Solid Energy

Statement of Corporate Intent

For three years commencing 1 July 2013

SOLID ENERGY
Coals of New Zealand

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This Statement of Corporate Intent (SCI) is submitted by Solid Energy New Zealand Limited (Solid Energy) pursuant to Section 14 of the State Owned Enterprises Act 1986 (the Act). It sets out Solid Energy's objectives and performance targets for the three years to 30 June 2016, and describes the nature and scope of the activities to be undertaken to achieve these objectives.

Contents

1. PREFACE

In February 2013 Solid Energy entered a support agreement with its major lenders following a sustained downturn in international coal markets with the resultant impact on profitability, cashflow and balance sheet which threatened the company's banking covenants. Solid Energy has embarked on a major corporate and operational restructuring which, combined with capital support from the Shareholder and accommodation from our banking group and bond holders, has enabled us to look ahead. However, the next three years are expected to be challenging in the absence of increased prices for exported coal in New Zealand dollar terms.

2. KEY OBJECTIVES

SOLID ENERGY'S VISION IS TO

Secure, develop and mine coal resources in order to create wealth for the Shareholder in a manner that has a strong and robust licence to operate from all stakeholders.

OUR VALUES ARE

For our business to be sustainable in the long term we must trade profitably in a depressed coal market and, ultimately, create wealth for our Shareholder and our customers and provide opportunities for our employees.

We acknowledge our responsibilities as a leading coal producer, exporter and New Zealand supplier to generate economic prosperity for our stakeholders in a socially responsible and environmentally sensitive way. Specifically we will aim to:

- be profitable
- support the development, safety, health and wellbeing of our people and our communities
- respect the natural environment in which we operate and seek to ensure that the cumulative result of all the activities we undertake will have a neutral net effect on the New Zealand environment
- engage with our stakeholders openly, clearly and honestly
- respect cultures, customs and values in our dealings with our people, suppliers and customers; and
- operate in accordance with business sustainability principles.

CURRENT BUSINESS OBJECTIVES

Solid Energy's business objectives reflect the serious financial challenges posed to our business by the continued market downturn in 2012 and 2013. Even with the significant cost reductions and productivity improvements achieved over the last 12 months the company must continue to focus on delivering on our business plan while retaining longer-term optionality where possible.

The key objective for the business is to return to producing consistent and reliable underlying earnings over time which will provide a return on the capital employed and give our Shareholder a suitable return for the risk involved in owning a New Zealand coal company. The ability of the company to pay a return to the Shareholder will require a significant reduction in debt and will rely upon retaining the confidence of our lenders and Shareholder.

This requires achieving annual earnings and cashflows which will permit:

- funding of the capital required to produce such earnings
- paying down debt to acceptable levels
- providing the Shareholder with returns consistent with the resource sector.

Specific business objectives therefore are to:

- maintain our licence to operate (environment, reputation).
- maintain statutory compliance (financial, environmental, health & safety etc.)
- not compromise safety
- remain financially viable through the market downturn
- manage markets and mining operations to achieve or exceed Business Plan forecasts
- ensure all expenditure realises tangible, and preferably short-term financial benefits
- retain and develop our market positions
- retain options for future growth at minimum cost

3. NATURE AND SCOPE OF ACTIVITIES

Solid Energy develops and supplies coal resource-based products in New Zealand and internationally. Solid Energy's business activities involve developing and producing coal and lignites from a resource base of 1.5 billion tonnes, from four major operating mines producing approximately 3.5 million tonnes of product per annum supplying the export and domestic markets.

These activities are supported by:

- logistics management, transportation and distribution
- marketing, sales and trading (in New Zealand and internationally)
- management of land and resources required for these activities
- coal resource development activities to maintain and renew the business
- environmental management.

Solid Energy may undertake these activities by way of full or shared ownership of operations including joint ventures, franchising arrangements, subcontracting, agency or any combination of these.

In carrying out these activities Solid Energy seeks to manage our assets and liabilities prudently, comply with all legislative and regulatory requirements, and consult with Shareholding Ministers in accordance with the provisions in this SCI and as agreed separately.

4. OUTLOOK AND STRATEGY

Solid Energy's business strategy is based predominantly on continuing global demand for coking coal driven primarily by steelmakers in New Zealand, India, China and Japan.

OUR VALUE PROPOSITION

The company has returned to being a conventional coal business focusing on cost efficiency and improved productivity. We shall maintain our high health, safety and environmental standards across our business as we continue to implement further business improvement.

OUR KEY BUSINESS STRATEGIES

West Coast Export

- Increase the value of our coking coal sales, production and logistics capacity; develop Millerton and Cypress extensions at Stockton Opencast Mine
- Accelerate the development of prospective coal resources to supply primarily export markets in the medium term
- Continue to improve performance at existing operations to secure positive cashflows (to maximise our return per tonne)

North Island Domestic

- Renew long-term contracts with major customers and seek market-growth opportunities
- Develop regional coal resources to meet this contracted customer base
- Continue to improve performance at existing operations to secure positive cashflows (to maximise our return per tonne)

South Island Domestic

- Consolidate a competitive and profitable customer-driven business
- Preserve lignite mining opportunities by retaining lignite mineral rights

Other

- Divest surplus assets

OUR PARTNERSHIP STRATEGY

Solid Energy may bring additional capital, expertise, technology and customers to our developments where partnership creates additional value or minimises risk.

