DIRECTORS REPORT
TO THE TRUSTEES OF THE
TOP ENERGY CONSUMER TRUST

OWNERSHIP REVIEW

MAY 2022

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1. Executive Summary

The Directors submit this report in response to the ownership review of the shares in Top Energy Limited, requested by Trustees and as provided for under the Trust Deed.

This report, supported by the independent PricewaterhouseCoopers (PwC) report, shows a consistent and sustained level of returns by the Top Energy Group. Actual Group Financial Performance has exceeded SCI targets for all five years since the last review and assets have increased 80% over the that period. In particular, the last financial year delivered the commissioning of the 32MW Ngawha expansion and increased consumer discounts by 31%.

The profitability (post discounts) of the network business is comparable with the industry and our peers which is expected given the regulated nature of the business and are reflective of prices allowed by the Commerce Commission.

Overall, reliability levels have improved since the last review although they remain higher than our industry peer group. The installation of diesel generators on the single 110kV Kaitaia line has reduced planned outages since 2020 and there has been a specific focus on minimising the impact of unplanned outages.

The new investments undertaken by Top Energy have been enabled by the present Trust ownership structure, and through the current subsidiaries. The ownership structure provides flexibility for the development of future growth opportunities and the aspirations contained in our future Strategy.

The Directors believe the objectives of Top Energy Limited, as reflected in the current Statement of Corporate Intent, are best achieved with the current Trust ownership structure, and therefore the Directors recommend:

That the shares of TOP ENERGY LIMITED continue to be retained by the Top Energy Consumer Trust.

For and on behalf of the Directors

Richard Krogh
Chairman

3 May 2022

2. Introduction

This is the sixth Ownership Review report compiled by Directors for the Trustees of the Top Energy Consumer Trust. The last ownership review was completed in 2016, which adopted a unanimous decision that the shares of Top Energy Limited (Top Energy) continued to be retained by the Top Energy Consumer Trust (the Trust).

The position recommended by the Directors was supported by the community through the public consultation process and endorsed by the Top Energy Consumer Trust.

In December 2021, the Trust requested the Directors to prepare a report in relation to the possible future ownership options and our views as to the best of those options, as far as they would benefit the power consumers of the Far North. The report is to be furnished by 1 June 2022.

3. Purpose of the Directors Report

The purpose of the report is to review and report on the ownership arrangements for the shares of Top Energy, a limited liability Company with 25 million shares.

The content of this report has been structured around the specific requirements of the ownership review as set out in clause 4 of the Trust's Deed.

The Trust's Deed requires that the Trustees undertake a review, from time to time, of their continued ownership of the shares in Top Energy. That review involves seeking the views of the Directors of the Company, followed by a public consultation process. At the end of this procedure the Trustees, after further discussion with the Directors, consider the submissions received and then make a decision on whether the Trust should continue to own the shares for (up to) the next 5 years, at which time another review is required to be undertaken.

As stated above, the requirement to carry out a review of the ownership is set out in the Trust's Deed. There is, however, no explanation as to why the Deed requires this to be done or the objective of the process. The wording of clause 4.1 (a) covers both the requirement for an analysis of past performance and the requirement for a discussion on the advantages and disadvantages of Trust ownership. This appears to represent an assumption by the writers of the Deed that there is a connection between the two.

4. Background of Top Energy Limited and Trust Ownership

The Trust was settled by Top Energy in 1993. The Deed under which the Trust was created was prepared by the (then) Directors of the Company, after public consultation. This was the result which arose from the Establishment Plan process, set out in the Energy Companies Act 1992. The creation of the Company was followed by the issuing of shares to the shareholder and the vesting of the undertakings of the Bay of Islands Power Board to Top Energy. As shareholder of the Company, the Trust carries out the usual shareholder responsibilities such as the appointment of Directors, setting of Directors fees and the approval (or otherwise) of major transactions proposed by the Directors. Between the Directors and the trustees, a Statement of Corporate Intent is also annually agreed and published.

The beneficiaries of the Trust are the power consumers of the district, at any point in time. As a group or class, these people and businesses have contributed to the development of the Company. This has occurred over many years, both under the Power Board regime and the current corporatised structure. Over time, some of these individuals and businesses will move out of the district. Similarly, others will move into the district. The benefits of being a power consumer connected to the Top Energy network will change for those people; but generally, the people who have contributed to the wealth of the company will enjoy the benefits that go with owning the local power network company. In the past, those benefits have included tariffs which were lower than could have been expected if the shareholders were requiring a dividend from their investment. Since 1998, the beneficiaries have received a distribution arising from a cash dividend or line charge discount paid by Top Energy. We expect this to continue.

When Top Energy was first established, it was based on a traditional electricity distribution and retailing structure, arising from the Electric Power Boards regime. This meant that the operations were essentially those of power distribution asset ownership and the purchasing of bulk electricity from a government owned entity and its retailing to end consumers. The electricity industry has changed markedly since that time and so has Top Energy.

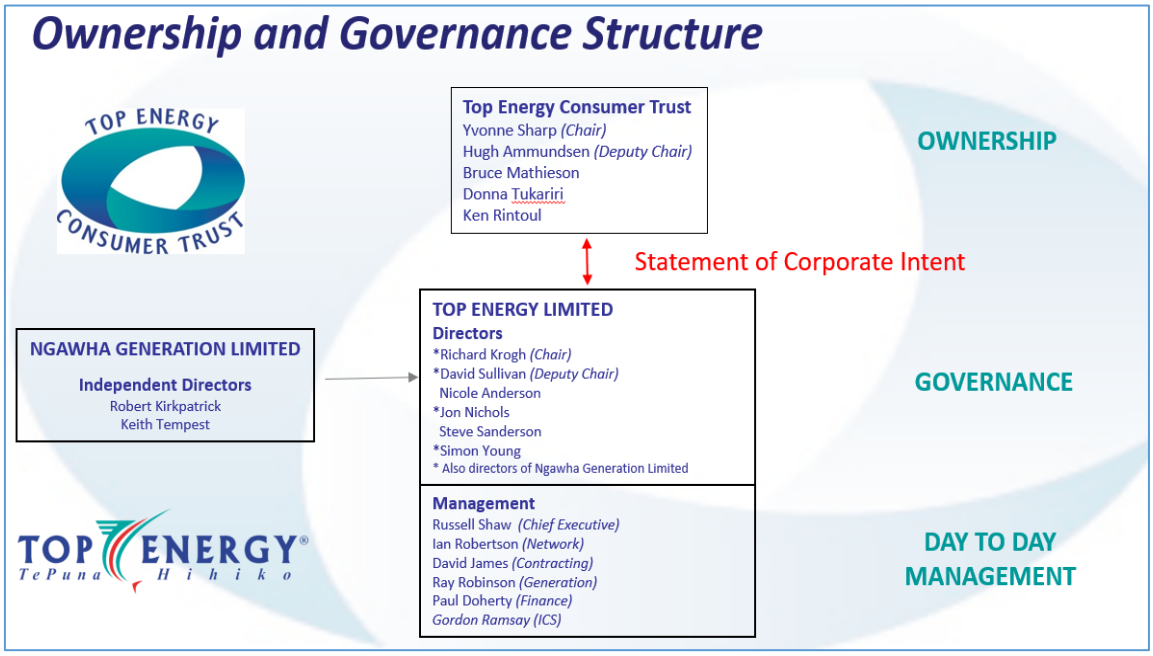
In 1998, the (then) government legislated for the separation of the distribution (lines) parts of the power companies and the retailing and generation activities of those companies. When the Company was first created and the Trust established to own the shares in it, Top Energy was essentially a lines distribution company.

In 2022, the Top Energy Group is a diverse energy company, involved in 57MW of geothermal power generation, power distribution and electrical contracting. All of these activities create value for the Group and provide employment opportunities in the Far North. Many other lines businesses throughout New Zealand have similarly developed a wide range of additional activities to their original core lines businesses.

As a result of the above, it is now difficult to make direct comparisons between the performance of Top Energy and other companies which operate in the electricity distribution sector. Any performance comparisons must also take into account the differences in the external environment of each business. These differences are due to the varying environmental factors and geographic characteristics of the regions in which the businesses are based. These are an important determinant of the service quality performance and efficiency measures of each network business. This is achieved by focusing specifically on comparisons with networks which exhibit the underlying characteristics which are the most like Top Energy

Any decision on whether to change the ownership structure must consider the likely results achievable to consumers in the future. The historic information referred to in this report shows how the Directors and management of the Company have performed in the past. While there are many things which will impact on the results achieved by the business in the future, almost all of these will impact on the business in a similar way, regardless of its ownership structure.

The following diagram sets out the relationships between the Trust (and beneficiaries) and the Company, including the Board of Directors and management.



The trustees are appointed under a process set out in the Deed and the appointment of local individuals to act as Trustees brings a local focus to the direction and performance of Top Energy. This involves the calling of nominations for appointment from members of the public, the short listing of nominees by an Independent Consultant and the selection from that shortlist, of the required number of trustees, by a selection panel made up of the Members of Parliament for Northland and Te Tai Tokerau and the Chair of the Northland Regional Council.

Due to the trustee appointment process, Top Energy is subject to the price and quality control regime set by the Commerce Commission, using its powers under the Commerce Act 1993.

The Directors of Top Energy are charged with the responsibility for the governance of the Group, including the delegation of appropriate authorities to the Chief Executive, to ensure achievement of the strategy and objectives of the Group.

5. Top Energy Limited

Description of the area served by Top Energy's Electricity Network

Total area	6,822 Sq kms
Length of distribution circuit (as at 31 March 2021)	4,088 kms
Combined Peak Demand	79 MVA
Number of Power Consumers (as at 31 March 2022)	33,500
Network Regulatory Asset Base (as at 31 March 2021)	$302.2 million
Average weekly income (Northland)	$1,357*
Average weekly income (National)	$1,701*

* Source: Statistics NZ June 2021

The business activities and investments of Top Energy fall into the following operational areas:

- The distribution lines business which operates the electricity infrastructure, taking electricity from Transpower's bulk point of supply in Kaikohe to the customers individual connection.
- Contracting Services which primarily provides construction and maintenance services for the Company's electrical network equipment and delivers supplementary external contracting services.
- Ngawha Generation Limited, which owns and operates 57MW of renewable geothermal generation.
- Top Energy Ngawha Spa Limited, currently a shell company which used to own land that was earmarked for development of the geothermal resource at Ngawha.

It is through the corporate structure of 100% owned subsidiaries that Top Energy has the capacity to expand its available resources for future growth opportunities.

Future Growth Opportunity

A substantial opportunity continues to exist for the Ngawha Generation 100% owned subsidiary. The Ngawha field is the only high temperature geothermal resource in New Zealand, outside of the Taupo Volcanic Zone and is the source of the only baseload generator north of Auckland, the largest electricity demand centre in the country. This is a significant opportunity with the decarbonisation of the energy sector and the electrification drive as the Government strives for 100% renewable generation by 2030.

In 2016, a revised resource consent was granted to 2052 that allow for the continued operation of the plant and expansion of geothermal generation of up to 89MW.

Since the last ownership review, the geothermal plant increased from 25MW (net) generation output to a total of 57MW (net) generation output in December 2020. Any future expansion will be completed to closely match forecast increases in demand for electricity but after providing a period between for monitoring on the geothermal field.

The expansion to date and in the future has considerable positive effects locally, regionally, and nationally. These include economic, security of generation and reliability of supply, increased locally sourced renewable generation and more competitive wholesale pricing. Future expansion could also help displace existing/additional investment in generation from fossil fuel sources.

The investment required for the final stage of the expansion is approximately $200 million.

6. Performance

The Group and Network business has exceeded the SCI financial targets each year from 2017-2021, this being achieved alongside a significant investment in both the electricity network and additional geothermal generation, and increasing discounts paid to consumers. Of note is that for two of the five years, the Group has also dealt with the challenges of the Covid-19 pandemic, ensuring the safety of our staff and the availability of our critical lifeline business services.

A key factor in setting performance targets and the level of returns is the consideration of the Statement of Corporate Intent Objectives, which include ensuring that the Company adopts a wider approach to value, looking at the more traditional financial returns and adding in social issues such as reducing the total delivered cost of electricity.

The Company has completed the core projects within the 10-year $200 million network investment strategy that commenced in 2010 to deliver reliability and security improvements. Unfortunately, the second 110kV line from Wiroa to Kaitaia has been unable to be completed due to lengthy land access legal proceedings for the past 5 years. This is now awaiting the findings of a recent Supreme Court hearing. As an interim solution, diesel gensets have been deployed to ensure the Company can deliver on the required security of supply.

The Group's further investment in geothermal generation through its subsidiary, was the largest project that has occurred in the Far North. This was successfully completed, 6 months ahead of the original schedule, in December 2020 and now provides the total energy needs of the Far North over 95% of the time.

To support improved performance, investment has continued in the development of technology systems ranging from a customer relationship management system, to improve customer interactions, through to the replacement of the Network's core operational SCADA system, to enhance the real time operation of the network. In addition, with the increased reliance on technology and the heightened cyber risk in today's environment, robust security improvements have been implemented to mitigate against cyber-attacks.

The Company has also been able to continue providing annual discounts to its consumers, amounting to more than $28 million (11% more) since the last review.

Taking the above into account, the Groups financial performance (measured as EBITDAF) has improved since the last review, with a total $198.1 EBITDAF in the last five years, compared to a total $152.9m over the previous 5 years (being the last ownership review period).

The investments made has also seen the asset value increase 80% to $680m highlighting that these investments in business operations and geothermal production assets have contributed to long-term shareholder value.

Performance extracts from the PricewaterhouseCoopers (PwC) report include:

"As a group, the Company has been met its financial SCI targets consistently over the review period. It has also met its newly introduced cultural and environmental targets since these have been implemented"

"Under 100% trust-ownership, Top Energy has substantially grown its asset based and increased the energy independence of the Far North region. It has laid the foundations of improving energy affordability and security in the region."

7. Ownership Options

To ensure that an independent assessment of the various ownership options is undertaken, the Directors engaged PricewaterhouseCoopers (PwC) to complete an independent review as required by clause 4.1 of the Trust Deed. This includes:

a) An analysis of the performance of the Trust and the Company to the date of the report, together with a discussion of the advantages and disadvantages of Trust ownership;

b) An analysis of various alternative ownership options, 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; and

c) A comparison of the performance by the Company with the performance of other energy companies with different ownership structures.

The various alternative forms of ownership considered by the PwC report (section 6) are summarised below:

- 100% Consumer Trust ownership of shares in Top Energy - status quo
- Distribution to beneficiaries or sale to the public or external investors of 24.9% of 49.9% of shares – a distribution of 24.9% allows the Trust to retain control over the constitution, a distribution of 49.9% allows the Trust to retain outright control
- Distribution of 100% of the shares to beneficiaries – would mean the Trust would cease to exist
- Sale of 100% of shares to the public or external investors - the Trust would need to consider whether it retains the proceeds of the sale and manage them for the benefit of the beneficiaries or distribute the proceeds to the beneficiaries.

8. Interaction of Shareholder and Beneficiaries

The Trust ownership model has been proven over the past 29 years to be a simple and effective method in ensuring that the interests of beneficiaries in the Far North are maintained. There is a threshold for shareholder involvement in any major business decisions as set out in the Company's Constitution (20% of asset value) and there is an interactive relationship between the Trust Deed which defines the Trusts objectives and duties, the Company's Constitution, the requirements for electricity companies set out in the Energy Companies Act 1992 and the Statement of Corporate Intent.

With the Trust model of ownership, it is the trustees who have the duty and responsibility of any decision making as shareholder of the Company. The Trust model allows the Company to make balanced trade off decisions between the timing of investments in network reliability and the ability of consumers in our region to pay.

The Trust is required to hold an Annual Public Meeting, to present to beneficiaries the operational and financial performance of the Trust for the year and provide an opportunity to beneficiaries to express their views on the performance and provide adequate responses to questions asked.

In addition, the five yearly ownership review provides beneficiaries the opportunity to submit and express views on how the Trust model of ownership is working on their behalf.

9. Conclusions and Recommendation

Clause 4.1(d) of the Trust Deed requires this document to outline:
"the conclusions of the Directors as to the most appropriate form of ownership together with an indication of whether the conclusions are unanimous and if the decision is not unanimous, a summary of the conclusions of the dissenting Directors shall be included"

The Directors have considered the requirements of the Trust Deed and the alternative forms of ownership that are outlined in section 6 of this report. In reaching their conclusions the Directors have considered the PwC report, the impact of industry regulation which has evolved since the last review, the growth opportunities available to Top Energy and the performance achieved by other network entities with various ownership structures.

The Directors of Top Energy see the Company as having a successful future. This success is built on strong foundations and achievements the Company has seen and delivered to date and will continue to be achievable with the support of the Trust and its beneficiaries. In anticipation of that support, we see:

- Continual growth in the Company and continuing increases in capital values;
- Continuing benefits to electricity consumers in the Far North;
- Wider regional and economic benefits to the Far North community from having a substantial commercial entity located in and focused upon this region; and
- Continued balanced decision making between investments in network reliability and the ability of Far North consumers to pay higher prices

The Trust ownership of Top Energy Limited does not restrict growth opportunities as evidenced by the Ngawha expansion. The existing structure of the Group allows sufficient flexibility so that additional funds could be obtained if required. This could be done by way of additional debt or sale of equity interests in selected subsidiaries whilst there is no loss of control by the beneficiaries in relation to Top Energy Limited.

The Directors believe the objectives of Top Energy Limited, as reflected in the current Statement of Corporate Intent, are best achieved with the current Trust ownership structure.

