Summary of Directors Report to the Trustees of the Electra Trust*

Electra Limited: Ownership Review

The Trustees support the Directors' conclusion that the objectives of Electra Limited are best achieved with the current 100% Trust ownership structure. It is considered to be the best outcome for the consumers of Kapiti and Horowhenua.

*Full report available at www.electratrust.co.nz

Executive Summary

The Directors of Electra Limited have prepared this report in response to the request by the Trustees under the Electra Trust Deed. Clause 4 of the Deed states that the Trustees shall require the Directors to prepare a report considering proposals and available options for the future ownership of the shares of Electra Limited. The Trust currently owns 100% of the shares in Electra Limited and this ownership review is pursuant to a resolution by the beneficiaries of the Trust in 2019. Clause 4 specifically requires the Directors to set out their conclusions as to the most appropriate form of ownership for the future period.

Key conclusions following the review are:

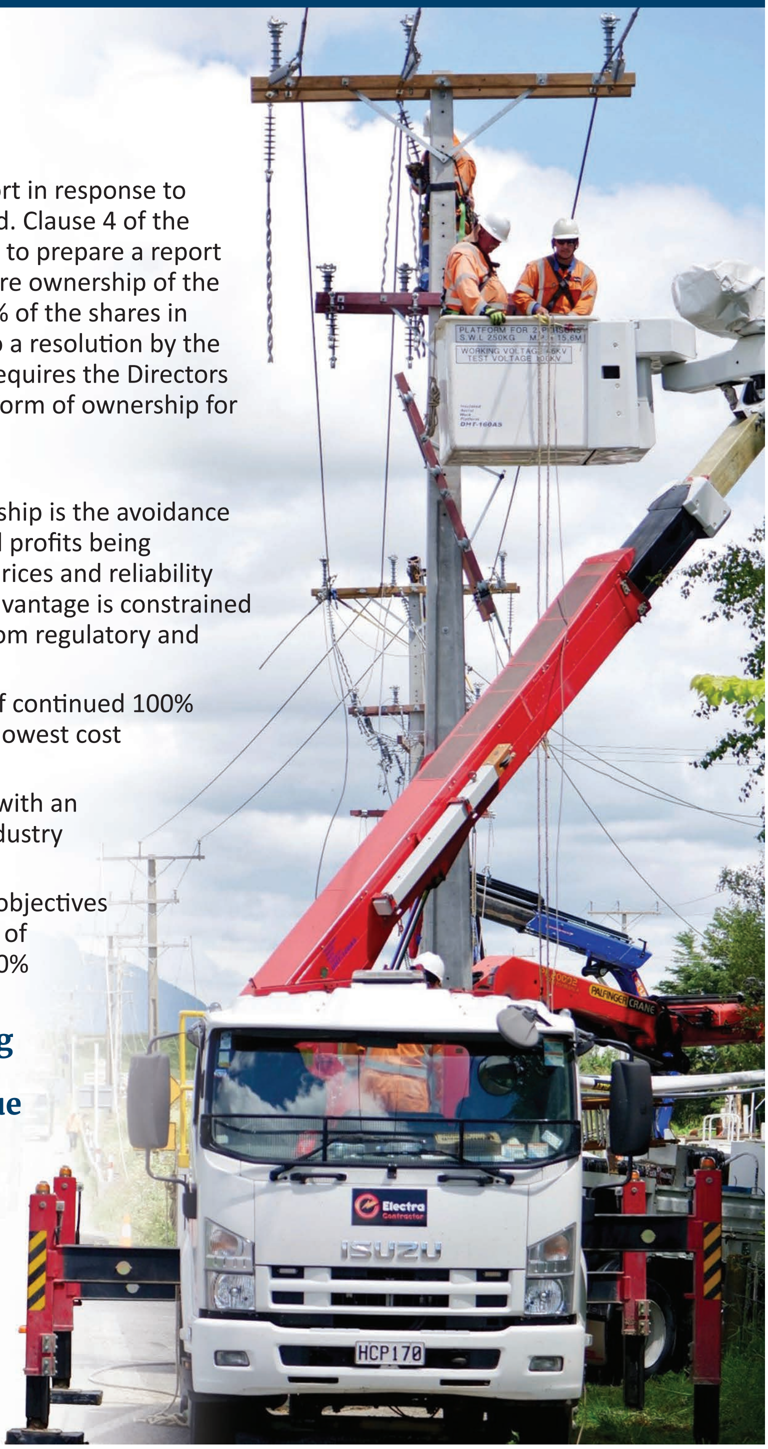
- The main advantage of continued 100% Trust ownership is the avoidance of tension between investing in supply reliability and profits being distributed to non-beneficial owners thus ensuring prices and reliability remain both competitive and efficient. The key disadvantage is constrained capital which reduces the ability to diversify away from regulatory and technology stranding risk.
- Of all the ownership options examined, the option of continued 100% Trust ownership would provide the most stable and lowest cost ownership model.
- Electra Limited's performance compares favourably with an identified group of comparators across a range of industry performance measures.

