

TRUSTEES' REPORT

On the operations and financial affairs of the

HAWKE'S BAY POWER CONSUMERS' TRUST

For the year ended 31 March 2004

ANNUAL REPORT TO CONSUMERS

The Trust holds all the shares in Unison Networks Limited, on behalf of consumers who are connected to the electricity lines system of Unison Networks Limited in Hawke's Bay.

This Annual Report is to those consumers, and gives a summary of the operations and financial affairs of the Hawke's Bay Power Consumers' Trust for the year ended 31 March 2004.

TRUST ACTIVITIES

Unison Networks: In our primary role as the sole shareholder in Unison, we have monitored the operational and financial performance of the Company on your behalf. We are very pleased to report that a strong financial result was achieved by Unison for the year and this has added value to the shareholders' equity in the Company. The integration of the Rotorua and Taupo networks has been successfully completed and the benefits of an expanded business are already apparent. [Refer to *Company Performance and Results* for details].

A Complex Industry: The electricity industry remains complex, cluttered and generally bewildering to most consumers. It will therefore come as no great surprise that the Trust has had to keep chipping away at many of the same issues we spoke about in our 2003 report. Regrettably, the strong push for transparency on electricity accounts, to require retailers to separate the lines and energy charges in their billing to consumers, has still not been achieved. Our Annual Meeting in 2003 was the third successive year that a unanimous resolution was passed to authorize the Trust to press for this change, which would allow consumers to see where changes in pricing occur.

The good news is that the Minister of Energy, Hon. Pete Hodgson, recently stated he is prepared to regulate to require retailers to show transparency in their accounts. This initiative would deliver on the Government's Policy Statement to require transparency of charge components. We welcome this step, which would place a greater level of accountability on retailers.

Regulations & Controls: While the Trust supports the overall objective of providing a secure supply of electricity at reasonable cost, we are concerned that only one sector of the electricity industry, the lines companies, is subject to regulatory control. Unison's charges make up only part of the delivered cost of electricity, yet there is no similar regulation or control imposed on generators, retailers or the national grid operator.

Through the activities of the Commerce Commission and, more recently the new Electricity Commission, Unison's and other lines companies' operational and financial affairs are now subject to scrutiny and regulatory control. Because of recent pricing changes, Unison is in breach of the price path thresholds set by the Commerce Commission and is currently subject to an inquiry by that Commission. We question why lines companies are subject to such control, particularly when Ministry of Economic Development reports show Unison's prices increased only 1% in the period from 15 November 1999 to 15 February 2004. In comparison, the major retailer in Hawke's Bay, Contact Energy, raised charges by 32% in the same period.

Benefits of Ownership: Our Deed of Trust states that all income and capital of the Trust can only be used for the benefit of its consumer-owners. In the 5 years from 1998 to 2003, more than \$20 million has been distributed to those owners.

Over recent years, the Trust has taken the view that the benefits of consumer ownership of the Company have been best passed on to shareholders through discounts and keeping the delivered costs

of electricity to the minimum. However, the dynamics of ownership of Unison have changed with the acquisition of the Rotorua and Taupo networks and the introduction of price regulations by the Commerce Commission. Furthermore, there is also the need to continually renew ageing components of Unison's networks and to meet the increasing demand for electricity as the regional economies continue to grow.

The Trust, on behalf of its consumer-owners, sanctioned the recent price rises to enable Unison to achieve its prime function of operating as a successful business and to grow the value of the owners' investment in the Company. As stated in its Annual Report, Unison has come from a history of low prices and better than average quality standards, and we are of the opinion that the company should not be constrained against earning an acceptable cost of capital and provide for sustainable cash flows for the future.

We have been kept fully apprised by the Board of Directors of the need for changes to pricing – both for the good of the Company and for its consumer-owners. We are satisfied that shareholders' interests are best served by delivering sustainable returns from providing our users with quality services at efficient prices.

Ongoing Benefits

The Trust remains committed to consumer-owners sharing in the success of the Company's financial performance through the distribution of discounts and other forms of benefits.

- **Discounts:** At the time of preparing this report, the Commerce Commission has not completed its inquiry into the alleged breach of the Commission's pricing threshold. Because of this uncertainty, and the need for Unison to reinvest in asset replacement and renewal, the Trust agreed that the discount to consumer-owners should be held over in the meantime. It is our very clear objective to reinstate this discount regime as soon as the financial outlook has been clarified and once the outcome of the Commission's inquiry has been factored in to the Company's financial situation. The Board of Directors of Unison is fully aware of our expectations in this regard.
- **Undergrounding:** The Trust also sees benefits of ownership being reflected in others ways, including the progressive undergrounding of Unison's networks in Hastings and Napier. It is planned to spend \$35 million over a 15 year programme to complete the underground conversion of overhead lines. The removal of lines and poles from above ground will certainly create a more pleasant and attractive environment for our communities.
- **Rural Improvements:** The Company is also to spend an additional \$4 million in rural areas to further improve reliability of supply and to reduce the duration of outages.
- **Energy Efficiency:** In these times of threatened generation shortages, it is important to use electricity wisely and to be efficient and conserve what we have available. As well as saving electricity, insulation of homes provides significant health benefits and, depending on the outcome of the Commerce Commission inquiry, we will be working with the Company to assist in energy efficiency projects over the next 10 years. In the meantime, the Trust has deferred its own investment in these projects until the Commission's decision is known.

Competition In Place: Our consumers now have choice as to which retailer they select to be their supplier of electricity. Switching between retailers is easy to do and our Citizens' Advice Bureaus are ready to assist with enquiries of this nature. Information is also readily available on the Internet at www.powerswitch.co.nz.