On balance:

1) the advantages of Trust ownership outweigh the disadvantages of such a structure; and

2) the financial performance of the Company has not been negatively affected by the ownership structure under which it operates.

Therefore, the Directors recommend:

That the shares of TOP ENERGY LIMITED continue to be retained by the Top Energy Consumer Trust.

The decision to recommend the above ownership option is a unanimous decision of all Directors.

Top Energy Ownership Review

Strictly confidential
Full report
April 2022

pwc

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Strictly confidential

The Board of Directors
Top Energy Limited
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5 April 2022

Top Energy Ownership Review – Full Report

Dear Directors,

We are pleased to present our report which has been prepared to assist the Directors of Top Energy Limited (the Company) with the five yearly ownership review of the Top Energy Consumer Trust (TECT, the Trust) as required under the TECT Trust Deed.

This report has been prepared in accordance with our letter of engagement dated 16 December 2021 and is to be read in conjunction with the terms and conditions set out within that document, and the restrictions set out in Appendix A of this report.

This report is confidential to the Trust and the Company. A summary report will also be provided, for public consultation purposes.

Yours sincerely,

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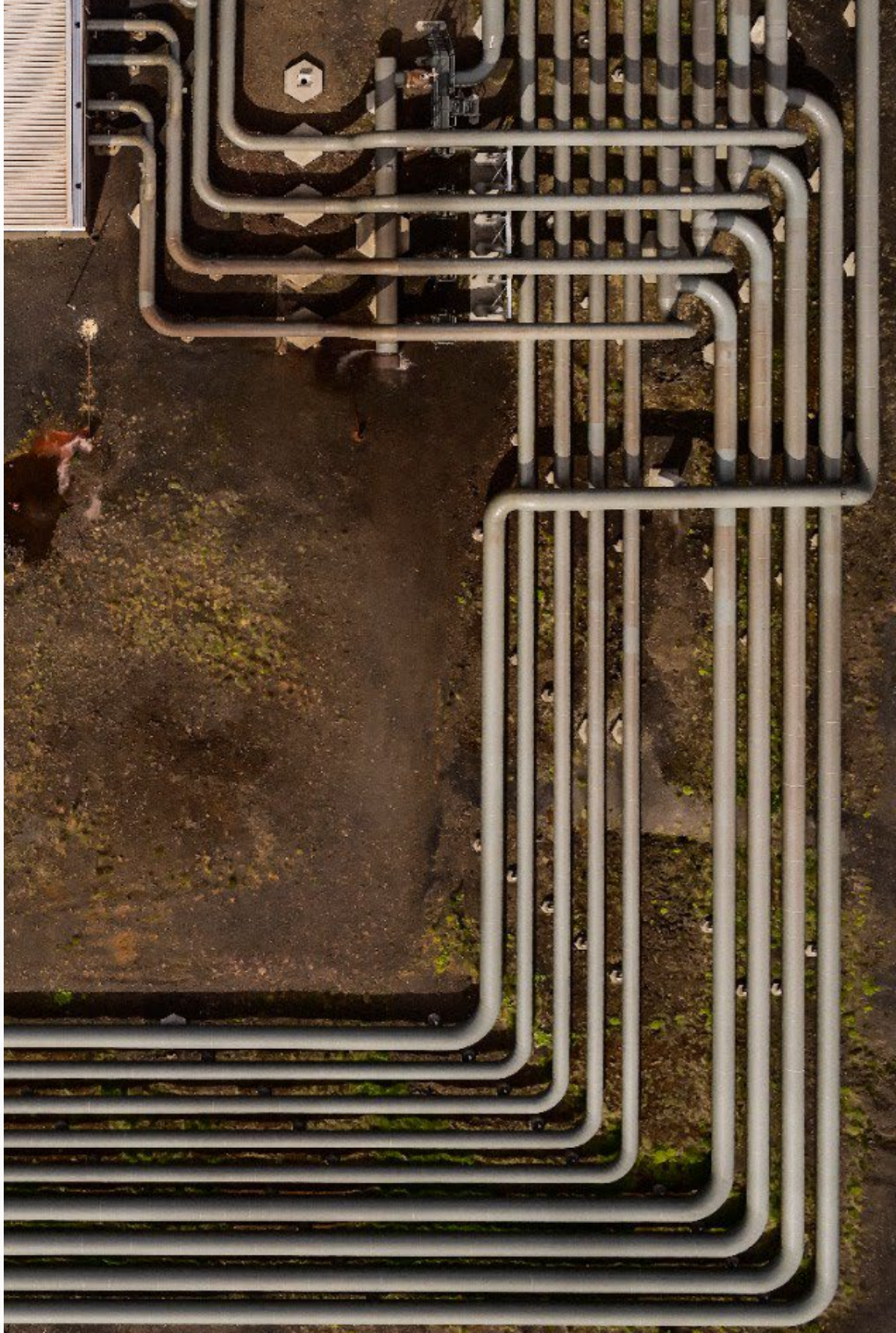


1 Introduction

Introduction

Introduction and purpose

This report has been prepared for the Directors of Top Energy Limited (Top Energy or the Company) to support the periodic review of the Top Energy Consumer Trust's (TECT) ownership of Top Energy.

Consistent with Clause 4.1 of the Trust Deed, the review must include:

- 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
- an analysis of alternative ownership options, including without limitation, a share distribution to Consumers or Electors, a sale of shares to the public, a sale of shares to institutional investors and retention by the Trust
- a comparison of the performance by the Company with the performance of other energy companies with different ownership structures.

This report has been structured into four parts:

1. Review of Top Energy's performance over the last five years (FY17 – FY21, the review period)
2. Review of Top Energy's electricity distribution business (EDB) performance against comparable companies
3. Analysis of TECT performance against other EDB trusts and comparison of Top Energy's performance against different EDB ownership structures
4. Analysis of ownership options available to the Trust and its beneficiaries, including the current trust ownership structure.

A summary of our analysis is included in the Executive Summary.

In conducting this review, PwC has relied on information supplied by Top Energy, Corporate Statements of Intent, Annual Reports, Pricing Methodologies, published information disclosure (ID) documents for EDBs, PwC databases and interviews with the Chair and Deputy Chair of the Board of Directors, the Chair and Deputy Chair of TECT, and members of the executive leadership team of the Company.

2

Executive summary

Executive summary

Group overview

Top Energy is the electricity generation and lines network company which employs over 150 people and distributes power to the approximately 32,000 power consumers of the Far North of New Zealand.

With operations throughout the region, the Company has interests in electricity generation, through its wholly owned subsidiary Ngawha Generation Limited, along with the EDB and an electrical contracting business sub-unit.

The Company's vision is:

Enabling Northland to contribute to the decarbonisation challenge.

With a capacity of 57MW, the Ngawha power station's output is fed into Top Energy's network and then connected to the National Grid, via Top Energy's sub-station near Kaikohe. With the recent expansion of capacity, Ngawha now generates more than the average electricity demand in the region and this has reduced the relative wholesale prices at the Kaikohe grid exit point (GXP). Further, the community's exposure to possible National Grid failures to the south has been significantly reduced by this expansion.

Top Energy's network consists of just over 4000 km of lines covering around 6,822 square kilometres of often remote and rugged terrain. The asset base is valued at approximately $300m which is above the median for EDBs. The network serves a widely distributed and often sparse population and much of it is uneconomic to maintain.

Top Energy's contracting business mainly provides services to Top Energy but also supplies third parties.

The Company supports a number of community projects including the rescue helicopter and Healthy Homes Tai Tokerau.

Executive summary

Outlook for the Company

There is increasing attention on the capability of the electricity sector to manage growth, given New Zealand's climate change policy goals, which will only be achieved with increased electrification of transport and industrial processes. Much more renewable electricity generation will be required, including small scale distributed generation (DG) located within distribution networks, but also more regional grid-scale generation.

The expansion of Ngawha coupled with the improved level of network reliability will make the Far North a more attractive region to invest in. Top Energy sees itself as being in the position to act as catalyst for economic development in the region.

New technologies such as solar photovoltaics (PV), battery storage, electric vehicles (EV), smart metering and automation management systems are expected to have a disruptive impact on the energy market. This may result in EDBs having their own 'system' to operate in conjunction with the Grid.

Being in the "sunny north" makes the Top Energy distribution region a prime candidate for commercial scale PV projects. For example, Lodestone Energy's "Lodestone Two" solar farm, near Kaitaia, is due to start distributing to the network this calendar year. These projects will provide new challenges for Top Energy to manage on its network.

Board overview

The objective of consumer trust ownership is creating long-term value for consumers through the Company. The Trust appoints the directors of the Company and monitors the performance of the director group. Chair Richard Krogh, who has been a director since 2013, is to stand down this June and will be replaced by David Sullivan who has been on the Board since 2018. The Trust has appointed three new Directors (Nicole Anderson, Jon Nichols and Steve Sanderson) to the Board since the last ownership review. The current Board has an appropriate mix of commercial and industry experience.

Trust overview

TECT was formed in 1993 to acquire all of the shares in Top Energy. The Trust's purpose is to hold the shares on behalf of power consumers connected to Top Energy's lines network and to distribute the benefits of share ownership to these consumer beneficiaries as a group. This means that all electricity consumers in Top Energy's network may receive a share of Top Energy's profits, irrespective of which electricity retailer they may purchase electricity from.

Since the last review, TECT has appointed Donna Tukariri as a new trustee, and Yvonne Sharp has remained the Chairperson of the Trust.

TECT's role, on behalf of consumers, is supporting the Company in meeting its objective of being a successful business. To fulfil this purpose, each year TECT negotiates Top Energy's Statement of Corporate Intent (SCI) with directors. The SCI is an integral aspect of ensuring that the Company maintains objectives that align with the Trust's purpose and the process of measuring performance against the SCI is robust.

The trustees are nominated by the public, shortlisted and then selected by a panel comprising of the Members of Parliament for Northland and Te Tai Tokerau and the Chair of the Northland Regional Council. Appointments to TECT are made with reference to capabilities of the existing trustees to ensure an appropriate representation of the shareholders and required skills.

This is a unique aspect to the TECT and the Trust has maintained a core team of trustees throughout the review period. This continuity was considered by all parties interviewed to have been a valuable aspect of the existing ownership model in providing the stability required to execute the Ngawha expansion.

The Company has delivered a major strategic project during the review period as well as maintained effective operations. It has managed to increase the discount to consumers in the latest year to assist with COVID induced financial hardship. The challenges ahead for the Trust and the Company are centred on clear alignment on what value means.

Executive summary

Ownership options

Ownership options available to the Trust range from continued 100% consumer trust ownership through to full distribution of shares. We have considered the advantages and disadvantages to beneficiaries of consumer trust ownership of Top Energy's shares, relative to the distribution or sale of these shares.

Ownership option	Description
100% trust ownership of shares (status quo)	Trust ownership is common practice with over 70% of EDBs in New Zealand operating under it to some degree We also consider variants to the current consumer trust option
Distribution to beneficiaries or sale to the public or external investors of 24.9% or 49.9% of shares	Distribution or sale of 24.9% allows the Trust to retain control over Top Energy's constitution Distribution or sale of 49.9% allows the Trust to retain control
Distribution of 100% of shares to beneficiaries	Where a 100% share distribution occurs, shares are typically on-sold by beneficiaries within a short period, making it possible for an interested party to gain majority control
Sale of 100% of shares to the public or external investors	A sale of 100% of shares would enable the Trust to test the market for interest in the Company and pass the proceeds to beneficiaries

Status quo – Trust ownership

Operating under 100% trust ownership, Top Energy has successfully expanded operations on one of its core businesses and enhanced the capability of the Company during the review period. Current and future Trust beneficiaries have been served well by the Company's execution of its strategy which has enabled it to build its capacity in the wider electricity sector.

The Company has established sufficient financial resourcing to provide full funding for the expansion of Ngawha, while maintaining its income distributions to beneficiaries through line charge discounts and dividends. Top Energy does not have the financial headroom to fund large projects in the near to medium term. The Company operates close to its debt covenants and its financial performance is being impacted by the hedging requirements set out in the financing agreements.

The status quo with regard to the core business ownership, is consistent with meeting the needs of current and future consumer beneficiaries. It is a low cost ownership model, which provides for the local interests of consumers to be reflected in the Company's prices, performance and direction.

Direct alignment of interests between beneficiaries and electricity consumers through a consumer trust structure means both financial and non-financial considerations such as health and safety, cultural relationships and environmental objectives can be balanced.

In the near-term, operating the existing businesses under 100% Trust ownership, means Top Energy may be constrained in responding to new industry opportunities.

If Top Energy were to become capital constrained, partial divestment of Ngawha may be a possible solution.

Executive summary

Conclusion

Operating under the trust model, Top Energy has increased its asset base by 80% during the review period. It has delivered a major project in the Ngawha expansion, involving numerous challenges, successfully and ahead of schedule. It is evident from our interviews that this is a source of great pride for the Trust, the Board, and Management. It is also evident that Ngawha is something of which the people of the Far North are also proud. This is a commendable achievement which clearly aligns with all four pillars of the SCI.

The Company can be expected to continue to perform in this way if the Trust maintains clear expectations for the Company which balance financial and non-financial considerations, and the interests of current and future beneficiaries.

At the same time as delivering a major project, Top Energy has continued to strive for improved performance in its network and has made notable progress through strategic investment in data management along with consistent expenditure in maintenance and renewals.

Although financing Ngawha on its own has pushed Top Energy to its financial capacity limit, there is every expectation that this investment will continue to benefit the consumers of electricity in the region for the long term in a number of ways.

A distribution of shares to beneficiaries would raise inter-generational equity issues, with value passed to current beneficiaries at the expense of future beneficiaries. Customers would lose future distributions and access to future growth in the value of the Company, and may have less influence over future prices and quality of service as a result.

The Trust's governance role allows it to represent the interests of the beneficiaries through the appointment of directors and contributing to the annual SCI. The Trust can encourage investment and initiatives which deliver additional value, while allowing the Company the flexibility to pursue new opportunities consistent with its wider strategic objectives.

3

Top Energy performance

Group overview

Top Energy

Top Energy is the electricity generation and lines network company which distributes power to more than 32,500 electricity consumers in the Far North of New Zealand.

Electricity generation

Top Energy is the sole shareholder in Ngawha Generation Ltd, which owns and operates a 57MW geothermal power station in Ngawha, slightly east of Kaikohe. The station's output is fed into Top Energy's network and then connected to the National Grid, via Top Energy's sub-station near Kaikohe. The Ngawha plant has recently been expanded from 25MW, and now generates more electricity than the average demand in the region and meets peak demand over 95% of the time.

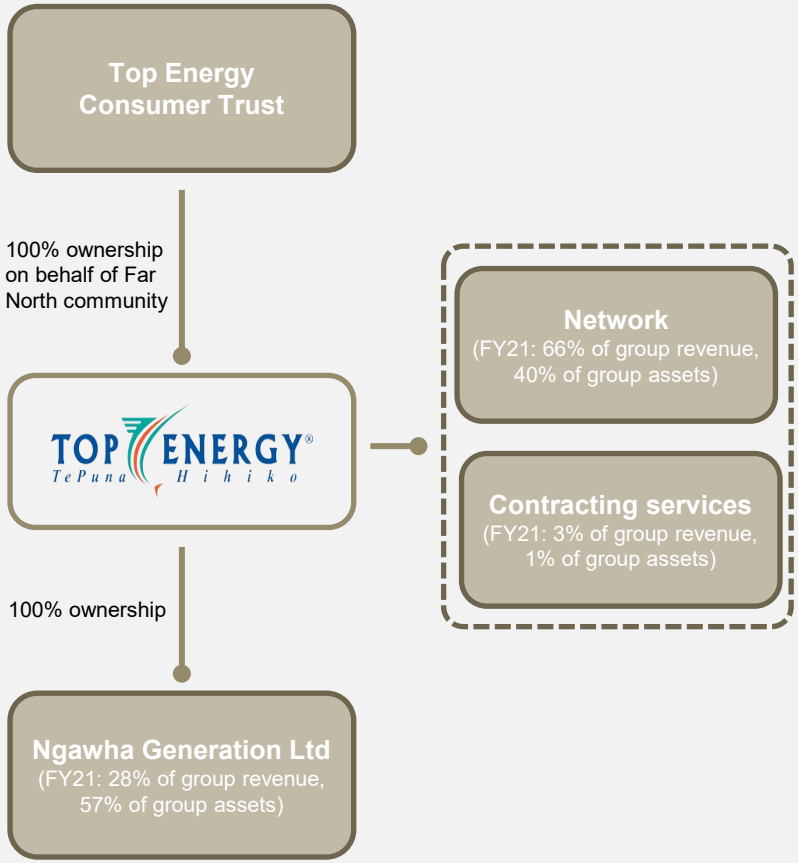
Electricity distribution

Top Energy owns the distribution network servicing all of the Far North region. It also owns the (former) transmission line from Kaikohe to Kaitaia. It is located at the northern most point of the National Grid.

Contracting

Top Energy's inhouse contracting team is responsible for ensuring the safety and reliability of Top Energy's network. The team provides construction, maintenance and vegetation management services. It also provides services to external parties.

Figure 1: Top Energy structure



Source: Top Energy, PwC analysis

Network overview

Overview of Top Energy's network

Top Energy owns over 4,000km of lines from Hukerenui in the south, to Te Paki in the north and spanning from the east to the west coast. The southern region of the network is supplied from the substation at Kaikohe and the northern region is fed from a single transmission line from Kaikohe to Kaitaia.