The Directors of the Company have concluded that the objectives of Electra Limited, as reflected in the current Statement of Corporate Intent, are best achieved with the current 100% Trust ownership structure.

The Directors were unanimous in reaching this conclusion and recommend: That the shares of Electra Limited continue to be 100% owned by the Electra Trust.

For and on behalf of the Directors.

Shelly Mitchell-Jenkins
Chair
22 May 2020



2. Analysis of the Trust's performance

Electra Trust's operating costs are lower than the operating costs of comparable trusts.

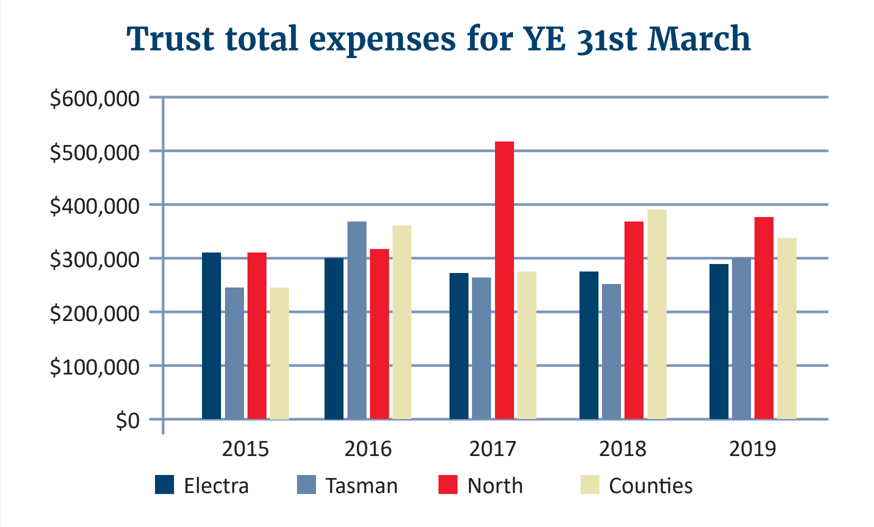
2.1 Comparators for performance analysis

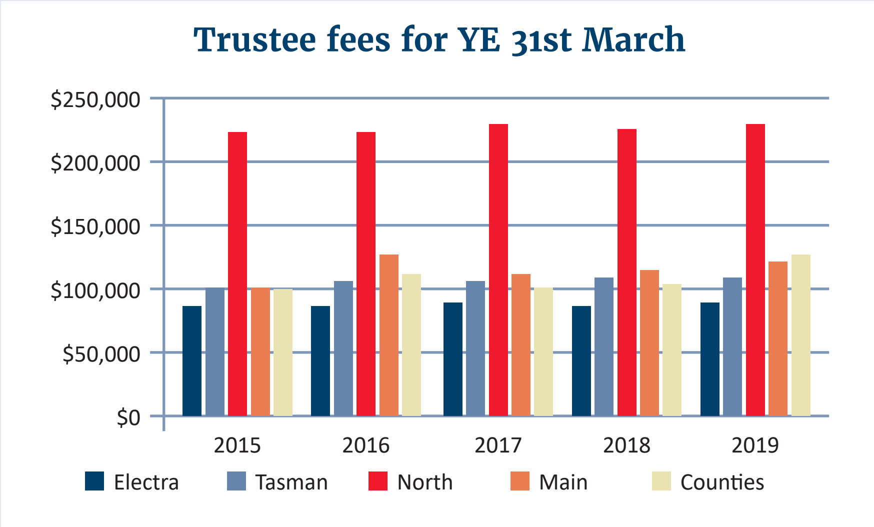
The Trust has approximately 45,600 beneficiaries. The following other energy trusts have been chosen as a Trust Comparable Group due to similar Trust beneficiaries' size. Network Tasman Trust ("Tasman"), Northpower Trust ("North"), MainPower Trust ("Main") (not all data available), Counties Power Trust ("Counties").

