2016 ANNUAL REPORT >> MERCURY NZ LIMITED


CREATING ENERGY WITH INFINITE POSSIBILITIES.


Mercury

AT MERCURY WE SEE A NEW ENERGY FUTURE THAT PROMISES GREATER BENEFITS FOR OUR CUSTOMERS, THIS COUNTRY AND GENERATIONS TO FOLLOW.

WE HAVE A WONDERFUL FOUNDATION IN NEW ZEALAND'S RENEWABLE ENERGY, WHICH IS ALSO A STRENGTH FOR OUR BUSINESS.

WE'RE EXCITED BY THE POSSIBILITIES WITH NEW TECHNOLOGY. WE'RE DRIVEN BY WHAT OUR CUSTOMERS WANT AND THEIR EXPECTATIONS FOR TOMORROW.

AT THE HEART OF OUR AMBITION IS DELIVERING SUSTAINABLE VALUE, INNOVATION AND OUTSTANDING EXPERIENCES.

GIVING KIWIS MORE ENERGY IN LIFE.


Mercury

OUR PURPOSE.

Inspiring New Zealanders to enjoy energy in more wonderful ways

Inspiring New Zealanders

We want to inspire New Zealanders by delivering value, innovation and outstanding experiences.

To enjoy energy

We want our customers to enjoy what energy does for them and choose Mercury because we make a positive difference in their lives.

In more wonderful ways

We will bring new technology and ideas to create wonderful experiences for our customers in a uniquely New Zealand context.

OUR GOAL.

To be New Zealand's leading energy brand

OUR STRATEGY.

Mercury will create long term value for our owners by:

1 DELIVERING CUSTOMER ADVOCACY

Outstanding customer experience

Leading digital offerings

Culture-driven innovation

2 LEVERAGING CORE STRENGTHS

Operational efficiency

Astute portfolio management

Efficient capital allocation

3 DELIVERING SUSTAINABLE GROWTH

Executing relevant strategic opportunities

Being ready for domestic growth

Embracing emerging technologies

ABOUT THIS REPORT.

At Mercury we have a genuine focus on the long term. This drives the way we do business, provide services to customers, our investment decisions, partnerships with stakeholders and our approach to reporting.

Our 2016 Annual Report includes our full financial statements and notes for the year ended 30 June 2016, along with commentary on the company's performance and outlook. This report outlines our goal, purpose, strategic priorities and an overview of Mercury's business (AT A GLANCE). For the first time, we have illustrated our business model and report on five key pillars (WHAT MATTERS MOST) that are important to our stakeholders and the business in sustaining and growing value.

The Corporate Governance section of this report describes how we set the objectives and direction for the business, and the framework for identifying and managing risks. Our corporate governance policies are available online at: mercury.co.nz/About/Leadership/Corporate-Governance. ●

The company changed its name from Mighty River Power Limited to Mercury NZ Limited on 29 July 2016. Our New Zealand Business Number (NZBN) is 9429037705305

This report is dated 23 August 2016 and is signed on behalf of the Board of Mercury NZ Limited by Chair, Joan Withers and Director, Keith Smith.

>> **JOAN WITHERS**, CHAIR

>> **KEITH SMITH**, DIRECTOR

REPORT CARD.

>> FINANCIALS

$493M ^

EBITDAF UP $11M, REFLECTING HIGHER GENERATION PARTIALLY OFFSET BY LOWER RELATIVE GENERATION PRICES AND THE ROLL-OFF OF SPECIFIC COMMERCIAL SALES CONTRACTS.

$160M ^

NET PROFIT $113M HIGHER DUE TO IMPAIRMENTS IN FY2015 AND IMPROVED EBITDAF IN FY2016.

$221M ˇ

FREE CASH FLOW DOWN 4%, WITH A SHORT-TERM PREPAYMENT OF TAX OFFSET BY REDUCED STAY-IN-BUSINESS CAPEX.

$14.3CPS ^

ORDINARY DIVIDEND PLUS AN ADDITIONAL 4CPS UNIMPUTED SPECIAL DIVIDEND.

>> CUSTOMERS

61%

OF MERCURY CUSTOMERS RATING AS 'HIGHLY SATISFIED'.

42%

OF MERCURY RESIDENTIAL CUSTOMERS ON FIXED-PRICE CONTRACTS.

>> COMMUNITY

$100K

EMPLOYEE COMMUNITY FUND ACROSS 79 PROJECTS.

$1.0M

DONATED TO STARSHIP CHILDREN'S HEALTH THROUGH STAR SUPPORTERS CLUB AND SPONSORSHIP.

>> PEOPLE

ZERO

HIGH SEVERITY INCIDENTS.

95%^

OF EMPLOYEES BELIEVE MERCURY IS COMMITTED TO THE HEALTH AND SAFETY OF ITS PEOPLE.

>> ENVIRONMENT

100%^

GENERATION FROM RENEWABLE RESOURCES FROM 1 JANUARY 2016 FOLLOWING SOUTHDOWN CLOSURE.

FULL COMPLIANCE

WAIKATO REGIONAL COUNCIL COMPLIANCE ASSESSMENT OF WAIKATO HYDRO SYSTEM ACROSS 121 CONSENT CONDITIONS.

BUILDING ON OUR STRENGTHS FOR THE FUTURE.

29 July 2016 was a significant day for our company. We introduced our owners, our customers and stakeholders to our new Mercury identity.

For the first time, we now have all of our energy and focus behind this single brand. Mercury weaves together a 90-year heritage in renewable generation with one of New Zealand's longest-established energy retail businesses. This is a taonga, a strength for our future.

OUR MISSION

The Mercury bee on the cover of this 2016 Annual Report symbolises our ambitions.

We see a new energy future, with benefits for Kiwi consumers and the country from advancing technology and renewable energy. Across Mercury, we have a very clear purpose: *Inspiring New Zealanders to enjoy energy in more wonderful ways.*

This is about building on the underlying strengths that show through in Mercury's operational performance and financial results this year.

Our electricity production is 100% renewable and close to large populations and demand centres. The Waikato Hydro System is the largest in the North Island, flexible and rain-fed. We also have a proven track-record in innovation for customers, in working with Maori landowners and through other valued relationships that help us sustainably harness natural energy resources.

These are competitive advantages for Mercury in evolving energy and retail landscapes.

Today customers are expecting much more from us than just generating the power that's delivered into their home. We are in a new era where New Zealanders are looking far beyond the light switch, embracing new technologies and valuing what renewable energy can do for them.

We want Mercury to stand out with customers for how we use energy in different ways to improve their lives.

We are also inspired by the unparalleled benefits for New Zealand in renewable energy.

At Mercury we call this 'Energy Freedom'. Every day we are focused on that mission.

FINANCIAL STRENGTH

Mercury is reporting a 2.3% lift in operating earnings (EBITDAF) to $493 million for FY2016, reflecting steady customer sales in a highly-competitive market and the strength of our renewable generation portfolio.

The strong cash flows in our business mean that more than 90,000 Mercury owners, including the Crown, will receive a final ordinary fully-imputed dividend of 8.6 cents per share (8 cents net of Resident Withholding Tax). This brings the full year fully-imputed ordinary dividend to a total of 14.3 cents per share, in line with guidance. This is a 2% increase on FY2015.

With our continuing focus on active capital management, and the current limited requirement for growth capital, we will be returning value to shareholders through an additional unimputed special dividend of 4 cents per share (2.68 cents net of Resident Withholding Tax).

This level of distribution represents both 100% of Free Cash Flow and the proceeds from land sales completed over the past two years. Both dividends are payable on 30 September 2016.

We are pleased to be returning $252 million to our shareholders for the full year, underscoring the strength of our company in a period of significant change and progress for the business, including our rebranding to Mercury at the end of July.

Net profit for the year increased $113 million to $160 million due to impairments in the prior period and the company's improved EBITDAF in FY2016. Underlying earnings after tax increased by $7 million or 4.8% to $152 million, reflecting the improved operating earnings.

CUSTOMER LED

During the year, our focus on rewarding customer loyalty, with initiatives such as Free Power Days, contributed toward higher customer satisfaction.

The average percentage of Mercury's residential customers rating as 'highly satisfied' over the past 12 months was 61%, significantly above all of the other major retail electricity brands, though short of our ambition. We have also gathered valuable insights through the development of our new brand and from research during the year involving our commercial and industrial customers.

We continue to be the brand of choice in New Zealand's largest and fastest-growing market, Auckland. As we look to build on the strong housing and population growth in the Auckland region, we are encouraged to see the powerful loyalty around Mercury. Independent measurement by the Electricity Authority shows customer switching (churn) in this primary geography for Mercury is 7% better than the other brands in this market.

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WE ARE PLEASED TO BE RETURNING $252 MILLION TO OUR SHAREHOLDERS FOR THE FULL YEAR, UNDERSCORING THE STRENGTH OF OUR COMPANY IN A PERIOD OF SIGNIFICANT CHANGE AND PROGRESS FOR THE BUSINESS.

>> **JOAN WITHERS**
CHAIR

Our fixed-price contracts remain popular, offering pricing certainty. Fulfilling this customer consideration has driven an increase in the proportion of residential customers choosing this option, up from 35% in FY2015 to 42% at year-end. Some of this growth was through a two-year fixed-price offer in conjunction with our energy price changes this financial year.

An increase in Mercury's commercial sales lifted overall volumes in the final quarter of the financial year. This contributed to a 4% fall in the average energy price to customers as new commercial contracts replaced higher-priced contracts signed between FY2011 and FY2013.

Mercury remains the leader in the breadth of customer services that use smart meters, including our Good Energy Monitor (GEM), Free Power Days, GLOBUG, and our electric vehicle off-peak charging package.

Investment in brand promotions and loyalty initiatives led to higher spend in the first half of the year, particularly to support growth in the pre-pay segment with GLOBUG. However, operating costs were flat year-on-year and included prudent investment in the rebrand to Mercury. We expect cost-savings from removing duplication and longer-term value from consolidating our focus.

This alignment between our company positioning and our customer brand is pivotal to relationships such as our Airpoints™ partnership with Air New Zealand announced in June.

Our companies share similar philosophies on sustainability and in aligning purpose with customers and the country. We were the first two companies in New Zealand to commit our car fleets to electric, and this agreement for Mercury to be the energy services provider for Airpoints™ is a natural extension, offering great potential to reward our customers.

RENEWABLE GENERATION

Mercury's annual hydro generation typically makes up about 10% of New Zealand's total electricity supply, and our geothermal about 7%.

Hydro generation was up 16% on the previous year to 3,866GWh. However, this was lower than the historical average of 4,000GWh due to low inflows to the Waikato River catchment. Geothermal generation was up 2% to a record 2,830GWh. Reduced volatility in the wholesale market led to subdued average pricing with a greater impact on generation prices (GWAP) relative to electricity purchase costs (LWAP).

Mercury's generation is now 100% renewable, with benefits that go well beyond our business, from climate change to provincial employment.

THE WAIKATO HYDRO SYSTEM IS A DISTINCTIVE STRENGTH FOR US, AND INTEGRAL TO NEW ZEALAND'S ELECTRICITY SUPPLY.

Renewable energy offers New Zealand's greatest green-growth opportunity, with the electrification of transport having absolutely compelling logic in this country. This is where we are leading a conversation around energy that has the potential to make a genuinely better future and a better world for generations that follow.

STRATEGIC EVOLUTION

Our new brand is part of a journey for Mercury to be truly customer-led. This change reflects a series of planned, strategic moves over the past year to position the company for the future. These include the closure of our thermal plant, acquisition of solar capability and changes to the Mercury lead team with the addition of new GM Digital Services and Chief Marketing Officer roles.

These decisions have been a deliberate part of creating opportunities for Mercury around service innovation and renewable energy.

Over the 2016 financial year the company's revenue from third-party metering and energy data services increased with additional meters deployed, reaching 396,000.

We recognised $13 million from the disposal of land, including parcels around the site of the former Marsden Point power station to the Office of Treaty Settlements.

This largely concludes the company's non-core land sales programme.

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OUR NEW BRAND IS PART OF A JOURNEY FOR MERCURY TO BE TRULY CUSTOMER-LED. THIS CHANGE REFLECTS A SERIES OF PLANNED, STRATEGIC MOVES OVER THE PAST YEAR TO POSITION THE COMPANY FOR THE FUTURE.

>> **FRASER WHINERAY**
CHIEF EXECUTIVE

WE WANT MERCURY TO STAND OUT WITH CUSTOMERS FOR HOW WE USE ENERGY TO IMPROVE THEIR LIVES. AT MERCURY WE CALL THIS 'ENERGY FREEDOM'.

Over the past year we have continued to contribute to and build on New Zealand's position as a global superpower in renewable electricity, while advocating new technologies such as electric vehicles, e-bikes, solar, smart homes and other data services that are creating opportunities for growth.

As we reported at the half year, the addition of solar capability is strategically important as we look to shape new customer offerings with our mission and purpose in mind.

Solar is a growing niche and the purchase of the well-established solar business, What Power Crisis, with a track-record in both New Zealand and the Pacific, adds proven expertise delivering both on-grid and off-grid solutions with storage.

We are very pleased with the momentum that we have created through consistent and sustained advocacy for the electrification of transport. Our fleet conversion to electric and plug-in hybrid vehicles is well underway and this has been a powerful example to other organisations.

A standout in the year was to be invited to stand alongside the Prime Minister and the Minister of Transport, Energy and Resources at the launch of the Electric Vehicle Partnership Programme in May. This shows just how much the conversation has moved in a few short years from electricity "issues" to transformational opportunity. The focus has turned to how we can sustainably enjoy this home-grown energy for Kiwis and the country.

CORE INVESTMENT

Our capital expenditure remains largely focused around the ongoing hydro reinvestment programme to improve the operational efficiency and long-term reliability of these key stations on the Waikato River, geothermal well drilling to sustain performance, and the further roll-out of smart meters and related technology by Metrix.

The Waikato Hydro System is a distinctive strength for us, and integral to New Zealand's electricity supply.

Lake Taupo and the eight dams provide large-scale, economic energy storage, and the nine stations are highly responsive. Mercury has 39 individual hydro generating units on the river that can quickly ramp up to meet residential and commercial demand peaks in the upper North Island.

The Waikato is New Zealand's most important and diverse water catchment at both a national and regional level, supporting pastoral and horticultural production and as a source of drinking water for more than 1.5 million people.

Mercury's primary interest is in harnessing the energy in the flow of the Waikato River for hydro generation. However, we approach this commercial imperative from a much broader perspective. This involves us maintaining a strong involvement in the growing discussion around fresh water quality and allocation, and we are pleased to be able to contribute our long-term view around the health and wellbeing of the catchment.

Both our company and the country benefit from making the best possible non-consumptive use of the flow available for hydro generation, and keeping the water in the river system.

A decade-long programme of lifecycle and maintenance investment in these vital assets is well underway, with the current focus on planning major projects at Whakamaru and Aratiatia hydro stations. This will improve efficiency, availability and reliability over the long-term. These projects and our scheduled geothermal drilling programme in the Central North Island to maintain the productivity from key reservoirs are forecast to more than double reinvestment spend from $59 million to more than $120 million in FY2017.

We are ready for domestic growth, with two highly-productive consented wind sites in the North Island, at Turitea and Puketoi, and other renewable generation opportunities when commercial conditions are right to add to our portfolio.

SAFETY CULTURE

Safety is a primary consideration for these projects, with close collaboration in planning and activity between our people and contractors. Our goal is "zero harm" across the business.

The results we achieved in FY2016 were pleasing evidence of a robust health and safety culture, beating our targets and New Zealand benchmarks. The trend over the past five years has been one of improving performance.

NEW ZEALAND'S MOVE FROM FOSSIL FUEL TO RENEWABLE ELECTRICITY GENERATION IS THE SINGLE-BIGGEST REDUCTION ACHIEVED TO DATE IN OUR COUNTRY'S EMISSIONS PROFILE... MORE THAN 2 MILLION TONNES OF CARBON EMISSIONS PER YEAR.

We were also pleased to see the benefit that has come from the uniquely collaborative StayLive initiative. It is remarkable to see the real results that have been achieved since the five major electricity generators came together in 2011 and Transpower joined in 2012. This community is proving the value of putting intense competition aside when it comes to safety, learning from each other and sharing our experiences.

GREAT PEOPLE

Another key focus is employee engagement and developing a customer-centric culture aligned with our new Mercury brand. The overall health of our business showed through in strong and improving engagement scores in FY2016 and very high recognition of the importance that we place on both wellbeing and environmental responsibilities.

Talent development and leadership training are areas of investment to lift both business performance and the strategic capability behind the transition to Mercury. Our management training programme, StepUP, is a key component of our drive to embed a high performance culture where all of our people are able to give their best.

In terms of our governance, Mike Taitoko joined our Board in August last year and we've welcomed his fresh insights to economic development, commercial experience in the digital space, and also his well-established networks into communities. Nicky Ashton has also joined our Board for an 18-month term as a Future Director as part of the Institute of Directors' programme. This reflects our confidence in the benefits of this initiative to both the company and to our previous appointee, Carolyn Luey from NZME. Nicky is GM Brand & Marketing for Kiwibank, and is joining us at an exciting time as we focus on our new Mercury brand and related initiatives with customers.

On the Mercury leadership team this year, we welcomed Julia Jack as our new Chief Marketing Officer and Kevin Angland as GM Digital Services. These two complementary roles support our focus on customer-led innovation.

FUTURE OPPORTUNITY

There has been a fundamental and positive change in sentiment around electricity in New Zealand since our company's listing in 2013.

The overall picture of the New Zealand electricity market is healthy, with two years of steady demand growth and a well-balanced market. A large amount of thermal generation has been retired, largely on the back of geothermal investment over the past decade. New Zealand's move from fossil fuel to renewable electricity generation is the single-biggest reduction achieved to date in our country's emissions profile. In total the displacement from geothermal equates to a cut of more than 2 million tonnes of carbon emissions per year.

As we focus on long-term outcomes for our customers and the country, we value a stable and well-functioning regulatory environment in New Zealand. It is an essential ingredient to deliver high levels of energy security, unprecedented choice for customers and 80% renewable electricity supply and rising.

Thank you to our customers for your loyalty, our owners for your support, and our people for your commitment and professionalism. Thank you to our business partners and to the many people and organisations sharing mutual relationships with Mercury that drive our success.

We have a new name that has meaning for us all. ●

Together we are Mercury.
Energy made Wonderful.

>> **JOAN WITHERS**, CHAIR

>> **FRASER WHINERAY**, CHIEF EXECUTIVE

YOUR DIRECTORS.
>>

PLEASE SEE OUR WEBSITE FOR FULL BIOGRAPHIES.


>> JOAN WITHERS
CHAIR


>> JAMES MILLER
DIRECTOR

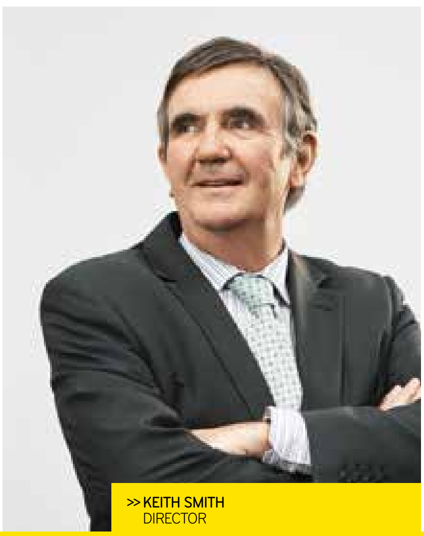

>> MIKE ALLEN
DIRECTOR


>> MIKE TAITOKO
DIRECTOR


>> PRUE FLACKS
DIRECTOR


>> PATRICK STRANGE
DIRECTOR


>> ANDY LARK
DIRECTOR


>> KEITH SMITH
DIRECTOR

OUR LEADERSHIP TEAM.

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PLEASE SEE OUR WEBSITE FOR FULL BIOGRAPHIES.

>> **FRASER WHINERAY**
CHIEF EXECUTIVE

>> **MATTHEW OLDE**
METRIX CHIEF EXECUTIVE

>> **TONY NAGEL**
GENERAL MANAGER CORPORATE AFFAIRS

>> **JULIA JACK**
CHIEF MARKETING OFFICER

>> **WILLIAM MEEK**
CHIEF FINANCIAL OFFICER

>> **KEVIN ANGLAND**
GENERAL MANAGER DIGITAL SERVICES

>> **PHIL GIBSON**
GENERAL MANAGER HYDRO & WHOLESALE

>> **MARLENE STRAWSON**
GENERAL MANAGER PEOPLE & SAFETY

>> **NICK CLARKE**
GENERAL MANAGER GEOTHERMAL

AT A GLANCE.

Mercury is an electricity retailer and generator providing energy services to homes, businesses and industrial customers throughout New Zealand.

We have a long heritage in renewable energy in New Zealand serving about 1-in-5 homes and businesses under the Mercury brand and other specialty brands, including the leading pre-pay product GLOBUG. We also have proven capability and technical expertise in smart metering services and solar.

Our electricity generation is 100% renewable, with the hydro and geothermal power stations operated by Mercury producing enough renewable electricity for about 1 million New Zealand homes. We have established a leadership position in encouraging the electrification of transport, supporting the adoption of e-bikes and electric vehicles and partnering on non-home charging infrastructure.

Our goal is to be the leading energy brand in New Zealand, inspiring New Zealanders by delivering value, innovation and outstanding experiences.

WE REPRESENT **14%** OF NATIONAL SALES

WE HAVE **825** EMPLOYEES

WE REPRESENT **17%** OF NATIONAL GENERATION

>> SOUTH ISLAND

> MERCURY

	FY16	YOY CHANGE
GENERATION VOLUME (GWh)	0	N/A
PHYSICAL SALES VOLUME[1] (GWh)	703	1.4%
CUSTOMERS (000)	37	8.8%
AMI METER ASSETS (000)	14	2.0%

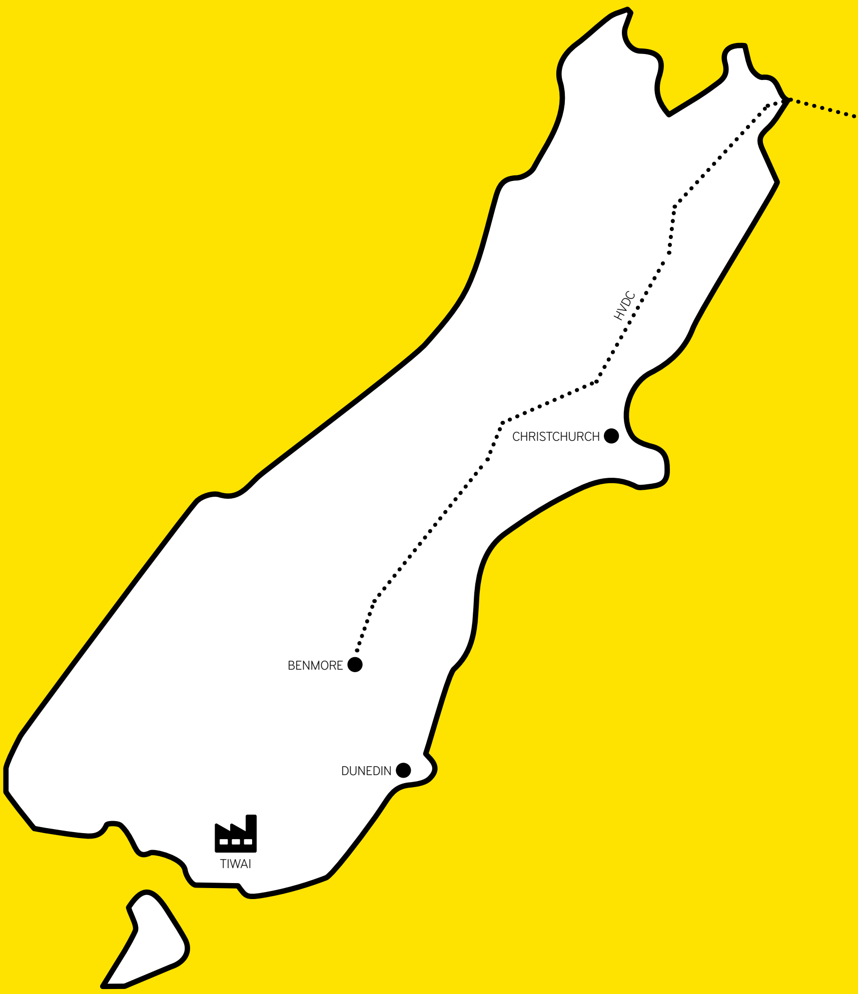
> INDUSTRY

FY16 MARKET SHARE

GENERATION SALES

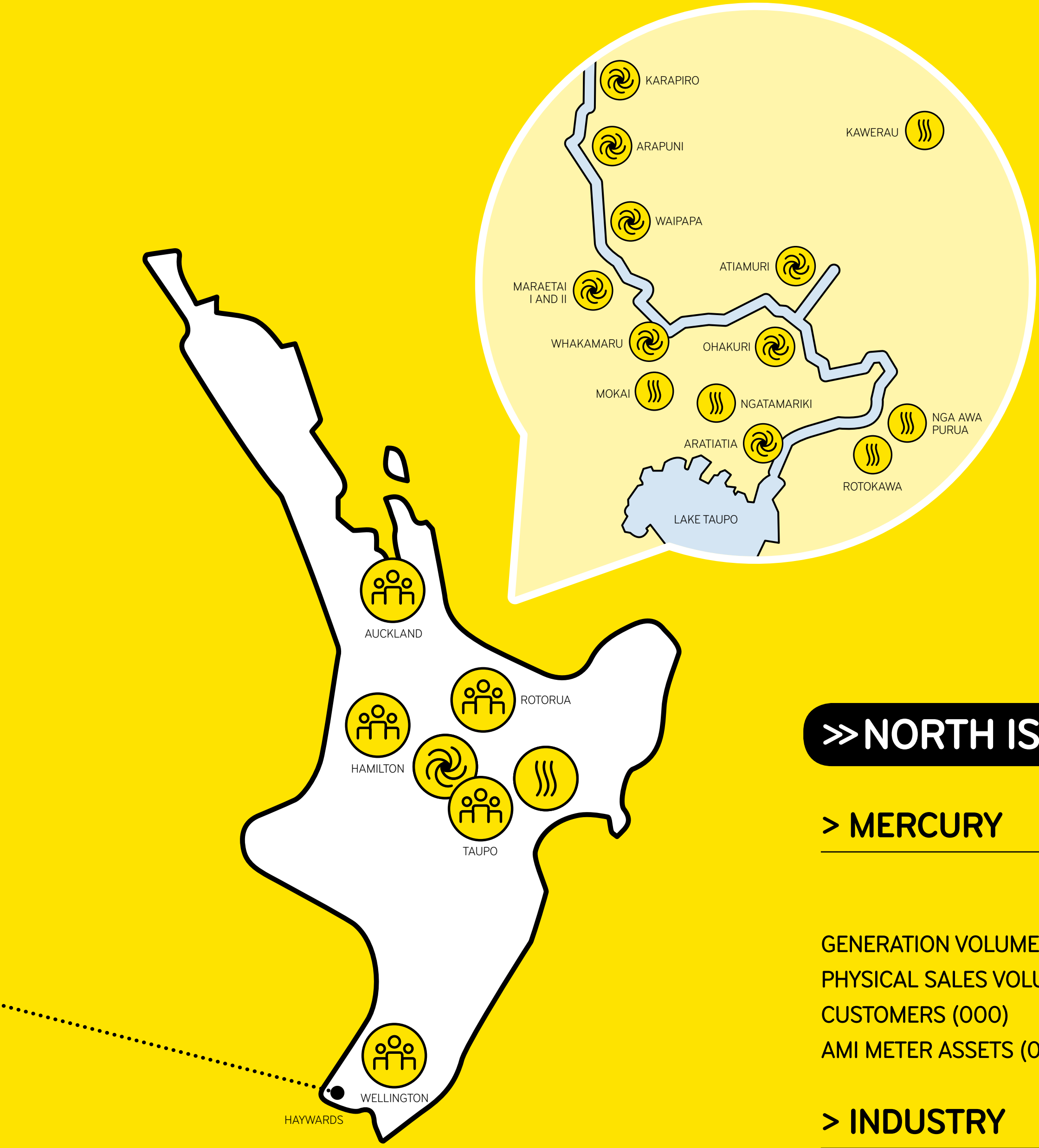
> TOTAL

	FY16	YOY CHANGE
DEMAND (GWh)	14,750	0.1%
POPULATION[2]	1,076,200	1.7%
GDP[2] (000,000)	56,232	3.7%



1 Based on NZEM purchases.

2 Based on 2015 Statistics New Zealand data, 2016 data not yet available.



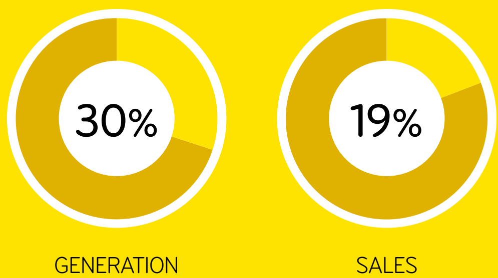
>> NORTH ISLAND

> MERCURY

	FY16	YOY CHANGE
GENERATION VOLUME (GWh)	6,842	4.3%
PHYSICAL SALES VOLUME[1] (GWh)	4,890	-9.6%
CUSTOMERS (000)	339	-2.6%
AMI METER ASSETS (000)	382	2.1%

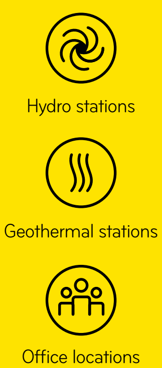
> INDUSTRY

FY16 MARKET SHARE



> TOTAL

	FY16	YOY CHANGE
DEMAND (GWh)	25,314	0.4%
POPULATION[2]	3,518,900	2.0%
GDP[2] (000,000)	184,955	3.8%



OUR BUSINESS MODEL.