Due to Top Energy's consumer ownership model with the trustees being appointed rather than elected, it is currently non-exempt from the Commerce Commission's price-quality regulation. Top Energy has to comply with a regulated revenue cap and the network reliability standards. The latest Default Price Path (DPP) reset has caused Top Energy's allowable revenue to drop substantially in the last year of the review period.

As an electricity market participant, Top Energy is subject to the Electricity Industry Participation Code which regulates the role of local distribution networks within the electricity market, including pricing. The utilisation of the network is heavily weighted towards small consumers, representing 99% of connections and around 80% of maximum demand. Average annual consumption per ICP is the one of the lowest in the country at 9,800 kWh. Top Energy's pricing structures are therefore strongly focused on the needs of the residential groups. There are few large consumer connections.

Current government policy settings will increase the electrification of transport and industrial processes throughout New Zealand in order to meet net carbon-zero targets by 2050. This means that demand for electricity across New Zealand, including the Far North region, is expected to increase for the foreseeable future.

The Top Energy network already has the second highest penetration of solar PV in the country at 2.7% of connections (4MW). Clustering of PV, particularly in the eastern (more affluent) part of the network, is already posing issues. Commercial scale generation for the purpose of export, some of which is planned to come online this year, is expected to cause capacity constraints at all levels in the future, including to the Grid to the south of Kaikohe.

Top Energy is set to participate in a pilot programme along with Transpower and Northpower to create a Renewable Energy Zone (REZ) in the north. This may open up the region to more growth and investment by facilitating the use of local renewable generation.

Table 1: Network characteristics (FY21)

Number of connections (ICPs)	32,877
Circuit length (km)	4,088
Connection point density (ICP/km)	8.0
Energy intensity (MWh/ICP)	9.7
Opening RAB ($m)	280.0

Table 2: Network growth (FY17-FY21)

Number of connections (ICPs)	+4.8%
Electricity delivered (kWh)	-1.2%
Installed capacity (MVA)	+0.6%
Circuit length (km)	+1.4%
Regulatory asset base (RAB)	+24.7%

Ngawha overview

Overview of Ngawha Generation Ltd (Ngawha)

In 2016 Top Energy received resource consents to construct two new power stations (OEC4 and OEC5) at its existing Ngawha generation site, giving a total potential capacity for the site of 75MW.

In July 2021, the Ngawha expansion (OEC4) was officially opened, bringing an extra 32MW of generation online, taking the total capacity of the plant to 57MW. The plant now supplies most of the electricity used by consumers on Top Energy's network, meeting average daily demand but not maximum demand.

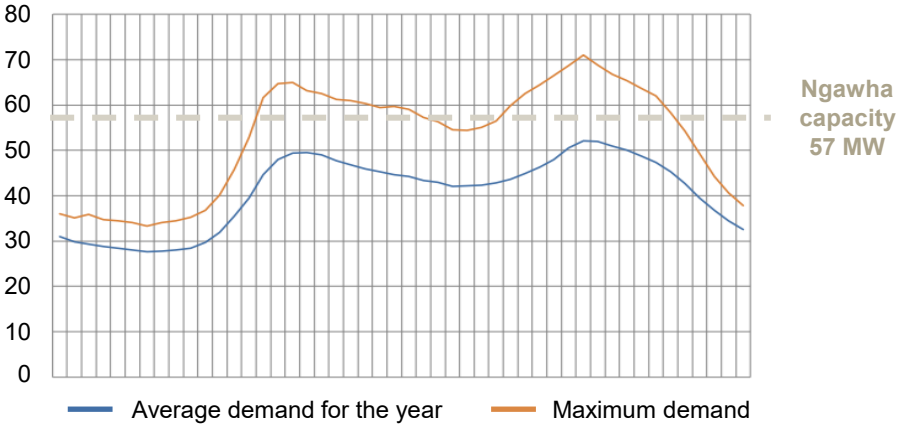
Wholesale electricity prices have been increasing over the review period and this will be reflected in increased retail energy prices to consumers. The impact of the increased generation can be seen in the reduction of the differential in wholesale electricity price between the Kaikohe GXP servicing the Top Energy network and the next GXP to the south at Maungatapere.

In a region with high energy poverty, Top Energy's participation in generating and selling wholesale electricity will reduce price risk to retailers, making the region more attractive for smaller retailers to offer pricing into. This should increase retail competition.

Expansion of generation capacity (OEC5) is still possible under the resource consent but will require careful monitoring of the market to determine if this is beneficial to Top Energy and its owners. Grid capacity constraints to the south are likely to make it impossible to increase export from Ngawha at times, unless transmission lines are upgraded. However, maximum demand in the region is forecast to continue to increase and there is also a potential for stepped up growth from large-scale projects like the planned Ngawha Industrial Park.

Figure 2: Demand by half hour period, YE September 2019

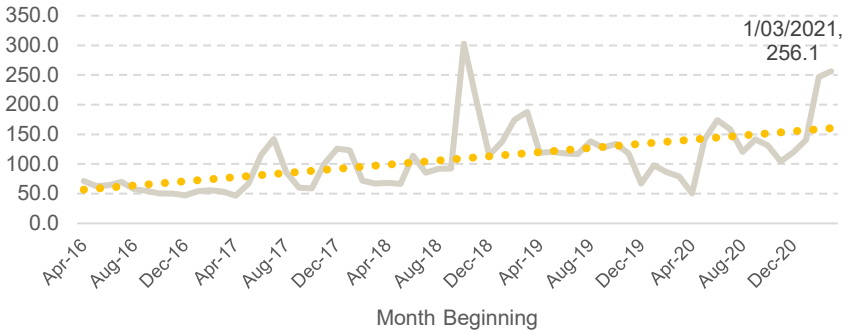
MW



Source: Top Energy Pricing Methodology 2021

Figure 3: North Island Average Monthly Electricity Price

NZ$/MWh



Group highlights

Ngawha expansion

The universal response to our interview question on highlights from the last five years was the Ngawha expansion. There is immense pride from a community perspective but also commercial and relationship perspective.

The complexities of delivering this project were navigated successfully and all parties interviewed are of the view that each played their role effectively. Not only has this been a commercial success for the Company and its owners, but it has increased engagement with iwi, and improved capability for economic development in the Far North.

Consumer awareness

Top Energy has a strong local brand. Consumer focus groups have shown that it is perceived as being highly responsive in emergency situations, has solid community involvement and contribution, and is highly visible in the community.

Investment in a Customer Relationship Management (CRM) system has heralded an increased focus on customers and all interactions are now tracked. This has improved positive feedback about the customer experience.

The upside of prices being high in the region is that consumers are more aware of the factors which drive prices and are engaged with the concept that use and pricing are linked. This engagement will continue to be an asset to Top Energy as it moves through the transformation required over the coming decades as the country moves towards net carbon zero.

Group highlights

Consumer discounts

Returns to shareholders, in the form of discounts issued to Top Energy consumers have been maintained over the review period, with a notable increase in FY21. The discount was brought forward to help deal with COVID impacts on winter bills. It was also increased to mitigate impacts of energy price increases. This clearly demonstrates commitment by the Company to fulfilling their mandate of lowering the cost of energy to the Far North consumer.

Improved safety culture

An objective in the SCI to improve the safety culture at Top Energy has been met with a commendable drop in lost time injuries (LTI) over the review period. The Group has met the newly introduced SCI targets for Total Recordable Injury Frequency Rate (TRIFR) two out of the three years since these were set. In FY20 the Group began including contractors in these measures and this demonstrates inclusive approach to the community workforce.

Network reliability

Top Energy has continued to improve the reliability of its network. There has been consistent investment in renewals. The investment in an Advanced Distribution Management System (ADMS) in FY20 should aid in improving this further.

The normalised System Average Interruption Duration Index (SAIDI) has decreased from 465 minutes at the beginning of the review period to 433 in FY21. This is a significant reduction in the duration of network interruption.

Table 3: Lost time injuries (LTI)

	FY17	FY18	FY19	FY20	FY21
Lost time injuries (LTI)	3	0	0	0	1

Figure 4: Discounts to consumers
NZ$m

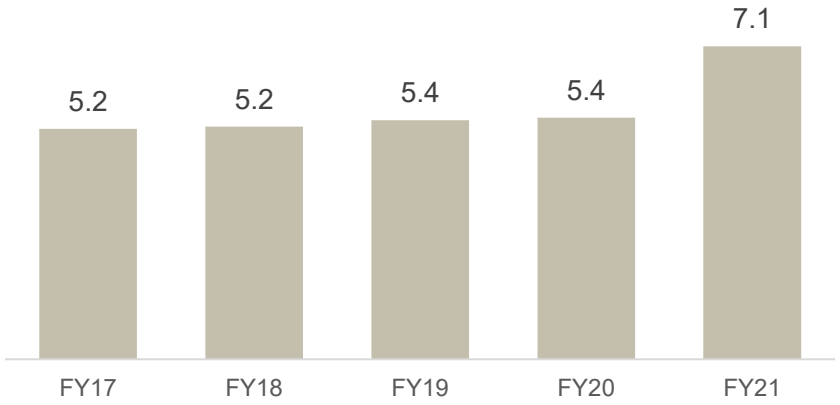
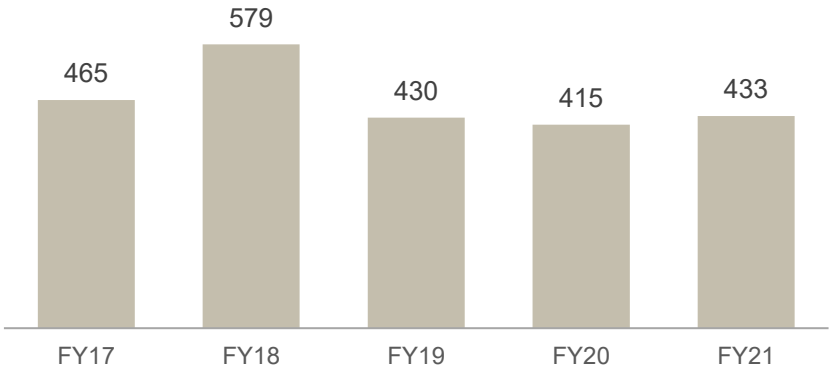


Figure 5: Normalised network interruption duration (SAIDI)
Minutes



Group financial performance

Financial performance

The revenue growth of Top Energy has been strong over the review period, with a minor pullback in FY21 due to a drop in electricity line revenue. The lines revenue decrease was primarily due to the drop in regulated weight average cost of capital (WACC) and out of the Company's control. This was partially offset by an increase in sales from electricity generation.

Top Energy has seen similarly strong growth in EBITDAF over the review period, but again shows the FY21 decrease in electricity line revenue flowing through to cash earnings. Top Energy's net profit after tax in FY21 was significantly impacted by the accounting treatment of derivative instruments but this does not reflect a cash loss.

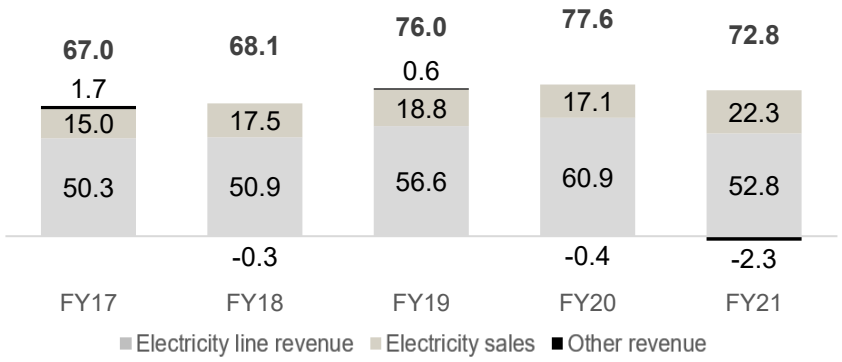
The Company entered into financial risk management positions (through the purchase of derivative products) to meet the financing requirements of delivering the Ngawha expansion on its own.

Carbon costs are set to play an increasing role in financial performance, due the rising cost of carbon and the increased emissions from Ngawha. The Company is taking steps to manage this both financially and in terms of its sustainability goals.

The timing of these factors coinciding has not been ideal but should not be considered reflective of the management of the Company.

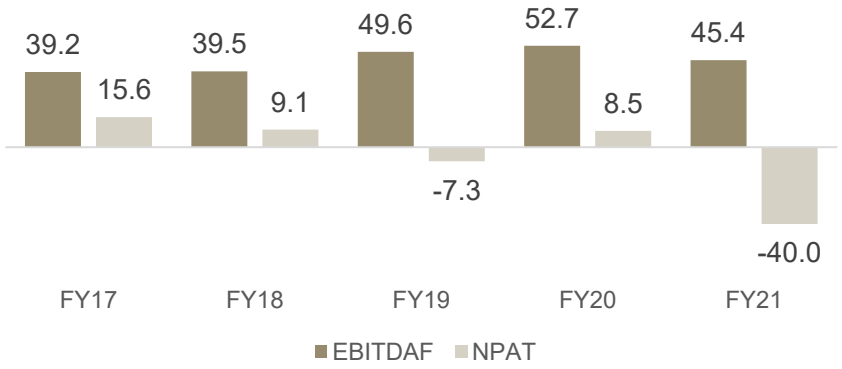
Top Energy's financial performance is presented overleaf in detail.

Figure 6: Top Energy revenue
NZ$m



Note: 1) Other revenue includes network line charge discount

Figure 7: Top Energy EBITDAF and NPAT (before discounts)
NZ$m



Group financial performance

Table 4: Top Energy statement of financial performance

NZ$000	31 March 2017	31 March 2018	31 March 2019	31 March 2020	31 March 2021
Electricity line revenue	50,319	50,906	56,579	60,858	52,768
Network line charge discount	(5,191)	(5,245)	(5,386)	(5,444)	(7,054)
Capital contributions	1,017	1,205	2,848	2,092	2,197
Electricity sales	14,968	17,494	18,767	17,131	22,328
Contracting services	3,687	2,445	2,907	2,762	2,417
Interest	-	-	-	-	-
Dividends	-	-	-	-	-
Other revenue	2,203	1,264	274	190	135
Operating revenue	**67,003**	**68,069**	**75,989**	**77,589**	**72,791**
Raw materials and consumables used	(3,027)	(4,463)	(2,673)	(3,242)	(2,277)
Employee benefits expense	(14,879)	(14,469)	(13,305)	(14,217)	(14,120)
Other expenses	(9,839)	(9,359)	(10,672)	(7,972)	(10,481)
Transmission charges	(5,204)	(5,156)	(5,090)	(4,855)	(4,644)
Impairment charges	-	(402)	-	-	-
Operating expenses	(32,949)	(33,849)	(31,740)	(30,286)	(31,522)
Construction related COVID-19 expenses	-	-	-	-	(2,931)
EBITDAF	**34,054**	**34,220**	**44,249**	**47,303**	**38,338**
Depreciation and amortisation	(15,423)	(16,856)	(17,412)	(18,786)	(19,427)
Finance costs	(8,513)	(8,367)	(7,878)	(6,940)	(7,787)
EBTF	**10,118**	**8,997**	**18,959**	**21,577**	**11,124**
Fair value gains (losses) on financial assets	6,410	(1,538)	(34,536)	(15,284)	(73,723)
Profit (loss) before income tax	**16,528**	**7,459**	**(15,577)**	**6,293**	**(62,599)**
Income tax credit (expense) from continuing operations	(4,536)	(1,760)	5,152	(1,199)	18,258
Profit (loss) from continuing operations	**11,992**	**5,699**	**(10,425)**	**5,094**	**(44,341)**
Margin %	*17.9%*	*8.4%*	*-13.7%*	*6.6%*	*-60.9%*
Profit (loss) from discontinued operations	-	20	(244)	-	-
Profit (loss) for the year	**11,992**	**5,719**	**(10,669)**	**5,094**	**(44,341)**
Margin %	*17.9%*	*8.4%*	*-14.0%*	*6.6%*	*-60.9%*

Source: Top Energy annual reports, PwC analysis

Group financial position

Financial position

Top Energy has increased its asset base by 80% over the review period. This is mainly due to the commissioning of OEC4 but the Regulatory Asset Base (RAB) also increased from $224.6m at the beginning of FY17 to $302.2m at the close of FY21.

The Ngawha expansion has seen liabilities more than double over the review period and paying down debt appears to be a priority for the Company in the near future. However, the risk appetites of the parties interviewed vary and this may pose some challenges for the ownership model in the coming years.

Top Energy's interest coverage ratio was impacted significantly in FY21 due to increased borrowings associated with the Ngawha expansion and a decrease in revenue. This reflects a transitional period where costs of a project were incurred, but associated revenues have not yet fully matured. A full year of sales of electricity should ameliorate this with forecast EBITDAF for FY22 at around 25% up on FY21.

Equity has been impacted by the fair value accounting adjustment of financial instruments in FY21. These instruments were to cover interest rate and wholesale electricity price risk, both of which moved against the held position.

