

# Aurora Energy Limited

**DRAFT**

**Statement of Intent  
for the year ending 30 June 2016**

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## **1 INTRODUCTION**

This Statement of Intent (Sol) sets out for Aurora Energy Limited (hereafter referred to as “Aurora” or “the Company”) the nature and scope of its activities, objectives, key performance targets and other measures by which performance may be judged.

## **2 STRATEGIC DIRECTION**

### **2.1 Vision**

Our vision for Aurora is a network that meets the community’s needs for reliable energy and shareholder requirements for adequate returns through targeted reinvestment, best practice asset management and tailored innovation.

### **2.2 Mission**

To provide reliable energy infrastructure for the communities we serve.

### **2.3 Corporate Goals**

The principal goal of Aurora is to operate as a successful business, achieving its goals and objectives as specified in this Sol. The specific goals of Aurora are as follows:

#### **General**

- To ensure that the Sol and operating policies for the Company are consistent with the operating policies of the Shareholder for the business
- To ensure that the Sol and operating strategies are adhered to
- To keep the Shareholder informed of matters of substance affecting Aurora
- To perform regular reviews of the operating strategies, financial performance and service delivery of the Company
- To grow the Company into a leading New Zealand business while taking into account the free cash flows required to meet the objectives of the ultimate shareholder.

#### **Network operations**

- To maximise the utilisation of electricity distribution assets while ensuring that service quality meets the needs of users.

#### **Network reliability**

- To deliver electricity supplies to consumers on the Aurora network of a reliability that meets or exceeds the regulated quality thresholds determined by the Commerce Commission.

**Community, safety and environment**

- To encourage non-discriminatory, culturally sensitive, equal opportunity and safe work practices by our service providers
- To act as a socially responsible and environmentally aware corporate citizen and to contribute to, or assist where possible, the Dunedin City Council community outcomes (as listed in the Annual Plan)
- To bring to the attention of the Shareholder any strategic or operational matters where there may be a conflict between the Dunedin City Council's community outcomes (as listed in the Annual Plan) and those of Aurora and to seek the Shareholder's view on these. Aurora will be mindful that the ultimate shareholder is the custodian of the community's interest and accepts that this may create a greater need for consultation with the ultimate shareholder than might be required in a normal commercial situation.

**Financial**

- To optimise the financial returns achieved and the value added by Aurora. Particular attention will be given to cash flow performance
- To maintain the Company's financial strength through sound and innovative financial management
- To ensure that the financial reporting requirements of Aurora and of the Shareholder are met.

**2.4 Specific Objectives for the Year Ending 30 June 2016**

In pursuit of its corporate goals, Aurora has the following objectives for the year ending 30 June 2016:

**General**

- To review the Sol and Strategic Plans for consistency with the objectives of Dunedin City Holdings Limited (DCHL)
- To review the operating activities of Aurora for compliance with the goals and objectives stated in the Sol and Strategic Plan
- To report all matters of substance to the Shareholder.

**Network operations**

- To review the asset management strategy and improvement plan to take into account the annual customer survey and, specifically, feedback on price-quality trade-offs for consumers on the Aurora network
- To deliver capacity upgrades for new irrigation loads in Central Otago in accordance with the Aurora Asset Management Plan, specific power system development proposals and their revisions
- To take an active part in national smart-grid initiatives and identify and implement technology initiatives for improving asset utilisation consistent with our asset management strategy.

### **Network reliability**

- To deliver electricity supplies to consumers on the Aurora network of a reliability that meets or exceeds the regulated quality threshold cap determined by the Commerce Commission
- To review and adopt an approach to the revenue-linked service quality schemes determined by the Commerce Commission that optimises outcomes for consumers and the Shareholder.

### **Community, safety and environment**

- To continue to review the activities undertaken by the Company for purposes of fulfilling its health and safety responsibilities
- To complete the preparation of a stakeholder engagement plan that formally identifies stakeholders and their priorities to inform Aurora's decision making
- To ensure no transgression of environmental and resource laws occurs
- To support community well-being through our sponsorship programme.

