6	The Power Company 0.2	6	Westpower 2.6
7	Network Waitaki 0.3	7	Marlborough Lines 2.6	7	Westpower 0.3	7	The Lines Company 2.7
8	Marlborough Lines 0.4	8	The Power Company 2.9	8	Buller Electricity 0.4	8	The Power Company 2.8
9	The Lines Company 0.6	9	The Lines Company 3.2	9	Marlborough Lines 0.4	9	Centralines 3.0
10	Buller Electricity 0.6	10	Centralines 4.8	10	The Lines Company 0.6	10	Eastland Network 3.8
11	OtagoNet Joint Venture 0.8	11	Top Energy 5.4	11	OtagoNet Joint Venture 1.3	11	Top Energy 5.4
	Industry Average 0.2		Industry Average 1.9		Industry Average 0.2		Industry Average 2.0
	Industry Median 0.1		Industry Median 1.5		Industry Median 0.2		Industry Median 1.9
	<b>Group (excluding MLL)</b>		<b>Group (excluding MLL)</b>		<b>Group (excluding MLL)</b>		<b>Group (excluding MLL)</b>
	First Quartile 0.1		First Quartile 1.5		First Quartile 0.2		First Quartile 1.7
	Median 0.2		Median 2.2		Median 0.2		Median 2.7
	Third Quartile 0.5		Third Quartile 3.1		Third Quartile 0.4		Third Quartile 3.0

# Comparative Performance

## Peer Group System Reliability

	Planned SAIDI (minutes)					Unplanned SAIDI (minutes)				
	Actual 2006	Actual 2007	SAIDI Average 1999-2003	2006	2007	Actual 2006	Actual 2007	SAIDI Average 1999-2003	2006	2007
				Change over Average	Change over Average				Change over Average	Change over Average
Buller Electricity	108	109	179	-40%	-39%	84	53	164	-49%	-68%
Centralines	41	39	95	-57%	-59%	100	148	218	-54%	-32%
Eastland Network	28	19	74	-63%	-75%	322	238	293	10%	-19%
MainPower New Zealand	33	32	68	-51%	-53%	70	185	79	-12%	134%
Marlborough Lines	94	109	62	50%	74%	167	155	134	24%	16%
Network Waitaki	50	41	19	161%	117%	47	291	51	-8%	469%
OtagoNet Joint Venture	174	293	89	95%	228%	133	177	160	-17%	11%
The Lines Company	98	110	215	-55%	-49%	180	233	322	-44%	-28%
The Power Company	15	42	38	-61%	12%	144	135	202	-29%	-33%
Top Energy	22	18	103	-78%	-82%	500	399	353	42%	13%
Westpower	76	56	73	4%	-24%	69	110	96	-28%	15%

	Planned SAIFI (interruptions)					Unplanned SAIFI (interruptions)				
	Actual 2006	Actual 2007	SAIFI Average 1999-2003	2006	2007	Actual 2006	Actual 2007	SAIFI Average 1999-2003	2006	2007
				Change over Average	Change over Average				Change over Average	Change over Average
Buller Electricity	0.6	0.4	0.7	-13%	-41%	1.2	0.9	1.7	-32%	-50%
Centralines	0.1	0.1	0.5	-72%	-76%	4.8	3.0	5.3	-11%	-43%
Eastland Network	0.2	0.2	0.6	-75%	-75%	2.5	3.8	3.0	-19%	25%
MainPower New Zealand	0.2	0.2	0.3	-45%	-20%	1.5	1.5	1.4	7%	8%
Marlborough Lines	0.4	0.4	0.3	7%	34%	2.6	2.5	1.6	59%	55%
Network Waitaki	0.3	0.2	0.1	168%	75%	0.9	1.3	1.0	-7%	28%
OtagoNet Joint Venture	0.8	1.3	0.5	46%	152%	2.0	2.2	1.9	7%	19%
The Lines Company	0.6	0.6	1.1	-44%	-47%	3.2	2.7	5.3	-40%	-48%
The Power Company	0.1	0.2	0.3	-73%	-23%	2.9	2.8	4.0	-28%	-30%
Top Energy	0.1	0.1	0.8	-87%	-87%	5.4	5.4	5.9	-8%	-8%
Westpower	0.3	0.3	0.4	-20%	-6%	1.5	2.6	1.3	18%	108%