Figure 8: Top Energy interest coverage ratio
EBITDAF/Finance costs

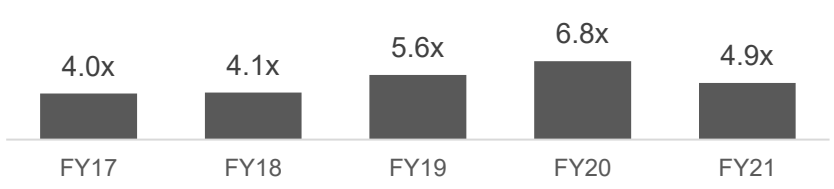
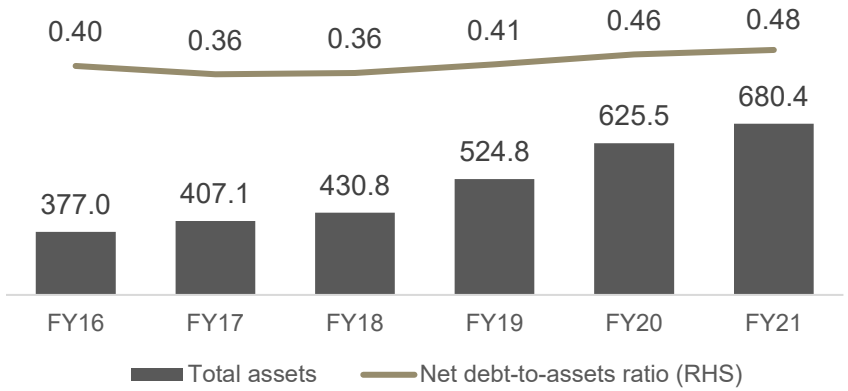
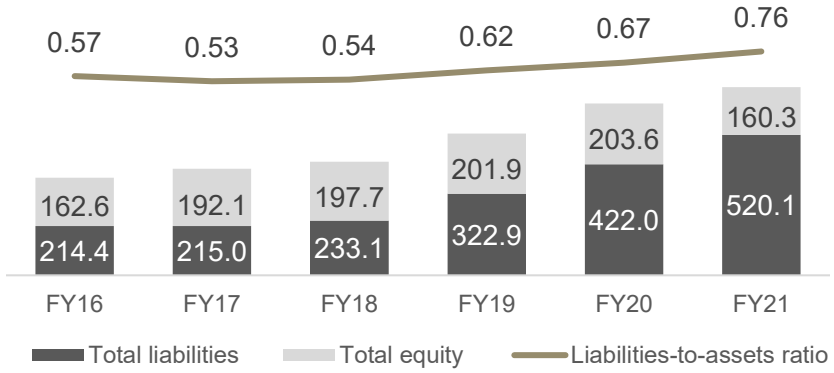


Figure 9: Top Energy assets and net debt-to-assets ratio
Total assets NZ$m



Note: Net debt to asset ratio: (interest bearing debt – cash) / (total assets - cash)

Figure 10: Top Energy liabilities and equity
NZ$m



Group financial position

Table 5: Top Energy statement of financial position

NZ$000	31 March 2017	31 March 2018	31 March 2019	31 March 2020	31 March 2021
Cash and cash equivalents	83	150	203	101	145
Receivables	7,577	7,915	8,643	9,942	12,142
Inventories	366	1,512	1,411	1,817	2,025
Derivative financial instruments	1,529	1,999	2,647	1,461	124
Other current assets	259	5,388	153	770	630
Total current assets	**9,814**	**16,964**	**13,057**	**14,091**	**15,066**
Property, plant & equipment	384,954	402,536	494,166	585,588	637,404
Intangible assets	9,770	10,746	17,531	19,498	22,588
Derivative financial instruments	363	558	12	627	-
Right-of-use lease assets	-	36	-	5,745	5,342
Other non-current assets	2,237	-	-	-	-
Total non-current assets	**397,324**	**413,876**	**511,709**	**611,458**	**665,334**
Total assets	**407,138**	**430,840**	**524,766**	**625,549**	**680,400**
Payables	8,391	13,863	13,896	20,448	25,156
Interest bearing liabilities	1,576	1,688	1,582	1,737	4,718
Current tax liabilities	686	1,470	372	2,240	-
Derivative financial instruments	404	879	9,824	3,901	58,667
Other current liabilities	478	384	379	792	811
Total current liabilities	**11,535**	**18,284**	**26,053**	**29,118**	**89,352**
Interest bearing liabilities	143,760	155,100	212,710	286,650	325,312
Derivative financial instruments	9,356	11,082	36,775	57,410	74,404
Deferred tax liabilities	50,341	48,664	47,330	43,337	25,983
Right-of-use lease liabilities	-	-	-	5,446	5,051
Total non-current liabilities	**203,457**	**214,846**	**296,815**	**392,843**	**430,750**
Total liabilities	**214,992**	**233,130**	**322,868**	**421,961**	**520,102**
Net assets	**192,146**	**197,710**	**201,898**	**203,588**	**160,298**
Current ratio	*0.85*	*0.93*	*0.50*	*0.48*	*0.17*
Quick ratio	*0.82*	*0.85*	*0.45*	*0.42*	*0.15*
Net debt to asset ratio	*35.7%*	*36.4%*	*40.8%*	*46.1%*	*48.5%*

Source: Top Energy annual reports

SCI targets

SCI targets

The SCI is agreed annually between the Trust and the Board, and outlines the objectives for the Company for the next three years. The objectives are supported by four strategic pillars:

- Vertical Integration
- Future Investment
- Maintaining Our Identity
- Trusted Source

The SCI includes target metrics for key performance outcomes across the business. The SCI objectives are categorised into network related metrics, non-network related metrics, group related metrics and non-financial operational performance metrics.

In the last few years the SCI has begun to include qualitative metrics to expand the concept of what 'value' to shareholders means. This includes adding measures for health and safety, cultural impact and environmental impact.

This demonstrates a strategic move forward in terms of the ownership model as it distinguishes it from a traditional ownership model which focuses on financial measures of value to shareholders. The intent of doing this was clear from interviews and appears to be wholly supported.

A summary of the performance against the SCI targets over the review period is included overleaf.

Group

As a group the Company has met its financial SCI targets consistently over the review period. It has also met its newly introduced cultural and environmental targets since these have been implemented.

The safety culture target (TRIFR) appears to have been impacted by increased activity in commissioning Ngawha. Although the target was not met in one of the three years, it was noted that in general the injuries sustained were moderate. The LTI numbers (which aren't explicitly an SCI measure) demonstrate clear improvement in the Company's approach to the wellbeing of its employees and contractors.

Network

Top Energy met all but one of its financial network SCI targets during the review period, falling shy by a fine margin of its 'Earnings before Interest and Tax as a percentage of Total Tangible Assets' target in FY18.

The quality standards targets have not been met more often than they have. That said, the SAIFI target has been reducing over the review period and there is a trend downward in the achieved result even if it does not meet the target. So the target appears to be driving the desired result. It is worth noting that all network quality measures were below the regulatory limits through the review period, which shows the Company and the Trust are striving to go beyond meeting the regulations.

Generation

The generation business has had patchy results in meeting its SCI targets, which is not unexpected given the period of significant change. It would be expected that this would improve over the coming years.

Performance against SCI targets

Table 6: Top Energy SCI performance

Measure	2017			2018			2019			2020			2021		
	SCI	Actual	Achieved	SCI	Actual	Achieved	SCI	Actual	Achieved	SCI	Actual	Achieved	SCI	Actual	Achieved
Shareholder's Funds to Total Assets	1:2.32	1:2.33	⦸	1:2.24	1:2.39	⦸	1:2.51	1:2.63	⦸	1:3.1	1:2.9	✓	1:3.1	1:3.1	✓
Network Business															
Earnings before Interest and Tax as a percentage of Total Tangible Assets	7.1%	7.5%	✓	6.3%	6.2%	⦸	7.2%	9.5%	✓	9.1%	10.1%	✓	4.5%	5.9%	✓
Net Profit after tax, as a percentage of Average Shareholder Funds	7.7%	8.4%	✓	6.1%	6.4%	✓	7.9%	12.2%	✓	11.0%	12.6%	✓	3.7%	5.8%	✓
Return on Investment	6.8%	7.0%	✓	6.1%	6.1%	✓		*na*			*na*			*na*	
Non-Network Business															
Earnings before Interest and Tax as a percentage of Total Tangible Assets	6.5%	6.3%	⦸	7.4%	7.6%	✓	6.6%	6.4%	⦸	3.7%	4.1%	✓	3.2%	3.1%	⦸
Net Profit after tax, as a percentage of Average Shareholder Funds	6.3%	4.9%	⦸	8.4%	9.3%	✓	22.4%	16.1%	⦸	11.5%	12.9%	✓	4.7%	9.7%	✓
Group															
Net Profit after tax, as a percentage of Average Shareholder Funds	7.2%	7.4%	✓	7.0%	7.3%	✓	10.9%	11.6%	✓	10.0%	11.8%	✓	10.0%	11.8%	✓
Return on Investment	6.1%	6.2%	✓	5.8%	5.8%	✓		*na*			*na*			*na*	
SAIFI	4.2	4.8	⦸	4.9	4.9	✓	4.9	3.6	✓	4.2	4.5	⦸	3.5	3.9	⦸
SAIDI	350	401	⦸	345	483	⦸	390	352	✓	318	366	⦸	379	363	✓
Total Recordable Injury Frequency Rate		*na*		*na*	1.5	*na*	3.6	2.1	✓	3.6	4.4	⦸	3.6	2.7	✓
Maintain consent compliance without remedy		*na*			*na*			✓			✓			✓	
Maintain Cultural Monitoring Plan without remedy		*na*			*na*			✓			✓			✓	

Source: *Top Energy annual reports, PwC analysis*

Network revenue, pricing and returns

Revenue

Target revenue is set from forecast costs and is subject to a revenue cap set by the Commerce Commission. A material factor in determining allowable revenue is the WACC determined by the Commerce Commission. The change in WACC for Default Price Quality Path (DPP3) resulted in a notable drop in lines revenue in FY21.

Prices

Prices are set to recover forecast revenue. Revenue is allocated across consumer groups with various pricing options, each with a fixed and variable component. Top Energy has recently introduced optional time of use (TOU) pricing for residential customers to better reflect the costs of network use. Prices have decreased in FY21 but are still among the highest in the country. Engaging with customers on how they can change their use to reduce costs will be key in improving affordability for both them and the network.

Return on investment (ROI)

The WACC was revised down significantly from 7.19% to 4.57% from DPP2 to DPP3. The main reason being the reduction in the risk-free rate. The timing for Top Energy and its owners was not ideal. However its achieved return on investment (ROI) has been stronger than median disclosed for other EDBs in all but FY21, where it was similar.

Table 7: Lines charge revenue

NZ$000	FY17	FY18	FY19	FY20	FY21
Lines revenue	50,319	50,906	56,579	60,858	52,768
Transmission charges	(5,204)	(5,156)	(5,090)	(4,855)	(4,644)
Distribution revenue	45,115	45,750	51,489	56,003	48,124
Line charge discounts	(5,191)	(5,245)	(5,386)	(5,444)	(7,054)
Net distribution revenue	**39,924**	**40,505**	**46,103**	**50,559**	**41,070**

Figure 11: Weighted average line charge per customer

Cents/KWh

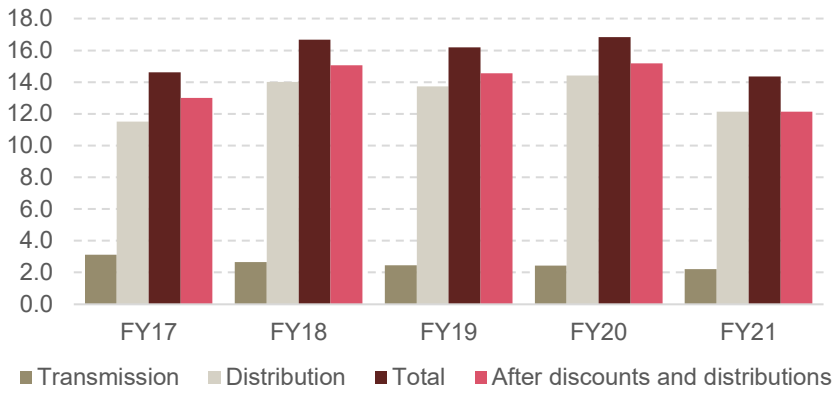
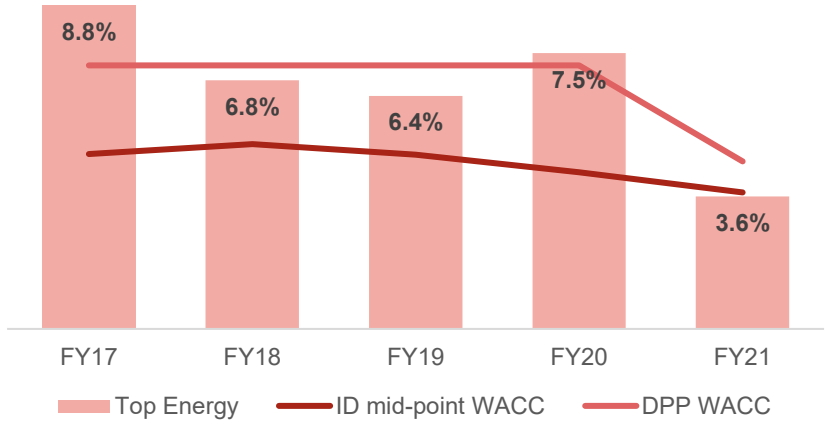


Figure 12: ROI and regulatory WACC benchmarks



**Discounts include posted and discretionary line charge discounts*

Network capex

Capex

There was a noticeable spike in capex in FY20 for a number of reasons:

- cost escalations and phasing variances for the Ngawha Generation 110kV line and substation interconnection project
- diesel generators purchased to increase reliability and back up supply in the Northern region
- a new ADMS system for operations.

The increase was forecast but not to the level of actual expenditure.

Variance to forecasts in FY20 and FY21 were generally due to project scheduling issues related to Ngawha and to COVID.

Forecast capex over the next five years is at FY17 levels and indicates a conservative approach in the near term. This is consistent with our interviewees' views that paying down debt was a priority.

Figure 13: Forecast capex
NZ$M

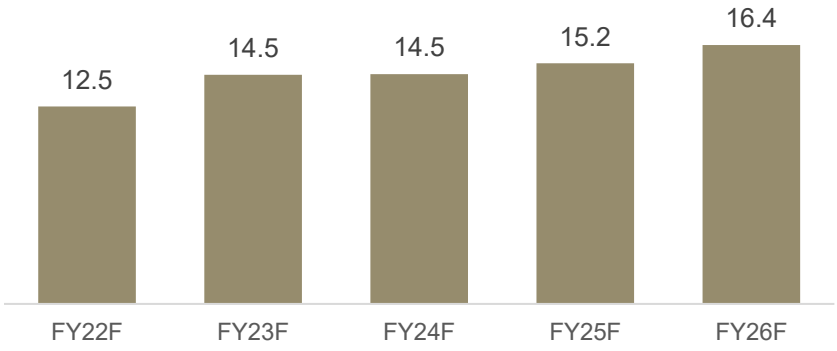


Figure 14: Actual vs forecast capex
NZ$m

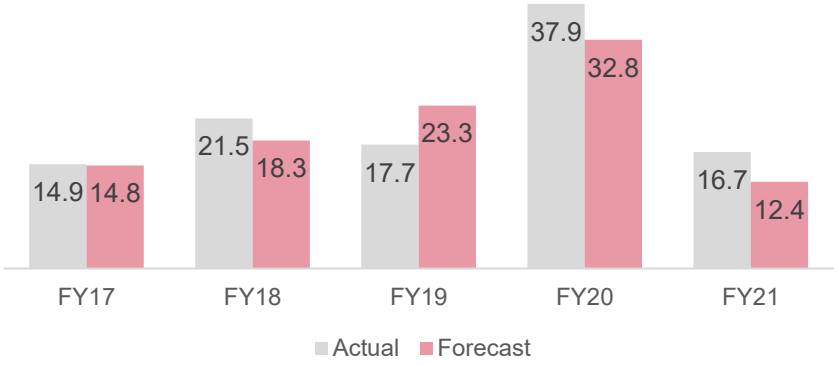
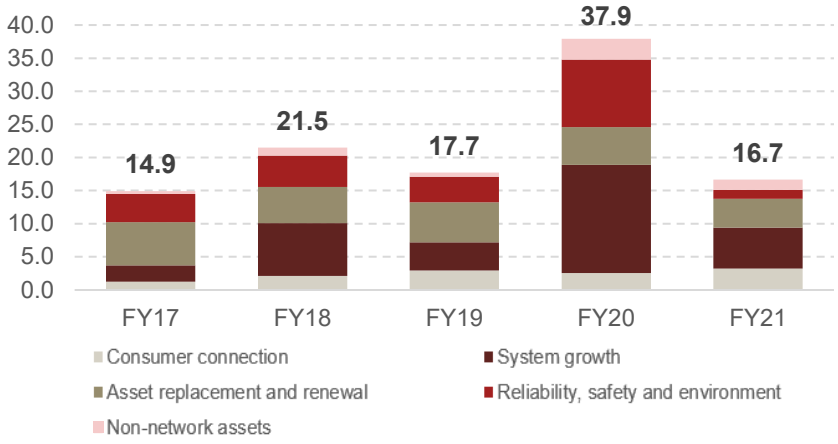


Figure 15: Capital expenditure by category
NZ$m



Network opex and contracting

Opex

Network opex has been reasonably flat throughout the review period. Consistency in year-on-year expenditure (particularly emergency maintenance) and low variance between actuals and forecast costs is demonstrative of improving asset management practices and is consistent with improved network reliability that is being observed.

Non-network opex increased substantially in FY20. This was due to increases in both business and network/system support.

Contracting

The inhouse contracting team at Top Energy provide construction, maintenance and vegetation management services. They also provide these services to external parties which generates a small amount of revenue.