How Mercury sustains and grows value

Mercury has a very long-term focus to deliver benefit for all of our customers, owners, employees and partners. At the foundation of our business is the wellbeing of our people and customers, together with deep respect for kaitiakitanga, the custodianship of natural resources, and commercially astute decisions.

RESOURCES

INTERNAL

- Skilled people and diverse thinking
- Retail brands and capability to execute specialised offerings
- Power stations: geothermal and hydro
- Financial and intellectual resources to invest and innovate

EXTERNAL

- Insights from customers
- Capital from owners
- Support from communities and access from landowners
- Natural resources – river flow and geothermal reservoirs
- Technology and business partnerships

FOCUS

VALUE CREATED

Through our licence to operate, relationships with communities and our commercial partners, we sustainably harness natural resources to generate low-cost renewable electricity. Mercury serves the energy needs of New Zealand homes and businesses, offering electricity-related experiences.

- Improved quality of life and experiences, with our customers enjoying energy in wonderful ways
- Sustainable and growing returns to our owners
- Creation of high-value sustainable jobs and positive career opportunities
- New Zealand's competitive advantage in renewable energy is fully leveraged
- Commercial partnerships producing economic and social community contributions

OUR FOUNDATIONS

WELLBEING – KAITIAKITANGA – COMMERCIAL

WHAT MATTERS MOST.

Renewables advantage for New Zealand

Few countries are blessed with the quality of raw energy that New Zealand has in our rivers, geothermal systems and wind resources.

Through more than a century of innovation and endeavour, we have harnessed this natural energy to provide comfort and convenience in our customers' homes and to power businesses that have delivered prosperity for our country and communities. This legacy has created hundreds of highly-skilled jobs in the provinces where the energy resources are and powers broader economic activity. The growth of renewable generation has also taken millions of tonnes of carbon emissions out of this country's annual energy profile.

New Zealand's electricity supply is more than 80% renewable, among the highest in the world. Further harnessing the potential of renewable energy, particularly in the electrification of transport, is New Zealand's greatest green-growth opportunity.

We are applying new thinking and collaborative action to deliver further benefits to our customers and enable New Zealand as a whole to build on this global competitive advantage. Ingrained in our business approach is a sustainability focus that includes responsible management of natural resources so that we live up to the expectations of our communities today and for future generations.

In our 2016 Annual Report, we have identified five key pillars that are important to Mercury's stakeholders and our business. We see these as material considerations to how we create long-term value for Mercury's owners. We have reported performance in each of these areas, and through our future reporting we will set out clear goals and targets that reflect the perspectives of our stakeholders and how they are integrated into our business approach.

1

CUSTOMER SATISFACTION.

New Zealand's electricity market is among the most competitive, with a stable and well-functioning regulatory environment. Mercury's purpose is to inspire New Zealanders to enjoy energy in more wonderful ways. We are doing this through a customer-driven approach that rewards loyalty, leverages advances in technology along with smart meter capability, and makes our services seamless and easy for people. Customer satisfaction is a core benchmark for our business and a component measure of executive remuneration.

2

OUR PEOPLE & SAFETY.

We aim to make Mercury a great place to work, with engaged and motivated employees who are passionate about creating value in our business and an outstanding customer experience. We value diversity, particularly in contributing to innovative thinking, and have a culture where people are encouraged to work together on shared goals. The health and safety of our people and everyone we work with is of paramount importance, and is a core benchmark for our business and a component measure of executive remuneration. We have a complementary focus on great people management, and a high performance culture, which ensures staff are recognised and rewarded for excellence.

3

CARE WITH NATURAL RESOURCES.

Mercury harnesses the energy from natural resources, with a long-term focus that recognises the interests of other stakeholders and the interests of future generations of New Zealanders. Our 100% renewable hydro and geothermal generation contributes towards New Zealand's renewable energy advantage that is a primary platform for delivering value to consumers and addressing New Zealand's climate change goals. Along with our focus on meeting or exceeding the expectations of our operating communities, we place a priority on resource consent compliance and collaborative efforts to protect and enhance environmental outcomes, including the health and wellbeing of the Waikato River and its catchment.

4

ENDURING PARTNERSHIPS.

Deep and enduring partnerships are a vital foundation for our business and broader economic outcomes. Kaitiakitanga (guardianship) is embedded in our operations and reflected in the relationships we have with our commercial, community and iwi partners. The partnerships we have with Maori landowners have been essential to our geothermal development programme and operations that rely on ongoing access to these natural resources. We are proud to have long-standing commitments to support local communities as they allow us to bring our purpose to life, and through mutual effort and shared values generate value well beyond the financial contributions from the company.

5

CREATING SHARED VALUE.

The financial results in our 2016 Annual Report are the product of a business strategy focused on creating long-term value for our owners. We take a broad perspective considering all stakeholders and outcomes for New Zealand as a whole. We apply strong financial disciplines and robust risk management, together with a respect for the inter-generational management of natural resources, in operating our business and pursuing future growth. Our aim is to deliver stable and sustainable cash flows that support dividends to our owners, and grow in value over time. Through our partnerships, and by consistently delivering on the expectations of our communities, we will also open up opportunities for economic development, and societal and environmental benefits. In addition to our key financial and operational measures, our Market Disclosure Policy and Stakeholder Communications Policy outline our approach to ensuring accurate, timely and meaningful information regarding Mercury's business and our focus on creating value.

CUSTOMER SATISFACTION.

The World Energy Council (WEC) ranks the New Zealand electricity sector among the best markets globally for energy security, affordability and sustainability. Mercury is a leader in this sector.

Key outcomes from a stable and progressive regulatory framework are intense retail and pricing competition along with genuine choice for consumers.

With global advances in technology, we see opportunities to inspire our customers with innovation that builds on our 100% renewable electricity, and our leading approach to customers' use of smart meter data. We believe that putting customers first is vital to our commercial success and growing long-term value for our owners.

Technology, partnerships and the national roll-out of smart meters have spurred development of value-added services, competition, and customer choice. Our purpose is to inspire New Zealanders to enjoy energy in more wonderful ways. We are also rewarding their loyalty and are focused on making our customer service seamless and easy for people. Our services help vulnerable people in our communities maintain electricity supply.

CHAMPIONING NEW TECHNOLOGIES

Changing approaches to energy use are inspiring us to champion new technologies. Solar is becoming an increasingly popular choice for home owners and businesses looking to complement grid-connected electricity in New Zealand.

In the past two years, solar installations have increased four-fold from 2,000 to more than 8,000. During the 2016 year, we acquired one of New Zealand's leading solar businesses, adding this proven technical capability to support a strong customer offering.

Given New Zealand's leadership in renewable electricity, plug-in electric vehicles (EVs) are the single largest green-growth opportunity for our country. There are huge benefits for consumers such as the low cost of electricity at the equivalent of 30 cents per litre of petrol, and more broadly in building economic resilience and addressing climate change.

Mercury took a leadership position in 2014 by progressively shifting 70% of our fleet to plug-in hybrids or full-electric vehicles by 2018. This transition is well underway and we have one of the largest EV fleets in the country. We have also been instrumental in raising awareness of EVs, educating other businesses, partnering with key organisations like EECA, and we contributed towards the development of the Government's EV policy. We offer customers with electric vehicles a 20% discount off overnight electricity as part of our efforts to promote uptake of EVs and to encourage off-peak charging.

E-bikes are another growing phenomenon around the world, that make sense in New Zealand's renewable context, as well as our historical culture of cycling in many of our towns and cities. As with other advancing technologies, there is huge potential to leverage renewable electricity and increase awareness of this smart mode of transport. The opening multi-channel Mercury brand campaign has strongly leveraged the e-bike positioning.

REWARDING CUSTOMERS

Free Power Days

Rewarding customer loyalty is important to Mercury. We offered a Free Power Day to reward our customers, and in FY2016 over 100,000 people took up this offer, saving them an average of $8.05. We offered customers an additional Free Power Day when we launched the Mercury brand on 29 July. This initiative has captured the imagination of our customers, contributing towards our highest annual customer satisfaction since measurement began in 2007, and successfully building better customer loyalty, which has positive commercial outcomes.

>>

PLUG-IN ELECTRIC VEHICLES (EVS) ARE THE SINGLE-LARGEST GREEN-GROWTH OPPORTUNITY FOR OUR COUNTRY.

0.1%
DISCONNECTION RATE LOWEST IN THE INDUSTRY

61%
CUSTOMERS HIGHLY SATISFIED

Air New Zealand Airpoints™ partnership

In June we announced a partnership with Air New Zealand's Airpoints™ programme, which extends our commitment to offer Mercury customers choice and reward their loyalty. From late 2016 this will deliver additional value for our customers in travel and related Airpoints™ products every time they use our electricity or gas for home or small business.

MAKING IT EASY

Smart services

Mercury's free online energy dashboard, Good Energy Monitor (GEM), has saved customers more than $5.5 million since its introduction in 2013. GEM gives customers an accurate, up-to-date picture of their electricity usage within a half hour timeframe using data from smart meters located on people's properties. It helps customers make informed decisions about their electricity consumption.

Like GEM, our pre-pay service GLOBUG is made possible by smart meters. GLOBUG, which offers rates among the most competitive in the market, helps people keep the lights on and stay out of debt.

MEASURING OUR SUCCESS

Beyond our 100% renewable generation, Mercury is focused on achieving the highest levels of satisfaction. Our primary measure of customer satisfaction (measured by independent customer demand agency, TRA) has averaged 61% over the 2016 financial year, and customer switching 'churn' rates for Mercury in our largest market, Auckland, are consistently below the average for other brands.

GLOBUG is a leader in its sector and many consumers prefer the pre-pay approach, just as in other sectors such as telecommunications. This innovative solution has helped customers better manage their electricity use in line with their income patterns, and helped Mercury to significantly reduce disconnection levels. Mercury's disconnection rate at 0.1% (as reported by the Electricity Authority) has consistently been among the lowest across all retail brands in New Zealand. ●

INNOVATING FOR CUSTOMERS.

IT'S AMAZING THE DIFFERENCE SMALL CHANGES CAN MAKE.

WINNING CUSTOMER LOYALTY IS AT THE HEART OF THE MERCURY SERVICE PROMISE. THIS IS SOMETHING THAT HAS KEPT AUCKLAND CUSTOMER, HELEN TATE, WITH US FOR 27 YEARS.

Helen followed her parents' lead as Mercury customers and, despite the market being intensely competitive, has never seen the need to change.

In her busy household of five, the home-based childcare worker usually has four toddlers during the day. So having a recent Free Power Day came as welcome relief. But it's having visibility of her power usage that Helen really values through the Good Energy Monitor (GEM).

"I love GEM! I look out for the emails every week so I can see how much power I have used, compared to the week before – it's always nice to see when we have used less."

Helen says she enjoys simple and clear information in GEM, showing exactly when she has used more or less power, and where she gets the most value.

Helen is one of nearly 150,000 customers actively using GEM, which uses data from smart meters on customers' properties to generate easy-to-read charts and a detailed breakdown of energy use. You can compare your electricity consumption from day to day, and season to season with similar homes.

GEM also includes tips to help customers reduce their energy use, and alerts to unusual spikes.

"Because I work from home there's a lot of power use that's necessary and I can't control, but thanks to GEM we are making more effort to switch off the lights and manage consumption in areas of the house we are not in – it's amazing the difference small changes can make."

Helen says her experiences with Mercury have always been positive and seamless. "It's always easy – every time when I've called I get the answers I need. And GEM's also easy to use – I get all the information I need in short emails or online." ●

GEM HAS SAVED CUSTOMERS MORE THAN $5.5M SINCE ITS INTRODUCTION IN 2013.

OUR PEOPLE & SAFETY.

Mercury is committed to attracting and retaining employees with the skills and passion that best serve our business and our customers. We focus on having a positive and inclusive culture that supports our people in achieving their full potential.

The safety and wellbeing of our people is a fundamental priority and we focus on and value the strong health and safety culture at Mercury.

Mercury values diversity of people and ideas in the workplace and our culture is based on working together to achieve our business objectives.[1]

We provide opportunities for personal and professional development, and recognise and reward excellence. Great people management helps drive a high performance culture. We are very pleased to be considered an employer of choice, which is reflected in feedback from our annual workplace engagement survey.

THE SAFETY OF OUR PEOPLE

Our philosophy is to safeguard all people on our worksites, irrespective of whether they work for us, for others or are members of the public. We have built a strong, proactive culture to keep people safe and to strive for "zero harm". This means that we aim to prevent any serious harm through the systematic identification of hazards and potential hazards.

Everyone at Mercury is strongly encouraged to report hazards and near misses to support our culture and enable the understanding of health and safety drivers across the business to track our performance. Our people complete an induction to health and safety awareness, and use an online tool to record health and safety, including a phone app for easy access and timely reporting.

Our key health and safety metrics are Total Reportable Injury Frequency Rate (TRIFR) and Lost Time Injury Frequency Rate (LTIFR).

We aim to have no high severity incidents. Our targets for TRIFR and LTIFR for this financial year were for levels below 0.94 and 0.48 respectively. We achieved very positive results in 2016 with rates well ahead of our targets and New Zealand benchmarks.

YEAR	TRIFR	LTIFR
2014	0.84	0.65
2015	1.25	0.48
2016	0.74	0.28

To support our people's wellbeing, Mercury offers reimbursement for an annual health check to all employees, provides access to an online wellbeing tool to employees and their families and provides comprehensive life and income protection insurance should an employee become seriously unwell and be unable to work.

In 2016, 75 employees identified themselves as having a disability. A range of support is offered to employees with disabilities to ensure they are able to perform and achieve at Mercury.

>>

11.5%
TURNOVER RATE FOR FY16

6.2 YEARS
AVERAGE TENURE OF EMPLOYEES AS AT 30 JUNE 2016

1 See Governance at Mercury section for more information on our Diversity Policy.


JEFF
Jeff

WORKING TOGETHER TO IMPROVE SAFETY IN NEW ZEALAND

We welcomed the establishment of WorkSafe NZ in 2013 as part of a major overhaul of workplace health and safety nationally. We have long valued and supported collaboration with other New Zealand businesses, including those in the electricity industry. We're part of the Business Leaders' Health and Safety Forum and a founding member of StayLive, an electricity industry safety group that strongly promotes sharing of learning, investigations, initiatives and reporting. We share our expertise and learning to grow safer workplaces.

ENGAGED EMPLOYEES

We believe that having engaged and motivated employees is good for our business and our customers. We measure engagement with our people, which provides valuable insight of our strengths and opportunities to improve. Our goal is to lift engagement levels every year. Our 2016 survey confirmed that our people are proud to work for Mercury, with our engagement rates in the top quartile for large New Zealand businesses. We were pleased to see that 87% of our people agree they are working for a successful organisation, with a clear mission and purpose, and 84% agree that we are making the changes we need to further enhance our future. The 2016 survey also showed that 95% agree we are committed to health and safety, and 94% agree that Mercury takes its environmental responsibilities seriously.

LEARNING AND TRAINING

Formal and informal learning is made available to support employees to perform and develop in their current role and be ready for their next career move.

Developing and retaining our emerging talent through Velocity, our 12-month development programme, helps to establish a network of influential change leaders across our business. This year 40 employees participated in this programme, identifying initiatives to tackle key business challenges. This programme resulted in the design and implementation of initiatives to enhance business performance.

During 2016 we introduced a network of Change Supporters throughout the business. This group, who were nominated by their peers, provided a bottom-up approach to change. This has helped improve the way our people experience change and ensures communication and support is targeted and relevant.

Great people management helps drive our high performance culture. StepUP, our management training programme, is designed to lift managers' performance and embed consistent expectations throughout Mercury.

"StepUP is a very engaging programme. It was memorable, targeted and relevant, with a great focus on self and team," Ian Stabler, Field Manager at Ngatamariki Geothermal Power Station.

INSPIRING OUR PEOPLE.

EVERY TWO YEARS MERCURY PROVIDES THE OPPORTUNITY FOR EMPLOYEES TO APPLY FOR THE $25K 'TAKE THE LEAD' SCHOLARSHIP TO ADVANCE THEIR CAREER.

John Clark, Kawerau Field Manager, is the 2016 recipient of the scholarship, which is supporting his MBA studies at Waikato University. Here he talks about what it's like to work for Mercury.

"I am proud to work for a company with such great vision and ambition that strongly values its people. Mercury is inspirational.

"The people and culture are the best thing about Mercury, making it a really fun place to work. Every day throws up new opportunities and challenges where I can work with clever people on really interesting things that actually matter. This enables me to grow and learn new skills.

"Mercury goes the extra mile in supporting staff development. Being selected to take part in this year's Velocity talent programme was a great opportunity to connect with highly motivated people and to work on projects together, then to present our initiatives to the Executive Management Team and see them implemented. The award of the 'Take the Lead' Scholarship is awesome. It means I can complete my MBA at Waikato, which I couldn't have done without Mercury's support.

"Right from the executive to the front line, the health and safety of our friends and colleagues are always top-of-mind.

OUR PHILOSOPHY IS TO SAFEGUARD ALL PEOPLE ON OUR WORKSITES, IRRESPECTIVE OF WHETHER THEY WORK FOR US, FOR OTHERS OR ARE MEMBERS OF THE PUBLIC.

GENERATING PRIDE IN OUR COMMUNITIES

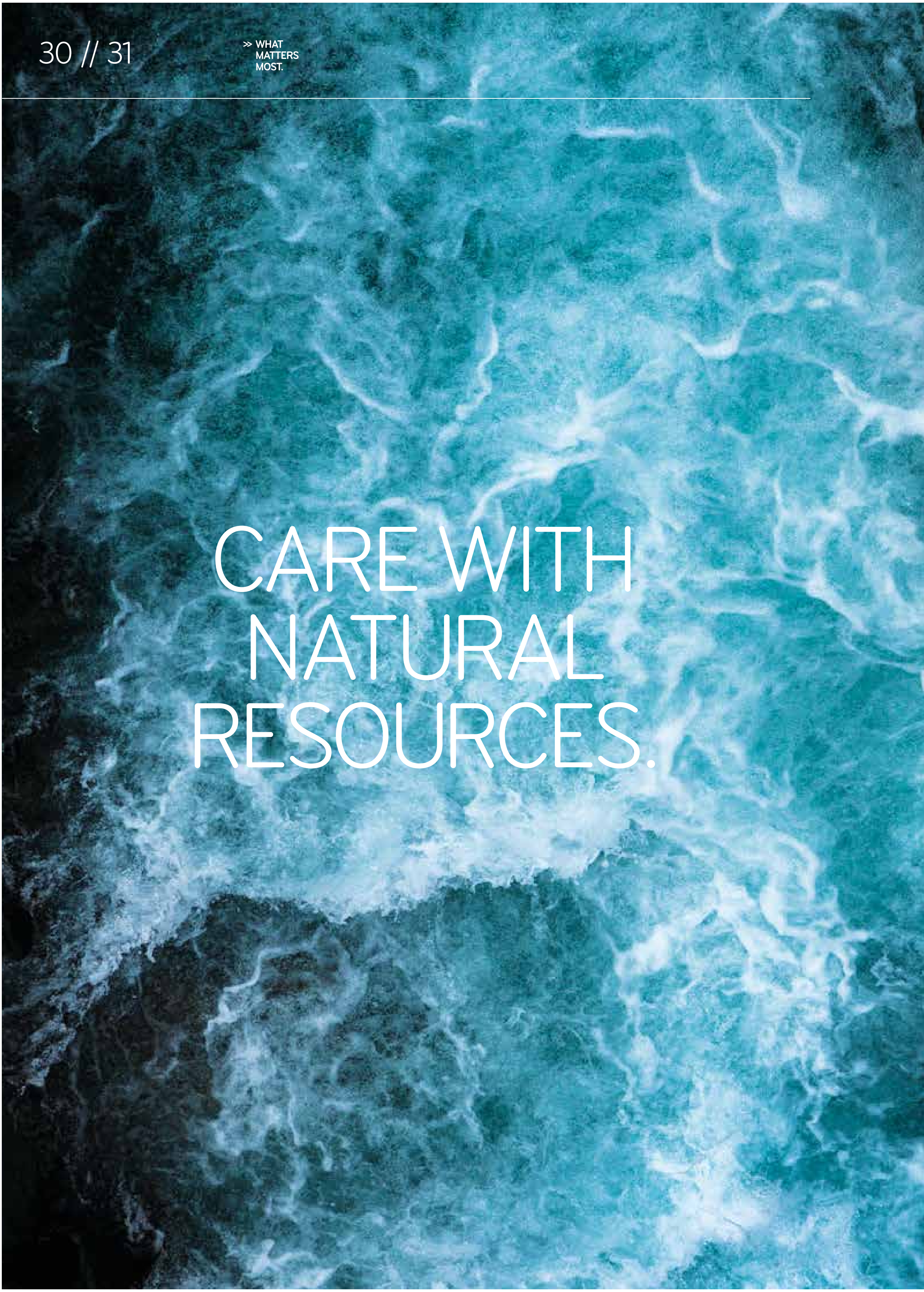
We recognise our employees are part of different communities in New Zealand and want to actively support these communities. We created the Employee Community Fund of $100,000 a year. Our employees apply to the fund to make a small donation to a community initiative they care about. In FY2016, a total of 79 projects and groups were helped through the Employee Community Fund.

"What wonderful news you have given us! Now we have the joy of having a team represented and upskilled to be better informed of the learning of these special children". $1,500 was donated to St Mary's Northcote Primary School for special needs teachers to attend seminars on autism. ●

"The implementation of the new safety reporting system has been fantastic for recording and measuring our health and safety performance, and creating transparency so we can continue to learn and improve.

"Mercury really values its people and sees us as an asset; sounds like a cliché but it is true. The great things for me are being able to take ownership of projects, having the freedom to question how things are done and whether there's a better way of doing them, and collaborating with exceptional people. That's what gets me out of bed in the morning." ●

I AM PROUD TO WORK FOR A COMPANY WITH SUCH GREAT VISION AND AMBITION THAT STRONGLY VALUES ITS PEOPLE. MERCURY IS INSPIRATIONAL.



CARE WITH NATURAL RESOURCES.

As a business that harnesses natural resources, we have a primary focus on both the sustainability of these raw energy sources and the important perspective of global climate health.

The renewable hydro and geothermal power plants operated by Mercury are an important part of New Zealand's renewable advantage, with more than 80% renewable electricity ranking this country among the highest in the world. Electricity will continue to be the primary platform for decarbonising the New Zealand economy and delivering positive health and climate change outcomes.

This clean and sustainable, home-grown electricity is already powering homes and businesses. The technology that it enables enriches almost every aspect of our daily lives. As a transport fuel of choice it will deliver benefits for the economy, our environment and health, and at a much lower cost to Kiwi consumers. From our research, more than 50% of all New Zealanders already believe EVs are the best transport solution. This is particularly strong amongst 18-24 year olds, with over 70% of that view.

Kaitiakitanga, or guardianship, is core to our long-term purpose and investment to support New Zealand's position as a world leader in renewable electricity.

We are harnessing the energy from these natural resources responsibly and sustainably for the benefit of generations that follow.

ELECTRIC VEHICLES

Electrification of transport to reduce carbon emissions and our country's reliance on expensive, imported fossil fuels makes huge sense. The need for action on this was strongly highlighted in the weight of submissions on the country's climate change target.

Mercury is taking a leading role in this area, strongly advocating to government, businesses and other large fleet owners to accelerate their uptake of EVs. We are also changing 70% of our fleet to plug-in electric vehicles by 2018 and this change is now well underway.

Reducing New Zealand's reliance on fossil fuels will significantly strengthen the country's economic resilience, and give credibility to New Zealand's '100% Pure' reputation with our global trading partners and tourists. These are powerful incentives, acknowledged in the Government's Electric Vehicle Partnership Programme, which sets a modest target to double EVs on our roads every year to 64,000 by 2021.