OUR INVESTMENT STRATEGY

Solid Energy will allocate capital expenditure only to ensure compliance, to sustain business-as-usual and to investments with short term-paybacks. We anticipate annual capital expenditure over the period to be considerably less than depreciation. We will continually assess the performance of each of our operating assets and projects to ensure that our invested capital is allocated efficiently and our cost structure is relevant to the market.

5. PERFORMANCE TARGETS

Solid Energy has the following performance objectives.

Value	Execute our turnaround plan, maximise operating cashflow and repay debt
People	Continually attract, retain and develop highly skilled, motivated and committed staff who perform at a high level, are well led, and see us as an excellent employer
Health & Safety	Have healthy people, with no harm to anyone, ever
Environment	Aim to have a neutral net effect on the New Zealand environment
Reputation	Maintain the trust of our Shareholder, lenders, customers, suppliers and key stakeholders

Key performance targets for Solid Energy over the period (financial years 2014-16) are based on conservative price projections that have formed the basis for the restructure agreement with the Shareholder and majority of lenders, which assume that the current price path continues for the period 2014-2016 and maintains productivity gains as presented. The business will need to outperform these targets over the forecast period to enable debt to be paid down to acceptable levels.

			2013/14	2014/15	2015/16
Value: Operations	Sales Units	Coal (Mt)	3.5	3.5	3.5
	Production Units	Coal (Mt)	3.4	3.3	3.4
Value: Shareholder Returns	Dividend Paid ($M)		0	0	0
	Dividend Yield[1]		0%	0%	0%
	Dividend Payout[2]		0%	0%	0%
	Return on Equity[3]		-79%	-144%	n.m*
Value: Profitability	Return on Capital Employed[4]		-7%	-4%	0%
	Operating Margin[5]		6%	8%	10%
Value: Leverage/Solvency	Gearing Ratio [6]		65%	72%	74%
	EBITDAF ($M)		30	41	54
	Interest Cover[7]		1.5	2.3	3.1
	Current Ratio[8]		1.9	1.8	1.7
Future value	Capital Investment ($M)		37	25	25
Health & Safety	All Injury Frequency Rate[9]		11.4	10.2	9.1
	Lost Time Injury Frequency Rate[10]		3.2	2.8	2.5
Environment	Regulatory, Abatement and Enforcement notices		0	0	0

*n.m =not meaningful

1. Dividends paid / Average commercial value, note average commercial value assumed to equal opening value 2012/13
2. Dividends paid / Net cashflow from operating activities less depreciation expense
3. Net profit after tax / Average Shareholder equity
   a) The calculation of Average Shareholder equity is assumed to be ordinary equity only and therefore excludes the value of the redeemable preference shares
   b) The business plan does not provide for any IFRS fair value movements or asset revaluations.
   c) In 2015/16 the calculation is not meaningful as ordinary equity turns negative.
4. EBIT / Average capital employed
   a) The calculation of average capital employed includes the value of redeemable preference shares
5. EBITDAF/Revenue
6. Net debt / (Net debt + equity)
   a) The calculation of equity includes the value of redeemable preference shares
7. EBITDAF / Interest expense
8. Current assets / Current liabilities
9. Number of injuries per 1,000,000 hrs requiring medical aid or greater treatment
10. Number of injuries per 1,000,000 hrs resulting in more than one lost work day or shift

PERFORMANCE TARGET DISCUSSION

The financial targets reflect a global coal market which is in a severely depressed part of the commodity cycle. This has resulted in the need for significant economies throughout the company to preserve cash and retain Shareholder and bank support for funding. While this downturn in global prices was predicted in the last SCI, its extent and duration has been sustained. This has been further compounded by the strength of the New Zealand dollar.

6. RATIO OF SHAREHOLDERS' FUNDS TO TOTAL ASSETS

	2013/14	2014/15	2015/16
Shareholders' funds ($M) [1]	$39.7	$6.5	-$12.6
Total assets ($M) [2]	$800.1	$765.1	$723.9
Shareholders' funds / total assets	5%	1%	-2%

1. Shareholders' Funds includes share capital, retained earnings and reserves, but excludes redeemable preference shares.
2. Total assets include current assets, fixed assets and intangibles.

7. ACCOUNTING POLICIES

Solid Energy will maintain accounting policies in accordance with the Financial Reporting Act 1993 and New Zealand International Financial Reporting Standards (NZ IFRS). Solid Energy's current accounting policies are attached as Appendix 1.

8. CAPITAL STRUCTURE

Solid Energy targets a balance of debt and equity that achieves consistent financial ratios and allows prudent balance sheet management and financial flexibility. Following the significant and sustained reduction in international coal prices, and a refocus of the company's strategy back towards its traditional coal operations, the company booked asset write-downs of $215.3 million at 30 June 2013 which, when combined with other restructuring adjustments, had the impact of raising gearing to 81% at June 2013 (June 2012: 42%).

Subsequent to balance date, Solid Energy reached a capital restructure agreement which has the support of the Shareholder and the majority of our lenders and note holders.

The key features of the capital restructure involve:

- The five banks rescheduling their debts in a syndicated term loan facility maturing on 7 September 2016
- The five banks and note holder TSB exchanging $75 million of the debt owed by the company for $75 million of equity in the form of non-voting redeemable preference shares
- The Crown providing a secured working capital loan of $50 million, repayable within three years: a secured mortgage-backed facility of $50 million (or 65% of the value of non-core Land, whichever is the lesser), repayable within three years, and a secured standby facility of up to $30 million if required
- The company issuing the Crown a further $25 million in non-voting redeemable preference shares in return for cash
- Note holder support

The key terms of the capital restructure were agreed at the date of signing the accounts, however the final settlement and documentation was not completed until 22 October 2013 and certain aspects of the restructure are the subject of a legal challenge by a dissenting bank creditor.