Figure 16: Actual vs forecast opex
NZ$m

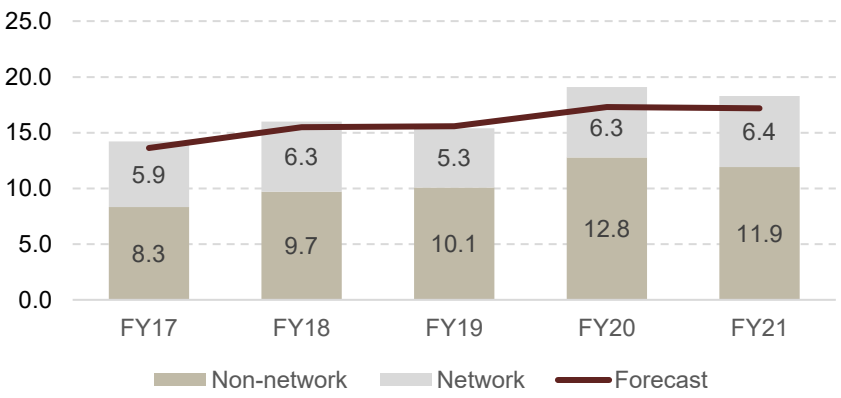


Figure 17: Network opex by preventative, emergency split
NZ$m

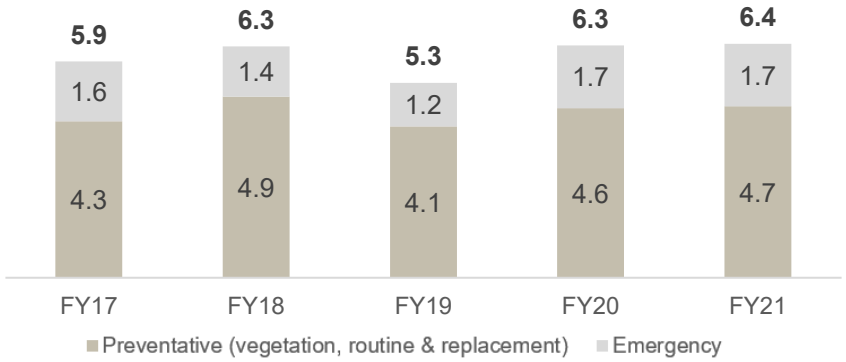
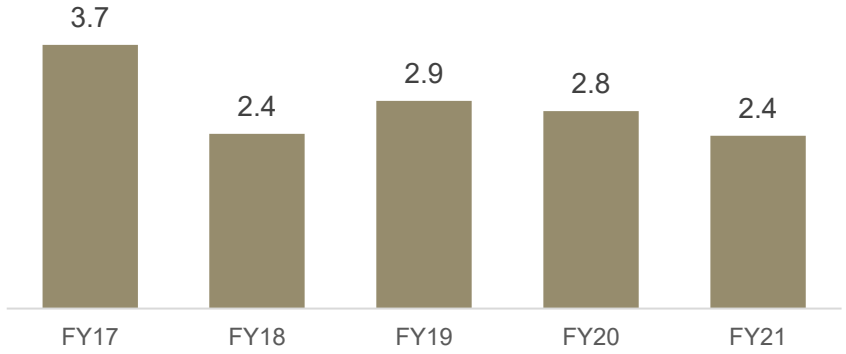


Figure 18: Top Energy contracting revenue
NZ$m



Regulatory asset base

Regulatory asset base (RAB)

The RAB has increased in value by 35% over the review period. Much of this can be attributed to newly commissioned 110kV line connecting Ngawha to the Kaikohe GXP. The average remaining asset life has also increased due to the investments made over the period.

The implementation of the ADMS represented a material investment in non-network capex and will likely result in a reduction in future opex.

Forecast ICP growth is moderate and in line with industry averages. Forecast capex for the next five years would indicate that there will be no significant changes to the RAB over that period. However, this may change if Top Energy becomes involved with the proposed Renewable Energy Zone (REZ) pilot or a similar intensive growth initiative.

The RAB started out the review period representing 58% of the Group's total assets. At the close of the period the RAB was around 44% of the Group's total assets. Ngawha is now the larger component of the total asset base.

Figure 19: Weighted average remaining asset life
Years

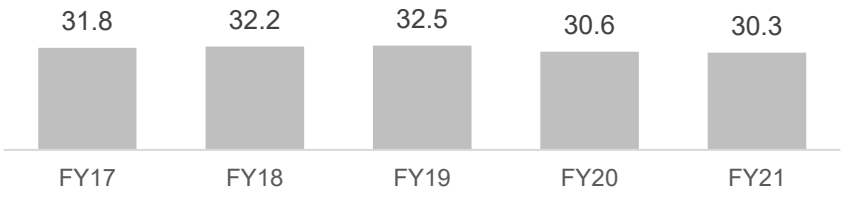


Figure 20: RAB waterfall (FY17-FY21)
NZ$m

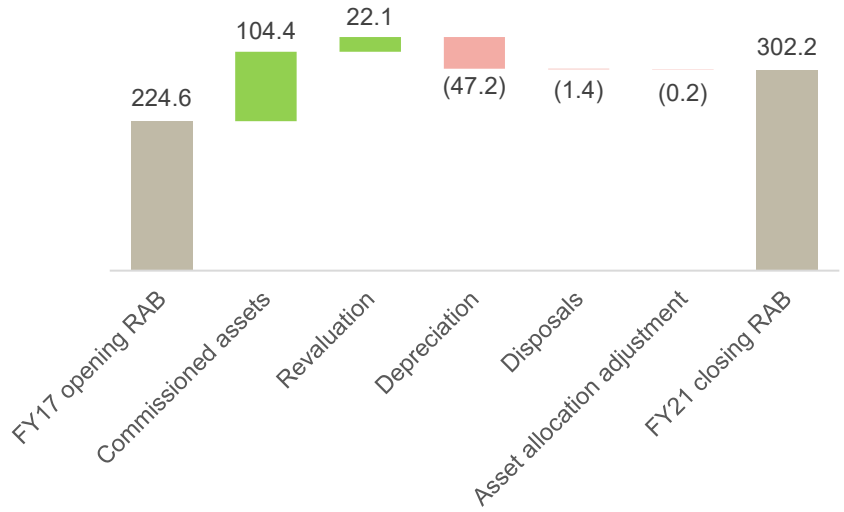
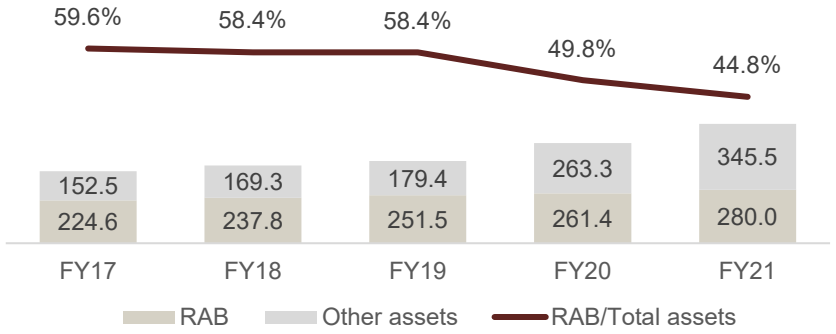


Figure 21: Top Energy RAB-to-total assets ratio (FY17-FY21)
NZ$m



Network reliability

SAIDI and SAIFI

SAIFI (interruption frequency) and SAIDI (interruption duration) are common industry measures for electricity network reliability.

Although Top Energy is still experiencing considerable reliability issues, there has been definite improvement over the review period.

Fluctuations in unplanned outages are generally expected as this measure is influenced by external events, such as bad weather or third party interference on the network. These events are largely outside of the control of a network owner and may result from vegetation or equipment failures.

Continued focus on maintenance activities and the ADMS should see these results continuing to improve.

Interruption rate

The interruption rate increased steadily over the previous review period (FY12-FY16), as shown below. Although there has been a minor increase this period, the rate appears to have stablised.

Figure 22: Network interruptions per 100km

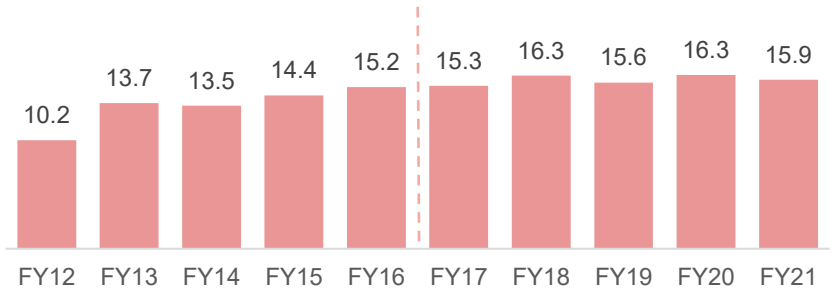


Figure 23: Network interruptions (SAIFI)

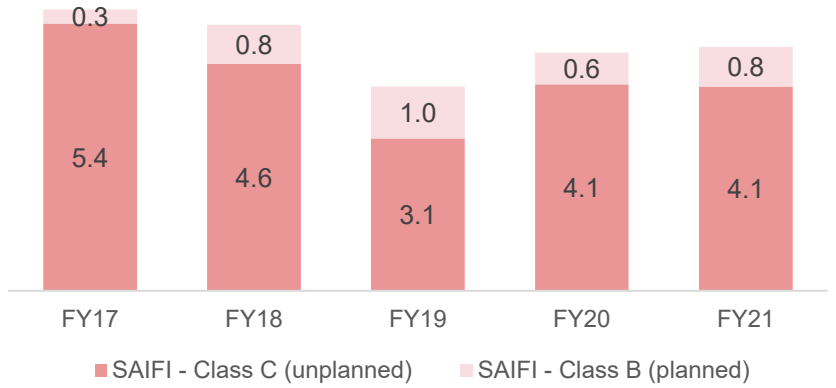
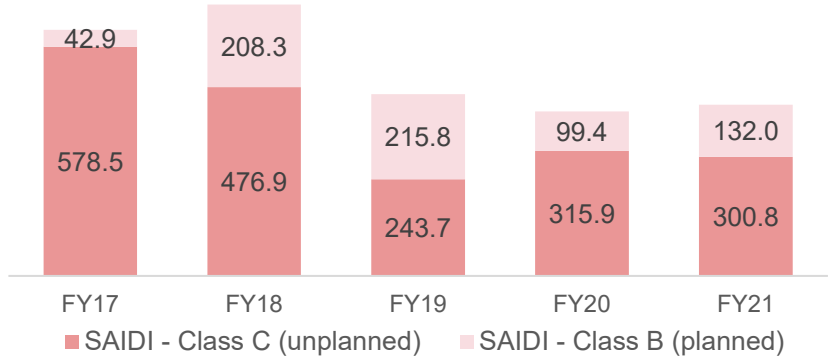


Figure 24: Network interruption duration (SAIDI)
Minutes



Top Energy generation performance

Revenue

Ngawha's revenues have increased over the review period due to the expansion in generation capacity which started to have an impact last financial year. Wholesale electricity prices also increased substantially but these are out of Top Energy's control. Moreover, Top Energy had hedge contracts in place to reduce the risk in financing the Ngawha expansion and did not fully benefit from these increased prices. From FY17-FY21, revenue from electricity sales grew around 50%.

Benefits

Bringing OEC4 online has had a notable downward impact on the wholesale price differential between the Kaikohe GXP and the Maungatapere GXP directly to the south. This will be due to the reduction in transmission losses and other transmission risks to the south of the region.

Costs

Operating expenses have not been significantly impacted by the Ngawha expansion and profitability should therefore be positively impacted by a full year of increased electricity sales.

Ngawha is the 2nd highest carbon emitter of all geothermal plant in New Zealand. The Group will need to balance out the increased emissions associated with increased generation with other activities or face the increased financial costs of these emissions.

Outlook

There is still further generation consented for the site at Ngawha (OEC5). There are investment, capital structure, ownership, regulatory, network, transmission and market issues which all need to be considered before undertaking any further expansion. This decision will be even more complex than OEC4.

Figure 25: Price differential MPE - KOE

NZ$

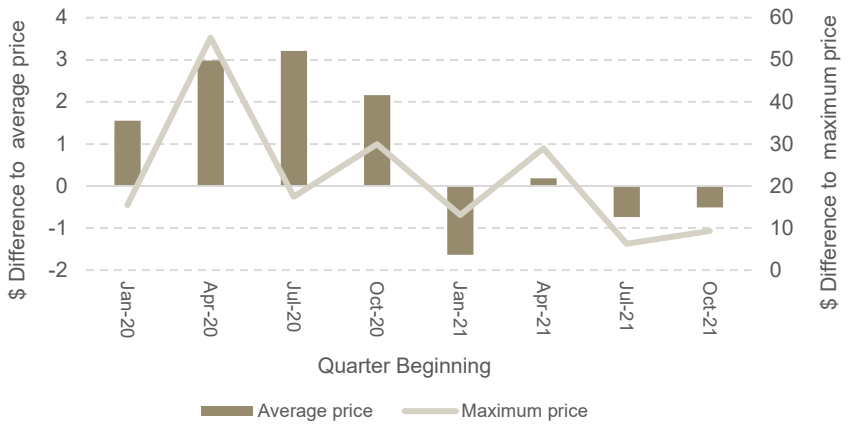
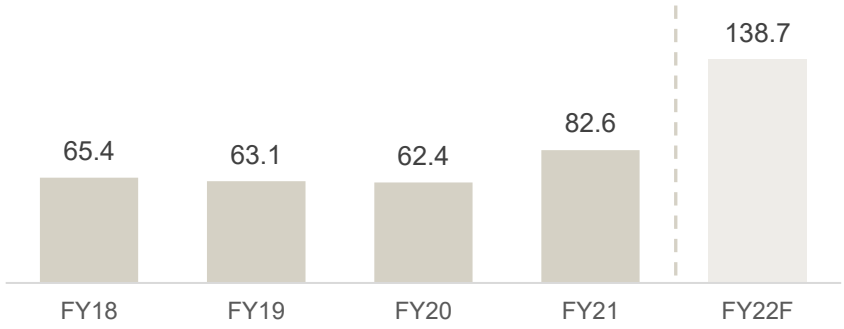


Figure 26: Top Energy carbon emissions

(tCO_2e 000s)



4

Comparative review of Top Energy's EDB

Comparative review

Top Energy and its peer group

We have benchmarked Top Energy's electricity network business performance against other EDBs using regulatory reporting information.

Profits, price, expenditure levels and network reliability have been considered in our comparative performance assessment.

We have placed Top Energy in a comparator group with seven other EDBs. We also present performance against the industry average.

We believe when comparing the performance of EDBs in New Zealand, it is appropriate to group networks by the following indicators:

- network density (the ratio of customer connections per circuit kilometre)
- total size of the network (the total number of customer connections to the network).

We have therefore chosen networks of a similar size and density, as illustrated opposite. Top Energy is larger than the median of the group, and has a slightly higher connection density.

The peer group includes two EDBs (MainPower New Zealand and Marlborough Lines) which are consumer-owned and are therefore exempt from price-quality regulation.

As illustrated opposite, Top Energy's network is predominantly rural overhead reticulation. The peer group is made up of networks servicing largely rural areas, with some smaller urban centres, and a proportion of more remote terrain.

Table 8: Top Energy peer group

EDB	ICP	ICP/km
Horizon Energy Distribution	25,416	9.8
MainPower New Zealand	42,117	8.2
Top Energy	32,877	8.0
Marlborough Lines	26,426	7.8
Alpine Energy	33,700	7.7
Eastland Network	25,783	6.5
EA Networks	20,001	6.4
The Lines Company	23,841	5.5
Peer Median	26,104	7.8
Industry Average	75,599	12.5

Table 9: Top Energy peer group

	Underground (% of total circuit length)	Overhead urban (%)	Overhead Rural (%)	Overhead Remote or Rugged (%)
EA Networks	23.2%	2.9%	94.7%	2.4%
Horizon Energy Distribution	23.2%	10.0%	55.1%	34.8%
Top Energy	22.5%	5.4%	65.5%	20.9%
MainPower New Zealand	20.8%	1.2%	59.1%	38.3%
Alpine Energy	19.3%	8.7%	88.6%	2.7%
Marlborough Lines	16.9%	12.0%	31.0%	57.0%
Eastland Network	10.6%	5.5%	42.2%	52.2%
The Lines Company	7.5%	12.4%	72.3%	15.3%
Peer Median	20.1%	7.1%	62.3%	27.9%
Industry Average	28.8%	21.6%	57.3%	20.5%

Profitability

EDB profitability is measured using the return on investment (ROI) metric which reports annual regulatory profit as a percentage of the RAB. It is presented as comparable to a vanilla WACC* because the regulator uses this approach when monitoring profitability performance and setting revenue caps for non-consumer owned EDBs.

Top Energy's ROI was higher than the peer group and industry averages in FY17 and FY18, and has aligned with the peer group average since FY19. The industry average has been similar to the peer group average across the review period, except for FY19.

The regulatory WACC benchmark reduced significantly in FY21, and Top Energy's ROI, as well as the comparator group averages reduced as a result. This reflects the regulated price caps which apply to most EDBs. Exempt EDBs apply similar targets, which is reflected in the data.

Return on investment (post discount)

An adjusted ROI measure is shown in figure 28. The adjusted ROI is inclusive of discretionary line charge discounts or rebates, which are not included in EDB tariffs**. This provides a more comparable measure of profitability between trust-owned businesses who use different forms of discounts.

The ROI of Top Energy over the review period broadly follows the trends of its peers, which is to be expected given the regulated nature of EBD profits.