Source: PricewaterhouseCoopers ELB Compendium 1999-2007

## Comparative Performance

### Peer Group Distribution Revenue

Rank	Total Distribution Revenue 2006 (c/kWh)	Rank	Total Distribution Revenue 2007 (c/kWh)	Rank	Total Distribution Revenue 2006 (\$/kVA)	Rank	Total Distribution Revenue 2007 (\$/kVA)
1	Buller Electricity 9.3	1	Buller Electricity 10.5	1	Buller Electricity 129.2	1	Westpower 156.4
2	Marlborough Lines 6.8	2	Westpower 9.9	2	Westpower 92.6	2	Buller Electricity 149.9
3	Eastland Network 6.2	3	Marlborough Lines 6.7	3	OtagoNet Joint Venture 90.8	3	Top Energy 104.3
4	The Lines Company 5.7	4	Centralines 6.1	4	Marlborough Lines 88.6	4	OtagoNet Joint Venture 103.4
5	Top Energy 5.6	5	Eastland Network 6.1	5	Top Energy 88.3	5	Eastland Network 85.7
6	Westpower 5.6	6	Top Energy 5.8	6	Eastland Network 88.2	6	The Power Company 83.2
7	MainPower New Zealand 5.5	7	The Lines Company 5.6	7	The Lines Company 82.3	7	Marlborough Lines 82.4
8	Centralines 5.4	8	MainPower New Zealand 5.4	8	The Power Company 72.3	8	Centralines 76.6
9	Network Waitaki 4.0	9	The Power Company 4.4	9	Centralines 71.8	9	The Lines Company 76.3
10	The Power Company 3.9	10	OtagoNet Joint Venture 4.3	10	MainPower New Zealand 70.8	10	MainPower New Zealand 69.6
11	OtagoNet Joint Venture 3.8	11	Network Waitaki 4.1	11	Network Waitaki 52.8	11	Network Waitaki 56.2
	Industry Average 4.7		Industry Average 5.0		Industry Average 77.6		Industry Average 82.5
	Industry Median 4.3		Industry Median 4.5		Industry Median 72.3		Industry Median 74.3
<b>Group (excluding MLL)</b>		<b>Group (excluding MLL)</b>		<b>Group (excluding MLL)</b>		<b>Group (excluding MLL)</b>	
	First Quartile 4.4		First Quartile 4.6		First Quartile 71.9		First Quartile 76.4
	Median 5.5		Median 5.7		Median 85.3		Median 84.4
	Third Quartile 5.7		Third Quartile 6.1		Third Quartile 90.2		Third Quartile 104.1

**Note:** Total Distribution Revenue is defined as:  
 Total income from line and access charges;  
 plus Total other income;  
 less Transmission charges;  
 less Interest revenue;  
 less Gain on sale of assets.

This provides our best estimate, from the data available, of line and access charges and capital contribution income for all EDBs in a consistent manner. It also by definition includes minor sources of other income, such as rent, but this is not believed to be material for any of the EDBs considered. It is not possible to examine income from line and access charges separately from income from capital contributions because some EDBs currently bundle these sources of income together in their disclosure information.

## Comparative Performance

### Peer Group Operating Expenditure

Rank	Direct & Indirect Line Costs 2006 (\$/kVA)	Rank	Direct & Indirect Line Costs 2007 (\$/kVA)	Rank	Direct & Indirect Line Costs 2006 (\$/km)	Rank	Direct & Indirect Line Costs 2007 (\$/km)
1	MainPower New Zealand 16.1	1	Network Waitaki 18.4	1	OtagoNet Joint Venture 742	1	OtagoNet Joint Venture 951
2	Network Waitaki 16.6	2	MainPower New Zealand 19.7	2	Centralines 927	2	Centralines 1,070
3	Centralines 19.3	3	Centralines 22.0	3	The Power Company 941	3	The Power Company 1,091
4	Eastland Network 21.4	4	The Lines Company 22.1	4	The Lines Company 1,099	4	The Lines Company 1,146
5	OtagoNet Joint Venture 22.4	5	Eastland Network 24.6	5	Eastland Network 1,171	5	Network Waitaki 1,350
6	The Lines Company 23.7	6	The Power Company 27.4	6	Network Waitaki 1,203	6	Eastland Network 1,397
7	The Power Company 23.9	7	OtagoNet Joint Venture 28.5	7	MainPower New Zealand 1,299	7	MainPower New Zealand 1,589
8	Marlborough Lines 28.3	8	Marlborough Lines 29.7	8	Top Energy 2,050	8	Top Energy 2,107
9	Westpower 35.9	9	Westpower 39.7	9	Westpower 2,253	9	Marlborough Lines 2,465
10	Top Energy 39.9	10	Top Energy 42.9	10	Marlborough Lines 2,256	10	Westpower 2,591
11	Buller Electricity 65.2	11	Buller Electricity 65.5	11	Buller Electricity 3,240	11	Buller Electricity 3,296
	Industry Average 22.7		Industry Average 25.0		Industry Average 2,102		Industry Average 2,392
	Industry Median 20.6		Industry Median 22.0		Industry Median 2,013		Industry Median 2,094
<b>Group (excluding MLL)</b>		<b>Group (excluding MLL)</b>		<b>Group (excluding MLL)</b>		<b>Group (excluding MLL)</b>	
	First Quartile 19.8		First Quartile 22.0		First Quartile 980		First Quartile 1,104
	Median 23.1		Median 26.0		Median 1,187		Median 1,373
	Third Quartile 32.9		Third Quartile 36.9		Third Quartile 1,862		Third Quartile 1,978