WATER

Water is vital to our business and to our renewable generation. It powers our Waikato hydro and geothermal stations, and underpins the environmental health and wellbeing of the Waikato River and its catchment.

Our historical links with the Waikato River, home to our eight dams and nine hydro plants, date back almost a century. Today the Waikato Hydro System produces about 10% of New Zealand's electricity supply and just over half of Mercury's annual generation.

The hydro system is crucial for the stability of the catchment, comprising 12% of the land in the North Island. The river provides town water supply for more than 1.5 million people, and is the lifeblood of infrastructure, agriculture and other economic activity along its 425km journey. Since the installation of the Taupo Gates in 1941, and every hydro plant since, the Waikato catchment has benefitted from the stability of the river as opposed to an unchecked, natural water flow. The Waikato River is a source of spiritual and physical sustenance for Maori, and it offers world-class opportunities for sports and recreation.

>>

> KAITIAKITANGA, OR GUARDIANSHIP, IS CORE TO OUR LONG-TERM PURPOSE AND INVESTMENT TO SUPPORT NEW ZEALAND'S POSITION AS A WORLD LEADER IN RENEWABLE ELECTRICITY.

Given these multiple objectives, water quality and allocation are becoming significant topics around New Zealand. We maintain a strong involvement in national and regional forums such as the Land and Water Forum, the Ministry for the Environment's consultation on 'Next Steps for Fresh Water' and Waikato Regional Council's 'Healthy Rivers/Wai Ora: Plan for Change' and 'Let's Talk Water' discussions. We believe the catchment has great opportunities to prosper for all stakeholders over the long term.

Our hydro operations have changed little over the last fifty years. However the character of the Waikato catchment has changed significantly, particularly as a result of land use intensification. We are strongly committed to understanding, managing and minimising any impacts of our operations, working very closely with the Waikato Regional Council, iwi and other stakeholders to ensure sustainability of these natural resources for generations that follow.

We carry out a wide range of activities, which go well beyond environmental and stakeholder expectations, to meet the 121 conditions of our hydro consents. These include hydrological analysis, geomorphological studies, and ecological monitoring. In 2015, for the third year running, Waikato Regional Council confirmed we achieved full compliance with our hydro consents.

GEOTHERMAL

Mercury is one of the world's largest geothermal power plant operators having successfully developed three major plants since 2008 (Kawerau, Nga Awa Purua and Ngatamariki), bringing the number of geothermal plants we operate to five and lifting us into the top ten geothermal operators in the world.

The addition in 2013 of the Ngatamariki geothermal station has increased the proportion of geothermal generation to around 40% of our total production, enough to supply half a million households. Geothermal generation is now New Zealand's number two fuel source for electricity, supplying 17% of the country's requirements.

Geothermal energy relies on water from naturally heated, underground reservoirs. Geothermal fluids are re-injected into the ground at all of our sites, supporting the sustainability of this valuable natural resource.

A large part of our growth in geothermal generation over the last ten years has been in partnership with Maori land owners, the Tauhara North No.2 Trust and the Tuaropaki Trust. Our partnerships are guided by the values of kaitiakitanga (guardianship) and kotahitanga (working together).

Rather than simply seeking to secure land access and purchase fuel from land owners, we have worked in partnership models so that benefits of the combined expertise are more widely shared, and with stronger alignment. This supports sustainable stewardship of resources. ●

3RD YEAR
RUNNING ACHIEVED FULL COMPLIANCE ON RESOURCE CONSENTS

100%
RENEWABLE HYDRO AND GEOTHERMAL GENERATION

OVER TIME, THE TRUST HAS DEVELOPED PRODUCTIVE ALLIANCES WITH GREAT PROJECT PARTNERS LIKE PROJECT TONGARIRO. TOGETHER WE ARE MAKING A REAL DIFFERENCE TO OUR ENVIRONMENT. THIS IS REALLY THE MOST REWARDING THING FOR ME.

>> WCEET CHAIR GWYNETH VERKERK

WAIKATO CATCHMENT ECOLOGICAL ENHANCEMENT TRUST.

WETLANDS HAVE A CRITICAL ROLE IN THE HEALTH OF NEW ZEALAND'S BIODIVERSITY AND ECOSYSTEMS, FILTERING SEDIMENT, NUTRIENTS AND BACTERIA AS WATER FLOWS FROM LAND INTO STREAMS AND RIVERS, AND EVENTUALLY INTO OUR OCEANS.

While we may never see the vast wetlands of pre-European times, the Waikato Catchment Ecological Enhancement Trust (WCEET) is playing an important part in helping to restore them.

Over the past eight years, WCEET has invested $500,000 in Project Tongariro's Te Matapuna initiative to restore wetlands south of Lake Taupo to their former glory by eradicating grey willows and replanting with native species.

The Te Matapuna initiative is just one of 184 projects WCEET has supported since the trust's establishment in 2003 with funding from Mercury. Investment now totals $5.5 million.

The trust was born through collaborative effort during Mercury's hydro operations consents process. It supports projects that foster and enhance the sustainable management of ecological resources in the Lake Taupo and Waikato River catchments.

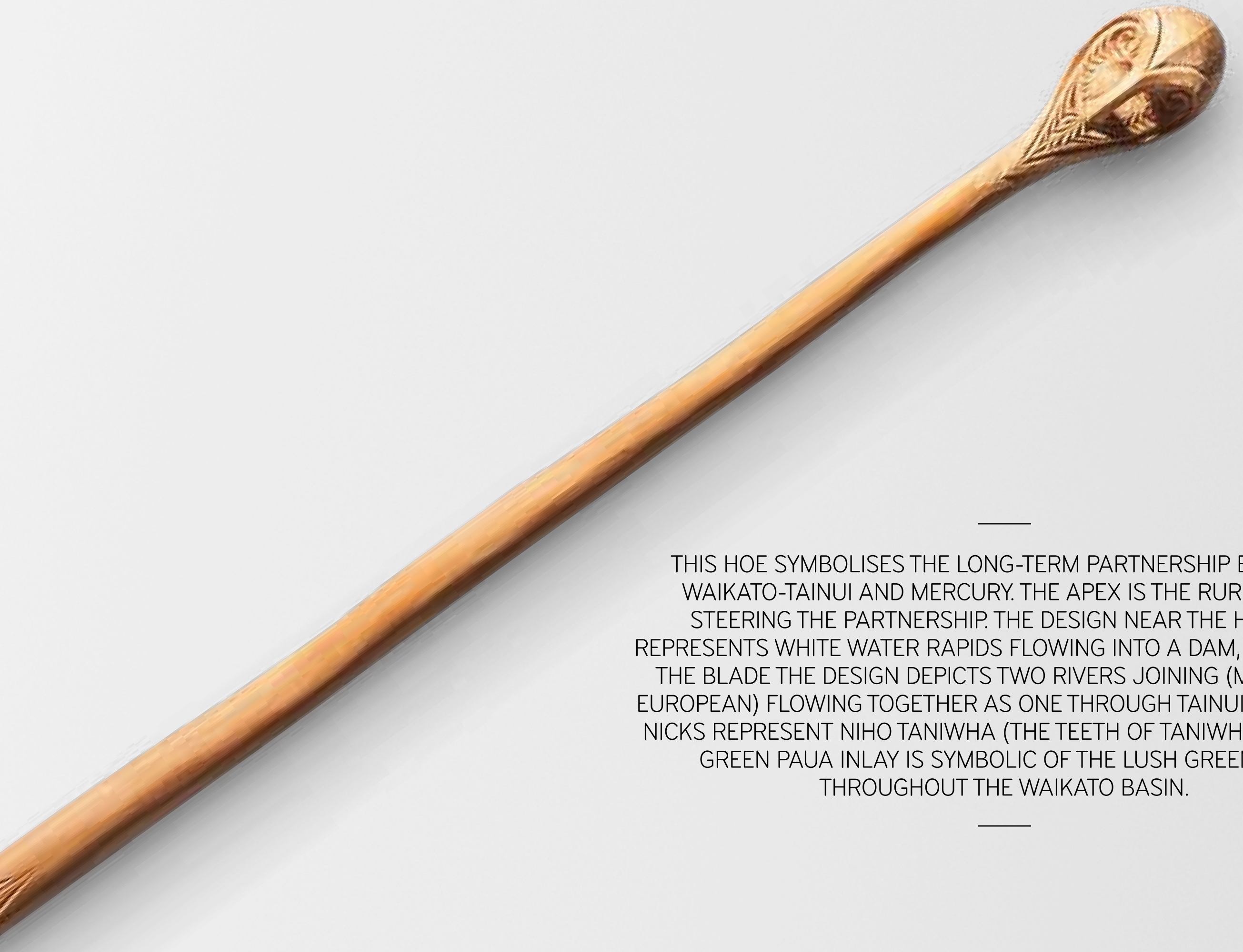
As well as wetland restoration, WCEET invests in a wide range of planting and pest eradication projects, and sustainable species and habitat management.

"Over time, the trust has developed productive alliances with great project partners like Project Tongariro. Together we are making a real difference to our environment. This is really the most rewarding thing for me," says WCEET Chair Gwyneth Verkerk. WCEET's original signatories are still represented today. These include Fish and Game New Zealand, The Royal Forest and Bird Society, the Advisory Committee on Regional Environment and the Department of Conservation, in partnership with Mercury. WCEET is a model of what can be achieved when people with a shared vision focus on kaitiakitanga (guardianship) of our precious natural resources for future generations. ●

ENDURING PARTNERSHIPS.

Harnessing the energy of New Zealand's natural resources to generate renewable electricity has created great opportunities for community partnerships, which deliver environmental, social and economic benefits.

These partnerships, based on shared values and a focus on the long term, are at the heart and foundation of our business.
The concept of kaitiakitanga (guardianship) of natural resources for future generations is embedded in our operations and is the foundation of our relationships with our partners.



THIS HOE SYMBOLISES THE LONG-TERM PARTNERSHIP BETWEEN WAIKATO-TAINUI AND MERCURY. THE APEX IS THE RURU (OWL) STEERING THE PARTNERSHIP. THE DESIGN NEAR THE HANDLE REPRESENTS WHITE WATER RAPIDS FLOWING INTO A DAM, THEN DOWN THE BLADE THE DESIGN DEPICTS TWO RIVERS JOINING (MAORI AND EUROPEAN) FLOWING TOGETHER AS ONE THROUGH TAINUI. THE SMALL NICKS REPRESENT NIHO TANIWHA (THE TEETH OF TANIWHA), AND THE GREEN PAUA INLAY IS SYMBOLIC OF THE LUSH GREENNESS THROUGHOUT THE WAIKATO BASIN.

> OUR PARTNERSHIPS WITH TANGATA WHENUA ARE VERY IMPORTANT TO OUR BUSINESS AND WE WORK CLOSELY WITH IWI, HAPU AND MARAE IN OUR OPERATIONAL AREAS, SO WE CAN BETTER UNDERSTAND THE WAY WE ENGAGE WITH NATURAL RESOURCES, PARTICULARLY WATER.

IWI

The Waikato River has immense cultural and historical significance for Waikato iwi. We respect those close links and the tupuna-awa relationship iwi have with the river.

Our partnerships with tangata whenua are very important to our business and we work closely with iwi, hapu and marae in our operational areas, so we can better understand the way we engage with natural resources, particularly water.

In the spirit of partnership, we look for opportunities that enhance the mana of our partners. We work closely with Waikato iwi and, alongside our partners, will continue to invest in cultural, environmental, educational, social and economic initiatives.

We have partnership agreements with Waikato Tainui, Ngati Raukawa, Ngati Tahu-Ngati Whaoa, and Ngati Tuwharetoa. In the Bay of Plenty we also have extensive engagement with Tuwharetoa ki Kawerau related to their Kawerau geothermal assets (Ngati Tuwharetoa Geothermal Assets).

PROFIT WITH PURPOSE

Deep partnerships with Maori landowners have underpinned one of the fastest geothermal development programmes in the world, helping catapult Mercury to be one of the leading global geothermal operators.

Since 2008, we have developed three renewable geothermal power plants. Much of this growth has been made possible through our partnership with the Tauhara North No.2 Trust.

We continue to enjoy the partnership of the Tuaropaki Trust in relation to the Tuaropaki Power Company for geothermal generation. We are inspired by their sustainable and innovative approaches to horticulture, milk production and land management.

Equity in these projects has created economic wealth for Maori from their land and unique capabilities, providing broader opportunities and optimism for the future.

>>

20 YEAR PARTNERSHIP WITH ROWING NEW ZEALAND

$1.03M DONATED TO STARSHIP BY MERCURY CUSTOMERS THIS YEAR

OUR WAIKATO CATCHMENT PARTNERS

We share the vision of our Waikato catchment community partners for a healthy Waikato River which will support biodiversity and prosperous communities over the long term. We work closely with many partners to achieve this through a wide range of collaborative projects, and our strong participation in the evolution of local, regional and national water policy.

We have contributed to Waikato Regional Council's 'Healthy Rivers/Wai Ora: Plan for Change' and 'Let's Talk Water'. We have regular, constructive discussions with local and regional councils and the Waikato River Authority. Mercury is a key partner of the Waikato Catchment Ecological Enhancement Trust which, with our support, has invested $5.5 million in 184 environmental projects since its establishment in 2003.

OUR SPONSORSHIPS

We are also passionate about supporting the communities we work in through our sponsorships.

Our 15-year partnership with the Starship Foundation is one of Mercury's targeted sponsorships. Mercury customers have donated $1.03 million this year, bringing the total amount donated to $8.8 million since the partnership began in 2001. In addition, the company contributes $150,000 a year and pays for all administration costs, so that all the money donated by customers helps children from all over New Zealand to access world-class, life-saving care by the dedicated and professional team at Starship Children's Hospital.

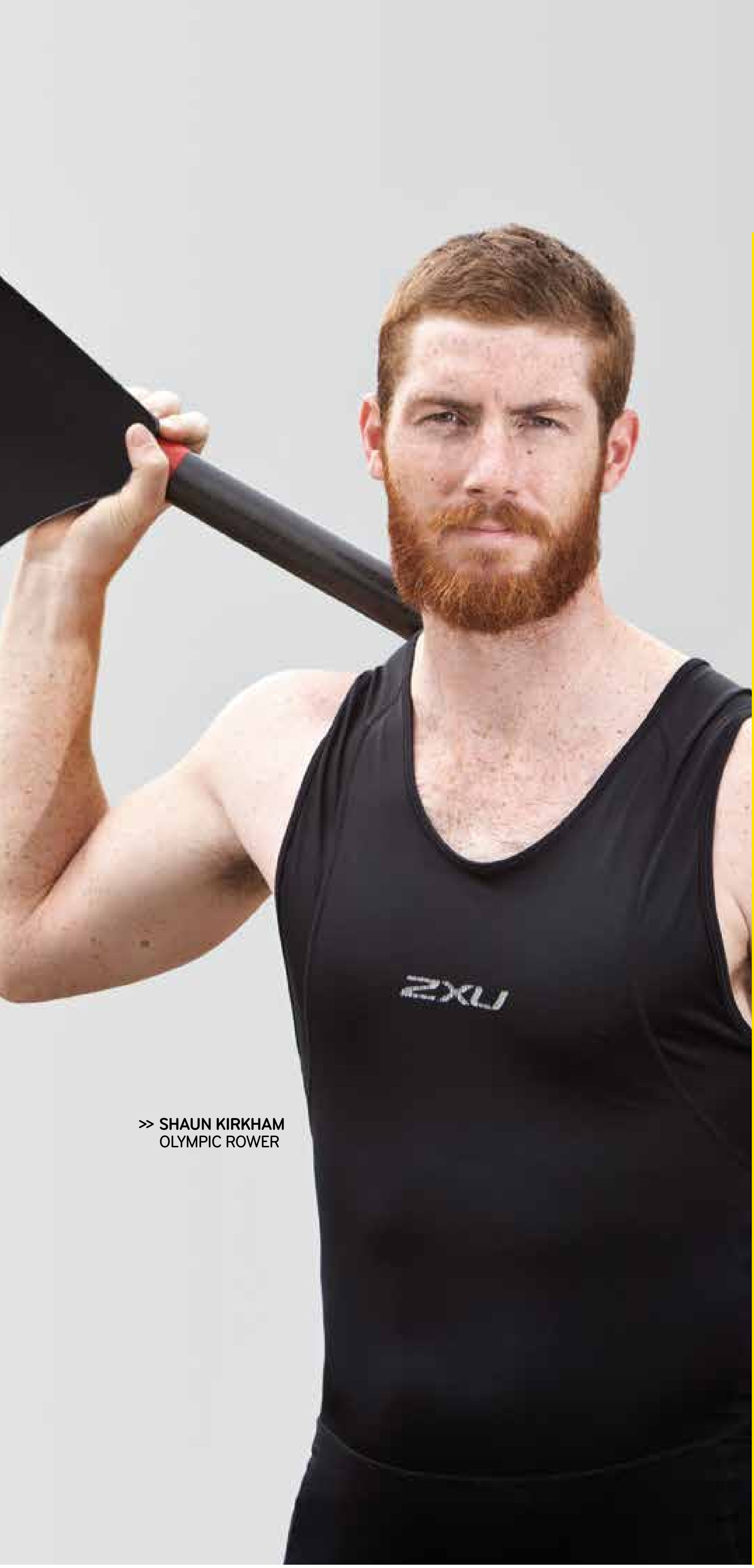
This year, we cemented our 20-year relationship with Rowing New Zealand, extending our sponsorship to 2018. Our support of our Kiwi rowers has helped New Zealand become a powerhouse on the world stage. Lake Karapiro provides the stunning backdrop for the Mighty River Domain, home to Rowing New Zealand's high performance centre. As well as national rowing events the domain supports a wide range of sports and community events.

We are proud to support this fantastic community facility.

Mercury encourages people to connect with the dramatic and beautiful natural environment of the Waikato River and has been a sponsor of the Waikato River Trails Trust since 2004. The 105 km trail showcases native bush, historic landmarks, geological formations and wetlands along the river banks and the Waikato hydro lakes. Since its completion in November 2011, visitors have clocked up an estimated one million kilometres walking, cycling or running along the trail – the equivalent of 25 times around Earth.

Our sponsorship extends beyond financial support. The trail's maintenance team base their operations out of our Whakamaru and Arapuni sites and our employees participate at many levels from barging plants up river and picking up a spade on riparian planting days, to joining in at multi-sports events.

Enduring partnerships are in the company's DNA. They allow us to bring our purpose to life, deliver value, and create pride among our customers, communities and employees. ●



>> **SHAUN KIRKHAM**
OLYMPIC ROWER

NZ ROWING MAKING HISTORY.

Mercury is proud to sponsor Rowing New Zealand, our world class athletes who did our country proud in 2016 with their amazing accomplishments.

The 2016 team topped the medal table at two World Cups becoming the overall World Cup points winner, before going on to claim two golds and one silver medal at the Rio 2016 Olympic Games.

> **THE DEPTH OF TALENT IN THIS YEAR'S TEAM REFLECTED YEARS OF COMMITMENT TO THE SPORT.**
>
> >> SIMON PETERSON, ROWING NZ CE

Mahé Drysdale secured gold in the single sculls in a thrilling photo-finish, and Hamish Bond and Eric Murray also took home gold in the Men's Pair. Women's Pair Rebecca Scown and Genevieve Behrent won silver, and were also part of the history-making women's eight crew who finished just out of the medals in fourth place, the first ever New Zealand women's crew to compete in this class.

"The depth of talent in this year's team reflected years of commitment to the sport. It's also thanks to generations of young people who have aspired to become world rowing champions and the long-term support from sponsors like Mercury," says Rowing New Zealand Chief Executive Simon Peterson.

Mercury has shared in the outstanding successes of kiwi rowers since 1998, with 44 World Championship and Olympic gold medals won during that time. Lake Karapiro, a world-class sporting venue, is the home of Rowing New Zealand and the training ground for its elite athletes and the next generation of world champions. ●

CREATING SHARED VALUE.

Our business strategy is focused on creating long-term value for our owners.

The foundation for creating shared value is a holistic business approach that takes a long-term and broad perspective considering all of our stakeholders and the outcomes for all New Zealanders.

We apply strong financial discipline, robust risk management and respect for the inter-generational management of natural resources in operating our business and pursuing growth opportunities.

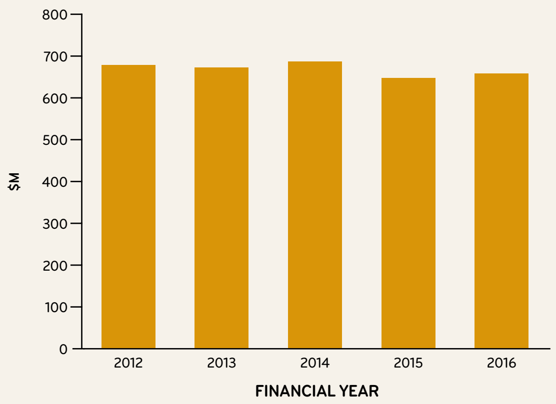
Our aim is to deliver sustainable and increasing cash flows that support higher dividends to our owners to enhance value over time. Through strong and enduring partnerships, and by consistently delivering on the expectations of our communities, we will open up opportunities for economic development and societal and environmental benefits.

The following sections provide an overview of our key financial results, providing readers of our Audited Financial Statements with better insight and understanding of our performance during FY2016.

ENERGY MARGIN

Energy Margin is a non-GAAP measure and is defined as sales less lines charges, energy costs and other direct costs of sales, including metering (see Note 4 of the Audited Financial Statements). Energy Margin provides a measure that, unlike total revenue, accounts for the variability of the wholesale spot market on our generation revenue and the broadly offsetting impact of wholesale prices on the purchase cost of our customers' electricity.

>> FIGURE 1: ENERGY MARGIN



The company's energy margin of $658 million was $10 million up for the year supported by the company's highest ever geothermal generation at 2,830GWh (up 2% on 2015), due to a high station availability of almost 96% for the year and the benefit of the turbine replacement at Nga Awa Purua. In addition, total hydro generation for 2016 was up 16% from 2015 to 3,866GWh. Annual inflows into the Taupo/Waikato catchment were again below normal at the 34th percentile for the year.

The LWAP/GWAP ratio for FY2016 was 1.03, with lower wholesale price volatility impacting both generation prices (GWAP) and purchase prices (LWAP). The relative difference between LWAP and GWAP was also impacted by locational price differences which are not expected to return to historic levels due to recent thermal plant closures in the Auckland region and changes to loss modelling in the System Operator's pricing model.

A drop in both sales volume and yields reflected the continued roll off of contracted commercial customers, with new sales contracts contributing to a fall in the average energy price to customers of 2% to $114.83/MWh as lower priced new commercial contracts replaced maturing contracts. A large proportion of these maturing contracts were signed between 2011 and 2013 when prices were higher. Healthy national storage and a strong demand/supply balance continue to weigh on customer pricing despite significant thermal closures in 2015.

OTHER INCOME

Other income incorporates revenue earned by the company's metering company Metrix through the provision of metering services to third parties, operations and maintenance services provided on a number of geothermal fields and revenue earned from the sale of the company's non-core land portfolio. The company's revenue from third party metering services increased during the year as smart meter deployment and services grew. The company also recognised revenue of $13 million from the disposal of non-core land, bringing the company's non-core land sales programme to a practical conclusion.

OPERATING COSTS

Operating costs represent the company's indirect costs of sales, including salaries and wages, maintenance costs and corporate overheads. Operating costs were flat year on year at $217 million and remain $30 million below their peak. This reflects reductions in maintenance costs due to a lower number of major maintenance projects across the generation fleet, offset by increases in branding costs, contractors and tail lease obligations due to the head office move to Newmarket.

EBITDAF

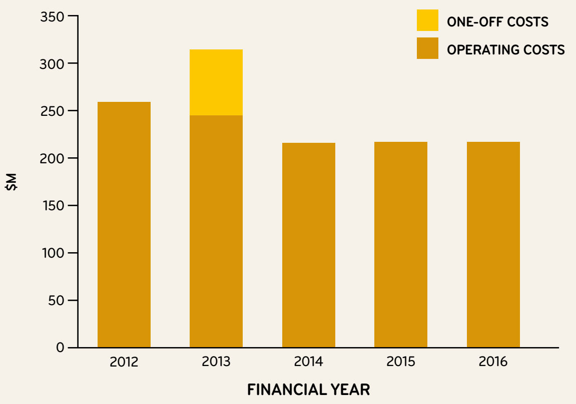
EBITDAF is reported in the income statement of the Audited Financial Statements and is a measure that allows comparison across the sector. EBITDAF is defined as earnings before net interest expense, income tax, depreciation, amortisation, change in fair value of financial instruments, impairments and equity accounted earnings. EBITDAF for the year was up $11 million or 2.3%, primarily due to the movements in Energy Margin mentioned earlier.

PROFIT FOR THE YEAR

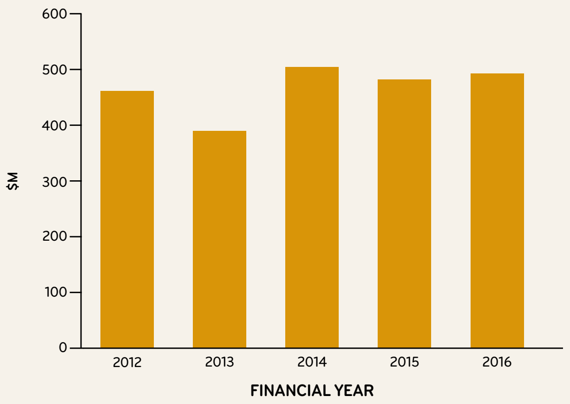
Profit for the year represents the profit for the company after taking into account EBITDAF, depreciation and amortisation, the change in the fair value of financial instruments, impairments, earnings of associates and joint ventures, net interest costs and the company's tax expense. Profit for the year increased $113 million, to $160 million due to the company's improved EBITDAF performance, along with a favourable reduction in impairment charges. Albeit, these improvements were offset by an increase in the company's non-cash depreciation expense as a result of the $504 million revaluation of the company's generation assets in 2015.