Communication & Publicity: The electricity industry does not generate any real "excitement" in people's minds, and for the most part it is only thought of when the power account arrives in the letter-box, or when the lights go out! Nevertheless, there are matters that the consumers we represent should be informed of and the Trust frequently issues statements in local newspapers, and on the radio, about the Trust's activities.

Detailed information about the Trust and its work is now accessible on the internet, under www.hbpowertrust.co.nz. This operates as a part of Unison's website and the following information is available:

- The role and purpose of the Trust
- The Deed of Trust
- Names of current Trustees and how they are elected
- Annual Reports and Financial Statements for the years 2002, 2003, and 2004
- Recent news articles

There are advantages in the Trust being aware of community issues and how the activities of the Trust and Unison impact on our communities. Accordingly, we have met with the Mayors of Hastings and Napier to gain a better understanding of the Councils' activities and matters of common interest.

Trustees are frequently invited to speak to various organizations about the Trust's work and we regard these links as helping consumers to understand more of the electricity industry and to assist where advice is needed. One issue of particular concern to many consumers is the accuracy of information from retailers about their electricity tariffs and pricing schemes. Trustees are willing to give advice on these and related matters.

COMPANY PERFORMANCE AND RESULTS

Each year the Trust, as the shareholder, is required to:

- Monitor the performance of the Directors of the Company, and
- Prepare a statement on the Company's compliance with its Statement of Corporate Intent (SCI).

Statement of Corporate Intent 2003-04

The Statement of Corporate Intent outlines the Company's overall objectives, intentions and operational and financial performance targets for the year.

Last year, we said that the "real test" of the Company achieving its financial targets would only be possible after a meaningful assessment is made of a full 12 months' operations, following integration of the Rotorua and Taupo Networks. We are now able to make that assessment.

The Statement for 2003-04 contained a number of primary goals, designed to achieve the Company's Mission of operating as a successful business to provide owners with a positive return on investment, and network users with high quality lines services at efficient prices.

The Trust endorsed those goals and the associated performance targets and measures set out in that Statement.

Financial Outcomes for 2003-04 close to targets

In financial performance, Unison has achieved a level close to the overall targets and measures for the year ended 31 March 2004. Specifically, Trustees note the solid overall trading surplus of \$28.1 million exceeded the target for the year. This improved result enabled debt repayment to be accelerated, and has lifted the ratio of Shareholders' Funds:Total Assets to 50.69%, ahead of the 46.74% target for 2003-04.

We also note the Company's Net Surplus as a percentage of Shareholders' Funds of 5.79% was higher than projected.

Although the Company did not meet the targets set down for the remaining performance indicators, the results achieved were only marginally below the expected outcomes. Consequently, Trustees regard the overall financial performance as a realistic result from a year in which the Company integrated the Rotorua and Taupo networks, and coped well operationally in spite of the Winter power supply crisis and the impact of a number of storms on the networks.

Operational Costs Higher

Total business operating costs per customer of \$148.06 were 10.5% above the target level set for the year, with direct costs per customer being nearly 14% higher than expected. Trustees recognise this increase has been driven by:

- additional safety inspections and safety work on transformers and pedestals
- an increase in investment for Information Technology
- regulatory costs, and
- additional investment in network activities to improve operational and capital efficiency

In the new operating year we acknowledge there will be further expenditure in these areas, plus recurring and additional “compliance” costs required of all lines companies for the operations of the Commerce Commission and the new Electricity Commission.

Network Performance

As stated in the Company’s report, the overall quality of supply targets which are measured by average interruption indices, were not achieved. The Trustees understand and accept that abnormal weather patterns and the combination of severe winds, snow and rain storms were the primary reason why targets have not been met.

It was pleasing to note, however, the number of interruptions experienced by the average consumer was less than projected.

Corporate Responsibility

Unison aspires to be regarded as a responsible corporate citizen. The Trust endorses the activities and contributions the Company makes to all communities in which it operates, particularly in Hawke’s Bay and through public safety awareness across all its networks.

THE FUTURE

Trustees are satisfied the initiatives that were taken in 2002 to acquire the Rotorua and Taupo networks, and thus expand the Company’s business affairs, were in the best interests of the shareholder-consumers.

The benefits of an expanded lines network are already evident in the results so far and we share the Company’s belief that, over the longer term, the acquisition will create future growth opportunities and provide greater benefit for shareholders.

Trustees give their support to the need for the Company to achieve a commercial rate of return on capital employed; this being essential to ensure the Company can attract the capital necessary to maintain and develop the network for the long term benefit of consumers. We will continue to monitor the Company’s performance and look forward to grow the business and create value for the benefit of its shareholder-consumers.

THANKS

The Trust is fortunate in the skills and commitment of Unison’s directors, and the Chief Executive and his team. On behalf of the Trust I extend our thanks to all for the successes over the past year.

Special thanks to Forrie Miller, past Chairman of the Company, who retired in January to take up a judicial appointment. Our thanks also to Arch Buntain who retired from the Board during the year.

The Company is now twice the size it was 18 months ago and to reflect the added responsibilities facing the Board, the Trust decided to increase the number of directors to six. As a result, the Trust appointed three new directors - Keith Valentine of Napier, Helen Walker of Central Hawke's Bay and Dave Frow of Wellington. With these appointments we have a solid mix of experience and fresh thinking at the Board table and that can only be for the future good of our Company. Brian Martin is now Chairman of the Board and we thank him for taking up that role..

My personal thanks to my co-trustees for their contributions and dedication to the work of the Trust. As with the Directorate, the tasks and duties required of us have grown and we expect another busy year ahead.

Ken Gilligan
Chairman