## Comparative Performance

### Peer Group Operating Expenditure, continued

Rank	Direct & Indirect Line Costs 2006 (\$/ICP)	Rank	Direct & Indirect Line Costs 2007 (\$/ICP)		
1	Eastland Network	173	1	Eastland Network	204
2	The Lines Company	185	2	The Lines Company	215
3	MainPower New Zealand	187	3	MainPower New Zealand	225
4	Network Waitaki	200	4	Network Waitaki	227
5	Centralines	201	5	Centralines	235
6	OtagoNet Joint Venture	222	6	Top Energy	275
7	The Power Company	249	7	OtagoNet Joint Venture	284
8	Top Energy	287	8	The Power Company	286
9	Marlborough Lines	316	9	Marlborough Lines	348
10	Westpower	379	10	Westpower	443
11	Buller Electricity	451	11	Buller Electricity	457
	Industry Average	207		Industry Average	236
	Industry Median	188		Industry Median	210
<b>Group (excluding MLL)</b>			<b>Group (excluding MLL)</b>		
	First Quartile	190		First Quartile	225
	Median	212		Median	255
	Third Quartile	277		Third Quartile	286

## Comparative Performance

### Peer Group Returns

Rank	2006 ROI (%)	Rank	2007 ROI (%)	Rank	2006 Adjusted ROI (%)	Rank	2007 Adjusted ROI (%)				
1	Eastland Network	7.5	1	Westpower	14.7	1	MainPower New Zealand	8.0	1	Westpower	15.5
2	OtagoNet Joint Venture	6.9	2	OtagoNet Joint Venture	7.9	2	Eastland Network	7.5	2	OtagoNet Joint Venture	7.9
3	Centralines	5.4	3	Centralines	6.9	3	Marlborough Lines	7.1	3	Centralines	6.9
4	Westpower	4.9	4	Buller Electricity	6.7	4	OtagoNet Joint Venture	6.9	4	MainPower New Zealand	6.7
5	Marlborough Lines	4.6	5	Top Energy	4.5	5	The Lines Company	5.6	5	Buller Electricity	6.7
6	MainPower New Zealand	4.2	6	MainPower New Zealand	3.3	6	Centralines	5.4	6	The Lines Company	5.3
7	Buller Electricity	3.9	7	Marlborough Lines	2.8	7	Westpower	4.9	7	Marlborough Lines	5.2
8	Top Energy	3.5	8	The Lines Company	2.4	8	Buller Electricity	3.9	8	Top Energy	4.5
9	The Lines Company	2.7	9	Eastland Network	2.3	9	Top Energy	3.5	9	Network Waitaki	3.4
10	Network Waitaki	0.8	10	Network Waitaki	1.2	10	Network Waitaki	2.2	10	The Power Company	2.4
11	The Power Company	0.5	11	The Power Company	1.0	11	The Power Company	1.5	11	Eastland Network	2.3
	Industry Average	5.7		Industry Average	5.5		Industry Average	7.2		Industry Average	7.1
	Industry Median	5.2		Industry Median	5.8		Industry Median	7.2		Industry Median	6.8
	<b>Group (excluding MLL)</b>			<b>Group (excluding MLL)</b>			<b>Group (excluding MLL)</b>			<b>Group (excluding MLL)</b>	
	First Quartile	2.9		First Quartile	2.3		First Quartile	3.6		First Quartile	3.7
	Median	4.0		Median	3.9		Median	5.2		Median	6.0
	Third Quartile	5.3		Third Quartile	6.9		Third Quartile	6.6		Third Quartile	6.9

Note: Adjusted ROI is calculated using returns prior to the deduction of customer discounts and rebates (net of the corporate tax effect).