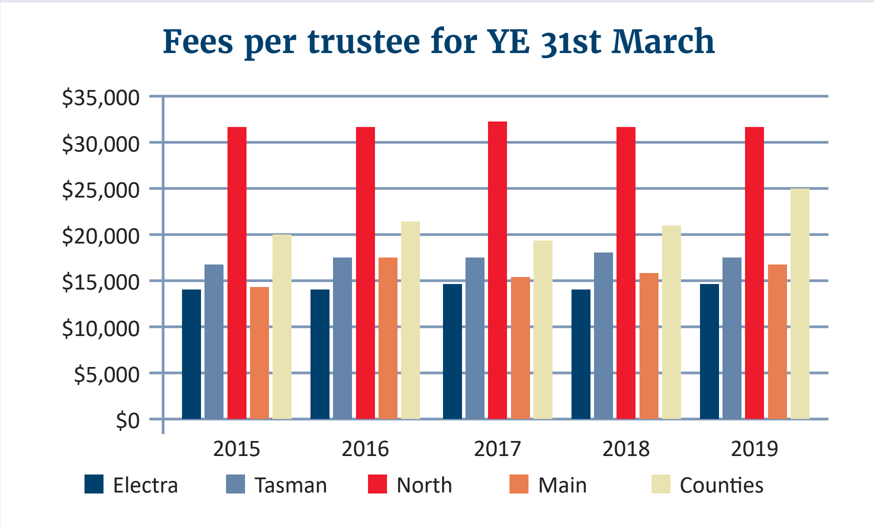
2.2 Performance comparisons

The following performance comparisons for Electra and the Trust Comparable Group are detailed for the years ending 31st March 2015, 2016, 2017, 2018 and 2019.

- Trust total expenses
- Trustee fees







3. Advantages and disadvantages of Trust ownership

- The key advantage of Trust ownership relative to the alternative ownership options examined is that 100% Trust ownership provides the most stable and lowest cost ownership model.

Summary:

- Avoids the tension between investing in supply reliability and paying dividends to non-beneficial owners.
- Ownership and management remain localised enabling strategic focus on regional benefits for the wider community.
- More likely to seek professional advice on industry issues as the Trust is not subject to operating cost constraints.
- Direct financial benefits flow to beneficiaries or community including initiatives such as local business network sponsorship.
- Avoids distributions being taxed in the hands of beneficiaries.
- Ability for a single shareholder to appoint a unified Board.

However:

- Ability to raise capital is limited to debt or retained earnings as 100% percentage ownership by the Trust means ability to introduce new equity is limited. Practically new equity in the core business is limited to retained earnings. However, Electra can share ownership in subsidiaries as a way of introducing equity. E.g. Electra has 50:50 joint ownership in Connect 8 Limited.
- Concentration of regulatory and technology stranding risks associated with delivery of centrally generated energy through poles and wires.

Benefits of trust ownership to consumers

The benefits to consumers of 100% trust ownership include:

- The discounts and dividends paid by the Company to its stakeholder(s) are attributed to the connected consumers rather than to a third-party owner.
- A trust representing beneficial owners is more likely to be able to afford and engage suitable external advice on either continued ownership or disposing of the shares in the Company, than individual shareholders.
- A single shareholder is likely to lead to a Board that is more united, and able to focus its efforts to improving company performance rather than reconciling potentially competing shareholder interests.
- The Company is likely to give more weight to consumer needs than if it had remote shareholders. Over-all there is a large local benefit.

The key disadvantages of 100% trust ownership include:

- Constrained ability to raise capital limiting opportunity to:
  - Diversify away from regulatory risk.
  - Diversify away from technology stranding risk.

4. Analysis of ownership options

Option 1 – Share distribution to Beneficiaries

Whether or not a controlling stake is retained by the Trust, a possible outcome of this option is that some of those distributed shares would be on-sold (either to another EDB keen on consolidation, or simply to another investor).

Option 2 – Sale of shares to the public

Broadly speaking, any sale of more than 10% of shares in the Company to non-customers would make the Company subject to a default price-quality path, providing a degree of customer protection against excessive price increases , however further additional compliance costs would be passed onto consumers via line charges.

Option 3 – Sale of shares to an institutional investor

This option could result in conflicting objectives for the Company (the Trust trying to balance returns with reliability, and the institutional investor focusing on returns), resulting in continual tension at Board level. This may compromise ability to fully deliver on community expectations for quality of service and regional development, even where the Trust has a controlling interest.