>>

>> **FIGURE 2:** OPERATING COSTS



>> **FIGURE 3:** EBITDAF



UNDERLYING EARNINGS AFTER TAX

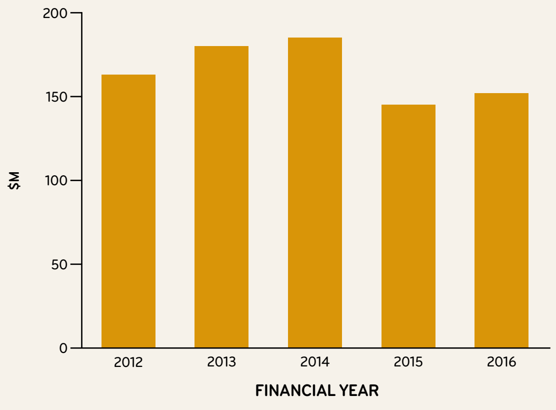
Underlying Earnings after tax is reported in Note 3 of the Audited Financial Statements and is a non-GAAP measure representing net profit for the year adjusted for one-off and/or infrequently occurring events exceeding $10 million of net profit before tax, impairments and any changes in the fair value of derivative financial instruments. In contrast to net profit, the exclusion of these items enables a comparison of the company's underlying performance between financial years. Underlying Earnings after tax increased by $7 million or 4.8% to $152 million, reflecting the company's increase in EBITDAF performance.

NET CASH FLOW FROM OPERATING ACTIVITIES

Net cash flow from operating activities represents the cash flows from the sale of electricity and metering services, along with the direct and indirect costs associated with their sale, which fell $20 million, reflecting a lower customer receivables balance in 2015 which benefited that year.

Net cash flow from operating activities also includes cash interest and income taxes paid by the company during the period. Interest paid by the company fell by $3 million as the prior year included the issuance costs paid in relation to the issue of the company's capital bonds. Taxation paid increased during the period by $10 million as the company elected to prepay its third provisional tax payment in March, which would otherwise have been payable in July, in order to fully impute the two and a half cents per share special dividend paid in September 2015.

>> FIGURE 4: UNDERLYING EARNINGS AFTER TAX



BALANCE SHEET

Total assets of the company increased by $27 million, due to a $139 million revaluation of the company's generation assets and capital expenditure of $72 million (excluding remediation capex in Chile), offset by land sales of $13 million.

The company's generation assets were independently revalued by PricewaterhouseCoopers at 30 June 2016, with a $139 million increase in their value recognised as a result and is in addition to the $504 million increase recognised a year earlier. These upward revaluations result in increased depreciation charges in the years following, as evidenced by the $11 million increase in depreciation charges in 2016. These revaluations do not affect tax depreciation.

Capital expenditure is comprised of $13 million of growth capex, $59 million of stay-in-business capex (SIB capex) and $18 million of remediation capex in Chile. Growth capex represents capital expenditure incurred on new initiatives and projects to enable the company to increase its earnings, with the majority of the expenditure relating to the further deployment of smart meters by Metrix.

Conversely, SIB capex represents the capital expenditure incurred by the company to maintain its assets in good working order and was down $20 million on 2015 and $21 million below the company's normalised SIB capex target of $80 million per annum. The lower level of expenditure in 2016 was primarily due to the significant planning work required to deliver the large refurbishment projects in 2017 at its Whakamaru and Aratiatia hydro power stations and the drilling of four geothermal wells to ensure reliable fuel supply to the company's geothermal power stations. Accordingly, the company expects FY2017 SIB capital expenditure to be $125 million. Average SIB capex over the last four years will match capital expenditure guidance of $80 million per annum over the medium term.

Following an unsuccessful sales process of the company's Chilean interests in 2015 the company embarked on a remediation programme on two geothermal fields at Tolhuaca and Puchuldiza. All geothermal wells were successfully plugged and abandoned, with the remediation of the Tolhuaca site completed and only minor surface works remaining at Puchuldiza. As previously noted, $18 million in relation to the remediation programme was treated as capital expenditure during 2016 and was subject to subsequent impairment.

During the year the company modified its approach to providing for the abandonment and subsequent restoration of areas from which geothermal resources have been utilised, with provisions now made at a steam field rather than individual well level. This change, along with a reassessment of well life and the ultimate cost of abandonment and restoration resulted in a $28 million provision increase, taking the company's domestic geothermal provision to $43 million. This increase reduced the asset revaluation reserves of the related operating stations.

CAPITAL STRUCTURE AND DIVIDENDS

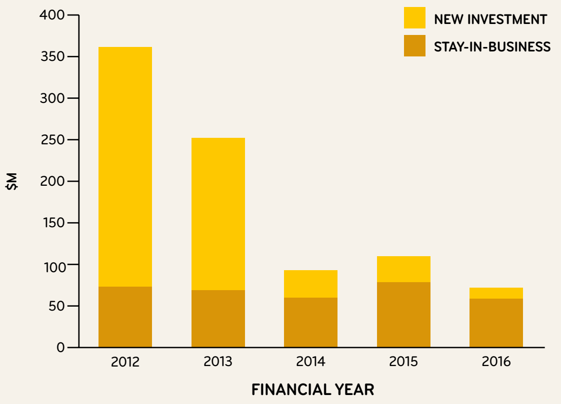
The company remains committed to an efficient and sustainable capital structure with a key reference to a 'bbb' stand-alone credit rating while maintaining appropriate balance sheet flexibility.

With this in mind, the company has $1,121 million of drawn debt and $300 million of undrawn committed facilities, both unchanged from the prior year. The average maturity profile for committed facilities fell from 9.9 years last year to 8.9 years at the end of FY2016.

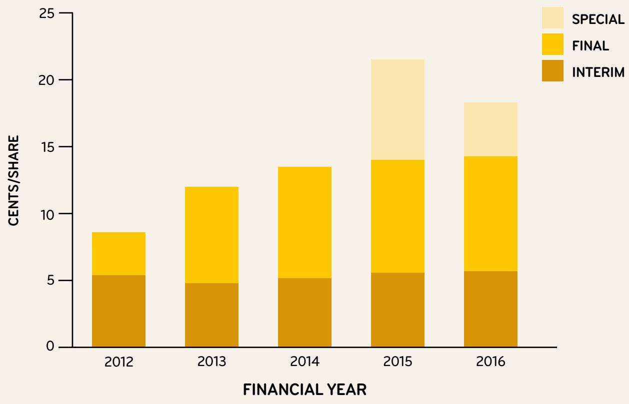
Average interest rates of 8.5% remained high reflecting interest rate hedges put in place in 2008 ahead of the company's domestic geothermal programme. These hedges roll off from the end of 2018 with an estimated net cash flow benefit in excess of $20 million at current rates.

In line with the company's dividend policy to make distributions with a pay-out ratio of 70% to 85% of Free Cash Flow on average over time, a fully imputed 8.6 cents per share final dividend has been declared. This took the full year ordinary dividend to 14.3 cents per share, also fully imputed, in line with guidance and representing a 2.1% increase on the 2015 level. In addition, the company has declared an unimputed 4.0 cents per share special dividend. Dividends will be paid on 30 September 2016. ●

>> **FIGURE 5:** CAPITAL EXPENDITURE



>> **FIGURE 6:** DIVIDENDS



FINANCIAL TRACK RECORD.

Financial Performance Trends

For the year ended 30 June ($ million)	2016	2015	2014	2013	2012
Income statement					
Energy margin	658	648	687	673	679
EBITDAF	493	482	504	390	461
Net profit for the year	160	47	212	115	68
Balance sheet					
Total shareholders' equity	3,315	3,337	3,219	3,183	3,014
Total assets	6,085	6,058	5,689	5,802	5,877
Total liabilities	2,770	2,721	2,470	2,619	2,863
Cash flow					
Operating cash flow	280	309	317	286	277
Investing cash flow	(37)	(103)	(99)	(84)	(292)
Financing cash flow	(228)	(195)	(213)	(230)	28
Capital expenditure					
Total capital expenditure[1]	72	110	93	252	362
Growth capital expenditure	13	31	33	183	288
Stay-in-business capital expenditure	59	79	60	69	74
Other financial measures					
Underlying earnings after tax	152	145	185	180	163
Free cash flow	221	230	257	217	203
Ordinary and special declared dividends	252	296	186	168	120
Ordinary dividends per share (cents)	14.3	14.0	13.5	12.0	8.6
Special dividends per share (cents)	4.0	7.5	–	–	–
Basic and diluted earnings per share (cents)	11.6	3.4	15.3	8.2	4.8
Net debt	1,068	1,082	1,031	1,028	1,116
Gearing (net debt/net debt+equity, %)	24.4	24.5	24.3	24.4	27.0
Debt/EBITDAF (x)[2]	2.0	2.0	2.1	2.7	2.6
Operational measures					
Total recordable injury frequency rate (TRIFR)[3]	0.74	1.25	0.84	1.52	1.84
Sales to customers (FPVV, GWh)	4,397	4,486	4,844	5,252	5,021
Electricity customers ('000)	376	382	382	388	386
Electricity generation (GWh)	6,842	6,563	6,295	6,462	7,068

1 In FY2016 the company spent an additional $18m of capital expenditure on remediation works in Chile which was not considered to be Growth or Stay-in-Business in nature.

2 Adjusted for S&P treatment of subordinated debt issued in FY2015.

3 Per 200,000 hours; includes onsite employees and contractors.

STATEMENT FROM THE DIRECTORS.

The Directors are pleased to present Mercury NZ Limited's annual report and financial statements for the year ended 30 June 2016.

The Auditor-General is required to be the company's auditor, and has appointed Simon O'Connor of Ernst & Young to undertake the audit on her behalf.

The Directors are not aware of any circumstances since the end of the year that have significantly or may significantly affect the operations of the Group.

This Annual Report is dated 23 August 2016 and is signed on behalf of the Board by:

>> **JOAN WITHERS,** CHAIR

>> **KEITH SMITH,** DIRECTOR

INDEPENDENT AUDITOR'S REPORT.

Building a better working world

Chartered Accountants

INDEPENDENT AUDITOR'S REPORT TO THE SHAREHOLDERS OF MERCURY NZ LIMITED
REPORT ON THE AUDIT OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2016

The Auditor-General is the auditor of Mercury NZ Limited and its subsidiaries and other controlled entities (collectively referred to as 'the Group'). The Auditor-General has appointed me, Simon O'Connor, using the staff and resources of Ernst & Young, to carry out the audit of the financial statements of the Group on her behalf.

OPINION

We have audited the financial statements of the Group on pages 48 to 73, that comprise the consolidated balance sheet as at 30 June 2016, the consolidated income statement, consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated cash flow statement for the year ended on that date and the notes to the financial statements that include accounting policies and other explanatory information.

In our opinion the financial statements of the Group comply with generally accepted accounting practice in New Zealand and present fairly, in all material respects, its financial position as at 30 June 2016 and its financial performance and cash flows for the year then ended in accordance with New Zealand Equivalents to International Financial Reporting Standards and International Financial Reporting Standards.

Our audit was completed on 23 August 2016. This is the date at which our opinion is expressed.

The basis for our opinion is explained below. In addition, we outline the responsibilities of the Board of Directors and our responsibilities, and explain our independence.

BASIS OF OPINION

We carried out our audit in accordance with the Auditor-General's Auditing Standards, which incorporate the International Standards on Auditing (New Zealand). Those standards require that we comply with ethical requirements and plan and carry out our audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

Material misstatements are differences or omissions of amounts and disclosures that, in our judgement, are likely to influence shareholders' overall understanding of the financial statements. If we had found material misstatements that were not corrected, we would have referred to them in our opinion.

An audit involves carrying out procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our judgement, including our assessment of risks of material misstatement of the financial statements whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the preparation of the Group's financial statements in order to design audit procedures that are appropriate in the circumstances but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.

An audit also involves evaluating:

- the appropriateness of accounting policies used and whether they have been consistently applied;
- the reasonableness of the significant accounting estimates and judgements made by the Board of Directors;
- the adequacy of the disclosures in the financial statements; and
- the overall presentation of the financial statements.

We did not examine every transaction, nor do we guarantee complete accuracy of the financial statements. Also we did not evaluate the security and controls over the electronic publication of the financial statements.

We believe we have obtained sufficient and appropriate audit evidence to provide a basis for our audit opinion.

RESPONSIBILITIES OF THE BOARD OF DIRECTORS

The Board of Directors is responsible for the preparation and fair presentation of financial statements for the Group that comply with generally accepted accounting practice in New Zealand and New Zealand Equivalents to International Financial Reporting Standards and International Financial Reporting Standards.

The Board of Directors' responsibilities arise from the Financial Markets Conduct Act 2013.

The Board of Directors is also responsible for such internal control as it determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error. The Board of Directors is also responsible for the publication of the financial statements, whether in printed or electronic form.

RESPONSIBILITIES OF THE AUDITOR

We are responsible for expressing an independent opinion on the financial statements and reporting that opinion to you based on our audit. Our responsibility arises from the Public Audit Act 2001.

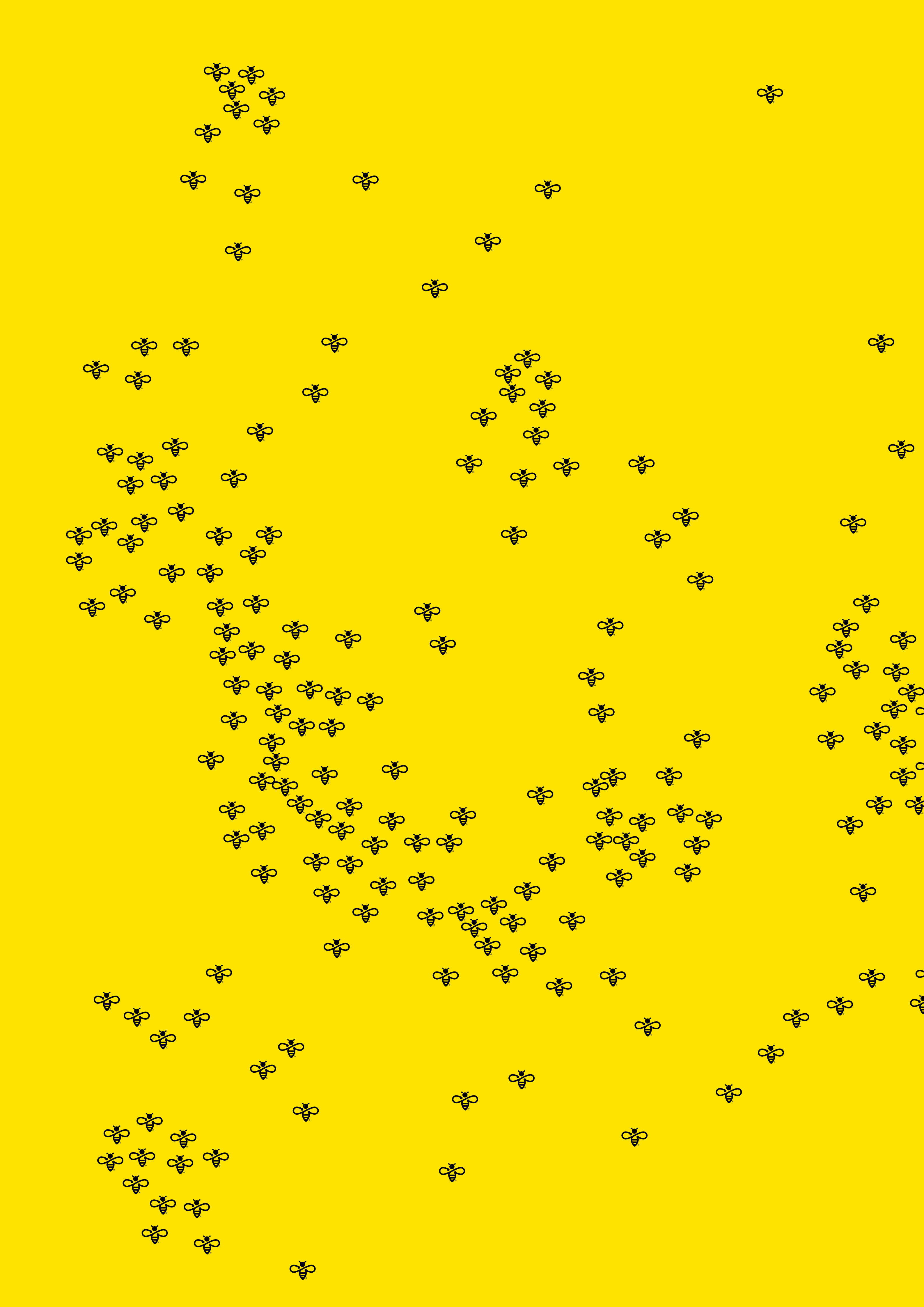
INDEPENDENCE

When carrying out the audit we followed the independence requirements of the Auditor-General, which incorporate the independence requirements of the External Reporting Board.

In addition to the audit we have carried out other assignments including a review of the Group's financial statements for the six months ended 31 December 2015, remuneration benchmarking services and tax compliance services in the United States, which are compatible with the independence requirements of the External Reporting Board. We have no other relationship with or interests in the Group.

Partners and staff of Ernst & Young may deal with the Group on normal terms within the ordinary course of trading activities of the business of the Group.

>> **SIMON O'CONNOR**
ERNST & YOUNG
ON BEHALF OF THE AUDITOR-GENERAL
AUCKLAND, NEW ZEALAND



FINANCIAL STATEMENTS

CONSOLIDATED INCOME STATEMENT

FOR THE YEAR ENDED 30 JUNE 2016

	Note	2016 $M	2015 $M
Total revenue	4	1,564	1,678
Total expenses	4	(1,071)	(1,196)
EBITDAF[1]		493	482
Depreciation and amortisation	8, 9	(182)	(170)
Change in the fair value of financial instruments	15	20	8
Impairments	4	(19)	(130)
Earnings of associates and joint ventures	10	3	3
Net interest expense	4	(97)	(99)
Profit before tax		218	94
Tax expense	6	(58)	(47)
Profit for the year attributable to owners of the parent		160	47
Basic and diluted earnings per share (cents)		11.63	3.42

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

FOR THE YEAR ENDED 30 JUNE 2016

		2016 $M	2015 $M
Profit for the year		160	47
Other comprehensive income			
Items that will not be reclassified subsequently to profit or loss			
Movement in asset revaluation reserve		106	497
Share of movements in associates' and joint ventures' reserves	10	6	(1)
Tax effect		(30)	(141)
Items that may be reclassified subsequently to profit or loss			
Movement in cash flow hedge reserve	15	(54)	(40)
Movement in other reserves		2	5
Tax effect		16	11
Other comprehensive income for the year, net of taxation		46	331
Total comprehensive income for the year attributable to owners of the parent		206	378

1 EBITDAF: Earnings before net interest expense, income tax, depreciation and amortisation, change in the fair value of financial instruments, impairments and equity accounted earnings of associates and joint ventures.

The accompanying notes form an integral part of these financial statements.

CONSOLIDATED BALANCE SHEET

AS AT 30 JUNE 2016

	Note	2016 $M	2015 $M
SHAREHOLDERS' EQUITY			
Issued capital		378	378
Treasury shares	5	(52)	(52)
Reserves		2,989	3,011
Total shareholders' equity		3,315	3,337
ASSETS			
Current assets			
Cash and cash equivalents		46	32
Receivables	11	198	190
Inventories	7	45	30
Derivative financial instruments	15	21	35
Taxation receivable	6	3	–
Total current assets		313	287
Non-current assets			
Property, plant and equipment	8	5,440	5,416
Intangible assets	9	68	70
Investment and advances to associates	10	78	74
Investment in joint ventures	10	14	14
Advances	10	10	12
Derivative financial instruments	15	162	157
Total non-current assets		5,772	5,743
Held-for-sale assets		–	28
Total assets		6,085	6,058
LIABILITIES			
Current liabilities			
Payables and accruals	11	156	159
Provisions	12	3	–
Borrowings	13	130	10
Derivative financial instruments	15	21	14
Taxation payable	6	–	15
Total current liabilities		310	198
Non-current liabilities			
Payables and accruals	11	2	2
Provisions	12	51	14
Derivative financial instruments	15	267	243
Borrowings	13	1,047	1,167
Deferred tax	6	1,093	1,092
Total non-current liabilities		2,460	2,518
Held-for-sale liabilities		–	5
Total liabilities		2,770	2,721
Net assets		3,315	3,337

For and on behalf of the Board of Directors who authorised the issue of the Financial Statements on 23 August 2016.

Joan Withers
Chair
23 August 2016

Keith Smith
Director
23 August 2016

The accompanying notes form an integral part of these financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

FOR THE YEAR ENDED 30 JUNE 2016

	Issued capital $M	Retained earnings $M	Asset revaluation reserve $M	Cash flow hedge reserve $M	Other reserves $M	Total equity $M
Balance as at 1 July 2014	378	534	2,383	(7)	(69)	3,219
Movement in asset revaluation reserve, net of taxation	–	–	356	–	–	356
Movement in cash flow hedge reserve, net of taxation	–	–	–	(29)	–	(29)
Movements in other reserves	–	–	–	–	6	6
Share of movements in associates' and joint ventures' reserves	–	–	–	(1)	–	(1)
Release of asset revaluation reserve, net of taxation	–	–	(1)	–	–	(1)
Other comprehensive income	–	–	355	(30)	6	331
Net profit for the year	–	47	–	–	–	47
Total comprehensive income for the year	–	47	355	(30)	6	378
Dividend	–	(260)	–	–	–	(260)
Balance as at 30 June 2015	378	321	2,738	(37)	(63)	3,337
Balance as at 1 July 2015	378	321	2,738	(37)	(63)	3,337
Movement in asset revaluation reserve, net of taxation	–	–	79	–	–	79
Movement in cash flow hedge reserve, net of taxation	–	–	–	(38)	–	(38)
Movements in other reserves	–	–	–	–	2	2
Share of movements in associates' and joint ventures' reserves	–	–	7	(1)	–	6
Release of asset revaluation reserve, net of taxation	–	–	(3)	–	–	(3)
Other comprehensive income	–	–	83	(39)	2	46
Net profit for the year	–	160	–	–	–	160
Total comprehensive income for the year	–	160	83	(39)	2	206
Dividend	–	(228)	–	–	–	(228)
Balance as at 30 June 2016	378	253	2,821	(76)	(61)	3,315

The accompanying notes form an integral part of these financial statements.

CONSOLIDATED CASH FLOW STATEMENT

FOR THE YEAR ENDED 30 JUNE 2016

	2016 $M	2015 $M
CASH FLOWS FROM OPERATING ACTIVITIES		
Receipts from customers	1,515	1,652
Payments to suppliers and employees	(1,051)	(1,168)
Interest received	3	5
Interest paid	(98)	(101)
Taxes paid	(89)	(79)
Net cash provided by operating activities	280	309
CASH FLOWS FROM INVESTING ACTIVITIES		
Acquisition of property, plant and equipment	(78)	(105)
Acquisition of intangibles	(12)	(13)
Disposal of property, plant and equipment	11	–
Disposal of land and associated real property	36	9
Distributions received from associates and joint ventures and advances to joint venture partner repaid	6	6
Net cash used in investing activities	(37)	(103)
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from loans	–	300
Repayment of loans	–	(235)
Dividends paid	(228)	(260)
Net cash used in financing activities	(228)	(195)
Net increase in cash and cash equivalents held	15	11
Net foreign exchange movements	(1)	2
Cash and cash equivalents at the beginning of the year	32	19
Cash and cash equivalents at the end of the year	46	32
Cash balance comprises:		
Cash balance at the end of the year	46	32

The accompanying notes form an integral part of these financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2016

NOTE 1. ACCOUNTING POLICIES

(1) Reporting entity

On 29 July 2016, Mighty River Power Limited changed its name to Mercury NZ Limited ("company"). The company is incorporated in New Zealand, registered under the Companies Act 1993, an FMC reporting entity under the Financial Markets Conduct Act 2013, and is listed on the NZSX and ASX.

The consolidated financial statements ("Group financial statements") are for Mercury NZ Limited Group ("Group"). The Group financial statements comprise the company and its subsidiaries, including its investments in associates and interests in joint arrangements.

The liabilities of the Group are not guaranteed in any way by the Crown or by any other shareholder.

(2) Basis of preparation

The Group financial statements have been prepared in accordance with the Financial Reporting Act 2013, the Companies Act 1993 and in accordance with New Zealand Generally Accepted Accounting Practice ("NZ GAAP"). They comply with New Zealand equivalents to International Financial Reporting Standards ("NZ IFRS") as appropriate for profit-oriented entities. These financial statements also comply with International Financial Reporting Standards ("IFRS").

The Group financial statements are prepared on the basis of historical cost, with the exception of financial instruments and generation assets measured at fair value, and held-for-sale assets measured at fair value less cost to sell.

The Group financial statements have been prepared so that all components are stated exclusive of GST, with the exception of receivables and payables that include GST invoiced.

Functional and presentation currency

These financial statements are presented in New Zealand Dollars ($) which is the Group's functional currency, apart from Mighty Geothermal Power Limited and its direct subsidiaries as their functional currency is the United States Dollar. Unless otherwise stated, financial information has been rounded to the nearest million dollars ($M).

The assets and liabilities of entities whose functional currency is not the New Zealand Dollar, are translated at the exchange rates ruling at balance date. Revenue and expense items are translated at the spot rate at the transaction date or a rate approximating that rate. Exchange differences are taken to the foreign currency translation reserve.

Estimates and judgements

The preparation of financial statements requires judgements and estimates that affect the application of policies and the reported amounts of assets and liabilities, income and expenses. Actual results may differ from these estimates.

The areas of significant estimates and judgements are as follows:

- Impairment of non-financial assets (refer note 4)
- Generation plant and equipment (refer note 8)
- Retail revenue accruals (refer note 11)
- Restoration and environmental rehabilitation (refer note 12)
- Valuation of financial instruments (refer note 14 and note 15)

Accounting policies and standards

No changes to accounting policies have been made during the year and policies have been consistently applied to all years presented. Certain comparatives have been restated where needed to conform to current year classification and presentation.

The Group has elected not to early adopt NZ IFRS 9, 15 and 16, nor has the impact of adopting these standards been assessed.

NOTE 2. SEGMENT REPORTING

Identification of reportable segments

The operating segments are identified by management based on the nature of the products and services provided. Discrete financial information about each of these operating businesses is reported to the Chief Executive, being the chief operating decision-maker, on at least a monthly basis, who assesses the performance of the operating segments on a measure of EBITDAF. Segment EBITDAF represents profit earned by each segment exclusive of any allocation of central administration costs, share of earnings of associates, change in fair value of financial instruments, depreciation, amortisation, impairments, finance costs and tax expense. Operating segments are aggregated into reportable segments only if they share similar economic characteristics.

Types of products and services

Energy Markets

The energy markets segment encompasses activity associated with the production, sale and trading of energy and related services and products, and generation development activities.

Other Segments

Other operating segments that are not considered to be reporting segments are grouped together as "Other Segments". Activities include metering and international geothermal development and operations.

Unallocated

Represents corporate support services and related elimination adjustments.

Inter-segment

Transactions between segments are carried out on normal commercial terms and represent charges by Other Segments to Energy Markets.