## Comparative Performance

### Peer Group Returns, continued

Rank	2006 ROE (%)	Rank	2007 ROE (%)	Rank	2006 ROF (%)	Rank	2007 ROF (%)				
1	Eastland Network	10.7	1	Westpower	15.9	1.0	Eastland Network	10.9	1	Westpower	15.4
2	OtagoNet Joint Venture	6.9	2	OtagoNet Joint Venture	7.8	2.0	Centralines	8.2	2	Centralines	9.2
3	Centralines	5.1	3	Eastland Network	7.2	3.0	OtagoNet Joint Venture	6.9	3	Buller Electricity	8.2
4	Marlborough Lines	4.9	4	Buller Electricity	6.5	4.0	Westpower	6.4	4	OtagoNet Joint Venture	7.9
5	Westpower	4.8	5	Centralines	6.5	5.0	Marlborough Lines	5.9	5	Top Energy	6.7
6	MainPower New Zealand	4.2	6	Top Energy	5.2	6.0	Top Energy	5.4	6	Eastland Network	6.0
7	Top Energy	3.7	7	MainPower New Zealand	3.3	7.0	MainPower New Zealand	5.3	7	Marlborough Lines	4.2
8	Buller Electricity	3.5	8	Marlborough Lines	3.1	8.0	Buller Electricity	4.7	8	MainPower New Zealand	3.9
9	Network Waitaki	2.2	9	Network Waitaki	2.3	9.0	The Lines Company	3.6	9	The Lines Company	3.6
10	The Lines Company	1.6	10	The Lines Company	1.3	10.0	Network Waitaki	3.3	10	Network Waitaki	3.3
11	The Power Company	0.5	11	The Power Company	0.9	11.0	The Power Company	1.6	11	The Power Company	2.1
	Industry Average	19.4		Industry Average	4.3		Industry Average	8.0		Industry Average	7.9
	Industry Median	5.0		Industry Median	6.0		Industry Median	6.7		Industry Median	8.0
	<b>Group (excluding MLL)</b>			<b>Group (excluding MLL)</b>			Group (excluding MLL)			<b>Group (excluding MLL)</b>	
	First Quartile	2.5		First Quartile	2.5		First Quartile	3.8		First Quartile	3.7
	Median	3.9		Median	5.9		Median	5.3		Median	6.4
	Third Quartile	5.0		Third Quartile	7.0		Third Quartile	6.8		Third Quartile	8.1

# Appendix 4

## Glossary

## Glossary

Term	Definition
<i>CAIDI</i>	Customer Average Interruption Duration Index
<i>EBIT</i>	Earnings Before Interest and Tax
<i>EBITDA</i>	Earnings Before Interest, Tax, Depreciation and Amortisation
<i>EDB</i>	Electricity Distribution Business
<i>EIL</i>	Electricity Invercargill Limited
<i>GWh</i>	Gigawatt Hours
<i>ICP</i>	Installation Control Point
<i>ISO</i>	International Standards Organisation
<i>JV</i>	Joint Venture
<i>km</i>	kilometre
<i>kV</i>	Kilovolt
<i>kVA</i>	Kilovolt Amp

## Glossary

Term	Definition
<i>kW</i>	Kilowatt
<i>m</i>	million
<i>MEPT</i>	Marlborough Electric Power Trust
<i>MLL</i>	Marlborough Lines Limited
<i>MVA</i>	Megavolt Amp
<i>MW</i>	Megawatt
<i>NEL</i>	Nelson Electricity Limited
<i>NZ GAAP</i>	New Zealand Generally Accepted Accounting Principles
<i>NZ IFRS</i>	New Zealand International Financial Reporting Standards
<i>ODV</i>	Optimised Deprival Value
<i>OJV</i>	OtagoNet Joint Venture
<i>OPSL</i>	Otago Power Services Limited

## Glossary

Term	Definition
<i>PwC</i>	PricewaterhouseCoopers
<i>ROE</i>	Return on Equity
<i>ROF</i>	Return on Funds
<i>ROI</i>	Return on Investment
<i>ROI Adjusted</i>	Return on Investment adjusted for customer discounts and rebates
<i>SAIDI</i>	System Average Interruption Duration Index
<i>SAIFI</i>	System Average Interruption Frequency Index
<i>SCI</i>	Statement of Corporate Intent
<i>The Company</i>	Marlborough Lines Limited
<i>The Trust</i>	Marlborough Electric Power Trust
<i>TPC</i>	The Power Company
<i>WACC</i>	Weighted Average Cost of Capital