9. PROFIT DISTRIBUTION POLICY

Ordinarily Solid Energy aims to distribute funds surplus to our investment and operating expectations, subject to meeting the solvency requirements of the Companies Act 1993. However the terms of the capital restructure agreement require that no distributions are made on the ordinary shares of Solid Energy within the term of the agreement.

10. INFORMATION TO BE PROVIDED TO SHAREHOLDER

To enable Shareholding Ministers to be fully aware of investment plans and intentions and to assess the value of their investment in Solid Energy, the following information will be provided:

- Detailed budget for the next financial year
- Detailed financial projections for the next three financial years

- A strategic and business plan for the group
- Any proposals likely to represent a major change in Solid Energy's balance sheet ratios or to involve capital expenditure significantly above that foreshadowed in the three year financial projections
- A quarterly report, including a summary and commentary on the previous quarter's financial performance and commentary on our outlook to year end. This report will include, as appropriate, a discussion of significant variances from previously forecast performance
- A Half-Year Report, including an unaudited profit and loss statement, balance sheet, statement of cashflows and such other details as are necessary to enable an informed assessment of performance
- An Annual Report and audited financial statements

In accordance with Section 18 of the Act, the company will provide other information relating to the affairs of the company as requested by Shareholding Ministers.

11. CAPITAL EXPENDITURE, ACQUISITION, DIVESTMENT AND SHAREHOLDER CONSULTATION

As part of the recent capital restructure announcements, Solid Energy will, in addition to the information above, and in relation to any single transaction, or connected series of transactions that commit the company, consult with its Shareholder and lenders on items over agreed thresholds, particularly those which have not been expressly provided for in any Approved Annual Budget and Business Plan including but not limited to:

- capital investment
- an expansion of current activities
- any proposed joint venture
- formation of any subsidiary
- subscriptions for or sale of shares or equity interests in any company
- asset sales over $500,000 (other than non-core land and inventory sales in the ordinary course of business)

12. ACTIVITIES FOR WHICH COMPENSATION IS SOUGHT

Where the Government instructs Solid Energy to undertake activities or assume obligations which will result in a reduction in our profit or net worth, the Board will seek compensation sufficient to allow the financial position of the company to be restored to the position it would have been in but for the Government's instructions. The Crown's Permanent Process for Land Disposal, which applies to all Crown Agencies, may trigger this provision.

No requests for compensation are currently under consideration.

13. VALUE OF THE CROWN'S INVESTMENT

There has been a significant change in the value of Solid Energy's business over the past 12 months. With global coal markets shifting structurally lower during the 2013 financial year Solid Energy has had to reconsider the current value of the business. Restructuring at all major sites, including the placement of Spring Creek Mine on care and maintenance and a change in strategic focus for the business, has resulted in every asset being retested under a range of scenarios.

The key drivers of value remain the revenue assumptions, being the long-term international price for coking coal and the long term NZD / USD cross rate.

The value of each asset has been assessed using a variety of assumptions and valuation methodologies including:

- Value in use approach for operating assets or near-term developments where projected near-term cashflows have been discounted using a real after-tax discount rate of 8.7%. Prices have been modelled based on hard coking coal prices increasing and stabilising at US$200/tonne by 2016, being the equilibrium price determined from a range of external industry sources, along with a long term NZD/USD exchange rate of 0.80c from 2016 onwards
- Resource multiples to assess longer-term resource development options using observed multiples of listed peer companies adjusted for specific risk factors
- Realisable value for assets held for sale or non-operational.

Given that the vast majority of assets have been valued based on an assessed recoverable amount within the 30 June 2013 financial statements, the directors believe a fair assessment of commercial value for the current period is reflected in the book value.

Hence the Board's estimate of enterprise value of Solid Energy as at 30 June 2013 is $473 million, equating to an equity value (commercial value) of $92 million after deducting net bank debt and notes of $381 million. Based on the book value in June 2012, the impact of the fair value impairments resulted in a Total Shareholders' Return of -78%.

Subsequent to balance date, on 22 October, $100 million of equity in the form of redeemable preference shares was issued in exchange for $25 million in cash and $75 million for the conversion of existing bank and notes resulting in an increase in the equity position by $100 million.

APPENDIX 1: STATEMENT OF ACCOUNTING POLICIES

1. CORPORATE INFORMATION

These financial statements are for Solid Energy New Zealand Ltd ("Solid Energy"), its subsidiaries and jointly-controlled entities.

Solid Energy is a profit-oriented company incorporated in New Zealand. Solid Energy is registered under the Companies Act 1993.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(A) BASIS OF PREPARATION AND STATEMENT OF COMPLIANCE

The financial statements for the year ended 30 June 2013 have been prepared in accordance with Generally Accepted Accounting Practice in New Zealand and the requirements of the Companies Act 1993, the Financial Reporting Act 1993, and the State Owned Enterprises Act 1986.

The financial statements comply with New Zealand equivalents to International Financial Reporting Standards, and other applicable Financial Reporting Standards, as appropriate for profit-oriented entities. The financial statements comply with International Financial Reporting Standards (IFRS).

The financial statements have been prepared on an historical cost basis, except for:

- Investment property, biological assets, derivative financial instruments and available-for-sale financial assets that have been measured at fair value
- Provisions and Crown Receivable which are measured at net present value
- Tangible mining assets which include capitalised rehabilitation provisions; and
- Assets classified as held for sale which are measured at the lower of carrying amount or fair value less cost to sell.