Segment results

June 2016	Energy markets $M	Other segments $M	Unallocated $M	Inter-segment $M	Total $M
Total segment revenue	1,542	50	2	(30)	1,564
Direct costs	(882)	(2)	–	30	(854)
Other operating expenses	(145)	(24)	(48)	–	(217)
Segment EBITDAF	515	24	(46)	–	493

June 2015	Energy markets $M	Other segments $M	Unallocated $M	Inter-segment $M	Total $M
Total segment revenue	1,666	45	(3)	(30)	1,678
Direct costs	(1,005)	(4)	–	30	(979)
Other operating expenses	(150)	(23)	(44)	–	(217)
Segment EBITDAF	511	18	(47)	–	482

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2016

NOTE 3. NON STATUTORY MEASURE – UNDERLYING EARNINGS

Underlying earnings is presented to enable stakeholders to make an assessment and comparison of earnings after removing one-off and/or infrequently occurring events (exceeding $10 million of net profit before tax), impairments and any changes in the fair value of derivative financial instruments or any equity accounted share of changes in the fair value of derivative financial instruments.

	2016 $M	2015 $M
Profit for the year	160	47
Change in the fair value of financial instruments	(20)	(8)
Income attributable to land and associated real property sold or held-for-sale	(13)	(17)
Impairments	19	130
Adjustments before tax expense	(14)	105
Tax expense	6	(7)
Adjustments after tax expense	(8)	98
Underlying earnings after tax	152	145

Tax has been applied on all taxable adjustments at 28%.

NOTE 4. OTHER INCOME STATEMENT DISCLOSURES

	2016 $M	2015 $M
Sales	1,512	1,627
Other revenue	52	51
Total revenue	1,564	1,678
Energy costs	(384)	(507)
Line charges	(419)	(422)
Other direct cost of sales, excluding third party metering	(28)	(26)
Third party metering	(23)	(24)
Employee compensation and benefits	(83)	(82)
Maintenance expenses	(45)	(54)
Other expenses	(89)	(81)
Total expenses	(1,071)	(1,196)
Interest expense	(100)	(104)
Interest income	3	5
Net interest expense	(97)	(99)

Audit fees

Fees incurred by EY for the audit and review of the financial statements were $596,000 (2015: $682,000). Non audit services in relation to NZ remuneration benchmarking services were $11,000 (2015: $8,000). EY (US) also provided US tax compliance services in the amount of $305,000 (2015: $340,000).

Impairments

During the previous financial year the Group announced its intention to exit from its geothermal development interests in Chile. Following an unsuccessful sales process, the Group commenced a remediation programme in February 2016. Accordingly, an additional $18 million provision for the works programme was recognised as capital expenditure and subsequently impaired (notes 8 and 12). This increase takes the total remediation provision for Chile to $22 million, of which $19 million was incurred during the current year. All geothermal wells have been successfully plugged and abandoned with the remediation of the Tolhuaca site complete. Only minor surface works remain at Puchuldiza.

Following the planned closure of the gas-fired Southdown power station on 31 December 2015 and as a consequence of the associated plant divestment process, an additional impairment of $1 million has been recognised in the current year.

NOTE 5. SHARE CAPITAL AND DISTRIBUTION

The share capital of the company is represented by 1,400,012,517 ordinary shares (2015: 1,400,012,517) issued and fully paid. The weighted average number of shares on issue during the year, on both a basic and diluted basis, was 1,376,076,400 (2015: 1,375,892,536). These shares do not have a par value, have equal voting rights and share equally in dividends and any surplus on winding up.

	2016 Number of shares (M)	2016 $M	2015 Number of shares (M)	2015 $M
Treasury shares				
Balance at the beginning of the year	24	52	24	52
Balance at the end of the year	24	52	24	52

Dividends declared and paid

	Cents per share	2016 $M	2015 $M
Final dividend for 2014	8.30	–	114
Special dividend paid December 2014	5.00	–	69
Interim dividend for 2015	5.60	–	77
Final dividend for 2015	8.40	116	–
Special dividend paid September 2015	2.50	34	–
Interim dividend for 2016	5.70	78	–
		228	260

Imputation credits available to shareholders in the future amount to $2.1 million (2015: $16.1 million).

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NOTE 6. TAXATION

Income Tax	2016 $M	2015 $M
(i) Tax expense		
Profit before tax	218	94
Prima facie tax expense at 28% on the profit before tax	(61)	(26)
Increase/(decrease) in tax expense due to:		
• share of associates' and joint ventures' tax paid earnings	1	–
• capital gain	4	–
• foreign entities' non-deductible costs	–	(2)
• non-deductible impairments	(5)	(23)
• other differences	1	1
• recognition of deferred tax on powerhouse assets	2	3
Tax expense attributable to profit from ordinary activities	(58)	(47)
Represented by:		
Current tax expense	(67)	(68)
Deferred tax recognised in the income statement	9	21

The tax expense charged to the income statement includes both the current year's provision and the income tax effect of:

- taxable temporary differences, except those arising from initial recognition of goodwill; and
- deductible temporary differences to the extent that it is probable that they will be utilised.

Deferred Tax

Deferred tax is provided in full, using the liability method, on temporary differences arising between the tax and accounting bases of the Group's assets and liabilities. A deferred tax asset is only recognised to the extent that there will be future taxable profit to utilise the temporary difference.

Property, plant and equipment is held on capital account for income tax purposes. Where assets are revalued, with no similar adjustment to the tax base, a taxable temporary difference is created that is recognised in deferred tax. The deferred tax liability on these revaluations is unlikely to crystallise in the foreseeable future under existing income tax legislation.

(i) Recognised deferred tax assets and liabilities

	Assets 2016 $M	Assets 2015 $M	Liabilities 2016 $M	Liabilities 2015 $M	Net 2016 $M	Net 2015 $M
Property, plant and equipment	–	–	(1,171)	(1,149)	(1,171)	(1,149)
Financial instruments	51	42	–	–	51	42
Employee benefits and provisions	2	2	–	–	2	2
Other	25	13	–	–	25	13
	78	57	(1,171)	(1,149)	(1,093)	(1,092)

(ii) Movement in deferred tax

	Property, plant and equipment $M	Financial instruments $M	Employee entitlements $M	Other $M	Total $M
Balance as at 1 July 2014	(1,030)	31	–	16	(983)
Charged/(credited) to the income statement	19	–	1	1	21
Charged/(credited) to other comprehensive income	(141)	11	–	–	(130)
Other movements	3	–	1	(4)	–
Balance as at 30 June 2015	(1,149)	42	2	13	(1,092)
Balance as at 1 July 2015	(1,149)	42	2	13	(1,092)
Charged/(credited) to the income statement	13	(5)	–	1	9
Charged/(credited) to other comprehensive income	(38)	16	–	8	(14)
Other movements	3	(2)	–	3	4
Balance as at 30 June 2016	(1,171)	51	2	25	(1,093)

Tax deductions for building depreciation were disallowed by the Inland Revenue from 1 July 2011. Since then, the Group has maintained the view that powerhouse assets are plant and not buildings and therefore should not be captured by this change. The Group accepted there was a potential risk that a portion of those assets may still be considered by the Inland Revenue to be a building for tax purposes. As a prudent measure, an adjustment was made to the deferred tax liability and tax expense recognised in the Group's 30 June 2010 financial statements relating to a portion of the geothermal powerhouse assets.

During the year, the Group engaged a quantity surveyor to identify the specific building components of the geothermal powerhouse assets. This resulted in an increase in tax depreciable assets. Consequently, a net adjustment of $2 million has been made to reverse a portion of the 2010 increase to deferred tax liabilities in respect of geothermal powerhouse assets. This adjustment has been recognised through the income statement as a lower tax expense. The Group acknowledges that the Inland Revenue may challenge the position adopted in respect of geothermal powerhouse assets. In the event a challenge by the Inland Revenue is successful, this could result in an additional deferred tax liability (and tax expense) of up to $6 million at that time.

NOTE 7. INVENTORIES

Cost is determined on a weighted average basis and includes expenditure incurred in acquiring inventories and bringing them to their existing condition and location. Consumable stores of $31 million (2015: $22 million) are held to service and repair operating plant. Meter stock of $14 million (2015: $8 million) is held in inventory until it is deployed into the field at which time it is transferred into property, plant and equipment.

NOTE 8. PROPERTY, PLANT AND EQUIPMENT

	Generation assets at fair value $M	Meters at cost $M	Other assets at cost $M	Capital work in progress at cost $M	Total $M
Year ended 30 June 2015					
Opening net book value	4,915	61	55	64	5,095
Additions, including transfers from capital work in progress	52	15	7	21	95
Disposals	(4)	–	–	–	(4)
Transfer to held-for-sale and other assets at cost	(12)	–	6	(8)	(14)
Net revaluation movement	497	–	–	–	497
Impairments	(76)	–	(2)	(24)	(102)
Exchange movements	4	–	–	1	5
Depreciation charge for the year	(132)	(11)	(13)	–	(156)
Closing net book value	5,244	65	53	54	5,416
Balance at 30 June 2015					
Cost or valuation	5,244	160	129	54	5,587
Accumulated depreciation	–	(95)	(76)	–	(171)
Net book value	5,244	65	53	54	5,416
Year ended 30 June 2016					
Opening net book value	5,244	65	53	54	5,416
Additions, including transfers from capital work in progress	30	7	21	13	71
Disposals	–	–	–	(1)	(1)
Transfer from held-for-sale	3	–	–	–	3
Net revaluation movement	137	–	–	–	137
Impairments	(1)	–	(18)	–	(19)
Depreciation charge for the year	(144)	(12)	(11)	–	(167)
Closing net book value	5,269	60	45	66	5,440
Balance at 30 June 2016					
Cost or valuation	5,269	167	132	66	5,634
Accumulated depreciation	–	(107)	(87)	–	(194)
Net book value	5,269	60	45	66	5,440

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2016

NOTE 8. PROPERTY, PLANT AND EQUIPMENT (CONTINUED)

Assets carrying values

The cost of property, plant and equipment purchased comprises the consideration given to acquire the assets plus other directly attributable costs incurred in bringing the assets to the location and condition necessary for their intended use.

The cost of property, plant and equipment constructed by the Group, including capital work in progress, includes the cost of all materials used in construction, associated direct labour and an appropriate proportion of variable and fixed overheads. Financing costs attributable to a project are capitalised at the Group's specific project finance interest rate, where these meet certain time and monetary materiality limits. Costs of testing whether the assets are functioning properly, after deducting the net proceeds from power generation, are also capitalised. Costs cease to be capitalised as soon as an asset is ready for productive use.

Costs incurred in obtaining resource consents are capitalised and recognised as a non-current asset where it is probable they will give rise to future economic benefits. These costs are depreciated over the life of the consent on a straight-line basis.

Generation plant and equipment is measured at fair value less accumulated depreciation. Any surplus on revaluation of an individual item of property, plant and equipment is transferred directly to the asset revaluation reserve unless it offsets a previous decrease in value recognised in the income statement, in which case it is recognised in the income statement. A deficit on revaluation of an individual item of property, plant and equipment is recognised in the income statement in the period it arises where it exceeds any surplus previously transferred to the asset revaluation reserve. Any accumulated depreciation at the date of the revaluation is eliminated against the gross carrying amount of the asset and the net amount is restated to the revalued amount of the asset. Additions to property, plant and equipment stated at valuation subsequent to the most recent valuation are recorded at cost. All other items of property, plant and equipment are recorded at cost less depreciation and impairments.

Assets carried at fair value

All generation assets shown at valuation (except Resource Management Act consents) were revalued using a net present value methodology by PricewaterhouseCoopers, an independent valuer, as at 30 June 2016. This resulted in an increase to the carrying value of generation assets of $139 million in the current year. This is in addition to the $504 million revaluation increase recognised in 2015. As a consequence of the revaluation, accumulated depreciation on these assets has been reset to nil.

The key assumptions that are used in the valuation include the forecast of the future wholesale electricity price path, volumes, projected operational and capital expenditure, capacity and life assumptions and discount rate. In all cases there is an element of judgement required as they make use of unobservable inputs including wholesale electricity prices of between $66/MWh and $102/MWh (2015: $63/MWh and $97/MWh), average operational expenditure of $174 million p.a. (2015: $168 million p.a.), average production volumes of 6,956/GWh p.a. (2015: 7,131/GWh p.a.) and a post-tax discount rate of between 7.4% and 7.9% (2015: 7.5% and 7.9%). The valuation also assumed the on-going operation of New Zealand Aluminium Smelters Limited at Tiwai Point and that the current regulatory environment is retained. The discounted cash flow valuation approach assumes 100% control and consequently a control premium should be applied if using an equity valuation technique to derive asset values.

The following table outlines the valuation impact of changes to assumptions, keeping all other valuation inputs constant, that the valuation is most sensitive to.

	Sensitivity	Valuation impact	
		2016 $M	2015 $M
Future wholesale electricity price path	+/- 10%	$786 / ($790)	$800 / ($803)
Discount rate	+/- 0.5%	($521) / $624	($648) / $891
Operational expenditure	+/- 10%	($237) / $238	($251) / $251

The carrying amount of revalued generation assets, had they been recognised at cost, would have been $1,974 million (2015: $2,014 million).

Depreciation

Depreciation is provided on a straight-line basis on all property, plant and equipment other than freehold land, capital work in progress and exploration and evaluation assets, so as to write down the assets to their estimated residual value over their expected useful lives.

The annual depreciation rates are as follows:

	2016	2015
Office fixture and fittings, including fitout	2–50%	2–20%
Generation assets:		
• Hydro and thermal generation	1–33%	1–33%
• Other generation	2–33%	2–33%
Meters	3–33%	3–33%
Computer hardware and tangible software	5–50%	5–50%
Other plant and equipment	2–50%	2–50%
Vehicles	5–33%	5–33%

NOTE 9. INTANGIBLE ASSETS

	Intangible software $M	Rights $M	Emissions units $M	Total $M
Year ended 30 June 2015				
Opening net book value	29	26	16	71
Additions	8	–	6	14
Impaired assets	–	(1)	–	(1)
Amortisation for the year	(12)	(2)	–	(14)
Closing net book amount	25	23	22	70
Balance at 30 June 2015				
Cost	123	33	22	178
Accumulated amortisation	(98)	(10)	–	(108)
Net book value	25	23	22	70
Year ended 30 June 2016				
Opening net book value	25	23	22	70
Additions	5	1	6	12
Amortisation for the year	(13)	(1)	–	(14)
Closing net book amount	17	23	28	68
Balance at 30 June 2016				
Cost	128	34	28	190
Accumulated amortisation	(111)	(11)	–	(122)
Net book value	17	23	28	68

Software

Acquired computer software licenses are capitalised on the basis of the costs incurred to acquire and bring to use. These costs are amortised over their remaining estimated useful lives of between 2 to 15 years (2015: between 2 to 15 years). As these assets are deemed to have a finite life, impairment testing will only be performed when there is an indication that the intangible asset may be impaired.

Rights

Rights, of which land access rights are the most significant, acquired to further the Group's generation development programme are stated at cost less accumulated amortisation and any accumulated impairment losses. Rights, which have a finite life, are amortised over the life of the rights, which range from 3 to 25 years (2015: 3 to 25 years). Testing for impairment will only arise when there is an indication that the asset may be impaired.

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NOTE 9. INTANGIBLE ASSETS (CONTINUED)

Emissions units and emissions obligations

Emissions units that have been allocated by the Government under the Projects to Reduce Emissions scheme are recorded at nominal value (nil value). Purchased emissions units are recorded at cost (purchase price). Emissions units, whether allocated or purchased, are recorded as intangible assets. Emissions units are not revalued subsequent to initial recognition.

Emissions units that are surrendered to creditors in compensation for their emissions obligations are recognised as an expense in the income statement and a reduction to intangible assets in the balance sheet, based on the weighted average cost of the units surrendered.

Emissions obligations are recognised as a current liability as the obligation is incurred. Up to the level of units held, the liability is recorded at the carrying value of those units intended to settle the liability. Forward contracts for the purchase of emissions units are recognised when the contracts are settled.

NOTE 10. INVESTMENT AND ADVANCES TO ASSOCIATES AND JOINT ARRANGEMENTS (JOINT VENTURES AND JOINT OPERATIONS)

The Group financial statements include the following:

			Interest held		
Name of entity	**Principal activity**	**Type**	**2016**	**2015**	**Country**
TPC Holdings Limited	Investment holding	Associate	25.00%	25.00%	New Zealand
Rotokawa	Steamfield operation	Joint operation	64.80%	64.80%	New Zealand
Nga Awa Purua	Electricity generation	Joint operation	65.00%	65.00%	New Zealand
Energy Source LLC	Investment holding	Joint venture	20.86%	20.86%	United States
Hudson Ranch I Holdings LLC	Electricity generation	Joint venture	75.00%	75.00%	United States

	Associates		Joint ventures	
	2016 $M	2015 $M	2016 $M	2015 $M
Balance at the beginning of the year	74	78	14	23
Share of earnings	3	2	–	1
Share of movement in other comprehensive income	6	(1)	–	–
Distributions received during the year	(5)	(5)	–	–
Impaired investment in joint venture	–	–	–	(14)
Exchange movements	–	–	–	4
Balance at the end of the year	78	74	14	14

At the end of the year the Group had an outstanding advance to its Rotokawa joint venture partner in the amount $10 million (2015: $11 million). For terms and conditions of this related party receivable refer to note 17.

Due to the nature of the contractual arrangements that surround the joint venture entities, which allows for a reduction in the Group's economic interest once prescribed preferred returns have been achieved, the share of movements in earnings and reserves has been calculated based on the Hypothetical Liquidation at Book Value method. This method more closely aligns the recognition of earnings through time with the expected contractually agreed economic outcomes compared to the recognition of earnings based on a strict percentage of ownership.

In compliance with the equity method under NZ IAS 28 - Investments in Associates and Joint Ventures, the Group has yet to recognise its share of losses relating to Energy Source LLC amounting to US$3 million (2015: US$3 million).

NOTE 11. RECEIVABLES, PAYABLES AND ACCRUALS

Receivables

	2016 $M	2015 $M
Trade receivables and accruals	190	182
Allowance for impairment loss	(2)	(2)
Net trade receivables and accruals	188	180
Prepayments	10	10
	198	190

Revenue accruals for unread gas and electricity meters at balance date involves an estimate of consumption for each unread meter, based on the customer's past consumption history.

Trade receivables are non-interest bearing and are generally on 30 day terms. For terms and conditions of related party receivables refer to note 17.

The Group recognises an allowance for impairment loss when there is objective evidence that the Group will not be able to collect amounts due according to the original terms of the receivable. An allowance charge of $5 million (2015: $2 million) was recognised during the year. Receivables of $5 million (2015: $4 million) which were known to be uncollectable were written off.

	2016 $M	2015 $M
Receivables past due but not considered impaired:		
Less than one month past due	5	6
Greater than one month past due	2	1
	7	7

	2016 $M	2015 $M
Payables and accruals		
Trade payables and accruals	149	154
Employee entitlements	6	6
Sundry creditors	3	1
	158	161

Trade payables are non-interest bearing and are normally settled on 30 to 60 day terms.

NOTE 12. PROVISIONS

	2016 $M	2015 $M
Balance at the beginning of the year	14	16
Provisions made during the year	54	–
Provisions used during the year	(19)	–
Discounting movement	2	2
Provisions transferred from/(to) held-for-sale liabilities	3	(4)
Balance at the end of the year	54	14
Current	3	–
Non-current	51	14
	54	14

Provisions have been recognised for the abandonment and subsequent restoration of areas from which geothermal resources have been utilised. The provision is calculated based on the present value of Management's best estimate of the expenditure required, and the likely timing of settlement. Changes in these estimates made during the year are reported as an increase in provisions and a reduction in revaluation reserves. The increase in provision resulting from the passage of time (the discount effect) is recognised as an interest expense.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2016

NOTE 13. BORROWINGS

	Borrowing currency denomination	Maturity	Coupon	2016 $M	2015 $M
Wholesale bonds	NZD	Oct-2016	7.55%	71	71
Wholesale bonds	NZD	Oct-2016	Floating	51	51
Wholesale bonds	NZD	Mar-2019	5.03%	76	76
Wholesale bonds	NZD	Feb-2020	8.21%	31	31
USPP – US$125m	USD	Dec-2020	4.25%	164	164
Wholesale/credit wrapper	NZD	Sep-2021	Floating	301	301
USPP – US$30m	USD	Dec-2022	4.35%	39	39
Wholesale bonds	NZD	Mar-2023	5.79%	25	25
USPP – US$45m	USD	Dec-2025	4.60%	58	58
Capital bonds	NZD	Jul-2044	6.90%	305	305
Deferred financing costs				(7)	(7)
Fair value adjustments				63	63
Carrying value of loans				1,177	1,177
Current				130	10
Non-current				1,047	1,167
				1,177	1,177

The company has entered into a Master Trust Deed and Supplementary Trust Deeds for all its NZD denominated Senior Fixed and Floating Rate Bonds with the New Zealand Guardian Trust Company Limited, acting as trustee for the holders. The company has agreed, subject to certain exceptions, not to create or permit to exist a security interest over or affecting its assets to secure indebtedness, and to maintain certain financial covenants. There has been no breach of the terms of these deeds.

The company has entered into a negative pledge deed in favour of its bank financiers in which the company has agreed, subject to certain exceptions, not to create or permit to exist a security interest over or affecting its assets to secure its indebtedness, and to maintain certain financial ratios in relation to the company. These undertakings and covenants also apply to the US Private Placement terms and conditions. There has been no breach of the terms of this deed or the terms and conditions of the US Private Placement.

The company has $300 million of committed and unsecured bank loan facilities, of which $200 million expires in August 2018 and a rolling bank loan facility of $100 million currently expiring in December 2017.

NOTE 14. FINANCIAL RISK MANAGEMENT

The Group's overall risk management programme focuses on the unpredictability of financial markets and seeks to proactively manage these risks with the aim of protecting shareholder wealth. Exposure to price, credit, foreign exchange, liquidity and interest rate risks arise in the normal course of the Group's business. The Group's principal financial instruments comprise cash and cash equivalents, trade receivables and accruals (not prepayments), advances, payables and accruals, borrowings and derivative financial instruments.

(A) MARKET RISK

Price risk – energy contracts

The Group enters into energy contracts that establish a fixed price at which future specified quantities of electricity are purchased and sold. The energy contracts are periodically settled with any difference between the contract price and the spot market price settled between the parties. At balance date, the principal value of energy contracts, including both buy and sell contracts, with remaining terms of up to 15 years, were $1,975 million (2015: $2,150 million).

Foreign exchange risk

The Group is exposed to foreign exchange risk as a result of transactions denominated in a currency other than the Group's functional currency. The currencies giving rise to this risk are primarily US Dollar, Japanese Yen and Euro.

Foreign exchange risk arises from future commercial transactions (including the purchase of capital equipment and maintenance services), recognised assets and liabilities (including borrowings) and net investments in foreign operations. It is the Group's policy to enter into forward exchange contracts to hedge its committed expenditure programme. At balance date the principal or contract amounts of foreign currency forward exchange contracts were $53 million (2015 $34 million).

The Group has certain investments in foreign operations whose net assets are exposed to foreign currency translation risk. Currency exposure arising from the net assets of foreign operations is currently unhedged but may be managed on a case-by-case basis.

Interest rate risk

The Group has exposure to interest rate risk to the extent that it borrows for fixed terms at floating interest rates. The Group manages its cost of borrowing by limiting the ratio of fixed to floating rate cover held. The Group uses interest rate swaps and interest rate options to manage this exposure. At balance date, the contract principal amount of interest rate swaps outstanding (including forward starts) was $3,051 million (2015: $2,951 million).

Sensitivity analysis

The following summarises the potential impact of increases or decreases in the relevant market risk exposures of the Group on post-tax profit and on other components of equity. The analysis does not take into account dynamic market response over time, which could be material.

Price risk

Sensitivity analysis is based on an assessment of the reasonably possible movements in forward price.

	Impact on post tax profit		Impact on equity	
	2016 $M	2015 $M	2016 $M	2015 $M
Group				
Electricity forward price increased by 10%	(4)	6	(36)	(36)
Electricity forward price decreased by 10%	4	(6)	36	36

Foreign exchange risk

Sensitivity analysis is based on the impact of the New Zealand Dollar weakening or strengthening against the most significant currencies for which the Group has foreign exchange exposure, allowing for reasonably possible movements in foreign exchange rates over a one year period based on the average actual movements experienced over the prior 10 years.

	Impact on post tax profit		Impact on equity	
	2016 $M	2015 $M	2016 $M	2015 $M
New Zealand Dollar – United States Dollar				
Currency strengthens by 10%	–	1	(1)	(1)
Currency weakens by 10%	–	(1)	1	1
New Zealand Dollar – Euro				
Currency strengthens by 10%	–	–	(2)	(1)
Currency weakens by 10%	–	–	3	2

Interest rate risk

Sensitivity analysis is based on an assessment of the reasonably possible movement in the 10 year swap rate over a one year period based on actual movements over the last 10 years. The movement in post-tax profits are due to higher/lower interest costs from variable rate debt and cash balances combined with the result of fair value changes in interest rate swaps and options that are valid economic hedges but which do not qualify for hedge accounting under NZ IAS 39. The movements in other components of equity result from fair value changes in interest rate swaps and options that have qualified for hedge accounting.

	Impact on post tax profit		Impact on equity	
	2016 $M	2015 $M	2016 $M	2015 $M
Interest rates higher by 100 bps	2	6	19	14
Interest rates lower by 100 bps	(2)	(6)	(21)	(16)

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2016

NOTE 14. FINANCIAL RISK MANAGEMENT (CONTINUED)

(B) CREDIT RISK

The Group manages its exposure to credit risk under policies approved by the Board of Directors. The Group performs credit assessments on all electricity customers and normally requires a bond from commercial customers who have yet to establish a suitable credit history. Customer bonds are held in a separate bank account.

It is the Group's policy to only enter into derivative transactions with banks that it has signed an ISDA master agreement with, and which have a minimum long-term Standard & Poor's (or Moody's equivalent) credit rating of A- or higher.

With respect to energy contracts, the Group has potential credit risk exposure to the counterparty dependent on the current market price relative to contracted price until maturity.

In the event of a failure by a retailer to settle its obligations to the Energy Clearing House, following the exhaustion of its prudential security, a proportionate share of the shortfall will be assumed by all generator class market participants. The Group consequently will be impacted in the event that this occurs.

The carrying amounts of financial assets recognised in the balance sheet best represent the Group's maximum exposure to credit risk at the reporting date without taking account of any collateral held by way of customer bonds.

(C) LIQUIDITY RISK

The Group manages its exposure to liquidity risk under policies approved by the Board of Directors. Policies require that prescribed headroom is available in undrawn and committed facilities to cover unanticipated needs and that a limited amount of facilities mature over the immediate 12 month forward-looking period. The Group's objective is to maintain a balance between continuity of funding and flexibility through the use of various funding sources.