Figure 27: ROI comparable to a vanilla WACC

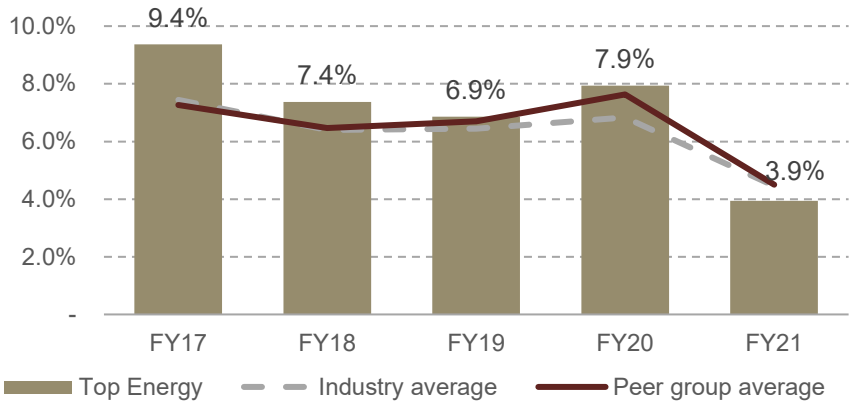
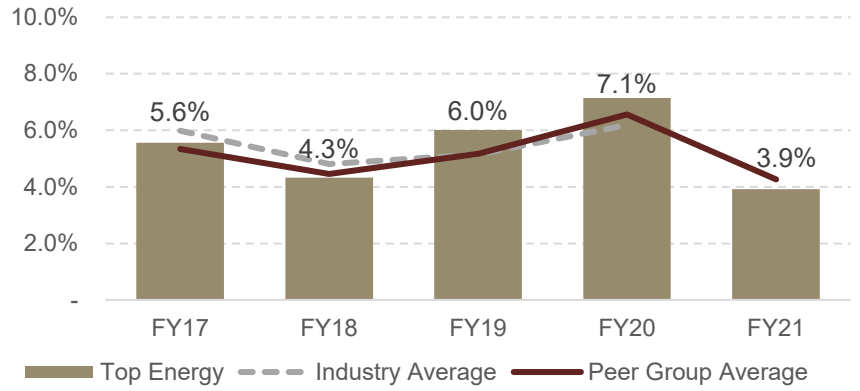


Figure 28: Adjusted ROI comparable to a vanilla WACC



* *Vanilla WACC reflects a post-tax cost of equity and a pre-tax cost of debt*

** *Distributions to consumers from TECT are not recognised as discretionary discounts*

Pricing

Pricing

Average revenue per unit of electricity delivered is a measure of the average prices charged for electricity lines services, and provides a basis for comparison between EDBs.

Average unit revenue is influenced by the mix of customers on the network. The charts opposite show unit prices (pre and post line charge discounts) for customers on standard contracts.

As illustrated, Top Energy's unit prices are higher than the average of the peer group and the industry group. Line charge discounts have reduced prices by approximately 2-3 c/kWh over the review period.

Figure 29 shows that Top Energy has lower average consumption per connection, than the comparator groups. This means that the per unit costs are higher for Top Energy's customers, which are reflected in the prices.

Figure 29 - Energy delivered per connection
(MWh/ICP)

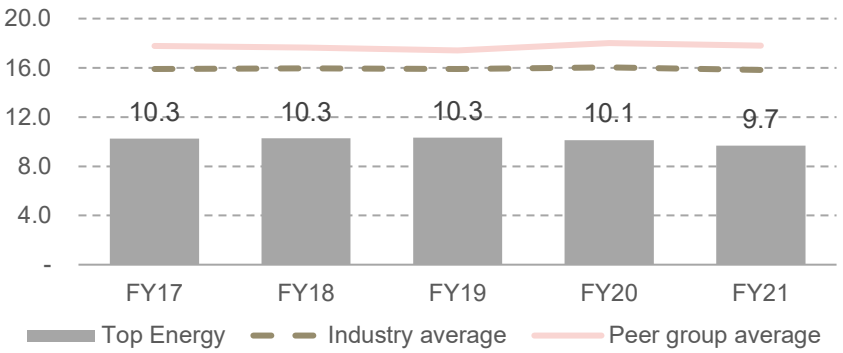


Figure 30: Average unit revenue – standard contracts
(cents/kWh)

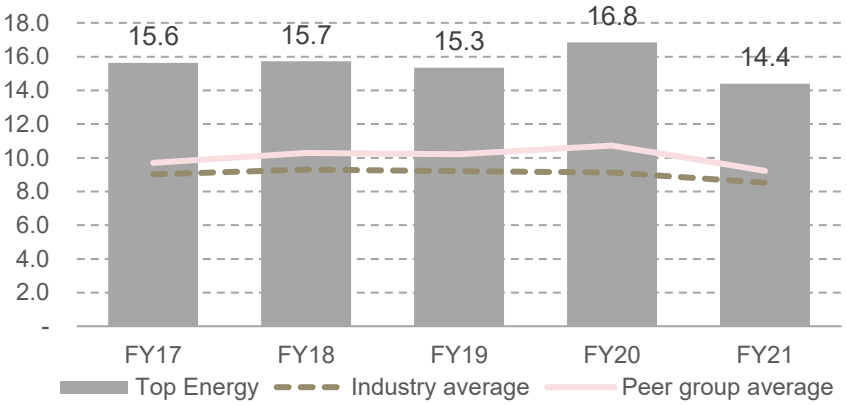
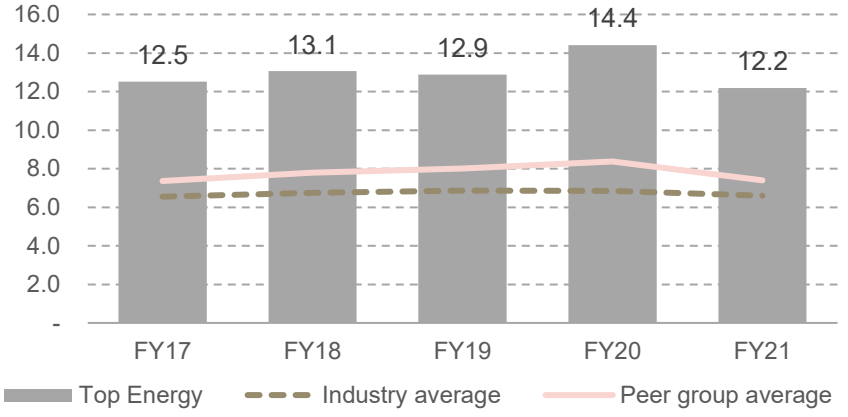


Figure 31: Average unit revenue (post discount) – standard contracts
(cents/kWh)



Network expenditure - Opex

Opex

Annual opex is categorised as either:

- network opex, which includes emergency maintenance, routine and replacement maintenance and vegetation management
- non-network opex, which includes system operations and network support opex and business support opex.

Top Energy's opex per ICP is similar to its peer group but higher than the industry average which is expected for the smaller, lower density networks. There has been an trend of increasing opex over the review period.

Top Energy has invested in additional systems and business capability, which is reflected in this data, particularly in FY20 and FY21.

Figure 33: Network opex per ICP ($/ICP)

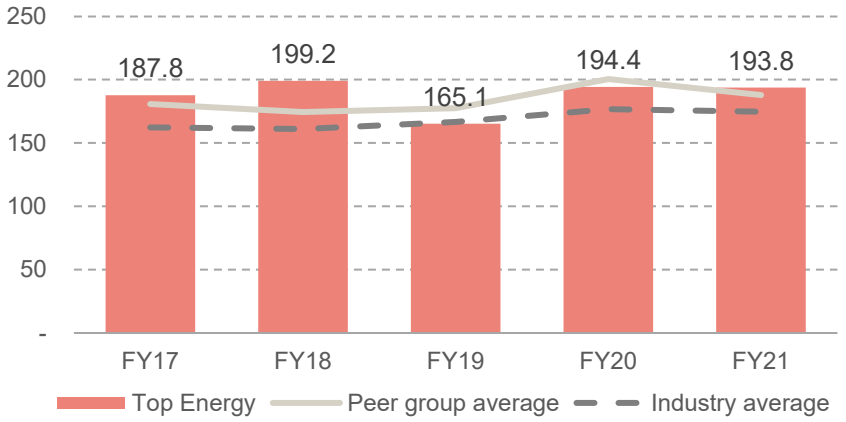


Figure 32: Total opex per ICP ($/ICP)

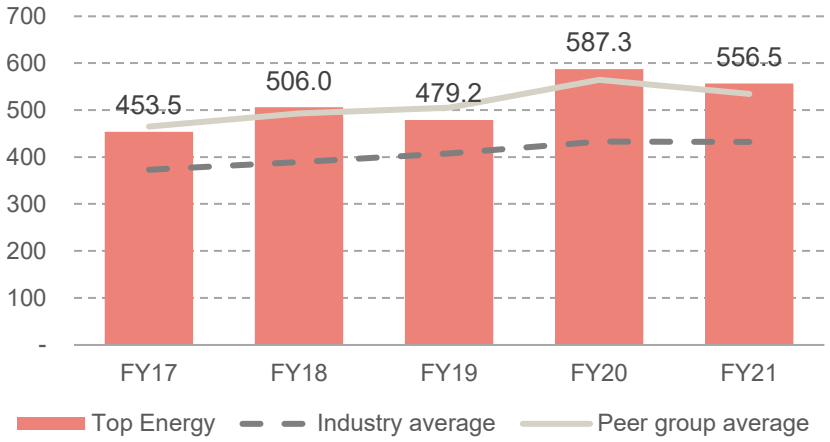
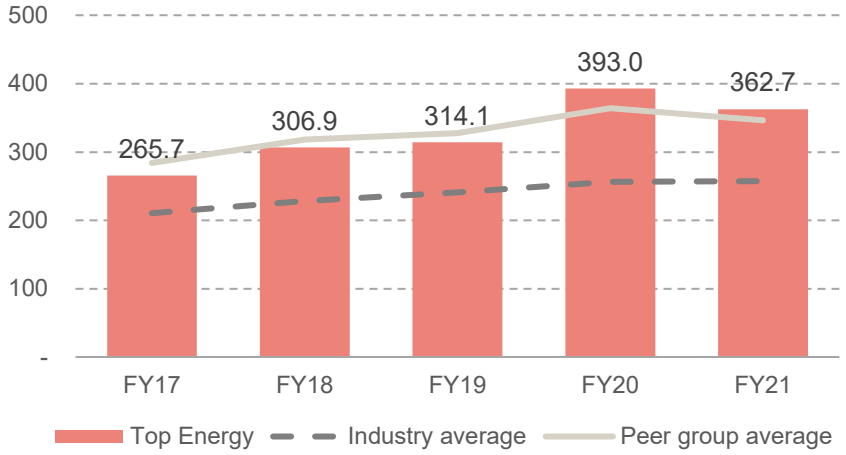


Figure 34: Non-network opex per ICP ($/ICP)



Network expenditure - Capex

Network capex

Top Energy's network capex as a proportion of RAB is near both the peer group and the industry average except for FY20. FY20 was heavily weighted with the one-off costs associated with bringing Ngawha online.

Growth capex

Top Energy's growth capex as a proportion of RAB is generally higher than the peer group and industry as a whole. This demonstrates investment in capacity and readiness for the expected growth in the region.

Renewal capex

Top Energy's renewal capex as a proportion of depreciation has been similar to the comparator groups, with some variance across FY20 and FY21.

Figure 35: Network capex as a proportion of RAB

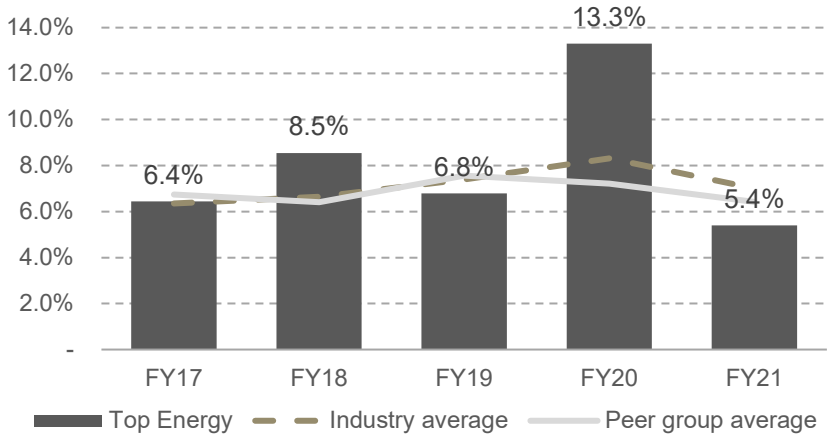


Figure 36: Growth capex as a proportion of RAB

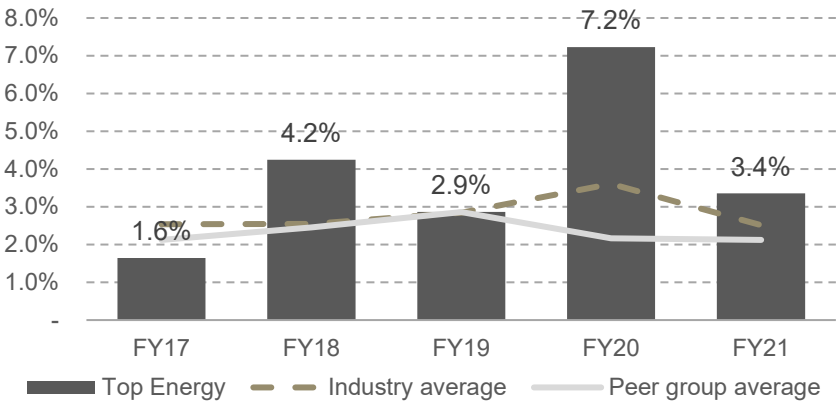
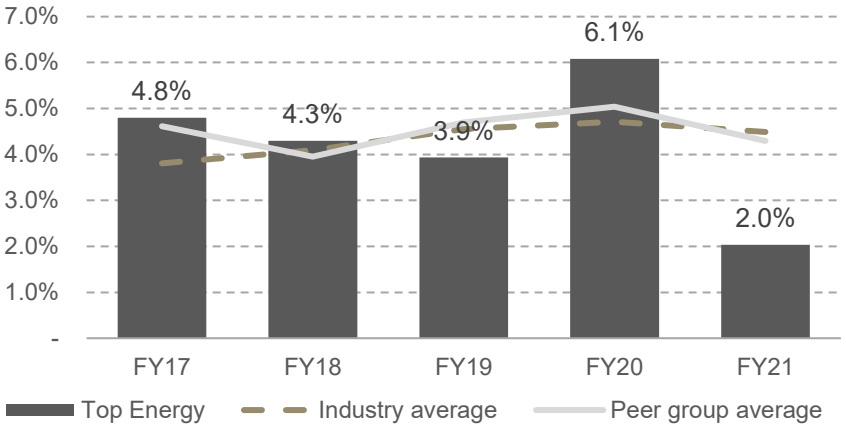


Figure 37: Renewal capex as a proportion of depreciation



Reliability SAIDI

SAIDI

SAIDI is a measure of the average interruption duration on the network each year. Class B SAIDI results from planned outages which are required to maintain and develop the network, Class C SAIDI results from unplanned outages due to interruptions on the network which result in loss of supply.

Top Energy's Class B planned SAIDI well exceeded the comparable groups in FY18 and FY19, but has aligned well since FY20. Unplanned SAIDI has improved considerably, but remains above the comparable averages.

Normalised data in figure 40, shows SAIDI once the impact of major events has been reduced. Top Energy's SAIDI is above the comparable group averages in all years for this measure.

Figure 38: SAIDI – Class B (Planned)
Minutes

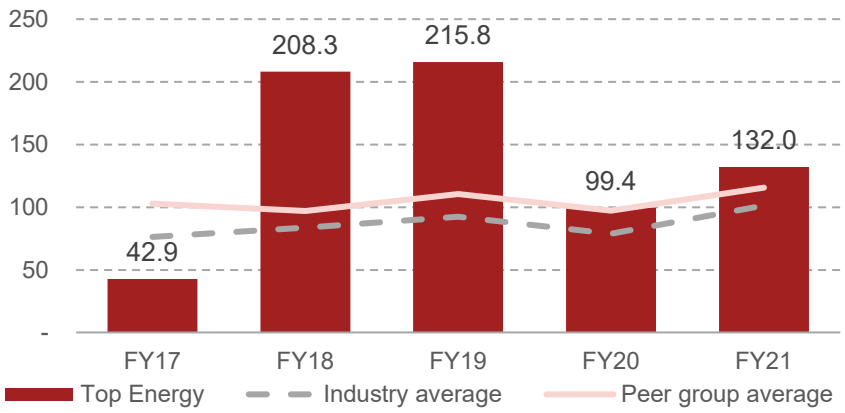


Figure 39: SAIDI – Class C (Unplanned)
Minutes

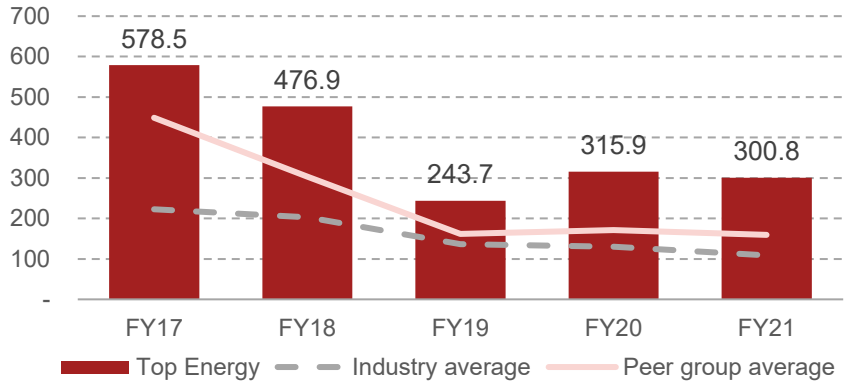
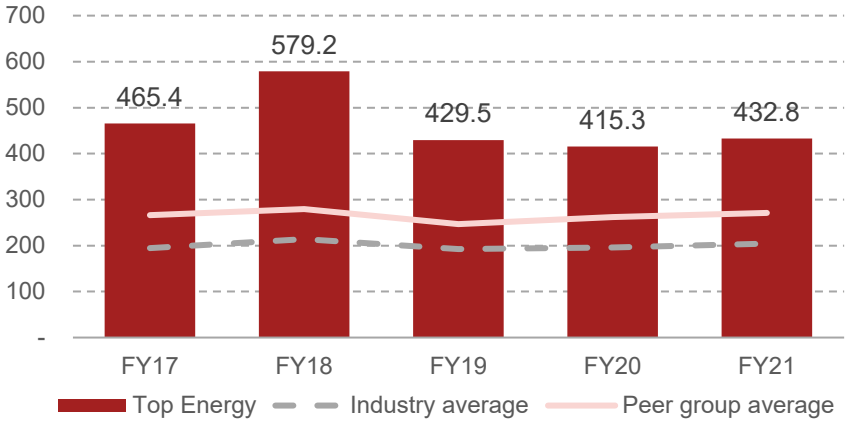


Figure 40: Normalised SAIDI
Minutes



Reliability SAIFI

SAIFI

SAIFI is a measure of the average interruption frequency on the network each year. Class B (planned) and Class C (unplanned) SAIFI are common industry metrics.