The financial statements are presented in New Zealand dollars and all values are rounded to the nearest one-tenth of one million dollars ($million).

New Accounting Standards and Interpretations

(i) Changes in accounting policy and disclosures.

The accounting policies adopted are consistent with those of the previous financial year.

Where necessary the analysis of certain comparatives has been amended to improve the information provided to the reader.

(ii) Solid Energy has elected not to early adopt the following relevant standards which have been issued but are not yet effective for the group:

- NZ IAS 28 Investments in Associates and Joint Ventures (effective for the reporting period commencing 1 July 2013).

  This standard prescribes the accounting for investments in associates and joint ventures, and sets out the requirements for the application of the equity method when accounting for investments in joint ventures. The impact on the group's financial statements has not yet been concluded.

- NZ IFRS 9 Financial Instruments (effective for the reporting period commencing 1 July 2015).

  The first phase of NZ IFRS 9 Financial Instruments addresses the classification and measurement of financial assets. At this stage it is expected that the new standard will only have a minor impact on the classification and measurement of Solid Energy's current financial assets.

- NZ IFRS 10 Consolidated Financial Statements (effective for the reporting period commencing 1 July 2013).

  This standard introduces a new approach to determining which investees should be consolidated. The standard was issued in June 2011 and the impact on the group's financial statements has not yet been concluded.

- NZ IFRS 11 Joint Arrangements (effective for the reporting period commencing 1 July 2013).

  This standard focuses on the rights and obligations of joint arrangements rather than the legal form. The standard was issued in June 2011 and the impact on the group's financial statements has not yet been concluded.

- NZ IFRS 12 Disclosure of Interests in Other Entities (effective for the reporting period commencing 1 July 2013).

This standard contains the disclosure requirements for entities that have interests in subsidiaries, joint arrangements and associates. The standard was issued in June 2011 and the impact on the group's financial statements has not yet been concluded.

- NZ IFRS 13 Fair Value Measurement (effective for the reporting period commencing 1 July 2013).

  This standard replaces the fair value measurement guidance within individual standards with a single source of fair value measurement guidance. The standard was issued in June 2011 and the impact on the group's financial statements has not yet been concluded.

- IFRIC 20 Stripping Costs (effective for the reporting period commencing 1 July 2013).

  This standard provides guidance on the treatment of production phase stripping costs. The standard was issued in October 2011 and the impact on the group's financial statements has not yet been concluded.

(B) BASIS OF CONSOLIDATION

The consolidated financial statements comprise the financial statements of Solid Energy and its subsidiaries at year end ("the group"). The financial statements of subsidiaries are prepared for the same reporting period as the parent company; adjustments are made to bring into line any dissimilar accounting policies that may exist.

All intercompany balances and transactions, including unrealised profits arising from intra-group transactions, have been eliminated in full. Unrealised losses are eliminated unless costs cannot be recovered.

Subsidiaries are consolidated from the date on which control is transferred to the group and cease to be consolidated from the date on which control is transferred out of the group. Where there is loss of control of a subsidiary, the consolidated financial statements include the results for the part of the reporting year during which Solid Energy had control.

Investments in subsidiaries held by Solid Energy are accounted for at cost in the separate financial statements of the parent entity. The acquisition of subsidiaries is accounted for using the purchase method of accounting. The purchase method of accounting involves allocating the cost of the business combination to the fair value of the assets acquired and the liabilities and contingent liabilities assumed at the date of acquisition (refer note 2(C)).

(C) BUSINESS COMBINATIONS

The purchase method of accounting is used to account for all business combinations regardless of whether equity instruments or operations are acquired. Cost is measured as the fair value of the assets given, shares issued or liabilities incurred or assumed at the date of exchange plus costs directly attributable to the combination.

Except for non-current assets or disposal groups classified as held for sale (which are measured at fair value less costs to sell), all identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. The excess of the cost of the business combination over the net fair value of the group's share of the identifiable net assets acquired is recognised as goodwill. If the cost of acquisition is less than the group's share of the net fair value of the identifiable net assets of the subsidiary, the difference is recognised as a gain in profit or loss, but only after a reassessment of the identification and measurement of the net assets acquired.

(D) FOREIGN CURRENCY TRANSLATION

Both the functional and presentation currency of Solid Energy and its New Zealand subsidiaries is New Zealand dollars ($). Transactions in foreign currencies are initially recorded in the functional currency at the exchange rates ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are re-translated at the rate of exchange ruling at the reporting date. All differences in monetary assets and liabilities in the consolidated financial statements are taken to profit or loss.

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate as at the date of the initial transaction. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

(E) REVENUE, FINANCE INCOME AND OTHER INCOME

Revenue, finance income and other income are recognised to the extent that it is probable that the economic benefits will flow to the group and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognised:

Revenue

Sale of goods

Revenue is recognised when the significant risks and rewards of ownership of the goods have passed to the buyer and can be measured reliably. Risks and rewards are considered to have passed to the buyer at the time of delivery of the goods to the customer. For free on board export shipments delivery is deemed to have taken place once the ship is fully loaded and the bill of lading is issued.

Finance Income

Interest

Revenue is recognised as the interest accrues (using the effective interest method, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial instrument) to the net carrying amount of the financial asset.

Dividends

Revenue is recognised when the shareholders' right to receive the payment is established.

Other Income

Rental income

Rental income arising on properties is accounted for on a straight-line basis over the lease term.