### **Financial**

- To achieve all financial projections
- To ensure that the reporting requirements of the Company and the Shareholder are met.

## **3 NATURE AND SCOPE OF ACTIVITIES**

Aurora's principal activities are the ownership, development and strategic management of electricity distribution network assets in Dunedin and in Central Otago. Our function is to transport electricity from the national grid to the end-use consumer, ensuring a safe, efficient, reliable and cost effective distribution network. Customers include large directly billed consumers, distributed generators and New Zealand's electricity retailers.

Aurora's total assets were \$390.8 million as at 30 June 2014, and the Company generated revenues of \$92.9 million for the year then ended.

Under the Commerce Commission's Electricity Information Disclosure Requirements, Aurora is required to publish, at least bi-annually, a 10 year Asset Management Plan (AMP). Aurora's AMP sets out the way in which it ensures that long-lived assets are managed sustainably.

Aurora invites comment on its AMP from electricity retailers (on behalf of their customers) and provides opportunity for public comments via its website.

### **3.1 Pricing Principles**

As a supplier of an essential service, Aurora intends to set fair and reasonable prices for the specific individual demands of small, large and seasonal electricity users having shared access to Aurora's network.

Under the Commerce Commission's Electricity Information Disclosure Requirements, Aurora is required to publish the pricing methodology used to derive the current use-of-system charges.



The Aurora pricing methodology is consistent with the following Pricing Principles:

- Prices are to signal the economic costs of service provision by:
  - being subsidy free (equal to or greater than incremental costs, and less than or equal to standalone costs), except where subsidies arise from compliance with legislation and/or other regulation and/or the Government Policy Statement
  - having regard, to the extent practicable, to the level of available service capacity; and
  - signalling, to the extent practicable, the impact of additional usage on future investment costs.
- Where prices based on 'efficient' incremental costs would under-recover allowed revenues, the shortfall should be made up by setting prices in a manner that has regard to consumers' demand responsiveness, to the extent practicable.
- Provided that prices satisfy (a) above, prices should be responsive to the requirements and circumstances of stakeholders in order to:
  - discourage uneconomic bypass
  - allow for negotiation to better reflect the economic value of services and enable stakeholders to make price/quality trade-offs or non-standard arrangements for services; and
  - where network economics warrant, and to the extent practicable, encourage investment in transmission and distribution alternatives (e.g. distributed generation or demand response) and technology innovation.
- Development of prices should be transparent, promote price stability and certainty for stakeholders, and changes to prices should have regard to the impact on stakeholders
- Development of prices should have regard to the impact of transaction costs on retailers, consumers and other stakeholders and should be economically equivalent across retailers.

Overall, Aurora considers that its current approach to pricing reflects the concerns of consumers and other stakeholders and ensures that sufficient revenue is generated in order to meet future asset improvement programmes.

### **3.2 Consumer Consultation**

Aurora regularly seeks the views of consumers through a range of survey mechanisms. In general, survey results indicate that:

- Consumers still consider price to be more important than quality of supply
- there is little appetite to accept an increase in line charges to achieve a proportionate improvement in quality; and
- the frequency of interruptions remains the single most important issue relating to quality of supply.

It is recommended that interested persons wishing to understand more about Aurora's consumer consultation approaches and subsequent analysis refer to the detailed analysis contained in Aurora's annual Asset Management Plan, available from the Information Disclosure section of Aurora's website [www.auroraenergy.co.nz](http://www.auroraenergy.co.nz).

## **4 GOVERNANCE**

### **4.1 Shareholder**

Aurora is ultimately owned by Dunedin City Council and accordingly is a Council Controlled Trading Organisation (CCTO) as defined by the Local Government Act 2002.

Aurora is a wholly owned subsidiary of DCHL. The ultimate owner of DCHL is Dunedin City Council.

The undertaking by Aurora of any activity of a nature or scope not provided for in the Company's mission or goals is subject to the prior approval of the Shareholder.

### **4.2 Board of Directors**

The Directors' role is defined in Section 58 of the Local Government Act which requires that all decisions relating to the operation of a CCTO shall be made pursuant to the authority of the directorate of the CCTO and its Sol.