Planned SAIFI has been higher than the peer group and the industry average since FY18.

Top Energy's unplanned Class C SAIFI has improved since the beginning of the review period, but remains above the comparator averages.

When normalised for major events, as illustrated in figure 43, Top Energy's total Class B and Class C SAIFI shows less year on year volatility, and remains above the comparable group averages.

Figure 42: SAIFI – Class C (Unplanned)
Interruptions

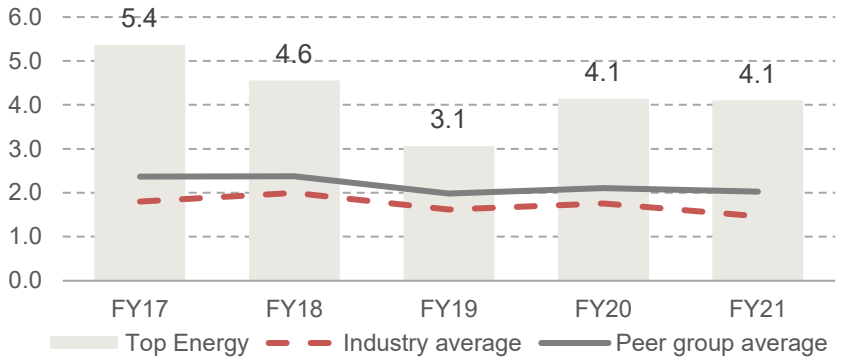


Figure 41: SAIFI – Class B (Planned)
Interruptions

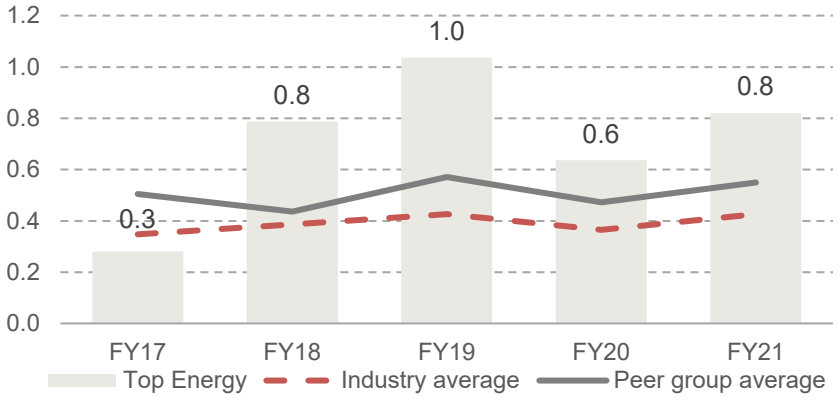
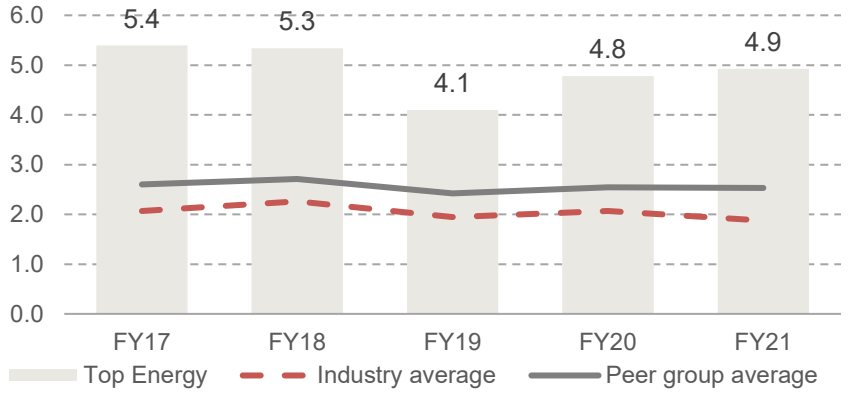


Figure 43: Normalised SAIFI
Interruptions



5

Top Energy Consumer Trust performance

TECT performance relative to other consumer trusts

Financial overview of TECT

TECT endeavours to operate financially as close to a breakeven cash position as possible. It meets 8 -12 times per year and receives income by way of dividends from Top Energy and interest.

To assess how well TECT performs, we have benchmarked it against other selected energy consumer trusts using information from the FY19 and FY20 years. The consumer trusts selected for this benchmarking are not the same trusts represented by the network businesses selected for benchmarking in Section 4 and some are quite different from TECT. This reflects the data that is available: not all trusts disclose separate financial information. We assessed all energy consumer trusts that disclose relevant information.

Trust expenses have been measured relative to the number of ICPs. Expenses have also been measured as a percentage of Trust assets. The Trustee fees are measured as average fees per Trustee, and Trustee fees per ICP. The numbers presented are based on an average of the most recent two years of disclosures available from each of the respective trusts.

TECT costs are below the average of other trusts on all measures. It has the lowest expenses per ICP of all the Trusts evaluated and this is reflective of its conservative breakeven approach to running the Trust.

Table 10: TECT high level profit and loss
NZ$m

	FY17	FY18	FY19	FY20	FY21
Income	208	170	185	221	158
Expense	200	185	183	219	152
Profit/(Loss)	8	-15	2	2	6

Table 11: Comparative performance of select consumer trusts
2020-2021 average

Consumer trust	No. of ICPs	Average fees /Trustee	Trustee fees /ICPs	Expenses /ICPs	Expenses /assets
Entrust	578,672	67,000	0.6	5.8	0.9%
Northpower Electric Power Trust	60,691	31,357	3.6	7.4	1.2%
Electra Trust	45,377	15,000	2.0	7.8	2.0%
Counties Power Consumer Trust	44,000	27,275	3.1	10.2	1.3%
Top Energy Consumer Trust	32,707	17,065	2.6	5.7	0.7%
West Coast Electric Power Trust	13,801	21,000	7.6	13.7	0.6%
Average	**129,208**	**29,783**	**3.2**	**8.4**	**1.1%**

Benchmarking by ownership status

Ownership status benchmarking

Ownership structure is correlated with the size of the EDB. The majority of EDBs are consumer trust owned and this is reflected in the small size and localised nature of those EDBs.

Non-trust owned EDBs as a group are on average several multiples larger, by all measures, than trust-owned EDBs. In many cases non-Trust owned EDBs are far outliers to the industry as a whole.

This reinforces the strong relationship between ownership structure and capital employed.

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Figure 45: ICP count (FY21)
000s

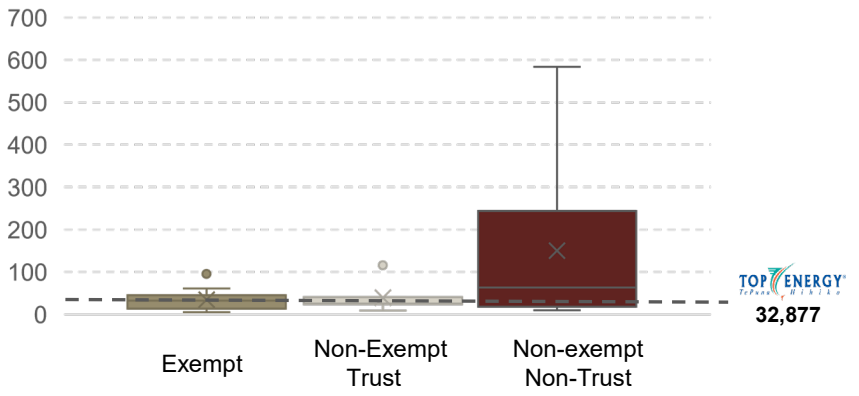


Figure 44: Circuit length (FY21)
Kilometre 000s

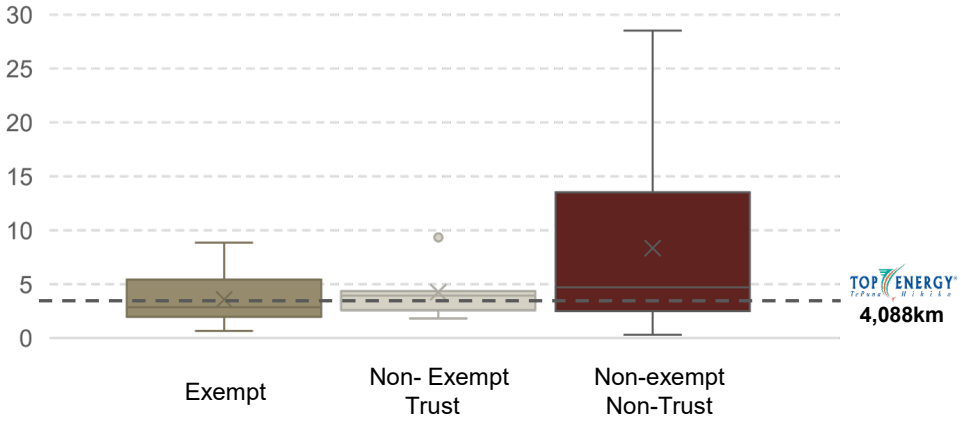
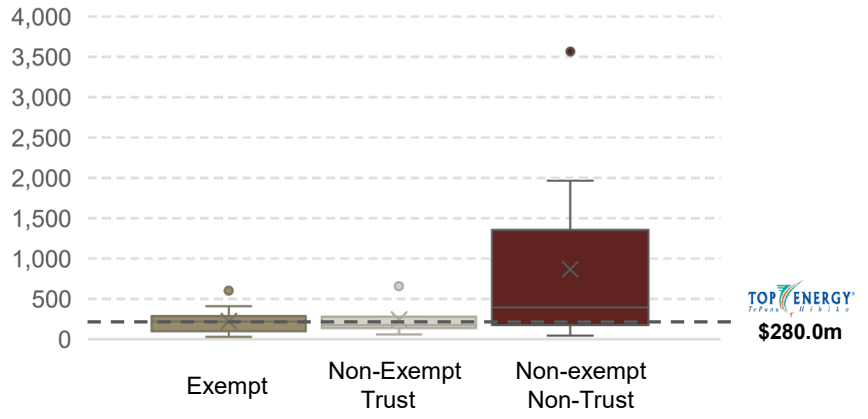


Figure 46: Total opening RAB (FY21)
NZ$m



Benchmarking by ownership status

ROI

The types of returns achieved by EDBs are comparable regardless of whether they are subject to price-quality regulation by the Commerce Commission or not. Exempt trusts are not motivated to achieve excessive returns as they serve the people who are also the beneficiaries. Non-exempt non-trust owned EDBs are prevented from earning excessive returns by regulation. Ownership structure or exemption status plays little observable role in returns.

Expenditure

Similarly, we cannot derive any insights into efficiency gains driven by ownership structure. Maintenance opex per km of circuit and non-network opex per connection are both increasing moderately over time regardless of ownership.

Figure 47: ROI - Comparable to vanilla WACC
(Excluding incentives & wash-ups)

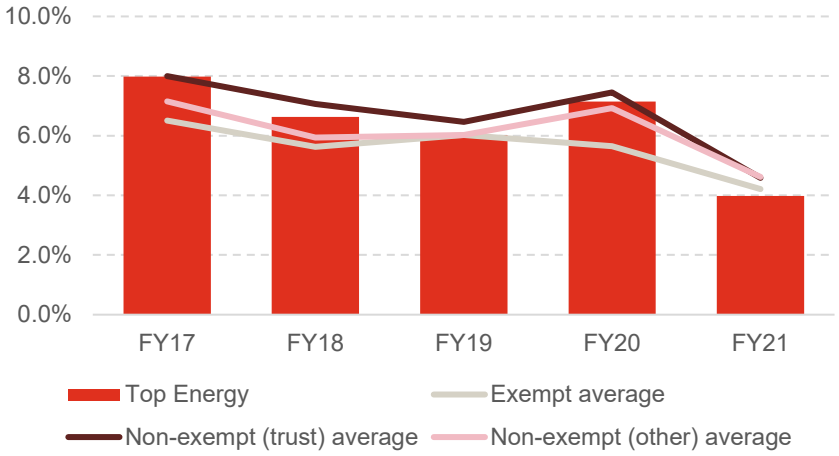


Figure 48: Network opex per total circuit length
($/km)

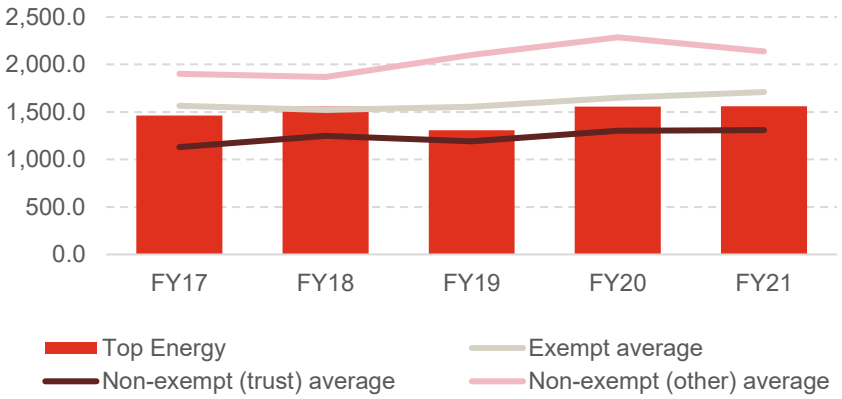
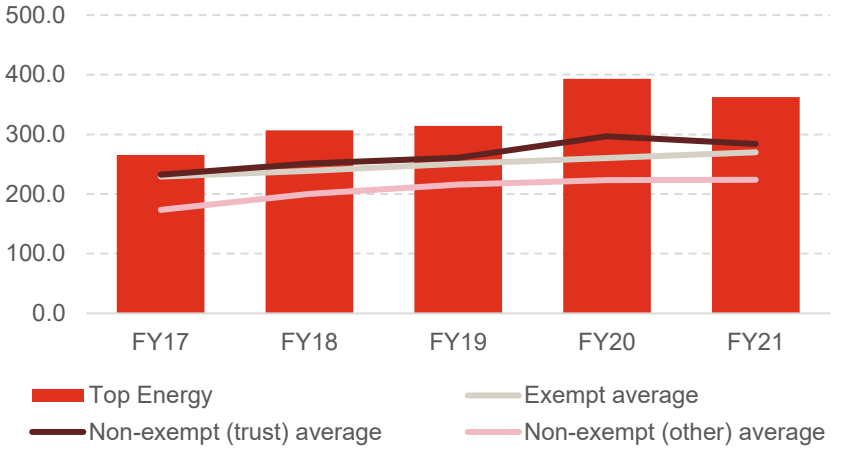


Figure 49: Non-network opex per ICP
($/ICP)



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Analysis of ownership options

Overview

Trust overview

TECT holds all the shares in Top Energy. The Trust Deed ensures that Top Energy's consumers, as both income and capital beneficiaries, benefit from ownership of the Company.

TECT's primary objective is to represent the beneficiaries by supporting the Company in meeting its objective of being a successful business, and to create long-term value to its owners. The definition of what 'value' is in this context was raised in a number of interviews and it is clear that across the parties represented that this is more than a financial measure.

The trustees are appointed by a public nomination and panel selection process. We understand that the relationship between trustees and the Company is strong, and the Board and management of the Company regularly update the trustees on Company matters, including financial and non-financial performance.

The Trust is active in agreeing the annual SCI with the Company each year, which sets out the Company's objectives and targets for the following three years. The Trust also appoints the directors of the Company and monitors the performance of the director group.

The Trust has a focus on the needs of the people of the Far North and the benefits that Top Energy's activities can deliver to those communities. It has been supportive of the significant development undertaken in the last five years, showing a focus on long-term outcomes, and the stability provided by the Board has been important during this high growth phase.

For this review we interviewed the Chair and Deputy Chair of TECT. Based on those interviews we have assessed that the Trust has a good understanding of its role and is supportive of both the operations and strategic direction of the Company. The trustees have a strong consumer focus and show pride in what Top Energy is providing the Far North community.

Evaluation of ownership options

We have evaluated continued consumer trust ownership of Top Energy's shares and alternative ownership options.