Non-derivative financial liabilities

The following liquidity risk disclosures reflect all contractually fixed payoffs, repayments and interest from recognised non-derivative financial liabilities. The timing of cash flows for non-derivative financial liabilities is based on the contractual terms of the underlying contract. It should be noted that the amounts presented are contractual undiscounted cash flows, consequently the totals will not reconcile with the amounts recognised in the balance sheet.

While the tables below give the impression of a liquidity shortfall, the analysis does not take into account expected future operating cash flows or committed and undrawn debt facilities that will provide additional liquidity support.

June 2016	Less than 6 months $M	6 to 12 months $M	1 to 5 years $M	Later than 5 years $M	Total $M
Liquid financial assets					
Cash and cash equivalents	46	–	–	–	46
Receivables	198	–	–	–	198
	244	–	–	–	244
Financial liabilities					
Payables and accruals	(156)	–	(2)	–	(158)
Loans	(148)	(24)	(710)	(442)	(1,324)
	(304)	(24)	(712)	(442)	(1,482)
Net inflow/(outflow)	(60)	(24)	(712)	(442)	(1,238)

June 2015	Less than 6 months $M	6 to 12 months $M	1 to 5 years $M	Later than 5 years $M	Total $M
Liquid financial assets					
Cash and cash equivalents	32	–	–	–	32
Receivables	189	–	1	–	190
	221	–	1	–	222
Financial liabilities					
Payables and accruals	(159)	–	(2)	–	(161)
Loans	(30)	(29)	(716)	(629)	(1,404)
	(189)	(29)	(718)	(629)	(1,565)
Net inflow/(outflow)	32	(29)	(717)	(629)	(1,343)

Derivative financial liabilities

The table below details the liquidity risk arising from derivative liabilities held by the Group at balance date. Net settled derivatives include interest rate derivatives and electricity price derivatives. Gross settled derivatives relate to foreign exchange derivatives that are used to hedge future purchase commitments. Foreign exchange derivatives are rolled on an instalment basis until the underlying transaction occurs. While the maturity of these derivatives are short-term the underlying expenditure is forecast to occur over different time periods. The tables also summarise the payments that are expected to be made in relation to derivative liabilities. The Group also expects to receive funds relating to derivative asset settlements. The expectation of cash receipts in relation to derivative assets should also be considered when assessing the ability of the Group to meet its obligations.

June 2016	Less than 6 months $M	6 to 12 months $M	1 to 5 years $M	Later than 5 years $M	Total $M
Derivative liabilities – net settled	(37)	(29)	(130)	(127)	(323)
Derivative liabilities – gross settled					
Inflows	49	–	–	–	49
Outflows	(53)	–	–	–	(53)
Net maturity	(41)	(29)	(130)	(127)	(327)

June 2015	Less than 6 months $M	6 to 12 months $M	1 to 5 years $M	Later than 5 years	Total $M
Derivative liabilities – net settled	(29)	(28)	(120)	(85)	(262)
Derivative liabilities – gross settled					
Inflows	37	–	–	–	37
Outflows	(34)	–	–	–	(34)
Net maturity	(26)	(28)	(120)	(85)	(259)

NOTE 14. FINANCIAL RISK MANAGEMENT (CONTINUED)

(D) FAIR VALUE ESTIMATION

Fair values

The carrying amount of financial assets and liabilities recorded in the financial statements approximates their fair values except for: (i) the Fixed Rate Bonds, the Floating Rate Bonds and the US Private Placement, the fair values for which have been calculated at $216 million (2015: $215 million), $339 million (2015: $339 million) and $306 million (2015: $312 million) respectively; and (ii) the Capital Bonds, the fair value for which has been calculated at $321 million (2015: $324 million). Fair values are based on quoted market prices and inputs for each bond issue.

Valuation techniques

The Group uses various methods in estimating the fair value of a financial instrument. The methods comprise:

- Level 1 – the fair value is calculated using quoted prices in active markets;
- Level 2 – the fair value is estimated using inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (as prices) or indirectly (derived from prices); and
- Level 3 – the fair value is estimated using inputs that are not based on observable market data.

As at 30 June 2016 all of the Group's financial instruments carried at fair value were categorised as level 2, except for electricity price derivatives. Electricity price derivative assets of $8 million were categorised as level 1 (2015: $15 million) and $77 million were categorised as level 3 (2015: $84 million). Electricity price derivative liabilities of $2 million were categorised as level 1 (2015: $4 million) and $89 million were categorised as level 3 (2015: $84 million).

Financial instruments that are measured using a valuation technique with only observable market inputs, or unobservable inputs that are not significant to the overall valuation, include interest rate derivatives and foreign exchange derivatives not traded on a recognised exchange.

Financial instruments that use a valuation technique which includes non-market observable data include non-exchange traded electricity contracts which are valued using a discounted cash flow methodology using a combination of ASX market prices for the first three years, combined with Management's internal view of forward prices for the remainder of the contract's term. Management's internal view of forward prices incorporates a minimum price of $66/MWh and a maximum price of $102/MWh (2015: minimum price of $63/MWh and a maximum price of $97/MWh) over the period in question (in real terms) and is determined by a demand supply based fundamental model which takes account of current hydrological conditions, future inflows, an assessment of thermal fuel costs, anticipated demand and supply conditions and future committed generation capacity.

Where the fair value of a derivative is calculated as the present value of the estimated future cash flows of the instrument there are two key inputs being used: the forward price curve and the discount rate. Where the derivative is an option, then the volatility of the forward price is another key input. The selection of inputs requires significant judgement, and therefore there is a range of reasonably possible assumptions in respect of these inputs that could be used in estimating the fair values of these derivatives. Maximum use is made of observable market data when selecting inputs and developing assumptions for the valuation technique.

Level 3 sensitivity analysis

The following summarises the potential impact of increases or decreases in price risk exposures of the Group on post-tax profit. Sensitivity analysis is based on an assessment of the reasonably possible movements in forward price.

	Impact on post tax profit	
	2016 $M	2015 $M
Group		
Electricity forward price increased by 10%	(2)	7
Electricity forward price decreased by 10%	2	(7)

Reconciliation of level 3 fair value movements

	2016 $M	2015 $M
Opening balance	–	53
New contracts	2	(1)
Matured contracts	(1)	(15)
Gains and losses		
Through the income statement	(3)	(4)
Through other comprehensive income	(10)	(33)
Closing balance	(12)	–

Level 3 fair value movements recognised within the income statement of the Group are recognised within 'change in the fair value of financial instruments'.

Deferred 'inception' gains/(losses)

There is a presumption that when derivative contracts are entered into on an arm's length basis, fair value at inception would be zero. The contract price of non exchange traded electricity derivative contracts are agreed on a bilateral basis, the pricing for which may differ from the prevailing derived market price curve for a variety of reasons. In these circumstances an inception adjustment is made to bring the initial fair value of the contract to zero at inception. This inception adjustment is amortised over the life of the contract by adjusting the future price path used to determine the fair value of the derivatives by a constant amount to return the initial fair value to zero.

The table below details the movements in inception value gains/(losses) included in the fair value of derivative financial assets and liabilities as at 30 June.

Electricity price derivatives	2016 $M	2015 $M
Opening deferred inception gains	15	18
Deferred inception gains on new hedges	(21)	–
Deferred inception (losses)/gains realised during the year	(8)	(3)
Closing inception gains	(14)	15

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2016

NOTE 14. FINANCIAL RISK MANAGEMENT (CONTINUED)

(E) CAPITAL RISK MANAGEMENT

Management seeks to maintain a sustainable financial structure for the Group having regard to the risks from predicted short and medium-term economic, market and hydrological conditions along with estimated financial performance. Capital is managed to provide sufficient funds to undertake required asset reinvestment as well as to finance new generation development projects and other growth opportunities to increase shareholder value at a rate similar to comparable private sector companies.

In order to maintain or adjust the capital structure, changes may be made to the amount paid as dividends to shareholders, capital may be returned or injected or assets sold to reduce borrowings.

Consistent with other companies in the industry, the Group monitors capital on the basis of its gearing ratio. This ratio is calculated as net debt divided by total capital. Net debt is calculated as total borrowings (both current and non-current) less cash and cash equivalents. Total capital is calculated as shareholders' equity plus net debt. The gearing ratio is calculated below:

	2016 $M	2015 $M
Borrowings at carrying value	1,177	1,177
Fair value adjustments US Private Placement	(63)	(63)
Less cash and cash equivalents	(46)	(32)
Net debt	1,068	1,082
Total equity	3,315	3,337
Total capital	4,383	4,419
Gearing ratio	24.4%	24.5%

Under the negative pledge deed in favour of its bank financiers the Group must, in addition to not exceeding its maximum gearing ratio, exceed minimum interest cover ratios and a minimum shareholder equity threshold.

The Group seeks to maintain a debt to EBITDAF ratio of less than 2.8 times to maintain credit metrics sufficient to support its credit rating on an on-going basis. For the purpose of calculating this ratio and consistent with the rating agency treatment, the calculation of debt is deemed to be all senior debt and 50% of subordinated debt. For the year ended 30 June 2016, the Group had a debt to EBITDAF ratio of 2.0 times (2015: 2.0 times).

NOTE 15. DERIVATIVE FINANCIAL INSTRUMENTS

The fair values of derivative financial instruments together with the designation of their hedging relationship are summarised below, based on maturity date:

	2016 $M	2015 $M
CURRENT ASSETS		
Interest rate derivative	9	9
Electricity price derivative	12	21
Foreign exchange derivative	–	4
Cross currency interest rate derivative	–	1
	21	35
CURRENT LIABILITIES		
Interest rate derivative	9	10
Electricity price derivative	8	4
Foreign exchange derivative	4	–
	21	14
NON-CURRENT ASSETS		
Interest rate derivative	43	34
Electricity price derivative	74	78
Cross currency interest rate derivative	45	45
	162	157
NON-CURRENT LIABILITIES		
Interest rate derivative	179	155
Cross currency interest rate derivative – margin	5	4
Electricity price derivative	83	84
	267	243

The majority of interest rate derivatives, short-term low value foreign exchange derivatives, and short-term low value exchange traded energy contracts, while economic hedges, are not designated as hedges under NZ IAS 39 but are treated as at fair value through profit and loss. All other interest rate derivatives (predominantly forward starting derivatives), foreign exchange and electricity prices derivatives (except those described below) are designated as cash flow hedges under NZ IAS 39.

Cross currency interest rate swaps, which are used to manage the combined interest and foreign currency risk on borrowings issued in foreign currency, have been split into two components for the purpose of hedge designation. The hedge of the benchmark interest rate is designated as a fair value hedge and the hedge of the issuance margin is designated as a cash flow hedge.

Electricity contracts not designated as hedges for accounting purposes

The Tuaropaki Power Company Foundation Hedge contract was originated in 1997 between the Tuaropaki Power Company (seller) and ECNZ (buyer). The contract was subsequently novated to Mercury NZ Limited. The contract settles on a moving hedge index rather than wholesale electricity prices.

Basis swaps: The company has entered into a number of contracts to hedge wholesale electricity price risk between the North and South Island generically called basis swaps. The most significant is a virtual asset swap with Meridian Energy which has a remaining life of 9 years.

Swaption: The company has entered into a swaption to provide optionality around hedging its exposure to wholesale electricity spot price exposure during pre-defined periods. If exercised, the company will receive a swap (contract-for-difference) for the period exercised. This swap will be designated as a hedge for accounting purposes.

The company has entered into an outage cover contract with Nga Awa Purua Joint Venture on commercial terms to support the Joint Venture's revenue in the event of a forced station outage, for which the company receives an annual premium.

During the year the company entered into a contract-for-difference with Meridian Energy that is contingent on the continued operation of New Zealand Aluminium Smelters at Tiwai Point. The contract matures in 2030.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2016

NOTE 15. DERIVATIVE FINANCIAL INSTRUMENTS (CONTINUED)

The changes in fair values of derivative financial instruments recognised in the income statement and other comprehensive income are summarised below:

	Income statement		Other comprehensive income	
	2016 $M	2015 $M	2016 $M	2015 $M
Cross currency interest rate derivatives	–	69	–	–
Borrowings – fair value change	–	(72)	–	–
	–	(3)	–	–
Interest rate derivatives	24	4	(39)	(14)
Cross currency interest rate derivatives – margin	–	–	(1)	8
Electricity price derivatives	(4)	8	(10)	(37)
Foreign exchange rate derivatives	–	–	(4)	3
Ineffectiveness of cash flow hedges recognised in the income statement	–	(1)	–	–
Total change in fair value of financial instruments	20	8	(54)	(40)

Movement in cash flow hedge reserve	2016 $M	2015 $M
Opening balance	(37)	(7)
The effective portion of cash flow hedges recognised in the reserve	(54)	(40)
Amortisation of fair values[1]	(1)	(1)
The amount transferred to balance sheet	1	1
Equity accounted share of associates' movement in other comprehensive income	(1)	(1)
Tax effect of movements	16	11
Closing balance	(76)	(37)

1 Amounts reclassified to the income statement recognised in amortisation.

NOTE 16. RECONCILIATION OF PROFIT FOR THE YEAR TO NET CASH FLOWS FROM OPERATING ACTIVITIES

	2016 $M	2015 $M
Profit for the year	160	47
Items classified as investing or financing activities		
• Foreign exchange movements	–	(2)
• Net interest accrual	–	4
Adjustments for:		
Depreciation and amortisation	182	170
Net loss on sale of property, plant and equipment	2	1
Change in the fair value of financial instruments	(20)	(8)
Impaired assets	19	130
Income attributable to land and associated real property held-for-sale	(13)	(15)
Movement in effect of discounting on long-term provisions	2	2
Share of earnings of associate and joint venture companies	(3)	(3)
Other non-cash items	1	–
Net cash provided by operating activities before change in assets and liabilities	330	326
Change in assets and liabilities during the year:		
• (Increase)/decrease in trade receivables and prepayments	(9)	28
• Increase in consumable inventories	(9)	(6)
• Decrease in trade payables and accruals	(3)	(9)
• Decrease in provision for tax	(18)	(10)
• Decrease in deferred tax	(11)	(20)
Net cash inflow from operating activities	280	309

NOTE 17. RELATED PARTY TRANSACTIONS

Majority shareholder

The majority shareholder of Mercury NZ Limited is the Crown, providing it with significant potential influence over the Group. All transactions with the Crown and other entities wholly or partly owned by the Crown are on normal commercial terms. Transactions cover a variety of services including trading energy, postal, travel and tax.

Transactions with related parties

Mercury NZ Limited has investments in subsidiaries, associates and joint arrangements, all of which are considered related parties.

As these are consolidated financial statements, transactions between related parties within the Group have been eliminated. Consequently, only those transactions between entities which have some owners external to the Group have been reported below:

	Transaction value	
	2016 $M	2015 $M
Associates		
Management fees and service agreements received	4	4
Energy contract settlements received	2	5
Joint operations		
Management fees and service agreements received	5	5
Energy contract settlements paid	(7)	(2)
Interest income	1	2

Energy contracts, management and other services are made on normal commercial terms.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2016

NOTE 17. RELATED PARTY TRANSACTIONS (CONTINUED)

An advance to TPC Holdings Limited of $4 million (2015: $4 million) is interest free and repayable on demand subject to certain conditions being met.

The long-term advance to our Rotokawa Joint Venture partner carries a floating interest rate. Repayments under the advance are linked to the level of receipts under the geothermal energy supply agreement. There is no fixed repayment date, the agreement will terminate on receipt of any outstanding balances.

The advance to Energy Source LLC of $1 million (2015: $1 million) at an interest rate of 10% per annum on the outstanding balance is repayable by 31 December 2016.

No related party debts have been written off, forgiven, or any impairment charge booked.

	Transaction value	
	2016 $000	2015 $000
Key management personnel compensation (paid and payable) comprised:		
Directors' fees	871	839
Benefits for the Chief Executive and Senior Management:		
Salary and other short-term benefits	5,302	5,043
Termination benefits:	259	130
Share-based payments	324	468
	6,756	6,480

Other transactions with key management personnel

Key management personnel are those people with responsibility and authority for planning, directing and controlling the activities of the entity. Key management personnel for the Group are considered to be the Directors and Senior Management.

Directors and employees of the Group deal with Mercury NZ Limited as electricity consumers on normal terms and conditions, with staff discounts for employees, within the ordinary course of trading activities. A number of key management personnel also provide directorship services to other third party entities. A number of these entities transacted with the Group, in all circumstances on normal commercial terms during the reporting period.

A number of key management personnel provide directorship services to direct subsidiaries and other third party entities as part of their employment without receiving any additional remuneration. Again, a number of these entities transacted with the Group, in all circumstances on normal commercial terms in the reporting period.

The Group purchases directors and officers insurance for the benefit of key management personnel in relation to the services they provide to the Group.

NOTE 18. COMMITMENTS AND CONTINGENCIES

	Capital		Operating lease		Other operating commitments	
Commitments	2016 $M	2015 $M	2016 $M	2015 $M	2016 $M	2015 $M
Within one year	39	30	6	6	6	6
One to five years	72	54	27	16	12	9
Later than five years	36	48	80	12	74	76
	147	132	113	34	92	91

Capital commitments include both commitments to purchase property, plant and equipment as well as intangible commitments. Intangible commitments include commitments to purchase emissions units. In the event the New Zealand emissions trading scheme (NZ ETS) is ever terminated, the forward purchase agreements for the acquisition of emissions units which cover a 13 year period, will also terminate.

Operating leases are of a rental nature and are on normal commercial terms and conditions. The majority of the lease commitments are for building accommodation, the leases for which have remaining terms of between 1 and 15 years and include an allowance for either annual, biennial or triennial reviews. The remainder of the operating leases relate to vehicles, plant and equipment.

Contingencies

The company holds land and has interests in fresh water and geothermal resources that are subject to claims that have been brought against the Crown. On 29 August 2014, the Supreme Court gave its decision in Paki v Attorney-General and dismissed the claimants' action seeking a declaration that the Crown holds those parts of the bed of the Waikato River which adjoin former Pouakani land on trust for the Pouakani people on the basis it was incorrectly advanced. The Supreme Court decision has left open the possibility of further litigation in respect of ownership of that land currently held by the company. The company has received advice that it may proceed with a high degree of confidence that future decisions on the matter will not impair the company's ability to operate its hydro assets. A separate claim by the New Zealand Maori Council relating to fresh water and geothermal resources was lodged in 2012 with the Waitangi Tribunal. The Tribunal concluded that Maori have residual (but as yet undefined) proprietary rights in fresh water and geothermal resources and it will be for the Crown to determine how any such rights and interests may best be addressed. The impact of this claim on the company's operations is unknown at this time.

From time to time the company will issue letters of credit and guarantees to various suppliers in the normal course of business. However, there is no expectation that any outflow of resource relating to these letters of credit or guarantees will be required as a consequence.

The Group has no other material contingent assets or liabilities.

NOTE 19. SHARE-BASED PAYMENTS

Long-term incentive plan

The Group operates an equity-settled share based long-term incentive (LTI) plan for senior executives. The plan is designed to enhance the alignment between shareholders and those executives most able to influence the performance of the company. Under the plan the senior executives purchase shares at market value funded by an interest free loan from the company, with the shares held on trust by the Trustee of the LTI plan until the end of the vesting period. Vesting of shares is dependent on continued employment through the vesting period and the company's relative total shareholder return. If the shares vest, executives are entitled to a cash amount which, after deduction for tax, is equal to the initial loan balance for the shares which have vested. That cash amount must be applied towards repayment of their loan balance and the corresponding shares are released by the trustee to the individual. The vesting periods for the plan are June 2016, June 2017 and June 2018. Under the plan, a relative total shareholder return measure is used. Performance is measured against a combination of: i) other electricity generators who were listed on the NZX; and (ii) all NZX50 companies, both as at the start of the vesting period.

The LTI plan represents the grant of in-substance nil-price options to executives. During the year the company expensed $324,251 in relation to equity-settled share based payment transactions (2015: $468,432).

Movements in the number of share options are as follows:

	2016	2015
Balance at the beginning of the year	567,363	559,161
Options granted	243,980	225,663
Options expired	(76,074)	(26,696)
Options exercised	(241,357)	(190,765)
Balance at the end of the year	493,912	567,363

111,220 options were exercisable at the end of the year (2015: 203,680) with the remaining options under the plan having a weighted average life of 1.5 years (2015: 1.6 years).

Employee Share Purchase Programme

The Group operated an employee share purchase programme which matured in May 2016. The scheme has not been rolled over.

NOTE 20. SUBSEQUENT EVENTS

The Board of Directors has approved a fully imputed final dividend of 8.6 cents per share and an unimputed special dividend of 4.0 cents per share, both to be paid on 30 September 2016.

There are no other material events subsequent to balance date that would affect the fair presentation of these financial statements.

GOVERNANCE AT MERCURY

At Mercury we have a genuine focus on the long term. This drives the way we do business, our investment decisions, services to customers, development of people and our partnerships with stakeholders.

Our corporate governance framework sets out how our Board is accountable to our owners for Mercury's actions and performance, along with the delegation of responsibilities to the Chief Executive and the Executive Management Team ("EMT"). Through this framework we create the objectives and direction for the business, identify and manage our risks, strengthen our business culture and assess and continuously improve our performance.

We are committed to maintaining the highest standards of business behaviour and accountability and regularly review Mercury's governance framework against national and international guidelines to ensure consistency with best practice. Accordingly, the Board adopts corporate governance policies and practices reflecting contemporary standards in New Zealand and Australia, incorporating best practice recommendations issued by NZX Limited ("NZX") and ASX Limited ("ASX").

Mercury's corporate governance practices comply with the NZX Corporate Governance Best Practice Code, the ASX Corporate Governance Principles and Recommendations (third edition) ("ASX Principles") and the Financial Markets Authority Corporate Governance Principles and Guidelines. We have also reviewed guidelines from the New Zealand Corporate Governance Forum, the International Corporate Governance forum, and the OECD and consider that our practices and procedures substantially reflect these guidelines.

In this section, we give an overview of our engagement with investors, our Board, how we manage risks, our commitment to act ethically and responsibly and our approach to diversity and inclusion. Our full Corporate Governance Statement is available in the corporate governance section of our website at www.mercury.co.nz.

Engaging with Investors

Mercury is committed to communicating effectively and providing comprehensive information to investors and other stakeholders to ensure they have enough information to make informed assessments of Mercury's value and prospects.

Our Head of Investor Relations runs a programme to build understanding and appropriate measurement of Mercury's performance among investors and research analysts. The programme is founded on:

- being responsive;
- providing clear, accurate and timely disclosures;
- providing appropriate access to management and directors; and
- providing meaningful insight into the company and industry.

Mercury believes effective engagement with investors will benefit both Mercury and investors. As a result of investor feedback, Mercury's aim over the next financial year and beyond is to provide clearer communication of our strategic direction, including articulating Mercury's strategic priorities and how these leverage Mercury's competitive advantages.

In FY2016 Mercury has continued a number of initiatives to improve communication with investors and other stakeholders:

- **Website**: The *Investors* section of our website contains a comprehensive set of investor-related information and data. Shareholders can direct questions and comments through the website or contact the Head of Investor Relations.
- **Webcasting our Annual Shareholders' Meeting**: Our ASM is webcast to allow participation by shareholders who are unable to attend the meeting in person.
- **Annual and interim reports**: Our periodic reporting provides an excellent opportunity to communicate with our investors.
- **Regular newsletter**: Our regular newsletters have proved a very popular way to update investors on business and community related activities.
- **Regular information disclosures**: We continue to disclose important information fully and transparently on the NZX and ASX announcement platforms.
- **Analyst and investor briefings and road shows**: We held a number of these in FY2016, including international roadshows in June. These roadshows are an effective way of communicating with institutional investors.
- **Electronic communications**: We encourage shareholders to provide email addresses to enable them to receive shareholder materials electronically. Communicating electronically is faster and more cost-effective. Almost 75% of our shareholders have told us they prefer to communicate in this way. We understand that this does not suit everybody and so hard copy reports are provided on request to shareholders who have not opted to receive documents electronically.

We have engaged with investors at a number of levels in FY2016. Highlights included announcing in early May 2016 our change of name to Mercury NZ Limited, our open day for investors and stakeholders at our Ngatamariki geothermal power station in October 2015 and the purchase of proven capability and technical expertise in solar power with our solar business, *What Power Crisis*, in March 2016.

Mercury's Board

Composition

The Board currently comprises eight directors, Joan Withers (the Chair), Mike Allen, Prue Flacks, Andy Lark, James Miller, Keith Smith, Patrick Strange and Mike Taitoko. Each of the directors is non-executive and independent. Details of each director are available in the Board of Directors section of this annual report and the *Leadership* section of Mercury's website.

The Board supports the Institute of Directors' Future Directors Programme which offers candidates valuable experience sitting at the Board table of a New Zealand company for 12 or more months. The programme is designed to increase the pipeline of Board-ready younger directors through giving them exposure to real-life governance in action along with valuable mentorship. Our second future director, Nicky Ashton, was selected in June 2016 and has taken the role for the period 1 July 2016 to 31 December 2017. Nicky participates in discussions in all Board meetings but does not participate in decision making.

The Board is structured to ensure that, as a collective group, it has the skills, experience, knowledge, diversity and perspective to fulfil its purpose and responsibilities. The responsibilities of the Board are set out in Mercury's Board Charter, which is reviewed by the Board as required and at least every two years, and is available in the corporate governance section of our website.

The Board has three standing Committees: the Risk Assurance and Audit Committee ("RAAC"), the Human Resources Committee and the Nominations Committee. Each committee focuses on specific areas of governance and together they strengthen the Board's oversight of Mercury. The current members of the committees are as follows:

Committee	Members
Risk Assurance and Audit Committee	Keith Smith (Chair), James Miller and Patrick Strange. Joan Withers is also a member by virtue of her position as Board Chair.
Human Resources Committee	Prue Flacks (Chair), Mike Allen, Andrew Lark and Mike Taitoko. Joan Withers is also a member by virtue of her position as Board Chair.
Nominations Committee	Joan Withers (Chair), Prue Flacks and James Miller.

Each committee operates in accordance with a written Charter approved by the Board and reviewed as required and at least every two years. The Committee Charters are available in the corporate governance section of our website.

Skills and Reviewing Performance

The Nominations Committee has developed a Board skills matrix setting out the mix of skills and diversity of the Board. The skills matrix is used to identify any "gaps" in the skills and experience of the directors required on the Board both currently and into the future. Attributes are weighted to indicate their relative importance. This matrix is completed by directors regularly and reviewed by the Nominations Committee. If any "gaps" are identified from this review, an expert consultant is engaged to assist in identifying and assessing potential director candidates. The most recent Board skills matrix is set out in Mercury's Corporate Governance Statement.