Aurora is also an electricity company within the meaning of the *Electricity Industry Reform Act 1998* and is deemed to be an energy company for the purposes of some sections of the *Energy Companies Act 1992*.

In addition to the obligations of the Local Government Act, the *Electricity Reform Act 1998*, and the *Energy Companies Act 1992*, Aurora is required to comply with the provisions of the *Companies Act 1993* which places other obligations on the Directors.

The Directors are responsible for the preparation of the Sol which, along with the three-year financial plan, is provided to Aurora's Shareholder. Monthly, six monthly and annual reports of financial and operational performance are provided to the Shareholder.

The Directors of Aurora are responsible for the overall control of the Company but no cost-effective internal control system will permanently preclude all errors or irregularities. The control systems operating within Aurora reflect the specific risks associated with the activities of the Company.

### **4.3 Information to be Reported to the Shareholder**

**Monthly reports** will be delivered to Aurora's Shareholder. These reports will comprise:

- Income Statement
- Balance Sheet
- Statement of Cash Flows
- Activity report

**Half yearly reports** will be delivered to Aurora's Shareholder within six weeks of the end of the six month period. These reports will comprise:

- Directors' Report - a review of performance over the half year
- Unaudited financial statements for the six month period.

**Annual reports** will be delivered to the Shareholder within three months of the end of the financial year. These reports will include:

- Directors' report - a review of Aurora's performance over the full year, including a comparison of performance against objectives and key performance measures
- Audited financial statements, comprising:
  - Income statement
  - Statement of movements in equity
  - Balance sheet
  - Statement of cash flows
  - Notes to the financial statements
- Auditor's report on the above financial statements and performance targets, with other measures by which the performance of Aurora has been judged in relation to its objectives.

**The Statement of Intent** covering the following financial period beginning on 1 July will be delivered to the Shareholder annually in draft form by 1 December and in final form by 30 June.

## 5 FINANCIAL AND ACCOUNTING POLICIES

### 5.1 General Accounting Policies

Aurora is a Tier-1 For-profit entity as defined by the External Reporting Board and reports in accordance with Tier 1 For-profit Accounting Standards. The Company's accounting policies are based on NZ IFRS standards and interpretations, as recognised by the New Zealand Institute of Chartered Accountants of New Zealand.

NZ IFRS standards and interpretations are subject to change and therefore the Company's accounting policies are also subject to change during the period of the Sol.

The particular accounting policies, which materially affect the measurement and reporting of financial performance and financial position, are consistent across the DCHL group and are fully listed in the Company's annual report.



## 5.2 Acquisition/Divestment

Aurora will only invest in the shares of another company or invest in an entity if the investment is considered to be likely to produce added value to Aurora. In order to maximise benefit to the Shareholder, shares or assets may also be sold in response to, or in anticipation of, ongoing changes in the marketplace.

If the Directors intend that the Company or any subsidiaries should subscribe for or otherwise acquire issued capital or an interest in any company or organisation (other than minimum holdings in listed companies in related industries) exceeding a total investment of \$5 million, they will obtain prior approval of the Shareholder.

If the Directors intend that the Company or any subsidiaries should acquire assets (other than additions to Aurora's existing electricity distribution network), they will obtain prior approval of the Shareholder where an investment into the new assets exceeds \$5 million.

The approval of the Shareholder is required before disposal by the Company of any segment of its business or shares in a subsidiary or associate company where the value of the asset to be disposed of exceeds the investment delegated authority of \$5 million.

## 5.3 Transactions with Related Parties

Dunedin City Council is the sole shareholder in DCHL. DCHL is the sole shareholder in Aurora. Transactions between Aurora, Dunedin City Council and other Dunedin City Council controlled entities will be conducted on a wholly commercial basis. Charges from Dunedin City Council and its other companies, and charges to Dunedin City Council and its other companies will be made for services provided as part of the normal trading activities of the Company.

Related party	Transaction
Delta Utility Services Limited	Provision of operating and management services and functions.
Dunedin City Holdings Limited	Provision of management services in accordance with the agreement between the parties and other functions appropriate between parent and subsidiary
Dunedin City Treasury Limited	Provision of treasury services.