(F) INCOME TAX

Income tax comprises current and deferred tax. Income tax is recognised in profit or loss except to the extent that it relates to items recognised directly into equity. Deferred income tax is provided on all temporary differences at the reporting date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred income tax liabilities are recognised for all taxable temporary differences:

i) except where the deferred income tax liability arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

ii) in respect of taxable temporary differences associated with investments in subsidiaries and interests in jointly controlled entities, except where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred income tax assets are recognised for all deductible temporary differences, carry-forward of unused tax assets and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carry-forward of unused tax assets and unused tax losses can be utilised:

i) except where the deferred income tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

ii) deferred tax assets are only recognised to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised. The carrying amount of deferred income tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilised.

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply in the year when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the reporting date.

(G) GST

Revenues, expenses and assets are recognised net of the amount of goods and services tax (GST) except:

i) where the GST incurred on a purchase of goods and services is not recoverable from the taxation authority, in which case the GST is recognised as part of the cost of acquisition of the asset or as part of the expense item as applicable; and

ii) for receivables and payables which are stated with the amount of GST included.

The net amount of GST recoverable from, or payable to, the taxation authority is included as part of receivables or payables in the Statement of Financial Position. Cashflows are included in the Statement of Cashflow on a gross basis and the GST component of cashflows arising from investing and financing activities, which is recoverable from, or payable to, the taxation authority is classified as an operating cashflow.

Commitments and contingencies are disclosed net of the amount of GST recoverable from, or payable to, the taxation authority.

(H) PROPERTY, PLANT AND EQUIPMENT

The group has five classes of property, plant and equipment:

- Land, buildings and structures
- Leasehold improvements
- Plant and equipment
- Leased infrastructure asset; and
- Capital work in progress.

Depreciation

Land is carried at cost less any impairment losses. Land is not depreciated. Capital work in progress is carried at cost less any impairment losses. Capital work in progress is not depreciated. When an item of capital work in progress is commissioned it transfers to the appropriate property, plant and equipment category and depreciation commences.

All other property, plant and equipment is stated at cost less accumulated depreciation and any impairment in value. Depreciation is calculated on a straight-line basis over the assets' expected economic life. Leased assets are depreciated over the shorter of the lease term and their useful economic lives. The expected economic lives of assets are as follows:

- Buildings and structures — 10 to 25 years
- Leasehold improvements — Lease term
- Plant and equipment — 5 to 15 years
- Leased infrastructure asset — 30 years

Depreciation methods, useful lives and residual values are reassessed at the reporting date. Property, plant and equipment under construction are recorded as work in progress and are not depreciated until they are ready for productive use.

Impairment

The carrying values of property, plant and equipment are reviewed for impairment when events or changes in circumstances indicate the carrying value may not be recoverable. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

If any such indication exists, and where the carrying values exceed the estimated recoverable amount, the assets or cash-generating units are written down to their recoverable amount. The recoverable amount of plant and equipment is the greater of fair value less costs to sell and value in use. In assessing value in use, the estimated future cashflows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. Impairment losses are recognised in profit or loss.

(I) BIOLOGICAL ASSETS

Forestry Assets

Forest assets are measured at fair value less point-of-sale costs, which include all costs that would be necessary to sell the assets. A gain or loss arising on initial recognition, or from a change in fair value less estimated point-of-sale costs, is included in profit or loss for the period in which it arises.

(J) MINING ASSETS

Mining assets includes exploration and evaluation, mines in development and mines in production, for both tangible and intangible assets.

Tangible Mining Assets

i) Exploration and evaluation

Exploration, evaluation and development expenditure is stated at cost and is accumulated in respect of each identifiable area of interest. Expenditure is only carried forward to the extent that it is expected to be recouped through the successful development of the area of interest (or alternatively by its sale), or where activities in the area have not yet reached a stage which permits a reasonable assessment of the existence, or otherwise, of economically recoverable reserves.

ii) Mines in development

Once a decision is made to proceed with commercial production, the expenditure incurred on successful areas of interest is reclassified as "Mines in development".

iii) Mines in production

Mining assets are transferred to "Mines in production" in the year production commences.

Mine production assets, comprising successful areas of interest, subsequent development expenditure and capitalised rehabilitation provisions are amortised to profit or loss over the remaining productive life of the operation on a unit of production basis, subject to a maximum production period of 20 years.

Accumulated costs in relation to an abandoned area are written off in full in the period in which the decision is made to abandon the area.

Intangible Mining Assets

Mineral reserve assets comprise mining rights and mining licences and are classified between exploration and evaluation, mines in development and mines in production as per tangible assets above. Mineral reserve assets are stated at cost less any accumulated amortisation and impairment loss. Amortisation is charged to profit or loss on mineral reserve assets on a straight-line basis over the estimated useful life of the mineral right. The estimated useful life of mineral right assets is subject to a maximum of 20 years.

(K) INTANGIBLE ASSETS

Goodwill

Goodwill on acquisition is initially measured at cost, being the excess of the cost of the business combination over the acquirer's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities. Following initial recognition, goodwill is measured at cost less any accumulated impairment losses.

Goodwill is not amortised. Goodwill is reviewed for impairment at each reporting date, or more frequently if events or changes in circumstances indicate that the carrying value may be impaired. As at the acquisition date any goodwill acquired is allocated to each of the cash-generating units expected to benefit. Impairment is determined by assessing the recoverable amount of the cash-generating unit to which the goodwill relates. Where the recoverable amount of the cash-generating unit is less than the carrying amount, an impairment loss is recognised.

Intellectual property

Intellectual property is measured at cost less accumulated amortisation and accumulated impairment losses. The amortisation period is 5 years.