Option 4 – Exchange of shares for shares or assets of another company

Any sale of more than 10% of Electra shares to non-customers would make the Company subject to a default price-quality path, providing a degree of customer protection against excessive price increases, however further additional compliance costs would be passed onto consumers via line charges. The cash return on the shares received by the Trust would need to achieve a risk-adjusted cash return equivalent to the current customer discounts.

Option 5 - Retain full Trust ownership

Retains Electra's exempt status (reducing compliance costs), ensures that line charges, after discounts, are optimised for current and future customers. Ownership and management remain localised, enabling strategic focus on regional benefits for the wider community.

5. Comparison of Company performance with other Line companies (customers per line km)

- ***Electra has the lowest revenue per customer within the Electra Comparator Group.***
- ***Electra has among the lowest costs within the Electra Comparator Group.***
- ***Electra has higher reliability than the Electra Comparator Group.***

Measure	Performance	Comments
Return on investment	Electra has the highest return on investment before discount within the Electra Comparators Group.	
Revenue	Electra has the lowest revenue per customer within the Electra Comparators Group.	Customers could be more likely to see revenue stated on a per kWh basis on their electric bill, which makes Electra appear less favourably due to Electra's lower average KWH usage per customer.
Operating expenditure	Electra's operating expenditure is around the average of the Electra Comparators Group.	Detailed analysis suggests that any reduction in Electra's operating expenditure could lead to an increase in both equipment faults and tree-related faults.
Capital expenditure	Electra's capital expenditure is the lowest of the Electra Comparators Group.	Capital expenditure is a complex issue that depends on demand growth and asset condition, which tend to be unique to each network. Hence care is required in interpreting comparisons between networks.
Reliability	The power is off to Electra's average customer for less time per year than for customers of the Electra Comparators Group.	
	Electra's average customer has fewer interruptions per year than customers of the Electra Comparators Group.	

This comparison shows that Electra's performance compares very favourably with the Electra Comparator Group.

6. Regard to views of Beneficiaries

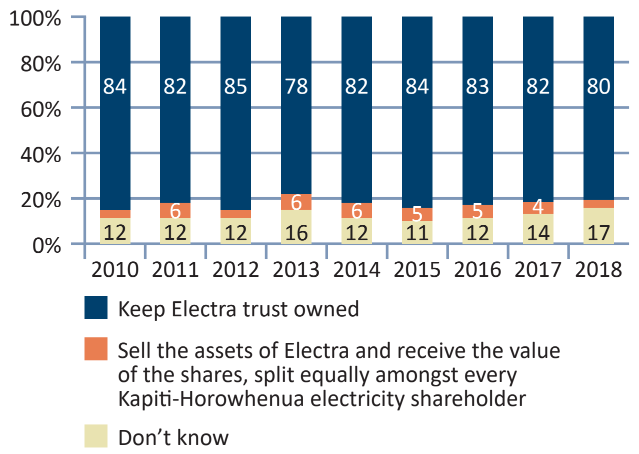
- Beneficiaries prefer the continued community involvement and support that 100% trust ownership provides.

Based on previous indications, beneficiaries may be reluctant to sell the company's assets to a major buyer. End-users have indicated in a recent survey in April 2019 as follows:

Question: "If you were to vote on Electra's Trust ownership tomorrow, how would you vote?"

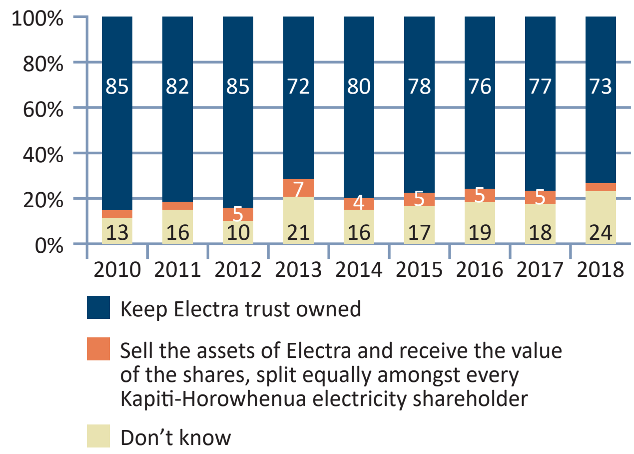
Residential

(n=200)



Commercial

(n=100)



Electra

electra.co.nz