Evaluations are regularly conducted to review the Board's role, Board processes and committees to support that role and the performance of the Board and each director. This is undertaken using a variety of techniques including external consultants, questionnaires and Board discussion. As at 30 June 2016, the Board was part way through its current full performance review and analysis of Board skills and tenure. The last full Board performance review, with the assistance of an external facilitator, was completed in February 2015. The Board also completed a comprehensive analysis of the skills and tenure of the Board at that time.

Managing Risk and Assurance

Risk management is an integral part of Mercury's business. Mercury has in place an overarching Risk Management Policy (available in the corporate governance section of Mercury's website) supported by a suite of risk management policies appropriate for its business which together form our Risk Management framework.

The purpose of the Risk Management Policy is to embed within Mercury a comprehensive, holistic, Group-wide capability in risk management which provides a consistent method of identifying, assessing, controlling, monitoring and reporting existing and potential risks to Mercury's business and to enable the achievement of its plans and objectives. The Policy sets out the risk management objectives and requirements of Mercury within which management is expected to operate. The Policy is reviewed periodically by the RAAC.

The Risk Management framework supports a comprehensive approach to risk, encompassing financial, strategic, environmental, operational, regulatory, social and governance risks, from internal and external sources. We work hard to improve the way we incorporate environmental, social and governance risk considerations into our Risk Management framework, policies and processes. We are also striving to further embed these considerations in our operations. This drive is underpinned by our Corporate Responsibility Policy (available in the corporate governance section of our website) which sets out the core principles and values that promote ethical and responsible decision making.

GOVERNANCE AT MERCURY (CONTINUED)

Mercury has a Risk Assurance Officer who has the authority to determine the effectiveness of risk management, assurance and audit. The Risk Assurance Officer has a dual reporting line to the Chief Executive and the RAAC Chair. The RAAC tasks the Risk Assurance Officer to ensure healthy and robust debate and interaction between management and risk assurance and audit providers.

Mercury's management operates a Risk Management Committee whose mandate is to promote risk awareness and appropriate risk management to all employees and to monitor and review risk activities as circumstances and our strategic and operational objectives evolve. Membership of the Risk Management Committee is made up of representatives from the EMT and is chaired by the Chief Executive. The Risk Management Committee meets at least four times each year.

Mercury accepts some commercial risks in order to achieve its strategic objectives and to deliver enhanced shareholder value. These are set out in more detail in Mercury's Corporate Governance Statement, available in the corporate governance section of our website.

In the event of a severe natural catastrophe, uninsured damages or uninsurable damages to Mercury's assets may not be fully recovered under the current insurance arrangements, impacting future operational performance and the financial condition of Mercury. Mercury is insured through a comprehensive programme including cover for generation property, plant and equipment and business interruption with a combined limit of $1,000,000,000.

The RAAC is responsible for overseeing, reviewing and providing advice to the Board on Mercury's risk management policies and processes. The Risk Assurance Officer reports regularly to the RAAC on the effectiveness of Mercury's management of material business risks. In addition, the RAAC annually reviews the risk management framework. A review of the risk management framework took place in FY2016.

The Auditor–General is the auditor of Mercury and each of its subsidiaries (together, the "Group"), under the Public Audit Act 2001. The Auditor–General appointed Simon O'Connor of Ernst & Young to carry out the FY2016 audit on her behalf. The NZX Main Board Listing Rules require rotation of the lead audit partner at least every five years. The provision of external audit services is guided by the Audit Independence Policy which is available on our website. Consistent with the Stakeholder Communications Policy, the external auditor attends the Annual Shareholders' Meeting and is available to shareholders to answer questions relevant to the audit.

Acting Ethically and Responsibly

Our purpose is to inspire New Zealanders to enjoy energy in more wonderful ways. Our Mercury Attitude, together with our Code of Ethics, Corporate Responsibility Policy and governance framework, set out the standards of business culture and behaviour as we deliver our corporate strategy and achieve our purpose.

OUR PURPOSE IS TO INSPIRE NEW ZEALANDERS TO ENJOY ENERGY IN MORE WONDERFUL WAYS.

Our Attitude

A Mercury employee is expected to apply three powerful elements that together form our attitude. These shape our decisions, our actions and our interactions with each other. Our Mercury Attitude aligns with our direction to achieve our purpose:

- Commit and Own it;
- Share and Connect; and
- Be Curious and Original.

Our Code of Ethics and policy framework

Our Code of Ethics requires all Mercury people, including directors, officers, employees and contractors to act honestly and in accordance with the highest standards of integrity and fairness at all times, and to strive to foster those standards within Mercury. The Code of Ethics is available in the corporate governance section of our website. The Code of Ethics and associated policy framework underpin our ethical and behavioural standards. They support our promises to each other and define our commitment to our customers, our investors and the communities in which we operate.

Our policy framework addresses behaviours in the following key areas:

Our People and Communities

- **Health and Safety**: This is our top priority. Our Health and Safety Framework is underpinned by the concept of *Together, Safe*. Everyone at Mercury is involved in reporting hazards and near misses using an online tool and phone app for easy access and timely reporting.
- **Wellbeing**: We practise wellbeing in its broadest sense. We reimburse Mercury employees for a free annual health check, offer free influenza vaccinations and subsidised health, income protection, life and travel insurance. Our online wellness programme, *Tracksuit Inc.* helps our people to manage and improve their fitness and wellbeing. We also provide a company-wide *My Days* programme, under which every Mercury employee is given five days a year, in addition to annual leave, to spend time with their communities, their families or simply on a bit of "me time".
- **Community support**: In order to support Mercury's many communities and more closely connect our people with those communities, we have set up the *Employee Community Fund*, an annual fund of $100,000 to benefit and support our communities. Any Mercury person can apply for some help for a community group or organisation they are involved with.

The Employee Community Fund has been shared with a range of community groups reflecting the diversity of our Mercury team: schools, sports clubs, groups supporting families and people with unique healthcare needs. Mercury has supported the Starship Children's Hospital and the *Starship Foundation* for over 15 years. We launched the Star Supporters Club in 2004 and we now have more than 30,000 members who have donated over $8.8 million over that time.

- **Discrimination**: Our workplace does not tolerate any form of discrimination or harassment. Our Corporate Responsibility Policy puts it simply: *We value workforce diversity and treat our employees with respect and consideration, maintaining a work environment free from any form of discrimination or harassment*.

Our Customers

- **Privacy**: We are committed through our Privacy Framework to the protection of personal information relating to our people and our customers.
- **Wellbeing**: As providers of an essential service, Mercury takes the health, safety and wellbeing of its customers very seriously, in particular those who are vulnerable and/or medically dependent. This extends beyond legislative compliance. During the Transpower Penrose (Auckland) outage in late 2014, a Mercury team urgently telephoned every one of our registered vulnerable and/or medically dependent customers to check that they were safe. Those that didn't answer their telephones were visited at their home by a member of the Mercury team.
- **Energy management and conservation**: Mercury has developed the *Good Energy Monitor* ("GEM"), an online tool that allows customers to know how much energy they are using and how much it is costing them. GEM allows customers to set an energy savings goal, track progress over time and gives tips on how to save. Mercury also developed *GLOBUG*, New Zealand's leading prepay power service.
- **Energy freedom and advancing technologies**: Mercury is committed to being customer-led. Mercury has promoted the benefits of electric vehicles for over two years as a way to enjoy New Zealand's home-grown, renewable energy. Mercury has committed to convert 70% of its own vehicle fleet to electric vehicles by 2018. Electric transport is New Zealand's largest green-growth opportunity and delivers benefits to the consumer, economy, healthcare, emissions, provincial employment and the balance of payments. Mercury has also invested in the purchase of proven capability and technical expertise in solar power. In March 2016, Mercury purchased its solar business, *What Power Crisis*.

Our Governance and Responsible Business Practices

- **Conflicts**: Conflicts of interest must be avoided. Mercury people are encouraged to discuss possible conflicts with their manager. Mercury takes practical, preventative action wherever possible, for example by substituting project managers in circumstances of possible conflict with contractors and suppliers. All potential conflicts of interest are declared prior to appointment and at each Board meeting, including in relation to specific agenda items if applicable.
- **Bribery**: The acceptance of bribes, including gifts or personal benefits of material value which could reasonably be perceived as influencing decisions, is prohibited under Mercury's Code of Ethics. Under Mercury's Delegations Policy, donations to political parties are prohibited.
- **Use of Mercury Assets**: The Code of Ethics places restrictions on the use of corporate information, assets and property. All persons covered by the Code of Ethics are encouraged to report any breach or suspected breach of the Code.
- **Whistleblowing**: We provide a framework for the protection of employees wishing to disclose serious wrongdoing. This is described in Mercury's *Employee Rights under the Protected Disclosures Act* statement, which was most recently reinforced to employees in July 2016. The framework is overseen by the RAAC.
- **Trading In Company Securities**: Mercury's *Trading in Company Securities Policy* sets out the rules and restrictions relating to trading in Mercury securities, including the prohibition on insider trading.
- **Market Disclosures**: Our *Market Disclosure Policy* ensures we maintain a fully informed market through communication with the markets, investors and stakeholders and by giving them equal and timely access to material information.
- **Corporate Responsibility**: Our *Corporate Responsibility Policy* sets out the core principles and values that promote ethical and responsible decision making.

Diversity and Inclusion

Diversity and inclusion is an integral part of Mercury's culture. We believe that having a team of individuals with different backgrounds, views, experience and capability working together makes us stronger and better as an organisation. Being reflective of the customers and communities we serve helps us connect more effectively with them, providing products and services that enhance their lives. We recognise the importance of being a good corporate citizen that complies with legislation, challenges inappropriate behaviours and promotes diversity through supply chains and community activities.

Mercury's progressive approach to diversity focuses on gender, age, ethnicity, inclusion and flexibility. Activity is aligned to the following principles:

- increasing the diversity of our workforce at senior levels;
- creating a flexible and inclusive work environment that values difference and enhances business outcomes;
- harnessing diversity of thought and capitalising on individual differences;
- leadership behaviours that reflect our belief in the value of diversity and inclusion; and
- attracting and retaining a talented workforce through increasing the diversity of the candidate pool and maintaining a recruitment strategy that is attractive to all candidates.

Our commitment to diversity and inclusion starts with our Diversity Policy and framework. Our Policy is available in the corporate governance section of our website.

Measureable objectives to achieve gender diversity were established in 2014 to drive our progress towards the challenge set by the Board to increase representation of women at all levels.

Over the last three years, Velocity, our talent development programme, has continuously increased the number of female participants. We have reviewed our recruitment and selection processes to challenge potential bias in panels and decisions. In addition, the Board participates in the Future Directors programme, appointing women Future Directors in 2015 and 2016 and Mercury is a signatory to the UN Women's Empowerment Principles. Progress towards meeting the measurable objectives is outlined in Mercury's Corporate Governance Statement available on our website.

At balance date, the proportion of women on the EMT (including the Chief Executive) was 22%, or two out of nine (as at 30 June 2015 this was 25% or two out of eight). The proportion of women on the Board at balance date was 25% or two out of eight, including the Chair (as at 30 June 2015 this was 37.5% or three out of eight).

Mercury invests in leveraging and building capability. This includes supporting all ages and life stages, leveraging the unique knowledge and experience we already have and developing new capability aligned to future direction.

In 2016, we launched a company-wide foundation management programme, StepUP, with a focus on strengthening our people managers' capability to develop and grow their teams. Unconscious bias training is the next targeted programme for our leaders.

Part of creating a culture of inclusiveness is to ensure everyone is valued and has a voice. This year our people nominated their peers to be part of a network of change supporters who created opportunities for authentic workforce participation in changes impacting our business.

In 2016, we introduced paid partner parental leave encouraging partners to spend time with their family after the arrival of a newborn.

Our annual Workplace Engagement Survey gives our people the opportunity to tell us how we are progressing. The responses from 2016 confirm that our commitment to diversity and inclusion is having an impact. More detail is included in Mercury's Corporate Governance Statement.

As part of the Survey we committed to collecting data to understand the ethnic mix of our people. We recognise that while our workforce is diverse, that diversity is not reflected to the same degree in leadership roles. This baseline data provides a starting point for us to measure our progress against. This data is set out in more detail in Mercury's Corporate Governance Statement.

Mercury acknowledges the important place Maori have as tangata whenua. The 2016 employee engagement survey confirmed Maori employees were the highest engaged ethnic group in Mercury.

The average age of our employees is 40 years, against the national average of 42 (Statistics NZ National Labour Force Projections updated August 2012).

For this reporting period, the Board believes Mercury has made good progress towards achieving its diversity and inclusiveness objectives and against its Diversity Policy generally.

DIRECTOR AND EXECUTIVE EMPLOYEE REMUNERATION

Mercury's Board is committed to a remuneration framework that promotes a high performance culture and aligns executive reward to the development and achievement of strategies and business objectives to create sustainable value for shareholders.

The Board is assisted in delivering its responsibilities and objectives with respect to Mercury's people by the Human Resources Committee. The role and membership of the Committee is set out in the Governance at Mercury section of this report.

The Human Resources Committee ensures rewards for executives are strongly aligned to the performance of the company. The Board is committed to demonstrating transparency in its remuneration policy and practice.

Overall remuneration philosophy

Mercury's remuneration approach aims to attract, retain and motivate high calibre employees at all levels of the organisation. It is based on a practical set of guiding principles that provide for consistency, fairness and transparency. This strategy promotes behaviours and values that drive performance, a strong customer focus and growth in sustainable shareholder value.

Executive remuneration

Mercury's remuneration policy for the Executive Management Team (EMT) provides the opportunity for them to receive, where performance merits, a total remuneration package in the upper quartile for equivalent market-matched roles.

The Human Resources Committee reviews the annual performance appraisal outcomes for all members of the EMT and approves the outcomes for all EMT members other than the Chief Executive. The Chief Executive's remuneration is approved by the Board on the recommendation of the Human Resources Committee. The review takes into account external benchmarking to ensure competitiveness with comparable market peers, along with consideration of an individual's performance, skills, expertise and experience. External benchmarking is commissioned by the Human Resources Committee from an independent party.

Total remuneration is made up of three components: fixed remuneration, short-term performance incentives and long-term performance incentives. Short and long-term performance incentives are deemed 'at-risk' because the outcome is determined by performance against a combination of pre-determined financial and non-financial objectives.

Fixed remuneration

Fixed remuneration consists of base salary and benefits. Mercury's policy is to pay fixed remuneration with reference to the fixed pay market median.

Short term performance incentives

Short term performance incentives (STIs) are at-risk payments designed to motivate and reward for performance typically in that financial year.

The target value of an STI payment is set annually, usually as a percentage of the executive's base salary. For FY2016 the relevant percentages were 25% to 35%.

A proportion (80% for the Chief Executive, 50% for other EMT members) of the STI is related to achievement of annual performance metrics which aim to align executives to a shared set of KPIs based on business priorities for the next 12 months.

The shared KPIs cover the areas of finance, customer, health and safety and employee engagement with respective weightings applied across areas as outlined below in FY2016:

Target area	Weighting %
Financial: EBITDAF	30
Customer Satisfaction	30
Health & Safety	20
Employee Engagement	20

There are three performance levels within each target area, 'threshold', 'on-plan' and 'stretch', with 100% of the amount allocated to that target area being payable when the on-plan level is achieved. The stretch performance levels allow employees to be rewarded for exceptional performance. The maximum amount of an STI payment for an EMT member is 178% of the STI on-plan amount for that EMT member.

The balance of the STI is related to individual (in the case of the Chief Executive) or business unit and individual (in the case of other EMT members) performance measures.

In the event all four performance thresholds are not met, no STI payment will be made.

Long term performance incentives

Long term incentives (LTIs) are at-risk payments designed to align the reward of certain executives with the enhancement of shareholder value over a multi-year period.

An LTI plan commenced on 1 July 2013 under which grants were made measured over two or three year periods based on Mercury's total shareholder return (TSR) relative to the performance of the NZX 50. This plan has now closed with final vesting occurring in July 2016.

An updated LTI plan commenced on 1 July 2014. Under this plan grants are made annually with performance measured over a three year period. The value of each grant is set at the date of the grant and currently represents 20% – 35% of an executive's base salary.

Each grant under the updated LTI plan is divided into two tranches having different performance hurdles:

- 50% of the grant is based on Mercury's TSR relative to the NZX 50 and is subject to a gate that Mercury's TSR over that period must be at least positive;
- 50% of the grant is based on Mercury's TSR relative to the performance of an industry peer group (comprising Meridian Energy, Genesis Energy, Contact Energy and Trustpower). There is no positive TSR performance gate on this tranche but Mercury's TSR must be at the 50th percentile of the comparator group for any award to be made on this component of the LTI plan.

LTI payments are made in shares rather than cash. The maximum number of shares which an executive may receive for each grant is determined by dividing the value of the grant less tax by the market value of one Mercury share as at the date of the grant.

The Board retains discretion over the final outcome, to allow appropriate adjustments where unanticipated circumstances may impact performance, positively or negatively, over a three year period.

DIRECTOR AND EXECUTIVE EMPLOYEE REMUNERATION (CONTINUED)

Chief Executive remuneration

Chief Executive remuneration (FY2016)

FY2016[2]	Salary $	Benefits[1] $	Subtotal $	Pay for performance $			Total remuneration $
				STI	LTI	Subtotal	
CEO 1	999,445*	60,302	1,059,747	332,486	109,201	441,687	1,501,434

* Actual salary paid includes holiday pay paid as per NZ legislation. The base salary was $935,000.

Chief Executive remuneration (FY2015)

FY2015[2]	Salary $	Benefits[1] $	Subtotal $	Pay for performance $			Total remuneration $
				STI	LTI	Subtotal	
CEO 1	852,524*	45,408	897,932	250,000	280,000	530,000	1,427,932
CEO 2[3]	359,559	62,386	421,945	807,115[4]	756,731[5]	1,563,846	1,985,791

* Actual salary paid includes holiday pay paid as per NZ legislation. The base salary was $850,000.

Five year summary – Chief Executive remuneration

		Total remuneration paid[6] $	Percentage STI against maximum[9] %	Percentage vested LTI against maximum %	Span of LTI performance period
CEO 1 – Fraser Whineray	FY2016	1,501,434	57	78	2013 - 2016
	FY2015	1,427,932	47	100	2013 - 2015
CEO 2 – Doug Heffernan	FY2015	1,985,791	87	100	2011 - 2014[7]
	FY2014	1,302,754[7]	N/A[7]	N/A[7]	2011 - 2014[7]
	FY2013	1,439,243[8]	75	N/A	N/A
	FY2012	1,400,097[8]	56	N/A	N/A

Explanation of above items

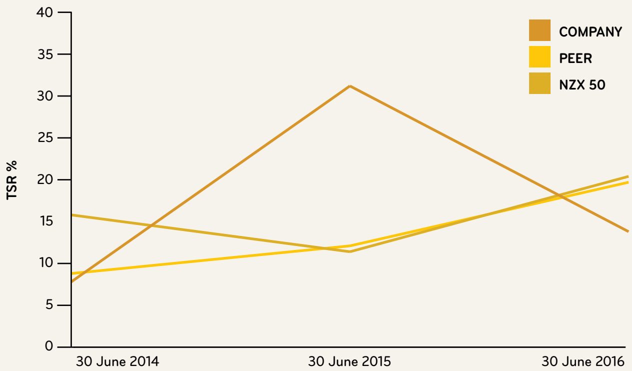
1 Benefits include KiwiSaver, insurance and carpark.
2 CEO 1 refers to Fraser Whineray and CEO 2 refers to Doug Heffernan.
3 Salary for Doug Heffernan covers a two month period.
4 STI payment for period 1 July 2013 to 31 August 2014.
5 LTI payment for period 1 July 2011 to 31 August 2014.
6 Total remuneration paid including Salary, Benefits, STI and LTI payments.
7 LTI and STI payments for FY2014 are included in the FY2015 year as schemes ended 31 August 2014.
8 No LTI was payable for FY2012 and FY2013.
9 Maximum STI is 178% of on-plan performance pay.

Breakdown of Chief Executive pay for performance (FY2016)

	Description	Performance measures	Percentage achieved %
STI[1]	Set at 35% of base salary. Based on a combination of key financial and non-financial performance measures.	80% based on the four Company Shared KPIs (see table earlier for weightings).	97
		20% based on individual measures.	120
LTI[1]	Conditional awards of shares under the historical long-term incentive scheme.	100% weighting relative TSR performance against NZX 50 (fixed at date of grant) with 50% vesting at 50th percentile and 100% at 75th percentile; pro rata vesting in between.	78

1 The above STI and LTI payments for FY2016 were paid in FY2017.

Three year summary – TSR performance (company vs peer)



KiwiSaver

The Chief Executive is a member of KiwiSaver. As a member of this scheme, the Chief Executive is eligible to contribute and receive a matching company contribution of 3% of gross taxable earnings (including short and long-term incentives). For FY2016 the company's contribution was $45,883.

FY2017 Chief Executive remuneration structure

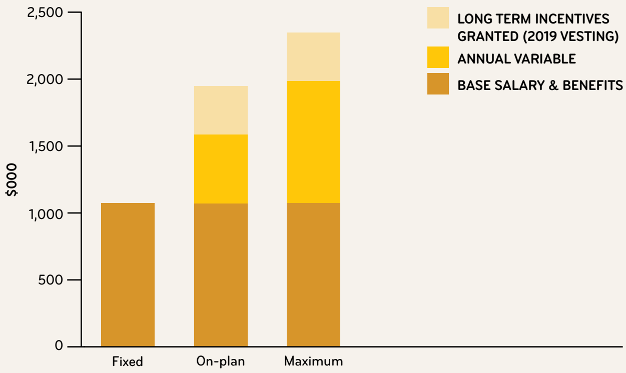
The Board has elected, in the interests of transparency, to disclose in advance the structure and package that will apply for FY2017.

FY2017	Base Salary $	Benefits[1] $	Subtotal $	Pay for performance "on-plan" $			Total remuneration $
				STI	LTI granted[2]	Subtotal	
CEO 1	1,028,500	45,274	1,073,774	514,250	359,975	874,225	1,947,999

1 Benefits include Kiwisaver, insurance and carpark.

2 This LTI is granted in FY2017 and if hurdles are met, paid in shares in 2019. The LTI tranche which has the potential to vest in FY2017 is $200,000 and dates from FY2014-FY2017.

Chief Executive remuneration performance pay for FY2017



Chief Financial Officer remuneration

In the interests of providing greater transparency of executive remuneration, the Board has elected to provide details regarding total remuneration paid to the Chief Financial Officer.

In FY2016, the Chief Financial Officer received remuneration totalling $943,028. This amount included $119,700 STI payment and $280,000 LTI payment for FY2015 paid in FY2016, with the remaining $543,328 being a combination of fixed remuneration and benefits (including a 3% superannuation allowance paid in lieu of KiwiSaver).

DIRECTOR AND EXECUTIVE EMPLOYEE REMUNERATION (CONTINUED)

Employee remuneration

The Group paid remuneration in excess of $100,000 including benefits to 364 employees (not including directors) during the FY2016 year in the following bands:

Remuneration band	Currently employed	No longer employed	Total
$100,001 – $110,000	66	7	73
$110,001 – $120,000	55	3	58
$120,001 – $130,000	37	3	40
$130,001 – $140,000	41	1	42
$140,001 – $150,000	31	4	35
$150,001 – $160,000	16	3	19
$160,001 – $170,000	11		11
$170,001 – $180,000	13		13
$180,001 – $190,000	7	2	9
$190,001 – $200,000	5	3	8
$200,001 – $210,000	7	3	10
$210,001 – $220,000	2	5	7
$220,001 – $230,000	2	2	4
$230,001 – $240,000	7	1	8
$240,001 – $250,000	4		4
$250,001 – $260,000	6		6
$260,001 – $270,000	1		1
$280,001 – $290,000	2		2
$290,001 – $300,000	1		1
$300,001 – $310,000	1		1
$310,001 – $320,000	1		1
$370,001 – $380,000		1	1
$380,001 – $390,000	2		2
$430,001 – $440,000	1		1
$440,001 – $450,000	1		1
$450,001 – $460,000		1	1
$470,001 – $480,000	1		1
$510,001 – $520,000		1	1
$940,001 – $950,000	1		1
$1,050,001 – $1,060,000		1	1
$1,580,001 – $1,590,000	1		1
	323	41	364

NB: The salary bands above include 25 employees who received redundancy payments in FY2016.

The total remuneration ratio for FY2016 between Employee (median) and Chief Executive was 1:21. The ratio of Employee (median) remuneration and Chief Executive base salary was 1:11.

Directors' remuneration

The directors' remuneration is paid in the form of directors' fees. Additional fees are paid to the Chair and in respect of work carried out by directors on various Board committees to reflect the additional time involved and responsibilities of these positions.

The total pool of fees able to be paid to directors is subject to shareholder approval and currently stands at $937,000. At the 2015 Annual Shareholders' Meeting, shareholders approved an increase of $139,750 to the pool (from $851,250) to be implemented over 2 years. The second increase will be effective from 5 November 2016, which will take the total pool to $991,000. Mercury meets directors' reasonable travel and other costs associated with Mercury business. The following people held office as directors during the year to 30 June 2016 and received the following remuneration during the period:

Director	Total fees paid
Joan Withers (Chair)	162,920
Michael Allen	97,485
Prue Flacks	113,485
Andy Lark	97,485
James Miller	103,485
Keith Smith	115,485
Patrick Strange	99,485
Mike Taitoko	80,798
Total	**$870,628**

DIRECTORS' DISCLOSURES

Interests Register

Disclosure of directors' interests

Section 140(1) of the New Zealand Companies Act 1993 requires a director of a company to disclose certain interests. Under subsection (2) a director can make disclosure by giving a general notice in writing to the company of a position held by a director in another named company or entity. The following are particulars included in the company's Interests Register as at 30 June 2016:

Joan Withers	
Television New Zealand Limited[1]	Chair
The Treasury Advisory Board	Director
ANZ Bank New Zealand Limited	Director
Sweet Louise Foundation	Trustee
The Tindall Foundation	Trustee
Pure Advantage	Trustee

Michael Allen	
Geothermal New Zealand Inc	Executive Director
ReEx Capital Asia Private Limited (Singapore)	Chair/Shareholder
Mid Century Design Limited	Director/Shareholder
Appointed Special Envoy for Renewable Energy by Ministry of Foreign Affairs and Trade	Officer
GNS Strategic Scientific User Advisory Panel	Member

Prue Flacks	
Bank of New Zealand Limited	Director
BBull Family Trust Limited	Director
Planboe Limited	Director
Chorus Limited	Director
Holds Capital Bonds worth $40,000 issued by the company	

James Miller	
NZX Limited	Chair
ACC	Director
Auckland International Airport Limited	Director
St Cuthbert's College Trust Board	Trustee

Mike Taitoko (appointed 28 August 2015)	
Waiora Consulting Limited[3]	Director/Shareholder
Takiwa Health Limited[3]	Director
Waiora Pacific Limited[3]	Director/Shareholder
Cognition Education Limited[3]	Director
Committee for Auckland Limited[3]	Director
Bioresource Processing Alliance[3]	Director

Keith Smith	
Healthcare Holdings Ltd and subsidiaries and associates	Chair
Enterprise Motor Group Ltd and subsidiaries	Chair
Mobile Surgical Services Limited and subsidiaries	Chair
Goodman (NZ) Limited and subsidiaries	Chair
The Warehouse Group Limited and subsidiaries	Deputy Chair
H J Asmuss & Co Limited	Chair
Community Financial Services Limited	Director
Electronic Navigation Limited and subsidiaries	Director
K One W One Limited and subsidiaries	Director
Sheppard Industries Ltd[2]	Director
Westland Dairy Corporate Ltd	Director
Harpers Gold Limited and subsidiaries	Director/Shareholder
James Raymond Holdings Limited (private family investment company)	Director/Shareholder
Gwendoline Holdings Limited (private family investment company)	Director/Shareholder
Cornwall Park Trust Board	Trustee
Sir John Logan Campbell Residuary Estate	Trustee
The Selwyn Trust	Trustee
Advisory board of The New Zealand Tax Trading Company	Member
Anderson & O'Leary Limited[3]	Chair
The Warehouse Financial Services Limited[3]	Director

Patrick Strange	
Waitahoata Farms Limited	Director
Ausgrid[3]	Director
Endeavour Energy[3]	Director
Essential Energy[3]	Director
WorkSafe New Zealand[2]	Director
Chorus Limited[3]	Chair
NZX Limited	Director
New Zealand Clearing and Depository Corporation Limited[3]	Director
Auckland International Airport[3]	Director
Holds 8,600 seven year Fixed Rate Bonds issued by the company	

Andy Lark	
No 8 Ventures Management Limited	Director
SLI Systems Limited	Director
Fronde	Director
Group Lark	Chair
Xero	Chief Marketing Officer
Simple	Director and Interim Chair
Marketshare[2]	Advisory Board Member

1 Even though this is outside the reporting period please note that the director has announced she will not seek reappointment as Chair of Television New Zealand Limited when her term ends early 2017 and will be appointed as Chair of Warehouse Group in September 2016.