Emission Trading Scheme (ETS) Units

As of 1 July 2010 the transport, energy and industrial sectors joined the forestry sector in having obligations under the New Zealand Emission Trading Scheme (ETS). Solid Energy is required to account for CO2 equivalent emissions associated with designated activities, principally the mining and selling of coal. Solid Energy, as a coal miner, is designated as a default participant for the coal that it mines and is required to surrender eligible emissions units associated with coal sold domestically and directly associated with mining coal that is subsequently exported. Very large customers can elect to manage the obligation themselves.

Solid Energy is required to surrender 1 eligible emission unit for every 2 tonnes of CO2 equivalent emitted. These units can be sourced:

- through the purchase of units
- directly from projects that reduce emissions
- via allocation by the Government as compensation for ETS costs; or
- by paying a fixed price of $25 per emission unit to the Government.

New Zealand Units, Removal Units, Certified Emissions Reductions and Emission Reduction Units are all valid ETS units which can be purchased to satisfy ETS obligations. Purchased ETS units are recognised as an intangible asset and measured at cost. ETS units are purchased in order to settle ETS obligations and are therefore not amortised.

(L) INVESTMENT PROPERTY

Investment properties are measured initially at cost, including transaction costs. The carrying amount includes the cost of replacing part of an existing investment property at the time that cost is incurred if the recognition criteria are met, and excludes the costs of day-to-day servicing of an investment property. Subsequent to initial recognition, investment properties are stated at fair value, which is based on active market prices, adjusted if necessary, for any difference in the nature, location or condition of the specific asset at the reporting date. Gains or losses arising from changes in the fair values of investment properties are recognised in profit or loss in the year in which they arise.

Investment properties are de-recognised either when they have been disposed of or when the investment property is permanently withdrawn from use and no future economic benefit is expected from its disposal. Any gains or losses on the retirement or disposal of an investment property are recognised in profit or loss in the year of retirement or disposal. Transfers are made to investment property when, and only when, there is a change in use, evidenced by ending of owner-occupation, commencement of an operating lease to another party or ending of construction or development. Transfers are made from investment property when, and only when, there is a change in use, evidenced by commencement of owner-occupation or commencement of development with a view to sale.

For a transfer from investment property to owner-occupied property or inventories, the deemed cost of property for subsequent accounting is its fair value at the date of change in use. If the property occupied by the group as an owner-occupied property becomes an investment property, the group accounts for such property in accordance with the policy stated under property, plant and equipment up to the date of change in use.

(M) INTEREST IN JOINTLY-CONTROLLED ENTITIES

Jointly-controlled entities are those entities over whose activities the group has joint control established by contractual agreement. The group has an interest in a joint venture that is a jointly-controlled entity.

The interest in a joint venture entity is accounted for in the consolidated financial statements using the equity method of accounting and is carried at cost by the parent entity. Under the equity method, the group's share of the results of the joint venture entity is recognised in profit or loss, and the share of movements in reserves is recognised in the Statement of Financial Position.

(N) OTHER INVESTMENTS

All other investments are initially recognised at fair value, being the consideration given and, in the case of an investment not at fair value, through profit or loss, including acquisition costs associated with the investment. After initial recognition, investments which are classified as available-for-sale are measured at fair value.

Gains or losses on available-for-sale investments are recognised as a separate component of equity until the investment is sold, collected or otherwise disposed of, or until the investment is determined to be impaired, at which time the cumulative gain or loss previously reported in equity is included in profit or loss.

Non-derivative financial assets with fixed or determinable payments and fixed maturity are classified as held-to-maturity when the group has the positive intention and ability to hold to maturity. Other long-term investments that are intended to be held to maturity, such as bonds, are subsequently measured at amortised cost using the effective interest method.

Amortised cost is calculated by taking into account any discount or premium on acquisition over the period to maturity. For investments carried at amortised cost, gains and losses are recognised in income when the investments are de-recognised or impaired. Purchases and sales of financial assets that require delivery of assets within the time-frame generally established by regulation or convention in the marketplace are recognised on the trade date, i.e. the date that the group commits to purchase the asset.

(O) LEASES

The determination of whether an arrangement is, or contains a lease, is based on the substance of the arrangement and requires an assessment of whether the fulfilment of the arrangement is dependent on the use of a specific asset or assets and the arrangement conveys a right to use the asset.

Group as a Lessee

Finance leases, which transfer to the group substantially all the risks and benefits incidental to ownership of the leased item, are capitalised at the inception of the lease at the fair value of the leased property or, if lower, at the present value of the minimum lease payments. Lease payments are apportioned between the finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are included in profit or loss as finance costs. Capitalised leased assets are depreciated over the shorter of the estimated useful life of the asset and the lease term. Leases where the lessor retains substantially all the risks and benefits of ownership of the asset are classified as operating leases. Initial direct costs incurred in negotiating an operating lease are added to the carrying amount of the leased asset and recognised over the lease term on the same basis as the lease payments. Operating lease payments are recognised as an expense in the income statement on a straight-line basis over the lease term. The cost of improvements to leasehold properties is capitalised, disclosed as leasehold improvements, and amortised over the unexpired period of the lease or the estimated useful life of the improvements, whichever is the shorter.

Group as a Lessor

Leases which transfer substantially all the risks and benefits incidental to ownership of the leased item are classified as finance leases. Finance lease receivables are capitalised at the inception of the lease at the fair value of the leased assets or, if lower, at the present value of the minimum lease payments. Operating lease receipts are recognised as other income in profit or loss on a straight-line basis over the lease term.