## 5.4 Group Purchasing

Aurora undertakes to operate "group" purchasing of goods and services unless it is demonstrated conclusively to the Shareholder that the total combined cost to the group and to Dunedin City Council of such group purchasing is greater than the total combined cost to the group and to Dunedin City Council of ceasing to purchase such goods and services as a group, including the cost to the group and to Dunedin City Council of ceasing any such group purchasing.

## **5.5 Estimate of Commercial Value of the Investment**

The commercial value of the Shareholders' investment in Aurora is considered by the Directors to be not less than the Shareholder's funds as published in the last Annual Report.

## **5.6 Use of Otago Manufactured Goods And Services**

Aurora will endeavour to use Otago manufactured goods and services where possible, subject to price, quality and other strategic considerations being met.

## **5.7 Compensation Sought from Local Authorities**

At the request of its shareholder, Aurora may undertake activities that are not consistent with its normal commercial objectives. Specific financial arrangements will be entered into to meet the full commercial cost of undertaking such activities. At present, Aurora does not have any activities in respect of which its Board wishes to seek compensation from any local authority.

# **6 DIVIDEND POLICY**

The Directors will apply the following principles when approving dividends for payment:

- Borrowing to pay dividends should be avoided
- Individual Company policy may be based on either after tax profit or a proportion of net operating cash flow
- Asset realisation amounts are to be considered for distribution where re-investment is not required
- The Company has adopted a target Shareholder Funds to Total Assets ratio (Equity ratio) of 50% but expects this ratio will fluctuate within an indicative range of 42% to 52%, depending on a variety of circumstances including asset renewal and investment cycles. Budgeted dividend levels between DCHL and its subsidiaries will be agreed as part of the annual business planning cycle
- As a guideline, annual dividend payments will be budgeted at up to 75% of after-tax profit or net operating cash flow, subject to maintenance of the target equity ratio
- Interim dividends will be paid by 31 December and 30 June based on forecast with a final dividend based on actual year end result thereafter.

## 7 PERFORMANCE MEASURES

The following long-term indicators and targets will demonstrate continuous management improvement and are integral to the Company meeting its goals and objectives.

### 7.1 General

Performance Measure	Actual 13/14	Target 14/15	Target 15/16	Target 16/17	Target 17/18	Measured by
The Sol will be submitted to and approved by DCHL, ensuring consistency across the Dunedin City Holdings Limited Group	30 June 2013	30 June 2014	30 June 2015	30 June 2016	30 June 2017	Sol submitted to Shareholder by target date specified
Monthly financial results will be provided to DCHL in line with the agreed timetable between Aurora and the Shareholder	Monthly	Monthly	Monthly	Monthly	Monthly	Information distributed to Shareholder per agreed timeframe
Monthly board reports, which review the operating activities of Aurora for compliance with the goals and objectives stated in the Sol and the Strategic Plan will be prepared	Monthly	Monthly	Monthly	Monthly	Monthly	Information distributed to Aurora Board monthly in accordance with Board calendar

### 7.2 Network Operations

Performance Measure	Actual 13/14	Target 14/15	Target 15/16	Target 16/17	Target 17/18	Measured by
Consumer Connections (ICP Count)	84,362	84,500	85,000	85,500	86,000	Average per annum
Energy received into the Network	1,351	1,375	1,375	1,400	1,400	Gigawatt hours per annum
Load Factor %	54.05%	≥ 54.00%	≥ 54.00%	≥ 54.00%	≥ 54.00%	Energy into network/peak kW hours
Loss Ratio %	5.3%	≤ 6.0%	≤ 6.0%	≤ 6.0%	≤ 6.0%	Energy into network less energy delivered/ Energy into network
Capacity Utilisation %	30.7%	≥ 30.0%	≥ 30.0%	≥ 30.0%	≥ 30.0%	Peak network kW /installed distribution transformer capacity kVA