2 Entries removed by notices given by directors during the year ended 30 June 2016.

3 Entries added by notices given by directors during the year ended 30 June 2016.

4 Entries amended (e.g., through change from director to Chair) by notices given by directors during the year ended 30 June 2016.

DIRECTORS' DISCLOSURES (CONTINUED)

Directors' and officers' indemnities

Indemnities have been given to and insurance has been effected for, directors and senior managers of the Group to cover acts or omissions of those persons in carrying out their duties and responsibilities as directors and senior managers.

Disclosure of directors' interests in share transactions

Directors disclosed, pursuant to section 148 of the New Zealand Companies Act 1993, the following acquisitions and disposals of relevant interests in shares during the period to 30 June 2016:

Name of director	Date of acquisition/ disposal of relevant interest	Nature of relevant interest	Consideration	Shares in which a relevant interest was acquired/(disposed)
Patrick Strange	31 August 2015	On market purchase of shares by JBWere (NZ) Nominees Limited as a nominee for the Three Kings Trust	$27,500	10,000
Prue Flacks	5 February 2016	Acquisition of beneficial interest in shares as a results of a distribution from the estates of Brian and Helen Bull.	Nil	13,374

Disclosure of directors' interests in shares

Directors disclosed the following relevant interests in shares as at 30 June 2016:

Director	Number of shares in which a relevant interest is held
Joan Withers	39,900
Michael Allen	2,080
Prue Flacks	23,474
James Miller	40,320
Mike Taitoko	0
Keith Smith	27,868
Patrick Strange	14,160
Andy Lark	0

SHAREHOLDER INFORMATION

Twenty largest registered shareholders as at 29 July 2016

Name	Number of shares	% of shares
Her Majesty The Queen In Right Of New Zealand	716,140,528	51.15
New Zealand Central Securities Depository Limited	284,554,767	20.32
Mercury NZ Limited	22,656,390	1.61
Custodial Services Limited	9,785,732	0.69
FNZ Custodians Limited	8,697,932	0.62
HSBC Custody Nominees (Australia) Limited	8,285,173	0.59
Forsyth Barr Custodians Limited	6,722,646	0.48
RBC Investor Services Australia Nominees Pty Limited	6,720,303	0.48
National Nominees Limited	6,629,808	0.47
Investment Custodial Services Limited	4,300,234	0.30
Custodial Services Limited	4,023,300	0.28
JP Morgan Nominees Australia Limited	3,876,868	0.27
New Zealand Depository Nominee Limited	3,113,729	0.22
Custodial Services Limited	2,880,763	0.2
Custodial Services Limited	2,657,751	0.18
Custodial Services Limited	2,097,176	0.14
Citicorp Nominees Pty Limited	1,782,077	0.12
Richard Wallace Shapero	1,690,000	0.12
Jbwere (NZ) Nominees Limited	1,679,440	0.11
NZPT Custodians (Grosvenor) Limited	1,423,677	0.10
Total	1,099,718,294	78.45

New Zealand Central Securities Depository Limited (NZCSD) provides a custodian depository service that allows electronic trading of securities to its members and does not have a beneficial interest in these shares. As at 29 July 2016, the 10 largest shareholdings in the company held through NZCSD were:

Shareholder	Number of shares	% of NZCSD holding	% of total Mercury shares
National Nominees New Zealand Limited	55,808,719	19.61	3.99
HSBC Nominees (New Zealand) Limited A/C State Street	54,945,433	19.31	3.92
HSBC Nominees (New Zealand) Limited	48,840,093	17.16	3.49
Citibank Nominees (New Zealand) Limited	45,288,315	15.92	3.23
JPMorgan Chase Bank NA NZ Branch-Segregated Clients Acct	27,010,916	9.49	1.93
Accident Compensation Corporation	20,267,403	7.12	1.45
HSBC Nominees – New Zealand Superannuation Fund Nominees Limited	13,325,571	4.68	0.95
TEA Custodians Limited Client Property Trust Account	3,731,710	1.31	0.27
BNP Paribas Nominees (NZ) Limited	3,430,405	1.21	0.25
BNP Paribas Nominees (NZ) Limited	2,069,697	0.73	0.15

Substantial product holders of the company as at 30 June 2016

	Class of securities	Number of securities in substantial holding	Total number of securities in class
Her Majesty The Queen In Right Of New Zealand	Ordinary shares	729,534,099[1]	1,400,012,517

1 This comprises (a) 716,140,528 shares held by the Crown on its own account; (b) 13,325,571 shares forming part of the New Zealand Superannuation Fund in which the Crown has a beneficial interest; and (c) 68,000 shares held by Public Trust on trust for the Crown and certain iwi.

SHAREHOLDER INFORMATION (CONTINUED)

Distribution of shareholders and holdings as at 29 July 2016

Size of holding	Number of shareholders	%	Number of shares	Holding quantity %
1 to 1,000	32,895	35.81	23,173,673	1.66
1,001 to 5,000	46,627	50.76	108,975,037	7.78
5,001 to 10,000	7,994	8.7	58,539,788	4.18
10,001 to 100,000	4,227	4.6	85,304,343	6.09
100,001 and over	121	0.13	1,124,019,676	80.2
Total	91,864	100.00	1,400,012,517	100.00

Distribution of bondholders and holdings as at 29 July 2016

Size of holding	Number of capital bondholders	%	Number of capital bonds	Holding quantity %
1 to 1,000	0	0	0	0
1,001 to 5,000	383	8.88	1,909,000	0.64
5,001 to 10,000	865	20.05	8,283,000	2.76
10,001 to 100,000	2,831	65.62	105,155,000	35.05
100,001 and over	235	5.45	184,653,000	61.55
Total	4,314	100.00	300,000,000	100.00

COMPANY DISCLOSURES

Stock Exchange listings

Mercury NZ Limited is listed on both the New Zealand and Australian stock exchanges.

In New Zealand, the company is listed with a "non-standard" (NS) designation. This is due to particular provisions of the Constitution, including the requirements regulating ownership and transfer of Ordinary shares.

ASX approved a change in Mercury NZ Limited's ASX admission category from an ASX Listing to an ASX Foreign Exempt Listing, effective from the commencement of trading on 19 February 2016.

The company continues to have a full listing on the NZX Main Board, and the company's shares are still listed on the ASX. The company is primarily regulated by the NZX, complies with the NZX Listing Rules, and is exempt from complying with most of the ASX Listing Rules (based on the principle of substituted compliance).

Mercury NZ Limited

The following persons held office as directors of Mercury NZ Limited (formerly Mighty River Power Limited) as at the end of FY2016, being 30 June 2016: Joan Withers, Mike Allen, Prue Flacks, James Miller, Mike Taitoko, Keith Smith, Patrick Strange and Andy Lark.

Subsidiary companies

The following persons held office as directors of subsidiaries of Mercury NZ Limited during FY2016:

Company name	**Directors**
Bosco Connect Limited	Fraser Whineray William Meek Tony Nagel
ECNZ International Limited[1]	Fraser Whineray William Meek Tony Nagel
Glo-Bug Limited	Fraser Whineray[2] William Meek[2] Tony Nagel[2] James Munro[3] Glenn Rockell[3]
Kawerau Geothermal Limited	Fraser Whineray William Meek Tony Nagel
Mercury Energy Limited	Fraser Whineray William Meek Tony Nagel
Metrix Limited	Fraser Whineray William Meek Tony Nagel
Ngatamariki MRP Limited	Fraser Whineray William Meek Tony Nagel
Rotokawa MRP Limited	Fraser Whineray William Meek Tony Nagel
MRP FinCo-Chile Limited[4]	Samuel Moore Carol Brougham
MRP FinCo-Peru Limited[4]	Samuel Moore Carol Brougham
MRP Holdings-Chile Limited[5]	Samuel Moore John Carbone Nikolai de Giorgio
MRP Holdings-Peru Limited[5]	Samuel Moore Carol Brougham
MRP NRI-Chile Holdings Limited	Samuel Moore John Carbone Nikolai de Giorgio
MRP NRI-Peru Holdings Limited	Samuel Moore John Carbone Nikolai de Giorgio
PT ECNZ Services Indonesia[6]	Agung Aryo Baskoro Ejoko Birmo Soegih Arto
MRP NRI-Germany Holdings Limited	Samuel Moore John Carbone Nikolai de Giorgio
MRP Holdings-Germany Limited[5]	Samuel Moore Carol Brougham
MRP FinCo-Germany Limited[4]	Samuel Moore Carol Brougham
Mighty Geothermal Power International Limited	Fraser Whineray William Meek Tony Nagel
Mighty Geothermal Power Limited	Fraser Whineray William Meek Tony Nagel
Mercury ESPP Limited (formerly Mighty River Power ESPP Limited)	William Meek Tony Nagel Marlene Strawson
Mercury Geothermal Limited (formerly Mighty River Power Geothermal Limited)	Fraser Whineray William Meek Tony Nagel
Mercury LTI Limited (formerly Mighty River Power LTI Limited)	Mike Allen[2] Karen Clayton[2] Prue Flacks Glenn Rockell[3] Tania Simpson[3]
Ngatamariki Geothermal Limited	Fraser Whineray William Meek Tony Nagel
Rotokawa Generation Limited	William Meek Nicholas Clarke[2] Tony Nagel[3] Paul Ware[7]
Rotokawa Geothermal Limited	Fraser Whineray William Meek Tony Nagel
Rotokawa Joint Venture Limited (50%)	Aroha Campbell Kevin Mcloughlin William Meek Nicholas Clarke[2] Paul Ware[7] Tony Nagel[3] Mark Thompson
Special General Partner Limited	Fraser Whineray William Meek Tony Nagel

1 Removed from New Zealand Companies register on 21 June 2016.
2 Directors who have been appointed during FY2016.
3 Directors who have resigned during FY2016.
4 Company in voluntary liquidation at 30 June 2016 and dissolved on 26 July 2016.
5 Company in voluntary liquidation at 30 June 2016.
6 Shareholding in company vested to the Crown on 21 June 2016.
7 Directors who have resigned during FY2017.

OTHER DISCLOSURES

Waivers from the New Zealand and Australian Stock Exchanges

ASX

ASX granted certain waivers in respect of the ASX Listing Rules to allow the Constitution to contain provisions reflecting the ownership restrictions imposed by the Public Finance Act and to allow the Crown to cancel the sale of shares to Applicants who acquired shares under the General Offer and were not New Zealand Applicants.

The majority of the waivers that ASX previously granted to the company in respect of the ASX Listing Rules are no longer relevant following the change to the company's admission category to an ASX Foreign Exempt Listing. The waivers from ASX Listing Rules 8.10 and 8.11 continue to apply. These waivers permit the Constitution to contain provisions:

- allowing the Crown and the company to enforce the 10% limit; and
- enabling the company to prevent shareholders who acquired shares under the General Offer and were not New Zealand Applicants from transferring those shares and to enable the company to sell those shares.

Information about Mercury NZ Limited Ordinary shares

This statement sets out information about the rights, privileges, conditions and limitations, including restrictions on transfer, that attach to shares in the company.

Rights and privileges

Under the Constitution and the Companies Act 1993 ("Companies Act"), each share gives the holder a right to:

- attend and vote at a meeting of shareholders, including the right to cast one vote per share on a poll on any resolution, such as a resolution to:
  - appoint or remove a director;
  - adopt, revoke or alter the Constitution;
  - approve a major transaction (as that term is defined in the Companies Act);
  - approve the amalgamation of the company under section 221 of the Companies Act; or
  - place the company in liquidation;
- receive an equal share in any distribution, including dividends, if any, authorised by the board and declared and paid by the company in respect of that share;
- receive an equal share with other shareholders in the distribution of surplus assets in any liquidation of the company;
- be sent certain information, including notices of meeting and company reports sent to shareholders generally; and
- exercise the other rights conferred upon a shareholder by the Companies Act and the Constitution.

Restrictions on ownership and transfer

The Public Finance Act 1989 ('Public Finance Act') includes restrictions on the ownership of certain types of securities issued by the company and consequences for breaching those restrictions. The Constitution incorporates these restrictions and mechanisms for monitoring and enforcing them.

A summary of the restrictions on the ownership of shares under the Public Finance Act and the Constitution is set out below. If the company issues any other class of shares, or other securities which confer voting rights, in the future, the restrictions summarised below would also apply to those other classes of shares or voting securities.

51% Holding

The Crown must hold at least 51% of the shares on issue.

The company must not issue, acquire or redeem any shares if such issue, acquisition or redemption would result in the Crown falling below this 51% holding.

10% Limit

No person (other than the Crown) may have a 'relevant interest' in more than 10% of the shares on issue ("10% Limit").

The company must not issue, acquire or redeem any shares if it has actual knowledge that such issue, acquisition or redemption will result in any person other than the Crown exceeding the 10% Limit.

Ascertaining whether a breach has occurred

If a holder of shares breaches the 10% Limit or knows or believes that a person who has a relevant interest in shares held by that holder may have a relevant interest in shares in breach of the 10% Limit, the holder must notify the company of the breach or potential breach.

The company may require a holder of shares to provide it with a statutory declaration if the Board knows or believes that a person is, or is likely to be, in breach of the 10% Limit. That statutory declaration is required to include, where applicable, details of all persons who have a relevant interest in any shares held by that holder.

Determining whether a breach has occurred

The company has the power to determine whether a breach of the 10% Limit has occurred and, if so, to enforce the 10% Limit. In broad terms, if:

- the company considers that a person may be in breach of the 10% Limit; or
- a holder of shares fails to lodge a statutory declaration when required to do so or lodges a declaration that has not been completed to the reasonable satisfaction of the company,

then the company is required to determine whether or not the 10% Limit has been breached and, if so, whether or not that breach was inadvertent. The company must give the affected shareholder the opportunity to make representations to the company before it makes a determination on these matters.

Effect of exceeding the 10% Limit

A person who is in breach of the 10% Limit must:

- comply with any notice that they receive from the company requiring them to dispose of shares or their relevant interest in shares, or take any other steps that are specified in the notice, for the purpose of remedying the breach; and
- ensure that they are no longer in breach within 60 days after the date on which they became aware, or ought to have been aware, of the breach. If the breach is not remedied within that timeframe, the company may arrange for the sale of the relevant number of shares on behalf of the relevant holder. In those circumstances, the company will pay the net proceeds of sale, after the deduction of any other costs incurred by the company in connection with the sale (including brokerage and the costs of investigating the breach of the 10% Limit), to the relevant holder as soon as practicable after the sale has been completed.

If a relevant interest is held in any shares in breach of the 10% Limit then, for so long as that breach continues:

- no votes may be cast in respect of any of the shares in which a relevant interest is held in excess of the 10% Limit; and
- the registered holder(s) of shares in which a relevant interest is held in breach of the 10% Limit will not be entitled to receive, in respect of the shares in which a relevant interest is held in excess of the 10% Limit, any dividend or other distribution authorised by the Board in respect of the shares.

However, if the Board determines that a breach of the 10% Limit was not inadvertent, or that it does not have sufficient information to determine that the breach was not inadvertent, the registered holder may not exercise the votes attached to, and will not be entitled to receive any dividends or other distributions in respect of, any of its shares (and not just the shares in which a relevant interest is held in excess of the 10% Limit).

An exercise of a voting right attached to a share held in breach of the 10% Limit must be disregarded in counting the votes concerned. However, a resolution passed at a meeting is not invalid where votes exercised in breach of the voting restriction were counted by the company in good faith and without knowledge of the breach.

The Board may refuse to register a transfer of shares if it knows or believes that the transfer will result in a breach of the 10% Limit or where the transferee has failed to lodge a statutory declaration requested from it by the Board within the prescribed timeframe.

Crown directions

The Crown has the power to direct the Board to exercise certain powers conferred on it under the Constitution (for example, where the Crown suspects that the 10% Limit has been breached but the Board has not taken steps to investigate the suspected breach).

Trustee corporations and nominee companies

Trustee corporations and nominee companies (that hold securities on behalf of a large number of separate underlying beneficial holders) are exempt from the 10% Limit provided that certain conditions are satisfied.

Share Cancellation

In certain circumstances, shares could be cancelled by the company through a reduction of capital, share buy back or other form of capital reconstruction approved by the Board and, where applicable, the shareholders.

Sale of less than a Minimum Holding

The company may at any time give notice to a shareholder holding less than a Minimum Holding of shares (as that term is defined in the NZX Main Board Listing Rules) that if, at the expiration of 3 months after the date the notice is given, shares then registered in the name of the holder are less than a Minimum Holding the company may sell those shares through the NZX Main Board or in some other manner approved by NZX Limited, and the holder is deemed to have authorised the company to act on behalf of the holder and to sign all necessary documents relating to the sale.

For the purposes of the sale and of Rule 5.12 of the ASX Settlement Operating Rules, where the company has given a notice that complies with Rule 5.12.2 of the ASX Settlement Operating Rules, the company may, after the expiration of the time specified in the notice, initiate a Holding Adjustment to move the relevant shares from that CHESS Holding to an Issuer Sponsored Holding (as those terms are defined in the ASX Settlement Operating Rules) or to take any other action the company considers necessary or desirable to effect the sale.

The proceeds of the sale of any shares sold for being less than a Minimum Holding will be applied as follows:

- first, in payment of any reasonable sale expenses.
- second, in satisfaction of any unpaid calls or any other amounts owing to the company in respect of the shares.
- the residue, if any, must be paid to the person who was the holder immediately before the sale or his or her executors, administrators or assigns.

Cancellation of sale of shares

The Crown may cancel the sale of shares to an applicant under the offer of shares by the Crown (the Offer) in the Mighty River Power Share Offer Investment Statement and Prospectus issued in April if the applicant misrepresented its entitlement to be allocated shares under the Offer as a 'New Zealand Applicant' (as that term is defined in the Share Offer Investment Statement and Prospectus). If the Crown cancels a sale of shares on those grounds:

- the company must sell shares held by that applicant, up to the number of shares sold to it under the Offer, irrespective of whether or not those shares were acquired by the applicant under the Offer (unless the applicant had previously sold, transferred or disposed of all of its shares to a person who was not an associated person of the applicant); and
- the applicant will receive from the sale the lesser of:
  - the sale price for the shares less the costs incurred by the Crown and the company; and
  - the aggregate price paid for the shares less those costs, with any excess amount being payable to the Crown.

OTHER DISCLOSURES (CONTINUED)

If an applicant who misrepresented their entitlement to shares has sold, transferred or otherwise disposed of shares to an associated person, then the power of sale will extend to shares held by that associated person, up to the number of shares transferred, sold or otherwise disposed of to the associated person by the relevant applicant.

Donations

Donations of $100,637 were made by the Group during the year ended 30 June 2016 ($70,434 during the year ended 30 June 2015). Donations to political parties are prohibited and none were made.

Other Disclosures

Mercury NZ Limited is incorporated in New Zealand and is not subject to Chapters 6, 6A, 6B and 6C of the Corporations Act 2001 (Australia). Mercury will not acquire any classified assets in circumstances in which the ASX Listing Rules would require the issue of restricted securities, without the written consent of ASX.

On 23 August 2016 the Board declared a fully imputed final dividend of 8.6 cents per share and an unimputed special dividend of 4 cents per share to be paid on 30 September 2016 to all shareholders who are on the company's share register at 5.00pm on the record date of 14 September 2016. The Final dividend will be imputed at a corporate tax rate of 28% which amounts to an imputation credit of 3.3444 cents per share. The company will also pay a supplementary dividend of 1.5176 cents per share relating to the final dividend to non-resident shareholders. The company will receive from the New Zealand Inland Revenue Department a tax credit equivalent to the supplementary dividends.

These dividends together with the interim dividend of $78 million (5.7 cents per share) paid to shareholders on 31 March 2016 brings total declared dividends to $252 million (or 18.3 cents per share).

As at the date of this annual report, the company has a Standard & Poor's BBB+ rating with a stable outlook. The company benefits from a one notch uplift due to the Crown's majority ownership.

The company's Net Tangible Assets per Share (excluding treasury stock) as at 30 June 2016 was $2.36, compared with $2.38 at 30 June 2015.

SHAREHOLDER INFORMATION

Shareholder enquiries

Changes in address, dividend payment details and investment portfolios can be viewed and updated online: **www.investorcentre.com/nz**. You will need your CSN and FIN numbers to access this service.

Enquiries may be addressed to the Share Registrar (see Directory for contact details).

Investor information

Our website at **www.mercury.co.nz** is an excellent source of information about what's happening within the company.

Our Investor Centre allows you to view all regular investor communications, information on our latest operating and financial results, dividend payments, news and share price history.

Electronic shareholder communication

It is quick and easy to make the change to receiving your reports electronically. This can be done either:

- Online at www.investorcentre.com/nz by using your CSN and FIN numbers (when you log in for the first time). Select 'View Portfolio' and log in. Then select 'Update My Details' and select 'Communication Options'; or
- Contacting Computershare Investor Services Limited by email, fax or post.

GLOSSARY

Dividend	The distribution of a proportion of a company's earnings, decided by the board of directors, to its shareholders. The dividend is most often quoted in terms of the dollar amount per share. May be paid as Interim Dividend and Final Dividend
Free Cash Flow	Is net cash flow from operating activities less normalised stay-in-business capital expenditure
Generation-weighted Average Price (GWAP)	Generation Weighted Average Price of electricity generated and sold to the wholesale electricity market
GWh	Gigawatt hour. One gigawatt hour is equal to one million kilowatt hours
Load-weighted Average Price (LWAP)	Load Weighted Average Price of electricity purchased from the wholesale electricity market
Lost-time Injury Frequency Rate (LTIFR)	A measure of the number of injuries resulting in lost time per 200,000 hours worked, including employees and on-site contractors
MWh	Megawatt hour. One megawatt hour is equal to 1,000 kilowatt hours. A megawatt hour is the metering standard unit for the wholesale market
Pre-pay	Customers pay for electricity as they use it, rather than receiving a monthly bill, making it much easier to manage their electricity spend, keep on top of payments and budget
Renewable electricity	Electricity produced from harnessing the power of water, geothermal heat and wind, along with solar and other natural sources, that can be used and managed sustainably
Smart meters	Advanced electricity meters that are a replacement for analogue meters, and send electronic meter readings to your energy retailer automatically
Spot market/ wholesale market	The buying and selling of wholesale electricity is done via a 'pool', where electricity generators offer electricity to the market and retailers bid to buy the electricity. This market is called the spot or physical wholesale market
Total Recordable Injury Frequency Rate (TRIFR)	A record of the number of reported medical treatment, restricted work, lost time and serious harm injuries per 200,000 hours, including employees and on-site contractors

DIRECTORY

Board of Directors

Joan Withers, Chair
Mike Allen
Prue Flacks
Andy Lark
James Miller
Keith Smith
Patrick Strange
Mike Taitoko

Executive Management Team

Fraser Whineray,
Chief Executive

Kevin Angland,
General Manager Digital Services

Nick Clarke,
General Manager Geothermal

Phil Gibson,
General Manager Hydro & Wholesale

Julia Jack,
Chief Marketing Officer

William Meek,
Chief Financial Officer

Tony Nagel,
General Manager Corporate Affairs

Matt Olde,
Metrix Chief Executive

Marlene Strawson,
General Manager People & Safety

Company Secretary

Tony Nagel

Investor Relations

Mercury NZ Limited
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New Zealand

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Fax: +64 9 308 8209
Email: investor@mercury.co.nz

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From 3 September 2016:
109 Carlton Gore Road, Auckland 1023

Registered Office in Australia

c/- TMF Corporate Services
(Aust) Pty Limited
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Phone: +61 2 8988 5800

Legal Advisors

Chapman Tripp
Level 35, ANZ Centre
23-29 Albert Street, Auckland 1010
PO Box 2206, Auckland
Phone: +64 9 357 9000

Bankers

ANZ Bank
ASB Bank
Bank of Tokyo-Mitsubishi UFJ
Bank of New Zealand
Westpac

Credit Rating (reaffirmed December 2015)

Long term: BBB+
Outlook: Stable

Share Register – New Zealand

Computershare Investor Services Ltd
Level 2, 159 Hurstmere Road, Takapuna,
Auckland 0622
Private Bag 92 119
Auckland 1142
New Zealand

Phone: +64 9 488 8777
Fax: +64 9 488 8787
Email: enquiry@computershare.co.nz

Web: www.investorcentre.com/nz

Share Register – Australia

Computershare Investor Services Pty Ltd
Yarra Falls, 452 Johnston Street, Abbotsford, VIC 3067
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Melbourne, VIC 3001
Australia

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Phone: +61 3 9415 4083 (outside Australia)
Fax: +61 3 9473 2500
Email: enquiry@computershare.co.nz

Mercury

ENERGY MADE WONDERFUL.