(P) IMPAIRMENT OF MINING AND OTHER NON-CURRENT ASSETS

The carrying amount of land, mineral reserve assets, exploration, evaluation and development expenditure and stripping in advance are reviewed at each reporting date to determine whether there is an indication of an impairment loss. If any such indication exists, the assets recoverable amount is estimated. For any asset that does not generate largely independent cashflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs. If the carrying amount of the asset (or cash-generating unit) exceeds this recoverable amount, the asset (or cash-generating unit) is written down. The recoverable amount of an asset is determined as the higher of its net selling value and value in use. Value in use is determined by estimating future cashflows and discounting them to their present value using a risk- adjusted pre-tax discount rate appropriate to the risks inherent in the asset.

Equity instruments are deemed to be impaired when there is a significant or prolonged decline in the fair value below the original purchase price. The recoverable amount of the group's investments in held-to-maturity debt instruments and receivables carried at cost is calculated as the present value of estimated cashflows, discounted at the original effective interest rate. Receivables with a short duration are not discounted. When an impairment loss subsequently reverses, the carrying amount of the asset (or cash-generating unit) is increased to the revised estimate of its recoverable amount, but only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

(Q) INVENTORIES

Inventories of by-product and saleable coal are valued at the lower of weighted average cost or net realisable value. By-product coal is contaminated and diluted coal which requires significant further processing to become saleable. When both saleable coal and by-product coal are produced from an operation the costs are allocated based on the relative net realisable values of the two products at the point they become separately identifiable.

Costs include direct material, labour and transportation expenditure incurred in getting such inventories to their existing location and condition, together with an appropriate portion of overhead expenditure.

Inventories of materials, consumable supplies and maintenance spares expected to be used in production are valued at weighted average cost. Surplus and obsolete inventories are valued at net realisable value if lower than cost.

Inventories of harvested crops are valued at the lower of fair value less estimated point-of-sale costs at the point of harvest or net realisable value.

Net realisable value is the estimated selling price in the ordinary course of business, less estimated costs of completion and the estimated costs necessary to make the sale.

(R) STRIPPING IN ADVANCE

Overburden and other waste materials are often removed in order to access the coal reserve. This activity is referred to as stripping.

- Development stripping is stripping that occurs during the initial development of a mine site; and
- Production stripping is stripping that commences at the time that saleable materials begin to be extracted from the mine.

Development Stripping

Directly attributable costs of development stripping are capitalised and classified as 'Stripping (non-current and current)'.

Capitalisation ceases and depreciation of those capitalised costs commences at the time that saleable materials begin to be extracted from the mine. Depreciation of capitalised development stripping costs is determined on a unit of production basis for each separate area of interest.

Production Stripping

Total production stripping costs are charged to profit or loss in the period which matches the proportion of coal extracted to the total proven and probable reserves expected from the mine.

Assumptions regarding the remaining overburden, units of production and estimated mine life are re-assessed on a quarterly basis.

Impairment

Stripping in Advance and Mining Properties are considered in combination with other assets of an operation for the purpose of undertaking impairment assessments.

(S) DERIVATIVE FINANCIAL INSTRUMENTS AND HEDGING

The group uses derivative financial instruments such as foreign currency contracts and interest rate swaps to hedge its risks associated with foreign currency and interest rate fluctuations. Solid Energy's treasury policy does not allow derivative financial instruments to be held or issued for trading purposes. However, derivatives that do not qualify for hedge accounting are accounted for as trading instruments.

Derivative financial instruments are recognised initially at fair value and retested on this basis at each reporting period. The gain or loss on re- measurement to fair value is recognised immediately in profit or loss unless the derivatives meet the criteria for hedge accounting (see below).

Cashflow Hedges

Cashflow hedges (forward foreign currency contracts and interest rate swaps) are used to hedge the foreign currency and interest rate risk of forecast transactions which meet the conditions for hedge accounting. The portion of the gain or loss on the hedging instrument that is determined to be an effective hedge is recognised directly in equity and the ineffective portion is recognised in profit or loss. For all cashflow hedges, the gains or losses that are recognised in equity are transferred to profit or loss in the same year in which the hedged forecasted transaction affects the net profit and loss, for example when the future sale actually occurs.

Hedge accounting is discontinued when the hedging instrument expires or is sold, terminated or exercised, or no longer qualifies for hedge accounting. Any cumulative gain or loss on the hedging instrument recognised in equity is kept in equity until the forecasted transaction occurs. If a hedged transaction is no longer expected to occur, the net cumulative gain or loss recognised in equity is transferred to profit or loss for the year.

De-recognition of Derivative Financial Instruments

The de-recognition of a financial instrument takes place when the group no longer controls the contractual rights that comprise the financial instrument, which is normally the case when the instrument is sold, or all the cashflows attributable to the instrument are passed through to an independent third party.

(T) ACCOUNTS RECEIVABLE

Trade Receivables

Accounts receivable, which generally have 30-90 day terms are recognised and carried at the invoice amount less an allowance for any uncollectible amounts.

Collectability of trade receivables is reviewed on an ongoing basis at an operating unit level. Individual debts that are known to be uncollectible are written off when identified. An impairment provision is recognised when there is objective evidence that the group will not be able to collect the receivable. Financial difficulties of the debtor and default on payments are considered objective evidence of impairment. The amount of the impairment loss is the receivable carrying amount compared to the present value of estimated future cashflows, discounted at the original effective interest rate.

Related Party Receivables

An impairment assessment is undertaken each financial year by examining the financial position of the related party and the market in which the related party operates to determine whether there is objective evidence that a related party receivable is impaired. When such evidence exists, the group recognises an allowance for the impairment loss.