We consider the advantages and disadvantages to TECT's beneficiaries of consumer trust ownership of Top Energy's shares, relative to the distribution of these shares. This evaluation is required under Clause 4 of the Top Energy Consumer Trust Deed.

Ownership options available to the Trust range from continued 100% consumer trust ownership through to full distribution of shares. This report examines the ownership options shown in the table below.

Ownership option	Description
100% trust ownership of shares (status quo)	Trust ownership is common practice with over 70% of EDBs in New Zealand operating under it to some degree We also consider variants to the current consumer trust option
Distribution to beneficiaries or sale to the public or external investors of 24.9% or 49.9% of shares	Distribution or sale of 24.9% allows the Trust to retain control over Top Energy's constitution Distribution or sale of 49.9% allows the Trust to retain control
Distribution of 100% of shares to beneficiaries	Where a 100% share distribution occurs, shares are typically on-sold by beneficiaries within a short period, making it possible for an interested party to gain majority control
Sale of 100% of shares to the public or external investors	A sale of 100% of shares would enable the Trust to test the market for interest in the Company and pass the proceeds to beneficiaries

Strategic direction

Approach

In considering the advantages and disadvantages of consumer trust ownership, relative to alternative options, we have drawn on the objectives set out in the SCIs published over the review period to help us evaluate the options.

Strategic direction

Since the previous ownership review, Top Energy has developed its vertical integration pillar with the expansion of Ngawha. It now generates most of the electricity consumed in its network.

Together the generation and network businesses provide Top Energy with the platform of capabilities to expand further. Access to capital is the main constraint in doing so.

Community value

Top Energy is an important business in the Far North. It plays a pivotal role in providing energy in the region, enabling economic and regional development, creating employment and development opportunities for local people and adding to a sense of wellbeing and community.

The capabilities that have been developed at TECT and Top Energy over this past review period are reflective of what good relationships between trusts and EDBs can achieve. TECT and Top Energy have demonstrated that they can deliver on their financial objectives while keeping a holistic view of value creation in the Far North front of mind.

Top Energy FY22 Statement of Corporate Intent

Principal Objectives

1. *To operate a successful business to optimise the long-term value of the Group for its Shareholder*
2. *To encourage a safety and organisational culture where all our employees take responsibility for themselves and others to minimise the risk of injuries to customers, staff, contractors and the public*
3. *To achieve network quality standards that are acceptable to our consumers*
4. *To operate in an environmentally sustainable manner, to be responsive to the social needs of our community and have a well-defined corporate governance system to support the long-term strategy*
5. *To minimise the total delivered cost of electricity to our consumers*

Guiding Principles

The Group has chosen to substantially comply with the corporate governance principles and guidelines issued by the Financial Markets Authority (FMA). In doing so, it recognises that it is entirely owned by a consumer trust, that the FMA principles and guidelines are not a checklist or set of rules and the Group has attempted to implement the spirit and intent of the principles and guidelines.

Top Energy Group Purpose

The Company operates and maintains the electricity supply network within its area of geographical operation and provides related construction and maintenance services. Through its subsidiary, the Company operates a geothermal electricity generator (The Group). Other activities may be considered if they meet the Objectives as set out in this Statement of Corporate Intent.

External factors

New energy future

In addition to Top Energy's current strategic direction, we have considered factors external to the Company which may present opportunities and challenges relevant to the assessment of alternative ownership options.

There is increasing attention on the capability of the electricity sector to manage growth, given New Zealand's climate change policy goals, which will only be achieved with increased electrification of transport and industrial processes. Significantly more renewable electricity generation will be required, including small scale distributed generation located within distribution networks.

New technologies such as solar PV, battery storage, EVs, smart metering and energy automation management systems are expected to have a significant and enduring impact on the energy market. There are a number of potential grid-scale solar generation projects located within Top Energy's supply area and it may become involved in the REZ pilot with Transpower and Northpower.

Accordingly, the energy system is rapidly evolving to adapt to distributed and digital micro-networks that more directly engage customers. Electricity distributors are critical to enabling these new technologies to be adopted and to ensure customers are able to benefit from them.

Distribution networks provide the local market place for these activities, which require distributors to manage more complex two-way electrical loads. This provides opportunities for Top Energy to achieve its growth aspirations, and enhance the well being of the local community.

Top Energy is committed to supporting the new energy future. However, the financial constraints it will likely experience over the coming review period may leave it without the capacity or flexibility to respond at the level it would desire.

The analysis on the following pages presents the advantages and disadvantages of consumer trust ownership, and alternative ownership options, assessed against the Company's strategic direction and external opportunities.

Consumer trust ownership

Advantages of consumer trust ownership

Evaluation Criteria	Reliable, effective network infrastructure services	Sustainable financial performance & improvement

100% consumer trust ownership of shares (status quo)	• The Trust's expectations are currently reflected in Top Energy's objectives which are supported by four strategic pillars:
	  • Vertical Integration
	  • Future Investment
	  • Maintaining Our Identity
	  • Trusted Source
	• As trustees are appointed to represent consumers, a trust structure allows close alignment between Top Energy's direction and value maximisation for consumers
	• Allows a long-term perspective and a focus on the interests of current and future consumers and the local community. This includes non-financial outcomes such as network quality and a safety culture
	• Direct alignment of interests between beneficiaries and electricity consumers means both financial and non-financial considerations of the term 'value' are considered in setting targets
	• A relatively simple and low cost model
	• Distributions via price discounts are tax effective
		• The Trust supports Top Energy in pursuing new opportunities
		• A trust structure allows flexibility for future opportunities and changes in direction but the method of trustee selection fosters stability in execution of strategy
		• Business structures including joint ventures (JVs) or partnerships can be explored at the company level provided this is supported by the Trust. These options may provide flexibility for pursuing growth and new opportunities and managing risk
		• Direct alignment of interests between beneficiaries and electricity consumers means investments which respond to changing customer needs and regional opportunities can be more easily justified
		• Exemptions from the Electricity Authority (EA) on the generation business are conditional on trust ownership
		• The investment in the Ngawha expansion has proved successful, resulting in significant additional revenue and diversification for the Company. This has made Top Energy an attractive proposition for governance roles and has drawn interest from high quality board candidates. This has reduced recruitment costs for TECT

Consumer trust ownership

Disadvantages of consumer trust ownership

Evaluation Criteria	Reliable, effective network infrastructure services	Sustainable financial performance & improvement
Consumer trust structure (status quo)	• May prioritise low prices or income distributions to beneficiaries over investment in network operations and assets, limiting operational capability • May be difficult to achieve scale efficiencies in operations • Dependent on ability to attract trustees with necessary skills • Unable to distribute funds to targeted areas of the community which may be more in need of financial support	• Optimal investment levels may not be obtained if the Trust's willingness to take risk differs from levels that would be targeted commercially • Distributions to beneficiaries may need to be deferred to pursue new opportunities • Unable to raise additional capital from beneficiaries • Mixed dividend/discount distribution model required to manage diverse business activities within Trust ownership • Expectations for distributions to beneficiaries may limit funds for growth

Community trust ownership

Advantages and disadvantages relative to status quo

Relative to status quo	Advantages	Disadvantages
Community trust ownership (alternative)	• Allows funds to be distributed to meet community needs, eg: investing in social infrastructure and engaging in community sponsorship	• Less incentive to manage network performance and the costs of electricity distribution services to consumers because beneficiaries are not necessarily users of the network • Complex process to identify priorities as wide range of potential beneficiaries • Reduced alignment between interests of beneficiaries and electricity consumers means investments which respond to changing customer needs and industry opportunities are more difficult to justify • More complex and costly to operate than consumer trust • May create conflicts between beneficiaries who are consumers and those who are not

Partial sale or distribution

Advantages and disadvantages relative to status quo

Relative to status quo	Advantages	Disadvantages
Partial distribution to beneficiaries of 24.9% or 49.9% of shares	• To a certain degree, the Trust can continue to support Top Energy and the interests of beneficiaries by: ◦ balancing both financial and non-financial considerations ◦ encouraging it to pursue new opportunities which respond to changes in consumer needs and sector developments	• Does not provide access to additional capital • Distribution of shares would raise inter-generational equity issues, with value passed to current generations at the expense of future generations • Beneficiaries would lose future distributions and access to future growth in the value of the Company, and may have less influence over future prices and quality of service • A dividend would likely replace the price discounts currently being provided to beneficiaries. This is likely to have tax implications • A more complex structure, with additional costs • Better outcomes for the people of the Far North, such as reducing energy hardship, may not be supported by other owners
Partial sale to the public or external investors of 24.9% or 49.9% of shares	• Sale of shares to an interested party with relevant experience may provide access to additional expertise to respond to industry opportunities • Additional capital from a sale of shares could be used to pursue new opportunities	• Financial considerations such as return on investment may be prioritised at the expense of non-financial objectives. This may lead to higher electricity prices for consumers • Short-term returns may be prioritised over investment for long-term gain. The amount external investors are willing to pay for a minority stake in Top Energy shares may involve a discount relative to the amount they would be willing to pay for a controlling stake • There may not be a material premium available in the market, given the value generated for current and future beneficiaries of Top Energy

Full sale or distribution

Advantages and disadvantages relative to status quo

Relative to status quo	Advantages	Disadvantages
100% distribution of shares to beneficiaries	• Assuming that the move away from trust ownership does not result in a reduction in value, current beneficiaries will receive access to the entire value of the assets held for them in trust	• Does not provide access to additional capital • Potential loss of consumer control, if consumers on-sell shares • Distribution of shares raises inter-generational equity issues, with value passed to current beneficiaries at the expense of future beneficiaries • Beneficiaries would lose future distributions and access to future growth in the value of the Company, and may have less influence over future prices and quality of service • A more complex structure, with additional costs • Better outcomes for the people of the Far North, such as reducing energy hardship, may not be supported by other owners
Sale of 100% of shares to the public or external investors	• If shares are sold or on-sold to an interested party who gains majority control, Top Energy may gain access to external capability to support it in responding to challenges and opportunities in the sector	• Loss of consumer control • Depending on the nature of new shareholders, financial considerations such as ROI may be prioritised at the expense of non-financial performance. This may lead to higher electricity prices for consumers • The Trust will no longer have influence over Top Energy, for example in encouraging it to pursue new opportunities in response to sector developments or for community benefit

Summary of ownership analysis

Status quo – Trust ownership

Operating under 100% trust ownership, Top Energy has successfully enhanced the capacity of its core businesses during the review period. Current and future Trust beneficiaries have been served well by the Company's execution of its strategy which will enable it to continue to take advantage of the wider business opportunities in the electricity sector.

The Company is successfully investing in improved health and safety outcomes, and has invested in systems and processes within the business to enhance operations and develop capabilities for future growth.

The Trust has effectively fulfilled its responsibilities to appoint directors and review director performance. The primary responsibility of the Trust is to appoint a quality board. The current Board has an appropriate mix of commercial and industry experience, and has effectively refocused the business to improve the performance of the Company. With the growth of the Company, the quality of the candidates interested in board roles has risen. The Trust is now in the position of being able to choose high-calibre directors.

The Trust also contributes to setting objectives for the Company through the annual SCI process. The Company is showing improvements in meeting targets or moving towards meeting these. The Trust has approved a major transaction within the review period and the Company has delivered on this successfully.

The Trust appears to have a good relationship with the Board of Directors and the Company, with both formal and informal information sharing and discussion.

The status quo is consistent with meeting the needs of current and future consumer beneficiaries. It is a low-cost ownership model, which provides for the local interests of consumers to be reflected in the Company's performance and direction.

Direct alignment of interests between beneficiaries and electricity consumers through a consumer trust structure means both financial and non-financial considerations can be balanced. Two of the strategic pillars supporting the SCI objectives, "Maintaining Our Identity" and "Trusted Source" are fundamentally dependent on trust ownership. Non-financial measures form part of the SCI targets and this formalises that value to shareholders goes beyond financial returns.

As all trustees are appointed, Top Energy is not exempt from price-quality regulation under Part 4 of the Commerce Act. This increases compliance obligations and results in higher costs and complexity for the business compared to exempt EDBs. However, appointed trustees may be able to better reflect the needs of beneficiary groups or provide for specific skills or experience on the Trust, than elected trustees. It also means that new trustees join a core team potentially filling skills gaps while maintaining stability through time. The interview process revealed that non-exempt status is considered more of a positive than a negative by all parties.

Under 100% trust ownership, Top Energy has a substantial degree of flexibility in meeting changing customer needs. It demonstrated this with its response to COVID hardship for customers during the review period.

Retaining full ownership of Ngawha may reduce Top Energy's flexibility in responding to other changes and opportunities which present over the next review period.

Summary of ownership analysis

Implications of alternative ownership options

Alternative ownership options which involve external shareholders taking a full or partial stake in Top Energy's shares may provide access to additional expertise and capital to respond to industry opportunities.

The extent to which such outcomes will apply will depend on the nature of new shareholders (e.g. another EDB, local iwi, or general diversified investors) and the size of the respective shareholdings.

Top Energy has proven that full Trust ownership has not limited its ability to access to high-quality human capital, technical capabilities, scale and innovation. However, the Company is now capital constrained.

There are attractive expansion opportunities available to Top Energy in the Far North region. Additionally, the Company must also be mindful of the capital requirements to maintain their existing asset base. These realities, coupled with the capital structure constraints imposed by the current trust ownership model, mean the Trust and the Company must either accept modest future growth or consider alternative ownership options.

A partial or full sale of Top Energy shares may result in financial considerations such as ROI being prioritised at the expense of non-financial considerations, including health and safety, maintenance of network assets and regional well-being.

JV arrangements for individual projects is an option for accessing equity investment while maintaining trust ownership of the parent company, Top Energy. JV approaches would be consistent with maximising long-term value of the Company and supporting growth. JVs can, however, introduce new risks by adding new relationships into the governance and management mix. Currently the relationships between the Trust, Board and management appear to be highly effective and significant value would be lost if this dynamic was disturbed.

Sale or distribution to beneficiaries

A sale of shares or distribution of shares to beneficiaries would allow beneficiaries to realise the market value of their investment in Top Energy.

This is likely to raise inter-generational equity issues since value would be passed to current beneficiaries at the expense of future beneficiaries. Beneficiaries would lose future distributions and access to future growth in the value of the Company, and may have less influence over future discounts and quality of service.

If a dividend replaces the discounts currently being provided to consumers this is likely to have tax implications.

Sale or distribution to the public or external investors

Alternative options which involve external shareholders taking a full or partial stake in Top Energy shares may create uncertainty as to whether new shareholders are open to pursuing new and innovative opportunities which meet future consumer needs. Short-term returns may be prioritised over investment for long-term gain. This may lead to higher delivered electricity prices for consumers.

There is extensive market evidence that the sale of a minority shareholding will attract a discount to the price that could be achieved by selling 100% of the shares. The Trust is therefore likely to maximise value by selling 100% of the business and distributing cash to beneficiaries, rather than selling part of the business or distributing shares, some of which are likely to be acquired by third parties seeking majority control.

As a wholly-owned subsidiary, there is the option to partially divest Ngawha Generation Ltd and for the Trust to retain 100% of Top Energy Ltd.

Conclusion

Conclusion

Under 100% trust-ownership, Top Energy has substantially grown its asset base and increased the energy independence of the Far North region. It has laid the foundations for improving energy affordability and security in the region.

Despite challenges brought by the COVID-19 pandemic, Top Energy successfully delivered on the expansion of their Ngawha power station ahead of schedule. This is a great source of pride for management, the Board and the people of the Far North. This, among other achievements highlighted throughout the report, show the alignment of the Company with the objectives set out in Top Energy's Statement of Corporate Intent.

Highlights of this review period include:

- appointment new Directors – increased diversity on the Board
- investment in data management systems (ADMS, CRM) for system operations and customer relationships
- improved health and safety culture
- relationship building with iwi at Ngawha
- increased employment options through Ngawha and the industrial park
- contributing to the wellbeing of the local community through the COVID-19 pandemic

The Company can be expected to continue to perform in this way if the Trust maintains clear expectations for the Company which balance ambitions of growth with the present responsibility to reduce the burden of electricity cost on Far North communities.

Debt financing to execute the expansion of the Ngawha power station has pushed Top Energy to the limits of its debt service capabilities, however, the debt is manageable and should become less burdensome in future years. The benefits of executing this project are already evident even before it has had a full financial year of operating.

A distribution of shares to beneficiaries would raise inter-generational equity issues, with value passed to current beneficiaries at the expense of future beneficiaries. Customers would lose future distributions and access to future growth in the value of the Company, and may have less influence over future prices and quality of service as a result.

The Trust's governance role allows it to represent the interests of the beneficiaries through the appointment of directors and contributing to the annual SCI. The Trust can encourage investment and initiatives which deliver financial growth, while allowing the Company the flexibility to pursue new opportunities consistent with its strategic objectives.

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Appendices

Appendix A - Restrictions

This report has been prepared to assist the directors of Top Energy Limited and the TECT trustees with the five yearly ownership review of the Top Energy Consumer Trust (TECT) as required under the TECT Trust Deed. This report has been prepared solely for this purpose and should not be relied upon for any other purpose. We accept no liability to any party should it used for any purpose other than that for which it was prepared.

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The statements and opinions expressed herein have been made in good faith, and on the basis that all information relied upon is true and accurate in all material respects, and not misleading by reason of omission or otherwise.

The statements and opinions expressed in this report are based on information available as at the date of the report. We reserve the right, but will be under no obligation, to review or amend our report, if any additional information, which was in existence on the date of this report, was not brought to our attention, or subsequently comes to light.

This report is issued pursuant to the terms and conditions set out in our engagement letter dated 16 December 2021.