### 7.3 Network Reliability

Performance Measure	Actual 13/14	Target 14/15	Target <sup>1</sup> 15/16	Target 16/17	Target 17/18	Measured by
SAIDI <i>System Average Interruption Duration Index</i>						
- Class B Interruptions Planned	22.80 minutes	≤ 25.00 minutes	≤ 14.10 minutes	≤ 14.10 minutes	≤ 14.10 minutes	Average minutes without electricity per consumer
- Class C Interruptions Unplanned	71.70 minutes	≤ 73.29 minutes	≤ 76.31 minutes	≤ 76.31 minutes	≤ 76.31 minutes	
- Total	94.50 minutes	≤ 98.29 minutes	≤ 90.41 minutes	≤ 90.41 minutes	≤ 90.41 minutes	
SAIFI <i>System Average Interruption Frequency Index</i>						
- Class B Interruptions Planned	0.10	≤ 0.15	≤ 0.09	≤ 0.09	≤ 0.09	Average frequency of outages per consumer
- Class C Interruptions Unplanned	1.11	≤ 1.52	≤ 1.40	≤ 1.40	≤ 1.40	
- Total	1.21	≤ 1.67	≤ 1.49	≤ 1.49	≤ 1.49	

### 7.4 Community, Safety and Environment

Performance Measure	Actual 13/14	Target 14/15	Target 15/16	Target 16/17	Target 17/18	Measured by
Zero serious harm events involving members of the public	0	0	0	0	0	Number of serious injury events (excluding car versus pole traffic accidents) involving members of the public
Reduce harm to contractors	8.79	7.50	7.00	6.50	6.00	Total Recordable Injury Frequency Rate (TRIFR) per 200,000 man hours
Support community initiatives	\$34,000	\$40,000	\$40,000	\$40,000	\$40,000	Sponsorship \$ per annum

<sup>1</sup> Targets for 2015/15 onward reflect resetting of the default price-quality path by the Commerce Commission from 1 April 2015, with planned interruptions expressed in this table weighted at 100%, whereas the Commerce Commission applies a 50% weighting, reflecting the lower level of disruption that planned events are considered to have on consumers.

## 7.5 Financial

The following projections have been prepared using a number of realistic assumptions about the future and relate to events and actions which have not yet occurred and may not occur. In deriving these projections, judgement has been applied to the uncertain future regulatory and commercial environments in which Aurora operates.

Financial year ending 30 June	13/14 Actual \$000	14/15 Budget \$000	15/16 Target \$000	16/17 Target \$000	2018 Target \$000
EBITDA (before subvention)	40,748	38,797	41,592	43,883	45,980
Net surplus (before subvention)	12,900	10,949	11,606	12,425	13,598
Shareholder's funds	180,983	182,372	186,478	191,403	197,493
Cash flow from operations	24,278	31,553	31,680	31,541	33,007
Capital expenditure	21,260	32,948	34,624	24,249	22,908
Term debt	138,800	158,600	174,950	178,800	179,600
Dividends/subvention	10,000	9,500	7,500	7,500	7,500

### At 30 June

Shareholder's funds to total assets	46.3%	44.2%	43.0%	43.2%	43.8%
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Aurora has adopted a target Shareholder Funds to Total Assets ratio (Equity ratio) of 50%, but expects this ratio will fluctuate depending on a variety of circumstances including asset renewal and investment cycles. During periods of higher capital expenditure, the Equity ratio will likely be lower and, at other times, may exceed the current target of 50%.

"Shareholder's funds" are represented by the paid up capital, reserves created by the revaluation of specific assets, and retained earnings.

"Total assets" means the aggregate amount of all current and non-current assets.

### Key assumptions

The key assumptions employed during the preparation of our financial performance targets included:

- Projected future revenue streams were based on the Commerce Commission's five-year default price-quality path (DPP) settings for the Company from 1 April 2014
- All price changes are "passed" through to customers
- Opex and capex in line with the Company's approved and published 10 year electricity distribution network asset management plan (AMP) effective from 1 April 2014
- No unforeseen impairments to existing asset values
- No major investments/divestments
- No large natural disasters
- No future decisions by the Government, the Commerce Commission or the Electricity Authority resulting in a materially adverse financial impact on the Company.