(U) CASH AND CASH EQUIVALENTS

Cash and cash equivalents comprise cash at bank and in hand, short-term deposits with an original maturity of three months or less and bank overdrafts and overnight cash facilities.

(V) PROVISIONS

Provisions are recognised when the group has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Where the group expects some or all of a provision to be reimbursed, for example the Crown's share of end of mine life rehabilitation costs, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain. The expense relating to any provision is presented in profit or loss net of any reimbursement, except for rehabilitation costs (see below).

If the effect of the time value of money is material, provisions are determined by discounting the expected future cashflows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognised as a finance cost.

Onerous Contracts

A provision is made for onerous contracts when the net present value of any contract in which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it.

Rehabilitation Costs

The group is required under the terms of its mining licences to rehabilitate mine sites at the end of their productive lives to a condition acceptable to the relevant authorities and consistent with the group's environmental policies. The estimated cost of any end of mine life rehabilitation is provided for at the commencement of the mining project, with a corresponding asset recognised in relation to the mine site. Measurement of the rehabilitation provision is on the basis of expected future costs discounted using a risk-free rate. The inflation rate and risk-free rates used are those published by the New Zealand Treasury for use in accounting valuations.

Any increases in the rehabilitation provision that relate to the ongoing production of the mine are expensed as the obligation arises. Any other change in the net present value of rehabilitation costs, including those resulting from new disturbances, updated cost estimates and changes to the lives of operations are capitalised to mine assets. Changes in net present value relating purely to discounting future values are reflected in interest expense.

Mobile Plant Costs

Mobile plant costs comprise mobilisation, demobilisation and mobile plant leased maintenance cost provisions. Mobilisation costs are those costs incurred in relocating contractor mobile plant to the mine site at the start of the contract. Mobilisation costs are initially recorded in prepayments and amortised over the life of the contract. Mobilisation assets are included within prepayments and mobilisation liabilities are included within provisions.

Demobilisation costs are those costs relating to the cost of removing mobile plant fleet from the mine site at the end of the contract. Demobilisation costs are provided for at the start of the contract and are amortised over the life of the contract.

The group is required to maintain leased mine site mobile plant equipment to a minimum standard under the lease agreements and to pay for costs associated with the removal of mobile plant fleets from the mine sites at the end of the contracts. The costs required to replace worn components on mine site mobile plant fleets are provided for based on the number of hours the mobile plant has been used. Costs associated with the removal of the fleet at the end of the contracts are provided for at the start of the mining contract and are amortised over the life of the contract.

(W) CROWN RECEIVABLE

The group has an indemnity from the Crown for its share of end of mine life rehabilitation costs relating to mining assets prior to 1 April 1987. Measurement of the Crown receivable is on the basis of expected future costs discounted using a risk-free rate.

(X) INTEREST-BEARING LOANS AND BORROWINGS

All loans and borrowings are initially recognised at cost, being the fair value of the consideration received net of issue costs associated with the borrowing. After initial recognition, interest-bearing loans and borrowings are subsequently measured at amortised cost using the effective interest method. Amortised cost is calculated by taking into account any issue costs, and any discount or premium on settlement. Gains and losses are recognised in profit or loss when the liabilities are de-recognised and as well as through the amortisation process.

Borrowing Costs

Borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset are capitalised as part of the cost of that asset. Qualifying assets are those that take a significant amount of time to get ready for their intended use or sale. Capitalisation of borrowing costs is not applied to the borrowing costs associated with mining assets in the exploration and evaluation phase or to assets held for potential future mining activities.

Other borrowing costs are recognised as an expense as incurred.

(Y) ACCOUNTS PAYABLE

Trade and other payables are carried at amortised cost. They represent liabilities for goods and services provided to the group prior to the end of the financial year that are unpaid and arise when the group becomes obliged to make future payments in respect of the purchase of these goods and services. The amounts are unsecured and are usually paid within 30 days of recognition.

(Z) EMPLOYEE ENTITLEMENTS

Long-term Employee Entitlements

Long-term employee entitlements such as long service leave and other entitlements that are vesting are recognised when they accrue to employees. Liabilities are accrued on an actuarial basis in respect to entitlements that are vested and expected to crystallise in the future.

Short-term Employee Entitlements

Short-term employee entitlement obligations such as salaries and wages and annual leave are expensed as the related service is provided.

Defined Contribution Plans

Obligations for contributions to defined contribution pension plans are recognised as an expense in profit or loss when they are due.

(AA) NON-CURRENT ASSETS HELD FOR SALE OR DISTRIBUTION

Non-current assets, or disposal groups comprising assets and liabilities, that are expected be recovered primarily through sale or distribution rather than continuing use, are classified as held for sale or distribution. Immediately before classification as held for sale or distribution, the assets, or components of a disposal group, are re-measured in accordance with the group's accounting policies. Thereafter the assets, or disposal group, are measured at the lower of their carrying amount and fair value less cost to sell. Any impairment loss on a disposal group is first allocated to goodwill and then to remaining assets and liabilities on a pro rata basis except that no loss is allocated to inventories, financial assets, deferred tax assets, employee benefit assets, investment property or biological assets, which continue to be measured in accordance with the Group's accounting policies. Impairment losses on initial classification as held for sale or distribution and subsequent gains or losses on re-measurement are recognised in profit or loss. Gains are not recognised in excess of any cumulative impairment loss.

Once classified as held for sale or distribution, intangible assets and property, plant and equipment are no longer amortised or depreciated, and any equity-accounted investee is no longer equity accounted.

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